Aspirations Against Feasibility

SHORT: SG

Last Close: $39.30

Target: $13.72

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Industry Overview

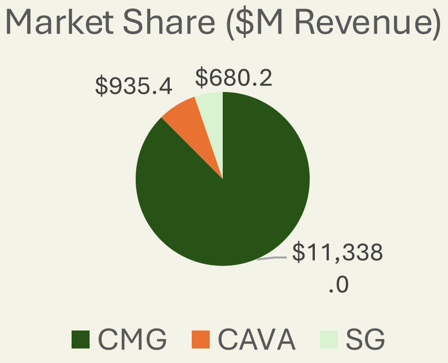
Sweetgreen is a player in the increasingly popular fast-casual restaurant chain space

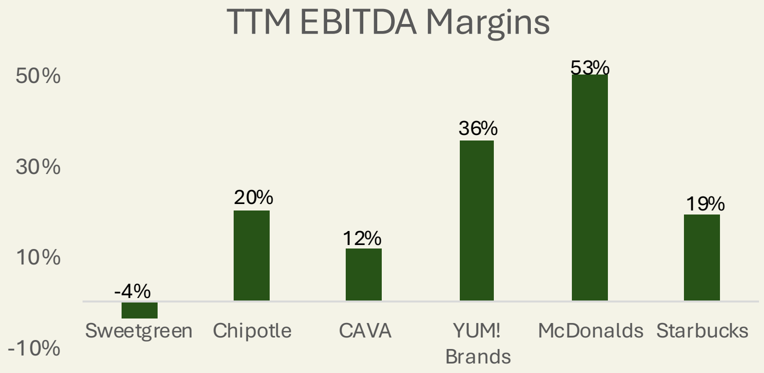
Sweetgreen History and Positioning

- Sweetgreen was **founded in 2007** as a **fast-casual restaurant chain** based in **Los Angeles, CA**. It differentiated itself by its focus on fresh, healthy, and locally sourced ingredients, **selling customizable salad bowls.**
- The company **IPO'd in 2021** at a **$1.6bn valuation.** Since then, it has grown at a **~40% Revenue CAGR** and opened **over 200 stores** nationwide.
- Sweetgreen eventually became popular as an **ESG-oriented company** and **strong alternative to staples** such as Chipotle Mexican Grill (CMG)

Competitive Landscape

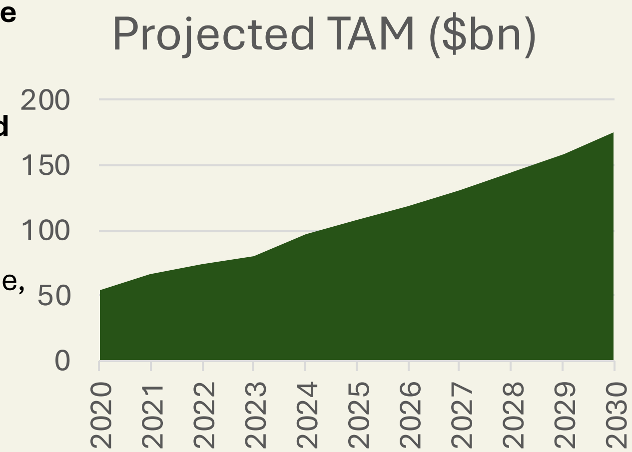
- The most comparable brands in the fast-casual sector are **CMG, CAVA, McDonald's, Starbucks, and YUM! Brands**
- Chipotle is the gold standard. It has **higher RLMs** (Restaurant-level margins) than CAVA/Sweetgreen, strong industry dominance, and a **national presence** similar to Starbucks and McDonald's while trading **at more premium levels**
- Sweetgreen, like any new entrant, is **constantly compared to Chipotle**





Total Addressable Market

- TAM has been **increasing rapidly over the past 15 years** in the fast-casual industry
- As a segment of the restaurant industry, fast-casual's market share has **increased** from **~5.4% to ~12.2% since 2010**
- There is an unaccounted risk: **<u>Quality of Zip Codes</u>**. TAM projections assume that the current rate of expansion can continue, but we are rapidly running out of untouched Zip Codes that can generate a profit in the fast-casual space.



... So, what does a good Zip Code look like?

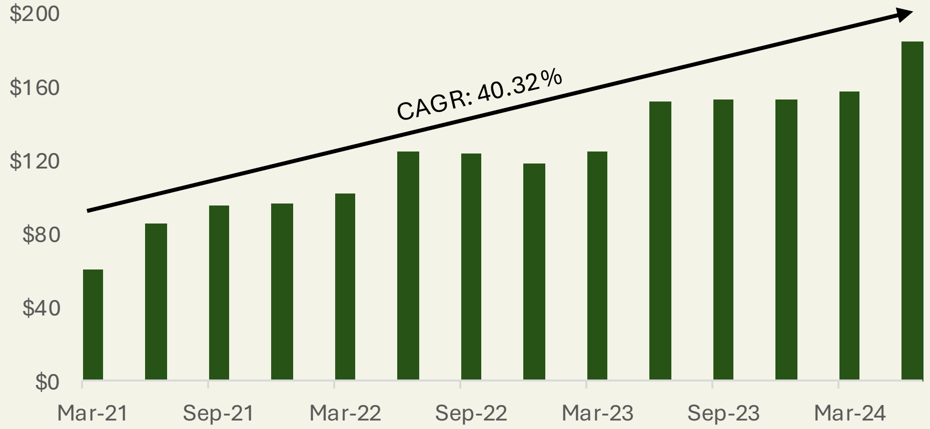
- Fast-casual restaurants experience peak sales for a **lesser number of hours**
- Gross-margins are **typically lower** than restaurants in other sectors
- As a result, only the **most premium locations** are pursued
- This means areas with very **dense populations**, **low unemployment**, and **high average household incomes**

Sweetgreen: The Next Chipotle?

Confidence in Sweetgreen future performance is through the roof, leading to insane long-term expectations

	Primary Driver of Future Value	Estimates / Guidance	2024 Numbers
Infinite Kitchens	• **Infinite Kitchens (IKs)** were unveiled mid-2024 • **Self-service AI** meant to cut labor expense ~33%	Management eventually **wants every location** to have an IK. Sell-side predicts **~71%** will have IKs in **2030.**	**4 Existing IKs**
TAM Expansion	• **Primary driver** of growth is opening new stores • **No salad chain** has exceeded 300 stores before	Sweetgreen promises to open **1,000 locations by 2040**. This requires a **~9.77% CAGR** in open stores.	**231 Stores Open**
SG&A Expense	• **Plans for reduction**, will improve EBITDA margins • **Egregious SBC** from overhiring engineers	Sell-side estimates **keep SG&A expense flat** in the long-term while revenue grows aggressively.	**~9% of Revenue**

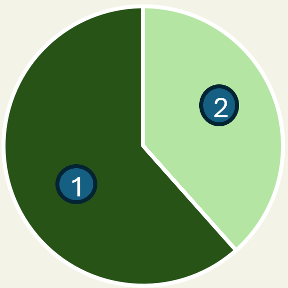
Historical Revenue Growth



Revenue Growth Driver Breakdown

1 **TAM Expansion**, or the rate at which Sweetgreen opens new stores, accounts for **~61.6%** of forward-looking revenue growth.

2 **Same-Store Sales (SSS)**, or average revenue growth of existing stores, accounts for **~38.4%** of forward-looking revenue growth.



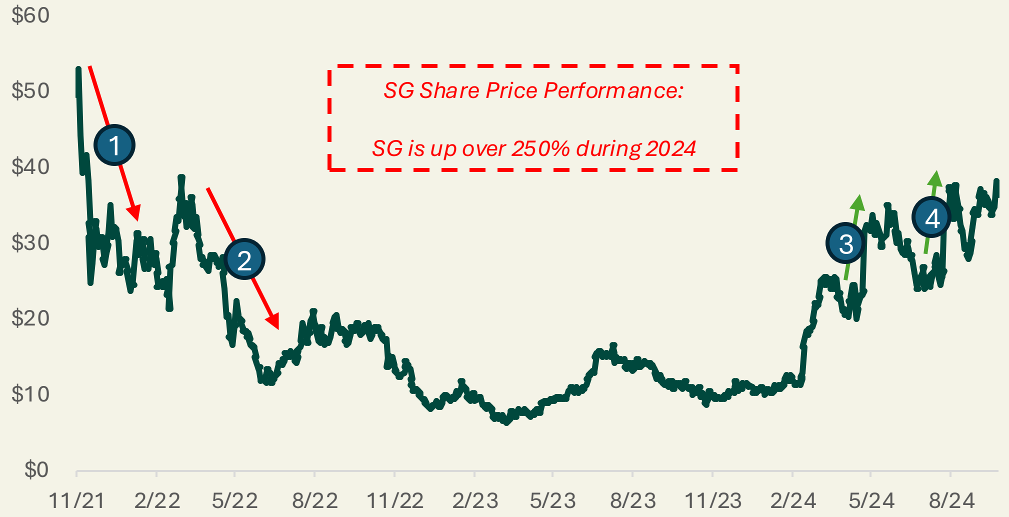
Chipotle-Oriented Valuation

*"We **apply Chipotle's 2024 EV/EBITDA multiple** of 34x to our Sweetgreen 2030 adj. EBITDA estimate. … it implies a $10.5B EV. Discounting this back at a 12% discount rate **implies that shares are worth $43.**"*

- TD Cowens, Sep. 4. 2024

Priced for Perfection

Confidence in Sweetgreen future performance is through the roof, leading to insane long-term expectations



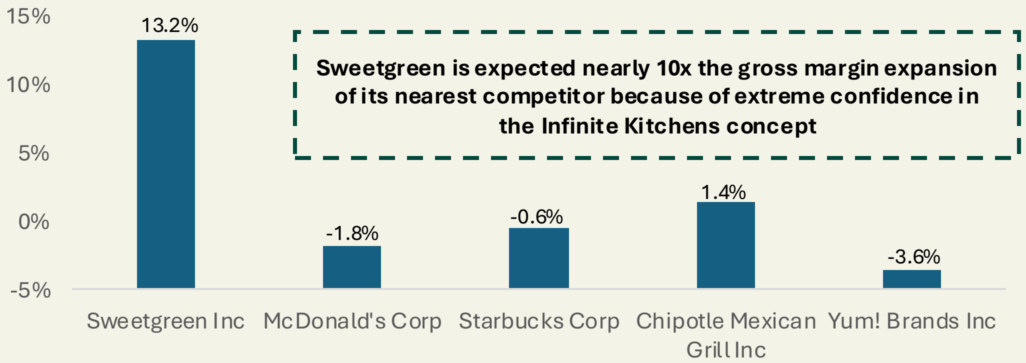
1. **-55%:** Q4 2021 reports wider-than-expected losses and a decline in same-store sales (SSS)
2. **-67%:** Q1 2022 reports further losses, management announces layoffs and lowers full-year guidance
3. **+45%:** Q1 2024 reports 5% SSS growth, management raises guidance, and sell-side increases estimates
4. **+32%:** Management unveils the Infinite Kitchen, promising improved margins and lower turnover

What's Baked In – Reverse DCF

10-Year Revenue CAGR	15.30%
2040 Open Locations	1000
2034 EBITDA Margin	49.14%
2034 Exit EV/EBITDA Multiple	22.0x

Extreme Optimism vs Competitors

2024E Gross Margin Improvement vs Comps



+ Bullish Sentiment

*"**2024's strength will drive upside** vs. 2025 consensus … we estimate Infinite Kitchens (IK) can drive … margin expansion that **exceeds consensus**. Longer term, … [our projections] **suggest meaningful upside** to 2030E adj EBITDA, and prompts a **greater TAM beyond the stated 1,000 U.S. locations**."*

- TD Cowens, Sep. 4. 2024

= Potential Short Opportunity

With such unbelievable targets priced in and unwavering optimism in Sweetgreen overdelivering on management promises, we believe there exists immense opportunity to generate an attractive return on a short position as estimates slowly come back to earth when these expectations can't be fulfilled.

Thesis Overview & Event Path

Sweetgreen is likely to miss targets in the next 1-2 years, leading to sell-offs

1

1000+ store TAM Goal is Extremely Unrealistic & Priced In

Sell-side analysts believe that Sweetgreen is a Chipotle-like growth story. We created a logistic regression model using zip-code level data (household income, race, age, geography) for current viable Sweetgreen locations which suggests the true TAM is much smaller than the baseless 1000+ store goal set by management.

2

Rapid Cava Expansion Hinders Sweetgreen's Success

Conflicting messaging from management shows that they are out of touch with reality, seeing Sweetgreen as a tech company rather than a salad chain. Cava Group, a notable competitor, is expanding its footprint twice as fast due to a simpler, more effective and standardized model, capturing market share before Sweetgreen can.

3

Smooth Infinite Kitchen (IK) rollout is *necessary* to justify valuation

The market is betting on automation via IK to cut labor costs and **yield a 1000+ bps improvement in company-wide RLM over time.** Many factors will likely prohibit the ambitious refitting of older stores and integrating new IKs into Sweetgreen's overall restaurant mix. It is questionable if IKs represent a sustainable competitive advantage for Sweetgreen as competitors are likely to emerge with similar models to IK.

Catalyst Timeline

FY '25

Management stated that at least half of new store openings would be IKs, which means around ~18 IKs opened. These IKs are necessary for Sweetgreen's IK mix and RLMs to increase. Only 1 New IK has been built by contract manufacturers, with the other 2 "built by hand in the Spyce Lab." Therefore, we believe Sweetgreen is likely to fail to hit the IK opening target due to a lack of proven scalability.

FY '26

Sweetgreen will need to reaccelerate unit openings to hit ~50 new stores per year to maintain the minimum 15% growth they are targeting. Based on the TAM research we conducted and increasing competition, we believe they will fail to hit this metric.

Thesis 1: Limited TAM means slowed openings

Using demographic data, it is increasingly unlikely that there are 1000 possible Sweetgreen locations

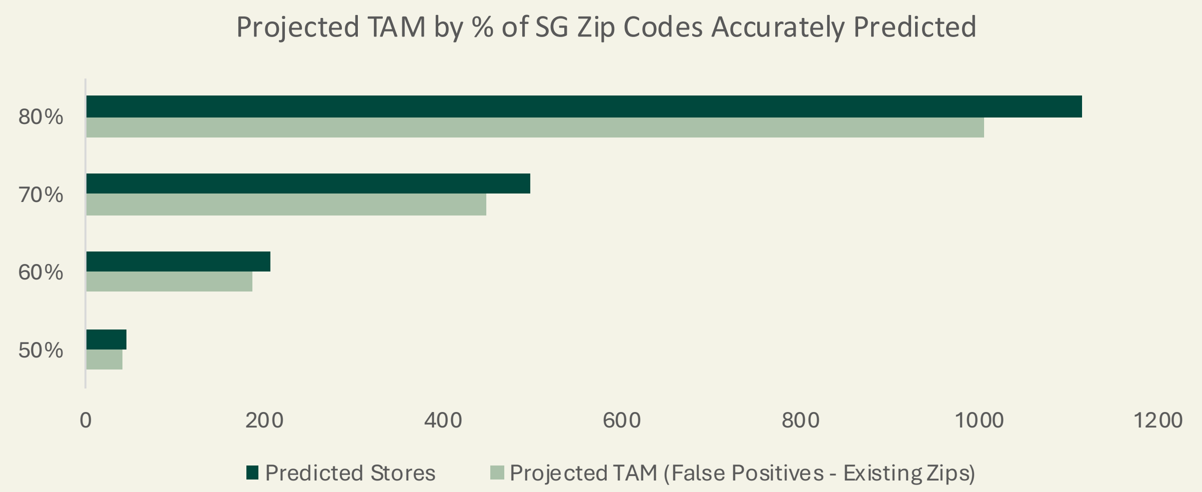
1000+ TAM – Baseless Management Claim Believed by Market

*"We remain on track to **double our footprint in the next three to five years and achieve 1,000 restaurants by the end of the decade**."*

- **Mitch Reback, CFO, during Sweetgreen's Q2 2022 Earnings Call**

Management has stated multiple times that they are "extremely" confident of operating 1000 units across the United States, despite very little market research to back up this claim.

Logistic Regression Model Results



Logistic Model Based On Current Sweetgreen Demographics

In order to estimate Sweetgreen's true TAM, we sought to predict the number of zip codes that Sweetgreen could *potentially* expand to, predicting the true TAM of Sweetgreen's model based on the Census demographic data of the zip codes they currently operate in.

Demographic Factors:

1. Median Household Income
2. Median Age
3. Total Population
4. College Educated Population
5. Zip Code Has Chipotle
6. Zip Code Has Cava

A logistic model was fit, and the odds of a zip code being viable for Sweetgreen operations were calculated for *every* zip code in the United States. The percent threshold of if a zip code was "viable" or "not viable" was manipulated based on the percentage current Sweetgreen operating zip codes accurately predicted by the model.

Analysis of The Results

- **The model validates that Sweetgreen's TAM is nowhere near Chipotle's due to the high amount of college-educated professionals and median household income needed for unit viability.**
- **False positives predicted by the model are the potential zip codes Sweetgreen could operate in. False Positives – Existing Operating Zip Codes = Sweetgreen's Estimated Remaining Market**
- **We multiply 1.11, the average amount of Sweetgreen locations per current operating Zip Code, by the number of newly identified Zip Codes to estimate potential locations.**

Thesis 2: Rapid Cava Expansion Hinders Success

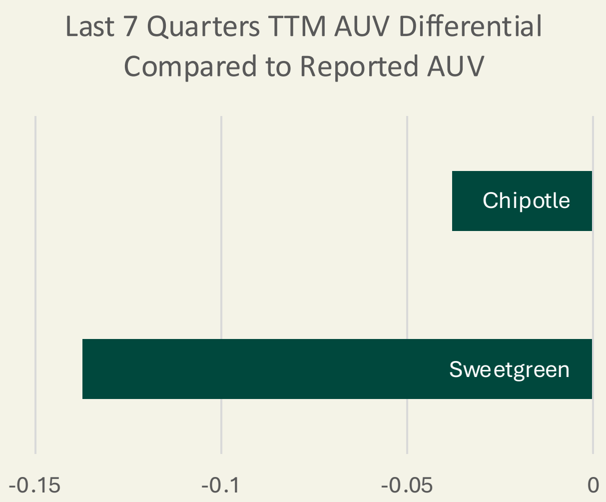
Even if there are 1000+ potential viable Zip Codes, CAVA Group is quickly eating up market share.

Management Has Expanded Too Quickly in The Past

"I think what we did over the past few years is we densified markets a little bit faster than we typically would have been going back in our history. So, as you'll see and a lot of end markets were going, instead of going and opening seven and eight stores right away, we'll open three high-profile stores with the right unit economics..."

\- **Jonathan Neman, CEO on March 14, 2023**

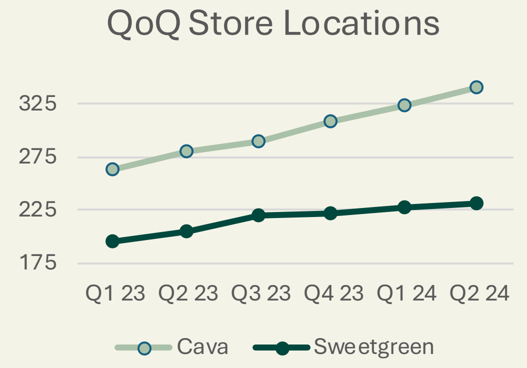
New Locations Are Performing Worse Than Current Ones



- The company reports Average Unit Volumes and SSS Metrics
- However, we can look closer at how companies like Chipotle and Sweetgreen define these terms, to reflect stores **that have been open for over a year.**
- Since new stores contribute to quarterly revenue, we calculated TTM AUV with this formula: **Average of Last 4 Quarter Sales / Average of Last 4 Quarter Store Count.**
- Sweetgreen's TTM AUV is significantly less than Reported AUV, meaning that **newer stores are contributing less to revenue**. This is **significantly less than Chipotle's differential**

Competition Heating Up Vs. Cava Group

- Cava's YoY Store Open Rate was **~23%** in Q1 and Q2 2024.
- Sweetgreen's YoY Store Open rate has declined from **23.49%** in Q2 23 to **12.68%** in Q2 24.
- Sell-side analysts are betting on reaccelerating unit growth to **15%-20%.**



Sweetgreen Pigeon-holed as CAVA Races On

- Sweetgreen and CAVA are competing for the same market share of young professionals with a median income of $100k-$150k. **CAVA is eating away at the remaining market share.**
- Sweetgreen seeks to transition from salad chain to a bowl food brand with a mediterranean emphasis. However, Sweetgreen is significantly more expensive than CAVA.
- The only way for Sweetgreen to be a Chipotle growth story is to **move down market** and dilute brand value by:
    - Continuing to offer menu items contrary to its vision of sustainability such as Caramelized Garlic Steak
    - Reducing ingredient costs and menu costs with IKs

Thesis 3: Infinite Kitchens are a distraction

Infinite Kitchens are likely not as scalable as the market thinks, with competitors closing the gap quickly.

Infinite Kitchen Outline

Proprietary to Sweetgreen, **Infinite Kitchens** were introduced **through the 2021 acquisition of Spyce** for $50.7M in equity. It introduces automation to the assembly line of food bowls, reducing labor costs and increasing restaurant level margins (RLMs) by an estimated 750-1000 bps. In addition, the increased efficiency results in substantial order time improvement and potentially increased throughput.

Scalability Concerns

- As outlined by the CFO, they are **only in phase II of development**. This is categorized by a **lack of scaling with IK production**
- Management outlines a **strong growth of retail stores**, but the IKs systems **lack the development to ensure long term success** through large revenue margins. This will require stores, particularly in high traffic areas to **go under for retrofitting** to implement IKs
  - This happened to Penn Plaza and Willis Tower
- Additionally, SG assumes that **economies of scale will begin to impact IK production costs**. This must be questioned - alongside the neglect of consensus models to consider **incremental costs within their modeling**

Competitor Innovation Can Erode Advantages

- Competitors like Chipotle have focused on **increasing worker productivity through "cobots"**
- "Demonstrated through the "**Autocado** ", (which cuts, cores and peels avocados), and most importantly the Chipotle's Augmented Makeline. The machine creates **any version of salad or bowls** (which represent 65% of all orders) using vision systems, radar and LIDAR."
- **<u>Chipotle already has this technology</u>**

Scenario Analysis

Bear	Base	Bull
Initial rollout of Augmented Makeline is successful, and Infinite Kitchen maintains current level efficiency or declines. Sweetgreen is unable to hit targets for Infinite Kitchen expansion due to scalability hiccups.	*Sweetgreen is able to scale infinite kitchens but not enough to meet analyst targets of 7-15 IKs per year. If there are any failures, the stock will sell off.*	*Infinite Kitchen turns out to be more effective due to its scalability. The likelihood is low as only one Infinite Kitchen has been developed by contract manufacturers,*

Valuation and Returns Analysis

Even if Sweetgreen mostly delivers on promises, it can't justify its current pricing and struggles to deliver value

Returns Analysis and Commentary

Summary Statistics: Base Case

Year	2022A	2023A	2024P	2025P	2026P	2027P	2028P	2029P	2030P	2031P	2032P
Revenue ($M)	$470	$584	$726	$825	$889	$981	$1,082	$1,194	$1,318	$1,454	$1,605
% Growth (1)		24.2%	24.3%	13.7%	7.7%	10.4%	10.4%	10.4%	10.4%	10.4%	10.4%
EBITDA ($M)	($147)	($63)	$4	$54	$72	$101	$134	$173	$219	$272	$333
% Margin (2)	-31.2%	-10.8%	0.6%	6.6%	8.1%	10.3%	12.4%	14.5%	16.6%	18.7%	20.8%
Unlevered FCF ($M)	($270)	($162)	($92)	($60)	($51)	($35)	($20)	($2)	$19	$45	$76
% Revenue Conversion	-57.4%	-27.8%	-12.7%	-7.2%	-5.8%	-3.6%	-1.9%	-0.2%	1.5%	3.1%	4.8%
EPS	($1.67)	($0.99)	($0.54)	($0.19)	($0.09)	$0.07	$0.24	$0.44	$0.68	$0.96	$1.29

Returns Analysis

WACC	***11.94%***
Terminal Multiple (3)	22.0x
Implied Enterprise Value ($M)	**1,308**
(+) Cash	257
(-) Debt	0
Implied Equity Value	**1,566**
(/) Weighted SO (Millions)	114
Implied Share Price	**$13.72**
Current Share Price	$39.30
Implied Upside	*65.09%*
3-Year IRR	*29.59%*

Base Case Assumptions

1. Long-term revenue build assumes growth from 231 stores now **to ~650 by 2040**, or **~70% of management's target**, as well as Same-Store Sales growth of **~3.38%, which is in-line with sellside estimates**

2. EBITDA margin is forecasted in two ways: COGS is **cut through labor expense** because of infinite kitchens piercing **75% of stores by 2032** (~10% margin expansion vs estimates of 15%), and **SG&A is near-flat** to reflect management guidance

3. A **terminal multiple of 22x** is used, slightly above late-stage comps (Starbucks, McDonald's, YUM!), to reflect perception that Sweetgreen **earnings are more premium**, **as per EV/Sales performance vs comps**

Situations Analysis

- **Downside** cuts 2040 store target to **500** and has Infinite Kitchens piercing **60%** of stores to reflect our **limited-TAM and IKs risks** theses more aggressively
- **Upside** raises 2040 store target to **1200** and has Infinite Kitchens piercing **98%** of stores to reflect infinite kitchens achieving **universal adoption** and Sweetgreen **overdelivering** on expansion promises

3-Year Returns: 2027 Exit

	Base	Downside	Upside
3-Year Target Price	**$13.72**	**$3.94**	**$43.25**
Implied Upside (%)	*65.09%*	*89.97%*	*-10.05%*
3-Year IRR	*29.59%*	*53.54%*	*-3.24%*
Current Share Price	$39.30		

Conclusion

sg

To justify the Market valuation, Sweetgreen must overdeliver on already unrealistic promises

Thesis Recap

The market views the ability of Sweetgreen management to deliver on 3 ideas extremely favorably: 1) **Grow TAM extremely fast**; 2) **differentiate and expand brand**; and 3) **efficiently roll-out Infinite Kitchens** (IKs). Management cannot meet **any** of these expectations. First, the market is overzealous and not considering that **there aren't even 1,000 viable locations that Sweetgreen could occupy**: when they compromise on location quality, they won't be able to generate the revenue growth that induces them to expand in the first place. Second, with regards to differentiation, existing locations are rapidly losing market share to CAVA, and analysis of Same-Store Sales vs Avg. Sales per Store growth reveals that **new stores perform worse than existing locations**. Finally, the Infinite Kitchen argument carries too many concerns. Primarily, we believe that management **can't implement the 75% piercing of IKs priced in**, nor do they have a way to address competitor implementation of IKs or risks of food poisoning. The market has **no leeway** on Sweetgreen underdelivering on three significant promises with its **extreme premium**, essentially forming a bubble for investors who missed out on Chipotle, but Sweetgreen is **not** the new Chipotle.

Risks & Mitigants

Risk: Infinite Kitchen roll-out is successful

Mitigant: Infinite Kitchen success would **only improve gross margins ~15%**. Additionally, competitor adoption would **erode any competitive advantage** it produces.

Risk: Menu innovation leads to outcompeting CAVA

Mitigant: Sweetgreen still **can't expand to the same Zip Codes** that CAVA can occupy, causing it to fall behind in the long-term, while **new stores are underperforming**.

Catalyst Timeline

IK/Locations Behind Schedule

FY '25:

Sweetgreen falls behind on their IK roll-out and TAM expansion, causing adjustments to sell-side estimates

Profitability Metrics

FY '26:

Earnings turnaround for FY '26 is incredibly vital to current valuations; as IKs and SG&A reductions fail, margins miss in earnings