

Weight Watchers International Inc.

NYSE: WTW

Analyst: Senan Loneragan

Sector: Consumer Disc.

Short

Price Target: \$6.20

Key Statistics as of 4/22/2016

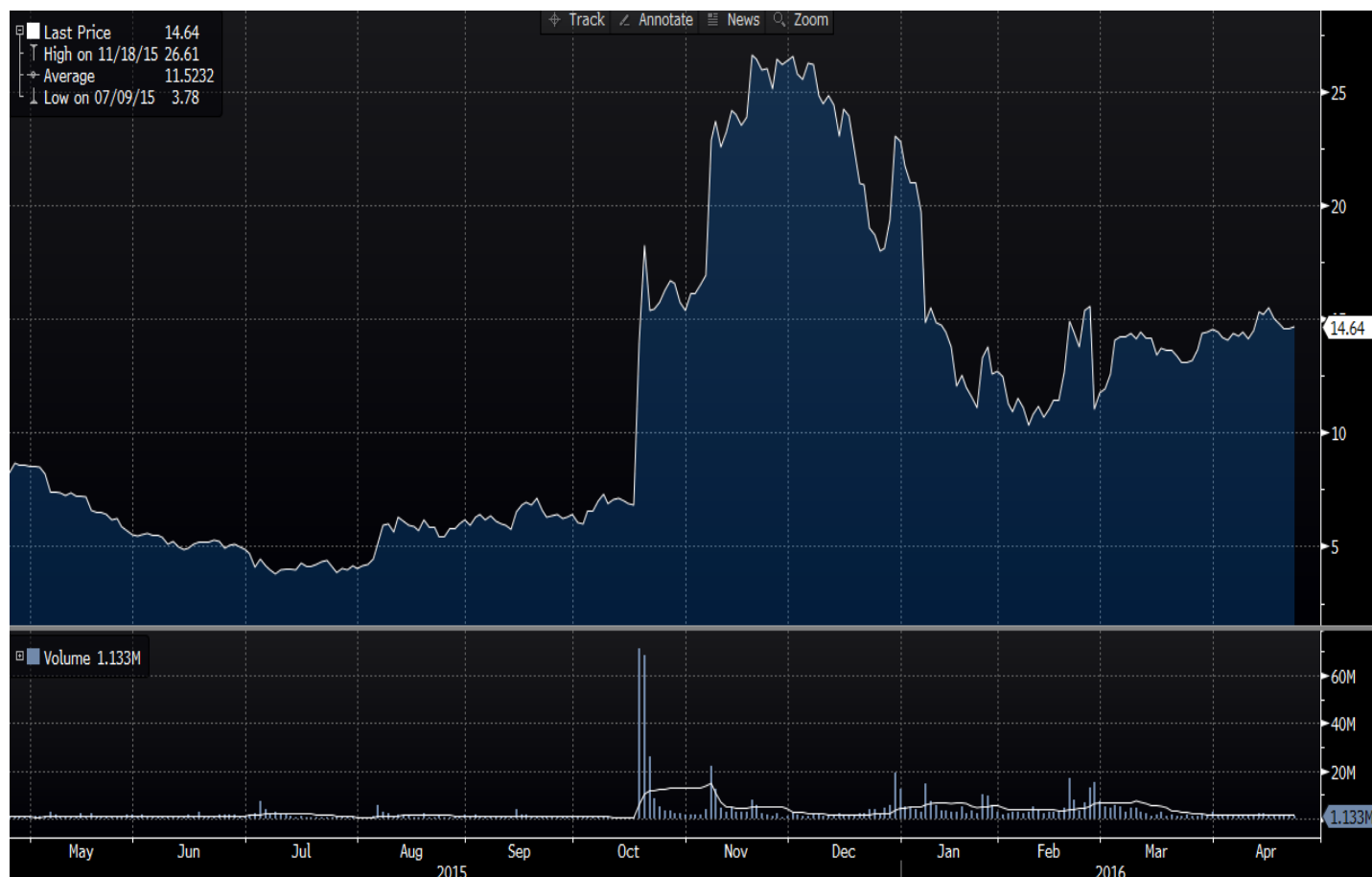
Market Price:	\$14.62
Industry:	Personal Services
Market Cap:	\$930.81M
52-Week Range:	\$3.67-28..05
Beta:	1.69

Thesis Points:

- Consistent revenue declines
- Overvalued stock as a result of Oprah Winfrey's 10% ownership
- Increased competition will continue to eat away at WTW's current market share

Company Description:

Weight Watchers International, Inc. is the world's leading commercial provider of weight management services, operating globally through a network of Company-owned and franchise operations. Weight Watchers holds more than 32,000 meetings each week where members receive group support and learn about healthy eating patterns, behavior modification and physical activity. Weight Watchers provides innovative, digital weight management products through its websites, mobile sites and apps. Weight Watchers is the leading provider of paid digital subscription weight management products in the world. In addition, Weight Watchers offers a wide range of products, publications and programs for those interested in weight loss and weight control.



Thesis

Although Weight Watchers still holds the largest market share in the weight loss services industry, WTW has consistently been declining in revenue, and will soon lose its hold as the industry's leader. The industry outlook is favorable in the sense of obesity and population metrics, however, increased competition is a serious threat. In addition to growing companies such as Nutrisystem, Medifast, and GNC, advancements in technology, such as phone applications, are making Weight Watchers less appealing. The partnership of Oprah Winfrey has driven the stock price up, but Q4 financials have indicated that she is not effecting growth, and as a result, the stock is largely overvalued.

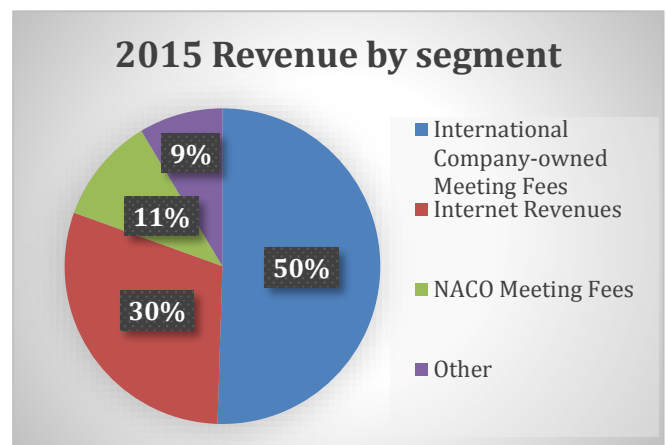
Industry Outlook

The Weight Loss Services industry has declined over the last five years, but analysts expect it to rebound in the coming five years. As more health-conscious individuals become aware of how weight loss plays an integral role in health and overall wellness, industry revenue will grow. Over the five years to 2021, industry revenue is forecast to grow at an annualized rate of 2.6% to \$2.6 billion. However, with this demand for health and fitness products and services comes increased competition. The Weight Loss Services industry is already saturated with companies such as Weight Watchers, Medifast, Nutrisystem, and many others, and the low barriers to entry in this industry will allow competition to continue increasing. Furthermore, advancements in technology, such as calorie-counting applications available on smart phones, poses as serious competition to WTW.

Business Model

Weight Watchers has several services and products that it offers to members, including weight management plans, meetings, nutritional products, a weightwatchers.com subscription and mobile services. Its weight management plans are offered through the company's PointsPlus and ProPoints plans. The PointsPlus system assigns specific point values to food, based on its protein, carbohydrate, and fat and dietary fiber content. Under the PointsPlus program, consumers are taught various techniques on how to lose weight by eating foods that are healthier and more satisfying. The ProPoints program was launched in Europe at the end

of 2009 and, at the end of 2010, the company introduced the PointsPlus program in the United States and Canada. Additionally, Weight Watchers offers weekly meetings so that members can support one another and discuss experiences with weight-management challenges. In 2015, the company acquired Weilos, a California-based company that developed a mobile platform for health and weight loss. The company also sells a range of products, including protein bars, snacks and cookbooks, as well as food and restaurant guides. Weight Watchers additionally has two internet subscription offerings, Weight Watchers Online and Weight Watchers eTools. Weight Watchers Online provides personalized resources so clients can follow weight-management plans via the internet. The following graph breaks down their revenue by segment, which has remained fairly consistent over the last few years. It is also important to note that Product Sales and Royalties were discontinued in 2013.



Financials

When compared to its publicly traded competitors, Nutrisystem (NTRI), GNC Holdings (GNC), and Medifast (MED), Weight Watchers Inc. poses as a short sell position. WTW's WAAC has remained relatively stable, and similar to its competitors, but its return on invested capital is now inferior, and has significantly declined over recent years. When breaking down the cost structure and margins of these companies, it is clear that the severe revenue declines has driven the devaluation of WTW. Historically, Weight Watchers has recorded 6.36 ROIC/WAAC, but has declined to 1.99 last fiscal year. Its competitors, on the other hand, have improved from 2.09 to 2.46 over the same time period. Revenue for WTW had declined each of the last three years, with -6.27% in 2013, -14.16% in 2014, and -

21.32% in 2015. Moreover, greater declines in operation income growth have occurred, with -9.8% in 2013, -35.04% in 2014, and -43.85% in 2015. While operating margins have improved as of late, it is crucial for companies in this space to continue growth in new customers, as well as customer retention, so that it can retain its brand recognition. The overarching factors attributing to this substantial decline with both growth and profitability is largely due to the increased competition previously discussed, but also an overall decrease in demand for Weight Watchers specifically. Other services have become more attractive, and cost effective, for consumers, and WTW is now losing loyal customers. Lastly, the discontinuation of its product segment has now limited Weight Watchers to strictly a services oriented company. The business model revolves around internet revenue, and meeting fees, while pre-aid meals are no longer distributed to members. The company has lost the little proprietary value that it once had, and is now a company that simply advises customers through meetings, forums, and other methods of marketing and media. This lack of innovation has discouraged customers and has allowed them to explore other weight loss methods.

Oprah Winfrey Q4 2015 Earnings

In an effort to revamp growth, WTW has partnered with famous icon, Oprah Winfrey. Oprah invested \$43 million for a 10% stake last October at \$6.79 per share, which included a seat on the board. The excitement of Oprah's ownership allowed the stock value to peak last November at \$28.05 per share. Oprah's investment involves active involvement in pitching Weight Watchers television ads, but Q4 earnings has demonstrated that the impact of Oprah's brand may not be as valuable as management perceived it would be. Weight Watchers' sales fell to \$259.2 million in the fourth quarter ended Jan. 2, from \$327.8 million in Q4 a year earlier. Additionally, active subscriber numbers, a key metric used by the company, fell 4.8 percent to 2.39 million and WTW recorded a net loss of \$11.3 million, or 18 cents per share, compared with net income of \$4.4 million, or 8 cents per share, seen in the prior year. The quarter four earnings report has brought the stock price back down to a more realistic value currently at \$14.62. However, the nearly 27% short interest, with 11.2 average days to cover, expresses investors pessimistic outlook for 2016.

Q1 2016 Earnings

Investors and management have made the argument that Oprah's effect on revenue growth has not been realized fully, as she partnered with WTW mid-way through Q4. WTW's Q1 report will be released on May 5th, and what all analysts will be excited to see is whether or not revenue expectations have been met, if Oprah's contribution to the company will be seen in the top line, and whether or not 2016 will be staged for a growth year for 2016. Q1 earnings are especially important for health, fitness, and weight management companies, as many consumer demand increases when headed to the warmer spring and summer months. Analysts estimate that revenue will decrease YOY from 322.1M to 309M, another decline of 4.1%. While there is the possibility of an earnings beat, in which Oprah's contribution to Weight Watchers improves revenue, I believe that downside far exceeds the upside.

Conclusion

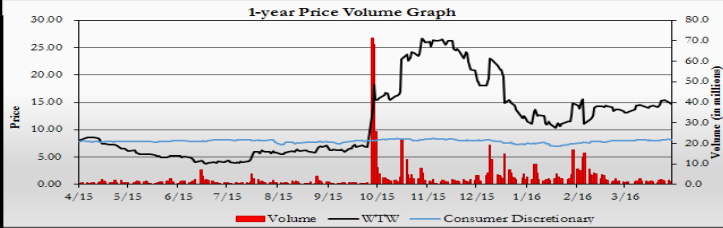
Using the analysts low estimates, and taking an optimistic approach in terms of revenue growth, WTW is still overvalued. Prior to the addition of Oprah Winfrey, WTW was fairly valued at around \$7 a share. Currently, the stock trades at \$14.62 with little justification to this 100% increase. Q4 earnings have indicated that the value to be added by Oprah Winfrey's advertisements was largely overstated. The proforma attached values WTW at \$6.20 a share, and a short sell position is my recommendation. While the downside to a short position is that Oprah's contribution will be recognized in the Q1 earnings report, many other analysts and I believe that the Oprah effect should have been seen last quarter. Ultimately, the upside of short selling Weight Watchers far exceeds the downside.

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Weight Watchers
International, Inc. (WTW)
Analysis by Senan Lonergan
4/22/2016

BEARISH

Current Price: \$14.65 **Intrinsic Value:** \$6.20
Dividend Yield: 0.0% **Target Price:** \$8.66
Target 1 year Return: -40.89%
Probability of Price Increase: 2.5%



Description		Market Data	
Weight Watchers International, Inc. provides weight management services worldwide.		Market Capitalization	\$929.90
		Daily volume (mil)	1.10
		Shares outstanding (mil)	63.65
		Diluted shares outstanding (mil)	58.97
		% shares held by institutions	78%
		% shares held by investments Managers	26%
		% shares held by hedge funds	14%
		% shares held by insiders	10.93%
		Short interest	29.74%
		Days to cover short interest	5.27
		52 week high	\$28.05
		52-week low	\$3.67
		Levered Beta	1.69
		Volatility	78.75%

Past Earning Surprises		Peers	
Quarter ending	Revenue	EBITDA	
1/3/2015	-6.34%	9.72%	Elizabeth Arden, Inc.
4/4/2015	-2.39%	14.36%	Dunkin' Brands Group, Inc.
7/4/2015	-2.72%	0.68%	Nutrisystem, Inc.
10/3/2015	1.91%	1.60%	The Estée Lauder Companies Inc.
1/2/2016	0.48%	-7.04%	Dominio's Pizza, Inc.
Mean	-1.81%	3.86%	GNC Holdings Inc.
Standard error	1.4%	3.7%	Nautilus Inc.
			Nature's Sunshine Products Inc.

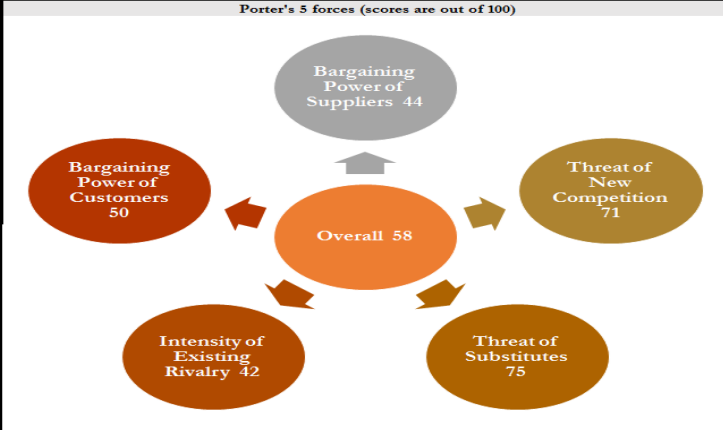
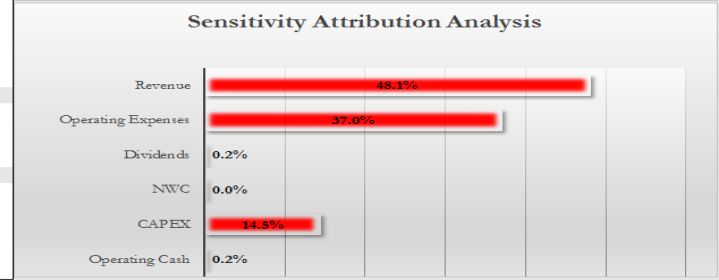
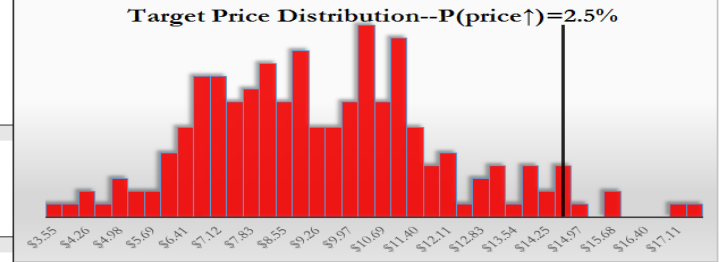
Management		Position	
Chambers, James	Chief Executive Officer, Pre		
Hochkin, Nicholas	Chief Financial Officer		
Colosi, Michael	General Counsel and Secretar		
Pellier-Bousquet, Corinne	President of International		
Kossov, Amy	Senior Vice President of Cor		
Crowe, Byron	Chief Technology Officer		

Profitability		WTW (5 years historical average)		Industry (LTM)	
ROIC	5.6%	35.30%	23.71%		
NOPAT Margin	9%	27.53%	17.7%		
Revenue/Invested Capital	0.61	1.28	1.34		
ROE	8.7%	56.26%	33.19%		
Adjusted net margin	1%	23.13%	14.7%		
Revenue/Adjusted Book Value	14.42	2.43	2.26		

Invested Funds		WTW (5 years historical average)		Industry (LTM)	
Total Cash/Total Capital	12.6%	9.5%	9%		
Estimated Operating Cash/Total Capital	6.7%	6.8%	N/A		
Non-cash working Capital/Total Capital	-6.7%	-9.6%	21%		
Invested Capital/Total Capital	94.3%	97.4%	91%		

Capital Structure		WTW (5 years historical average)		Industry (LTM)	
Total Debt/Common Equity (LTM)	1.77	1.23	0.48		
Cost of Existing Debt	5.14%	5.03%	5.56%		
Estimated Cost of new Borrowing	15.29%	12.99%	5.56%		
CGFS Risk Rating	F	D	CC		
Unlevered Beta (LTM)	0.65	0.76	0.57		
WACC	6.42%	7.25%	6.46%		

General Information	
Sector	Consumer Discretionary
Industry	Diversified Consumer Services
Last Guidance	November 3, 2015
Next earnings date	May 4, 2016
Estimated Country Risk Premium	4.92%
Effective Tax rate	28%
Effective Operating Tax rate	37%



Period	Revenue growth	Valuation	ROIC/WACC
Base Year	-21.3%	NOPAT margin	0.86
1/2/2017	1.9%	9.1%	1.05
1/2/2018	2.7%	11.4%	1.70
1/2/2019	0.5%	15.7%	1.56
1/2/2020	0.7%	15.6%	1.53
1/2/2021	0.9%	15.1%	1.51
1/2/2022	1.1%	14.8%	1.50
1/2/2023	1.3%	14.5%	1.49
1/2/2024	1.5%	14.2%	1.48
1/2/2025	1.7%	13.9%	1.46
1/2/2026	1.9%	13.6%	1.45
Continuing Period	2.1%	13.3%	1.45

Period	Invested Capital	Net Claims	Price per share
Base Year	\$1,251.66	\$2,526.12	\$6.02
1/2/2017	\$1,422.82	\$2,371.91	\$8.22
1/2/2018	\$1,609.63	\$2,363.76	\$10.40
1/2/2019	\$1,867.00	\$2,244.01	\$12.61
1/2/2020	\$1,904.12	\$2,082.77	\$15.49
1/2/2021	\$1,813.04	\$1,975.83	\$17.54
1/2/2022	\$1,719.12	\$1,874.60	\$19.57
1/2/2023	\$1,844.17	\$1,778.92	\$21.61
1/2/2024	\$1,848.26	\$1,688.69	\$23.64
1/2/2025	\$1,845.98	\$1,603.81	\$25.67
1/2/2026	\$1,846.42	\$1,524.22	\$27.71
Continuing Period			