Darden Restaurants Inc. (DRI)

Updated April 24th, 2021 by Felix Martinez

Key Metrics

Current Price:	$121	**5 Year CAGR Estimate:**	4.9%	**Market Cap:**	$18.8 B
Fair Value Price:	$118	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	7/09/2021[1]
% Fair Value:	122%	**5 Year Valuation Multiple Estimate:**	-3.9%	**Dividend Payment Date:**	8/01/2021[2]
Dividend Yield:	2.4%	**5 Year Price Target**	$173	**Years Of Dividend Growth:**	1
Dividend Risk Score:	D	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	138%

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 the fiscal year ending May 31, 2021, it owns and operates over 1,800 restaurants in the United States and Canada, and 71 franchisees served restaurants. Darden Restaurants Inc. has an $18.8 billion market capitalization and a 10-year dividend growth CAGR of 15.0% before the COVID-19 pandemic.

On March 25, 2021, Darden Restaurants Inc. reported third-quarter results for Fiscal Year (FY)2021. The Company saw total sales of $1.73 billion for the quarter, a decrease of (26.1)%, which was driven by negative same-restaurant sales. However, total sales decrease was offset by ten net new restaurants. Same-restaurant sales were down (25.8)% for Olive Garden, (12.6)% for LongHorn Steakhouse, and down (45.2)% for Fine Dining. Net earnings were down (44.6)% for the quarter when compared to 3Q20. For the nine months of FY2021, net earnings were down (39)% from $427.6 million in FY2021 to $260.8 million. The difference in net earnings year over year is the direct results of lower sales for the quarter and nine months. On a per-share basis, the Company made $0.99 per share for the quarter and $2.00 per share for the nine months, which is down (48)% and (42.7)% compared to last year, respectively. The Company saw an improvement in cash flow and increase confidence in cash flow projections. Free Cash Flow (FCF) was $568.7 million, up 3.8% year over year.

The management team announced two investments into its team members. They are first investing approximately $17 million to provide a one-time bonus for their hourly restaurant team members to recognize their hard work and dedication. They will also increase its hourly restaurant team members pay to at least $10 per hour, including tip income.

The Company also increased the quarterly dividend to $0.88 per share. This represents an increase of 138% compared to the last dividend of $0.37 per share. The Company is now paying the same dividend before the COVID-19 pandemic. Also, the board of directors authorized a new buyback program to repurchase up to $500M of its outstanding common stock. We will be using normalized earnings of $5.90 per share for FY2021 for our fair value calculation because of the COVID-19 one-time event.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$3.41	$3.58	$3.14	$2.47	$2.63	$3.53	$4.02	$4.81	$5.82	$3.13	***$5.90***	***$8.67***
DPS	$1.28	$1.72	$2.00	$2.20	$2.20	$2.10	$2.24	$2.52	$3.00	$2.64	***$1.55***	***$1.55***
Shares[3]	140.0	133.0	131.0	133.0	129.0	129.0	126.0	126.0	125.0	125.0	***131.0***	***131.0***

Darden Restaurants, Inc. has grown operating margins for the past five years. 2014 operating margin was 4.6%, which increased to 8.4% at the end of 2019. This performance was attributable to revenue growth, outpacing selling, general,

[1] Ex-Dividend Date and Payment Date are estimates

[2] Ex-Dividend Date and Payment Date are estimates

[3] Share count is in millions

and administrative expenses. However, for FY2020, the company operating margin was 5.6%. We expect an increase in earnings for FY2021 from $3.13 to $3.94 due to reopening and social distancing regulations and pent-up demand. After FY2021, we forecast 8% earnings-per-share growth annually over the next five years. This is because regulations will become more lenient, and consumers will have more confidence and demand to start eating out. However, as mentioned above, we will be using normalized earnings of $5.90 for our calculation.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	13.3	12.94	14.77	18.16	22.32	19.22	22.12	18.17	20.0	24.4	***24.2***	***20.0***
Avg. Yld.	3.3%	4.1%	3.9%	3.8%	3.5%	2.9%	2.5%	2.8%	2.7%	3.4%	***2.4%***	***1.3%***

Darden Restaurants Inc. is estimated to grow earnings by 8% over the next five years. This is much lower than in the past five years of earnings growth of 19.4%. In the previous five years, revenue grew at 5.9% CAGR, and operating profit grew at an 18.7% CAGR. Darden Restaurants Inc. has traded at a historical 10-year average P/E of 17.4x. However, we believe 20x is a reasonable approximation of fair value moving forward. As such, we determine the fair value of Darden Restaurants Inc. to be $118 based on the normalized EPS of $5.90 for FY2021. Thus, at the current price, the Company is still overvalued.

Safety, Quality, Competitive Advantage, & Recession Resiliency

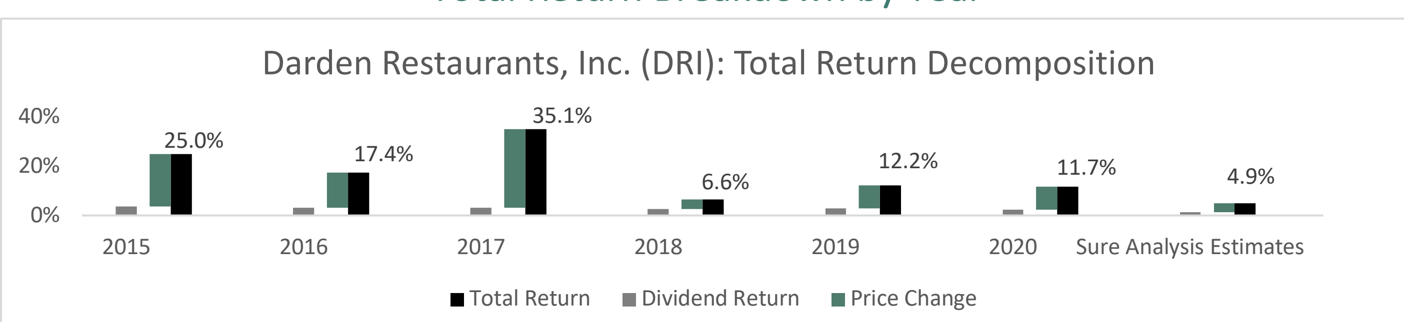
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	38%	48%	64%	89%	84%	59%	56%	52%	52%	84%	***26%***	***26%***

Darden Restaurants Inc. generates stable free cash flow and has demonstrated a record of managing costs while improving sales. Darden has $777.3 million in cash and cash equivalents, which is an increase of 1.8%, which is positive. The Company debt/equity ratio of 1.9, which is an improvement from the last report. 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 COVID-19 pandemic, The Company had suspended the dividend as 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 draw on its $750 million credit fully, and it had to suspend its dividend but has since reinstated it. We rate the company as a Hold because of the mediocre estimated five-year total return of 4.9%.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	7500	5327	5921	6286	6764	6934	7170	8080	8510	7807
Gross Profit	1801	1239	1304	1295	1423	1541	1569	1745	1849	1408
Gross Margin	24.0%	23.3%	22.0%	20.6%	21.0%	22.2%	21.9%	21.6%	21.7%	18.0%
SG&A Exp.	743	540	625	665	674	623	627	662	661	614
D&A Exp.	317	241	278	304	319	290	273	313	337	356
Operating Profit	741	457	401	325	430	628	669	770	852	438
Op. Margin	9.9%	8.6%	6.8%	5.2%	6.4%	9.1%	9.3%	9.5%	10.0%	5.6%
Net Profit	476	476	412	286	710	375	479	596	713	-52
Net Margin	6.4%	8.9%	7.0%	4.6%	10.5%	60.2%	76.4%	90.0%	108.0%	-8.5%
Free Cash Flow	345	-126	439	324	158	526	580	583	779	227
Income Tax	169	76	37	-9	-21	90	155	2	64	-112

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	5467	5944	6937	7083	5995	4583	5292	5470	5893	9946
Cash & Equivalents	71	71	88	98	536	275	233	147	457	763
Acc. Receivable	65	71	38	40	47	44	43	40	40	23
Inventories	300	404	357	197	164	175	179	205	207	207
Goodwill & Int.	1055	1089	1482	1447	1447	1447	2152	2135	2135	1843
Total Liabilities	3530	4102	4877	4926	3661	2631	3191	3275	3500	7615
Accounts Payable	251	261	297	233	199	242	250	277	333	249
Long-Term Debt	1593	2066	2661	2686	1467	440	937	927	928	1199
Total Equity	1936	1842	2060	2157	2334	1952	2102	2195	2393	2331
D/E Ratio	0.82	1.12	1.29	1.25	0.63	0.23	0.45	0.42	0.39	0.51

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	8.9%	8.3%	6.4%	4.1%	10.9%	7.1%	9.7%	11.1%	12.6%	-0.7%
Return on Equity	24.9%	25.2%	21.1%	13.6%	31.6%	17.5%	23.6%	27.7%	31.1%	-2.2%
ROIC	13.5%	12.8%	9.5%	6.0%	16.4%	12.1%	17.6%	19.4%	22.1%	-1.5%
Shares Out.	140.0	133.0	131.0	133.0	129.0	129.0	126.0	126.0	125.0	125.0
Revenue/Share ($)	53.46	39.99	44.99	47.19	52.15	53.62	56.91	64.13	67.87	63.63
FCF/Share ($)	2.46	-0.95	3.34	2.43	1.22	4.07	4.60	4.62	6.21	1.85

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.