

04/21/2025

Outperform

Price: \$12.32

Price Target: \$20.00

Industry

Consumer

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Stock Data

52-Week Range	\$12.32/\$18.61
Avg. Daily Volume	1,251
Market Cap. (MM)	\$78
Shares Out. (MM)	6.3
Cash Per Share	\$3.31
Debt-to-Capital	82.4%
Book Value Per Share	\$19.26
Dividend Yield	0.00%
FY End	Jan
Source: Factset	

Revenue Estimates (\$M)

	2023	2024	2025
1Q	157.7A	162.9A	154.5E
2Q	176.6A	172.4A	181.0E
3Q	170.3A	164.9A	173.1E
4Q	167.9A	168.7A	177.2E
FY	672.5A	668.8A	685.8E
P/S	0.1x	0.1x	0.1x
Prev CY	--	--	702.2E

Adjusted EBITDA (\$M)

	2023	2024	2025
1Q	5.0A	9.9A	2.2E
2Q	15.6A	12.9A	15.2E
3Q	8.1A	6.3A	14.7E
4Q	9.8A	13.2A	15.0E
FY	38.9A	42.4A	47.1E
Prev CY	--	42.9A	49.7E

Diluted EPS Estimates (\$)

	2023	2024	2025
1Q	0.30A	0.11A	(0.51)E
2Q	0.65A	0.33A	0.54E
3Q	(0.09)A	(0.34)A	0.46E
4Q	0.16A	0.59A	0.48E
FY	0.56A	0.75A	0.98E
P/E	22.0x	16.4x	12.6x
Prev CY	--	0.97A	1.36E

Meritage Hospitality (MHGU)

Q1 Earnings Update; Reaffirms 2025 EPS Growth Outlook

Summary

Meritage reported Q1 results that were challenged by atypical weather that negatively impacted sales in all markets. While mgmt decreased its full year revenue growth outlook to +3% growth from its previous 3-5% to reflect the weakness in Q1, it reaffirmed its outlook for 30-40% EPS growth. We like that Meritage is recording strong same-store sales growth with its Morning Belle brand and will begin leveraging technology (Wendy's Fresh AI) to drive efficiency and improve the customer experience.

Key Points

On Friday after market close, Meritage announced its preliminary Q1:25 results, reporting revenue of \$154.5M (-5.1% YoY) and adjusted EBITDA of \$2.2M (vs \$9.9M YoY), comparing to our \$171.0M and \$12.1M estimates, respectively. We attribute the weaker than expected results to the atypical weather that negatively impacted sales across all of Meritage's markets, with severe weather events in the southern US that resulted in decreased consumer traffic and numerous temporary restaurant closures from record snow, ice, and floods.

Based on the weaker than anticipated start to the year, we are decreasing our 2025 revenue forecast to ~3% growth from our previous ~5% growth estimate, reflecting management's updated outlook. We continue to appreciate the success Meritage is seeing with its in-house / independent restaurant concept brand Morning Belle, which continues to outperform industry trends.

More specifically, Morning Belle (single shift, breakfast / brunch concept) delivered same-store sales growth of 21.9% YoY. As this proof of concept and strong demand continues, Meritage plans to open 3-5 new Morning Belle locations throughout 2025. Further, after opening 3 new Wendy's stores in the quarter, Meritage plans to open 7-10 additional Wendy's locations through the remainder of the year.

Despite the challenging start to the year, Meritage reaffirmed its outlook for 30-40% diluted EPS growth in 2025, which we expect to be supported by robust new product offerings at Wendy's in the back half, as they are expected to launch protein-led innovations and marketing collaborations.

Further, we expect the implementation of Wendy's Fresh AI (generative AI Bot technology that brings a digital automated ordering experience to the drive-thru) to drive additional efficiencies at restaurants, while improving the overall customer experience. Meritage will be launching this AI technology at several locations during Q2:25.

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Meritage Hospitality Group Inc. (OTCPK:MHGU)
 4/20/2025
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 Model (Fiscal Year Ended Dec. 31)

\$ in millions except EPS and shares	FY17	FY18	FY19	FY20	FY21	1Q22	2Q22	3Q22	4Q22	FY22	1Q23	2Q23	3Q23	4Q23	FY23	1Q24	2Q24	3Q24	4Q24	FY24	1Q25E	2Q25E	3Q25E	4Q25E	FY25E
Revenue	312.6	435.3	467.5	516.2	577.1	145.1	161.0	160.6	159.4	626.0	157.7	176.6	170.3	167.9	672.5	162.9	172.4	164.9	168.7	668.8	154.5	181.0	173.1	177.2	685.8
COGS	84.8	116.4	124.9	134.4	150.8	39.0	44.3	44.8	43.8	172.0	44.0	48.0	47.0	45.3	184.2	41.8	44.4	43.3	44.9	174.4	42.5	48.9	46.7	47.8	185.9
Gross Profit	227.8	318.9	342.6	381.8	426.4	106.0	116.7	115.7	115.6	454.0	113.7	128.6	123.4	122.6	488.2	121.0	128.0	121.6	123.8	494.4	112.0	132.1	126.4	129.3	499.8
<i>Operating Expenses</i>																									
Advertising Expenses	13.3	18.4	18.2	18.2	22.3	5.7	6.2	6.3	6.3	24.4	6.1	6.8	6.7	6.6	26.3	6.5	6.9	6.7	6.8	27.0	6.3	7.2	6.9	7.1	27.6
Labor & Related Expenses	89.8	124.9	137.6	153.1	183.4	48.1	49.6	52.3	51.8	201.9	51.4	54.6	54.0	53.8	213.8	52.6	54.0	54.2	56.0	216.8	51.8	55.2	52.8	54.0	213.8
Franchise Fee Expense	0.0	16.1	17.6	19.5	21.8	5.5	6.1	6.1	6.1	23.8	5.9	6.6	6.5	6.4	25.4	6.2	6.7	6.4	6.5	25.8	6.0	7.0	6.7	6.9	26.6
Occupancy Expense	0.0	59.2	66.0	69.9	76.5	19.0	18.9	20.1	19.9	77.9	20.8	21.7	22.9	21.4	86.8	22.9	22.7	23.6	21.4	90.5	19.6	23.0	22.0	22.5	87.0
General and Administrative Expenses	17.3	21.2	23.4	27.8	32.2	6.3	8.1	8.1	8.3	30.8	7.2	9.2	7.4	8.2	32.0	7.8	8.2	6.3	8.7	31.0	8.5	9.0	8.7	8.9	35.1
Preopening, Acquisition and Closing Expenses	3.4	3.9	4.0	8.5	4.0	1.8	1.5	1.2	3.2	7.6	2.0	0.4	1.2	1.2	4.8	0.6	1.3	2.9	0.2	5.0	1.4	1.6	1.6	1.6	6.2
Other Operating Expenses	81.1	37.9	40.6	42.7	51.8	13.0	14.1	14.3	14.7	56.1	14.8	15.7	16.9	15.5	62.8	15.7	16.7	16.2	17.1	65.6	17.2	16.3	15.6	15.9	65.0
Depreciation and Amortization	8.4	12.0	14.1	16.3	16.3	4.3	4.3	4.4	4.5	17.4	4.5	4.6	4.6	4.8	18.6	4.8	4.8	4.8	4.8	19.2	4.9	4.9	5.0	5.0	19.8
Operating Income (Loss)	14.4	25.4	21.2	25.8	18.1	2.4	7.7	3.0	0.8	14.0	0.9	8.9	3.2	4.8	17.8	3.9	6.7	0.4	2.3	13.3	(3.7)	7.8	7.2	7.5	18.8
<i>Other Expenses / Income</i>																									
Interest Expense	5.7	9.7	12.3	10.8	6.7	1.7	1.8	2.2	2.5	8.2	2.6	2.9	3.2	3.2	11.9	3.3	3.2	3.4	3.1	13.0	3.1	3.2	3.3	3.4	13.0
Other, Net	(2.6)	(0.8)	(7.6)	(3.2)	(11.9)	(1.4)	(2.1)	(1.2)	0.8	(3.9)	0.4	(1.8)	(0.0)	0.4	(1.1)	(0.9)	(0.8)	(0.8)	(6.3)	(8.8)	(2.0)	(1.0)	(1.0)	(1.0)	(5.0)
Earnings before Taxes	11.3	16.5	16.5	18.2	23.3	2.1	8.1	2.0	(2.5)	9.7	(2.1)	7.7	0.0	1.2	6.9	1.5	4.4	(2.2)	5.5	9.1	(4.8)	5.6	4.9	5.1	10.7
Provision for Income Tax	2.3	3.4	3.6	2.4	5.1	0.1	2.1	0.1	(1.8)	0.6	(0.6)	1.8	0.1	(0.4)	0.9	(0.1)	1.3	(0.4)	0.3	1.1	(0.6)	0.7	0.6	0.6	1.3
Net Income (Loss)	9.0	13.2	12.9	15.8	18.2	2.0	6.0	1.8	(0.7)	9.1	(1.5)	5.9	(0.0)	1.6	6.0	1.6	3.0	(1.8)	5.2	8.0	(4.3)	4.9	4.3	4.5	9.4
Noncontrolling Interest (After Tax)	0.1	0.1	0.8	0.8	0.8	0.1	0.1	0.2	0.2	0.6	(0.1)	(0.1)	(0.0)	0.1	(0.1)	0.3	(0.1)	(0.1)	0.2	0.2	0.2	0.2	0.2	0.2	0.8
Net Income Attributable to MHGU	9.0	13.0	12.1	14.9	17.4	1.8	5.9	1.6	(0.8)	8.5	(1.4)	6.1	(0.0)	1.5	6.1	1.3	3.1	(1.7)	5.1	7.8	(4.5)	4.7	4.1	4.3	8.6
Change in Interest Rate Swap Valuation	0.0	0.0	0.0	0.0	(1.4)	(3.9)	(1.5)	(2.7)	0.0	(7.6)	1.5	(0.9)	(0.1)	2.2	2.6	(0.4)	0.4	2.1	(0.8)	1.3	0.0	0.0	0.0	0.0	0.0
Consolidated Comprehensive Net Income	9.0	13.0	12.1	14.9	18.8	5.7	7.4	4.4	(0.8)	16.0	(2.9)	7.0	0.1	(0.7)	3.5	1.7	2.7	(3.8)	5.9	6.5	(4.5)	4.7	4.1	4.3	8.6
Diluted EPS	\$ 1.46	\$ 1.44	\$ 1.27	\$ 1.58	\$ 1.81	\$ 0.15	\$ 0.62	\$ 0.15	\$ (0.10)	\$ 0.84	\$ 0.30	\$ 0.65	\$ (0.09)	\$ 0.16	\$ 0.56	\$ 0.11	\$ 0.33	\$ (0.34)	\$ 0.59	\$ 0.75	\$ (0.51)	\$ 0.54	\$ 0.46	\$ 0.48	\$ 0.98
Diluted Shares Outstanding	6.2	9.1	9.0	9.4	9.6	8.4	9.4	8.4	8.4	8.7	6.8	9.4	6.8	9.4	8.3	8.2	8.9	6.8	8.5	8.5	8.8	8.8	8.9	8.9	8.9

Company Description

Meritage Hospitality Group Inc. (OTC: MHGU) operates quick-service and casual dining restaurants primarily in the Middle East, South, and Southeastern regions of the United States. MHGU is a leading restaurant operator built around the company's highly efficient structure supported by cloud-based information technology and architecture, restaurant-level operations, real estate, accounting, data security, and consumer analytics. The company is one of the largest Wendy's franchisors with 375 locations across 16 states. The company also currently operates 4 Taco John's and has entered an agreement to develop up to 200 locations across the Midwest. The company also owns 6 casual dining restaurants in Michigan under the Morning Belle and Stan's Taco's brands. MHGU was founded in 1986 and is headquartered in Grand Rapids, MI with ~11,000 employees.

Valuation

We are maintaining our Outperform rating and decreasing our price target to \$20.00 from our previous \$24.00, to reflect the challenging start to the year and our reduced 2025 estimates, along with the greater pull-back across the peer group. Our updated price target roughly equates to a ~20x P/E on our updated 2025 estimate and compares to the QSR peer group average at ~25x 2025 P/E. The stock currently trades at ~12.5x 2025 P/E.

We continue to like Meritage's opportunity to implement / translate its effective operational and real estate development practices used with its Wendy's footprint, supported by its operating and technology platforms, to success with newer quick-service brands / stores, including Morning Belle and 7 Brew Coffee.

Risks to the achievement of price target

Competition Risk - The quick-service industry is highly competitive with countless options for consumers to choose from. If the company or the brands it franchises fail to innovate the products and experience or fail to differentiate itself from competition this could negatively affect the company.

Worsening Economic Conditions Risk - If economic conditions deteriorate and consumers have less discretionary money this could lead to a prolonged decrease of sales for the company.

Food-related Illnesses Risk - Any contamination of its products from suppliers or improper handling of food could lead to customer illness, which would harm the company's reputation and potentially lead to temporary closures of locations.

Nutritional Concerns Risk - National concerns about the nutritional quality and health effects around the quick-service industry broadly could have adverse effects on the company.

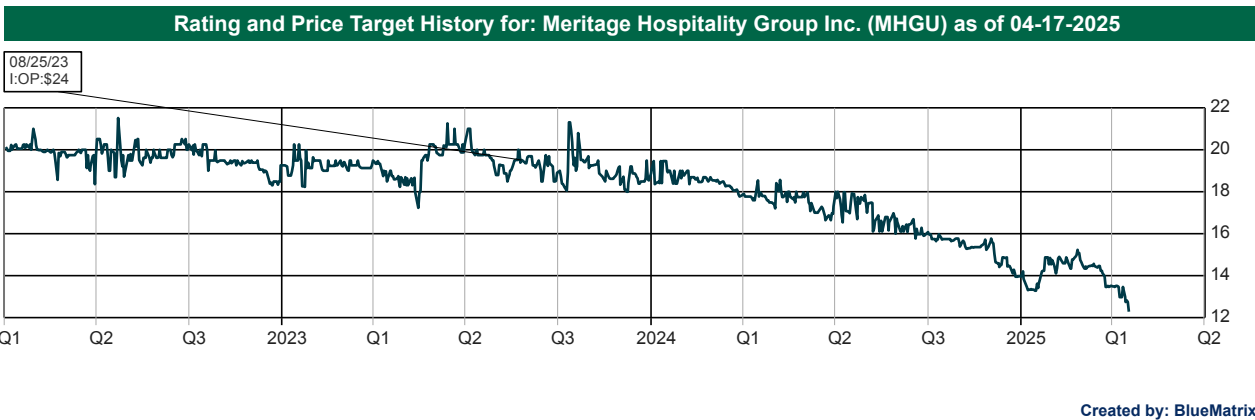
Changing Food Preferences Risk - As consumer's eating habits change, if the company and the brands it franchises cannot properly adapt, the company could see negative effects.

Brand Dependency Risk - The company is highly dependent on the national image of the Wendy's brand. If the brand was to have unfavorable news around them this could negatively impact MHGU.

Analyst Certification

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Outperform (BUY) – Outperform the S&P 500 by at least 10%.

Market Perform (HOLD) – Perform within 10% above or below the S&P 500.

Underperform (SELL) – Underperform the S&P 500 by at least 10%.

Rating Distribution Breakdown as of 04/21/2025

Rating Category	Count	Percent	IB Serv./ Past 12Mos.	
			Count	Percent
Buy [OP]	159	81.96%	25	15.72%
Hold [MP]	34	17.53%	3	8.82%
Sell [UP]	1	0.52%	0	0.00%

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