

Shake Shack

Valuation Models

Feb-26

Model #1 - Sell Company Owned Restaurants; i.e. Liquidate the Company

Sell each company-owned location individually, add five years of royalties.

Assumptions:

- 1) The sale of each location includes transfer of its lease obligation and share of debt/liabilities.
- 2) The sales price per location is net of that location's allocation of the tax benefit.
- 3) Add back that location's share of existing cash on hand.

Key financial data points:

		<u>Impact Factors</u>		
Average Sales per Location		1	\$	3,900,000
Average Gross Profit Margin		0.23		23%
Contribution Margin			\$	897,000
Allocation of Depreciation (1/390)				(264,000)
Allocation of Overhead, Taxes, Interest				(475,000)
Net Profit per Location			\$	158,000
				4.1%
				Net Profit Margin
Licensing Revenue/YR	\$ 38,867,000			
Allocation (1/370)	105,046			
Multiplier of Licensing Revenue as Function of Time		5	\$	525,230
Value Per Store			\$	683,230
Multiplicative Factor of a Perfect Score of THREE		3	\$	2,049,689
Allocation of Current Assets/Tax Benefit				1,820,000
Asset Value of Lease				1,088,746
Less: Share of all Liabilities				(3,085,500)
Technical Book Value of Each Company Owned Restaurant			\$	1,872,935
Thus, each location is worth about \$1.9M as an asset.			\$	1,872,935
# of Locations				370
Total Value of the Company if Liquidate All Assets			\$	692,986,020
Total # of Shares				44,300,000
Value Per Share			\$	15.64

*Current earnings per share is \$1.14; thus a P/E of 14 exists which is NORMAL for the fast-food industry.

Model #2 - Ten Years of Earnings

To prepare for this model, the analyst has to determine expected earnings in 10 years. This means some reasonable assumptions must be made.

Assumptions:

- 1) All dollar values are in today's dollars, i.e. no inflation.
- 2) Shake Shack is at 2,200 locations in the same ratio as today, i.e. 1,270 company owned and 930 licensed locations.
- 3) Gross Profit Margin is maintained at 22%.
- 4) Depreciation/Amortization is a factor of \$276k per company owned location matching today's current amount.
- 5) G&A, Admin, Pre-Opening Costs, Other, Interest, Taxes only grows by a factor of 3.0 (actual should be 3.4).
- 6) Assume a linear line of earnings back to the current \$1.14 for 2025.

Revenue:	<u>Locations</u>			
Company Owned Stores	1,270	\$3.8 M Sales Each	\$4,826,000,000	\$4.8 billion
Licensing	930	\$180,000 per location	<u>167,400,000</u>	
Total Revenue			\$4,993,400,000	
Cost of Operating Company Owned Stores			<u>(3,716,020,000)</u>	*Nets to a 23% company level contribution
Contribution Margin			\$1,277,380,000	profit
G&A			<u>(\$447,141,000)</u>	
Depreciation/Amortization			<u>(\$348,885,000)</u>	
Pre-Opening/Interest/Taxes			<u>(\$152,540,000)</u>	*Actual Taxes will force this value to
Other Costs			<u>(\$7,518,000)</u>	exceed \$200 million)
Net Profit			\$321,296,000	
# of Shares Outstanding			44,300,000	
Net Earnings per Share			\$7.25	*This is the net earnings/share in 2035.

Earnings Chart:	<u>YEAR</u>	<u>ESTIMATED EARNINGS</u>
	2035	\$7.25
	2034	6.65
	2033	5.90
	2032	5.10
	2031	4.50
	2030	3.90
	2029	3.25
	2028	2.75
	2027	2.10
	2026	<u>1.55</u>
Total Ten Year Earnings		\$42.95
Average Earnings Per Year		\$2.39 *Assumes a 12% growth rate
Price to Earnings		14

Market Valuation **\$33.46**

Maximum Market Valuation

Liberal Considerations	\$33.46
Reasonable Conditions NO RECESSION	\$24.25
Reasonable Conditions Mild Recession	\$20.00
Reasonable Conditions Strong Recession	\$16.25
Conservation Considerations	\$12.50
Intrinsic Value	\$10.00 *See Note
Margin of Safety Buy Point for Value Investing	\$6.25

Note: Intrinsic value is less than current book value which is uncommon for companies that have some history. In this case, it makes sense because this company has a lot of risk AND is not in conformance with the fast-food business model. It is heavily reliant on its own stores for profits.

Model #3 - Market Valuation Comparison

With this method, the analyst compares the existing company against a similar size equivalent operation; OR scales the comparison model.

Let's compare Shake Shack to Wendy's.

	<u>Wendy's</u>	<u>Shake Shack</u>	
Locations	7,240	579	
Domestic Ratio	83%	64%	
Company Operated Restaurants	381	329	Year End 2024
Revenue From Company Operated Stores	\$925,905,000	\$1,207,561,000	Year End 2024
Avg Sales/Location	\$ 2,430,197	\$ 3,670,398	
Average Earnings/Franchisee	\$91,267	\$180,188	
Franchise Rental Income	\$ 236,493,000	ZERO	
Earnings Per Share 2025	\$0.92	\$1.14	With a P/E ratio of 10, market valuation warrants an \$11.40 per share value.
Gross Profit Margin	15%	23%	
Cash Flow From Operations	\$200,000,000	\$171,200,000	
Current Market Value	\$8.10	>\$90	
Dividends/Share	\$0.56	\$0.00	
Net After Tax Profit %	11%	12%	

Risk Factors for Shake Shack

- A) No economies of scale
- B) Highly dependent on the company owned locations to generate margin
- C) Non conformance to utilizing the franchising rental model
- D) Limits the issuing of licenses for domestic restaurants

Notes:

- 1) Shake Shack's sales per location are one of the best in the industry.
- 2) Wendy's risk factor is dramatically lower due to:
 - A) Volume of restaurants
 - B) Strong emphasis on franchising
 - C) Receives Franchising rents similar to McDonald's business model.
 - D) Wendy's pays dividends.
 - E) Wendy's has a very strong United States footprint ratio in comparison to other fast-food operations.
 - F) Wendy's has 16 years in a row of profits; has been in business for 50 years.
- 3) Shake Shack has a very strong gross profit margin; it is better than McDonald's.