

Papa Johns(PZZA)

\$95.17 (As of 08/12/20)

Price Target (6-12 Months): **\$109.00**

Long Term: 6-12 Months

Zacks Recommendation:
Outperform

(Since: 07/06/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: B

Summary

Shares of Papa John's have outperformed the industry so far this year. The outperformance can be primarily attributed to product innovation, strategic partnerships, international expansion and franchising initiatives. The company reported mixed second-quarter 2020 results, wherein earnings beat the Zacks Consensus Estimate while revenues missed the same. Nonetheless, the top and the bottom line increased 15.3% and 300%, respectively, on a year-over-year basis. Moreover, the company is focusing on TV and digital spend (including sponsorship/venue spending) to drive new customer count. Also, the company is continually striving to eliminate barriers to expansion in existing international markets and identify new market opportunities. Earnings estimates for 2020 have moved up over the past 30 days.

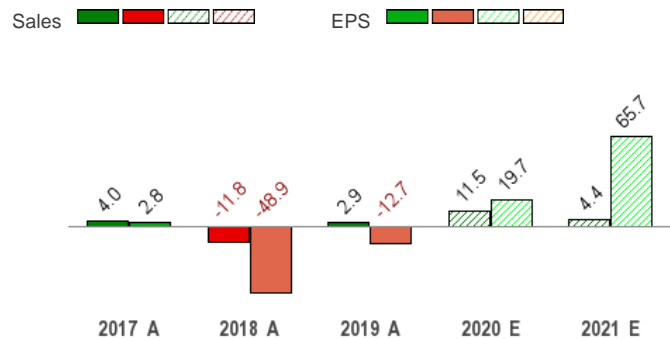
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$100.69 - \$28.55
20 Day Average Volume (sh)	553,233
Market Cap	\$3.1 B
YTD Price Change	50.7%
Beta	1.02
Dividend / Div Yld	\$0.90 / 0.9%
Industry	Retail - Restaurants
Zacks Industry Rank	Top 49% (125 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	20.0%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	10.1%
Expected Report Date	11/04/2020
Earnings ESP	-10.3%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	461 E	460 E	469 E	485 E	1,884 E
2020	410 A	461 A	467 E	466 E	1,805 E
2019	398 A	400 A	404 A	418 A	1,619 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.59 E	\$0.60 E	\$0.50 E	\$0.56 E	\$2.32 E
2020	\$0.15 A	\$0.48 A	\$0.27 E	\$0.48 E	\$1.40 E
2019	\$0.31 A	\$0.28 A	\$0.21 A	\$0.37 A	\$1.17 A

*Quarterly figures may not add up to annual.

P/E TTM	78.7
P/E F1	68.0
PEG F1	5.4
P/S TTM	1.9

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/12/2020. The reports text is as of 08/13/2020.

Overview

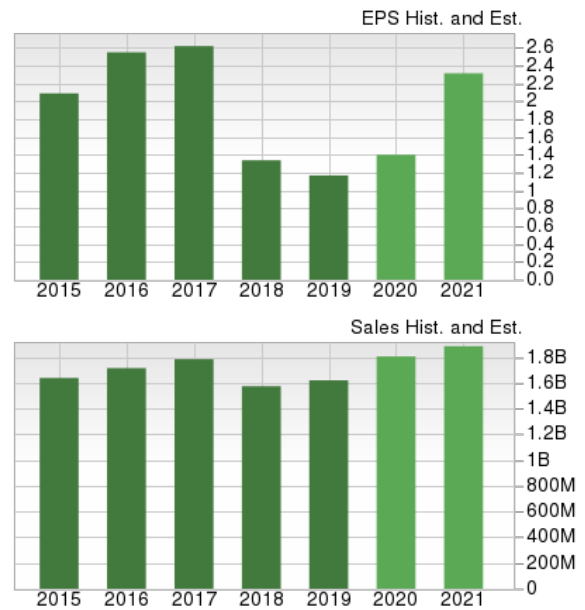
Headquartered in Louisville, KY, Papa John's began its operations in 1984. This Delaware Corporation, operates and franchises pizza delivery and carryout restaurants in the United States and other specific international markets. The company's dine-in and delivery restaurants operate under the brand name Papa John's.

As of Jun 28, 2020, there were 5,347 Papa John's restaurants operating in 49 countries and territories. Out of these, 598 were company-owned while the remaining 2,686 were franchised restaurants in North America. Meanwhile, 2,063 are operating internationally.

Papa John's reportable segments include domestic company-owned restaurants, domestic commissaries, North America franchising and international operations. North America encompasses operations in the United States and Canada. Domestic incorporates the adjoining areas of the United States. International franchisees are defined as all franchise operations outside of the United States and Canada.

Papa John's has been reeling under negative publicity for quite a long time, owing to the denouncement of its ex-CEO, John H. Schnatter, on grounds of a racial slur. Ever since Papa John's have been trying to make significant changes in its board and is trying to revive consumer sentiment.

Going by the current scenario, the company has managed to hire more than 20,000 new restaurant team members during second-quarter 2020 and intends to employ another 10,000 by the third quarter of 2020. To better its equation with customers, the company continues to help those affected by the pandemic. Notably, the initiatives are likely to drive long-term sustainable loyalty toward its brand even after the pandemic dies out.



Reasons To Buy:

▲ **Strong Brand Building in Focus:** Papa John's is a leading take-out and pizza delivery restaurant chain in the world. As part of its clean label commitment, Papa John's was the first pizza delivery chain to announce the removal of preservatives such as BHA and BHT, flavor enhancer, MSG, cellulose, partially hydrogenated oils and high-fructose corn syrup. All these efforts reinforce the company's commitment to provide quality food and deliver better ingredients to its customers, and thereby living up to its strong brand commitment.

The company's continued international expansion plans, strategic partnerships, strong digital platform and various sales initiatives bode well

▲ **Product Launches to Drive Growth:** The company continues to focus on product introduction to drive growth. Notably, menu innovation like Garlic Parmesan Crust, toasted handheld Papadials and Jalapeno Popper Rolls continues to witness solid popularity among customers, thereby boosting the top line. Backed by better brand positioning, the new products have driven higher ticket and traffic across dayparts without cannibalizing core premium products and complexing operations at other stores.

Nonetheless, the product innovation pipelines are likely to be continued into the third quarter. In July 2020, the company in collaboration with Shaquille O'Neal (Papa John's Board member and restaurant owner) launched a new Shaq-a-Roni pizza. Markedly, the launch has turned out to be hugely popular among consumers and has generated more than \$2 million in charitable contributions.

▲ **International Expansion & Focus on Franchising:** Many of Papa John's restaurants are located in international markets like Europe, the Middle East, Latin America, Portugal and China, and continue to perform strongly. The China region continues to experience growth, driven by the company's optimized restaurant model, brand design enhancements and increased integration with third-party aggregators that is broadening its accessibility channels. Papa John's has inked developmental agreements in many regions including Mexico, Egypt, Russia, Spain, Chile, the Netherlands, Colombia and Boston. In 2019, it opened 233 international units, bringing the total number of open units to more than 2,100 stores across 48 countries outside the United States, including Portugal and Pakistan. The company added 92 net worldwide units in 2019. As of Mar 29, 2020, the company's development pipeline included 1,140 restaurants (90 units in North America and 1,050 units internationally), the majority of which are scheduled to open over the next six years.

Notably, Papa John's is committed to develop and maintain a strong franchise system. The company is continually striving to eliminate barriers to expansion in existing international markets and identify new market opportunities. Notably, in 2019, it re-franchised 46 company-owned restaurants — including 19 in Georgia and 23 restaurants in Florida — for \$4.74 million. Over the next several years, the company plans to increase its international units, a large portion of which will be franchised. We believe re-franchising a large chunk of its system reduces a company's capital requirements and facilitates earnings per share growth and ROE expansion. Alongside, free cash flow continues to grow, allowing reinvestment for increasing brand recognition and shareholder return.

▲ **Capitalizing on Technology to Boost Sales:** Papa John's is investing heavily in technology-driven initiatives like digital ordering to boost sales. The company's online and digital marketing activities have increased significantly over the past several years in response to increasing use of online and mobile web technology. In fact, Papa John's continues to reinforce its commitment toward providing a better customer experience with enhancements to its digital ordering process. The company further expanded its digital ordering capabilities with the launch of Facebook Instant Ordering and became the first national pizza chain to do so. It is also the foremost national restaurant chain to launch a custom ordering app for Apple TV, commence a nationwide digital rewards program and surpass 60% of the total U.S. sales via digital channels. Currently, the company has 100 corporate and franchise restaurants that enable customers to visually track delivery on a map. Notably, Papa John's announced that it has entered into a national partnership with UberEATS, and its existing fastest-growing door-to-door delivery service providers DoorDash and Postmates.

Meanwhile, Papa John's continues to invest in direct customer delivery. In March 2020, the company re-engineered its ordering and delivery process with the launch of no contact delivery. Notably, it drove substantial gains in its satisfaction metrics and delivered seamless customer experience during the second quarter.

▲ **Effective Changes in Marketing Mix and Tactics:** A change in marketing mix and tactics is driving new customers to the company and reactivating lapsed customers. The company is focused on TV and digital spend (including sponsorship/venue spending). In the fourth quarter of 2019, the company started buying TV ads in the upfront market allowing the advertisements to reach more customers with a significant increase in media impressions. During the second quarter of 2020, the company had more than 3 million new customers on its digital channels.

▲ **Solid Comps Growth:** The company recorded positive comparable sales growth in the second quarter of 2020, which marks the second straight quarter of comps growth. Global restaurant sales climbed 19.1% against the year-ago quarter's fall of 3.8%. Also, domestic company-owned restaurant comps rose 22.6% in the reported quarter against a 6.8% decline in the year-ago quarter.

Risks

- **Withdraws 2020 Outlook Due to Coronavirus:** Considering the panoptic impact of coronavirus (COVID-19) pandemic on its business and the industry, the company has withdrawn its fiscal 2020 guidance. Of the company's 2,100 international franchised stores, approximately 225 are temporarily closed (mostly in parts of Europe and Latin America) in accordance with government policies.
 - **High Debt a Concern:** A strong balance sheet will help a company tide over the ongoing crisis. As of Jun 28, 2020, the company had \$327.9 million of long-term debt, compared with \$342.6 million at the end of Mar 29, 2020. Although debt has declined marginally, the company's debt-to-capitalization at the end of second-quarter 2020 stands at 241%. Moreover, the company ended second-quarter 2020 with cash and cash equivalent of \$75.7 million, which may not be enough to manage the high debt level.
 - **High Costs Hurt:** During the second quarter, the company witnessed high costs associated with product launch, marketing campaigns and other sales-building initiatives. Also, rise in food and other operating costs took a toll on margins. Notably, total costs for the second quarter 2020 increased 11.6% year over year to \$430.1 million from \$385.6 million reported in the prior-year quarter.
 - **Affordable Care Act to Hurt Profits:** The Affordable Care Act, commonly known as Obamacare, is expected to have an adverse impact on restaurant operators. The Affordable Care Act required employers to extend health benefits. The law entails restaurants with 100 or more full-time equivalent employees to offer health care coverage to substantially all full-time employees and their dependents. Meanwhile, from 2016, these rules apply for employers with 50 to 99 full-time-equivalent employees. Moreover, the collapse of the Republican-led bill, which was intended to replace Obamacare, means that the Affordable Care Act is here to stay. This means that the restaurant operators will have to continue shouldering increased labor costs, which in turn will hurt margins.
 - **Cutthroat Competition:** The restaurant space is highly competitive as numerous restaurant operators are ongoing advanced and prudent strategies to increase their sales. In fact, going by the current retail scenario, adapting to shifting demand has become a major precedence for retailers. Companies with continual digital innovation, focus on product customization, and launch and delivery of seamless consumer experience can only thrive in the competitive space. This puts a lot of pressure on Papa John's to continuously change its strategies in correspondence to the fickle consumer demand.
 - **Soft International Performance a Concern:** The company has been generating soft revenues over the last several quarters in the International segment. In 2019, its international revenues declined 6.7%. Papa John's, which has a significant international presence, is exposed to unfavorable fluctuations in currency. Also, the International segment's revenues are hurt by the same. Currently, markets in the Middle East and Latin America are facing government closures as well as heavy restrictions on trade.
 - **Valuation Looks Stretched:** Papa John's valuation looks a bit stretched compared with the 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 53.18. Hence, the stock is relatively overvalued right now compared with its peers, as the industry's average P/E is 31.53.
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Last Earnings Report

Papa John's Q2 Earnings Beat Estimates, Increase Y/Y

Papa John's reported mixed second-quarter 2020 results, wherein earnings beat the Zacks Consensus Estimate, while revenues missed the same. The top and the bottom line increased on a year-over-year basis.

Adjusted earnings of 48 cents per share surpassed the Zacks Consensus Estimate of 40 cents by 20% and increased 300% from 16 cents reported in the prior-year quarter.

During the second quarter, total revenues of \$460.6 million missed the Zacks Consensus Estimate of \$463.9 million by 0.7%. However, the top line grew 15.3% on a year-over-year basis. Notably, the upside can be attributed to positive comparable sales in North America, higher royalties and commissary revenues from the United Kingdom as well as increased marketing fund revenues on an increase in national marketing fund contribution rate and higher online revenues.

Quarter Ending

Report Date	Aug 06, 2020
Sales Surprise	NA
EPS Surprise	20.00%
Quarterly EPS	0.48
Annual EPS (TTM)	1.21

Global Restaurant Sales & Comps

In the second quarter, global restaurant sales rose 19.1% against the year-ago quarter's fall of 3.8%. Excluding foreign currency impact, global restaurant sales rose 20.8% against the year-ago quarter's decline of 2.6%.

Domestic company-owned restaurant comps moved up 22.6% in the reported quarter against a 6.8% decline in the year-ago quarter.

At North America franchised restaurants, comps rose 29.7% against a decline of 5.3% in second-quarter 2019. Also, comps at system-wide North America restaurants improved 28% against a 5.7% decline seen in the year-ago quarter.

Comps at system-wide international restaurants were up 5.3% compared with 0.3% growth in the prior-year quarter.

Nonetheless, for the first month of the third quarter (Jun 29-Jul 26, 2020), comparable sales at domestic company-owned, North America franchised and systemwide North America restaurants are estimated to grow 23.6%, 32.4% and 30.3%, year over year, respectively. Comps at system-wide international restaurants are estimated to grow 13.9% year over year.

Operating Highlights

Total operating income in the second quarter was \$30.5 million compared with \$14.2 million in the year-ago quarter. Total costs and expenses amounted to \$430.1 million, up 11.6% from the prior-year quarter.

Balance Sheet

As of Jun 28, 2020, cash and cash equivalents totaled \$75.7 million compared with \$27.9 million as on Dec 29, 2019. Long-term debt was \$327.9 million at the end of second-quarter 2020 compared with \$347.3 million at 2019-end.

Inventories at the end of the reported quarter increased to \$32.5 million from \$27.5 million on Dec 29, 2019. Free cash flow for the six months ended Jun 28, 2020, summed \$67 million compared with \$8.9 million in the year-ago period.

The company paid out cash dividends worth \$10.7 million in second-quarter 2020 and announced third-quarter 2020 cash dividend of approximately \$10.8 million. The third-quarter dividend will be payable on Oct 1, 2020.

Unit Developments

During the second quarter, Papa John's opened nine restaurants in North America and exited 10, with the global restaurant count being 5,347. Currently, the company is operating in 48 countries and territories worldwide.

Recent News

Papa John's Reports Preliminary Comps, Stock Gains – Jun 30, 2020

Papa John's reported preliminary comparable restaurant sales for the five weeks and fiscal second quarter ended Jun 28, 2020.

For the five weeks ended Jun 28, comparable sales at Domestic company-owned restaurants, North America franchised restaurants, System-wide North America restaurants and System-wide international restaurants rose 18.5%, 26.3%, 24.4% and 6%, respectively. Markedly, in the month of June, the company not only witnessed double-digit sales growth in North America but also strong growth internationally.

For the fiscal second quarter (ended Jun 28), the metrics improved 22.6%, 29.6%, 28% and 5.3%, at Domestic company-owned restaurants, North America franchised restaurants, System-wide North America restaurants and System-wide international restaurants, respectively.

Papa John's Spruces Up Menu With Launch of Shaq-a-Roni Pizza – Jun 29, 2020

In a bid to boost its pizza offerings, Papa John's recently announced its collaboration with its board member, entrepreneur and restaurant owner - Shaquille O'Neal -- for the launch of a new pizza, Shaq-a-Roni.

Valuation

Papa John's shares are up 50.7% in the year-to-date period and 109.1% over the trailing 12-month period. Stocks in the Zacks sub-industry is down by 1.6%, but Zacks Retail-Wholesale sector is up by 25.5% in the year-to-date period. Over the past year, the Zacks sub-industry is down by 7.7%, while sector is up by 39.7%.

The S&P 500 index is up 3.3% in the year-to-date period and 17.4% in the past year.

The stock is currently trading at 53.18x forward 12-month earnings, which compares to 31.53x for the Zacks sub-industry, 33.03x for the Zacks sector and 22.6x for the S&P 500 index.

Over the past five years, the stock has traded as high as 56.18x and as low as 18.04x, with a 5-year median of 28.31x. Our Outperform recommendation indicates that the stock will perform better-than the market. Our \$109 price target reflects 61.23x forward 12-month earnings.

The table below shows summary valuation data for PZZA.

Valuation Multiples - PZZA					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	53.18	31.53	33.03	22.6
	5-Year High	56.18	34.04	34.76	22.62
	5-Year Low	18.04	20.49	19.08	15.25
	5-Year Median	28.31	23.09	23.46	17.58
P/S F12M	Current	1.73	3.72	1.23	3.65
	5-Year High	1.86	3.93	1.24	3.65
	5-Year Low	0.68	2.81	0.82	2.53
	5-Year Median	1.24	3.32	0.97	3.05
EV/EBITDA TTM	Current	24.83	22.53	19.36	12.55
	5-Year High	29.11	22.53	19.75	12.84
	5-Year Low	10.98	11.94	11.13	8.24
	5-Year Median	16.74	14.36	12.94	10.9

As of 08/12/2020

Industry Analysis Zacks Industry Rank: Top 49% (125 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Jack In The Box Inc. (JACK)	Outperform	2
BJs Restaurants, Inc. (BJRI)	Neutral	3
Dunkin Brands Group, Inc. (DNKN)	Neutral	3
DaveBusters Entertainment, Inc. (PLAY)	Neutral	4
Red Robin Gourmet Burgers, Inc. (RRGB)	Neutral	3
RESTAURANT GRP (RSTGF)	Neutral	4
Carrols Restaurant Group, Inc. (TAST)	Neutral	2
The Wendys Company (WEN)	Neutral	3

Industry Comparison Industry: Retail - Restaurants				Industry Peers		
	PZZA	X Industry	S&P 500	DNKN	RRGB	WEN
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	1	-	-	3	3	3
VGM Score	C	-	-	C	D	D
Market Cap	3.12 B	473.77 M	23.75 B	5.86 B	148.88 M	4.97 B
# of Analysts	8	4	14	11	4	14
Dividend Yield	0.95%	0.00%	1.68%	0.00%	0.00%	0.90%
Value Score	F	-	-	C	D	C
Cash/Price	0.02	0.13	0.07	0.11	0.71	0.07
EV/EBITDA	47.99	12.44	13.35	17.41	8.94	19.58
PEG Ratio	5.44	4.56	2.98	2.85	NA	4.61
Price/Book (P/B)	NA	2.07	3.20	NA	0.78	10.26
Price/Cash Flow (P/CF)	31.35	8.58	12.97	18.89	1.24	18.88
P/E (F1)	67.98	38.05	22.17	26.48	NA	41.04
Price/Sales (P/S)	1.85	0.79	2.54	4.50	0.14	2.97
Earnings Yield	1.47%	0.90%	4.31%	3.78%	-113.57%	2.43%
Debt/Equity	-1.55	1.28	0.77	-5.73	4.13	7.46
Cash Flow (\$/share)	3.04	1.81	6.94	3.77	7.72	1.18
Growth Score	A	-	-	D	F	D
Hist. EPS Growth (3-5 yrs)	-18.64%	3.47%	10.41%	11.83%	-22.89%	12.38%
Proj. EPS Growth (F1/F0)	19.77%	-66.06%	-6.32%	-15.11%	-1,854.35%	-8.35%
Curr. Cash Flow Growth	8.17%	3.07%	5.22%	5.44%	-15.30%	-0.70%
Hist. Cash Flow Growth (3-5 yrs)	-2.98%	5.23%	8.55%	5.81%	-0.74%	-1.18%
Current Ratio	0.98	0.95	1.33	1.60	0.52	1.42
Debt/Capital	NA%	70.06%	44.59%	NA	80.51%	88.18%
Net Margin	1.32%	-0.23%	10.13%	16.79%	-22.56%	6.70%
Return on Equity	-15.73%	-10.35%	14.59%	-38.22%	-52.03%	21.11%
Sales/Assets	2.30	0.87	0.51	0.34	0.92	0.33
Proj. Sales Growth (F1/F0)	11.45%	-7.96%	-1.40%	-6.61%	-29.38%	1.25%
Momentum Score	B	-	-	B	A	D
Daily Price Chg	1.62%	0.00%	0.67%	0.23%	-12.11%	0.54%
1 Week Price Chg	3.63%	3.68%	2.30%	-0.28%	10.87%	-3.62%
4 Week Price Chg	2.27%	4.22%	4.87%	5.35%	11.52%	-1.14%
12 Week Price Chg	19.55%	14.20%	13.54%	10.67%	-31.03%	8.46%
52 Week Price Chg	109.17%	-25.23%	6.06%	-12.03%	-69.41%	12.70%
20 Day Average Volume	553,233	308,737	2,006,991	925,771	1,350,014	2,983,144
(F1) EPS Est 1 week change	10.12%	0.00%	0.00%	0.00%	0.00%	-1.30%
(F1) EPS Est 4 week change	10.12%	4.41%	1.95%	4.41%	6.73%	1.75%
(F1) EPS Est 12 week change	16.45%	13.33%	2.72%	6.36%	-78.91%	5.43%
(Q1) EPS Est Mthly Chg	14.86%	10.56%	0.84%	11.42%	10.95%	-6.78%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	B
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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