Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
386.91 USD	370.00 USD	Medium	Wide	Stable	Exemplary	Restaurants

Value, Convenience, Safety Strategies Position Domino's for Market Share Despite Coronavirus

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The primary analyst covering this company does not own its stock.

Research as of 20 Jul 2020
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Currency amounts expressed with "$" are in U.S. dollars (USD) unless otherwise denoted.

Contents

Business Strategy and Outlook 20 Jul 2020

The global restaurant sector has come under pressure as several markets have restricted operations to curb the spread of the coronavirus. Restrictions vary by geography, but we anticipate uneven traffic in the back half of 2020. Nevertheless, we believe investors should prioritize companies with the scale to be more aggressive on pricing (value-oriented firms tend to outperform during economic shocks), give their consumers greater access through robust mobile platforms, and have healthy balance sheets (both at the corporate and franchisee level) when evaluating industry investment opportunities.

In our view, Domino's meets each of these investment criteria. We had expected Domino's to be one of the top market share gainers as the industry recovered from coronavirus-related disruptions, but its recent comp trends are well above industry averages and other delivery/to-go-focused concepts. In our view, this indicates that consumers view Domino's value, digital ordering, and safety protocols (including contactless delivery) in a more favorable light than most other restaurant operators. Coupled with the potential to accelerate its fortressing strategy (increasing store density by splitting franchisee territories), a more rational delivery pricing environment due to third-party aggregator fee caps in several markets, and new product innovations, Domino's is operating from a position of strength. As such, we believe Domino's will come close its 2025 targets of 25,000 stores worldwide (versus 17,000 in 2019) and $25 billion global retail sales ($14.2 billion).

We expect the global pizza category will become more competitive as existing players attempt to replicate Domino's strategy and as newer fast-casual players continue to expand. Additionally, delivery (70% of systemwide sales) competition will likely intensify as more cuisines become available through third-party delivery services. However, as carryout becomes an increasingly important contributor and Domino's stays ahead of the industry technology curve with autonomous delivery, GPS tracking, and in-store operational improvements, we expect Domino's to remain ahead of industry growth trends.

Vital Statistics

Market Cap (USD Mil)	15,224
52-Week High (USD)	422.15
52-Week Low (USD)	220.90
52-Week Total Return %	48.7
YTD Total Return %	32.2
Last Fiscal Year End	29 Dec 2019
5-Yr Forward Revenue CAGR %	9.8
5-Yr Forward EPS CAGR %	15.8
Price/Fair Value	1.05

Valuation Summary and Forecasts

Fiscal Year:	2018	2019	*2020(E)*	*2021(E)*
Price/Earnings	29.5	30.7	*30.4*	*30.0*
EV/EBITDA	21.7	21.8	*24.6*	*23.4*
EV/EBIT	23.7	23.9	*26.7*	*25.4*
Free Cash Flow Yield %	2.7	3.6	*3.6*	*3.3*
Dividend Yield %	0.9	0.9	*0.8*	*0.9*

Financial Summary and Forecasts (USD Mil)

Fiscal Year:	2018	2019	*2020(E)*	*2021(E)*
Revenue	3,433	3,619	*4,110*	*4,401*
Revenue YoY %	23.1	5.4	*13.6*	*7.1*
EBIT	572	629	*727*	*763*
EBIT YoY %	9.7	10.1	*15.4*	*5.0*
Net Income, Adjusted	365	401	*505*	*499*
Net Income YoY %	29.5	9.9	*26.0*	*-1.2*
Diluted EPS	8.42	9.57	*12.73*	*12.90*
Diluted EPS YoY %	42.5	13.6	*33.1*	*1.3*
Free Cash Flow	404	521	*629*	*580*
Free Cash Flow YoY %	25.9	28.9	*20.9*	*-7.9*

Historical/forecast data sources are Morningstar Estimates and may reflect adjustments.

Profile

Domino's is a leading player in the $84 billion global quick service pizza category with nearly 19% market share and 36% of delivery dollars spent. The company generates revenue through franchise royalties, company-owned stores, and sales from 27 dough-manufacturing and supply chain centers. Of the 17,200 stores in 85 markets around the world as of March 2020, 5,800 are operated by domestic franchisees, 11,000 by international franchisees, and 350 are company owned. Domino's posted $14.3 billion in systemwide retail sales in 2019.

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Fair Value & Profit Drivers 20 Jul 2020

We're raising our fair value estimate for Domino's to $370 per share from $355 after adjusting for better-than-expected near-term sales trends despite coronavirus-related operating restrictions. Our updated fair value estimate implies a 2021 price/adjusted earnings multiple of 28 times, enterprise value/adjusted EBITDA multiple of 22 times, and a free cash flow yield of 3%. These metrics are at a premium to current franchised QSR industry averages, but we believe this is warranted as Domino's exhibits a more resilient long-term growth story and meaningful potential for market share gains as the industry recovers from recent disruptions.

For 2020, we now estimate 13.6% top-line growth (including contribution from a 53rd week), backed by low-double-digit U.S. comp growth, nominal international comps growth, 1%-2% systemwide unit growth, and midteens supply chain growth. For the year, we expect adjusted income from operations as a percentage of revenue to increase 20 basis points to 17.7% as operating expense leverage largely offsets any incremental coronavirus-related expenses.

We continue to believe that Domino's U.S. outperformance will it to outperform its previous two- to three-year guidance calling for 6%-8% unit growth, 2%-5% U.S. comp growth, 1%-4% international comp growth, and global retail sales growth of 7%-10%. We've raised our 10-year average annual revenue forecast to almost 9% with restaurant operating margins expanding to the low- to mid-40s (versus 38.8% in 2019) and adjusted operating margins expanding to just north of 20.0% by 2029 (compared with 17.4% in fiscal 2019 and implying about 30 basis points of annual improvement). Our longer-term revenue growth forecast assumes 4%-5% annual comp growth (owing to improved franchisee unit economics stemming from inflationary price increases, carryout expansion efforts, and continued loyalty program marketing) and 6% unit growth as the firm continues to build store density and improve delivery speeds. By 2029, we assume there will be around 30,600 Domino's locations globally (22,000 international and 8,600 domestic), compared with 17,000 locations at the end of 2019 (10,900 international and 6,100 locations domestic).

Domino's maintains a moderately more aggressive capital structure than much of our restaurant coverage because of its franchised business model, resulting in one of the lower cost of capital assumptions (8.1%) in the industry.

Scenario Analysis

The quick-service restaurant industry is competitive, marked by minimal switching costs, volatile food, energy, and labor costs, and franchisees' dependence on the credit markets for new unit growth and remodeling activity. We've balanced the potential impact of these structural industry issues and uncertainties stemming from coronavirus-related restaurant operation restrictions with Domino's established global brand portfolio, impressive franchisee economics, and supply chain/operational enhancements to arrive at a medium uncertainty rating.

We view the pace of new restaurant openings and same-store comparable sales as the most important variables in our fair value assumptions for Domino's. Based on consumers' acceptance of the brand, current market saturation rates, franchisees' access to capital, and commercial real estate availability for quick-service pizza locations, we believe Domino's has ample opportunity to expand globally. Our model now forecasts that the company will fall just short of its previous goal of more than 25,000 global Domino's units by 2025 because of coronavirus-related capital and construction constraints. However, we believe domestic Domino's (U.S. and Canada) can add approximately 2,500 franchise locations in the U.S. over the next 10 years, suggesting close to 8,300 franchisee locations by the end of 2029. We believe the majority of unit growth will come from outside the U.S. With almost 10,900 restaurants outside the U.S., Domino's appears to be among the handful of quick-service restaurant chains with the

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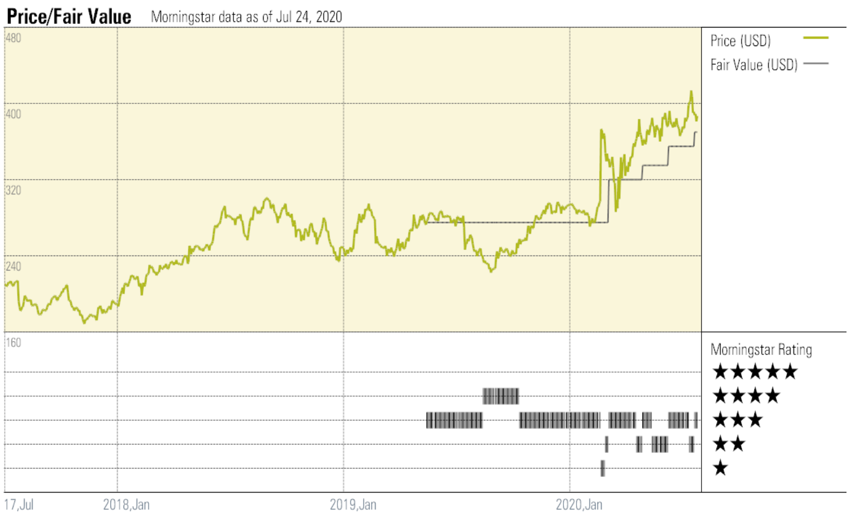

potential for mid-single-digit international unit growth over the next 10 years. We contend that using master franchise agreements to manage the international stores, Domino's is able to capitalize on local management expertise and additional capital to drive growth. By the end of 2029, our base case assumes 22,000 international locations.

In our view, fortressing (also known as splitting current franchisee territories and increasing store density) offers significant unit growth potential for Domino's and could push ultimate U.S. and international unit growth targets higher than management's current estimates. If consumer demand, commercial real estate availability, increased incremental carryout sales, and improved unit economics enable franchisees to open an average of almost 1,450 locations annually from 2021-29 (compared with 1,350 net new openings in our base-case assumptions), Domino's would be at 31,300 global locations by the end of 2029 (including 8,800 company and franchised locations in the U.S.). Assuming the company sustains unit-level productivity growth with this pace of openings, 10-year annual operating profit growth would be a few percentage points higher than our base-case assumptions (13% versus 10%) through overhead and advertising expense leverage. Under this scenario, our fair value estimate would be approximately $457 per share.

On the other hand, there are countless examples of quick-service restaurant concepts that have overextended themselves amid intense industry competition. Quick-service pizza restaurant chains are upgrading their menus, increasing promotional activity, and renovating restaurant exteriors and interiors to better compete in delivery, adding another layer of industry competition. Additionally, with third-party delivery aggregators like Uber Eats, Grubhub, DoorDash, and Postmates competing in a market share landgrab, many could continue un-economic promotions to gain scale and cause competition to intensify in the years to come. If we have overestimated consumer demand for Domino's brand or underestimated the viability of growth plans from other national pizza chains, it is possible that the Domino's brand reaches market saturation sooner than anticipated, with its unit growth trajectory slowing over the next decade. Under a more pessimistic scenario than our base-case assumptions, we would expect 29,700 global units by the end of 2029 (including nearly 8,300 U.S. locations). With a slower pace of unit expansion and 10-year average annual operating profit growth that is a few percentage points below our base-case assumptions (7% versus 10%), our fair value estimate would be approximately $288 per share.

Economic Moat

Nonexistent customer switching costs, intense industry competition, and low barriers to entry make it inherently challenging for restaurant operators to develop an economic moat. However, after revitalizing its brand and pizza offering in late 2009, we believe Domino's Pizza has established a wide moat. Our moat rating is predicated on Domino's intangible assets in the form of a well-known brand name, technology advancements that remain well ahead of peers, a franchise system aligned with driving unit-level

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productivity, and cost advantages stemming from buying scale and delivery route density. We also believe these qualities will help Domino's compete for market share ceded by smaller independents that are unable to survive extended periods of coronavirus-related restaurant regulation and uneven guest traffic trends.

Domino's Pizza's intangible assets are based on strong global brand recognition. Domino's was founded in 1960 and now extends to over 85 countries, with almost 17,200 stores. Domino's is the market share leader for the U.S. QSR pizza category (doubling its share from 9% in 2009) with Domino's, Pizza Hut, and Papa John's market shares of approximately 17%, 13%, and 7%, respectively, based on third-party market research from NDP/CREST. Domino's has a larger market share, but this is accomplished with fewer restaurants than Pizza Hut (Domino's has approximately 6,200 U.S. stores, compared with Pizza Hut's 7,200 locations). The U.S. QSR pizza category remains highly fragmented with regional chains and independents accounting for 52% of the market. Additionally, Domino's has the number 1 or 2 pizza delivery market share position in its top 15 international markets (such as the U.K., Japan, and Australia). Domino's has supported these market share positions through advertisements to drive awareness and requires franchisees to contribute a portion of sales (6% for U.S. franchisees) to fund them. Domino's spends approximately 3% of systemwide sales on advertising (accounting for domestic franchisees and company owned-stores), below the industry average of 4%. However, Domino's often uses these funds for novel and memorable advertisements such as the recent "Carryout Insurance" and "Paving for Pizza" promotions and the historic "We're Sorry for Sucking" commercial in 2009, which jump-started the brand revitalization process. Additionally, Domino's franchisees have increased sales almost entirely through order counts with minimal ticket increases from add-on item attachment rates over the past five years (approximately 85% of retail sales growth was through increased traffic). We see this as a positive, given Domino's stakes it's brand identity on customer value and this is highlighted in the lack of menu price changes over the past decade. For reference, Domino's launched its two medium pizzas with two toppings for $5.99 delivery deal in December 2009 and the offer has not changed since. Intangibles also stem from internally generated intellectual property, with Domino's being a leader in restaurant logistics and technology tools that build and maintain customer engagement and loyalty. Additional investments in streamlining its cooking and fulfilment process have fostered the brand image to make Domino's synonymous with fast and reliable service at an affordable price.

Technology plays an important role in Domino's efforts to develop and enhance its brand image. Domino's global technology platform includes a digital loyalty program with a rewards system, electronic customer profiling, geo-tracking of pizzas being delivered to customer homes, and customer geo-tracking to have carryout pizzas ready just as they enter the store. Other innovations include high-speed ovens (which reduced cooking time to four minutes) and Pulse (a unified point-of-sale system) which have re-engineered fulfillment processes to be best-in-class. Pulse integrates all orders (regardless of origin) into a seamless interface that provides detailed monitoring of every aspect of the ordering, cooking, fulfilment, and delivery processes which reduces bottlenecks and minimizes downtimes, enabling Domino's to offer faster delivery times than competitors. These technology developments have helped the firm achieve over 25 million active users on their rewards app (active defined as a customer who ordered through the loyalty program within the last six months) and in turn facilitated the shift of sales to digital platforms (more than 70% of U.S. sales and over half of global system sales were digital in fiscal 2019). We contend this channel shift to mobile/digital has

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been beneficial as it is easier to promote sides and drinks leading to larger tickets while also reducing labor needs and increasing order accuracy. Domino's remains focused on technology developments seen in the creation of the "Tech Garage" at its Ann Arbor headquarters, which consolidated Domino's R&D investments and led to the 2017 collaboration with Ford Motor Company to test delivery using self-driving vehicles, the 2018 launch of Domino's "HotSpots" which feature over 200,000 non-traditional delivery locations (parks, beaches, and landmarks), and the 2019 testing of autonomous delivery through a partnership with Nuro. While these recent innovations have not led to material economic returns, we contend these highlight the company's culture and efforts to stay ahead of the industry technology curve and could evolve into a more meaningful source of guest traffic and operational efficiency in the future.

Domino's intangible assets are also supported by a globally cohesive franchisee system. Franchisee financial health remains exceptionally strong; franchisees have strong cash-on-cash returns of just above 40% (versus an industry average for quick-service restaurants of 15% to 20%) that rank among the highest in the U.S. quick-service restaurant industry and have low franchisee bankruptcy rates. U.S. cash-on-cash payback is about two-and-a-half years (with average store costs of $300,000-$350,000), while globally it is just below three years. Additionally, while these returns are extremely attractive for outside investors, Domino's continues to implement a rigorous process to accept new franchisees. All prospective operators in the U.S. must start by working in the stores and then complete Domino's' proprietary franchise management school to understand the operating model above the store level. Additionally, Domino's enforces franchisee exclusivity, where Domino's franchisees are not allowed to participate in multi-brand franchising (unlike many other national quick-service franchisors). The advantage of this model is clear, Domino's gets highly motivated entrepreneurs who understand the business of running the stores, while also controlling the number of franchisees. At the same time, the number of franchisees continues to consolidate; in 2008 there were 1,270 franchisees (552 single store operators) and in 2017, there were 788 franchisees (278 single store operators). This consolidated profile reduces the franchisee risk as the owners are more capitalized to withstand the inherent sales volatility in the restaurant industry (average EBITDA per franchisee is north of $1 million) while also more clearly defining territorial rights among franchisees. Domino's also utilizes data-driven pricing recommendations, which are designed to help franchisees more effectively price by product category relative to the competition instead of blanket recommendations from management, helping to better manage labor cost inflation. Finally, Domino's utilizes an international master franchise model where more than half the international stores are owned by four public companies (Domino's Pizza Enterprises, Jubilant FoodWorks Ltd., Domino's Pizza Group PLC, and Alsea SAB de CV). These companies are well capitalized and have local management teams which allows them to capitalize on local experience and ownership to facilitate international growth as Domino's navigates unique cultural and culinary preferences.

Domino's boasts healthy operating margins which is partly the result of being 98% franchised. Given the brand's considerable presence throughout the United States, we believe Domino's has meaningful influence over suppliers, which helps to provide access to food and other raw materials to its franchisees at competitive prices. Using its supply chain buying arm, Domino's effectively consolidates the buying power of its franchise base to achieve competitive pricing while also passing the volatility of commodity prices to the franchisee and insulating corporate level profits. Measured by systemwide sales, Domino's was the leading player in the U.S. pizza quick-service category

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in 2019, and the number-nine player in U.S. quick-service restaurant market (behind McDonald's, Yum Brands, Subway, Starbucks, Restaurant Brands International, Wendy's, Dunkin' Donuts, and Chick-Fil-A) making it difficult to argue Domino's has more favorable bargaining clout with suppliers. However, given the fragmented nature of the pizza industry, we believe Domino's has significant purchasing power versus these peers. Relative to other pizza quick-service restaurants, this advantage is seen in Domino's superior restaurant-level margins. Over the past five years, Domino's has averaged a 24% restaurant margins while Papa John's and Pizza Hut have lagged at 19% and 6%, respectively. Additionally, we believe that franchisee buildout costs for Domino's stores remain lower than peers, but the gap is shrinking as Pizza Hut and Papa John's pivot to more delivery friendly "delco" store models. Relative to Domino's $300,000-$350,000 average opening cost, we estimate Pizza Hut averages $600,000 (while this is partly due to 42% of its stores being "dine-in") and Papa John's averages $350,000.

Combined with the ability to source inputs at a competitive price and store/delivery route density, we believe Domino's has developed a cost advantage. In 2012, Domino's implemented a fortressing corporate strategy where the firm focused on increasing store density by splitting and subdividing franchise store territories. Domino's utilizes a data-driven approach to allocate territory splits using statistics such as population density, the success of current stores in the area by sales and foot traffic, and the percentage of a new store's deliveries that would fall within one mile. Additionally, with the consolidated franchisee base, most fortressing occurs with franchisees building inside of their own territories, so cannibalization does not pit franchisees against each other (avoiding what occurred with McDonald's in the late 1990s). In a fortressed market, delivery drivers are able to double their average deliveries per hour, from two and a half to five. This increased number of deliveries is a valuable tool to attract labor in especially tight markets. The increasing trends in delivery initiated by other chains and delivery aggregator businesses has made sourcing labor highly competitive. However, Domino's strong deliveries per hour statistics have been able to continue to attract drivers at a reasonable cost as they are paid more for each delivery they complete (primarily through additional tips). The improved store density also reduced average delivery time to 22 minutes (management cited in ideal markets this drops to 17 minutes) versus Pizza Hut, reportedly sitting at around 30 minutes. We contend this proximity generates a virtuous cycle where proximity leads to better service, which leads to more orders, which incentivizes delivery drivers to work for Domino's as they will get more deliveries. Additionally, this allows Domino's to deliver for cheaper making it extremely difficult for smaller chains to compete on price. Essentially, as Domino's fully penetrates a market the marginal cost to serve a new delivery customer is far lower than a potential new entrant leading to a sustainable cost advantage.

Historical adjusted returns on invested capital (excluding goodwill) support our wide-moat rating, given the 94% average over the past 10 years, greatly outpacing our 8% cost of capital estimate. Additionally, we forecast the company's average annual adjusted ROICs will exceed its weighted average cost of capital over the next 20 years as required for our wide moat rating. We estimate Domino's Pizza's adjusted ROICs to average around 100% over the next decade.

Moat Trend

The impressive success of Domino's delivery has led to a host of substitutes, including traditional QSR pizza chains (Pizza Hut, Papa John's), fast-casual chains (Blaze, MOD Pizza, &pizza), and new delivery aggregators (Uber Eats, Grubhub, DoorDash). However, we view Domino's Pizza's moat trend as stable. We contend the firm benefits from a

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secular industry trend with consumer preferences shifting to convenience (delivery), while also making brand-accretive investments through increased store density. Taken together, we think these factors stand to ultimately support the firm’s intangible assets and cost advantages in the face of tough competitive headwinds.

Domino’s has done a commendable job implementing several global customer engagement and operational improvements aimed at improving the company's intangible asset moat source. These include using technology for capacity/throughput/delivery optimization initiatives, providing a seamless and integrated e-commerce platform across the globe, and expanding menu offerings away from their core pizza items (sandwiches, specialty chicken, salads) that utilize existing restaurant equipment and minimize undue operational complexity. While these initiatives have had a positive impact on transaction trends across the globe and should result in incremental trade-up and add-on purchases, we believe the company will continue to have limited pricing power amid industry promotional activity and new sources of competition across multiple channels.

Same-store sales trends have been impressive with 37 consecutive quarters of positive same store sales growth in the U.S. (49% of systemwide sales) and 106 consecutive quarters internationally (51% of systemwide sales) and have remained well ahead of much of the quick-service restaurant industry in the low-single-digit range much of the past five years. Despite coronavirus-related changes in consumer behavior, we expect Domino’s will continue to outpace the broader QSR pizza category over the next several years. New restaurant productivity trends (sales volume generated during a restaurant location's first year of operation) have remained healthy the past few years, but do not conclusively support the strengthening of the Domino’s brand, in our opinion. We estimate these productivity metrics will remain in line with industry peers indicating a stable trend.

Despite these positive developments, we believe the improvements to Domino's business may be offset by increased competition due to delivery aggregators and traditional restaurants and an extremely competitive labor market pressuring near-term profit. Yum Brands, Restaurant Brands International (Burger King/Tim Hortons/Popeye's), Subway, Wendy's, Chick-fil-A, and a host of fast-casual restaurant rivals all vie for market share in the intensely competitive restaurant industry (and now specifically delivery), making it more difficult for the Domino’s brand to stand out among consumers, both in terms of pricing power and driving restaurant traffic. Returns on invested capital have trended down from 112% in fiscal 2017 to 87% in 2019. However, some of this degradation is also due to increased spending as the firm executes on expanding store density, growing its supply chain, and funding technology investments, which we estimate will support the firm’s growth initiatives toward the end of our 10-year forecast. In addition, the coronavirus outbreak has the potential to have a longer lasting impact on consumer behavior regarding restaurant delivery, digital ordering, and food sourcing preferences.

If Domino’s continues to execute on its international growth plans and continues to improve store density, in-spite of the extreme competition in the food delivery space, it could indicate that its brand intangible assets and cost advantages are strengthening, and we’d consider assigning the company a positive moat trend.

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Bulls Say/Bears Say

Bulls Say

- Domino's has one of the industry's healthiest QSR franchisee systems with cash-on-cash returns around 40% for new restaurants, surpassing industry averages of 15%-20%.
- Domino's has considerable international demand, which we believe will drive store base growth and allow it to execute its fortressing store density strategy.
- Given the widespread adoption of online commerce and on-demand delivery solutions, we believe convenience will continue to be a priority for consumer purchasing decisions, which we see as a tailwind to Domino's carryout and delivery offerings.

Bears Say

- Bankruptcies among QSR franchisees could escalate during the industry COVID-19 containment and recovery period because of depressed franchisee economics or overleveraged situations following recent refranchising activity.
- Delivery aggregators could turn to aggressive promotional tactics to sustain growth and negatively impact Domino's sales trends as new restaurant options become available for delivery.
- The global QSR industry is competitive, with operators facing nonexistent switching costs, regular price wars, and constantly-evolving consumer tastes and preferences.

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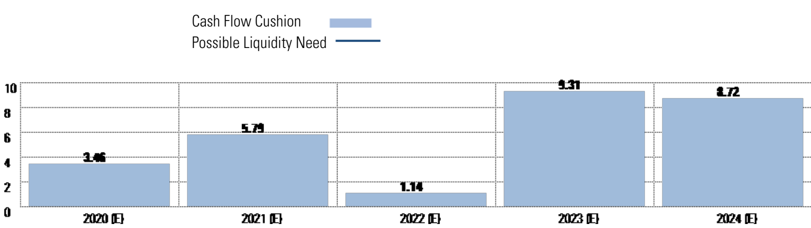
Five Year Adjusted Cash Flow Forecast (USD Mil)

	2020(E)	2021(E)	2022(E)	2023(E)	2024(E)
Cash and Equivalents (beginning of period)	191	760	677	1,380	1,235
Adjusted Available Cash Flow	527	467	543	606	673
Total Cash Available before Debt Service	717	1,227	1,219	1,987	1,908
Principal Payments	-43	-43	-898	-34	-34
Interest Payments	-164	-169	-174	-179	-185
Other Cash Obligations and Commitments	—	—	—	—	—
Total Cash Obligations and Commitments	-208	-212	-1,072	-213	-219

Cumulative Annual Cash Flow Cushion



Adjusted Cash Flow Summary

	USD Millions	% of Commitments
Beginning Cash Balance	191	9.9
Sum of 5-Year Adjusted Free Cash Flow	2,816	146.4
Sum of Cash and 5-Year Cash Generation	3,006	156.3
Revolver Availability	95	4.9
Asset Adjusted Borrowings (Repayment)	—	—
Sum of Cash, 5-Year Cash Generation, Revolver and Adjustments	3,101	161.2
Sum of 5-Year Cash Commitments	-1,924	—

Financial Strength

Domino's is in solid financial health, with roughly $4.2 billion of debt as June (including $58 million drawn from variable funding notes for additional coronavirus-related funding flexibility), representing a debt/EBITDA ratio of just over 6 times (at the high end of management's stated range of 3-6 times). We aren't overly concerned about the leverage position, given the low interest rate (effective rate of about 4% across the entire securitized debt facility) and the general health of Domino's franchisees. Franchisees put up the majority of capital for most new restaurant locations, maintenance capital expenditures for remodeling activity, and to purchase new restaurant equipment, resulting in strong free cash flow growth for Domino's Pizza (we forecast free cash flow to the firm will average almost 12% of revenue the next five years, or $590 million annually). We do not expect the company to resume share repurchase activity (the company currently has $327 million remaining under board authorization for future repurchases) until late in the year, but we expect the company to pay its full planned $3.12 dividend for 2020 and maintain low to midteens dividend per share growth over the next several years.While its capital structure is highly leveraged, we expect Domino's to satisfy its debt load through continued free cash flow growth. The firm's debt consists of seven tranches of senior secured notes with expected repayment dates spread between 2022 and 2029. The company's 2019 recapitalization package also allows for the issuance of as much as $200 million of variable-funding senior notes, which the company has tapped to provide coronavirus-related financial flexibility. Our model projects Domino's debt/EBITDA will average 5 times over our 10-year forecast as the firm will continue to utilize debt and repurchase shares as free cash flow growth expands.

Risk & Uncertainty

We've assigned Domino's a medium uncertainty rating. Restaurant chains are subject to cyclical headwinds,

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including consumer tastes, unemployment rates and commodity, labor, and occupancy cost volatility. We expect QSR chains, including Domino’s, McDonald's, Yum Brands, Papa Johns and Little Caesars, to increasingly compete on price and product differentiation while also facing competition from fast-casual chains like Blaze Pizza and MOD Pizza. On top of competitive issues, Domino's must also strike a balance between growth initiatives and unit-level profitability, which can occasionally result in friction between management and franchisees. We also expect coronavirus-related restaurant disruptions and changes in consumer behavior will have a lasting impact on the industry and drive near-term operating volatility.For a franchised restaurant business model, we view the pace of new restaurant openings as a key variable for our long-term cash flow assumptions. Based on consumer acceptance of the brand, market saturation rates, franchisee access to capital, and commercial real estate availability, we believe Domino’s has meaningful growth opportunities. In our view, a new more technological-leveraged and “delco” focused restaurant format will continue to drive unit growth expansion. However, we believe competition in the QSR and pizza categories will become more pronounced in the future due to expansion plans from existing and emerging players and delivery expansion from QSR chains. Other pizza chains, such as Pizza Hut, are emulating Domino’s playbook by optimizing their store base for delivery/carryout, while traditional QSR players are partnering with delivery aggregators (Uber Eats, Grubhub, DoorDash) to offer delivery for cuisine that traditionally has not had a delivery option. These increased delivery options--which could see wider adoption following coronavirus-related social distancing measures--may disrupt Domino’s systemwide sales growth.

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
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Management & Ownership

Management Activity

Name	Position	Shares Held	Report Date*	InsiderActivity
ANDREW B. BALSON	Director	57,723	21 Apr 2020	—
MR. RICHARD E. ALLISON, JR	Director/CEO,Director	43,098	18 Jul 2020	—
MR. RUSSELL J. WEINER	President, Geographical/COO	29,917	18 Jul 2020	—
MR. TIMOTHY P. MCINTYRE	Executive VP, Divisional	14,082	18 Jul 2020	—
MS. DIANA F. CANTOR	Director	14,030	01 Jun 2020	—
MR. THOMAS B. CURTIS	Executive VP, Geographical	11,638	18 Jul 2020	—
MR. STEVEN JAMES GODA	Chief Accounting Officer/ Treasurer/Vice President	10,718	18 Jul 2020	—
MR. RICHARD L. FEDERICO	Director	7,380	21 Apr 2020	—

*Represents the date on which the owner's name, position, and common shares held were reported by the holder or issuer.

Fund Ownership

Top Owners	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
Vanguard US Total Market Shares ETF	2.88	0.05	-13	30 Jun 2020
Vanguard Total Stock Market Index Fund	2.71	0.05	-64	30 Jun 2020
Capital Group Fundamental Invtrs Comp	2.63	0.41	—	30 Jun 2020
American Funds Fundamental Invs	2.63	0.41	—	30 Jun 2020
Vanguard Mid-Cap Index Fund	2.35	0.34	-100	30 Jun 2020
Concentrated Holders				
FT Stifel Best Picks May 2019	0.00	5.23	0	30 Jun 2020
Invesco Dynamic Leisure and Entmnt ETF	0.08	5.19	0	30 Jun 2020
FT Top Picks April 2019	0.00	4.83	0	30 Jun 2020
TimesSquare FOCUS Growth Equity	0.01	4.83	3	30 Jun 2020
Rational Dynamic Brands Fund	0.01	4.81	6	30 Jun 2020

Institutional Transactions

Top 5 Buyers	% of Shares Held	% of Fund Assets	Shares Bought/ Sold (k)	Portfolio Date
Melvin Capital Management LP	1.58	1.68	650	30 Jun 2020
Citadel Advisors Llc	1.09	0.07	412	30 Jun 2020
AllianceBernstein L.P.	2.00	0.19	362	30 Jun 2020
Rheos Capital Works Inc	0.88	12.46	349	30 Jun 2020
William Blair Investment Management, LLC	0.76	0.49	312	30 Jun 2020
Top 5 Sellers				
Lone Pine Capital LLC	—	—	-1,731	30 Jun 2020
BlackRock Fund Advisors	2.63	5.33	-1,340	30 Jun 2020
Fidelity Management & Research Company LLC	2.36	7.22	-725	30 Jun 2020
Capital World Investors	9.41	0.36	-653	30 Jun 2020
Goldman Sachs Group Inc	0.77	0.04	-526	30 Jun 2020

Stewardship 20 Jul 2020

Domino's Pizza appointed Richard Allison as CEO in July 2018, with previous CEO Patrick Doyle resigning after 20 years of work at Domino's (with eight years as CEO). Prior to becoming CEO, Allison headed the international business from October 2014 until his promotion. Allison also brings a long career of restaurant experience gained while working at Bain & Company Inc. for more than 13 years, serving as a partner from 2004 to December 2010, and as co-leader of Bain's restaurant practice. We expect that Allison will continue to execute on the company's fortressing strategy, as it has been a positive for franchise relationships, restaurant operations, channel expansion, and digital innovation efforts. Additionally, we have a favorable view of Allison's international experience and believe it will help Domino's focus on expanding international sales.

We've assigned Domino's an Exemplary equity stewardship rating predicated on its balanced approach to financial leverage and a franchise restaurant model, shareholder-friendly efforts to return cash through dividends and buybacks, and investments over the past 10 years that have enhanced the firm's brand intangible asset and cost advantage moat sources.

Operating with a capital light franchise model has allowed Domino's to optimize its capital structure, focus on returning cash to shareholders while maintaining high returns on newly invested capital. Domino's has returned over $4.3 billion to shareholders through $3.6 billion in share buybacks and $700 million in dividends since 2009 (as of fiscal 2019). We have viewed these repurchases as prudent uses of shareholder capital when completed at prices below our assessment of the firm's intrinsic value. Additionally, the firm has maintained high levels of adjusted returns on incremental invested capital averaging 111% over the past five years. We believe this highlights the firm's "moat-accretive" investments with its heavy focus on technology, delivery, and store density. These investments have paid off, as evidenced by adjusted returns on invested capital and U.S. comparable store sales growth of 86% and 6%, respectively, on average over the past 10 years. We believe the current board and management team will continue to be prudent stewards of shareholder capital as they continue to execute on corporate goals outlined until 2025.

Additionally, we believe the board has awarded fair executive compensation and has reasonable corporate governance practices. In 2019, Allison's total compensation was $5.5 million: a base salary of $865,000, stock and option awards of $2.2 million, and nonequity incentive compensation of $2.2 million. This strikes us as reasonable relative to executive compensation levels at other quick-service restaurant chains and justified by the company's recent operating performance. Incentive compensation is based on annual segment income (earnings before interest, taxes, depreciation, and amortization adjusted for one-time charges) targets, which we see as fair as it adequately represents cash flows generated by the firm, but we would prefer it to be tied to returns on invested capital. With 70% of Allison's compensation derived from equity awards, we believe he is adequately aligned with common shareholder interests.

The nine-member board consists of David Brandon (former CEO and current chairman), Allison, and seven independent directors (including two representatives with Bain Capital experience, the firm's former private equity sponsor). We have a favorable view of the annual elections used for all board members and believe they have extensive restaurant, technology, and retail experience. Directors and executive officers collectively control roughly 4% of the total shares, including former CEO Patrick Doyle's 2.6% stake.

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Analyst Notes

Shares Fairly Valued, but Don't Expect Wide-Moat Domino's to Give Up Its Momentum Anytime Soon 16 Jul 2020

With wide-moat Domino's disclosing strong intra-quarter sales (including quarter-to-date U.S. comps of 14.0%), the key question heading into its second-quarter update was whether the company could maintain its momentum as dine-in focused rivals have started to reopen. The company answered this emphatically, with U.S. second-quarter comps of 16.1% implying accelerating sales trends as the quarter progressed. We believe this acceleration underscores that consumers continue view Domino's value, digital ordering, and safety protocols (including contactless delivery options) in a more favorable light relative to other operators.

Looking ahead, Domino's is operating from a position of strength. We believe its value proposition will become even more important, in the words of CEO Ritch Allison, "when we're facing a recession and high unemployment." Domino's also appears to be prioritizing innovation more than it has in the past, including last week's revamped chicken wing platform launch and other menu additions planned for the back half of the year. These factors should keep comps well ahead of industry averages, and we plan to raise our full-year U.S. comp outlook from the high-single-digits to the low-double-digits. We also see opportunities to accelerate its fortressing strategy (increasing store density by splitting franchisee territories) due to strong franchisee health and an increase in the amount suitable real estate availability due to other retail/restaurant closures. As such, we believe Domino's can post 10% average annual revenue growth the next 10 years.

We're planning to raise our $355 fair value estimate by a mid-single-digit percentage to reflect a more optimistic revenue outlook but believe the market has effectively priced in this long-term growth. While we don't see a ton of downside catalysts as macro and industry forces make Domino's top-of-mind for consumers, we'd prefer a greater margin of safety at current levels.

One of the more notable developments coming out of second-quarter results is the Domino's $40 million non-controlling investment in its China master franchisee partner Dash Brands, and agreement to invest another $40 million in the first quarter of 2021 assuming certain performance benchmarks are satisfied. While management was quick to note that this was more opportunistic and not a signal for future deals--the company has not historically invested in its master franchisee partners--we believe management's rationale focused on helping Dash accelerate its unit and comp growth is sound. Dash recently opened its 300th location in the region and has posted a 30%-plus revenue growth CAGR the past five years. Competition in the region is increasing--Yum China operates almost 2,300 Pizza Hut locations (including 300-plus delivery locations) and Dash estimates there are another 1,200 local pizza chain locations in the region--but we believe greater usage of the technology assets underpinning our intangible asset moat source gives the company a high probability of continued growth in the region.

The other notable announcement was the retirement of CFO Jeff Lawrence, who we view as one of the top executives in the restaurant industry given his exceptional work across Domino's financial planning, operational strategies, and capital allocations. Lawrence will stay with the company through the end of the year and will assist Allison and the board in identifying and appointing a successor. Lawrence's departure won't impact our exemplary stewardship rating, and while he will difficult to replace, we believe the company has a deep internal bench and several qualified external candidates to choose from.

For 2020, we now estimate roughly midteens top-line

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growth (including contribution from a 53rd week), backed by low-double-digit U.S. comp growth, nominal international comps declines (positive comp growth excluding temporary restaurant closures), 1%-2% systemwide unit growth, and midteens supply chain growth. For the year, we expect adjusted income from operations as a percentage of revenue to increase 20 basis points to 17.6% as operating expense leverage largely offsets any incremental coronavirus-related expenses.

We continue to believe that Domino's U.S. outperformance will it to outperform its previous two- to three-year guidance calling for 6%-8% unit growth, 2%-5% U.S. comp growth, 1%-4% international comp growth, and global retail sales growth of 7%-10%. We plan to raise our 10-year average annual revenue forecast to almost 10% with restaurant operating margins expanding to the low- to mid-40s (versus 38.8% in 2019) and adjusted operating margins expanding to just north of 20.0% by 2029 (compared with 17.4% in fiscal 2019 and implying about 30 basis points of annual improvement). Our longer-term revenue growth forecast assumes 5% annual comp growth (owing to improved franchisee unit economics stemming from inflationary price increases, carryout expansion efforts, and continued loyalty program marketing) and 6% unit growth as the firm continues to build store density and improve delivery speeds. By 2029, we assume there will be around 30,600 Domino's locations globally (22,000 international and 8,600 domestic), compared with 17,000 locations at the end of 2019 (10,900 international and 6,100 locations domestic).

Domino's Impressive Quarter-to-Date Sales Also Telegraphs Industry Outperformance as 2020 Progresses
27 May 2020
In our view, the most impressive aspect of wide-moat Domino's intraquarter sales update wasn't the market share gains implied by the sharp uptick in U.S. comparable sales growth (from 7.1% the first four weeks of the second quarter to 20.9% the second four weeks, resulting in 14.0% gains quarter to date), but rather its opportunity to build on its customer engagement efforts. We had expected Domino's to be one of the top market share gainers as the industry recovers from coronavirus disruptions, but its second-quarter results (which are well above quick-service restaurant industry averages and also other delivery/to-go concepts) indicate that consumers view Domino's value, digital ordering, and safety protocols (including contactless delivery options) in a more favorable light than those of most other restaurant operators. Coupled with the potential to accelerate its fortressing strategy (increasing store density by splitting franchisee territories) due to strong franchisee health, a more rational delivery pricing environment due to third-party aggregator fee caps in several large markets, and plans to launch a new product platform this summer, Domino's is operating from a position of strength.

While we plan to increase our $335 fair value estimate by 5%-10% on increased optimism over near-term sales trends, including full-year domestic comps in the mid- to high single digits, we believe the market valuation already fully reflects these trends. Domino's near-term sales trends may soften as other restaurants experience a pent-up demand surge in early summer, potentially creating some downside pressure. However, we also expect uneven industry traffic trends in mid- to late summer due to restaurant execution issues, recessionary pressures, and a potential return of COVID-19 containment restrictions, which should again make Domino's top of mind for consumers and keep sales trends ahead of industry averages in the back half of the year.

Domino's Strong U.S. April Sales Trends Indicative of Future Market Share Gain Potential 23 Apr 2020
With Domino's already reporting first-quarter comps (+1.6% U.S., +1.5% international), our focus on its April 23 update

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Analyst Notes

shifted to April trends and how it is positioning itself for the future. Despite government assistance, we believe at least 30% of the 1 million U.S. restaurant locations are at risk of permanent closure in the next 12-18 months. The U.S. QSR pizza category is particularly threatened, with 51% of 2019 sales coming from regional chains and independents (NPD Group/CREST). This leaves wide-moat Domino's primed to take advantage.

In our view, Domino's U.S. sales for the four-week period ended April 19 were the clear highlight, with U.S. comps up 7.1% and system sales up 10.7%. Management called out industry factors--pantry depletion and stimulus checks--but we believe Domino's has also benefited from the "value/ digital/financial health" framework that we've laid out to identify post COVID-19 market share gainers. While it is unlikely to keep its current pace, we do see a path to at least mid-single-digit growth for 2020 because of a compelling value proposition, new contactless options through its digital platform, and franchisees that are on solid financial footing and can keep operations running smoothly. International sales the past four weeks (comps down 3.2%, system sales down 13.2% on a constant currency basis) have been hit harder because of temporary restaurant closures, but the financial strength of international joint-venture partners should help to mitigate distress situations.

We plan to raise our full-year U.S. comp growth outlook to the mid-single-digit range but also factor in incremental employee, safety equipment, and community investments (including $15 million in the second quarter) and international closures. Coupled with market share gains during a COVID-19 recovery period, we plan to raise our $320 fair value estimate by around 5%. Shares still strike us as overvalued, but we don't see many neat-term downside catalysts.

For 2020, we now estimate roughly 7%-8% top-line growth (including contribution from a 53rd week), backed by mid-single-digit domestic comp growth, low-single-digit international comps declines, 1% systemwide unit growth, and 8%-9% supply chain growth. For the year, we expect income from operations as a percentage of revenue to decline 140 basis points to 27.0% due to coronavirus-related expenses and international operating expense develerage.

However, we believe the factors that led to April's strong sales trends in the U.S. will allow Domino's to outperform its previous two- to three-year guidance calling for 6%-8% unit growth, 2%-5% U.S. comp growth, 1%-4% international comp growth, and global retail sales growth of 7% to 10%. Our 10-year forecast calls for 7% average annual top-line growth, restaurant operating margins expanding to the low- to mid-40s (versus 38.8% in 2019) and adjusted operating margins expanding to approximately 21.4% by 2029 (compared with 17.4% in fiscal 2019 and implying about 40 basis points of annual improvement). Our longer-term revenue growth forecast assumes 4%-5% annual comp growth (owing to improved franchisee unit economics, carryout expansion efforts, and continued loyalty program marketing) and 6% unit growth as the firm continues to build store density and improve delivery speeds. By 2029, we assume there will be around 29,400 Domino's locations globally (21,000 international and 8,100 domestic), compared with 17,000 locations at the end of 2019 (10,900 international and 6,100 locations domestic).

From a financial flexibility standpoint, Domino's remains on solid footing. The company has not repaid its variable funding notes out of an abundance of caution but has more than $325 million in available cash on top of expectations of around $450 million in free cash flow this year. We do not expect the company to resume share repurchase activity (the company currently has $327 million remaining under our board authorization for future repurchases) until late in the year, but we expect the company to pay its full $3.12

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Analyst Notes

dividend for the year.

Domino's Navigating Coronavirus-Related Disruptions but Reflected in Current Market Valuation 31 Mar 2020
Wide-moat Domino's Pizza's first-quarter sales update showed that even those restaurant companies that are well positioned to navigate coronavirus-related disruptions will see an impact to their operations. Domino's January comps (+3.6% U.S., +2.3% international) were roughly consistent with fourth-quarter results, but February (+0.3% U.S., +2.4% international) and March (+1.0% U.S., negative 0.2% international) illustrated the disruption that shelter in place, emergency preparedness shopping, and event cancellations have had on Domino's business. While we believe these headwinds will likely result in flattish global comps for the year (below management's two- to three-year guidance calling for 2%-5% U.S. comp growth), we believe Domino's still exemplifies the criteria investors should use to screen new restaurant industry investments: a compelling value proposition (value-oriented players tend to outperform during economic shocks), dynamic mobile ordering and payment platforms, and healthy balance sheets (both at the corporate and franchisee level). From a financial health perspective, Domino's announced that it has drawn down the remaining $158 million available under its variable funding notes, leaving the company with sufficient funding over the foreseeable future ($300 million in unrestricted cash on top of expectations of around $350 million in free cash flow this year).

We're planning to adjust our full-year assumptions to account for coronavirus-related disruptions, but we believe the impact will be temporary. Our 10-year forecast calling for 7% average annual top-line growth (3%-4% comp growth, 6% unit growth), restaurant operating margins expanding to the low- to mid-40s (versus 38.8% in 2019), and adjusted operating margins expanding to approximately 21.7% by 2029 (compared with 17.4% in fiscal 2019) remains largely intact. As such, our $320 fair value estimate remains unchanged, and we see shares as fairly valued.

We believe the market recognizes Domino's ability to navigate coronavirus-related disruptions over the near future, explaining the stock's relative outperformance the past month. We expect Domino's to outperform the mid- to high-single comp declines that we forecast for the broader QSR industry during 2020 and don't see many downside risks outside of a prolonged depression in the U.S. (which would impact all restaurant operators) or financial distress among its master franchisee partners (though we haven't identified any severe situations at this point). Not surprising, but Domino's management has also withdrawn previous 2020 guidance calling for $400 million-$405 million in SG&A expenses and $90 million-$100 million in capital expenditures. We plan to reduce our 2020 SG&A outlook by roughly 5%-10% and 2020 capital expenditures outlook by around 50% to account for coronavirus-related store closures and other changes in consumer behavior but expect management to provide additional commentary on its first-quarter update scheduled for April 23.

Investor Keys to Weathering COVID-19 Restaurant Closures: Value, Technology, Healthy Balance Sheets 16 Mar 2020
The restaurant sector is under pressure as several U.S. markets have restricted dine-in service in an effort to curb the spread of COVID-19. Restrictions vary by state and city, but even in markets where carry-out and drive-thru orders are still permitted, we expect severe guest count declines for at least the next two months and an uneven traffic recovery into the back half of 2020. The situation is fluid, but our best guess is that most U.S. quick-service chains will experience at least high-single-digit to low-double-digit comp declines for the year while casual-dining chains are looking at comp declines of 30% or more. While restaurants find themselves with a difficult 2020 ahead, we believe the sector's pullback offers several investment opportunities.

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What criteria should investors use to evaluate opportunities during heightened uncertainty? First, value-oriented players tend to outperform during economic shocks, positioning those players that can be more aggressive on pricing for relative transaction outperformance as the year progresses. Second, we believe those players that are further along with their mobile platforms--particularly personalized marketing efforts--should be better positioned to communicate with consumers during the social distancing and the coronavirus recovery period. Third, we'd look at companies and franchisee systems with healthy balance sheets. Because of recent refranchising activity, many operators and their franchisees are now overleveraged (many are now leveraged 6-7 times forward EBITDA), making it more difficult to navigate extended periods of restaurant restrictions.

We will be adjusting near-term estimates for our restaurant coverage list but would gravitate to names that best satisfy these three criteria, including wide-moat Domino's (limited disruption from dine-in restrictions), wide-moat McDonald's (value leader and balance sheet health), and wide-moat Starbucks (technology investments and solid licensing partners).

While many restaurants chains are adopting "to-go" models for their locations due to marketplace restrictions, several operators have told us that delivery comparable sales have seen a material drop-off in sales the past two weeks, even as restaurants and delivery aggregators have slashed or temporarily halted delivery fees. We attribute some of this disruption to consumer fears about multiple handlers during delivery transactions (which has led to a spike in online grocery transactions, according to our discussions with online retail executives). We expect restaurant delivery trends to rebound before in-store traffic recovers, but would also caution investors from automatically assuming those restaurant chains with more sophisticated delivery operations will outperform over the next several quarters (though we still believe Domino's will face less disruption on this front than many of its' peers due to its in-store operational technologies and value proposition).

We also believe extended periods of uneven spending force restaurants to become more efficient operators. We've already seen many restaurants adopt smaller, more technology-enabled restaurant formats due to softer guest counts and rising labor costs in recent years and expect the COVID-19 situation will likely accelerate this effort. We expect many restaurant operators will pull back their 2020 unit opening expectations over the next several weeks, but maintaining longer-term restaurant count targets due to these technology changes as well as market share opportunities ceded by smaller independents that are unable to survive extended periods of operating restrictions.

Domino's Poised for Big 2020 as Aggregator Disruption Wanes and Carryout and Tech Efforts Accelerate 20 Feb 2020

Domino's big finish to 2019--accentuated by fourth-quarter comps of 3.4% in the U.S. and a sequential improvement in guest counts versus the third quarter--tells us several things. First, disruption from delivery aggregators appears to be leveling-off, and we expect this trend to continue in future (CEO Ritch Allison aptly described third-party aggregators as a "circular firing squad" and we expect more rational pricing going forward as some players exit the market). Second, carryout continues to become an increasingly important contributor to revenue--order counts increased 8.1% in the U.S.--and store-level profits, which should endure into the future as new personalization technology features are rolled out. Third, Domino's remains well ahead of industry technologies such as autonomous delivery, GPS tracking, and in-store operations, each of which should drive outperformance in the years to come. Taken together, Domino's fourth-quarter update validates several pillars of

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Analyst Notes

our wide moat rating.

Looking ahead, we believe Domino's momentum will continue in 2020. Assuming a more rational delivery pricing environment, the launch of a new product platform in the summer, continued benefit from carryout, and new customer-facing, store operations, and delivery technology enhancements, we're expecting the company to come in near the high end of its two- to three-year guidance ranges (net unit growth of 6%-8%, U.S. comps of 2%-5%, international comps of 1%-4%, and global retail sales growth of 7%-10%) while posting a modest uptick in restaurant margins (versus 38.8% in 2019) and low-double-digit EPS growth in 2020 (which also assumes in $400 million-$405 million in SG&A expenses and $90 million-$100 million in capital expenditures for 2020). While the stock is now trading ahead of our $275 fair value estimate--which we plan to increase by approximately 10% due to time value of money and increased near-term optimism--we don't identify many near-term downside catalysts.

While we expect more rationale competition from third-party aggregators in 2020, we acknowledge that there are new variables that Domino's must navigate through from traditional players, including the potential bankruptcy of Pizza Hut's largest franchisee NPC international as well as a resurgent Papa John's and new delivery capabilities from Little Caesar's. Nevertheless, we believe Domino's is well positioned to compete through new technology and product news as well as the health of its franchisees. Domino's U. S. franchisees are on track to meet the high-end of management's previous outlook calling for $136,000-$139,000 in EBITDA per store in 2019 (a slight decline versus $141,000 in 2018 but still very strong when factoring third-party aggregator discounting in early 2019), which puts it in a position of strength as other chains struggle with labor cost inflation (and rent and insurance inflation to a lesser extent).

Our 10-year forecast remains largely unchanged, including 7% average annual top-line growth, restaurant margins expanding to the low-40s, and adjusted operating margins expanding to approximately 21% by 2029 (implying about 40 basis points of annual improvement). Our longer-term revenue growth forecast assumes low- to mid-single-digit comp growth (owing to improved franchisee unit volumes stemming from inflationary price increases, carryout expansion efforts, and continued loyalty program marketing) and mid-single-digit unit growth as the firm continues to build store density and improve delivery speeds. By 2029, we assume there will be around 28,000 Domino’s locations globally, with more than 20,000 international units and 8,000 domestic units.

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Morningstar Analyst Forecasts

Financial Summary and Forecasts

Fiscal Year Ends in December

Growth (% YoY)	3-Year Hist. CAGR	2017	2018	2019	Forecast 2020	Forecast 2021	5-Year Proj. CAGR
Revenue	13.5	12.8	23.1	5.4	13.6	7.1	9.8
EBIT	11.5	14.8	9.7	10.1	15.4	5.0	11.1
EBITDA	11.9	14.9	10.6	10.2	14.4	4.9	10.5
Net Income	23.2	31.6	29.5	9.9	26.0	-1.2	13.0
Diluted EPS	30.6	37.8	42.5	13.6	33.1	1.3	15.8
Earnings Before Interest, after Tax	28.1	46.1	32.7	8.5	29.9	-1.7	12.3
Free Cash Flow	22.0	12.0	25.9	28.9	20.9	-7.9	9.8

Profitability	3-Year Hist. Avg	2017	2018	2019	2020	2021	5-Year Proj. Avg
Operating Margin %	17.6	18.7	16.7	17.4	17.7	17.3	17.9
EBITDA Margin %	19.2	20.3	18.2	19.1	19.2	18.8	19.2
Net Margin %	10.6	10.1	10.6	11.1	12.3	11.3	12.1
Free Cash Flow Margin %	12.6	11.5	11.8	14.4	15.3	13.2	14.2
ROIC %	94.1	107.8	89.8	84.7	97.6	99.0	98.7
Adjusted ROIC %	97.0	111.9	92.3	86.7	100.0	101.3	100.8
Return on Assets %	37.4	35.8	41.5	35.0	29.2	23.7	23.7
Return on Equity %	-12.3	-12.0	-12.5	-12.4	-15.6	-16.8	-20.7

Leverage	3-Year Hist. Avg	2017	2018	2019	2020	2021	5-Year Proj. Avg
Debt/Capital	6.87	7.54	7.18	5.89	3.34	3.18	2.63
Total Debt/EBITDA	5.73	5.58	5.65	5.97	5.59	5.06	5.09
EBITDA/Interest Expense	4.58	4.67	4.37	4.70	4.80	4.89	5.37

Valuation Summary and Forecasts

	2018	2019	2020(E)	2021(E)
Price/Fair Value	—	1.07	—	—
Price/Earnings	29.5	30.7	30.4	30.0
EV/EBITDA	21.7	21.8	24.6	23.4
EV/EBIT	23.7	23.9	26.7	25.4
Free Cash Flow Yield %	2.7	3.6	3.6	3.3
Dividend Yield %	0.9	0.9	0.8	0.9

Key Valuation Drivers

Cost of Equity %	9.0
Pre-Tax Cost of Debt %	5.8
Weighted Average Cost of Capital %	8.2
Long-Run Tax Rate %	14.8
Stage II EBI Growth Rate %	6.9
Stage II Investment Rate %	9.1
Perpetuity Year	20

Additional estimates and scenarios available for download at http://select.morningstar.com.

Discounted Cash Flow Valuation

	USD Mil	Firm Value (%)	Per Share Value
Present Value Stage I	5,642	30.6	136.69
Present Value Stage II	5,413	29.4	131.13
Present Value Stage III	7,377	40.0	178.72
Total Firm Value	**18,432**	**100.0**	**446.55**
Cash and Equivalents	400	—	9.69
Debt	-4,114	—	-99.68
Preferred Stock	—	—	—
Other Adjustments	-87	—	-2.10
Equity Value	**14,631**	**—**	**354.46**
Projected Diluted Shares	41		
Fair Value per Share (USD)	**370.00**		

The data in the table above represent base-case forecasts in the company's reporting currency as of the beginning of the current year. Our fair value estimate may differ from the equity value per share shown above due to our time value of money adjustment and in cases where probability-weighted scenario analysis is performed.

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
386.91 USD	370.00 USD	Medium	Wide	Stable	Exemplary	Restaurants

Morningstar Analyst Forecasts

Income Statement (USD Mil)
Fiscal Year Ends in December

				Forecast	
	2017	2018	2019	*2020*	*2021*
Revenue	**2,788**	**3,433**	**3,619**	***4,110***	***4,401***
Cost of Goods Sold	1,922	2,130	2,216	*2,526*	*2,697*
Gross Profit	**866**	**1,303**	**1,402**	***1,584***	***1,704***
Selling, General & Administrative Expenses	345	372	382	*404*	*453*
Other Operating Expense (Income)	—	359	391	*454*	*487*
Other Operating Expense (Income)	—	—	—	—	—
Depreciation & Amortization (if reported separately)	—	—	—	—	—
Operating Income (ex charges)	**521**	**572**	**629**	***727***	***763***
Restructuring & Other Cash Charges	—	—	—	—	—
Impairment Charges (if reported separately)	—	—	—	—	—
Other Non-Cash (Income)/Charges	—	—	—	—	—
Operating Income (incl charges)	**521**	**572**	**629**	***727***	***763***
Interest Expense	121	143	147	*164*	*169*
Interest Income	—	—	—	—	—
Pre-Tax Income	**400**	**429**	**483**	***562***	***594***
Income Tax Expense	122	67	82	*57*	*95*
Other After-Tax Cash Gains (Losses)	—	—	—	—	—
Other After-Tax Non-Cash Gains (Losses)	—	—	—	—	—
(Minority Interest)	—	—	—	—	—
(Preferred Dividends)	—	—	—	—	—
Net Income	**278**	**362**	**401**	***505***	***499***
Weighted Average Diluted Shares Outstanding	48	43	42	*40*	*39*
Diluted Earnings Per Share	**5.83**	**8.36**	**9.56**	***12.73***	***12.90***
Adjusted Net Income	282	365	401	*505*	*499*
Diluted Earnings Per Share (Adjusted)	**5.91**	**8.42**	**9.57**	***12.73***	***12.90***
Dividends Per Common Share	1.84	2.20	2.60	*3.12*	*3.51*
EBITDA	**566**	**625**	**689**	***788***	***827***
Adjusted EBITDA	**566**	**625**	**689**	***788***	***827***

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
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Morningstar Analyst Forecasts

Balance Sheet (USD Mil)

Fiscal Year Ends in December	2017	2018	2019	Forecast 2020	Forecast 2021
Cash and Equivalents	36	25	191	*760*	*677*
Investments	192	167	209	*238*	*255*
Accounts Receivable	174	190	210	*239*	*256*
Inventory	40	46	53	*60*	*64*
Deferred Tax Assets (Current)	—	—	—	—	—
Other Short Term Assets	139	138	125	*141*	*151*
Current Assets	**580**	**567**	**788**	***1,438***	***1,403***
Net Property Plant, and Equipment	170	235	243	*231*	*267*
Goodwill	15	15	15	*15*	*15*
Other Intangibles	—	—	—	*20*	*40*
Deferred Tax Assets (Long-Term)	3	6	10	*11*	*12*
Other Long-Term Operating Assets	53	64	302	*343*	*367*
Long-Term Non-Operating Assets	16	21	25	*25*	*25*
Total Assets	**837**	**907**	**1,382**	***2,083***	***2,129***
Accounts Payable	107	93	111	*118*	*126*
Short-Term Debt	32	36	43	*218*	*43*
Deferred Tax Liabilities (Current)	—	—	—	—	—
Other Short-Term Liabilities	259	251	299	*340*	*364*
Current Liabilities	**398**	**380**	**454**	***677***	***533***
Long-Term Debt	3,121	3,496	4,071	*4,186*	*4,143*
Deferred Tax Liabilities (Long-Term)	—	—	—	—	—
Other Long-Term Operating Liabilities	31	31	237	*270*	*289*
Long-Term Non-Operating Liabilities	22	41	36	*36*	*36*
Total Liabilities	**3,572**	**3,947**	**4,798**	***5,167***	***5,000***
Preferred Stock	—	—	—	—	—
Common Stock	0	0	0	*0*	*0*
Additional Paid-in Capital	6	1	0	*0*	*0*
Retained Earnings (Deficit)	-2,739	-3,036	-3,413	*-3,031*	*-2,668*
(Treasury Stock)	—	—	—	*-50*	*-200*
Other Equity	-2	-4	-4	*-4*	*-4*
Shareholder's Equity	**-2,735**	**-3,040**	**-3,416**	***-3,084***	***-2,871***
Minority Interest	—	—	—	—	—
Total Equity	**-2,735**	**-3,040**	**-3,416**	***-3,084***	***-2,871***

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
386.91 USD	370.00 USD	Medium	Wide	Stable	Exemplary	Restaurants

Morningstar Analyst Forecasts

Cash Flow (USD Mil)

Fiscal Year Ends in December	2017	2018	2019	Forecast 2020	Forecast 2021
Net Income	278	362	401	*505*	*499*
Depreciation	44	54	60	*62*	*64*
Amortization	—	—	—	—	—
Stock-Based Compensation	21	23	20	*21*	*23*
Impairment of Goodwill	—	—	—	—	—
Impairment of Other Intangibles	—	—	—	—	—
Deferred Taxes	6	-1	-3	*-1*	*-1*
Other Non-Cash Adjustments	-20	-20	-18	—	—
(Increase) Decrease in Accounts Receivable	-23	-18	-21	*-29*	*-17*
(Increase) Decrease in Inventory	2	-12	-7	*-7*	*-4*
Change in Other Short-Term Assets	—	—	—	*3*	*10*
Increase (Decrease) in Accounts Payable	22	10	66	*7*	*8*
Change in Other Short-Term Liabilities	11	-3	-1	*41*	*24*
Cash From Operations	**341**	**394**	**497**	***602***	***606***
(Capital Expenditures)	-90	-120	-86	*-50*	*-100*
Net (Acquisitions), Asset Sales, and Disposals	7	8	9	*-40*	*-40*
Net Sales (Purchases) of Investments	—	—	50	*-28*	*-17*
Other Investing Cash Flows	-1	23	-1	*-9*	*-5*
Cash From Investing	**-84**	**-88**	**-28**	***-127***	***-162***
Common Stock Issuance (or Repurchase)	-1,058	-581	-686	*-50*	*-150*
Common Stock (Dividends)	-84	-92	-106	*-124*	*-136*
Short-Term Debt Issuance (or Retirement)	—	—	—	*175*	*-176*
Long-Term Debt Issuance (or Retirement)	972	366	583	*115*	*-43*
Other Financing Cash Flows	-27	-15	-14	*-21*	*-23*
Cash From Financing	**-197**	**-323**	**-223**	***94***	***-527***
Exchange Rates, Discontinued Ops, etc. (net)	0	1	0	—	—
Net Change in Cash	**60**	**-16**	**247**	***569***	***-83***

Domino's Pizza Inc DPZ (NYSE) | ★★★

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Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Valuation Analysis

		Price/Earnings			EV/EBITDA			Price/Free Cash Flow			Price/Book			Price/Sales		
Company/Ticker	Price/Fair Value	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	0.97	24.4	35.1	26.4	17.5	23.5	19.7	25.7	40.4	27.9	—	—	—	6.9	8.1	7.2
Starbucks Corp SBUX USA	0.88	26.7	111.4	26.5	20.7	42.4	19.0	32.3	NM	27.5	—	—	—	4.0	3.8	3.1
Chipotle Mexican Grill Inc CMG USA	1.51	59.6	173.6	68.5	35.5	79.6	39.8	59.9	129.7	62.7	—	—	—	4.2	5.5	4.7
Darden Restaurants Inc DRI USA	0.83	20.4	24.6	34.0	9.8	18.8	20.1	12.9	55.6	34.5	—	—	—	1.3	1.8	1.4
Average		32.8	86.2	38.9	20.9	41.1	24.7	32.7	75.2	38.2	—	—	—	4.1	4.8	4.1
Domino's Pizza Inc DPZ US	**1.05**	**30.7**	**30.4**	**30.0**	**21.8**	**24.6**	**23.4**	**27.8**	**27.6**	**30.1**	**—**	**—**	**—**	**3.2**	**3.7**	**3.5**

Returns Analysis

		ROIC %			Adjusted ROIC %			Return on Equity %			Return on Assets %			Dividend Yield %		
Company/Ticker	Last Historical Year Total Assets (Mil)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	47,511 USD	20.6	11.8	17.2	22.1	12.6	18.4	-87.4	-49.5	-61.7	15.7	8.8	10.8	2.4	2.5	2.8
Starbucks Corp SBUX USA	19,220 USD	17.0	8.4	26.7	23.6	12.0	38.8	-142.2	-8.4	-35.5	16.6	2.7	11.2	1.5	2.2	2.3
Chipotle Mexican Grill Inc CMG USA	5,105 USD	19.5	5.2	12.6	19.7	5.2	12.7	22.4	10.4	26.9	9.5	3.4	8.7	—	—	—
Darden Restaurants Inc DRI USA	— USD	13.4	9.7	4.9	17.1	12.0	5.8	31.1	4.2	12.8	12.6	1.3	3.1	2.6	3.4	1.3
Average		17.6	8.8	15.4	20.6	10.5	18.9	-44.0	-10.8	-14.4	13.6	4.1	8.5	2.2	2.7	2.1
Domino's Pizza Inc DPZ US	**1,382 USD**	**84.7**	**97.6**	**99.0**	**86.7**	**100.0**	**101.3**	**-12.4**	**-15.6**	**-16.8**	**35.0**	**29.2**	**23.7**	**0.9**	**0.8**	**0.9**

Growth Analysis

		Revenue Growth %			EBIT Growth %			EPS Growth %			Free Cash Flow Growth %			Dividend/Share Growth %		
Company/Ticker	Last Historical Year Revenue (Mil)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	21,389 USD	1.7	-15.0	12.5	6.2	-26.8	24.9	4.3	-30.0	33.1	17.3	-22.0	27.8	12.9	5.7	10.0
Starbucks Corp SBUX USA	26,508 USD	7.2	-11.5	20.9	2.9	-75.1	329.8	15.0	-76.8	338.0	-58.4	-127.4	-554.4	25.7	24.2	5.0
Chipotle Mexican Grill Inc CMG USA	5,586 USD	14.8	2.3	17.2	71.8	-57.5	212.8	58.2	-53.7	153.2	15.9	-46.1	109.0	—	—	—
Darden Restaurants Inc DRI USA	8,510 USD	5.3	-8.3	-4.7	10.6	-48.6	-5.7	18.5	-45.3	-26.1	18.5	-129.9	-228.9	19.1	-12.0	-62.1
Average		7.3	-8.1	11.5	22.9	-52.0	140.5	24.0	-51.5	124.6	-1.7	-81.4	-161.6	19.2	6.0	-15.7
Domino's Pizza Inc DPZ US	**3,619 USD**	**5.4**	**13.6**	**7.1**	**10.1**	**15.4**	**5.0**	**13.6**	**33.1**	**1.3**	**28.9**	**20.9**	**-7.9**	**18.2**	**20.0**	**12.5**

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
386.91 USD	370.00 USD	Medium	Wide	Stable	Exemplary	Restaurants

Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Profitability Analysis

		Gross Margin %			EBITDA Margin %			Operating Margin %			Net Margin %			Free Cash Flow Margin %		
Company/Ticker	Last Historical Year Net Income (Mil)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	6,186 USD	53.4	52.2	54.2	51.4	45.7	48.2	43.8	37.7	41.9	28.9	23.1	27.1	26.8	20.1	25.9
Starbucks Corp SBUX USA	4,081 USD	67.8	66.1	68.0	20.2	11.0	20.2	14.8	4.2	14.8	15.4	3.4	11.7	12.2	-0.3	11.4
Chipotle Mexican Grill Inc CMG USA	398 USD	20.5	16.3	21.2	12.7	7.4	12.7	8.0	3.3	8.8	7.1	3.2	6.9	6.9	4.3	7.5
Darden Restaurants Inc DRI USA	715 USD	18.7	15.0	15.1	14.0	10.2	10.0	10.0	5.6	5.6	8.4	5.0	4.1	9.8	3.3	4.0
Average		40.1	37.4	39.6	24.6	18.6	22.8	19.2	12.7	17.8	15.0	8.7	12.5	13.9	6.9	12.2
Domino's Pizza Inc DPZ US	**401** USD	**38.8**	**38.5**	**38.7**	**19.1**	**19.2**	**18.8**	**17.4**	**17.7**	**17.3**	**11.1**	**12.3**	**11.3**	**11.4**	**13.4**	**11.5**

Leverage Analysis

		Debt/Equity %			Debt/Total Cap %			EBITDA/Interest Exp.			Total Debt/EBITDA			Assets/Equity		
Company/Ticker	Last Historical Year Total Debt (Mil)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	34,177 USD	-416.3	-449.7	-465.1	131.6	128.6	127.4	9.8	6.2	7.2	3.1	4.9	4.2	-5.8	-5.5	-6.0
Starbucks Corp SBUX USA	11,167 USD	-179.2	-186.3	-161.4	226.3	215.9	262.9	16.2	5.8	12.3	2.1	6.7	2.7	-3.1	-3.1	-3.3
Chipotle Mexican Grill Inc CMG USA	— USD	—	—	—	—	—	—	—	—	—	—	—	—	3.0	3.2	3.0
Darden Restaurants Inc DRI USA	928 USD	38.8	51.4	38.7	27.9	34.0	27.9	23.7	13.9	12.4	0.8	1.5	1.3	2.5	4.3	3.9
Average		-185.6	-194.9	-195.9	128.6	126.2	139.4	16.6	8.6	10.6	2.0	4.4	2.7	-0.8	-0.3	-0.6
Domino's Pizza Inc DPZ US	**4,114** USD	**-120.5**	**-142.8**	**-145.8**	**588.9**	**333.7**	**318.4**	**4.7**	**4.8**	**4.9**	**6.0**	**5.6**	**5.1**	**-0.4**	**-0.7**	**-0.7**

Liquidity Analysis

		Cash per Share			Current Ratio			Quick Ratio			Cash/Short-Term Debt			Payout Ratio %		
Company/Ticker	Market Cap (Mil)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)	2019	2020(E)	2021(E)
McDonald's Corp MCD USA	147,760 USD	0.62	7.56	8.20	0.98	1.62	1.62	0.97	1.61	1.62	7.96	2.64	2.68	57.2	87.0	73.0
Starbucks Corp SBUX USA	88,534 USD	2.18	3.17	2.26	0.92	1.07	0.92	0.67	0.83	0.66	—	3.00	5.22	45.2	299.9	60.1
Chipotle Mexican Grill Inc CMG USA	31,607 USD	16.99	14.83	15.10	1.61	1.45	1.52	1.57	1.41	1.48	—	—	—	—	—	—
Darden Restaurants Inc DRI USA	10,209 USD	3.65	6.16	3.89	0.61	0.61	0.59	0.46	0.50	0.46	—	2.83	—	52.7	330.1	43.4
Average		5.86	7.93	7.36	1.03	1.19	1.16	0.92	1.09	1.06	7.96	2.82	3.95	51.7	239.0	58.8
Domino's Pizza Inc DPZ US	**15,224** USD	**4.55**	**19.15**	**17.49**	**1.74**	**2.13**	**2.63**	**1.62**	**2.04**	**2.51**	**4.39**	**3.48**	**15.79**	**27.2**	**24.5**	**27.2**

Research Methodology for Valuing Companies

Qualitative Equity Research Overview
At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. We believe this bottom-up, long-term, fundamentally based approach allows our analysts to focus on long-term business drivers, which have the greatest valuation impact, rather than short-term market noise.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at an uncertainty-adjusted discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk-adjusted discount to their fair values whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

1. Economic Moat
The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define excess economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

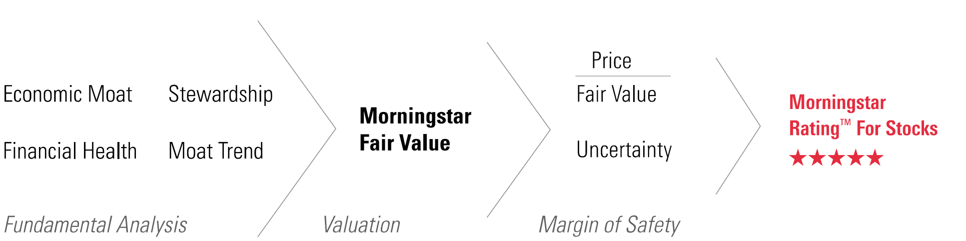
Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

To assess the direction of the underlying competitive advantages, analysts perform ongoing assessments of the moat trend. A firm's moat trend is positive in cases where we think its sources of competitive advantage are growing stronger; stable where we don't anticipate changes to competitive advantages over the next several years; or negative when we see signs of deterioration.

All the moat and moat trend ratings undergo periodic review and any changes must be approved by the Morningstar Economic Moat Committee, comprised of senior members of Morningstar's equity research department.

2. Estimated Fair Value
Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Morningstar Research Methodology for Valuing Companies



Our model is divided into three distinct stages:

Stage I: Explicit Forecast
In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working-capital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes, or EBI, and the net new investment, or NNI, to derive our annual free cash flow forecast.

Stage II: Fade
The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital, or RONIC, and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until the perpetuity stage is reached. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity
Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term market-value weights.

Research Methodology for Valuing Companies

3. Uncertainty Around That Fair Value Estimate
Morningstar's Uncertainty Rating captures a range of likely potential intrinsic values for a company and uses it to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating represents the analysts' ability to bound the estimated value of the shares in a company around the fair value estimate, based on the characteristics of the business underlying the stock, including operating and financial leverage, sales sensitivity to the overall economy, product concentration, pricing power, and other company-specific factors.

Analysts consider at least two scenarios in addition to their base case: a bull case and a bear case. Assumptions are chosen such that the analyst believes there is a 25% probability that the company will perform better than the bull case, and a 25% probability that the company will perform worse than the bear case. The distance between the bull and bear cases is an important indicator of the uncertainty underlying the fair value estimate.

Our recommended margin of safety widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the estimated value of the equity, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the uncertainty rating provides guidance in portfolio construction based on risk tolerance.

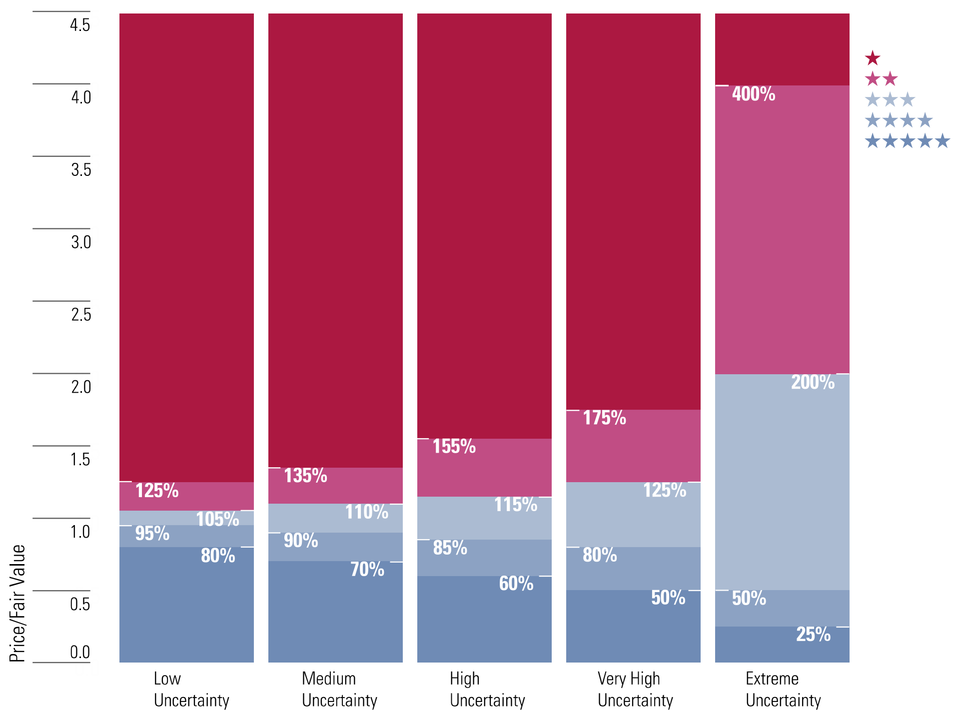
Our uncertainty ratings for our qualitative analysis are low, medium, high, very high, and extreme.

- Low–margin of safety for 5-star rating is a 20% discount and for 1-star rating is 25% premium.
- Medium–margin of safety for 5-star rating is a 30% discount and for 1-star rating is 35% premium.
- High–margin of safety for 5-star rating is a 40% discount and for 1-star rating is 55% premium.
- Very High–margin of safety for 5-star rating is a 50% discount and for 1-star rating is 75% premium.
- Extreme–margin of safety for 5-star rating is a 75% discount and for 1-star rating is 300% premium.

4. Market Price
The market prices used in this analysis and noted in the report come from exchange on which the stock is listed, which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com.

Morningstar Equity Research Star Rating Methodology



Morningstar Star Rating for Stocks
Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open.
Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time, generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk-adjusted return is highly likely over a multiyear time frame. The current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. The market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Stewardship Rating: Represents our assessment of management's stewardship of shareholder capital, with particular emphasis on capital allocation decisions. Analysts consider companies' investment strategy and valuation, financial leverage, dividend and share buyback policies, execution, compensation, related party transactions, and accounting practices. Corporate governance practices are only considered if they've had a demonstrated impact on shareholder value. Analysts assign one of three ratings: "Exemplary," "Standard," and "Poor." Analysts judge stewardship from an equity holder's perspective. Ratings are determined on an absolute basis. Most companies will receive a Standard rating, and this is the default rating in the absence of evidence that managers have made exceptionally strong or poor capital allocation decisions.

Quantitative Valuation: Using the below terms, intended to denote the relationship between the security's Last Price and Morningstar's quantitative fair value estimate for that security.

- ► Undervalued: Last Price is below Morningstar's quantitative fair value estimate.
- ► Fairly Valued: Last Price is in line with Morningstar's quantitative fair value estimate.
- ► Overvalued: Last Price is above Morningstar's quantitative fair value estimate.

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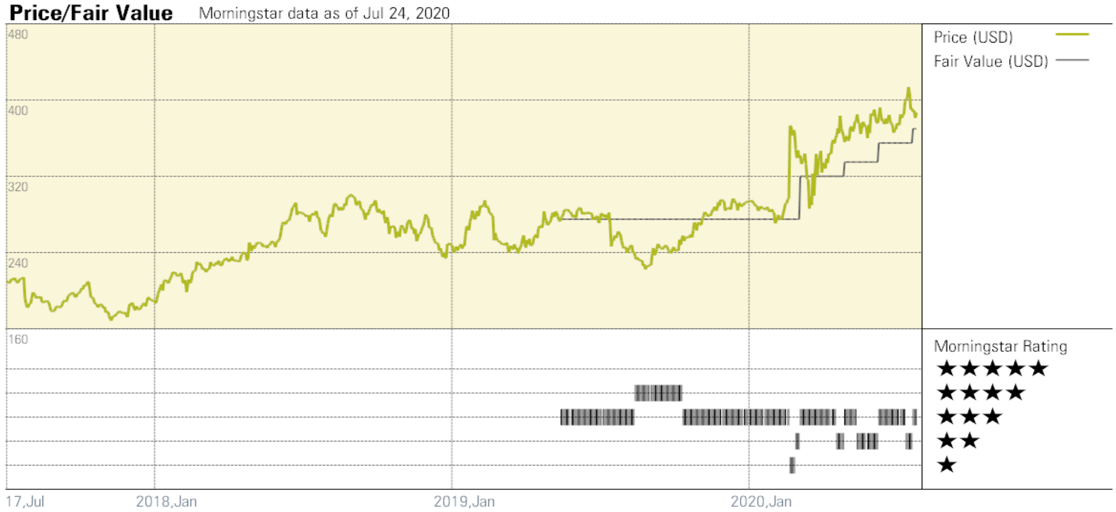
Please note that investments in securities are subject to market and other risks and there is no assurance or guarantee that the intended investment objectives will be achieved. Past performance of a security may or may not be sustained in future and is no indication of future performance. A security investment return and an investor's principal value will fluctuate so that, when redeemed, an investor's shares may be worth more or less than their original cost. A security's current investment performance may be lower or higher than the investment performance noted within the report. Morningstar's Uncertainty Rating serves as a useful data point with respect to sensitivity analysis of the assumptions used in our determining a fair value price.

Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
386.91 USD	370.00 USD	Medium	Wide	Stable	Exemplary	Restaurants

Price/Fair Value Morningstar data as of Jul 24, 2020



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Domino's Pizza Inc DPZ (NYSE) | ★★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Industry Group
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