Darden Restaurants Inc. (DRI)

Updated April 14th, 2020 by Felix Martinez

Key Metrics

Current Price:	$61	**5 Year CAGR Estimate:**	-2.5%	**Market Cap:**	$7.7 B
Fair Value Price:	$44	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	NA
% Fair Value:	138%	**5 Year Valuation Multiple Estimate:**	-6.2%	**Dividend Payment Date:**	NA
Dividend Yield:	NA	**5 Year Price Target**	$54	**Years Of Dividend Growth:**	4
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	17.3%

Overview & Current Events

Darden Restaurants Inc. is a restaurant company with a portfolio of brands including Olive Garden, LongHorn Steakhouse, Cheddar's Scratch Kitchen, Yard House, The Capital Grille, Seasons 52, Bahama Breeze, and Eddie V's. The Company employs 165,000 team members, and as of fiscal year ending May 26, 2019, it owned and operated over 1,800 restaurants in the United States and Canada and 71 franchisees operated restaurants. Darden Restaurants Inc. has a market capitalization of $7.7 billion and a 10-year dividend growth CAGR of 15.0%.

On March 19, 2020, Darden Restaurants Inc. reported 3rd quarter results for the fiscal year 2020. Total sales increased by 4.5% to $2.35 billion, driven by the addition of 40 net new restaurants and a blended same-restaurant sales increase of 2.3%. Net Earnings also increased from $223.6 million in 3Q19 to $232.3 million this quarter, a rise of 3.89%. However, Net Earnings decreased (15.4)% for the first nine months of FY2020. This was due to an increase in expense of $153.3 million. Diluted Earnings Per Share (EPS) saw the same kind of fate; EPS was $1.89 for the quarter or an increase of 5.58%. Nine-months EPS saw a decrease of (13.9)%, from $4.02 to $3.46.

The biggest news on the report is that the Board of Directors has suspended the quarterly dividend for the foreseeable future. This is due to the COVID-19 Shutdown/Social Distancing mandate issued by the government. Management will review the Company's quarterly cash dividend once the situation gets better, and the company can start opening their doors. Management is also fully drawing on its $750 million credit facility. This will give Darden $1 billion cash on hand. CFO Rick Cardenas said this about the cash, "We believe this position us well to deal with potential near term volatility under the current market conditions."

The Company is also withdrawing its full-year outlook. For the fourth quarter through Sunday, March 15, the company same-restaurant sales declined (5.9)%. Same-restaurant sales were +3.0%, (0.2)%, and (20.6)% for the first three weeks of the quarter, respectively.

Consensus has drop EPS forecast from $6.38 for FY2020 to $2.54. This is a decline of (60.2)%.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$2.86	$3.41	$3.58	$3.14	$2.47	$2.63	$3.53	$4.02	$4.81	$5.82	***$2.54***	***$3.09***
DPS	$1.00	$1.28	$1.72	$2.00	$2.20	$2.20	$2.10	$2.24	$2.52	$3.00	***$0.00***	***$0.00***
Shares[1]	142.0	140.0	133.0	131.0	133.0	129.0	129.0	126.0	126.0	125.0	***124.0***	***124.0***

Darden Restaurants, Inc. has grown operating margins for the past five years. 2014 operating margin was 5.2%, and this increased to 10.0% at the end of the fiscal year 2019. This performance was attributable to revenue growth, outpacing the growth in selling, general, and administrative expenses. As a percentage of sales, selling, general, and administrative costs were 10.6% of revenue in 2014, steadily declining to 7.8% in 2019. As a result of the COVID-19 and Social Distancing, we forecast 4.0% earnings-per-share growth annually over the next five years. This is a decrease from our last earnings growth of 7.8% from the previous quarter report.

[1] Share count is in millions

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.43	13.3	12.94	14.77	18.16	22.32	19.22	22.12	18.17	20.0	***24.3***	***17.4***
Avg. Yld.	2.5%	3.3%	4.1%	3.9%	3.8%	3.5%	2.9%	2.5%	2.8%	2.7%	***0.0%***	***0.0%***

Darden Restaurants Inc. is estimated to grow earnings by 4.0% over the next five years. This is much lower than in the past five years of earnings growth of 19.4%. Also, in the previous five years, revenue grew at 5.9% CAGR, and operating profit grew at an 18.7% CAGR.

Darden Restaurants Inc. traded at a historical 10-year average P/E of 17.4x. We believe this is a reasonable approximation of fair value moving forward. As such, we determine the fair value of Darden Restaurants Inc. to be $44 based on the new projected EPS of $2.54 for FY2020. Thus, at the current price, the company is overvalued.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2025
Payout	35%	38%	48%	64%	89%	84%	59%	56%	52%	52%	***0%***	***0%***

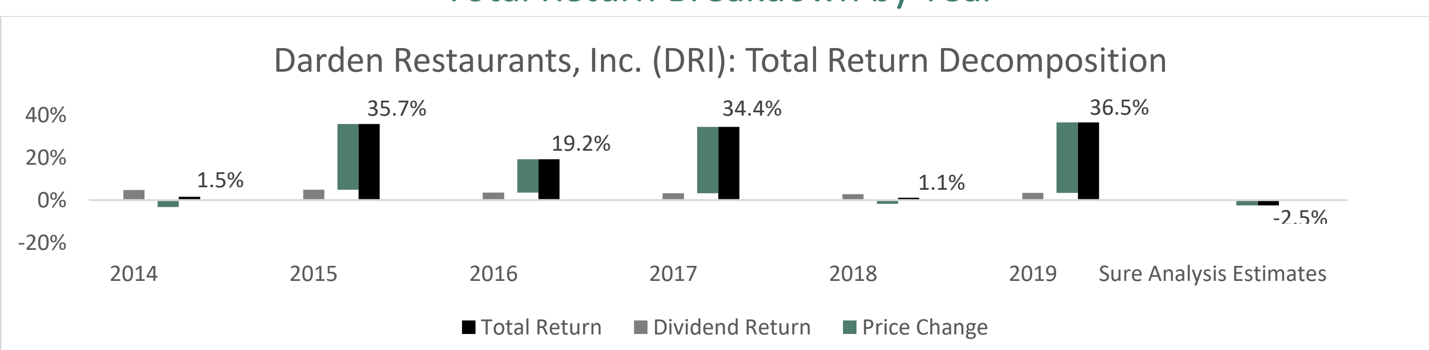
Darden Restaurants Inc. generates stable free cash flow and has demonstrated a record of being able to manage costs while improving sales. The company increased its Cash and Cash equivalents by 6.2% for 9M20 compared to 9M19. The company debt/equity ratio of 3.26 suggests a sustainable debt position.

Darden Restaurants Inc. had also managed to maintain profitability and dividends during the financial crisis. In 2009, the dividend yield was 3.1% ($0.80 per share), while earnings-per-share were $2.65, which suggests that although the business is exposed to consumption and economic cycles, Darden Restaurants Inc. was able to weather the financial crisis. However, during the COVEID-19 pandemic, the company had to suspend its dividend as almost all its locations had to resort to take-out only.

Final Thoughts & Recommendation

Darden Restaurants Inc. is a well-managed company that has introduced successful marketing and value-driven promotional campaigns to customers through a digital transformation strategy relying on data analytics and leveraging its network of more than 1,800 stores. During the pandemic, the company had to fully drawn on its $750 million credit, and it had to suspend its dividend for now. We rate the company as a Sell because of the estimated five-year total return of (2.5)%. This is because of the strong headwind of valuation multiple, and consumer confidence to start heading out to restaurants once the government lifts the Social Distance.

Total Return Breakdown by Year



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Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	4,627	4,980	5,327	5,921	6,286	6,764	6,934	7,170	8,080	8,510
Gross Profit	1,077	1,194	1,239	1,304	1,295	1,423	1,541	1,569	1,745	1,849
Gross Margin	23.3%	24.0%	23.3%	22.0%	20.6%	21.0%	22.2%	21.9%	21.6%	21.7%
SG&A Exp.	480	539	540	625	665	674	623	627	652	661
D&A Exp.	206	219	241	278	304	319	290	273	313	337
Operating Profit	275	341.1	355	274	309	368	622	678	767	833
Op. Margin	5.9%	6.8%	6.7%	4.6%	4.9%	5.4%	9.0%	9.4%	9.5%	9.8%
Net Profit	405	476	476	412	286	710	375	479	596	713
Net Margin	8.7%	9.6%	8.9%	7.0%	4.6%	10.5%	5.4%	6.7%	7.4%	8.4%
Free Cash Flow	224	194	56	84	141	578	592	623	569	807
Income Tax	52	71	76	37	(9)	(21)	90	155	2	64

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	5,276	5,467	5,944	6,937	7,101	5,995	4,583	5,292	5,470	5,893
Cash & Equivalents	249	71	71	88	98	536	275	233	147	457
Acc. Receivable	53	65	71	85	84	78	64	76	84	88
Inventories	221	300	404	357	197	164	175	179	205	207
Goodwill & Int.	971	971	1,004	1,482	1,447	1,447	1,447	2,152	2,135	2,135
Total Liabilities	3,382	3,530	4,102	4,877	4,944	3,661	2,631	3,191	3,275	3,500
Accounts Payable	246	251	261	297	233	199	242	250	277	333
Long-Term Debt	1,409	1,407	1,454	2,496	2,481	1,452	440	937	927	928
Total Equity	1,894	1,936	1,842	2,060	2,157	2,334	1,952	2,102	2,195	2,393
D/E Ratio	1.79	1.82	2.23	2.37	2.29	1.57	1.35	1.52	1.49	1.46

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	7.7%	8.7%	8.0%	5.9%	4.0%	11.8%	8.2%	9.1%	10.9%	12.1%
Return on Equity	21.4%	24.6%	25.8%	20.0%	13.3%	30.4%	19.2%	22.8%	27.2%	29.8%
ROIC	12.2%	14.2%	14.4%	9.0%	6.2%	18.7%	15.7%	15.8%	19.1%	21.5%
Shares Out.	142	140	133	132	133	130	129	126	126	125
Revenue/Share ($)	32.49	35.50	39.99	44.99	47.19	52.15	53.62	56.91	64.13	67.87
FCF/Share ($)	1.57	1.38	0.42	0.64	1.06	4.45	4.58	4.95	4.51	6.44

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise. 2019 refers to fiscal year period ending May 26, 2019.