

Mossberg's Investor Digest

Best Idea Profile:

Arcos Dorados Holdings (NYSE:ARCO)

DESCRIPTION:

Arcos Dorados is Latin America's largest fast-service chain and the largest McDonald's franchisee in the world with approximately 2,000 restaurants, 2,000 dessert kiosks and 340 McCafe units. It operates in 20 countries including Argentina, Aruba, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, Panama, Peru, Puerto, St. Thomas and Venezuela. Arcos Dorados, based in Argentina, employs more than 90,000 people, many of whom are first-time job holders, and serves approximately 4.3 million customers per day.

KEY INVESTMENT CONSIDERATIONS:

Exclusive Franchise Rights – Arcos is the largest McDonald's franchisee in the world with 2,000 stores in Latin American and the Carribean. It has exclusive rights for franchises in 20 countries, with Brazil as its largest market.

Success Despite Environment – The economic environment in Brazil is not stellar by a long shot. Brazil's currency has been in free fall, having declined 15% last year against the dollar, and interest rates have been rising. Inflation has continued to dampen financial results for many companies in Brazil. However, last month Brazil had its slowest increase in inflation in the past four years. Not ideal but definitely manageable for Arcos, particularly as it has successfully increased prices with inflation. Third-quarter same-store sales increased 12.6%, compared with less than 1% for McDonalds U.S.

Signs of Health From Competitors – Results from Burger King's Latin American operations may indicate an overall improvement for fast food in the area. Burger King in Latin America had declining same-store sales until a few quarters ago and is now experiencing positive comparisons with growth of 2% and system-wide sales growth of 17%, in large part because of aggressive growth in Brazil.

Dominance in Brazil – Brazil represents Arcos' biggest market and should prove an exciting opportunity over the next few years. The much-anticipated World Cup Soccer is being held in Brazil this summer and the Summer Olympics will be there in 2016. Arcos has multiple promotions and special programs in place leading up to and during the World Cup, which begins June 12. These are exciting events that will promote growth and expansion. Comparable sales in Brazil grew 5.6% in the third quarter, driven by average check.

Financial comparisons for Brazil will be tough in the fourth quarter because of big promotions in the previous quarter, but the long-term outlook is positive.

Dividend – With the stock at near lows, the dividend is yielding almost 3%. Additionally an improved debt profile (reduced blended interest rate and extended average maturity) and management's declaration of targets for improving profitability help build confidence in a continued strong performance.

Guidance – Management's update on guidance following the third quarter was for consolidated revenue growth between 15% and 18%, and consolidated adjusted EBITDA growth above 10%.

VALUATION:

The stock is hovering near a 52-week low. Arcos will announce earnings on March 11. Positive results could relieve much pressure on the stock and bolster the expectations for 2014. With a dividend yield of 3% and substantial potential for continued growth in 20 countries, this stock could attract higher ratios and attractive returns for shareholders.

Arcos Dorados (NYSE:ARCO)

Investment Data (as of 3/7/14)

Recent Price	\$9.25
52-Week Range	\$8.30 - \$15.52
Fiscal Year End	Dec
Dividend	\$0.24
Yield	2.6%
Shares Outstanding	210 M
Average Trading Volume (3 mos)	1.8 M
Market Capitalization	\$1.9 B
Cash	\$338 M
Long-term Debt	\$886 M
Enterprise Value (EV)	\$2.4 B
Book Value	\$3.25
TTM Revenue	\$4.0 B
P/ Revenue	0.5x
TTM EPS	\$0.31
P/ EPS	30x
TTM EBITDA	\$103 M
EV/ EBITDA	24 x

We attempt to provide subscribers with reasoned opinions based on our analysis of publicly available information from sources believed to be reliable, but make no representations as to its accuracy or completeness. Best Idea profiles are not based upon individual needs of subscribers nor are they an offer to buy or sell securities. Additional disclosures can be found under the Disclosures portion of the Mossberg's Investor Digest website.