

BJ'S Restaurants, Inc.

NASDAQ:BJRI

Analyst: Justin Capuano

Sector: Consumer Disc.

BUY

Price Target: \$43

Key Statistics as of 11/4/2016

Market Price:	\$35.55
Industry:	Leisure/Restaurants
Market Cap:	\$875.09M
52-Week Range:	\$32.24-\$47.55
Beta:	1.03
Current P/E:	19.46x
High (2015)	49.64x
Low (2015)	25.89x
D/E:	35.42%

Catalysts:

- SAME STORE SALES
- Materialization of organic growth plans
- Consumer spending reports

Company Description:

Founded in 1978 in Huntington Beach, California, BJ's Restaurants, Inc. (BJ's) owns and operates 182 casual dining restaurants in 24 states around the United States. Restaurants operate under the brand names BJ's Restaurant & Brewery, BJ's Restaurant & Brewhouse, BJ's Pizza & Grill, and BJ's Grill Restaurant. The menu features award winning deep dish pizza, BJ's proprietary craft beers, and a variety of other low priced appetizers, entrees, pastas, sandwiches, specialty grilled items, salads and desserts. BJ's currently has 20,700 employees and generated record high revenue of \$919.56 million in FY2016.



Thesis

BJ's is currently feeling the effects of the restaurant industry downturn. The industry wide consequences provide reasoning for the Q3 2016 miss on the top and bottom line. However, the company has implemented a strategic new restaurant growth plan that will allow them to outperform its competitors. BJ's is currently trading at a historically low P/E multiple of 19.46x and EV/EBITDA of 7.33x, well below its 5 year average of 12.4x. Both multiples signal that the company is currently undervalued. Rapidly improving margins and an investor friendly management team support my case of a BUY for BJRI at a price of \$35 or below.

Industry Outlook

United States based restaurants have struggled in 2016 through their display of poor revenue growth. The industry is quickly evolving to meet the needs of the growing millennial consumer base with the emergence of the fast casual dining scene. Millennials' and other consumers' spending habits are becoming more conservative as more people are favoring home cooked meals over eating out. Also negatively impacting the growth prospects of the restaurant industry is simply the oversupply of restaurants in the market. New restaurants are attempting to steal a share of the \$300 billion dining market with casual dining claiming two-thirds of the market. The highly competitive marketplace is putting a toll on the weaker companies as chief executives are being fired, companies are consolidating, and chains are closing down poor performing locations. While attempting to combat the industry down turn, companies are resorting to discounting meal prices and revamping operating strategies in order to optimize economies of scale and increase traffic to their restaurants.

Business Model

BJ's primary objective is to build customer loyalty through its efforts of consistently delivering excellent service by passionately connecting with every customer.

Customers dine at BJ's to experience the world class service, award winning pizza and proprietary craft beer. Introduced in 1978, the deep dish pizza is unusually light, crisp, has a bakery crust, and represents approximately, on average, 12% of total restaurant sales. Complementing the desirable pizza is the craft beer lineup. BJ's in house brewery operations produce approximately 20,000 barrels of beer, and independent third party brewers produce over 45,000 barrels of BJ's craft beer. Notably, the BJ's PM Porter and Lightswitch Lager won World Beer Cup gold medals in their respective categories at the Great American Beer Festival. BJ's owned craft beer sales, combined with other alcohol sales contribute, on average, 22% of total revenues.

Marketing is targeted toward generating higher foot traffic through television ads in areas surrounding each restaurant. Ads generally focus on the staple menu items such as pizza, desserts, and beer, as well as promotions for new menu items. With marketing expenses ranging from 2.2% to 2.3% from 2013 to 2015, management plans to stay consistent with its level of marketing by spending around 2%-3% of total sales in 2016. In 2015, and improved in 2016, BJ's launched new menu items such as the Enlightened Quinoa Bowl, Barbacoa Chicken, and the Loaded Burger to target the healthy, active customer. The menu prices range \$7.50 to \$24.50 with an average per customer check of \$14.50. Low cost meals and a diverse menu are attractive aspects of creating brand loyalty and customer satisfaction.

Currently BJ's owns and operates 182 restaurants in 24 states spread across the entire United States. Restaurant locations are typically found in densely populated suburban areas that target family oriented customers and the millennial customer. Management typically follows a growth rate of around 10% a year for new openings, ranging from 10 to 20 new locations per year. Historically, BJ's year over year growth in revenue has been reliant the number of stores it opens each year. New restaurants are not included in the same store sales measure until they reach a maturity of 18 months. Based on the table below, it is evident that same store sales has had implications on total revenue growth. This sparked management's decision to change their business model from a growth oriented stand point to a model structured around improving operations in existing stores. Management gave guidance of 12 new

store openings in 2017 in the Q3 earnings calls, significantly lower than the expected 17 new stores in 2016 and toward the lower end of the historical average.

	FY2013	FY2014	FY2015
Total Revenue Growth	9.40%	9.10%	8.80%
Same Store Sales	-1.10%	-0.80%	1.70%
Net Locations Opened	17	11	16

Investor Friendly

Despite the lack of dividends, BJ's management team has proven to implement plans to increase shareholder's wealth. Firstly, in 2014, the board of directors approved of a \$250 million share buyback program which was increased to \$350 million in 2016. From the Q3 2016 earnings call, approximately \$23 million, or 600,000 shares of common stock was repurchased in Q3 alone. As of April 2014, over 6 million shares were repurchased and retired for a price of \$243 million, leaving a total of \$107 million remaining in the repurchase program. Guidance on further repurchase plans has not been provided, however, management believes in the brand name and wants investors to believe in the company as well. Share repurchases are funded by a mix of cash and carefully allocated amounts from outstanding lines of credit.

Secondly, there has been a recent surge of insider transactions. After the decline in stock price to near 52 week lows due to poor results in Q3 2016, 1,500 shares were purchased on the open market by company CFO Gregory Levin. More significantly was the 15,000 share purchase made by company Director Noah Elbogen. At average prices of \$33.61, the total value of the shares purchased was \$554,565. This all comes after Director Elbogen's purchase of 30,000 shares in August 2016 for an average price of \$39.16. It must be noted that insider buying occurs when management believes that the company is undervalued and expects the company to deliver shareholder value by exceeding future expectations.

Company Initiatives

Maximizing organic growth is a pivotal factor for driving value in the slowing restaurant industry. The BJ's management team is aware that the necessary changes need to be made in order to survive and outperform its peers in the highly competitive environment. They have introduced company wide initiatives to combat their historically lagging organic growth and to improve future performance.

Marketing Strategies: A major factor in the -3.14% decrease in same store sales in Q3 2016 was the approximately 4% decline in foot traffic. A declining trend was apparent throughout the industry but BJ's took a harder hit than most of its peers. At BJ's there has been a recent trend of higher traffic during lunch hours compared to dinner hours. Customers prefer lighter, healthier meal options during the afternoon and management was targeting this by introducing and promoting its Enlightened meal options. This proved to be destructive because lunch options are typically sold at reduced prices while lowering margins and the average check per customer. While still utilizing the same marketing channels, the new strategy that is currently underway in Q4 will focus on promoting the same menu items as dinner specials. This will enable the company to raise the average check value and also increase the likelihood that customers will purchase an alcoholic beverage with their meals. BJ's owned craft beer is sold at the highest margins on the menu and will be an important factor in improving same store revenues.

Technology Advancements: BJ's strives for building relationships with its customers through positive experiences with waiters and fast service times. Every location, old and new, will receive an overhaul in kitchen and ordering technologies. The service staff will be able to use mobile tablets and specialized applications to send orders to the kitchen. Managers and kitchen staff will use a new system to monitor inventory levels as well as gauge daily performance while using new mobile applications. Optimizing the efficiency of each location is a key factor in raising customer and employee satisfaction.

Reduction in New Store Growth Rate: As mentioned before, BJ's will be reducing its level of new store growth rate to unleash the quality and value of its

current locations. Despite the slowdown in growth, management maintains their expectation of growing to a total of 425 domestic stores in the long term. Capital expenditures, labor costs, and sales, general, and administrations expenses will be greatly reduced in future quarters as fewer stores are being built. While no guidance has been given to estimate the level of future cost savings, it is evident that there will be an increase in free cash flow. The newly available cash will be used to fund the marketing and technology advancements, future share repurchases, and will provide a safety net for the uncertainty of the restaurant industry.

Financials vs. Competitors

ROIC /WACC					
		History		LFY	
BJRI		0.93		1.21	
Competitors		0.83		1.56	

ROIC W/O GW			WACC		
			History		LFY
BJRI		10.1%	11.1%		9.1%
Competitors		10.6%	19%		10.2%

COR/Revenue		EBITA Margin		SGA/Revenue	
		History		History	LFY
BJRI		80.6%		7.3%	6.3%
Competitors		76.8%		8.6%	8.0%

According to the historical analysis as displayed in the table above, BJ's has been growing value by increasing its ROIC to WACC ratio from its average of 0.93 to 1.21 in the last fiscal year, but the rate is slower when compared to its peers. This shows the company are still displaying returns on their invested capital, even when the industry is poorly performing. BJ's lagging performance is attributed to low ROIC without goodwill. It is important to analyze ROIC without goodwill because the industry is currently going through a consolidation phase, adding a goodwill premium to the participating companies. Costs of revenue and the low EBITA margin is driving the BJ's ROIC without goodwill of 11.1%, compared to the 19% industry average. Since these values represent the historical averages and last fiscal year, it reflects BJ's old business model that focused on growing the number of stores at high levels. Under the new business model, BJ's will have lower costs of revenue due to the decrease in labor, maintenance, and restaurant opening expenses. EBITA margins will also improve because of the company wide initiatives to maximize current store operations. The competitors used as comparisons are illustrated in the table below:

COMPETITORS	SYMBOL
Bloomin' Brands, Inc.	BLMN
The Cheesecake Factory Incorporated	NasdaqGS:CAKE
Chuy's Holdings, Inc.	CHUY
Dave & Buster's Entertainment, Inc.	NasdaqGS:PLAY
Famous Dave's of America Inc.	DAVE
Darden Restaurants, Inc.	NYSE:DRI
Brinker International, Inc.	NYSE:EAT
Ruby Tuesday, Inc.	NYSE:RT
DineEquity, Inc.	DIN
Red Robin Gourmet Burgers Inc.	RRGB

BJ's margins have shown growing momentum over the past three years as shown in the table below.

	2013	2014	2015
Gross Margin	17.52%	17.95%	19.89%
Operating Margin	3.08%	4.19%	6.86%
Net Margin	2.71%	3.24%	4.93%

With gross margins approaching 20%, operating margins approaching 7% and net margins nearing 5%, it seems that BJ's is in a position to handle a potential restaurant industry downturn if it does occur in the near future. With their current operating capabilities and efficiency improvement plans, BJ's will likely outperform its competitors.

Summary

BJ's Restaurants has the right strategy to combat a further restaurant industry downturn if it does persist. The unfavorable conditions have tarnished previous earnings which resulted in 25% stock price decrease since June. My assumptions about the impact of the efficiency improvement plan show that the price will revert back to its previous levels in the \$40 range, with a 1-year target price of \$42.50.

BJ's Restaurants, Inc. (BJRI)

CENTER FOR GLOBAL FINANCIAL STUDIES

NEUTRAL

Analysis by Justin Capuano
11/4/2016

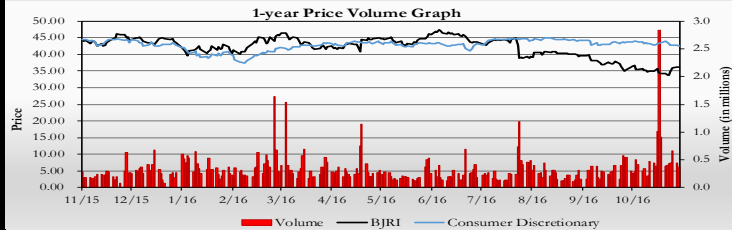
Current Price:
Divident Yield:

\$35.55
0.0%

Intrinsic Value
Target Price:

\$35.33
\$41.26

Target 1 year Return: 16.07%
Probability of Price Increase: 78.6%



Description
BJ's Restaurants, Inc. owns and operates casual dining restaurants in the United States.

General Information
Sector: Consumer Discretionary
Industry: Hotels, Restaurants and Leisure
Last Guidance: November 3, 2015
Next earnings date: February 16, 2017
Estimated Country Risk Premium: 6.25%
Effective Tax rate: 29%
Effective Operating Tax rate: 25%

Market Data	Market Data
Market Capitalization	\$826.83
Daily volume (mil)	0.32
Shares outstanding (mil)	23.26
Diluted shares outstanding (mil)	24.82
% shares held by institutions	82%
% shares held by investments Managers	61%
% shares held by hedge funds	27%
% shares held by insiders	6.68%
Short interest	9.31%
Days to cover short interest	5.88
52 week high	\$47.55
52-week low	\$32.24
Levered Beta	1.08
Volatility	31.40%

Quarter ending	Past Earning Surprises
9/29/2015	-0.64%
12/29/2015	-3.72%
3/29/2016	-1.85%
6/28/2016	-1.52%
9/27/2016	-5.77%
Mean	-2.70%
Standard error	0.9%

Management	Position
Trojan, Gregory	Chief Executive Officer, Pre
Levin, Gregory	Chief Financial Officer, Pri
Lynds, Gregory	Chief Development Officer an
Ledwith, Lon	Executive Vice President of
Krakower, Brian	Chief Information Officer an
Miller, Kendra	Senior Vice President, Gener

Profitability	BJRI (LTM)
ROIC	10.4%
NOPAT Margin	8%
Revenue/ Invested Capital	1.30
ROE	12.5%
Adjusted net margin	7%
Revenue/ Adjusted Book Value	1.80

Invested Funds	BJRI (LTM)
Total Cash/Total Capital	3.4%
Estimated Operating Cash/Total Capital	3.4%
Non-cash working Capital/Total Capital	-10.5%
Invested Capital/Total Capital	99.4%

Capital Structure	BJRI (LTM)
Total Debt/Common Equity (LTM)	0.42
Cost of Existing Debt	4.30%
Estimated Cost of new Borrowing	5.31%
CGFS Risk Rating	C
Unlevered Beta (LTM)	0.89
WACC	9.04%

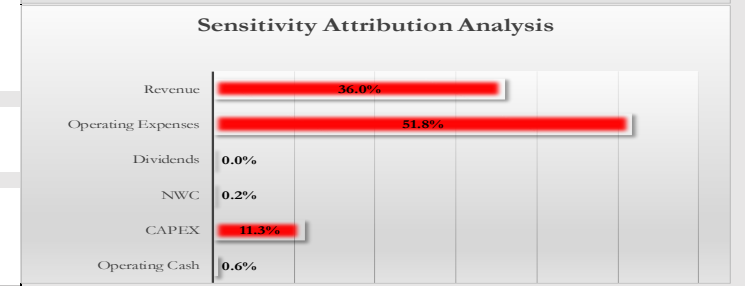
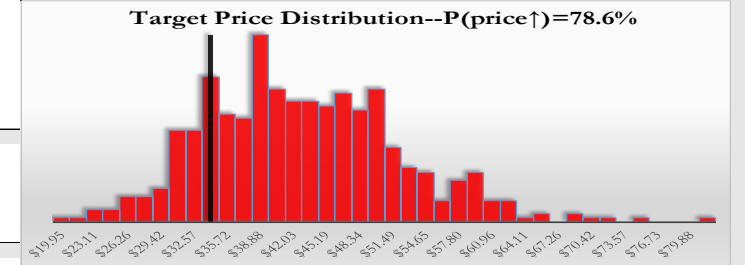
EBITDA	Peers
-0.33%	Bloomin Brands, Inc.
-0.06%	The Cheesecake Factory Incorporated
0.79%	Buffalo Wild Wings Inc.
-3.56%	Dave & Buster's Entertainment, Inc.
-16.91%	Texas Roadhouse, Inc.
-4.01%	Darden Restaurants, Inc.
3.3%	Brinker International, Inc.
	Ruby Tuesday, Inc.

Total compensations growth	Total return to shareholders
-9.68% per annum over 4y	-6.05% per annum over 4y
9.77% per annum over 5y	2.72% per annum over 5y
5.13% per annum over 5y	2.72% per annum over 5y
20.06% per annum over 3y	4.27% per annum over 3y
-100% per annum over 1y	-10.97% per annum over 1y
N/M	0% per annum over 0y

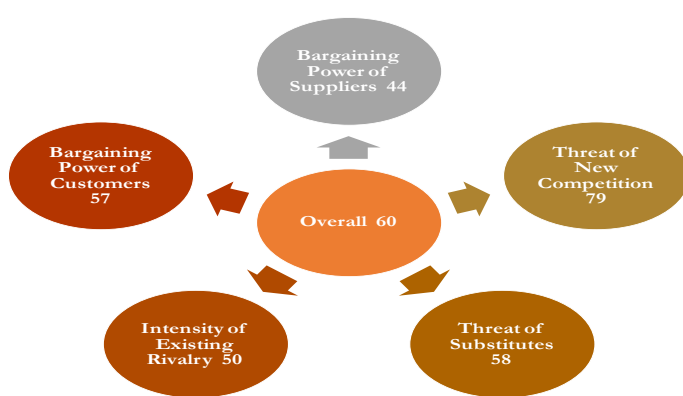
BJRI (5 years historical average)	Industry (LTM)
9.71%	23.70%
7.90%	13.9%
1.23	1.70
10.37%	31.54%
7.19%	12.1%
1.44	2.60

BJRI (5 years historical average)	Industry (LTM)
4.5%	21%
3.7%	N/A
-8.3%	-29%
98.3%	87%

BJRI (5 years historical average)	Industry (LTM)
0.23	0.37
5.06%	3.93%
5.31%	3.93%
C	B
0.74	0.70
8.33%	7.71%



Porter's 5 forces (scores are out of 100)



Period	Revenue growth	Valuation	ROIC/WACC
Base Year	6.7%	NOPAT margin	1.15
9/27/2017	6.1%		0.85
9/27/2018	7.3%		0.97
9/27/2019	6.9%		0.95
9/27/2020	6.5%		1.02
9/27/2021	6.2%		1.08
9/27/2022	5.8%		1.13
9/27/2023	5.5%		1.19
9/27/2024	5.1%		1.25
9/27/2025	4.8%		1.29
9/27/2026	4.4%		1.35
Continuing Period	4.1%		1.34
Period	Invested Capital	Net Claims	Price per share
Base Year	\$521.66	\$382.29	\$34.76
9/27/2017	\$572.79	\$384.47	\$39.31
9/27/2018	\$645.79	\$413.26	\$44.47
9/27/2019	\$693.66	\$378.01	\$50.04
9/27/2020	\$736.10	\$343.07	\$55.89
9/27/2021	\$769.22	\$298.84	\$62.04
9/27/2022	\$832.45	\$243.86	\$68.50
9/27/2023	\$941.71	\$179.99	\$75.25
9/27/2024	\$991.46	\$119.28	\$82.04
9/27/2025	\$1,050.22	\$40.80	\$89.03
9/27/2026	\$1,108.42	-\$40.33	\$96.21
Continuing Period			