
The Long Case For Wingstop, Inc.

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Short-term horizon, REITs, gold, long/short equity

Summary

- The popular restaurant chain foresees a market potential of 2500 stores.
- Wingstop will expand internationally, with 100 commitments in Saudi Arabia alone.
- Franchisees love Wingstop: the top ten Wingstop franchisees own 248 stores and almost 80% operate more than 1 store.
- Price target of \$35.28 for 2017, \$74.17 for 2021.

Invest in Wingstop

Wingstop (NASDAQ:[WING](#)) has seen growth in revenues and earnings of over 15 and 20%, respectively. The chain is popular among several consumer demographics, specifically sports enthusiasts. Franchisees, on average, operate over 3 locations each. Low entry costs and efficient economics of scale make Wingstop primed for growth both domestically and internationally. The most important driver for growth, along with willing franchisees, is the expansion of stores into Saudi Arabia. My price target is conservatively estimated at \$35.28.

The company is undervalued because investors underestimate two key factors. One, 75% of Wingstop's revenues come from carry out orders, through a point of sale system the company has simplified for consumers. Wingstop will begin national advertising this year, and it will be financed by an additional 2-3% of franchisees gross profits. The company will focus a portion of advertising online and on social media, which will tie together their mobile application to catapult carry out sales.

The other reason, which investors in the United States may have trouble quantifying, is the expansion of franchise locations into Saudi Arabia. Over the next ten years, starting with 2017, Wingstop has an agreement to roll out 100 restaurants in Saudi Arabia, where a restaurant like Wingstop will likely see massive success because of the food, carry out efficiency, and socioeconomic factors.

*All information related to Wingstop's operations and financials were found consulting the company's 2017 [10-K](#) report, filed March 3rd of this year.

Valuation

Last close (April 17): \$28.23

2017 Price Target: \$35.28

2021 Price Target: \$74.17

*These valuations are projected from conservative estimates compared to many analyst forecasts of over [19.5% annual growth](#) in earnings.

Wingstop Restaurants, Inc.
Stock Recommendation: **Buy**
Last Close (April 17): \$28.23
2017 Price Target: \$35.28

Wingstop is a United States fast casual dining restaurant chain with nearly 1000 locations worldwide, the majority of which are within the country. The company serves chicken with limited options beyond chicken wings. The fast casual dining segment, a subset of the restaurant industry, is a fiercely competitive growing market. Wingstop is exceptionally positioned to provide steady, and ultimately breakthrough, growth. The restaurant is a fan favorite and popular among several consumer demographics. Several high profile celebrities and athletes have had personal investment in the company, including football hall-of-famer [Troy Aikman](#) and rappers [E-40](#) and [Rick Ross](#). Shares of Wingstop last closed at \$28.23 on April 17, with a market cap of 818 million. Shares have traded since January 2015, opening at \$19.00 and since experiencing a current 52-week high of \$33.42.

Wingstop has excelled with a simple business model unrivaled by its competitors. Successfully establishing wings as the "center-of-the-plate" item, Wingstop derives 92% of sales directly from orders of wings, a drink, and fries. In 2016, 75% of sales came from carry-out orders, highlighting a business model which creates exceptional restaurant real estate efficiency. In 2016, average sales per square foot for Wingstop were \$655, far superior to any estimated restaurant industry average, and even further appealing when compared to fast casual dining competitors. Chipotle Mexican Grill, perhaps Wingstop's strongest competitor, operates over 2000 locations with similar, slightly higher, average sales per square feet.

Wingstop's franchisee system thrives on low cost entry, and the company has not missed a beat exploiting the franchisee model's success. It costs about \$30000 to establish a first location. In the last year, Wingstop opened 139 new restaurants (of which 137 were franchise locations). Of these new franchises, almost eighty percent of owners already operated a franchise beforehand. Wingstop's low entry cost, efficient use of real estate, brand recognition, and menu simplicity make it an attractive investment for franchisees. Wingstop is well on its way to operate a target 2500 domestic restaurants with over 500 new commitments (by end of 2016) already.

Wingstop has only pursued national advertising in 2017. Their new marketing campaign will be financed in whole by 2-3% of gross sales from franchise locations. The company intends to focus advertising efforts on online search engines and social media platforms. This should prove advantageous, as Wingstop implemented a successful online ordering system in 2014 which now accounts for almost 20% of fourth quarter 2016 sales. Moreover, online orders averaged \$4 higher than all others in fiscal 2016. In the future, expect Wingstop's already prominent carry out sales and efficiency to grow. Their simple business model will soon extend to procedural ease for consumers.

PERFORMANCE

Wingstop reported and earnings per share of 54 cents in 2016, compared to 37 cents the year before. Net Income grew over 50% last year, compared to 12% in 2015. Royalty Sales have consistently grown 22% in both the past two years. Same store sales have seen tremendous growth in the past 3 years; however, in 2016, same store sales growth slowed from 12% in 2015 to just 3%. This is a concerning figure for Wingstop moving forward, but the company has focused its efforts in streamlining sales through expansion. Most importantly, new national marketing efforts will be a key determinant in retaining same store growth velocity. Still, revenue growth remains consistent, with a 15% increase (compared to 17% the year before). In the last 3 years, Wingstop has opened over 400 locations, with 159 last year alone. The average United States' Wingstop franchisee operates 3 locations, while ten franchisees alone operated 248 restaurants. Share price of Wingstop are up over 16% in the past year to date. Consensus estimates expect annual growth in earnings of approximately 20% annually.

Wingstop has aggressively employed a franchise model growth strategy. Of their 998 locations, only 21 are corporate owned. Wingstop occupies forty states domestically, and six countries. Wingstop hopes to fulfill a forecasted 2500 possible stores within the United States alone. Internationally, Wingstop has 76 locations. In 2017, it will begin operations in 3 more countries.

KEY GROWTH FACTOR

The most overlooked factor is the expansion of franchise restaurants into the Kingdom of Saudi Arabia. Wingstop has an agreement with Saudi Arabia to open 100 restaurants in the next ten years. This is especially important, and, on one hand, hedges against systematic risk within the United States; Saudi Arabia has an economy less exposed to distress than other markets. Wingstop has access to public information and research - because chicken is a commodity - which can identify several international market penetration strategies, yet the company struck its largest international commitment with Saudi Arabia. Whoever within the company orchestrated the expansion made a smart and innovative decision. 100 locations is no small agreement either. Furthermore, socioeconomic factors make Saudi Arabia the optimal demographic for Wingstop internationally. Not only is this a first world country, the culture is a perfect fit for its business model. Low labor costs in Saudi Arabia are unparalleled to any other developed nation. The average family size is more than double that of The United States, according to the National Center for Biotechnology Information. The restaurant industry is quite different; restaurants such as McDonald's, KFC, and Applebee's all provide delivery services in Saudi Arabia, appealing to leisure friendly and home centric social environments. Many restaurant and fast food businesses experience peak hours late in the night and past midnight. Although Wingstop may not yet adopt delivery, the carry out dominance built into the business model will be monumentally advantageous in Saudi Arabia. The sporting event lure in Wingstop will not halt in the new market, with mass appeal for professional soccer potent across all generations. Many popular restaurant chains with diverse products must often innovate their menu selections to some extent when crossing borders. Wingstop has no such hurdle, as, again, chicken (along with a side and drink) drives over ninety percent of sales. Aggregate poultry consumption is similarly potent in Saudi Arabia as it is in United States, among the highest in the world.

RISK AND COMPETITION

Competition in the fast dining restaurant includes Chipotle Mexican Grill and The Habit Burger Grill. The closest competitor to Wingstop when it comes to food composition is Buffalo Wild Wings; however, it operates with a very different business model and relies on alcohol for 20% of sales. Businesses with similar business models produce vastly different goods, like Krispy Kreme and new fast casual pizza restaurants. Wingstop, again, is positioned to excel in the fast casual dining segment of the restaurant industry. Key risk factors include the rising price of chicken and possible decline in disposable income of consumers. Of course, Wingstop will need to comply with all food safety regulations to maintain a good reputation. It is also not unusual for 10% of franchise commitments to fall through; but Wingstop has experience only 6 closures since the end of 2015.

BUY RECOMMENDATION

Although Wingstop operates with serious risks potent to the restaurant industry such as sales decline, elastic consumer sentiment, and input price variability, investors are underestimating future performance in a growth model the company continues to evaluate, streamline, and accelerate in the near and foreseeable future. Investors are looking at steady growth for a number of years coupled with immediate cash inflows from franchise fees and royalties before domestic store potential is fulfilled, which, at that point, will provide steady and forecast friendly revenues in the form of royalties. Expansion of the franchisee network and new store openings will be assisted with brand recognition and media marketing exploiting online and carry out orders to catapult sales. Finally, Wingstop franchisees will begin operations in new countries this year, most promisingly in Saudi Arabia. Expect the stock price to rise 25% in 2017 to \$35.28, and to \$74.17 in 2021.

*Conclusions drawn in this article reflect opinions of the author, and do not qualify as investment advice. The author is not liable for any consequences of action taken.

Disclosure: I/we have no positions in any stocks mentioned, but may initiate a long position in WING over the next 72 hours. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.