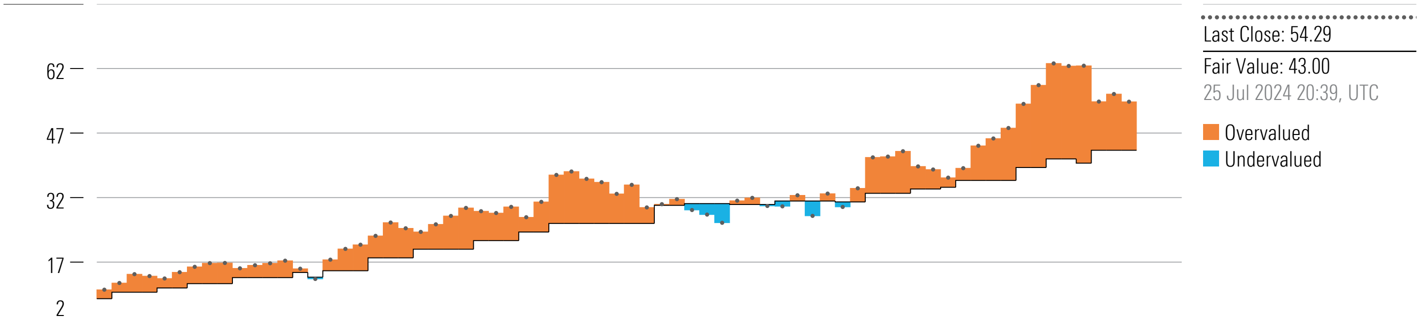
Morningstar Equity Analyst Report | Report as of 10 Sep 2024 15:12, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 1 of 24

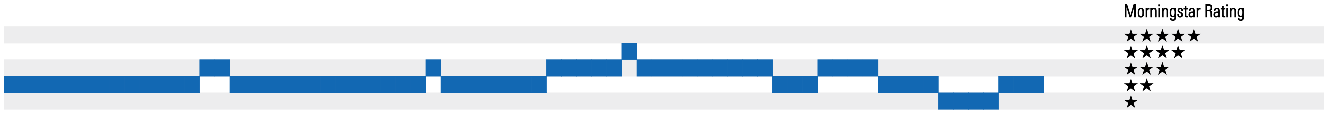
Chipotle Mexican Grill Inc CMG ★★ 9 Sep 2024 21:23, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
54.29 USD 9 Sep 2024	43.00 USD 25 Jul 2024 20:39, UTC	1.26	73.86 USD Bil 10 Sep 2024	Wide	Large Growth	Medium	Exemplary	7 Aug 2024 05:00, UTC

Price vs. Fair Value



	2019	2020	2021	2022	2023	YTD	
	1.25	1.39	1.34	0.89	1.27	1.26	Price/Fair Value
	93.87	65.65	26.07	-20.64	64.83	18.69	Total Return %



Total Return % as of 09 Sep 2024. Last Close as of 09 Sep 2024. Fair Value as of 25 Jul 2024 20:39, UTC.

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The primary analyst covering this company does not own its stock.

[1]The ESG Risk Rating Assessment is a representation of Sustainalytics' ESG Risk Rating.

Starbucks: Luring Brian Niccol Should Stimulate Sagging Coffee Chain

Analyst Note Sean Dunlop, CFA, Senior Equity Analyst, 13 Aug 2024

Leadership matters. Wide-moat Starbucks certainly isn't through the weeds as it navigates an extremely challenging consumer environment, but the addition of Wall Street favorite Brian Niccol to the team stands to restore investor confidence in the battered brand. As we digest the news, we plan to maintain our respective $95 and $43 fair value estimates for Starbucks and wide-moat Chipotle (where Niccol will serve as CEO until Aug. 31, 2024) and our Exemplary Capital Allocation Ratings, although we will reevaluate our outlook for Chipotle once a permanent successor to Niccol is named. The burrito chain will be served in the interim by Chief Operating Officer Scott Boatwright, whose seven years of company experience, in tandem with retiring CFO Jack Hartung's willingness to stay on "indefinitely" with the brand until a permanent CEO is announced, should assuage any immediate concern, despite Chipotle shares falling 13% during Aug. 13 intraday trading (Starbucks shares surged a striking 22%-23%).

We're particularly encouraged by Niccol's sterling restaurant industry track record and favorable timing, the lack of which hampered a forgettable run by Laxman Narasimhan that began in April 2023. In retrospect, our views outlined in a September 2022 note to clients have aged well—at the time, we wrote that "prima facie, the move strikes us as a curious one, particularly when juxtaposed against Howard Schultz's commentary . . . that his permanent successor would have domain expertise, sensitivity to the values and culture of Starbucks, global experience, and a commitment to leading for the long term." Narasimhan's lack of domain experience and standoffish mien likely contributed to his

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Sector	Industry
Consumer Cyclical	Restaurants

Business Description

Chipotle Mexican Grill is the largest fast-casual chain restaurant in the United States, with systemwide sales of $9.9 billion in 2023. The Mexican concept is predominately company-owned, although it recently inked a development agreement with Alshaya Group in the Middle East. It had a footprint of nearly 3,440 stores at the end of 2023, heavily indexed to the United States, although it maintains a small presence in Canada, the UK, France, and Germany. Chipotle sells burritos, burrito bowls, tacos, quesadillas, and beverages, with a selling proposition built around competitive prices, high-quality food sourcing, speed of service, and convenience. The company generates its revenue entirely from restaurant sales and delivery fees.

removal, though we note that his biggest mistake was unfortunate timing, stepping into the brand as a widening inflation gap between grocery stores and restaurants, pressure in the firm's large Chinese market, and souring labor relations finally spilled over into results.

Business Strategy & Outlook Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

Chipotle's business strategy rests on five pillars: running successful restaurants, attracting and retaining diverse talent, making the brand visible, relevant, and loved, investing heavily in restaurant tech and innovation, and improving access and convenience for customers. In our view, the company has carved out an enduring niche in the US restaurant landscape, with competitive menu prices, extreme convenience, and "food with integrity" allowing it to lure away customers from both casual dining and traditional fast-food competitors.

Chipotle's digital investments have seen the firm build a loyalty program 40 million members deep in just five years, with online sales of $1.1 million per store in 2023 outpacing total unit sales at many name-brand competitors. We view a strong loyalty program as accretive to customer lifetime value and the brand's value proposition, spurring increased order frequency, reducing customer churn, and helping the firm drive menu development and marketing strategies based on relevant-time customer data. While we expect many technology features to become table stakes in the industry, we appreciate Chipotle's attention to unmediated access to its customers, building a compelling database of order history, price elasticity, and new product resonance.

The burrito chain's unit development narrative remains compelling, with strong returns on investment driving our high-single-digit annual unit growth estimates. New-format stores (Chipotlanes, digital-only concepts) offer attractive upside, with the latter format representing more than 80% of new store additions and providing a meaningful uplift to store-level sales—as well as a much higher mix of more profitable carryout transactions than conventional units.

We view management's strategy as appropriate, with Chipotle well positioned to meet future customer demands—elevated off-premises mix, blurring lines between fulfillment channels, faster service, increased importance of health and sustainable sourcing—and appearing to boast sufficient pricing power to defray persistent inflationary pressure. It continues to invest ahead of the curve, defending its enviable growth runway.

Bulls Say Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

- Accelerated digital adoption during the pandemic supercharged Chipotle's loyalty program, which should continue to drive increased order frequency and reduce customer churn.
- Chipotlanes should position the brand to better compete with quick-service rivals while opening up new trade areas. They're in 25% of the existing store footprint and in 80% of new unit openings.

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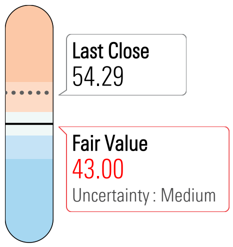
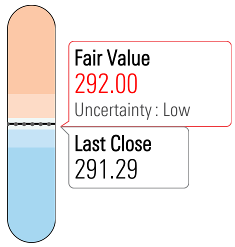
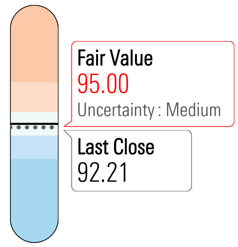
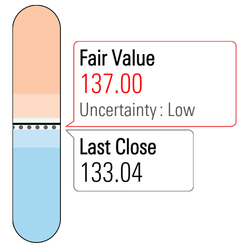
Competitors

	Chipotle Mexican Grill Inc CMG	McDonald's Corp MCD	Starbucks Corp SBUX	Yum Brands Inc YUM
				
Economic Moat	Wide	Wide	Wide	Wide
Currency	USD	USD	USD	USD
Fair Value	43.00 25 Jul 2024 20:39, UTC	292.00 30 Jul 2024 14:55, UTC	95.00 2 Aug 2024 13:53, UTC	137.00 8 Aug 2024 18:11, UTC
1-Star Price	30.10	365.00	128.25	171.25
5-Star Price	58.05	233.60	66.50	109.60
Assessment	Overvalued 9 Sep 2024	Fairly Valued 9 Sep 2024	Fairly Valued 9 Sep 2024	Fairly Valued 9 Sep 2024
Morningstar Rating	★★9 Sep 2024 21:23, UTC	★★★9 Sep 2024 21:21, UTC	★★★9 Sep 2024 21:24, UTC	★★★9 Sep 2024 21:23, UTC
Analyst	Sean Dunlop, Senior Equity Analyst	Sean Dunlop, Senior Equity Analyst	Sean Dunlop, Senior Equity Analyst	Sean Dunlop, Senior Equity Analyst
Capital Allocation	Exemplary	Standard	Exemplary	Standard
Price/Fair Value	1.26	1.00	0.97	0.97
Price/Sales	7.04	8.22	2.88	5.34
Price/Book	20.06	—	—	—
Price/Earning	51.60	24.69	25.83	25.54
Dividend Yield	0.00%	2.29%	2.47%	1.97%
Market Cap	74.35 Bil	208.95 Bil	104.49 Bil	37.41 Bil
52-Week Range	35.37—69.26	243.53—302.39	71.55—107.66	115.53—143.20
Investment Style	Large Growth	Large Blend	Large Value	Mid Blend

- The firm remains behind its 2014 throughput high-water marks, suggesting that recent operational initiatives targeting transaction capacity could provide a durable, multiyear lever for growth.

Bears Say Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

- Consumer spending may shift toward grocery and convenience store channels if the macroenvironment continues to deteriorate, as it has during previous periods of pressure.
- Input availability for key inputs like avocado, cilantro, and poblano peppers could complicate international expansion, with the firm forced to rely on imports rather than farm-to-table supplies in certain markets.
- Competition for real estate with drive-thru capacity has meaningfully increased, potentially forcing the chain to pay a premium for those pads, posing a risk to restaurant margin expansion.

Economic Moat Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

MORNINGSTAR®

The restaurant industry is intensely competitive, with nonexistent switching costs and constantly evolving customer demands rendering it difficult for operators to carve out durable competitive advantages. Firms able to do so, in our view, generally benefit from some combination of pricing power attributable to an enduring brand intangible asset, strong relationships with master franchise partners, an internationally replicable concept, compelling store-level economics, or scale-driven cost advantages. In our view, Chipotle merits a wide economic moat. Its industry-leading comparable sales growth, loyal customer base, and advantaged positioning to meet changing consumer demands are likely to catalyze excess returns through the 20-year horizon implied by our wide moat rating. Our forecast for adjusted returns on invested capital embodies this view, with average ROICs of 40% during our explicit forecast healthily outpacing the firm's 9% cost of capital.

Following Chipotle's food safety scares in 2015-18, we maintained a narrow moat rating for the firm, with the view that the Mexican chain may have permanently impaired its brand intangible asset, which we anticipated would materialize through slower comparable sales growth and elevated marketing expenses as the firm "bought" traffic with free and discounted food. We viewed increased costs attributable to onerous food safety requirements, legal scrutiny, and outperformance by fast-casual competitors as likely to stymie growth, while ongoing absence of the firm's loyal customers due to restaurant closures could have instigated a migration toward competing health-oriented fast-casual concepts. In retrospect, some of our concerns were valid—average store sales dropped nearly 20% from $2.4 million before the crisis to a bottom of $1.9 million in the fourth quarter of 2016 before slowly recovering to $2.5 million in 2021—but a strong rebound in unit growth and comparable-store sales performance between 2017 and 2020 drove double-digit systemwide sales growth, allowing the firm to quickly return to generating excess returns for shareholders after a brutal 2016.

In our view, a slew of changes since the nadir of the food safety scare suggest that the firm's brand intangible asset has materially strengthened. We're particularly impressed with operational enhancements, technology investments, and disciplined pricing, which we believe are largely responsible for the meaningful margin expansion and broader appeal that Chipotle has enjoyed over the past few years. A narrowing value gap with the quick service restaurant (QSR) channel, attributable to disciplined pricing, has allowing Chipotle to tap into a broader customer base, and the firm boasts an assortment of other levers (daypart and menu expansion, premium beverage innovation, international development, assumption of leverage, refranchising) that underpin meaningful longer-term potential.

Addressing these in sequence, Chipotle's operational enhancements, including the addition of a digital-only second make line and the rollout of "Chipotlanes," or order-ahead drive-thrus, have materially increased throughput capacity, allowing stores to offer competitive prices and make up the difference on volume. The introduction of the second make line appears particularly prescient, with digital orders still clocking around 35% of total sales, even with a strong recovery of in-store traffic.

These operational improvements are enabled by technology investments, like the firm's attention to seamless ordering across platforms, whether third-party delivery, white-label delivery, mobile order and pickup, or traditional counter service. As we see it, Chipotle remains in the early innings of rolling out its technology roadmap, with digital acuity likely to remain integral to the firm's ongoing success. We believe that omnichannel ordering and a 40 million-member loyalty program provide a strong foundation for one-to-one marketing, funneling orders toward high-margin fulfillment channels, and driving data-driven menu innovation in line with customer demands. The firm's success in the digital vertical is difficult to overstate—Chipotle's digital sales per restaurant were nearly $1.1 million in 2023, which would have been good enough to be within the top 50 US restaurant chains by sales volume (per Technomic) on a stand-alone basis.

Regarding price discipline, Chipotle has grown increasingly attractive to a price-sensitive clientele, with its chicken burritos and bowls selling for less than $10 in many markets and representing a viable alternative to many QSR offerings, while being as much as 20%-30% cheaper than lookalike fast-casual competitors. While foot traffic and app usage data indicate that Chipotle customers skew younger and more affluent than most pure QSR competitors, they also shop at fast-food stalwarts like McDonald's and Burger King, leading us to believe that the brand should not be considered in complete isolation from conventional QSRs. Instead, should average checks continue to converge, and as Chipotle offers sufficient capacity, drive-thru convenience through its Chipotlanes (now 25% of its footprint), and comparable or better speed of service to quick-serve peers, we expect a broader swath of the population to include the Mexican chain in its decision about an affordable meal out. This view is validated by high-single-digit traffic growth in the firm's most recent quarter against a backdrop of declining traffic industrywide, suggesting that Chipotle's strong value positioning is allowing the firm to capture transaction share across customer income cohorts and dayparts. Finally, we view food safety risks as unlikely to materialize again at scale, with DNA-based bacterial testing upon delivery, sous vide meat preparation at distribution centers, third-party inspections, preshift employee wellness checks, mandatory hand-washing, and air purification systems representing some of the exhaustive steps the brand has taken to shore up its supply chain.

Turning to Chipotle's brand intangible asset, we believe that robust comparable-store sales performance, strong loyalty program uptake, and compelling unit economics attest to the brand's strength, while forward-looking investments stand to entrench pricing power and affinity moving forward. In our view, comparable sales performance represents the most appropriate gauge of brand strength, with the best operators able to consistently outpace inflation between pricing power and increases in guest traffic. A strong brand brings consumers into the store and entices them to pay more for their food than they would at a competitor's restaurant, all else equal. To this effect, Chipotle has seen median comparable sales growth of 8.1% over the past five years, more than offsetting inflation during that period and comfortably outperforming the vast majority of industry competitors. While the firm has been historically reluctant to flex its pricing power—leaning instead on comparable transaction and mix growth—it was able to completely offset margin pressure from delivery costs during 2020 and 2021, raising menu prices by 17% in the channel and funneling orders toward more profitable mobile-order, Chipotlane, and in-store fulfillment, with minimal impact to volume. Chipotle's success in defraying recent costs leaves us encouraged as restaurants are forced to adapt to a changing competitive environment, with labor and input cost inflation continuing to push higher in 2024 in no small part due to California's rollout of out an industry wage floor of $20, a roughly 20% increase from the prelegislation market rate.

Chipotle's loyalty program rollout has also proved encouraging, with 40 million registered members putting the chain in the same league as some of the most successful loyalty programs in the industry—Domino's, Starbucks, and Panera. This performance is particularly impressive considering the much smaller scale of its domestic footprint (roughly 3,500 stores against more than 18,500 at Starbucks). Loyalty program members have historically been highly incremental and permit the firm to bolster sales through promotions and channel cross-selling, with just 15%-20% historical overlap between in-store and mobile app users.

We view Chipotle's unit economics as among the best in the industry, with our estimates suggesting cash-on-cash returns of roughly 60% for full-volume stores, suggesting a payback period just shy of two years. This suggests materially higher returns on investment than most competitive QSR concepts, which tend to see payback in four to six years, attributable to larger footprints and lower restaurant margins at the latter. While we often cite unit economics and growth as a proxy for franchisee health, given the Mexican chain's majority company ownership, we approach it in this case as reinforcing the firm's high-single-digit (8%-10%) unit growth aspirations instead. While growth is not in and of itself evidence of a competitive advantage, it does allow Chipotle to generate scale over advertising expenditure, supply chain and quality assurance investments, (relatively) fixed labor and rent costs, and ongoing investments in the technology stack, allowing it to more effectively compete with larger QSR peers. Although marketing expenses jumped sharply in 2016 as the firm relied on free meals and discounting to drive traffic after food safety concerns, trailing five-year figures of 2.6% of system sales are materially lower than wide-moat McDonald's (4%), wide-moat Yum Brands (4.5% at KFC, 6% at Pizza Hut, 5.5% at Taco Bell), and wide-moat Domino's Pizza (6%), dispelling our concerns about a permanent uptick in discounting and promotional activity to buy comparable sales growth, which would point to brand impairment.

Finally, we view the likelihood of durable economic value creation as quite high for the restaurant brand, which finds itself on the leading edge of most of the changes we expect to affect the restaurant industry over the medium to long term. Though Chipotle saw economic value destruction in 2016, we view the likelihood of similar events as exceedingly unlikely—and to the extent that an outbreak were

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to happen, supply chain tracing should allow it to be quelled more quickly and traced to its source, which represented perhaps the biggest systemic issue from the original incident. In our view, risks lie to the upside for the brand, which boasts an attractive following among an affluent, experience-oriented millennial and Gen Z customer base that spends materially more on eating out than older cohorts. Chipotle's technological proficiency has already borne fruit, but a robust loyalty program and omnichannel ordering—increasing store capacity and allowing orders to be funneled toward higher margin channels—is a positive, while an order-ahead drive-thru eliminates the labor and payment pain points associated with the traditional QSR model. Further, $1.1 million in store-level digital sales offers longer-term potential, positioning Chipotle as one of the few operators in our coverage with viable aspirations to open smaller-concept, digital-only stores, which are heavily reliant on a brand and digital platform to drive traffic. Ultimately, we expect operating leverage over store-level expenses, corporate general and administrative expenses, and rental expenses to offer meaningful operating margin improvement as Chipotle has finally eclipsed pre-2016 average store sales figures, with operational efficiencies, higher-margin premium beverages, Chipotlanes, and smaller-format stores contributing to strong ROIC expansion—to nearly 50% in 2033, by our estimates.

Fair Value and Profit Drivers Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

We've raised our fair value estimate for Chipotle to $43 from $40 after digesting the firm's second-quarter results. Strong market share gains and operational leverage tied to striking 8.7% growth in comparable transactions (and 11% growth in comparable store sales) suggest more upside to the firm's already robust restaurant margin profile than originally contemplated, leading us to raise our long-term prognosis to 31% from 29% previously. While this would be comfortably the highest rate in our restaurant coverage, it aligns with management commentary on prior calls and recognizes that transaction-led growth drives incremental margins of nearly 40%.

Consistent with the rest of our restaurant coverage, we view comparable-store sales, new unit openings, and restaurant margins as the most important valuation drivers for Chipotle. We're impressed by management's prescient investments in loyalty and mobile ordering, with the adoption of operational improvements from CEO Brian Niccol's Taco Bell playbook (complementary rotating menu items, targeted marketing) helping to drive comparable sales outperformance relative to peers. Our forecast calls for 4.7% average annual comparable sales growth through 2033, with investments in peak transaction capacity, price increases roughly in line with inflation, and untapped menu development levers providing qualitative support for those aggressive estimates.

We expect Chipotle to open just shy of 300 net units in 2024, with Chipotlanes and smaller-footprint stores continuing to unlock new trade areas for the firm. Our model calls for high-single-digit unit growth through 2033 (8.5%), with the firm leveraging commanding unit economics (we estimate cash on cash returns in the 60% range today, against QSR peers in the midteens to low 20s) and strong cash flow generation to push a median run rate of approximately 425 net new stores per year over that period, ahead of the absolute figures in the mid-2010s. We view management's long-term target of 7,000 US units as achievable, with strong uptake in smaller and rural markets and meaningful digital volumes the key catalysts for growth.

We expect strong restaurant margin expansion to around 31% in 2033 as fixed-cost leverage, the roll-off of pandemic-related expenses, and modest leverage over labor costs provide upside. Robust comparable-store sales growth defends the store-level economic model, and Chipotle's proven ability to improve its transaction capacity, innovate around its established core menu, and capture industry traffic share with a compelling value proposition should bear fruit for years to come.

Risk and Uncertainty Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

We maintain a Medium Morningstar Uncertainty Rating for Chipotle as we consider our qualitative assessment of the firm's systematic risks alongside our quantitative methodology.

Chipotle remains a compelling growth story, with system sales consistently expanding at double-digit annual rates as the brand aggressively develops its US footprint and benefits from impressive, largely transaction-driven same-store sales growth. In our view, maintaining these results against lofty investor expectations will require nearly flawless execution as the firm continues to scale its supply chain, source new real estate opportunities, and enter new trade areas. Market expectations don't allow Chipotle much room to catch its breath, with our own expectations for high-single-digit percentage growth in net new units through 2033 placing heavy demands on Chipotle's developmental, technological, and operational teams, while competition for real estate, construction crews, and staff adds a layer of risk to our forecasts.

We believe Chipotle's environmental, social, and governance risk remains muted on the product side and see labor relations as the firm's largest ESG concern going forward. With restaurant operators representing the bottom of the labor market stack, increased attention to minimum wage growth and worker benefits could pressure results, forcing restaurants to look for ways to keep costs in check by reducing their dependency on labor—particularly if efforts like California's wage floor restaurant legislation gain broader national traction. Efforts toward automation are a step forward, if not a panacea, and Chipotle's strong value positioning and restaurant margins help insulate it from the worst of labor market volatility.

Chipotle maintains exposure to risks consistent with the rest of our restaurant coverage, including input cost inflation, pressure on consumer wallets, and category competition.

Capital Allocation Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

We assign Chipotle an Exemplary Capital Allocation Rating after considering the firm's performance against the three pillars of our capital allocation framework. Balance sheet strength and a strong investment record support our view, with our assessment of shareholder returns remaining mixed.

Chipotle carries no long-term debt, with $1.5 billion in cash, investments, and cash equivalents at the end of the second quarter of 2024 and access to a $500 million undrawn credit line providing a substantial buffer. Lease payments for restaurants are the firm's only meaningful fixed charges. While the firm's balance sheet risk is minimal, we wonder if the assumption of some debt might help better optimize the chain's cost of capital, providing dry powder to fund international expansion (or be returned to shareholders). Nonetheless, we understand management's reluctance to assume leverage and its associated constraints, given the firm's growth profile and ready access to internally generated funds. While we expect investors to push for capital structure optimization as domestic growth slows, we appreciate management's attention to leveraging its brand intangible asset and driving strong domestic unit growth before adding the distraction of a broader global push, particularly with our assessment that the European market will prove less amenable to fast-casual development than the US and Canada.

Given Chipotle's deep bench of management talent featuring decades of experience at strong global brands (McDonald's, Starbucks, Taco Bell), we expect investments to remain moat-accretive through our forecast, resulting in ROICs strengthening from 27% in 2023 to 50% in 2033 as incremental capital is channeled toward high-return projects. Recent investments have proved moat-accretive, with a digital push driving seamless in-app and online ordering, the 2019 relaunch of the loyalty program quickly becoming a strong vehicle for customer acquisition and driving higher customer lifetime value, and new store development providing robust 60% cash-on-cash returns (net operating income/initial cash outlay), by our calculations. We do not expect diminishing returns on new units over the course of our 10-year forecast, with rural stores featuring similar or better returns on incremental investment and unlocking a sizable addressable market. Investments have positioned the brand well to compete in an environment liable to increasingly skew off-premises, move closer to customers, provide faster fulfillment, and offer customizable, "better for you" fare that readily suits a variety of dietary restrictions.

Further, we're encouraged by a compensation structure that privileges same-store sales growth (driven by guest traffic, menu pricing, and mix) and restaurant margins, which should align management interests with those of investors. In our view, this structure encourages investments in operational efficiency, menu development, and customer experience, which should allow Chipotle to support its brand through the 20-year horizon implied by our wide moat rating. Our model calls for ongoing investments in technology, equipment, and maintenance capital expenditures, with robust free cash flow generation, a willingness to embrace new technology, and an emphasis on a unique, unmediated customer experience allowing the firm to remain a step ahead of competitors.

We view Chipotle's capital returns philosophy as mixed, with the magnitude of distributions appearing appropriate at this stage in the company’s life cycle, but with share repurchases proving moderately

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dilutive, as they have historically been conducted at prices above our fair value estimate. We forecast buybacks in the low-single-digit percentage of shares through 2028, and we've layered in a modest dividend payment in the back half of our forecast (initiated in 2028) as unit growth rates begin to slow and as balance sheet cash begins to build—though we acknowledge management's reluctance, we suspect pressure from investors will build as cash balances do. Considering these factors, we assign the firm an Exemplary Capital Allocation Rating and expect management's decisions to be accretive to the firm's competitive advantages.

Analyst Notes Archive

Chipotle Earnings: Transaction-Led Share Gains Lay Market Concerns to Rest; Shares Still Pricey

Sean Dunlop, CFA, Senior Equity Analyst, 25 Jul 2024

Wide-moat Chipotle reported strong second-quarter earnings, posting 11% comparable store sales growth on the back of 8.7% growth in comparable transactions as operational improvements and a triumphant return of the chicken al pastor limited-time offer resonated with consumers. While Chipotle kept its full-year comparable store sales and store development guidance, resulting in very little expected change to our $11.4 billion sales and $1.04 diluted earnings per share estimates for the year, we're increasingly encouraged by the ramifications of transaction-led comparable sales growth for the firm's long-term store-level profitability prospects. So, we expect to lift our long-term restaurant margins by about 200 basis points to 31.2% by 2033 as a result of stronger expected leverage (incremental transactions flow through at about a 40% margin rate), driving an expected mid-single-digit percentage increase to our $40 per share fair value estimate. However, shares continue to look meaningfully overvalued after a 4%-5% increase in volatile after-market July 24 trading.

Quarterly results modestly exceeded our expectations—$2.95 billion in revenue aligned with our forecast, while $0.33 in diluted EPS comfortably topped our $0.27 estimate. Nevertheless, we're impressed with the firm's ability to continue to attract traffic, with 11% same-store sales edging our 9.5% estimate by a wide margin. This outperformance attests to the chain's compelling value proposition, which continues to resonate despite challenging trends in the restaurant industry. For perspective, Revenue Management Solutions data suggests that quick-service restaurant traffic fell 2.3% during the second quarter, implying material market share gains for the burrito stalwart. Slight underperformance relative to our expectations for unit growth saw consolidated revenue arrive as expected, though we continue to expect Chipotle to open roughly 300 net stores during 2024 before a 2025 acceleration to north of 360.

Chipotle: Adjusting Fair Value Estimate to $40 per Share After Stock Split; Shares Remain Overvalued Sean Dunlop, CFA, Senior Equity Analyst, 26 Jun 2024

Effective June 26, wide-moat Chipotle shares have split 50-for-1, one of the largest stock splits in the history of the New York Stock Exchange. Each shareholder of record on June 18, 2024, will receive 49 additional shares for each share held, and the firm will offer a one-time equity grant for both its restaurant general managers and its crew members with more than 20 years of service. Given that we expect a negligible dilutive impact from the latter move, we revise our fair value estimate to $40 per share from $2,050, leaving shares looking expensive on a post-split basis. Our assessment of the firm's intrinsic valuation in dollar terms remains unchanged, with our $40 revised fair value estimate continuing to correspond with an equity fair value just north of $55 billion.

Chipotle Earnings: Robust Growth Prospects, but Shares Too Pricey Sean Dunlop, CFA, Senior Equity Analyst, 25 Apr 2024

We are believers in wide-moat Chipotle Mexican Grill's robust competitive position and growth prospects, but the share price leaves us with indigestion. After another quarter of outperformance, we expect to raise our $1,950 fair value estimate by a mid-single-digit percentage, but the stock would still trade at almost a 50% premium to our revised valuation, deep in 1-star territory. We suggest that investors await a more attractive entry point.

For the first quarter, Chipotle posted $2.70 billion in sales and $13.37 in adjusted diluted earnings per share, matching our $2.71 billion sales estimate and exceeding our $11.85 EPS forecast. We plan to bump our 2024 comparable-store sales growth estimate to 7.5% from 5%, consistent with management's mid-single-digit to high-single-digit guidance (raised from mid-single-digit), and our diluted EPS estimate by about 5%-6%, reflective of operating leverage and strong restaurant margin performance. It was encouraging to see Chipotle post strong transaction growth of 5.4% despite consistent traffic declines industrywide. We believe that firms with strong value-for-money positioning will capture traffic share in the near term, and Chipotle's market share gains across both income demographics and dayparts seem to validate this view.

We think the chain's throughput improvements, which reflect historically low staff turnover and its commitment to operational excellence through its "four pillars of throughput," should provide a multiyear comparable-store sales growth lever. While average unit volume of $3.1 million is historically high, the firm still has headroom between its peak historical throughput rates in 2014 and its current mid-20s (peak 15-minute entree capacity) cadence systemwide. 2014 is far from a ceiling, in our eyes, as Chipotle has added an entire digital business and second make line in the interim.

Biggest Restaurant Brands Set To Gain Market Share as Industry Navigates Tough Environment

Sean Dunlop, CFA, Senior Equity Analyst, 15 Apr 2024

As we gear up for the release of first-quarter earnings, our top picks in the restaurant industry remain wide-moat McDonald's and wide-moat Starbucks, trading at 14% and 19% discounts to our $312 and $105 fair value estimates, respectively. While industry traffic has been depressed for two years, both brands boast strong digital platforms that allow them to defend transaction frequency without indiscriminate national discounting, and both benefit from scale-driven cost advantages that should allow them to meet the needs of the increasingly value-sensitive consumer without sacrificing financial performance. These are the two most important factors, in our view, that will distinguish the best and worst performers in our industry coverage over the coming years. The industry looks fairly priced in aggregate, trading at a 3% premium to our market-cap weighted fair value estimates. The aggregate figure masks a very bimodal return distribution: Brands like narrow-moat Wingstop (up 108% annually) and wide-moat Chipotle (74%)—which boast strong unit economics and have taken material industry transaction share—have materially outperformed brands like no-moat Wendy's (down 9%) and narrow-moat Papa John's (down 17%), which have not. Those top-performing brands are fully priced, trading at material premiums to our intrinsic valuation (163% and 52%, respectively), suggestive of meaningful execution risk.

The industry looks set for a challenging couple of years, despite a recent rebound in consumer real hourly income, which tends to be strongly predictive of consumption spending. From a macroeconomic perspective, that's tied to two key factors: a divergence between income and spending, driven by recovering savings rates, and an unusually large share of wallet funneled toward food away from home (7.4% of total income, against a long-term average of 6.8%). We expect gradual normalization in 2024 and 2025, with our estimates calling for 2% real industry growth over that period.

Chipotle: Stock Split Doesn't Affect Valuation; We Love Prospects but Stock Price Gives Indigestion

Sean Dunlop, CFA, Senior Equity Analyst, 20 Mar 2024

Wide-moat Chipotle's board of directors has approved a 50-for-1 stock split, which we expect to be approved at the company's general meeting on June 6. The net effect is that each Chipotle shareholder would receive 49 extra shares for each share they hold today after the market closes on June 25, bringing the firm's total share count to roughly 1.4 billion, up from 27.4 million today. Chipotle's stock price rose nearly 7% on the news, which strikes us as myopic. To be fair, a cheaper per-share stock price could allow more retail investors to purchase the stock that might previously have been locked out of the market, but the firm's underlying cash flow prospects, competitive position, and valuation remain unchanged by the move. As a result, we expect no change to our $1,950 fair value estimate, and view shares as meaningfully overvalued.

We remain big fans of Chipotle's growth narrative. Our forecasts contemplate a 13%, 16%, and 19% compound annual growth rate in sales, operating profit, and earnings per share, respectively, over the decade to come, which is astounding given the firm's scale ($10 billion in 2023 revenue). Chipotle derives ethereal cash payback periods between two to three years on new stores, continues to expand its attractive Chipotlane drive-thru format, and should continue to grow its comparable store sales ahead of inflation as it leverages its 38-million-member loyalty program, invests in throughput-driving initiatives, and continues to boast excess capacity through its second make line. The net effect is further improvement to an already stellar 26% restaurant margin, with our forecast calling for 30% restaurant and 22% operating margins in a decade, underpinning our 8.3% annual unit growth forecast through 2033. Nevertheless, it's tough for us to palate the nearly 60 times 2024 earnings multiple that current prices imply. We admire the company, but its stock price continues to leave us queasy.

Chipotle Earnings: Strong Traffic and Unit Growth Are Encouraging, but Share Prices Still Concern Us Sean Dunlop, CFA, Senior Equity Analyst, 7 Feb 2024

Wide-moat Chipotle posted strong quarterly earnings, with sales growth across income cohorts and an impressive 7.4% increase in comparable transactions assuaging market concerns after a few high-profile earnings misses. While we expect to leave our 2024 targets for $11.1 billion in revenue and 8.8% unit growth largely intact, we expect to raise our $1,800 fair value estimate by a high-single-digit percentage as we now forecast a sharper increase in net unit growth and comparable store sales over the medium term. More concretely, we now expect annual comparable store sales growth of 5% and unit growth of 9.4% between 2024 and 2028, up from 4.6% and 9%, respectively, driven by normalizing construction timelines and stronger comparable store sales benefits from its throughput initiatives and loyalty program innovation than previously expected. We also plan to decrease our Morningstar Uncertainty Rating to Medium from High as we reconsider the firm's sensitivity to systematic risk factors.

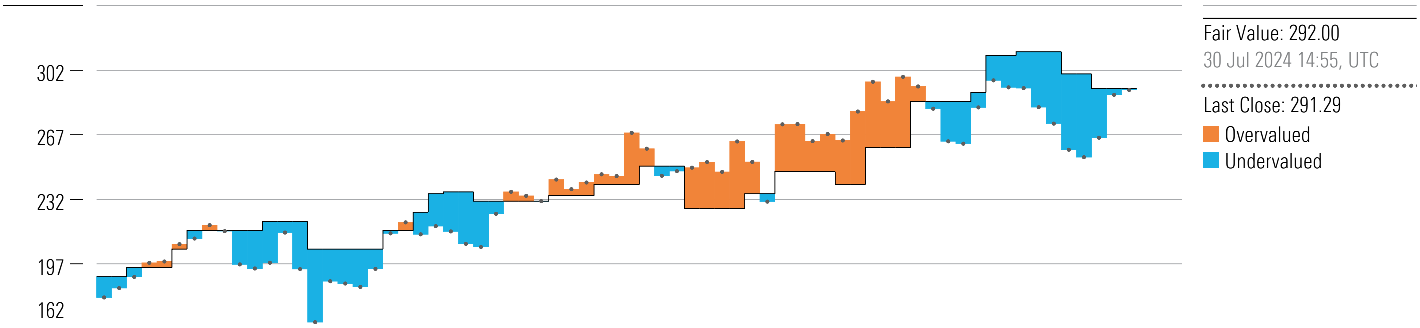
The two biggest stories from earnings, in our view, were Chipotle's ongoing strength in comparable transaction growth, and the firm's ability to open stores at a historically fast pace while maintaining strong new unit productivity (89%). Considering the former, the firm's 8.4% comparable store sales print edged our 8% expectation, and its 7.4% growth in comparable transactions is particularly impressive when juxtaposed against a year and a half of U.S. restaurant industry traffic declines. Considering the latter, while the firm's 250 net units fell slightly short of our earlier expectation (263 stores), our impression is that the firm will achieve the high end of its 8%-10% targeted unit growth range in 2025, and should blow through its estimated 7,000 unit U.S. addressable market ceiling in 2030. Quarterly revenue of $2.5 billion and adjusted earnings per share of $10.36 arrived roughly in line with our $2.5 billion and $10.47 estimates, respectively.

Morningstar Equity Analyst Report | Report as of 10 Sep 2024 15:12, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 14 of 24

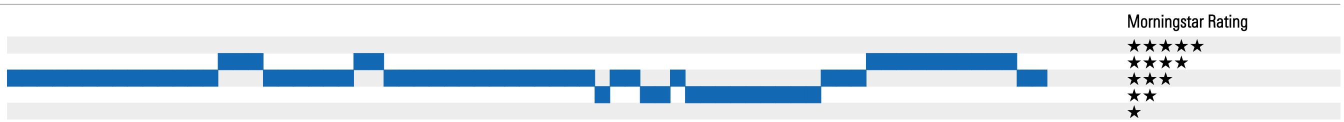
Chipotle Mexican Grill Inc CMG ★★ 9 Sep 2024 21:23, UTC

Competitors Price vs. Fair Value

McDonald's Corp MCD

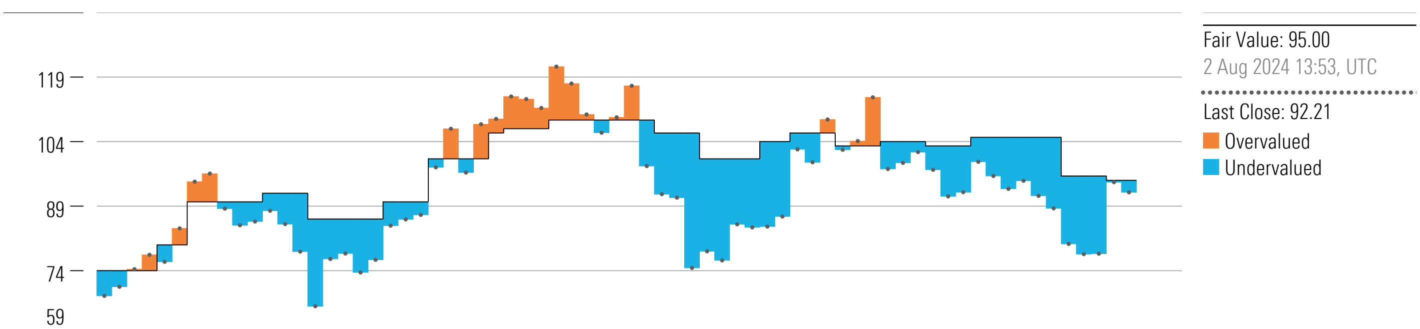


	2019	2020	2021	2022	2023	YTD	
	0.90	0.91	1.12	1.07	0.96	1.00	Price/Fair Value
	13.95	11.14	27.37	0.42	14.88	-0.07	Total Return %

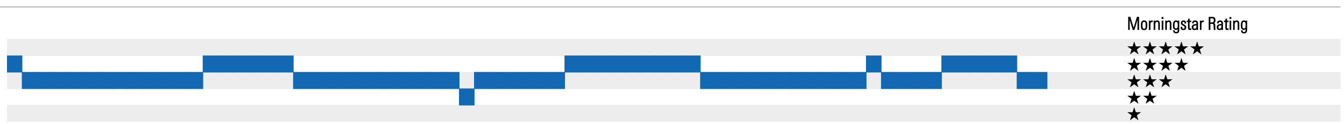


Total Return % as of 09 Sep 2024. Last Close as of 09 Sep 2024. Fair Value as of 30 Jul 2024 14:55, UTC.

Starbucks Corp SBUX



	2019	2020	2021	2022	2023	YTD	
	0.96	1.07	1.07	0.94	0.91	0.97	Price/Fair Value
	38.84	23.59	11.06	-13.48	-1.04	-2.18	Total Return %



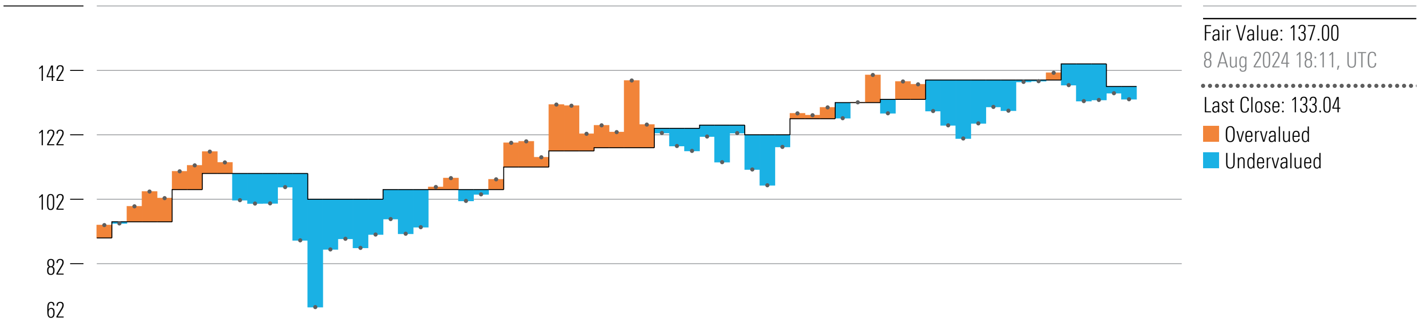
Total Return % as of 09 Sep 2024. Last Close as of 09 Sep 2024. Fair Value as of 2 Aug 2024 13:53, UTC.

Morningstar Equity Analyst Report | Report as of 10 Sep 2024 15:12, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 15 of 24

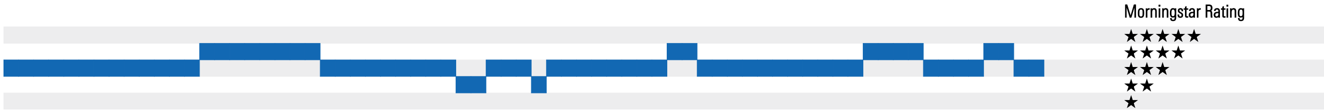
Chipotle Mexican Grill Inc CMG ★★ 9 Sep 2024 21:23, UTC

Competitors Price vs. Fair Value

Yum Brands Inc YUM



	2019	2020	2021	2022	2023	YTD
Price/Fair Value	0.92	1.03	1.18	1.01	0.94	0.97
Total Return %	11.41	9.64	29.75	-6.12	3.90	3.36



Total Return % as of 09 Sep 2024. Last Close as of 09 Sep 2024. Fair Value as of 8 Aug 2024 18:11, UTC.

Morningstar Equity Analyst Report | Report as of 10 Sep 2024 15:12, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 16 of 24

Chipotle Mexican Grill Inc CMG ★★ 9 Sep 2024 21:23, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
54.29 USD 9 Sep 2024	43.00 USD 25 Jul 2024 20:39, UTC	1.26	73.86 USD Bil 10 Sep 2024	Wide	Large Growth	Medium	Exemplary	7 Aug 2024 05:00, UTC

Morningstar Historical Summary

Financials as of 30 Jun 2024

Fiscal Year, ends 31 Dec	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	TTM
Revenue (USD Mil)	4,108	4,501	3,904	4,476	4,865	5,586	5,985	7,547	8,635	9,872	5,675	10,663
Revenue Growth %	27.8	9.6	-13.3	14.6	8.7	14.8	7.1	26.1	14.4	14.3	16.2	14.9
EBITDA (USD Mil)	844	924	222	460	536	691	575	1,100	1,498	1,953	1,222	2,181
EBITDA Margin %	20.5	20.5	5.7	10.3	11.0	12.4	9.6	14.6	17.3	19.8	21.5	20.5
Operating Income (USD Mil)	733	794	76	296	334	478	336	845	1,211	1,633	1,055	1,850
Operating Margin %	17.8	17.6	1.9	6.6	6.9	8.6	5.6	11.2	14.0	16.5	18.6	17.3
Net Income (USD Mil)	445	476	23	176	177	350	356	653	899	1,229	815	1,410
Net Margin %	10.8	10.6	0.6	3.9	3.6	6.3	5.9	8.6	10.4	12.5	14.4	13.2
Diluted Shares Outstanding (Mil)	1,576	1,575	1,489	1,428	1,398	1,415	1,421	1,426	1,403	1,386	1,381	1,382
Diluted Earnings Per Share (USD)	0.28	0.30	0.02	0.12	0.13	0.25	0.25	0.46	0.64	0.89	0.59	1.02
Dividends Per Share (USD)	—	—	—	—	—	—	—	—	—	—	—	—

Valuation as of 30 Aug 2024

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Recent Qtr	TTM
Price/Sales	5.5	3.3	2.9	1.9	2.5	4.4	6.8	6.9	4.7	6.7	8.5	7.3
Price/Earnings	53.5	28.7	156.3	55.9	64.1	76.3	166.7	69.9	48.3	54.3	66.7	55.2
Price/Cash Flow	31.3	21.0	30.3	18.7	20.8	35.6	53.5	52.1	28.8	33.1	45.7	41.3
Dividend Yield %	—	—	—	—	—	—	—	—	—	—	—	—
Price/Book	11.2	6.1	7.5	5.8	8.3	14.3	21.5	21.2	16.5	21.7	25.6	20.7
EV/EBITDA	24.6	14.8	47.6	16.5	21.1	36.5	71.2	46.9	27.6	33.5	0.0	0.0

Operating Performance / Profitability as of 30 Jun 2024

Fiscal Year, ends 31 Dec	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	TTM
ROA %	19.6	18.1	1.0	8.7	8.2	9.5	6.4	10.3	13.2	16.4	9.6	17.1
ROE %	25.1	23.0	1.3	12.7	12.6	22.4	19.2	30.3	38.5	45.3	24.1	43.5
ROIC %	25.1	23.0	1.3	12.7	12.1	11.0	7.3	11.8	14.8	17.9	10.4	18.5
Asset Turnover	1.8	1.7	1.6	2.2	2.3	1.5	1.1	1.2	1.3	1.3	0.7	1.3

Financial Leverage

Fiscal Year, ends 31 Dec	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Recent Qtr	TTM
Debt/Capital %	—	—	—	—	—	61.4	59.4	59.0	59.6	55.4	52.0	—
Equity/Assets %	79.6	78.1	69.2	66.7	63.6	33.0	33.8	34.5	34.2	38.1	41.6	—
Total Debt/EBITDA	—	—	—	—	0.0	4.1	5.5	3.2	2.5	2.1	3.5	—
EBITDA/Interest Expense	—	—	—	—	—	—	—	—	—	—	—	—

Morningstar Analyst Historical/Forecast Summary as of 25 Jul 2024

Financials

Fiscal Year, ends 31 Dec 2023	2022	2023	Estimates 2024	2025	2026
Revenue (USD Mil)	8,635	9,872	11,308	13,528	15,627
Revenue Growth %	14.4	14.3	14.5	19.6	15.5
EBITDA (USD Mil)	1,447	1,877	2,197	2,824	3,420
EBITDA Margin %	16.8	19.0	19.4	20.9	21.9
Operating Income (USD Mil)	1,160	1,558	1,854	2,367	2,892
Operating Margin %	13.4	15.8	16.4	17.5	18.5
Net Income (USD Mil)	899	1,229	1,443	1,798	2,196
Net Margin %	10.4	12.5	12.8	13.3	14.1
Diluted Shares Outstanding (Mil)	28	28	1,375	1,347	1,316
Diluted Earnings Per Share(USD)	32.04	44.34	1.05	1.34	1.67
Dividends Per Share(USD)	0.00	0.00	0.00	0.00	0.00

Forward Valuation

	2022	2023	Estimates 2024	2025	2026
Price/Sales	4.5	6.4	6.6	5.5	4.8
Price/Earnings	43.3	51.6	51.7	40.5	32.5
Price/Cash Flow	—	—	—	—	—
Dividend Yield %	—	—	—	—	—
Price/Book	16.4	20.7	21.8	18.9	16.7
EV/EBITDA	28.6	34.8	35.1	27.3	22.6

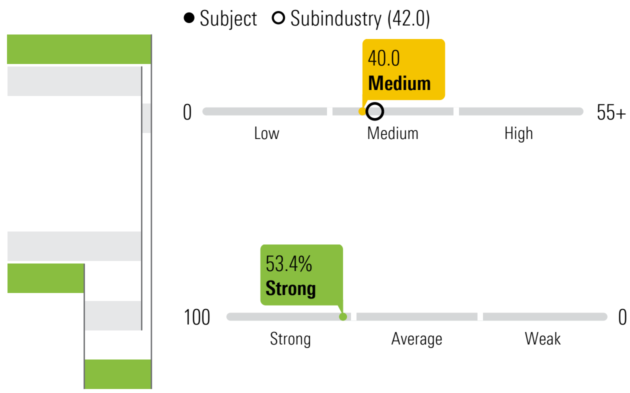
Morningstar Equity Analyst Report | Report as of 10 Sep 2024 15:12, UTC | Reporting Currency: USD | Trading Currency: USD | Exchange: NEW YORK STOCK EXCHANGE, INC. Page 17 of 24

Chipotle Mexican Grill Inc CMG ★★ 9 Sep 2024 21:23, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Equity Style Box	Uncertainty	Capital Allocation	ESG Risk Rating Assessment[1]
54.29 USD 9 Sep 2024	43.00 USD 25 Jul 2024 20:39, UTC	1.26	73.86 USD Bil 10 Sep 2024	Wide	Large Growth	Medium	Exemplary	7 Aug 2024 05:00, UTC

ESG Risk Rating Breakdown

Exposure	
Company Exposure[1]	40.0
– Manageable Risk	37.3
Unmanageable Risk[2]	**2.6**
Management	
Manageable Risk	37.3
– Managed Risk[3]	19.9
Management Gap[4]	**17.4**
Overall Unmanaged Risk	**20.0**



- Exposure represents a company's vulnerability to ESG risks driven by their business model
- Exposure is assessed at the Subindustry level and then specified at the company level
- Scoring ranges from 0-55+ with categories of low, medium, and high-risk exposure

- Management measures a company's ability to manage ESG risks through its commitments and actions
- Management assesses a company's efficiency on ESG programs, practices, and policies
- Management score ranges from 0-100% showing how much manageable risk a company is managing

ESG Risk Rating

ESG Risk Ratings measure the degree to which a company's value is impacted by environmental, social, and governance risks, by evaluating the company's ability to manage the ESG risks it faces.

1. A company's Exposure to material ESG issues 2. Unmanageable Risk refers to risks that are inherent to a particular business model that cannot be managed by programs or initiatives 3. Managed Risk = Manageable Risk multiplied by a Management score of 53.4% 4. Management Gap assesses risks that are not managed, but are considered manageable 5. ESG Risk Rating Assessment = Overall Unmanaged Risk = Management Gap plus Unmanageable Risk

ESG Risk Rating Assessment[5]

ESG Risk Rating is of Aug 07, 2024. Highest Controversy Level is as of Sep 08, 2024. Sustainalytics Subindustry: Restaurants. Sustainalytics provides Morningstar with company ESG ratings and metrics on a monthly basis and as such, the ratings in Morningstar may not necessarily reflect current Sustainalytics' scores for the company. For the most up to date rating and more information, please visit: sustainalytics.com/esg-ratings/.

Peer Analysis 07 Aug 2024

Peers are selected from the company's Sustainalytics-defined Subindustry and are displayed based on the closest market cap values

Company Name	Exposure			Management			ESG Risk Rating		
Chipotle Mexican Grill Inc	40.0 | Medium	0	55+	53.4 | Strong	100	0	20.0 | Medium	0	40+
McDonald's Corp	42.6 | Medium	0	55+	42.0 | Average	100	0	25.8 | Medium	0	40+
Yum Brands Inc	41.5 | Medium	0	55+	54.1 | Strong	100	0	20.5 | Medium	0	40+
Starbucks Corp	39.7 | Medium	0	55+	46.9 | Average	100	0	22.3 | Medium	0	40+
Restaurant Brands International Inc	42.9 | Medium	0	55+	52.5 | Strong	100	0	21.8 | Medium	0	40+

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Appendix
Historical Morningstar Rating

Chipotle Mexican Grill Inc CMG 9 Sep 2024 21:23, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
—	—	—	★★	★★	★★	★	★	★	★	★★	★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★	★★	★★★	★★★	★★★	★★★	★★	★★	★★	★★★	★★★	★★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★★	★★★	★★★	★★★	★★★	★★★	★★★★	★★★	★★★	★★★	★★★	★★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★	★★	★★	★★	★★	★★	★★	★★★	★★	★★	★★	★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★	★★	★★	★★	★★	★★	★★	★★	★★	★★★	★★★	★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★	★★	★★	★★	★★	★★	★★	★★	★★	★★	★★	★★

McDonald's Corp MCD 9 Sep 2024 21:21, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
—	—	—	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★★★	★★★★	★★★★	★★★	★★★	★★★	★★	★★	★★	★★	★★	★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★	★★	★★	★★★	★★	★★	★★★	★★★	★★	★★★	★★★	★★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★	★★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★

Starbucks Corp SBUX 9 Sep 2024 21:24, UTC

Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
—	—	—	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★	★★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★★	★★★	★★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★★	★★★	★★★	★★★	★★★	★★	★★★	★★★	★★★	★★★	★★★	★★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★★	★★★	★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★★

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Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Jun 2024	May 2024	Apr 2024	Mar 2024	Feb 2024	Jan 2024
—	—	—	★★★	★★★	★★★★	★★★★	★★★	★★★	★★★	★★★	★★★★
Dec 2023	Nov 2023	Oct 2023	Sep 2023	Aug 2023	Jul 2023	Jun 2023	May 2023	Apr 2023	Mar 2023	Feb 2023	Jan 2023
★★★★	★★★★	★★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★
Dec 2022	Nov 2022	Oct 2022	Sep 2022	Aug 2022	Jul 2022	Jun 2022	May 2022	Apr 2022	Mar 2022	Feb 2022	Jan 2022
★★★	★★★	★★★★	★★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★
Dec 2021	Nov 2021	Oct 2021	Sep 2021	Aug 2021	Jul 2021	Jun 2021	May 2021	Apr 2021	Mar 2021	Feb 2021	Jan 2021
★★	★★★	★★★	★★★	★★	★★	★★★	★★★	★★★	★★★	★★★	★★★
Dec 2020	Nov 2020	Oct 2020	Sep 2020	Aug 2020	Jul 2020	Jun 2020	May 2020	Apr 2020	Mar 2020	Feb 2020	Jan 2020
★★★	★★★	★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★★	★★★
Dec 2019	Nov 2019	Oct 2019	Sep 2019	Aug 2019	Jul 2019	Jun 2019	May 2019	Apr 2019	Mar 2019	Feb 2019	Jan 2019
★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★	★★★

Research Methodology for Valuing Companies

Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, indepth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss shortterm market-price movements), but we believe these negatives are mitigated by deep analysis and our longterm approach.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our singlepoint star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in workingcapital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes (EBI) and the net new investment (NNI) to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

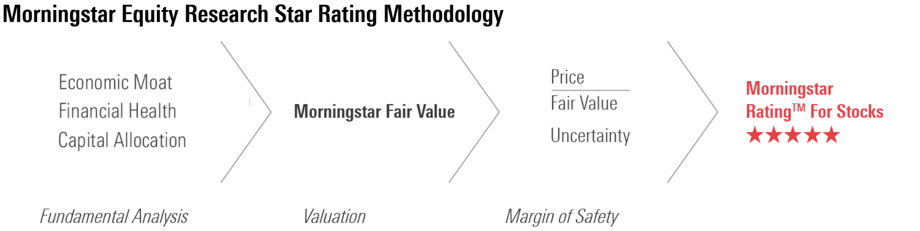
Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating is designed to capture the range of potential outcomes for a company's intrinsic value. This rating is used to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating is aimed at identifying the confidence we should have in assigning a fair value estimate for a given stock.

Our Uncertainty Rating is meant to take into account anything that can increase the potential dispersion of future outcomes for the intrinsic value of a company, and any-

Morningstar Equity Research Star Rating Methodology



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thing that can affect our ability to accurately predict these outcomes. The rating begins with a suggested rating produced by a quantitative process based on the trailing 12-month standard deviation of daily stock returns. An analyst overlay is then applied, with analysts using the suggested rating, historical rating data, and their own knowledge of the company to inform them as they make the final Uncertainty Rating decision. Ultimately, the rating decision rests with the analyst. Analysts take into account many characteristics when making their final decision, including cyclical factors, operational and financial factors such as leverage, company-specific events, ESG risks, and anything else that might increase the potential dispersion of future outcomes and our ability to estimate those outcomes.

Our recommended margin of safety—the discount to fair value demanded before we'd recommend buying or selling the stock—widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the potential dispersion of outcomes, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the Uncertainty Rating provides guidance in portfolio construction based on risk tolerance.

Our Uncertainty Ratings are: Low, Medium, High, Very High, and Extreme.

	Margin of Safety	
Qualitative Analysis Uncertainty Ratings	★★★★★Rating	★Rating
Low	20% Discount	25% Premium
Medium	30% Discount	35% Premium
High	40% Discount	55% Premium
Very High	50% Discount	75% Premium
Extreme	75% Discount	300% Premium

Our uncertainty rating is based on the interquartile range, or the middle 50% of potential outcomes, covering the 25th percentile–75th percentile. This means that when a stock hits 5 stars, we expect there is a 75% chance that the intrinsic value of that stock lies above the current market price. Similarly, when a stock hits 1 star, we expect there is a 75% chance that the intrinsic value of that stock lies below the current market price.

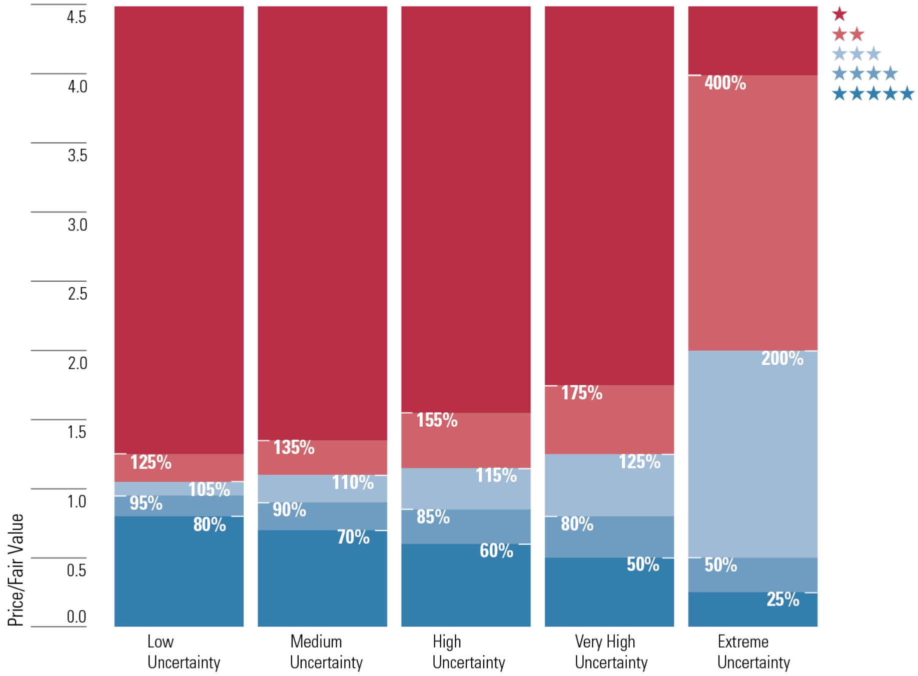
4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com

Morningstar Star Rating for Stocks

Morningstar Equity Research Star Rating Methodology



Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close tabs on the companies they follow, and, based on thorough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk adjusted return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider compan-

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ies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

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Sustainalytics ESG Risk Rating Assessment: The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environment, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score. Unmanaged Risk is measured on an open-ended scale starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit sustainalytics.com/esg-ratings/

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

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