

May 7, 2012

Food Retail

Chefs' Warehouse

(CHEF-NASDAQ)

Stock Rating: Outperform
Industry Rating: Market Perform

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Management Expectations Differ From Investor Expectations

Event

And this disconnect resulted in a ~20% sell-off on Friday. So while a downgrade was tempting, the sell-off keeps us at **OUTPERFORM**. *Our* reality: we are less concerned with the loss of a drayage customer (~\$0.02 in FY2012) and the potential for dairy deflation to negatively impact the top line for 2Q12-4Q12, both headwinds are more or less beyond management's control. Our concerns: CHEF – now armed with ~\$180m of liquidity to pursue acquisitions must 1) demonstrate spending discipline, and 2) be willing to provide investors with details on the rationale for acquisitions – the “trust us” approach won't work for a company with a 9-month track record as a public entity. Investors need hand-holding, like it or not. Given the apparent lofty multiple of the Praml acquisition, somewhat vague responses to inquiries regarding the purchase, as well as the fact that the asset was based in a geography where CHEF already had a presence, our communication requirements were not met on Thursday's call. Lastly, we believe legal may be having an increasing influence on CHEF's reporting and communication practices with the Street – and not in a positive light.

Impact

Despite these concerns – we like the long term prospects for CHEF. So we will give CHEF a pass and think the pull-back presents investors with a compelling entry point, keeping in mind CHEF could remain range-bound until management regains credibility.

Forecasts

Our 2Q12 and FY2012 EPS are revised downward to \$0.23 and \$0.91, respectively. Consensus is \$0.26 and \$0.95.

Valuation

CHEF is trading at a FY2013 EV/EBITDAR of 9.0x and a P/E of 16.9x.

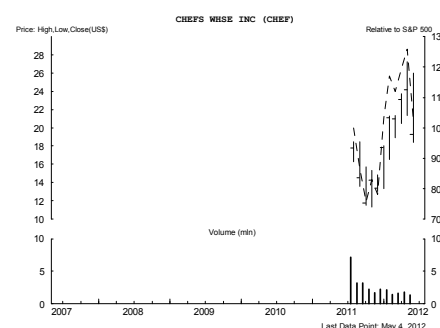
Recommendation

We maintain our **OUTPERFORM** rating.

Securities Info

Price (4-May)	\$19.27	Target Price	\$26
52-Wk High/Low	\$27/\$11	Dividend	--
Mkt Cap (mm)	\$403	Yield	--
Shs O/S (mm, BASIC)	20.9	Float O/S (mm)	10.8
Options O/S (mm)	45.7	ADVol (30-day, 000s)	88

Price Performance



Valuation/Financial Data

(FY-Dec.)	2010A	2011A	2012E	2013E
EPS Pro Forma	\$0.76	\$0.77	\$0.91↓	\$1.14↓
P/E			21.2x	16.9x
First Call Cons.			\$0.95	\$1.13
EPS GAAP	\$0.76	\$0.77	\$0.91	\$1.14
FCF	na	na	na	na
P/FCF			na	na
EBITDA (\$mm)	\$24	\$30	\$37	\$44
EV/EBITDA			12.0x	9.9x
Rev. (\$mm)	\$330	\$400	\$461	\$512
EV/Rev			1.0x	0.9x
Quarterly EPS	1Q	2Q	3Q	4Q
2011A	\$0.13	\$0.20	\$0.19	\$0.26
2012E	\$0.13A	\$0.23↓	\$0.23↓	\$0.32↑
Quarterly EBITDA	1Q	2Q	3Q	4Q
2011A	\$4.7	\$7.6	\$7.5	\$10.2
2012E	\$5.7A	\$9.3	\$9.1	\$12.5
Balance Sheet Data (30-Dec)				
Net Debt (\$mm)	\$35		Total Debt/EBITDA	1.2x
Total Debt (\$mm)	\$46		EBITDA/IntExp	na
Net Debt/Cap.	50.5%		Price/Book	17.0x

Notes: All values in US\$.

Source: BMO Capital Markets estimates, Bloomberg, Thomson Reuters, and IHS Global Insight.

Save the Date
May 15-16, 2012
BMO Capital Markets
2012 FARM TO MARKET CONFERENCE, NYC

For a list of participating companies, please go to:
<http://www.bmocm.com/conferences/farmtomarket2012/fmparticipating>
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Changes

Annual EPS
 2012E \$0.96 to \$0.91
 2013E \$1.17 to \$1.14

Quarterly EPS

Q2/12E \$0.26 to \$0.23
 Q3/12E \$0.25 to \$0.23
 Q4/12E \$0.31 to \$0.32

Please refer to pages 6 to 8 for Important Disclosures, including the Analyst's Certification.

Key Points

Exhibit 1. CHEF Current Valuation

Chefs' Warehouse Current Valuation		
	2012E	2013E
Net Income	\$19.07	\$23.85
EPS	\$0.91	\$1.14
EBITDA	\$37	\$44
EBITDAR	\$46	\$54
Net Forward Debt	\$26	\$7
# Shares	21	21
Current Stock Price	\$19.27	\$19.27
Market Cap	\$403	\$403
EV	\$429	\$411
P/E	21.1x	16.9x
EV/EBITDA	11.7x	9.2x
EPS Growth	17.7%	25.0%

Source: Company reports, BMO Capital Markets estimates.

Exhibit 2. Change in Guidance

FY12 Guidance	at 4Q11	at 1Q12
Revenue	\$450-\$460 million	\$452-\$462 million
Adjusted EPS	\$0.91-\$0.96	\$0.91-\$0.94
Duplicate Rent	(\$0.03)	(\$0.02)
Write-off of Deferred Financing Fees	na	(\$0.03)
Loss of Drayage Contract	na	(\$0.02)
Praml Acquisition (est.)	na	\$0.02
Reported EPS	\$0.88-\$0.93	\$0.86-\$0.89

Source: Company reports, BMO Capital Markets estimates.

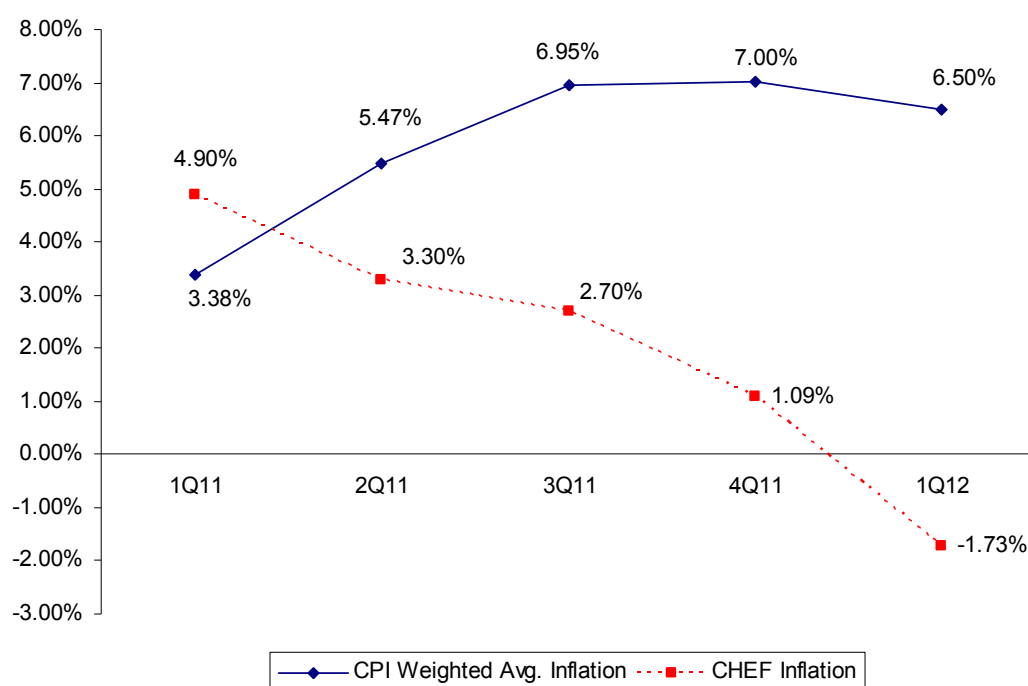
On April 30, 2012, CHEF announced that it is purchasing Praml International for \$19.5 million. Our view:

1. If we assume the \$12 million impact to FY2012 revenues (as stated on the call) is based on an 8-month time frame (because the deal has already closed), this actually implies a ~1.1x sales multiple – too rich in our view. **If acquisitions are to play a meaningful role in the company's future growth (which we assume to be the case), multiples need to remain in the 0.3x-0.5x range. If they don't, ROIC will deteriorate and so will CHEF's valuation.**
2. EBITDA multiples are meaningless in our view because expenses at small, family-run operations are usually out of whack.
3. Given Praml's expertise – a dominant provider of French cuisine products while CHEF is known for its Italian cuisine products – we understand why this acquisition makes sense strategically, and the customer base should serve to expand CHEF's market share in an extremely robust region of the country.
4. In addition, CHEF will move its existing operations in Las Vegas (~11,440 sq. ft) to the Praml facility (>30,000 sq. ft.).

5. We would have preferred to see CHEF make an acquisition in a new market – Dallas, Boston, Chicago – to name a few. While we do trust management's ability to execute on integration of the Praml acquisition to ensure the acquisition is accretive, we are still perplexed as to why Las Vegas was a focus when the company already has a presence in the Las Vegas market.

In 1Q12, CHEF's sales growth was negatively impacted by deflation of 1.7%, largely due to deflation in the dairy category, which represents ~26% of sales at Chefs' Warehouse. In Exhibit 3 below, we compare the inflation rate provided by CHEF each quarter with a weighted average CPI inflation rate (using CHEF's category sales as weights). We acknowledge that this is not a perfect comparison, but it does appear to indicate that deflation is unique to CHEF given its specific product mix.

Exhibit 3. CHEF Inflation vs. CPI Inflation



Source: Company reports, BLS, BMO Capital Markets estimates.

We are decreasing our 2Q12 EPS estimate to \$0.23 from \$0.26 vs. consensus of \$0.26. Our EBITDA estimate is \$9.3 million. Our estimate assumes total sales increase 19.0% to \$118.1 million, driven by 9.0% organic sales growth, and we assume gross margins expand 75 bp to 27.2%. We forecast operating expenses (excluding D&A) grow 22.5% to \$22.9 million, or a 55-bp increase as a percentage of sales to 19.3%, leading to an 8-bp improvement in operating margins to 7.3%, or \$8.7 million. This gets us to EBITDA of \$9.3 million, a 20-bp expansion in margin to 7.9%. We assume interest expense of \$0.4 million, a 41.0% tax rate and 20.9 million shares outstanding, which gets us to EPS of \$0.23, a 18.4% increase from 2Q11.

In FY2012, we estimate EPS decreases to \$0.91 from \$0.96. Consensus EPS is \$0.95. Our EBITDA estimate is \$36.6 million. Our estimate assumes total sales increase 15.2% to \$461.0 million (vs. consensus of \$459.0 million), with gross margins improving 67 bp to 27.0%. We

forecast operating expenses (excluding D&A) grow 16.6% to \$87.8 million, a 24-bp year-over-year deterioration in margin, leading to a 39-bp improvement in operating margins to 7.4%, or \$34.1 million. This gets us to EBITDA of \$36.6 million, a 44-bp improvement in margin to 7.9%. We assume interest expense of \$1.8 million, a 41.1% tax rate and 20.9 million shares outstanding, which gets us to EPS of \$0.91.

In 1Q12, CHEF reported EPS of \$0.13, which missed our \$0.14 estimate and consensus of \$0.16. Total sales increased 18.3% to \$98.1 million. Gross margins improved 75 bp to 25.6%. Operating expenses (excluding D&A) grew 22.1% to \$20.4 million. Operating margins expanded 21 bp to 5.2%, or \$5.1 million, while EBITDA margins expanded 11 bp to 5.8%, or \$5.7 million. Interest expense came in at \$0.6 million. Using a 41.6% tax rate and 20.9 million shares outstanding gets us to EPS of \$0.13.

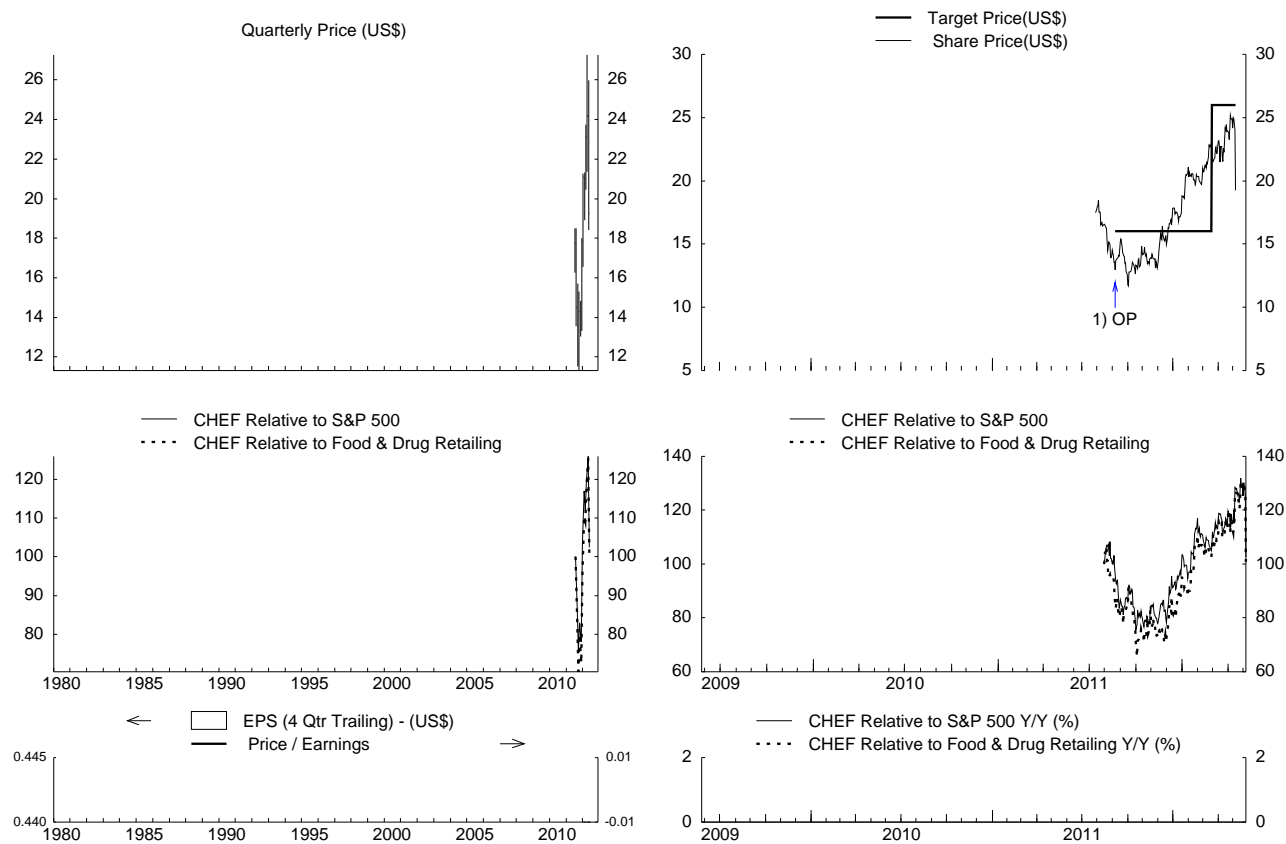
Additional Takeaways

- Management updated its FY2012 guidance to reflect EPS of \$0.91-\$0.94 and revenues of \$452-\$462 million.
- In 1Q12, organic sales slowed sequentially from 4Q; however, similar to last quarter we believe this is a function of the Harry Wils and Provvista acquisitions since CHEF was taking share from these companies before they bought them. Additionally sales was also negatively impacted by deflation in the dairy category, which began to occur in January and persisted throughout the quarter, and the loss of a drayage contract. The drayage contract was a one-off contract to accommodate a customer, and we are not surprised the company discontinued this service since it does not fit within CHEF's current business model.
- On acquisitions, the integration of the Harry Wils and Provvista Specialty Food acquisitions remains on track.
- In contrast to the casual dining segment, which saw sales deteriorate in March and further into April, sales trends at fine dining restaurants (CHEF's core customer) held steady throughout the entire quarter.
- During 1Q, the company saw product placement and unique customer growth at levels similar to FY2011. The company saw increased case volumes in all categories, but particularly in dairy (which when combined with deflation caused some of the lighter than expected sales growth).
- On real estate, CHEF transitioned to a new, larger facility in Miami during 1Q, and recently signed a lease for its new facility in the Bronx that will replace the two existing facilities.
- In April, the company entered into a new credit facility that provides \$180 million in additional liquidity, comprising a \$100-million cash flow revolver, \$40-million term note and \$40-million accordion feature.
- The loss of the drayage contract will cost the company \$4 million in FY2012 revenues and \$0.02 in FY2012 EPS. Management expected to discontinue the contract in FY2013, and was caught slightly off guard that it ended in FY2012.

Chefs' Warehouse Income Statement															
	52 weeks 12/28/2007	52 weeks 12/26/2008	52 weeks 12/25/2009	52 weeks 12/24/2010	3/25/2011	6/24/2011			53 weeks 12/30/2011						
	2007	2008	2009	2010	1Q11	2Q11	3Q11	4Q11	2011	1Q12	2Q12E	3Q12E	4Q12E	2012E	2013E
Revenues	\$256.13	\$281.70	\$271.07	\$330.12	\$82.90	\$99.26	\$101.68	\$116.51	\$400.35	\$98.07	\$118.11	\$117.95	\$126.91	\$461.04	\$511.76
Cost of Goods	\$190.79	\$211.39	\$199.76	\$244.34	\$61.50	\$73.00	\$75.05	\$85.50	\$295.05	\$72.02	\$85.98	\$86.17	\$92.49	\$336.67	\$372.43
Gross Profit	\$65.35	\$70.32	\$71.31	\$85.78	\$21.40	\$26.26	\$26.63	\$31.01	\$105.30	\$26.05	\$32.13	\$31.78	\$34.42	\$124.37	\$139.33
D&A	\$1.94	\$1.99	\$1.92	\$2.10	\$0.60	\$0.39	\$0.43	\$0.51	\$1.93	\$0.61	\$0.61	\$0.61	\$0.61	\$2.44	\$2.44
Total Operating Expenses (Incl. D&A)	\$59.39	\$60.31	\$57.98	\$64.21	\$17.30	\$19.05	\$19.57	\$21.32	\$77.24	\$20.99	\$23.46	\$23.28	\$22.51	\$90.25	\$97.35
Total Operating Expenses (Ex. D&A)	\$57.45	\$58.33	\$56.06	\$62.10	\$16.70	\$18.66	\$19.14	\$20.81	\$75.31	\$20.39	\$22.85	\$22.67	\$21.90	\$87.81	\$94.91
Operating Income	\$5.96	\$10.00	\$13.33	\$21.57	\$4.10	\$7.20	\$7.06	\$9.70	\$28.06	\$5.06	\$8.67	\$8.49	\$11.90	\$34.12	\$41.98
EBITDA	\$7.90	\$11.99	\$15.25	\$23.68	\$4.70	\$7.60	\$7.491	\$10.207	\$29.99	\$5.66	\$9.28	\$9.10	\$12.51	\$36.56	\$44.41
Interest	\$3.52	\$3.24	\$2.82	\$4.04	\$0.40	\$0.42	\$0.51	\$0.53	\$1.85	\$0.55	\$0.40	\$0.40	\$0.40	\$1.75	\$1.63
Gain on Settlement	\$1.10														
Gain/Loss on Interest Rate Swap	-\$0.62	-\$1.12	\$0.66	\$0.91	\$0.40	\$0.00	\$0.00	\$0.00	\$0.40	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.07
Other					\$0.00			\$0.00							
Income Before Tax	\$2.92	\$5.65	\$11.17	\$18.44	\$4.10	\$6.79	\$6.56	\$9.17	\$26.61	\$4.51	\$8.27	\$8.09	\$11.50	\$32.37	\$40.42
Taxes	\$0.79	\$3.45	\$2.21	\$2.57	\$1.50	\$2.69	\$2.56	\$3.76	\$10.50	\$1.88	\$3.39	\$3.32	\$4.72	\$13.30	\$16.57
Net Income	\$2.14	\$2.20	\$8.96	\$15.87	\$2.60	\$4.10	\$4.00	\$5.41	\$16.11	\$2.63	\$4.88	\$4.77	\$6.79	\$19.07	\$23.85
Tax Rate	26.9%	61.1%	19.8%	13.9%	36.6%	39.6%	39.0%	41.0%	39.5%	41.6%	41.0%	41.0%	41.0%	41.1%	41.0%
Diluted EPS	\$0.10	\$0.11	\$0.43	\$0.76	\$0.13	\$0.20	\$0.19	\$0.26	\$0.77	\$0.13	\$0.23	\$0.23	\$0.32	\$0.91	\$1.14
Diluted	20.77	20.77	20.77	20.77	20.67	20.83	20.83	20.84	20.79	20.90	20.93	20.93	20.93	20.92	20.92
Consensus EPS								\$0.25	\$0.77	\$0.16	\$0.26	\$0.25	\$0.30	\$0.95	\$1.13
Growth															
Sales		10.0%	-3.8%	21.8%	18.4%	18.7%	19.7%	27.2%	21.3%	18.3%	19.0%	16.0%	18.0%	15.2%	11.0%
Organic Sales growth		4.2%	-6.2%	10.9%	10.9%	13.0%	10.6%	8.8%	11.4%	7%	9%	9%	9%		8%
Inflation - contribution to sales		n/a	-0.6%	7.8%	4.9%	3.3%	2.7%	1.1%	2.2%	-1.7%	-2.0%	-2.0%	0.0%		3%
Acquisitions - contribution to sales		5.8%	3.0%	3.1%	3.0%	2.0%	6.4%	10.0%	5.7%	11%	12%	9%	9%		0%
Impact of extra week - contribution to sales								7.2%	2.0%						
Operating Expenses (Ex. D&A)		1.5%	-3.9%	10.8%	15.3%	19.3%	24.3%	25.5%	21.3%	22.1%	22.5%	18.5%	5.3%	16.6%	8.1%
Operating Expenses (Incl. D&A)		1.6%	-3.9%	10.7%	15.7%	18.1%	23.8%	23.2%	20.3%	21.3%	23.2%	19.0%	5.6%	16.8%	7.9%
Operating Income		67.9%	33.3%	61.8%	35.3%	24.1%	12.9%	49.6%	30.1%	23.4%	20.3%	20.3%	22.8%	21.6%	23.0%
EBITDA		51.7%	27.2%	55.3%	34.5%	20.4%	12.5%	41.5%	26.7%	20.5%	22.1%	21.5%	22.6%	21.9%	21.5%
Net Income		2.8%	308.1%	77.1%	69.0%	-8.7%	-9.3%	-0.6%	1.5%	1.4%	19.0%	19.4%	25.5%	18.4%	25.0%
EPS			308.1%	77.1%					1.4%					17.7%	25.0%
Margins															
Gross	25.5%	25.0%	26.3%	26.0%	25.8%	26.45%	26.19%	26.62%	26.30%	26.56%	27.20%	26.94%	27.12%	26.98%	27.2%
D&A	0.8%	0.7%	0.7%	0.6%	0.7%	0.4%	0.4%	0.4%	0.5%	0.6%	0.5%	0.5%	0.5%	0.5%	0.5%
Operating Expenses (Ex. D&A)				18.8%	20.1%	18.8%	18.8%	17.9%	18.8%	20.8%	19.3%	19.2%	17.3%	19.0%	18.5%
Operating Expenses (Incl. D&A)	23.2%	21.4%	21.4%	19.4%	20.9%	19.2%	19.2%	18.3%	19.3%	21.4%	19.9%	19.7%	17.7%	19.6%	19.0%
Operating Income	2.3%	3.6%	4.9%	6.5%	4.9%	7.3%	6.9%	8.3%	7.0%	5.2%	7.3%	7.2%	9.4%	7.4%	8.2%
EBITDA	3.1%	4.3%	5.6%	7.2%	5.7%	7.7%	7.4%	8.8%	7.5%	5.8%	7.9%	7.7%	9.9%	7.9%	8.7%
Tax	26.9%	61.1%	19.8%	13.9%	36.6%	39.6%	39.0%	41.0%	39.5%	41.6%	41.0%	41.0%	41.0%	41.1%	41.0%
Net	0.8%	0.8%	3.3%	4.8%	3.1%	4.1%	3.9%	4.6%	4.0%	2.7%	4.1%	4.0%	5.3%	4.1%	4.7%
Change in Margins															
Gross		-55bp	134bp	-32bp	12bp	21bp	21bp	64bp	32bp	75bp	75bp	75bp	50bp	67bp	25bp
D&A		-5bp	0bp	-7bp	6bp	-20bp	-6bp	-36bp	-15bp	-11bp	12bp	10bp	4bp	5bp	-5bp
Operating Expenses (Ex. D&A)				18.8%	-55bp	10bp	69bp	-24bp	0bp	64bp	55bp	40bp	-60bp	24bp	-50bp
Operating Expenses (Incl. D&A)		-178bp	-2bp	-194bp	-49bp	-11bp	63bp	-60bp	-16bp	54bp	67bp	50bp	-56bp	28bp	-55bp
Operating Income		122bp	137bp	162bp	62bp	31bp	-42bp	124bp	47bp	21bp	8bp	25bp	106bp	39bp	80bp
EBITDA		117bp	137bp	155bp	68bp	11bp	-47bp	88bp	32bp	11bp	20bp	35bp	110bp	44bp	75bp
Net		-5bp	253bp	150bp	94bp	-124bp	-126bp	-130bp	-78bp	-45bp	0bp	11bp	71bp	11bp	52bp

Source: Company reports, BMO Capital Markets estimates.

CHEFS WHSE INC (CHEF)



CHEF - Rating as of 28-Jul-11 = NR

Date	Rating Change	Share Price
1 6-Sep-11	NR to OP	\$13.56

Last Daily Data Point: May 4, 2012

Important Disclosures

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Disclosure 9: BMO Capital Markets makes a market in this security.

Methodology and Risks to Our Price Target/Valuation

Methodology: Our target price values CHEF at an FY2013 EV/EBITDA of 11.7x and P/E of 22.8x.

Risks: Key risks to our CHEF price target include increased competition from traditional broadline operators or consolidation among other regional specialty distributors, deterioration in the national or New York economy as it relates to discretionary spending at restaurants, the success and completion of future acquisitions at fair prices, significant increases in raw material costs, and tainted product or product recall which could tarnish the company's image.

Distribution of Ratings (March 31, 2012)

Rating Category	BMO Rating	BMOCM US Universe*	BMOCM US IB Clients**	BMOCM US IB Clients***	BMOCM Universe****	BMOCM IB Clients*****	Starmine Universe
Buy	Outperform	37.2%	12.1%	52.1%	39.2%	48.3%	54.6%
Hold	Market Perform	60.0%	7.0%	47.9%	57.6%	51.0%	40.1%
Sell	Underperform	2.4%	0.0%	0.0%	3.2%	0.7%	5.3%

* Reflects rating distribution of all companies covered by BMO Capital Markets Corp. equity research analysts.

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OP = Outperform - Forecast to outperform the market;

Mkt = Market Perform - Forecast to perform roughly in line with the market;

Und = Underperform - Forecast to underperform the market;

(S) = speculative investment;

NR = No rating at this time;

R = Restricted – Dissemination of research is currently restricted.

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