



**QUO VADIS**  
CAPITAL

Proprietary Structural Analysis & Forecasting

# Brinker International, Inc. (EAT): VALUEx Zürich-Klosters



**John M. Zolidis**

**Jan. 30- Feb. 1, 2019**

# Presentation Outline

<b>Speaker Bio</b>	<b>Slide 3</b>
<b>Investment Thesis</b>	<b>Slide 4</b>
<b>What is Brinker International, Inc. (EAT)</b>	<b>Sides 5</b>
<b>Review of Valuation &amp; Sentiment</b>	<b>Slide 7-10</b>
<b>State of the U.S. Restaurant Industry</b>	<b>Side 11-13</b>
<b>Recent Results and Forecasts</b>	<b>Slides 15-20</b>
<b>Cash flow and Capital Return</b>	<b>Slides 21-22</b>
<b>Investment recap, risks</b>	<b>Slide 23-24</b>
<b>Disclosures</b>	<b>Slide 25</b>

## Presenter Bio – John Zolidis

- **Founded Quo Vadis Capital, a research boutique and Registered Investment Advisor in 2017**
- **Analyst following U.S. consumer sector since 1999**
- **Education at Kenyon College & Oxford University (Mansfield College)**
- **Named to Wall Street Journal's Best on the Street list in 2005**
- **Based mostly in Paris, France**

## Investment Thesis to Prove

*EAT initiatives have produced a **positive inflection** in traffic and sales which have not yet been recognized by the investment community. We see the potential for **upward revisions** to current estimates and **valuation expansion** for a stock that trades near the lowest multiples in its peer group and has an embedded buyer with **30% of shares outstanding sold short**.*

## Brinker International, Inc. (EAT) Overview

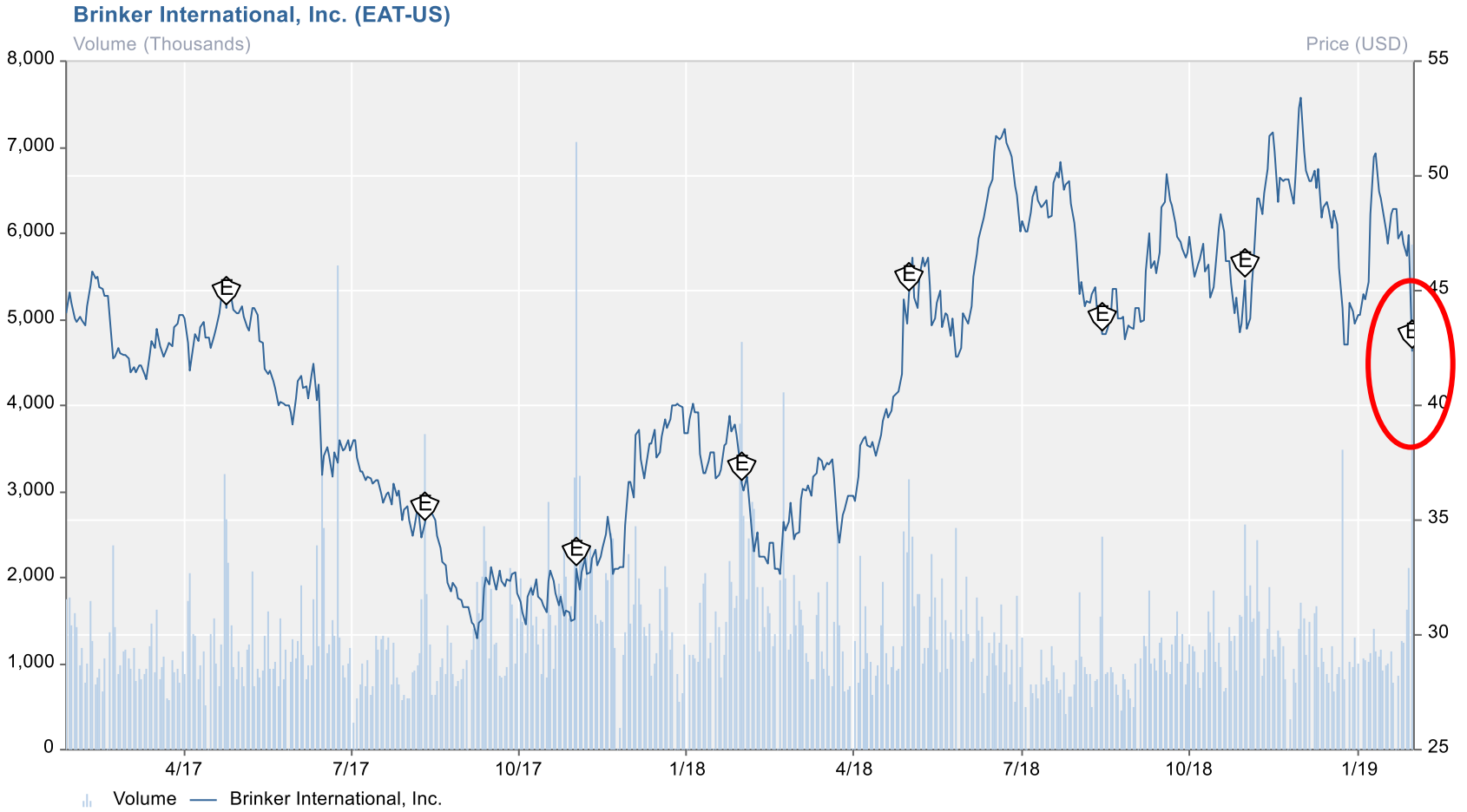
Brinker International is a **mature restaurant company** with two casual dining concepts: Chili's and Maggiano's

- 1,686 total restaurants
- Most recent fiscal year revenues were \$3.1B, **of which 84% came from U.S. company-operated Chili's**, 13% from Maggiano's, and 3% franchisee fees.
- EBITDA margin: 13% most recent fiscal year
- FY19E Capex ~\$145M (4.5% of sales)
- Capital Structure: \$1.26B LT debt, \$855M Shareholders' deficit (4x leverage)
- FY18 Free cash flow was \$183M (~\$4/ share);
- Recent price \$42.00 on the U.S. exchange, current market cap: \$1.7B

***As company-operated Chili's generate the vast majority of sales and earnings our presentation will only focus on this division.***

# Brinker (EAT) Recent Stock Price Performance:

## Two Year Chart:

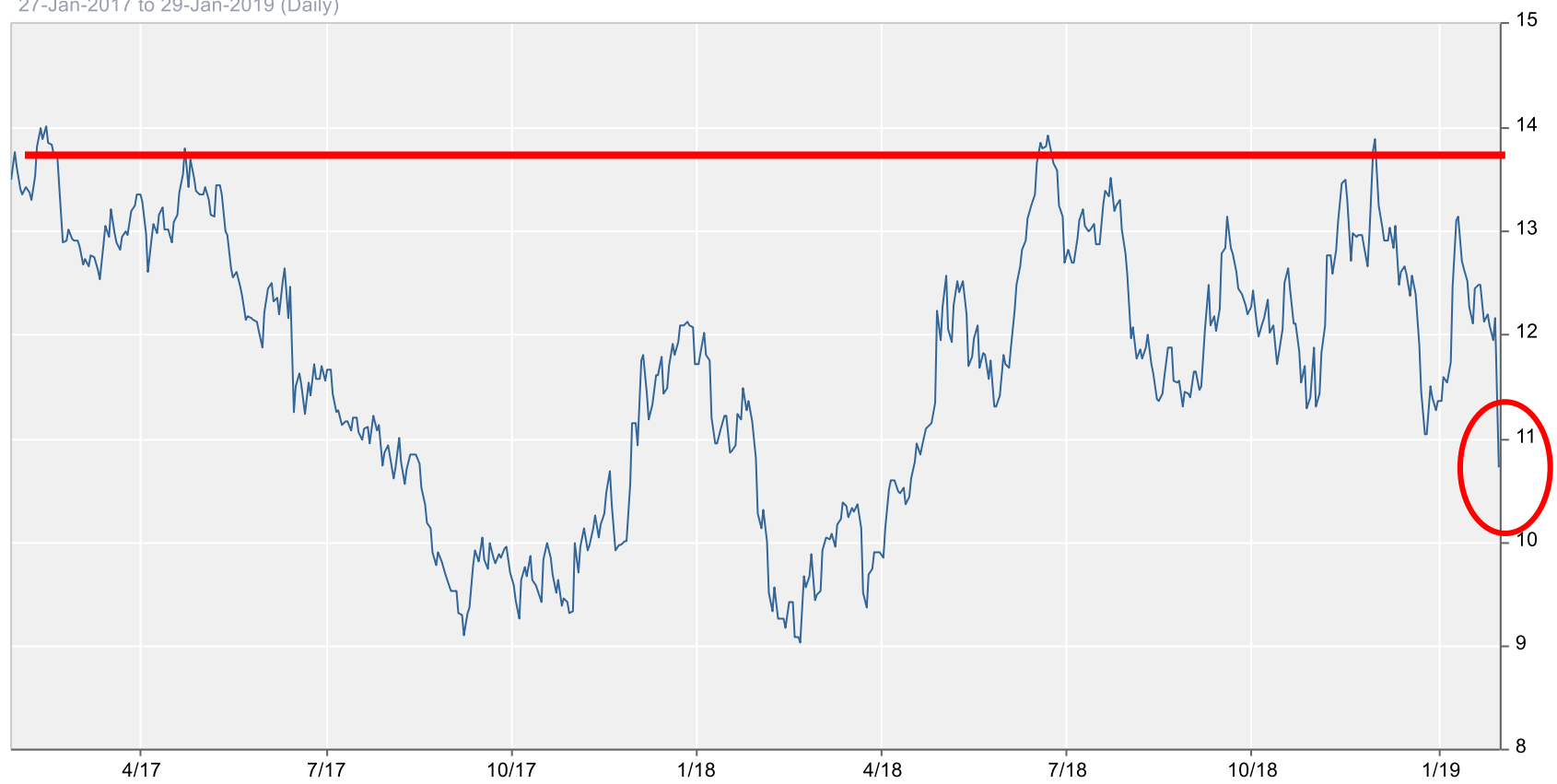


Source: FactSet Prices

# Valuation and Sentiment Overview

**EAT is trading below its 5-year average P/E (red line) (2-year PE chart):**

Price to Earnings - NTM (Mean)  
27-Jan-2017 to 29-Jan-2019 (Daily)



— Brinker International, Inc.

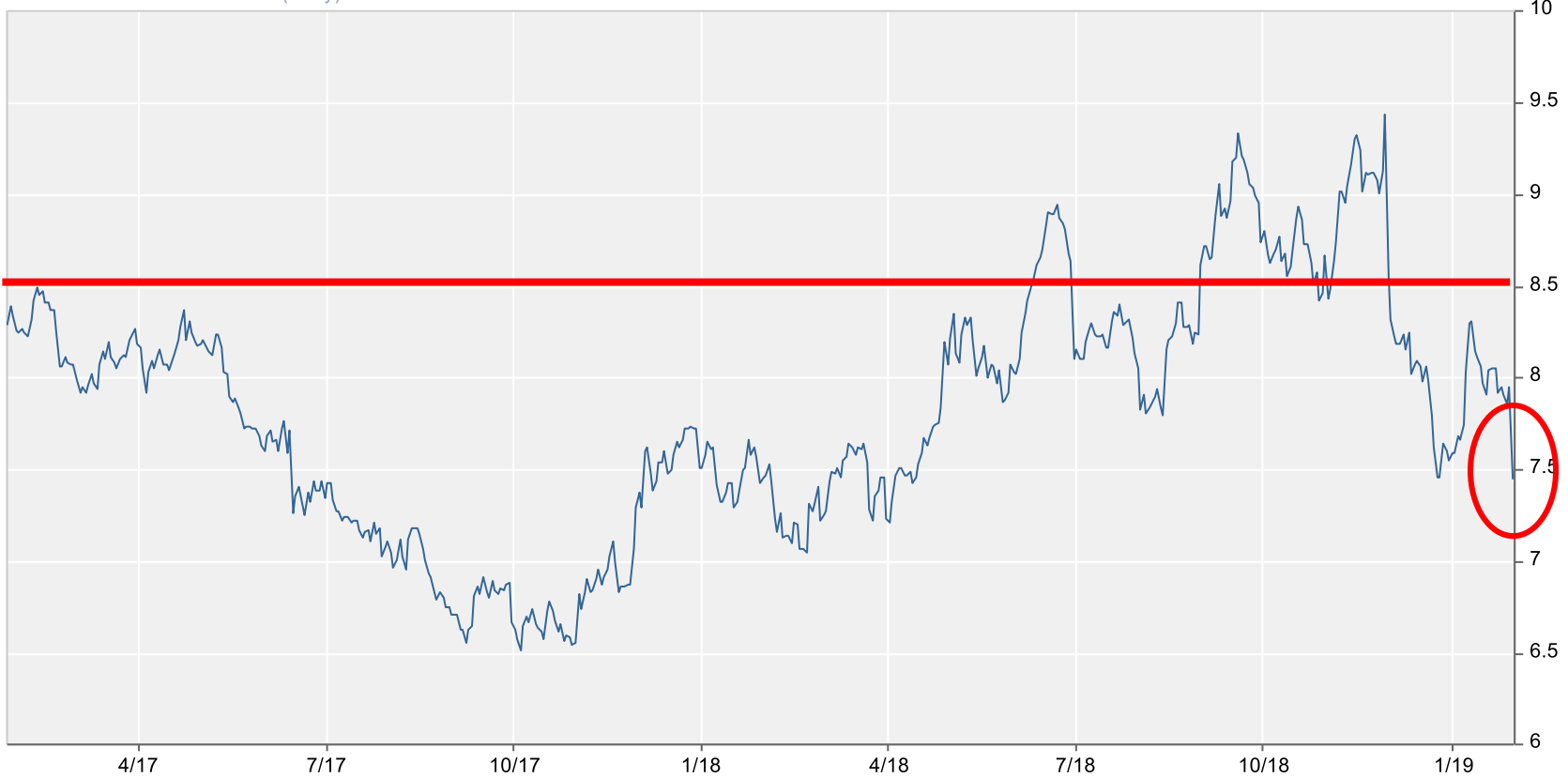
Source: FactSet Fundamentals

# Valuation and Sentiment Overview

EAT is trading below its 5-year average EV/ EBITDA (red line) (2-year chart):

## Enterprise Value to EBITDA - NTM

27-Jan-2017 to 29-Jan-2019 (Daily)



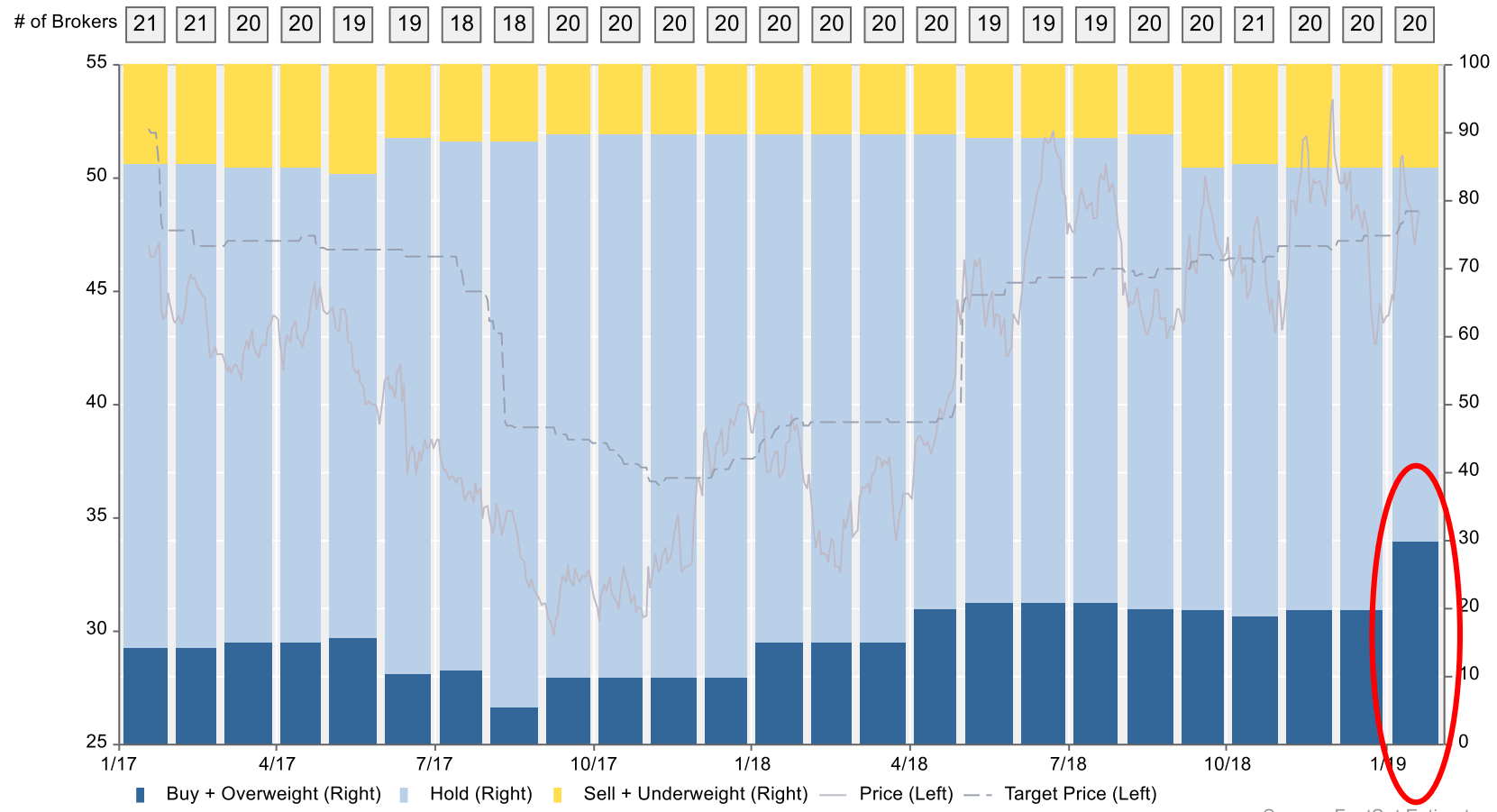
— Brinker International, Inc.

Source: FactSet Fundamentals



# Valuation and Sentiment Overview

**Recent Uptick in Buy Ratings but Still Only 30% of Analysts Recommend:**



Source: FactSet Estimates

# Valuation and Sentiment Overview

Among the cheapest on P/E and EV/ EBITDA with highest short interest (30%)

## Quo Vadis Capital, Inc. Restaurant Universe

### Relative Growth, Profitability, Balance Sheet & Valuation Metrics (Consensus Forecasts)

1/29/2019

	AVG.	BJRI	CAKE	CBRL	CHUY	CMG	EAT	HABT	NDLS	PLAY	RRGB	SBUX	SHAK	TACO	TXRH	YUMC
Recent Price		\$52.71	\$44.73	\$169.0	\$21.31	\$530.3	\$42.0	\$10.60	\$7.10	\$50.95	\$32.85	\$66.98	\$48.21	\$10.68	\$61.05	\$36.14
Mkt Cap (\$B)		\$1.1	\$2.1	\$4.1	\$0.4	\$14.9	\$1.7	\$0.3	\$0.3	\$2.0	\$0.4	\$84.0	\$1.8	\$0.4	\$4.4	\$14.2
ENT VALUE (\$B)		\$1.2	\$2.2	\$4.4	\$0.4	\$14.7	\$2.9	\$0.3	\$0.4	\$2.4	\$0.6	\$84.5	\$1.7	\$0.6	\$4.2	\$12.7
<b>Valuation Metrics</b>																
Vs. 2018E EPS (P/E)	28.0x	22.4	18.3	18.3	24.0	62.0	12.0	NM	NM	18.1	19.6	27.7	70.8	18.9	27.9	23.7
Vs. 2019E EPS (P/E)	27.0x	21.2	16.7	18.6	22.5	44.2	11.1	NM	50.8	16.8	18.6	24.6	67.3	18.6	23.9	22.4
EV / 2019 Sales	1.5x	1.0	0.9	1.4	0.8	2.8	0.9	0.6	0.8	1.7	0.5	3.2	3.0	1.1	1.6	1.4
EV / 2018E EBITDA	12.3x	9.5	9.5	11.2	9.8	27.5	7.3	8.6	11.7	8.7	5.2	15.1	27.2	8.5	14.5	9.9
EV / 2019E EBITDA	11.0x	9.0	8.9	11.0	8.8	22.3	7.0	7.9	10.0	8.0	5.1	14.5	22.0	8.3	12.6	9.6
Free Cash Flow Yield ('18)	2.6%	5.6%	1.7%	0.3%	N/A	1.6%	7.1%	-6.7%	N/A	3.0%	9.5%	N/A	0.0%	2.2%	1.1%	5.5%
Dividend Yield	1.0%	0.3%	2.1%	5.9%	0.0%	0.0%	3.1%	0.0%	0.0%	0.0%	0.0%	2.0%	0.0%	0.0%	1.6%	0.2%
<b>EV/ NTM EBITDA 5-Year Valuation History</b>																
HIGH	21.5	13.9	11.7	12.1	21.6	29.3	10.2	12.6	22.6	11.6	9.9	18.4	99.0	11.0	15.8	13.4
LOW	8.1	6.2	7.1	8.5	6.3	12.4	6.7	8.2	5.1	6.8	4.4	12.3	21.0	0.9	8.4	7.4
AVERAGE	11.8	9.4	9.6	10.0	11.6	19.6	8.5	11.7	11.0	9.0	7.1	14.6	25.7	8.1	11.1	10.0
<b>Current EV/ EBITDA on FY19 Compared to 5-Year Average</b>																
% Premium or Discount	-8%	-5%	-7%	9%	-24%	14%	-18%	-32%	-10%	-11%	-28%	0%	-14%	2%	14%	-3%
<b>Sentiment</b>																
Short Interest	12%	20%	19%	14%	9%	9%	31%	7%	9%	14%	23%	3%	12%	5%	5%	1%
% buys	40%	44%	17%	22%	0%	35%	30%	50%	50%	100%	27%	48%	31%	63%	19%	60%
% holds	51%	44%	74%	56%	88%	44%	55%	50%	38%	0%	73%	52%	46%	38%	67%	40%
% sells	9%	13%	9%	22%	13%	21%	15%	0%	13%	0%	0%	0%	23%	0%	14%	0%

Source: FactSet

Note: EPS and EBITDA Estimates for CRBL are based on July YE, SBUX based on Sep. YE, EAT based on June YE

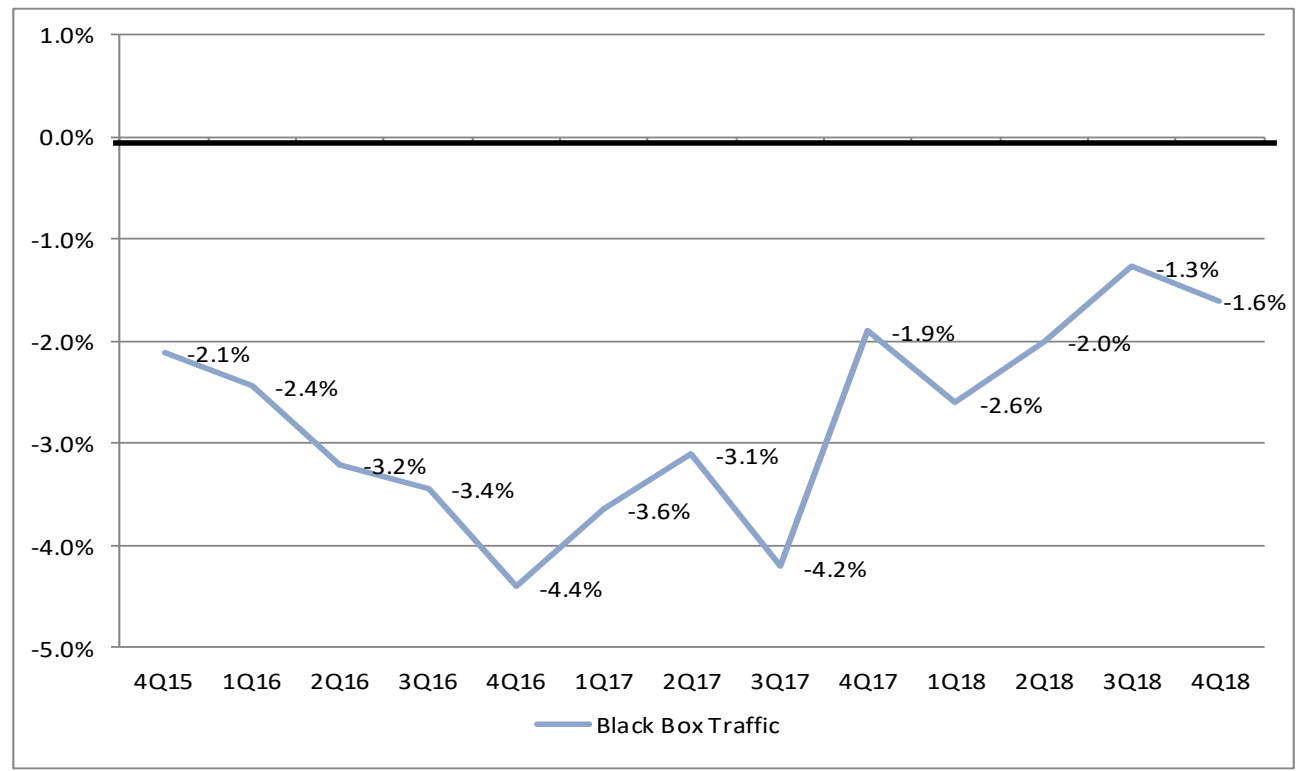


**The question you should be asking: Why is everyone so negative?**

# U.S. Restaurant Industry Overview

Traffic at existing restaurants has **fallen every quarter for more than three years** due to overcapacity, increased competition from grocery and other sources & possibly popularity of cooking:

Restaurant Industry YOY% Change in Quarterly Traffic

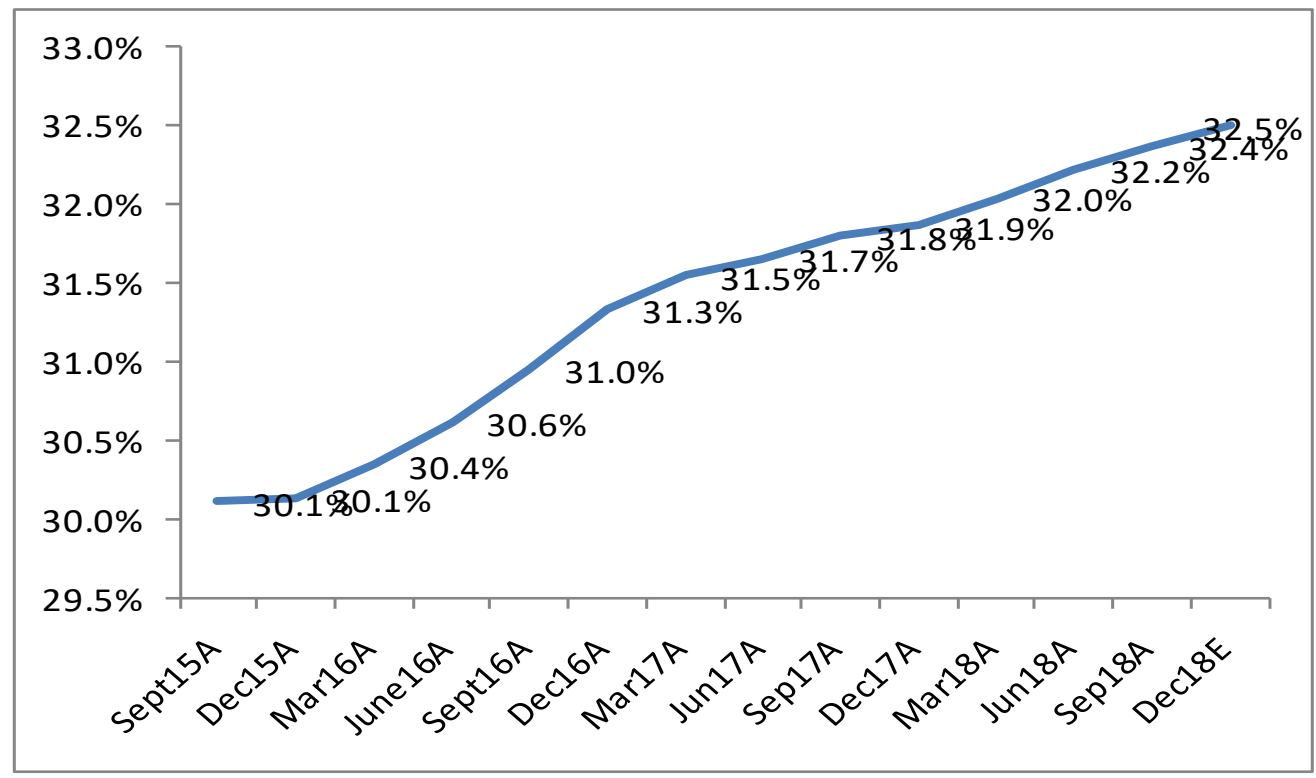


Source: Black Box

# U.S. Restaurant Industry Overview

Meanwhile labor costs have **deleveraged ~250 bps over three years** for the industry and are likely to continue to rise faster than sales in 2019

## AVERAGE -- Labor as a % of Restaurant Sales



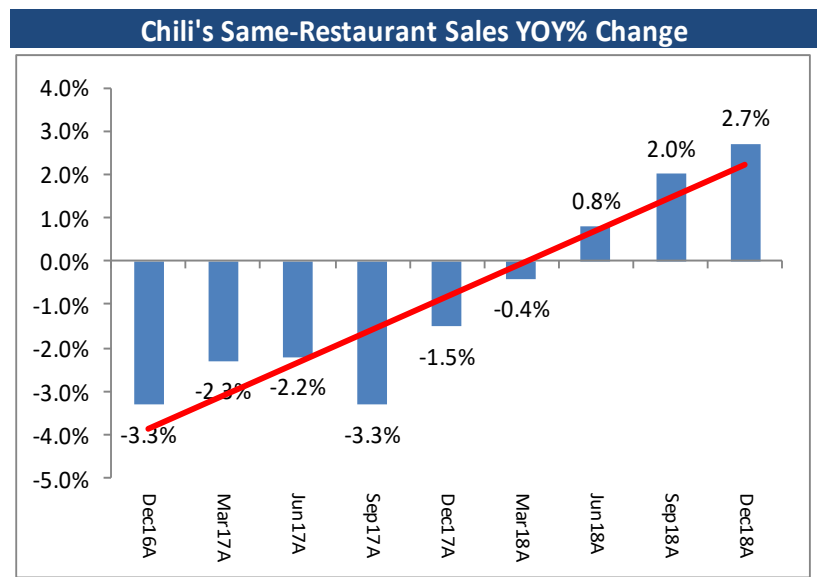
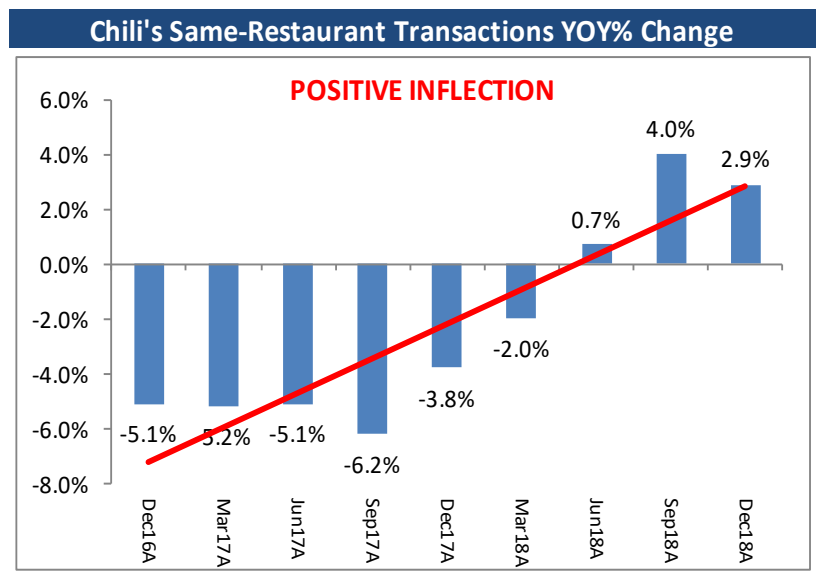
Source: Company Reports & Quo Vadis Capital, Inc. estimates

## Given the traffic & labor dynamic why get involved?

*Company-specific initiatives have produced a **positive inflection in traffic** and we estimate **upside to existing estimates**. Meanwhile cash flow, and return of capital dynamics are favorable for shareholders and short interest provides a potential kick.*

# Positive Inflection in Key Metrics Including Traffic

At Chili's, starting in 2HCY18 EAT **cut 1/3 of menu items, invested in quality and value** which improved speed of service and guest satisfaction, resulting in an improved trend in traffic and same-restaurant sales. In 2HFY18 Chili's layered on a **new to-go platform**, driving a 20% increase to 12% of sales in the December 2018 quarter.

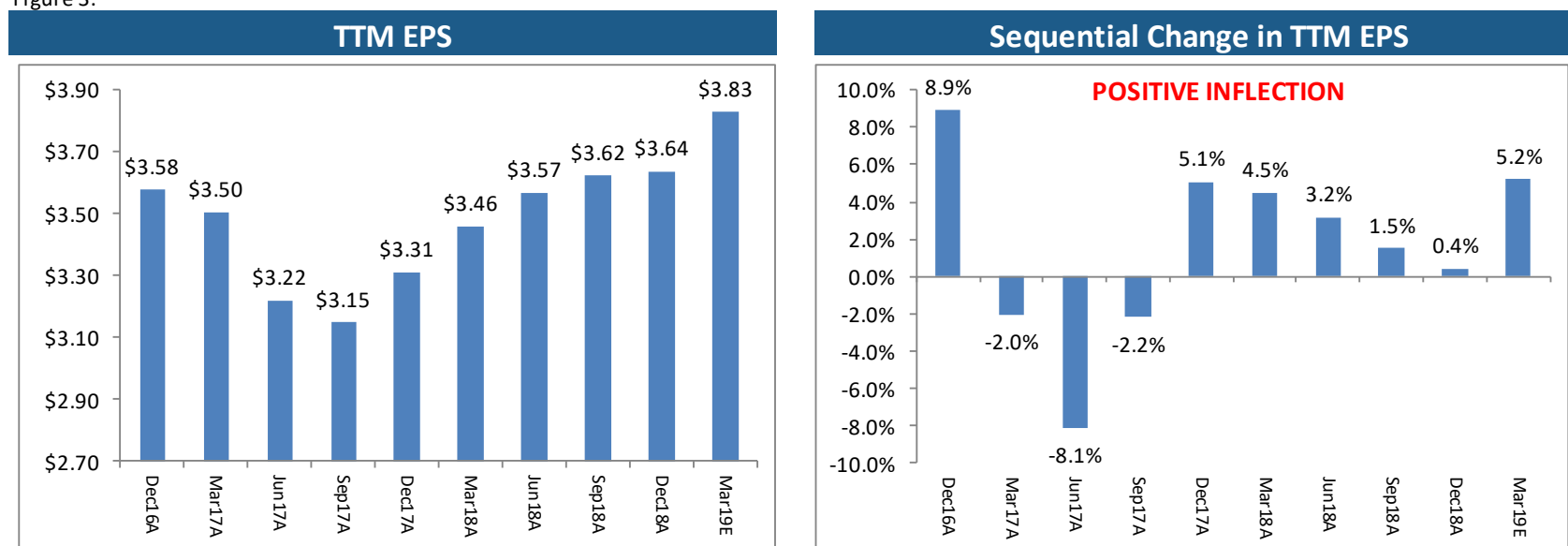


Source: Company reports and Quo Vadis Capital, Inc. estimates

# Positive Inflection in EPS Growth

Slightly better sales, a lower corporate tax rate and a significant reduction in the share count due to repurchase (partially funded by a sale-leaseback of previously owned real estate) has created a **positive inflection in EPS growth**.

Figure 3.



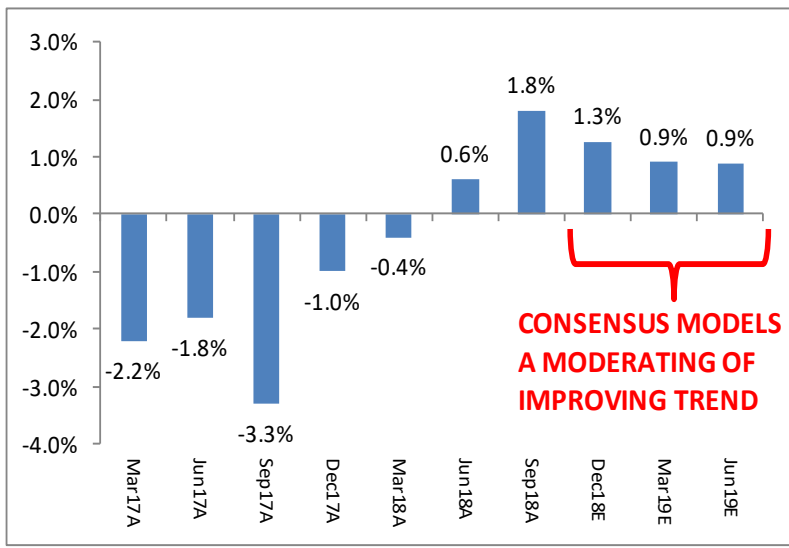
Source: Company reports and Quo Vadis Capital, Inc. estimates



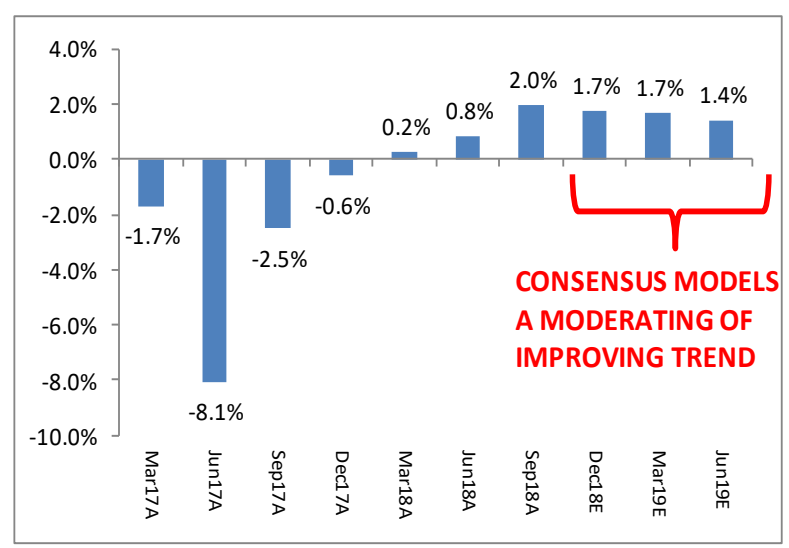
# However, Consensus does not believe it:

Going forward, consensus estimates reflect analyst skepticism. We believe momentum may actually accelerate, rather than slow. These charts show same-store sales and total revenue estimates.

**Consensus Same-Store Sales YOY % Change**

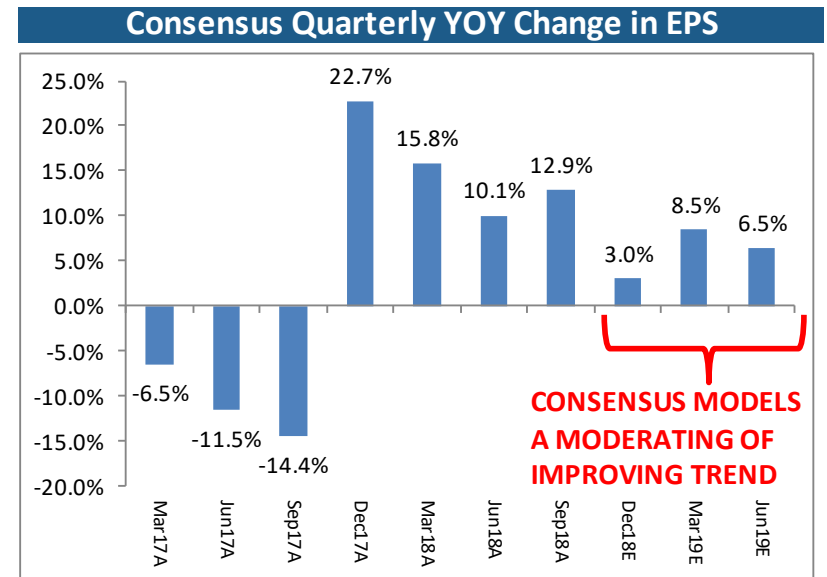
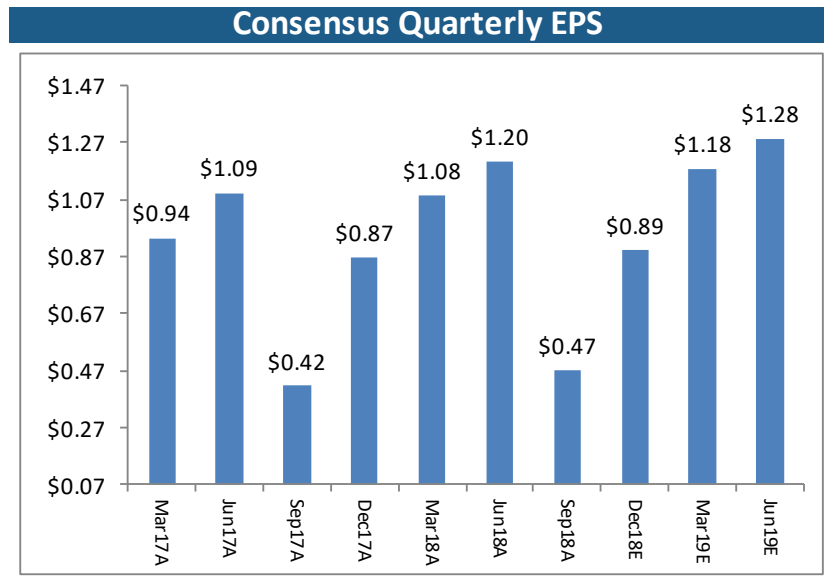


**Consensus Total Quarterly Revenues YOY % Change**



# However, Consensus does not believe it:

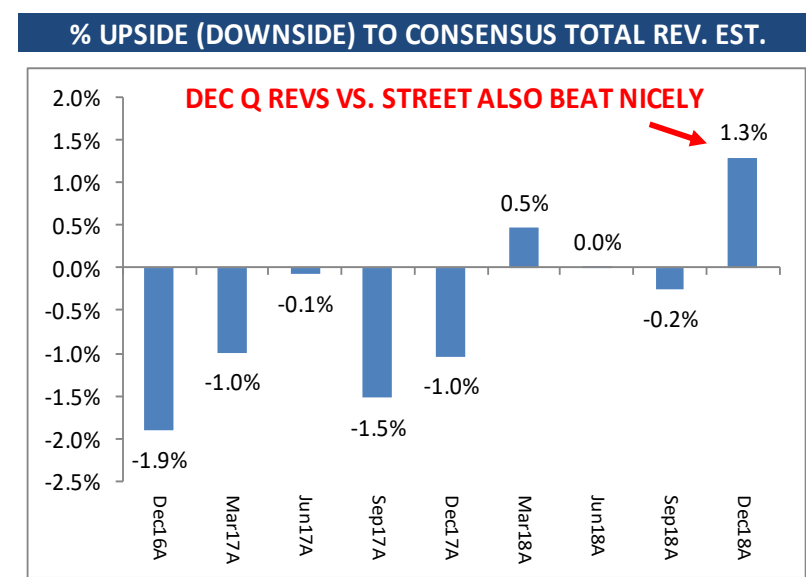
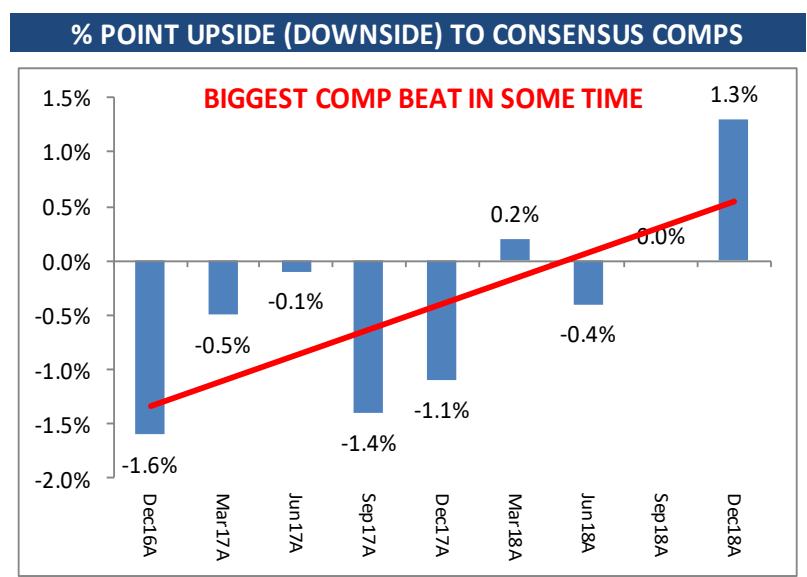
Going forward, consensus estimates reflect analyst skepticism. We believe momentum may actually accelerate, rather than slow. These charts show forecasts for EPS growth to decelerate.



Source: Company Reports, FACTSET, Quo Vadis Capital, Inc. estimates

# Which is Leading to Upside to Estimates:

During the December quarter, EAT produced the largest upside to Street comp and total revenue forecasts in many years

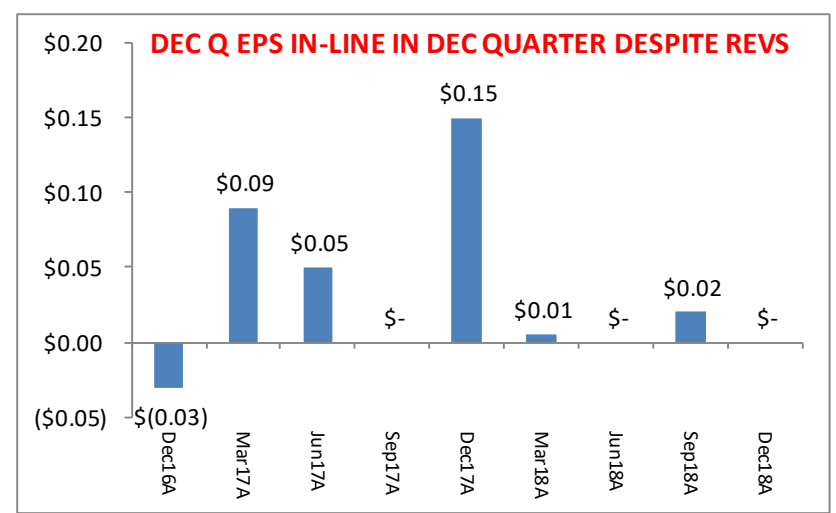


Source: Company reports, FactSet and Quo Vadis Capital, Inc. estimates

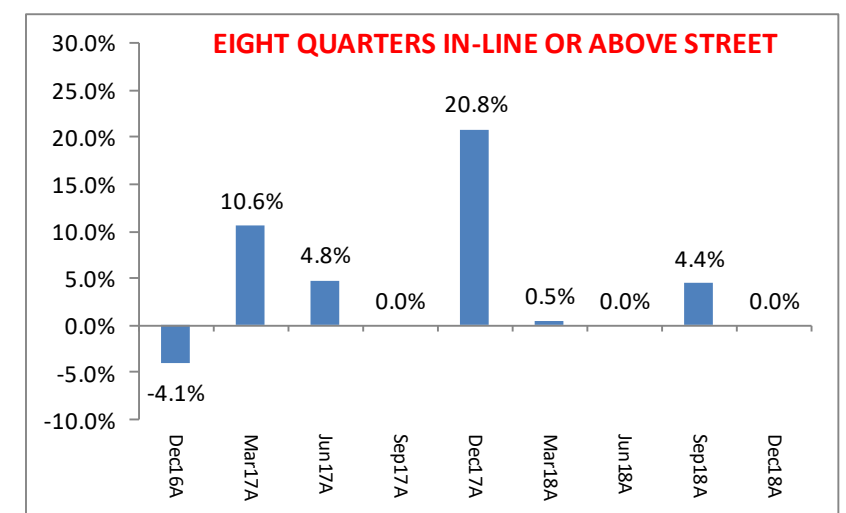
# Which is Leading to Upside to Estimates:

Investors were disappointed when the December quarter beat did not flow through to the bottom line. However, we believe the direction of revisions to both the top-and bottom-line remains favorable:

**EPS UPSIDE (DOWNSIDE) TO CONSENSUS ESTIMATE**



**% UPSIDE (DOWNSIDE) TO CONSENSUS EPS ESTIMATE**

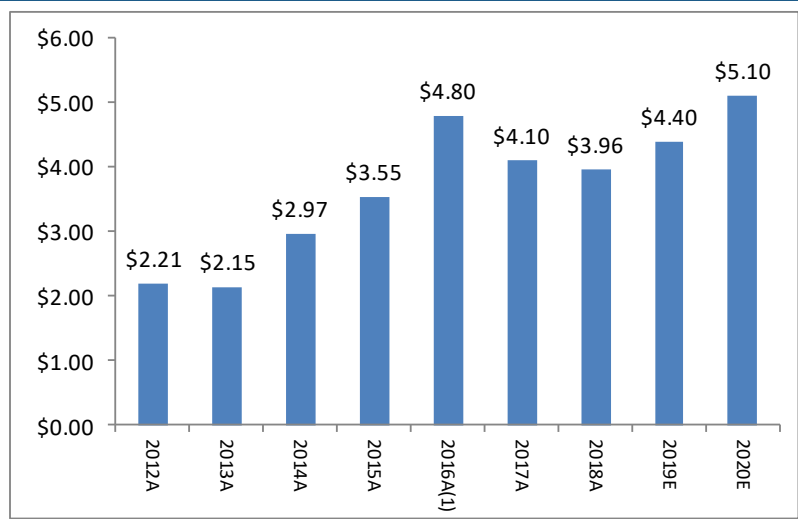


Source: Company reports, FactSet and Quo Vadis Capital, Inc. estimates

# Capital Allocation Review: Cash Flow & Capital Return Create Downside Protection

**FCF/ share has exceeded EPS in 7 of past 8 years** and should continue to exceed EPS going forward. Meanwhile, EAT’s dividend has grown at a 14% CAGR over the past 10 years.

**ANNUAL FCF PER SHARE FY11-FY20E**



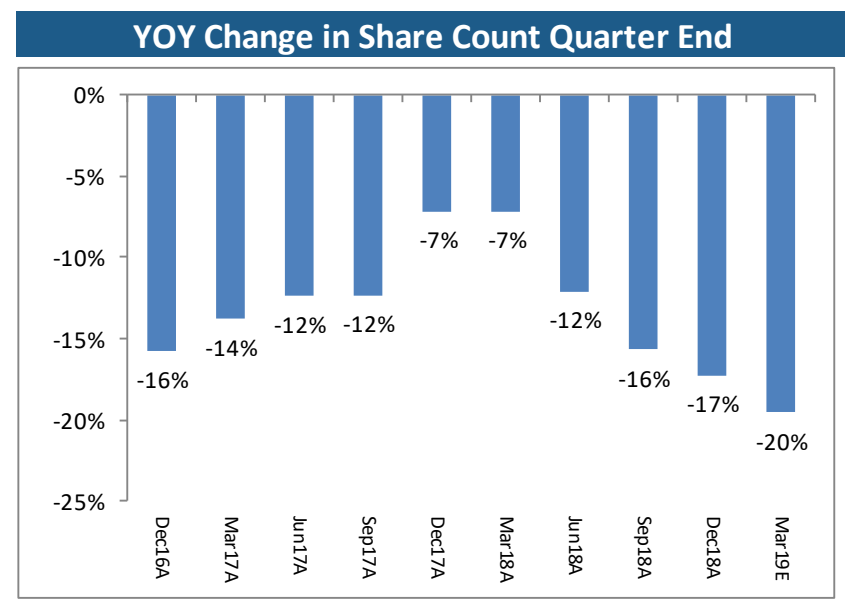
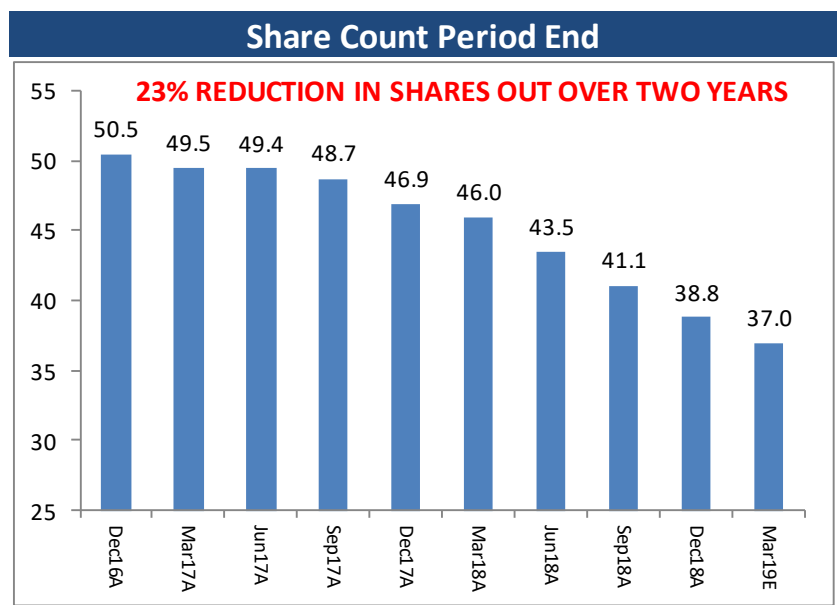
**ANNUAL DIVIDENDS PER SHARE FY11-FY20E**



Source: Company reports and Quo Vadis Capital, Inc. estimates

# Capital Allocation Review: Cash Flow & Capital Return Create Downside Protection

EAT has significantly reduced shares outstanding, buying back over a quarter of the company in the past two years.



Source: Company reports and Quo Vadis Capital, Inc. estimates

## Investment Recap:

- Recent company-led initiatives have produced a **positive inflection in traffic & sales** which together with a lower tax rate and share count have led to a positive inflection in EPS growth
- The Sell-side is skeptical and modeling moderating improvement going forward, we think the opposite could happen and thus see **upside to earnings.**
- Shares trade at among the **lowest multiples of a peer group and have a 30% short interest**, indicating that the buy-side is also not on board
- **Factoring in 5% estimated upside to current forecasts and valuation expansion to 9x EV/ EBITDA (slightly above average) = \$60 stock (43+% upside +3% dividend) in a bullish scenario.**
- Consistent FCF generation and return of capital provides **downside protection**
  - Dividend growth = 14% CAGR over 10 years; Should continue to go up
  - Repurchased more than a quarter of shares out over past two years; Expect to continue

## Risks & Other Considerations

- **Competition in the restaurant industry is intense and Chili's is exposed to promotional offers from other casual diners**
- **We expect labor cost pressure to continue to rise**
- **After 1H19 we will lap the benefit of tax reform on consumer spending**
- **The U.S. economy may be slowing and restaurants are economically sensitive**
- **Future new menu items or promotions may not be successful**



# Disclosures

## General Disclosures:

Quo Vadis Capital, Inc. ("Quo Vadis") is an independent research provider offering research and consulting services. The research products are for institutional investors only.

The price target, if any, contained in this report represents the analyst's application of a formula to certain metrics derived from actual and estimated future performance of the company. Analysts may use various formulas tailored to the facts and circumstances surrounding a specific company to arrive at the price target. Various risk factors may impede the company's securities from achieving the analyst's price target, such as an unfavorable macroeconomic environment, a failure of the company to perform as expected, the departure of key personnel or other events or circumstances that cannot be reasonably anticipated at the time the price target is calculated. Quo Vadis may change the price target on this company without notice. Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources Quo Vadis believes to be reliable; however, Quo Vadis does not guarantee its accuracy and does not purport to be complete. Opinion is as of the date of the report unless labeled otherwise and is subject to change without notice. Updates may be provided based on developments and events and as otherwise appropriate. Updates may be restricted based on regulatory requirements or other considerations. Consequently, there should be no assumption that updates will be made. Quo Vadis disclaims any warranty of any kind, whether express or implied, as to any matter whatsoever relating to this research report and any analysis, discussion or trade ideas contained herein. This research report is provided on an "as is" basis for use at your own risk, and neither Quo Vadis nor its affiliates are liable for any damages or injury resulting from use of this information. This report should not be construed as advice designed to meet the particular investment needs of any investor or as an offer or solicitation to buy or sell the securities or financial instruments mentioned herein. This report is provided for information purposes only and does not represent an offer or solicitation in any jurisdiction where such offer would be prohibited. Commentary regarding the future direction of financial markets is illustrative and is not intended to predict actual results, which may differ substantially from the opinions expressed herein. Past performance is not a guide to future performance, future returns are not guaranteed, and a loss of original capital may occur.

The analyst who is the author of this report does not have a position in shares of the companies that are the subjects of this report. However, Quo Vadis prohibits analysts from trading in a way that is inconsistent with opinions expressed in reports [subject to exceptions for unanticipated significant changes in the personal financial circumstances of the analyst].

This report may not be reproduced in part or in whole. Please do not redistribute this report.

## Reg AC Certification:

All of the views expressed in this research report accurately reflect the research analyst's personal views about any and all of the subject securities or issuers. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the subject company of this research report.

