Abstract

Business Description
Domino’s Pizza, Inc through its subsidiaries operates as a pizza chain serving domestic and overseas markets. The company has grown vastly since being founded in 1960 in Ann Arbor Michigan. Having stores operating in 85 countries, the company has managed to open more than 14,000 locations and is actively continuing this trend. The company today is known for both their pizza and their continued innovation in the fast-casual food industry. Always at the forefront of technology, the company is known for their investment in a tracking bar that allowed consumers to see in real time where their pizza was and when it will arrive on the customer’s doorstep. Domino’s operated through three segments: Domestic Stores, International Franchise, and Supply Chain

Investment Summary:
Hold: With an intrinsic price of $222
Domino’s has proved to be a worthy investment in the past as the company has provided their stockholders with positive top-line growth coming from both Same Store Sales (SSS) growth as well as unit growth to their store count. These two factors have contributed to consistent cash flow generation. Moving forward, we continue to believe the growth story can be convincing, but have reservations that lead us to believe this company to be a strong hold.

The Good
- Sales Growth
  Domino’s continues to impress when it comes to comparable sales. The company has seen 26 successive quarters of positive US SSS sales and 95 consecutive quarters internationally. This leads the restaurant industry and along with continued store build-out, investors have seen rapid appreciation of the company’s stock price.
- Technology
  With more than 60% of customers ordering via digital channels, the company has made a continued commitment to make this a seamless and enjoyable process. With over 15 million active users, the company has seen a lot of positives trying to move away attracting new consumers with various price promotions and PR programs to having a continual compounding income from returning customers.
- Reinvestment
  Management had asked their 97% franchised owners to reinvest in their store and this effort has led to higher franchises average annual per store EBITDA. Profits nearly doubled from the 2010 levels. The stores that were remodeled had an initial outlay of around $300,000-$350,00 with a payback period less than three years. To date, approximately 80% of domestically located stores are realigned with management’s vision. Looking abroad, the figure is around 70%. Management hopes for 100% completion by 2020

The Bad
• **Saturation**
  Recent strategy has shifted this new store generation predominately overseas. According to the company's investor day presentation, store openings are being dominated by their overseas market, as roughly five new foreign stores are being opened to one domestic opening.

• **Debt**
  Already highly levered at a Debt/EBITDA ratio of 6x, double the multiple of their peer group, the company is continuing to take out massive amounts of debt to fund this plan, as well as buy back stock. Given rising interest rate in the near term, borrowing capacity might be limited to fund future sizable share repurchases to support the stock price.

**Valuation:**
To arrive at our intrinsic price of $222 we used potential store openings given by management guidance. These figures did not distinguish between domestic and international stores, but we continued with the assumption that the company will open domestic stores at a rate of 10% of foreign openings. From here, we grew the domestic storefronts at 20% of the foreign market following the precedent of the last several years. Lastly, we used a 7% SSS growth rate derived from an average of previous SSS growth both domestically and abroad. Using the new effective tax rate along with the prior assumptions, resulted in a bullish case for the company’s free cash flow. A 3% terminal growth rate was used along with a discount rate of 7.52%, derived from the company’s cost of debt and equity. To find cost of equity we looked at a variety of different betas and decided upon a six month daily as it was around the franchisee model industry average. To find cost of debt we took the credit spread of a B rated bond of 3.8% and tacked it on to a risk free rate of 2.3 percent.