

Chipotle Mexican Grill (CMG)

\$933.84 (As of 02/19/20)

Price Target (6-12 Months): **\$981.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/01/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: D

Summary

Shares of Chipotle have outperformed the industry in the past year. The uptrend is likely to continue as the company reported better-than-expected fourth-quarter 2019 results. While the bottom line beat the consensus mark for the ninth straight quarter, the top line surpassed the same for the fifth consecutive quarter. Focus on increasing food safety and enhancing customer experience, along with various sales-building and strategic initiatives are likely to drive the top line. In an effort to attract more customers, the company launched its loyalty program — Chipotle Rewards — nationwide. For 2020, management expects comps to grow in mid-single digit. It expects to open 150-165 restaurants in 2020 and is also expected to introduce one or two new menu items every year. However, high costs and intense competition remain concerns.

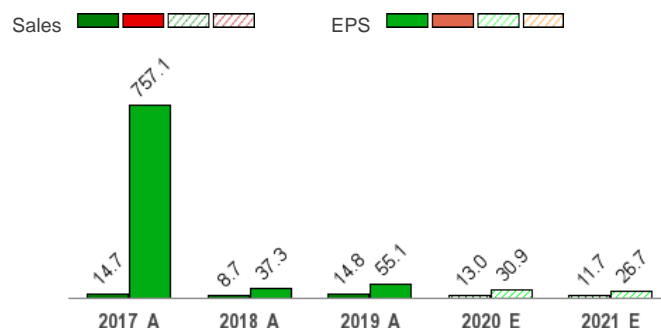
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$938.88 - \$592.73
20 Day Average Volume (sh)	422,761
Market Cap	\$25.9 B
YTD Price Change	11.6%
Beta	0.74
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Retail - Restaurants
Zacks Industry Rank	Top 27% (69 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.4%
Last Sales Surprise	2.7%
EPS F1 Est- 4 week change	2.7%
Expected Report Date	04/22/2020
Earnings ESP	0.0%
P/E TTM	66.4
P/E F1	50.8
PEG F1	2.6
P/S TTM	4.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,662 E	1,811 E	1,773 E	1,803 E	7,048 E
2020	1,501 E	1,618 E	1,583 E	1,606 E	6,311 E
2019	1,308 A	1,434 A	1,404 A	1,440 A	5,586 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$5.11 E	\$6.63 E	\$5.75 E	\$5.50 E	\$23.30 E
2020	\$3.79 E	\$5.48 E	\$4.71 E	\$4.46 E	\$18.39 E
2019	\$3.40 A	\$3.99 A	\$3.82 A	\$2.86 A	\$14.05 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/19/2020. The reports text is as of 02/20/2020.

Overview

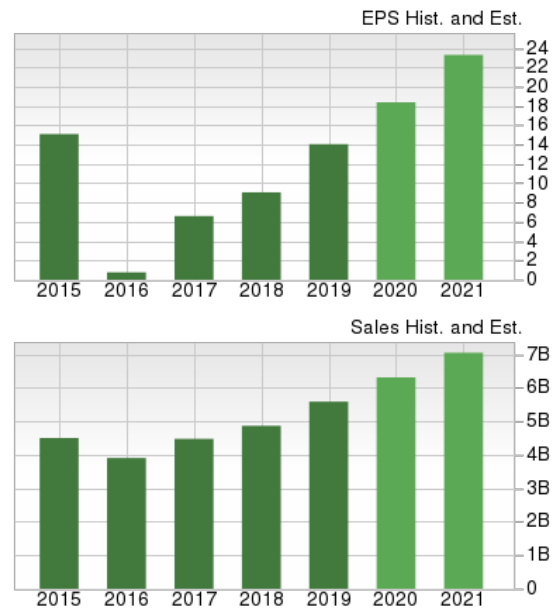
A Delaware corporation, Chipotle Mexican Grill, together with its subsidiaries operates quick-casual and fresh Mexican food restaurant chains. The company was founded in 1993 by Steve Ells who started with a single restaurant in Denver, CO. The company offers a focused menu of burritos, tacos, burrito bowls (a burrito without the tortilla) and salads. Chipotle restaurants feature free-range, hormone-free pork, natural chicken and other meat products cooked through traditional methods and served in a unique atmosphere. Chipotle classifies its restaurants as end-caps (at the end of a line of retail chains), in-lines (in a line of retail chains), free-standing units and others.

Chipotle, being one of the most recognized fast-casual Mexican restaurant chains in the United States, had a good share of negative publicity throughout 2016 due to an issue of food-borne illnesses that surfaced toward 2015-end. As a safety measure, the company was forced to close several outlets. In order to chalk out a viable business strategy, Chipotle discarded its former co-CEO model and appointed former Yum! Brands' executive Brian Niccol as the CEO.

The company is committed to using high-quality real ingredients, classic cooking techniques and distinctive interior design to serve customers. As of Dec 31, 2019, the company operated nearly 2,622 restaurants across the United States, Canada, the U.K., France and Germany. Notably, the company manages operations and restaurants based on 11 regions that make one reportable segment.

Chipotle's marketing strategy shifted from a promotion driven decentralized approach in 2017 to a more central model designed to generate higher consumer awareness and attract guests. The company utilizes multiple marketing channels, including national television, digital marketing, social media, fundraising, events and sponsorships to reach consumers. Delivery services are mostly made by third party service providers.

In 2018, Chipotle launched a loyalty program called Chipotle Rewards, which provides customers with the opportunity to earn bonus points or free food. Earned rewards generally expire one to six months after they are issued, and points generally expire if an account is inactive for a period of six months.



Reasons To Buy:

▲ **Share Price Gains on Robust Earnings Trend:** Shares of Chipotle have gained over the past year, outperforming the industry's rally. The robust share price appreciation can be attributed to better-than-expected earnings in nine consecutive quarters. In fourth-quarter 2019, adjusted earnings of \$2.86 per share surpassed the Zacks Consensus Estimate of \$2.74. The bottom line also improved 66.3% from the year-ago quarter driven by increased revenues and strong operating margins. For 2020, earnings estimates have been revised upward over the past 30 days, reflecting analysts' optimism surrounding the company's earnings potential.

Chipotle's increased focus on food safety and enhancing customer experience, along with various sales-building and strategic initiatives bode well.

▲ **Efforts to Revive Brand Recognition:** Chipotle, being one of the most recognized fast-casual Mexican restaurant chains in the United States, had a good share of negative publicity throughout 2016 due to an issue of food-borne illnesses that surfaced toward 2015-end. As a safety measure, the company was forced to close several outlets. Ever since then, this fast-casual Mexican chain has been undertaking aggressive efforts to restore its economic model as well as regain customer trust. In order to chalk out a viable business strategy, Chipotle discarded its former co-CEO model and appointed former Yum! Brands' executive Brian Niccol as the CEO. Niccol's expertise in restaurant operations, digital technologies and branding significantly helped Chipotle in boosting earnings.

In order to strengthen its brand position, Chipotle pursued the Big Fix initiative, designed to revive restaurant standards. Through Cultivate University, the company trained its field leaders via an in-restaurant and in-classroom one-week training session, launched in April. This is expected to reinforce crew member engagement and drive consumer awareness of the brand.

▲ **Increased Focus on Food and Environment Safety:** As a part of its revival strategy, Chipotle fulfilled its pledge of using no added colors, flavors or preservatives of any kind in any of its ingredients. In fact, Chipotle has long been a pioneer in serving superior quality ingredients including the use of local and organically grown produce, dairy from cows raised on pasture, and meat from animals raised without hormones or antibiotics.

The company has also taken noteworthy steps to reduce the amount of food and packaging waste to be disposed of in landfills. As announced, Chipotle is implementing practices like minimal food waste disposal during the preparation process, recycling and compost programs for food packages, use of reusable lids replacing plastic wraps, and participation in the Harvest Program to donate leftover food to local communities. The company is also increasing composting convenience in its restaurants to 20% by 2020.

For ensuring food safety, the company introduced a crew bonus program, which will pay its employees a bonus amount if they achieve their desired goal in food safety. Further, the company recently introduced the Debt-Free Degrees program in addition to its newly expanded tuition reimbursement program to develop a better restaurant culture.

▲ **Various Initiatives to Spur Growth:** Chipotle is working on strengthening its brand and recovering sales by shifting its strategy from giveaways, discounts and rewards to new menu items, operational excellence, enhancement of guest experience by retraining workers, technology-driven convenience, and more aggressive brand marketing. Roll out of queso substantially spurred sales. Additionally, Chipotle has been working on a new pipeline for its menu offerings. Last year, Chipotle launched its first menu innovation called Lifestyle Bowls for mobile and web orders that resonated well with consumers. The company introduced new kitchen ovens, which are improving the quality of its latest Quesadillas. The company is also testing queso blanco, salads in quesadillas that are gaining valuable feedback in various markets besides carne asada. Carne asada will be available for a limited time period and is also recently added in the Lifestyle Bowls. The company announced that it plans to introduce one or two new menu items every year.

Notably, the company's robust marketing activities, including a combination of brand-building efforts, as well as transaction-driving promotions and advertising, are resulting in a steady inflow of new customers. The company also partnered with a film director, David Gelb, for the carne asada launch. For 2020, the company's priorities will revolve around the five key initiatives namely, digital system investments such as pickup shelves, digitized make lines, loyalty and delivery; marketing programs focusing on cooking techniques; and menu innovation and operational excellence. Moreover, the company is also focusing on unit expansion to drive growth. It expects to inaugurate 150-165 restaurants in 2020.

▲ **Strengthening Digital Capabilities:** Chipotle is prioritizing its e-Commerce program to gain customer confidence as part of its digital innovation. The company is aggressively trying to make digital ordering more appealing to customers and more efficient for its restaurants, in order to drive digital sales and retain customers. In the regard, Chipotle has redesigned and simplified its online ordering site, enabled online payment for catering, online meal customizations and collaborated with several well-known third-party providers for delivery.

The third quarter also witnessed particularly strong traction in delivery sales. In the fourth quarter, digital sales grew 78% year over year. Digital sales totaled \$282 million during the fourth quarter and accounted for 19.6% of sales. Also, since the rollout of its "Smarter Pickup Times" technology, there has been a significant increase in digital orders and higher guest satisfaction. As the company's digital orders are made on a second makeline, it allows it to deliver excellent throughput and enhance the experience of customers, who are increasingly shifting to digital ordering. Meanwhile, the company is pressing ahead with its plans to enhance delivery system. Delivery remains a key driver for its digital growth. In fact, delivery is now available for more than 98% of its restaurants.

Reasons To Sell:

- ▼ **Cost Issues Keeping Profits Under Pressure:** Chipotle continued efforts to connect with its customers in order to retrieve their trust and loyalty as well as bring them back to its stores on the back of high marketing and promo expenses, has been hurting its profitability. Moreover, costs to support the company's newly designed food safety program can weigh on the company's margins. Also, implementation of food safety practices has increased the amount of labor required to prepare and serve food, resulting in higher labor costs which may continue to keep profits under pressure.
- ▼ **Valuation Looks Stretched:** Chipotle's valuation looks a bit stretched compared with its industry average. Looking at the company's forward 12-month price-to-earnings (P/E) ratio, which is one of the most commonly used valuation ratios and is best suited for evaluating restaurants, investors might not want to pay any further premium. It currently has a forward 12-month P/E ratio of 48.99. So, the stock is relatively overvalued right now compared with its peers as the industry's average PE is 23.25 currently.
- ▼ **Industry Susceptible to Consumer Discretionary Spending:** Chipotle operates in the retail restaurant space that is highly dependent on consumer discretionary spending. Consumers' propensity to spend largely depends on the overall macroeconomic scenario. Although higher disposable income and increased wages are favoring the industry right now, it can change with the slightest disruption in the economy. The company, therefore, is highly vulnerable to the inconsistent nature of consumer discretionary spending. If it does not make pragmatic use of advanced technologies to innovate across value chains, it has high chances of fading out like many other restaurant retailers.

High costs associated with U.S. restaurant space remain potent headwinds.

Last Earnings Report

Chipotle Earnings & Revenues Beat Estimates in Q4

Chipotle Mexican Grill, reported fourth-quarter 2019 results, wherein both earnings and revenues surpassed the respective Zacks Consensus Estimate. While the bottom line beat the consensus estimates for the ninth straight quarter, the top line came ahead of the same for the fifth consecutive quarter. Following the results, the company's shares gained 1.5% in after-hour trading session on Feb 4.

The company's adjusted earnings of \$2.86 per share surpassed the Zacks Consensus Estimate of \$2.74. The bottom line also improved 66.3% from the year-ago quarter, driven by increased revenues and strong operating margins.

Chipotle's increased focus on augmenting customer experience by introducing food-safety programs, various sales-building initiatives and greater digital innovation resulted in revenue growth in the fourth quarter.

Revenues & Comparable Restaurant Sales

Quarterly revenues of \$1.4 billion surpassed the consensus mark by 2.7% and improved 17.6% year over year. This upside can primarily be attributed to improvement in comps and restaurant openings. In the quarter under review, Chipotle opened 80 restaurants and closed three, taking the total restaurant count to 2,622.

Comps in the fourth quarter rose 13.4%, driven by a rise of 8% in comparable restaurant transactions and an increase of 5.4% in average check.

Costs, Operating Highlights & Net Income

Food, beverage and packaging costs, as a percentage of revenues, decreased 10 basis points (bps) to 33.1% on the back of menu price increases and favorable avocado pricing, partially offset by higher costs of ingredients.

Restaurant-level operating margin was 19.2%, up 220 bps from 17% in the year-ago quarter. This upside was primarily driven by comps growth, partially negated by wage inflation, increased food costs, and marketing and delivery expenses.

Net income in the reported quarter amounted to \$72.4 million, up from \$32 million in the prior-year quarter.

Balance Sheet

Cash and cash equivalents as of Dec 31, 2019, were \$480.6 million compared with \$250 million as of Dec 31, 2018.

Inventory totaled \$26.1 million as of Dec 31, 2019, down from \$21.6 million as of Dec 31, 2018. Goodwill, as a percentage of total assets, was 0.4% at the end of the fourth quarter compared with 1% at the end of 2018.

2020 Outlook

For 2020, management expects comps to grow in a mid-single digit. The company estimates effective tax rate between 26% and 29%. It expects to inaugurate 150-165 restaurants in 2020.

Quarter Ending **12/2019**

Report Date	Feb 04, 2020
Sales Surprise	2.65%
EPS Surprise	4.38%
Quarterly EPS	2.86
Annual EPS (TTM)	14.07

Valuation

Chipotle's shares are up 55.3% over the trailing 12 months. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are up 17% and 19.3% over the past year, respectively.

The S&P 500 index is up 20.7% in the past year.

The stock is currently trading at 48.99x forward 12-month Price to Earnings value, which compares with 25.76x for the Zacks sub-industry, 26.22x for the Zacks sector and 19.3x for the S&P 500 index.

Over the past five years, the stock has traded as high as 206.3x and as low as 24.82x, with a 5-year median of 44.55x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$981 price target reflects 51.46x forward 12-month Price to Earnings value.

The table below shows summary valuation data for CMG.

Valuation Multiples - CMG					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	48.99	25.76	26.22	19.3
	5-Year High	206.3	26.41	26.22	19.34
	5-Year Low	24.82	20.45	19.07	15.18
	5-Year Median	44.55	23.25	22.99	17.47
P/S F12M	Current	4.04	3.67	1.09	3.57
	5-Year High	4.6	3.85	1.11	3.57
	5-Year Low	1.44	2.91	0.8	2.54
	5-Year Median	2.79	3.25	0.92	3
P/CF	Current	36.72	17.62	15.11	25.09
	5-Year High	38.1	20.39	15.18	25.09
	5-Year Low	15.15	8.5	10.74	11.78
	5-Year Median	26.9	16.53	12.85	16.29

As of 02/19/2020

Industry Analysis Zacks Industry Rank: Top 27% (69 out of 255)



Top Peers

Arcos Dorados Holdings Inc. (ARCO)	Neutral
Bloomin Brands, Inc. (BLMN)	Neutral
Cracker Barrel Old Country Store, Inc. (CBRL)	Neutral
Dominos Pizza Inc (DPZ)	Neutral
Darden Restaurants, Inc. (DRI)	Neutral
Brinker International, Inc. (EAT)	Neutral
Restaurant Brands International Inc. (QSR)	Neutral
Yum! Brands, Inc. (YUM)	Underperform

Industry Comparison Industry: Retail - Restaurants				Industry Peers		
	CMG Neutral	X Industry	S&P 500	BLMN Neutral	QSR Neutral	YUM Underperform
VGM Score	C	-	-	A	C	C
Market Cap	25.93 B	443.37 M	24.59 B	2.00 B	19.69 B	31.82 B
# of Analysts	16	5.5	13	7	11	11
Dividend Yield	0.00%	0.00%	1.78%	1.74%	3.03%	1.79%
Value Score	F	-	-	A	C	F
Cash/Price	0.03	0.03	0.04	0.03	0.09	0.02
EV/EBITDA	41.32	15.28	14.21	11.47	14.52	20.98
PEG Ratio	2.64	2.21	2.09	1.29	1.93	2.20
Price/Book (P/B)	15.42	3.08	3.28	13.20	4.84	NA
Price/Cash Flow (P/CF)	42.52	11.96	13.59	5.69	11.43	26.05
P/E (F1)	50.78	22.35	19.17	12.69	22.12	26.97
Price/Sales (P/S)	4.64	0.95	2.68	0.48	3.51	5.68
Earnings Yield	1.97%	4.27%	5.18%	7.90%	4.52%	3.71%
Debt/Equity	1.59	0.94	0.70	15.62	3.18	-1.26
Cash Flow (\$/share)	21.96	1.53	6.93	4.05	5.77	4.04
Growth Score	A	-	-	C	C	A
Hist. EPS Growth (3-5 yrs)	0.15%	7.71%	10.84%	7.11%	28.00%	0.67%
Proj. EPS Growth (F1/F0)	30.88%	8.95%	7.00%	17.99%	9.56%	9.86%
Curr. Cash Flow Growth	34.05%	7.67%	7.81%	4.05%	19.29%	3.60%
Hist. Cash Flow Growth (3-5 yrs)	1.89%	6.24%	8.25%	2.17%	32.62%	-6.71%
Current Ratio	1.61	0.60	1.24	0.27	1.09	0.99
Debt/Capital	61.41%	61.12%	42.37%	93.98%	76.05%	NA
Net Margin	6.27%	3.15%	11.69%	3.15%	11.48%	23.12%
Return on Equity	25.14%	7.75%	16.86%	73.91%	32.40%	-13.90%
Sales/Assets	1.16	1.14	0.55	1.18	0.26	1.14
Proj. Sales Growth (F1/F0)	12.97%	3.02%	4.05%	2.01%	3.73%	3.47%
Momentum Score	D	-	-	C	C	D
Daily Price Chg	0.68%	0.13%	0.38%	3.32%	-0.35%	1.12%
1 Week Price Chg	6.68%	1.87%	1.65%	5.95%	5.29%	3.18%
4 Week Price Chg	6.22%	0.96%	0.86%	6.27%	1.21%	-1.22%
12 Week Price Chg	14.34%	1.01%	4.56%	-2.82%	-0.54%	4.52%
52 Week Price Chg	56.23%	5.00%	14.15%	6.96%	1.93%	11.05%
20 Day Average Volume	422,761	224,325	1,989,235	920,463	2,171,958	1,776,722
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	6.27%	0.00%	-0.76%
(F1) EPS Est 4 week change	2.74%	0.00%	-0.03%	6.27%	0.34%	-5.61%
(F1) EPS Est 12 week change	3.79%	0.00%	-0.21%	6.27%	0.30%	-6.18%
(Q1) EPS Est Mthly Chg	-5.56%	0.00%	-0.40%	-0.57%	0.52%	-9.67%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	A
Momentum Score	D
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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