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Domino's Pizza (DMP)

Pizza for everyone's taste

Recommendation
Buy (unchanged)
Price
\$83.70
Target (12 months)
\$96.50 (previously \$62.40)

GICS Sector
Hotels Restaurants and Leisure

Expected Return

Capital growth	15.3%
Dividend yield	1.7%
Total expected return	17.0%

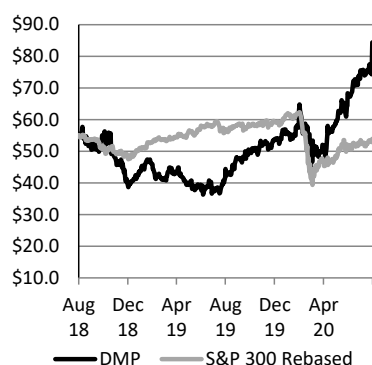
Company Data & Ratios

Enterprise value	\$8,624m
Market cap	\$7,394m
Issued capital	88.3m
Free float	100%
Avg. daily val. (52wk)	\$23.0m
12 month price range	\$40.21 - \$84.26

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	73.59	57.38	39.96
Absolute (%)	14.70	47.11	111.24
Rel market (%)	11.61	30.89	114.51

Absolute Price



Japan/Germany standouts, strong momentum entering FY21

DMP announced underlying FY20 NPAT (post-AASB16) of \$145.5m, in line vs BPe \$144.6m. Same store sales (SSS) increased +5.8% (cycling +3.6%), with online sales lifting +21.4% and accounting for 72.1% of total sales. Key result highlights include:

- **Europe resilient as a whole, Germany again the standout:** Notwithstanding COVID-19 disruption (including temporary closure of stores in France), Europe EBITDA finished flat vs pcp with SSS up +2.8% (cycling +3.1%). DMP estimate COVID-19 reduced EBITDA by ~\$18.1m (implying normalised growth of ~24%). Germany again led the region benefiting from a focus on a single brand. After an initial lull period, store openings has resumed with an expected catch-up in FY21.
- **Japan continues to outperform, with strong underlying SSS drivers:** Japan SSS lifted +18.4% (cycling +8.4%) reflecting growth in delivery & carry-out albeit materially buoyed by the pandemic in 4Q20. SSS continues to be underpinned by new customer growth & additional frequency (i.e. traffic volume rather than ticket value). This growing customer base has provided DMP foundation to increase its store network target to 1,500 (+500) by 2032. 74 stores were opened in FY20.
- **Australia also relatively resilient at a national level:** ANZ SSS were up +5.1% (cycling +2.4%) although EBITDA dipped -5.8% due to additional store support & temporary store closures relating to COVID-19. DMP est. COVID-19 reduced EBITDA by -\$14.8m (adding back would imply normalised growth of ~5% vs pcp).
- **Strong trading update:** SSS growth continues to show positive momentum in all regions. Group SSS in the first 7 weeks of 1H21 is up +11.0% (cycling +4.7%) with total network sales lifting 18.5% vs pcp. So far 24 new stores have opened.

Earnings changes & investment View: Retain Buy, PT \$96.50

We have strengthened our store opening assumptions (end-FY20 stores ahead BPe + Japan target upgraded). We have also reduced our beta assumption used in our DCF WACC to reflect significant headway being achieved in Japan and across Europe (esp. Germany). Net effect is our FY21/FY22/FY23 EPS increase by 0%/1%/7% with more material increases beyond. Including model roll-forward our PT increases to \$96.50 (previously \$62.40). We believe DMP has significant long-term growth prospects, with Europe, Japan and acquisitions the major drivers. We retain our Buy rating.

Earnings Forecast

Jun Year end	2020a	2021e	2022e	2023e
Sales (A\$m)	1,926.4	2,131.5	2,370.8	2,600.0
EBITDA (A\$m)	355.8	405.2	475.2	557.0
NPAT (reported) (A\$m)	138.5	170.1	212.5	255.9
NPAT (underlying) (A\$m)	145.5	173.6	212.5	255.9
EPS underlying (cps)	165.6	196.7	240.6	289.6
EPS underlying growth (%)	2.4%	18.7%	22.3%	20.4%
PER (on underlying EPS) (x)	50.5	42.6	34.8	28.9
EV/EBITDA (x)	24.2	21.3	18.1	15.5
Dividend (¢ps)	119.3	140.8	171.7	206.7
Yield (%)	1.4%	1.7%	2.1%	2.5%
Franking (%)	100%	87%	87%	87%
ROE (%)	38.3%	40.8%	43.4%	47.2%

Resilient result vs challenging backdrop

Headline result

DMP announced underlying FY20 EBITDA (post-AASB16) of \$355.8xm, in line vs BPe \$352.4m. Underlying FY20 NPAT (post-AASB16) was \$145.5m, in line vs BPe \$144.6m. On a pre-AASB16 basis, underlying NPAT was \$145.8m, up 3.3% on pcp.

DMP declared a final DPS of 52.6¢ps (100% franked), largely in line vs pcp.

Group FY20 same store sales (SSS) growth was +5.8% (cycling +3.6%). Regional SSS growth is as follows: ANZ +5.1% (cycling +2.4%); Europe +2.8% (cycling +5.7%); & Japan +18.4% (cycling +8.4%).

Regional FY20 EBITDA growth: ANZ down -5.8% (incl. COVID-19 impact -\$14.8m), Europe up 1.8% or down -1.5% constant currency (incl. COVID-19 impact -\$18.1m), and Japan up 42.3% or up 29.9% constant currency (incl. COVID-19 benefit of +\$24.8m).

Figure 1 below provides a summary of the result.

Figure 1 - Actual vs expected summary								
	Actuals History (FY20 and beyond is post AASB-16)					Actual FY20	Expected FY20e	Actual vs Expected
	1H19	2H19	FY19	1H20	2H20			
Total Revenue	707.2	745.6	1,452.8	917.0	1009.4	1,926.4	1,821.8	5.7%
% - Growth (pcp)	22.6%	25.0%	23.8%	29.7%	35.4%	32.6%		
EBITDA	137.2	145.2	282.4	176.7	179.1	355.8	352.4	1.0%
%-Margin	19.4%	19.5%	19.4%	19.3%	17.7%	18.5%	19.3%	-0.9%
% - Growth (pcp)	12.1%	6.1%	8.9%	28.8%	23.4%	26.0%		
Depn & Amort.	-28.9	-32.7	-61.6	-36.1	-38.1	-74.3	-71.6	3.8%
EBIT	108.3	112.5	220.8	115.7	114.7	230.3	230.3	0.0%
%-Margin	15.3%	15.1%	15.2%	12.6%	11.4%	12.0%	12.6%	-0.7%
% - Growth (pcp)	12.1%	2.9%	7.2%	6.8%	1.9%	4.3%		
Net Interest	-6.7	-7.3	-14.0	-7.3	-7.2	-14.5	-14.4	
Profit before Tax	101.6	105.2	206.8	108.4	107.5	215.8	215.9	0.0%
Tax	-31.1	-28.9	-60.0	-33.5	-30.7	-64.2	-66.2	
Associates/Minorities	-2.3	-3.3	-5.6	-2.5	-3.6	-6.1	-5.1	19.4%
Underlying NPAT	68.2	73.0	141.2	72.4	73.2	145.5	144.6	0.6%
%-Margin	9.6%	9.8%	9.7%	7.9%	7.3%	7.6%	7.9%	-0.4%
% - Growth (pcp)	8.5%	3.9%	6.0%	6.1%	0.2%	3.1%		
Abnormals post tax	-14.9	-10.4	-25.3	-3.2	-3.8	-7.0	-6.7	
Reported NPAT	53.3	62.6	115.9	69.2	69.4	138.5	137.9	0.5%
DPS (¢ps)	62.7	52.8	115.5	66.7	52.6	119.3	118.7	0.6

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

Group SSS trading update for first 7 weeks of 1H21 of +11.0% (cycling +4.7%) with +24 new stores opened. DMO noted "very strong network sales growth and store openings continued across all regions for the first 7 weeks of FY21". Total network sales in the first 7 weeks are up 18.5% vs pcp.

Company guidance and outlook commentary

As previously flagged, DMP no longer provides guidance for the one-year forecast period, but rather only on a 3-5 year forecast horizon, which was reaffirmed as follows:

- Annual same store sales growth reaffirmed: +3 - 6%;
- Annual store growth reaffirmed: +7-9%; and
- Annual net capex reaffirmed: \$60-100m.

Forecast changes

We have strengthened our store opening assumptions (end-FY20 stores ahead BPe plus Japan target upgraded). We have also reduced our beta assumption used in our DCF WACC to reflect significant headway being achieved in Japan and across Europe (esp. Germany). The net effect is our FY21/FY22/FY23 EPS increase by 0%/1%/7% with more material increases beyond. Including model roll-forward our PT increases to \$96.50 (previously \$62.40). Figure 2 summaries of our forecast changes for FY21e-FY23e.

Figure 2 – Earnings revisions summary

		FY21e			FY22e			FY23e		
		Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	\$m	2039.3	2131.5	5%	2276.1	2370.8	4%	2481.5	2600.0	5%
EBITDA	\$m	399.9	405.2	1%	468.9	475.2	1%	531.9	557.0	5%
EBITDA Margin	%	19.6%	19.0%	-1%	20.6%	20.0%	-1%	21.4%	21.4%	0%
Underlying NPAT	\$m	172.1	173.6	1%	208.2	212.5	2%	235.9	255.9	8%
Underlying EPS	¢ps	197.4	196.7	0%	238.8	240.6	1%	270.6	289.6	7%
DPS	¢ps	141	141	0%	170	172	1%	193	207	7%

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

Domino's Pizza (DMP)

Company Description

Domino's Pizza Enterprises Limited (DMP) is Domino's largest franchisee outside of the USA. It holds the Master Franchise licence to the Dominos brand and network for Australia, New Zealand, France, Belgium, the Netherlands, Germany, Japan and Luxembourg. DMP currently operates >2,000 franchised and corporate owned stores across 8 countries. The company earns revenue from a combination of sales, royalties and regular franchise fees.

Investment Strategy

DMP is a high growth business operating in the Quick Service Restaurant (QSR) industry across 8 countries. DMP earns revenue through a combination of corporate store sales, franchisee royalties and regular franchise fees. DMP has managed to grow earnings and achieve positive same store sales growth through the cycle. By CY25-28, DMP is targeting 1,200 stores in ANZ, ~1,000 stores in Japan and ~2,700 across its European operations.

Valuation

Our 12 month valuation is \$96.50 based on a DCF methodology. Major DCF assumptions are a WACC of 9.2% and a terminal growth rate of 4.0%. We believe a full DCF methodology best reflects DMP's long term growth prospects.

Risk

Key downside risks to our valuation include (but are not limited to):

- **COVID-19:** The substantial impact of COVID-19 on the global & domestic economies is creating enormous volatility and uncertainty in global share markets. The forecasts in the report may be subject to significant changes if this situation continues for an extended period of time. DMP may need to temporarily close additional stores, which would weigh on our forecasts.
- **Store rollout changes:** This may impact our revenue and earnings forecasts.
- **"Red tape" in Europe may slow the pace of new store rollouts:** There is a considerable amount of red tape associated with local government's approval of Dominos stores which require road frontage and parking for delivery. This process can take 6-9 months, which compares with the 3-4 months in Australia and New Zealand.
- **Credit availability to franchisees:** Risk of tight credit availability which may constrain the capacity of franchisees to invest in new store openings.
- **Promotions:** Revenue growth is highly reliant on successful promotions/new products.
- **Food ingredient cost pressures:** inflationary pressures on food (with cheese accounting for ~1/3 of DMP's ingredient costs) placing pressure on gross margins.
- **Brand equity deterioration:** due to poor product quality, service quality, and/or poor marketing and PR practices. This would ultimately lead to loss of market share.
- **Increased competition:** Periods of heavy discounting and increased competition can place pressure on franchisee margins and volume growth.
- **Currency:** Overall a strong AUD is negative to earnings. While a higher AUD is positive for the cost of imported products, it has an adverse translation impacts.
- **Offshore risk** – Deterioration of economic conditions in offshore markets.

Domino's Pizza

as at 19 August 2020

Recommendation

Buy

Price

\$83.70

Target (12 months)

\$96.50

Table 1 - Financial summary

Jun Year end	2018	2019	2020	2021e	2022e	2023e
Profit & Loss (A\$m)						
Sales revenue	1,173.5	1,452.8	1,926.4	2,131.5	2,370.8	2,600.0
... Change	7.5%	23.8%	32.6%	10.6%	11.2%	9.7%
EBITDA	259.3	282.4	355.8	405.2	475.2	557.0
... Change	12.3%	8.9%	26.0%	13.9%	17.3%	17.2%
Deprec. & amort.	(53.4)	(61.6)	(74.3)	(76.7)	(78.0)	(79.5)
EBIT	205.9	220.8	230.3	272.1	335.1	409.2
Net Interest	(10.3)	(14.0)	(14.5)	(15.7)	(20.5)	(29.4)
Pre-tax profit	195.6	206.8	215.8	256.4	314.6	379.8
Tax expense	(59.5)	(60.0)	(64.2)	(76.1)	(93.4)	(112.7)
... tax rate	30%	29%	30%	30%	30%	30%
Associates	-	-	-	-	-	-
Minorities/Prefs	(3.0)	(5.6)	(6.1)	(6.7)	(8.8)	(11.2)
Underlying Net Profit	133.2	141.2	145.5	173.6	212.5	255.9
... Change	12.4%	6.0%	3.1%	19.3%	22.4%	20.4%
Abs. & extras.	(11.7)	(25.3)	(7.0)	(3.5)	-	-
Reported Profit	121.5	115.9	138.5	170.1	212.5	255.9
Assumed AASB16 adjustment to Underlying EBITDA			(52.8)	(58.1)	(63.9)	(70.4)
Underlying EBITDA (Pre-AASB16)			303.0	347.0	411.3	486.6
Cashflow (A\$m)						
EBITDA	259.3	282.4	355.8	405.2	475.2	557.0
Working capital changes	15.9	14.0	76.6	(12.9)	14.9	14.6
Net Interest Expense	(5.4)	(8.0)	(9.2)	(15.7)	(20.5)	(29.4)
Tax	(33.8)	(41.6)	(59.4)	(65.4)	(83.8)	(102.6)
Other operating items	(50.6)	(70.4)	(52.5)	(46.8)	(48.6)	(48.8)
Operating Cash Flow	165.4	176.4	311.4	264.5	337.2	390.7
Capex	(54.1)	(89.2)	(95.9)	(95.9)	(94.8)	(104.0)
Free Cash Flow	131.4	87.2	215.5	168.6	242.3	286.7
Acquisitions	(112.0)	(40.0)	(25.6)	(24.2)	(26.2)	(27.8)
Disposals	21.8	7.3	13.7	13.7	13.7	13.7
Payment of leases	-	-	-	(65.0)	(71.5)	(78.7)
Dividends paid	(90.8)	(96.1)	(102.8)	(111.7)	(137.3)	(167.4)
Other investing items	(9.7)	30.5	8.9	(5.0)	-	-
Equity	(155.4)	11.7	24.7	43.1	-	-
Debt increase/(reduction)	238.0	19.9	66.3	(19.4)	(21.0)	(26.5)
Balance Sheet (A\$m)						
Cash	76.0	101.4	245.7	195.5	195.5	195.5
Receivables	78.2	93.9	146.5	158.4	175.7	192.7
Inventories & WIP	19.3	22.1	27.9	32.8	36.3	39.8
Other current assets	56.2	47.9	102.3	102.3	102.3	102.3
Current Assets	229.6	265.3	522.4	489.0	509.9	530.3
Receivables	-	-	-	-	-	-
Assoc & investments	2.8	3.1	2.2	2.2	2.2	2.2
Fixed Assets (PP&E)	200.1	253.2	272.8	278.4	281.4	292.2
Right-of-use Assets	-	-	379.0	416.6	457.7	503.7
Intangibles	794.5	843.8	879.3	903.4	929.7	957.4
Other non-curr assets	75.4	73.0	415.4	415.4	415.4	415.4
Non Current Assets	1,072.8	1,173.1	1,948.7	2,016.0	2,086.4	2,170.9
Total Assets	1,302.4	1,438.4	2,471.1	2,505.1	2,596.3	2,701.2
Short term debt	3.7	5.4	50.2	50.2	50.2	50.2
Creditors	156.0	188.6	323.6	327.6	363.3	398.3
Provisions	28.7	37.1	32.0	33.1	34.6	36.1
Other curr liabilities	12.6	15.4	129.8	140.3	151.7	164.4
Current Liabilities	201.0	246.5	535.7	551.1	599.8	649.0
LT debt (incl. leases)	594.8	646.1	1,320.3	1,250.7	1,229.7	1,203.2
Creditors	-	-	-	-	-	-
Provisions	77.0	70.1	75.5	87.3	96.9	106.2
Other non curr liabilities	121.9	129.8	146.3	146.3	146.3	146.3
Non Current Liabilities	793.7	845.9	1,542.1	1,484.3	1,472.8	1,455.6
Total Liabilities	994.7	1,092.4	2,077.7	2,035.4	2,072.6	2,104.7
Net Assets	307.7	346.0	393.4	469.7	523.7	596.6
Share Capital	192.8	206.2	235.4	278.5	278.5	278.5
Reserves	(76.4)	(57.3)	(70.0)	(70.0)	(70.0)	(70.0)
Retained Earnings	191.2	197.1	228.0	254.5	299.8	361.4
Shareholders Equity	307.7	346.0	393.4	463.0	508.2	569.9
Outside Equity Interests	-	-	-	6.7	15.5	26.7
Total Equity	307.7	346.0	393.4	469.7	523.7	596.6
Core Net debt/(cash) \$m	522.5	550.0	461.8	452.8	443.2	429.4
Net debt/(cash) [incl. leases] \$m	522.5	550.0	1,230.0	1,221.0	1,211.4	1,197.7

Price	\$83.70
Recommendation	Buy
Diluted issued capital (m)	88.3
Market cap (\$m)	7,393.5
Target Price (A\$m)	\$ 96.50

Jun Year end	2018	2019	2020	2021e	2022e	2023e
Valuation Ratios						
Underlying EPS (eps)	150.0	161.7	165.6	196.7	240.6	289.6
... % change	13.9%	7.8%	2.4%	18.7%	22.3%	20.4%
PE (on underlying EPS) (x)	55.8	51.8	50.5	42.6	34.8	28.9
EV/EBITDA (x)	33.26	30.54	24.23	21.28	18.15	15.48
EV/EBIT (x)	41.88	39.05	37.44	31.69	25.73	21.07
NTA (\$ps)	(5.58)	(5.69)	(5.52)	(4.91)	(4.60)	(4.09)
P/NTA (x)	(15.00)	(14.71)	(15.17)	(17.04)	(18.21)	(20.49)
Book Value (\$ps)	3.53	3.96	4.47	5.32	5.93	6.75
Price/Book (x)	23.73	21.16	18.74	15.74	14.12	12.39
DPS (eps)	107.8	115.5	119.3	140.8	171.7	206.7
... % pay-out	70.1%	70.0%	70.7%	71.6%	71.4%	71.3%
Yield (%)	1.3%	1.4%	1.4%	1.7%	2.1%	2.5%
Franking (%)	56%	86%	100%	87%	87%	87%
Capital Return Payouts (pps)	-	-	-	-	-	-

Performance Ratios						
Revenue growth (%)	7.5%	23.8%	32.6%	10.6%	11.2%	9.7%
EBITDA growth (%)	12.3%	8.9%	26.0%	13.9%	17.3%	17.2%
EBITDA/sales margin (%)	22.1%	19.4%	18.5%	19.0%	20.0%	21.4%
EBIT/sales margin (%)	17.5%	15.2%	12.0%	12.8%	14.1%	15.7%
Gross cash conversion (%)	86.6%	80.0%	106.8%	85.3%	92.9%	93.9%
Free cash-flow yield (%)	1.8%	1.2%	2.9%	2.3%	3.3%	3.9%
ROE (%)	37.0%	42.9%	38.3%	40.8%	43.4%	47.2%
ROIC (%)	19.0%	17.8%	11.7%	11.5%	13.7%	16.3%
Capex/Depn (x)	1.0	1.4	1.3	1.3	1.2	1.3
Net interest cover (x)	20.0	15.8	15.9	17.4	16.4	13.9
Core Net Debt/EBITDA (pre-AASB16) (x)	2.0	1.9	1.5	1.3	1.1	0.9
Net debt/equity (%)	169.8%	159.0%	312.7%	263.7%	238.4%	210.2%
Net debt/net debt + equity (%)	62.9%	61.4%	75.8%	72.5%	70.4%	67.8%

Half yearly (A\$m)	1H18	2H18	1H19	2H19	1H20	2H20
Sales revenue	576.9	596.6	707.2	745.6	917.0	1,009.4
EBITDA	122.4	136.9	137.2	145.2	176.7	179.1
Deprec. & amort.	(25.8)	(27.6)	(28.9)	(32.7)	(36.1)	(38.1)
EBIT	96.6	109.3	108.3	112.5	115.7	114.7
Interest expense	(4.1)	(6.2)	(6.7)	(7.3)	(7.3)	(7.2)
Pre-tax profit	92.5	103.2	101.6	105.2	108.4	107.5
Tax expense	(28.3)	(31.2)	(31.1)	(28.9)	(33.5)	(30.7)
... tax rate	31%	30%	31%	27%	31%	29%
Associates	-	-	-	-	-	-
Minorities	(1.3)	(1.7)	(2.3)	(3.3)	(2.5)	(3.6)
Underlying Net Profit	62.9	70.3	68.2	73.0	72.4	73.2
Abs. & extras.	(4.2)	(7.5)	(14.9)	(10.4)	(3.2)	(3.8)
Reported Profit	58.7	62.8	53.3	62.6	69.2	69.4

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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