

# Domino's Pizza, Inc., 2013

www.dominos.com, DPZ

Based in Ann Arbor, Michigan, Domino's is the largest pizza delivery company in the USA having a 22.5 percent share of the pizza delivery market. Domino's digital ordering channels include online ordering at [www.dominos.com](http://www.dominos.com), mobile ordering at <http://mobile.dominos.com>, and ordering on iPhone, Kindle Fire, and Android apps. More than \$2 billion of Domino's pizza is ordered online annually. There are more than 10,300 Domino's stores in over 70 countries. Domino's had sales of over \$7.4 billion in 2012, with \$3.6 billion of that coming from the USA.

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## History

Growing up in foster homes most of their childhood, Tom Monaghan and his brother James borrowed \$900 in 1960 to purchase a mom-and-pop pizza store in Ypsilanti, Michigan, named Domi-Nick's. After trading his brother James a Volkswagen Beetle for his half of the business in 1961, Tom changed the store name in 1965 from Domi-Nick's to Domino's Pizza Inc. The company experienced steady growth during the 1960s, and by 1978, there were 200 Domino's stores in the USA. During the 1980s, the company expanded rapidly both in the USA and internationally.

By the end of the decade, Domino's had more than 5,000 stores in the USA, Canada, United Kingdom, Japan, Australia, and Colombia. By 1998, there were more than 6,000 Dominos, with 1,500 located outside the USA. Tom Monaghan retired in 1998 and sold 93 percent of the company (worth \$1 billion) to Bain Capital Inc. In the six years following the sale, Domino's enjoyed great success under Bain Capital and in 2004 Domino's became a publically traded company on the New York Stock Exchange under the ticker symbol DPZ. The initial stock price was \$16 per share and placed a value on the company at more than \$2 billion (double the price Bain paid). Domino's changed its 49-year-old recipe at year end 2009 and started a heavily advertised marketing campaign called "new inspired pizza." Domino's stock price appreciated from around \$8 a share at the start of 2010 to \$60 in mid-2013. Fueled by the new recipe and new products, Domino's celebrated its 50th anniversary in 2010 and was awarded best pizza chain in 2010 and 2011 by *Pizza Today magazine*, marking the first time ever that the same pizza chain had received the award in consecutive years. Domino's CEO Patrick Doyle was named the best CEO of 2011 by CNBC. Domino's was recently ranked number 1 in *Forbes magazine's* "Top 20 Franchises for the Money" list. About 96 percent of Domino's stores are owned by franchisees. There are very few company-owned Domino's stores.

## Corporate philosophy and mission statement

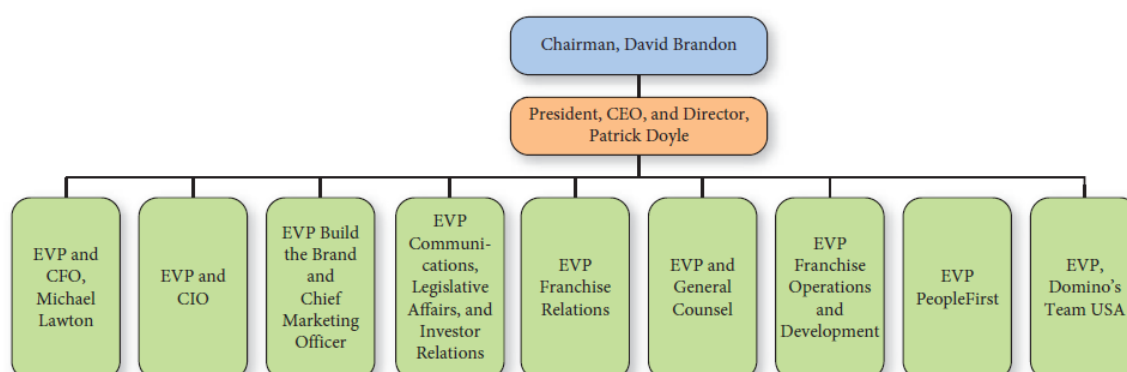
Domino's does not have a stated vision statement, but the company mission statement is as follows: "Exceptional franchisees and team members on a mission to be the best pizza delivery company in the world." Domino's "guiding principles" are based on the concept of one united brand, system and team:

- putting people first;
- striving to make every customer a loyal customer;
- delivering with smart hustle and positive energy; and
- winning by improving results every day. (2012 *Annual Report*)

## Organizational structure

As indicated in Exhibit 1, Domino's has 11 top executives, mostly executive vice-presidents (EVPs). It appears that Domino's operates from a functional organizational structure with Doyle being "where the buck stops," although for a firm of this size, a divisional or strategic business

## EXHIBIT 1 Domino's Organizational Chart



unit type structure by region (or by franchised versus company owned) may be more effective in promoting delegation of authority, responsibility, and accountability.

## Business Segments

Domino's provides financial information for four key business segments: (1) domestic company-owned stores, (2) domestic franchise stores, (3) domestic supply chain, and (4) international. Note in Exhibit 2 that the largest revenue-generating segment is the domestic supply

chain with more than 50 percent of all revenue. Note also the large revenue numbers for the relatively few company owned stores, because each Domino's domestic franchisee owns his or her own store(s) and reports their revenues on their own personal financial statements rather than Domino's. From franchisees, Domino's reports only the royalties and advertising fees it receives from franchisees as revenue. The financial data for the international supply chain centers are included in the international division, not under the domestic supply chain division. Also note in Exhibit 2 the slight revenue decline in 2012 for domestic company-owned stores.

Exhibit 3 reveals that for 2012, Domino's international stores had the highest growth in revenue, followed by U.S. company-owned stores. However the sales growth among all three segments slowed in 2012.

Exhibit 4 reveals that Domino's growth in number of stores is highest outside the USA, with the actual number of company-owned stores in the USA falling to 388. About 10,000 employees work for Domino's, but counting all workers for all franchisees, this number is closer to 205,000.

## EXHIBIT 2 Finances by Segment (in millions)

| Business Segment              | Revenue,<br>2012 | Revenue,<br>2011 | Revenue,<br>2010 | Revenue<br>Increase (%) |
|-------------------------------|------------------|------------------|------------------|-------------------------|
| Domestic company-owned stores | \$324            | \$336            | \$345            | (3.6)                   |
| Domestic franchise            | 195              | 187              | 173              | 4.3                     |
| Domestic supply chain         | 942              | 928              | 876              | 1.5                     |
| International                 | 217              | 201              | 176              | 8.0                     |
| TOTAL                         | \$1,678          | \$1,652          | \$1,571          | 1.6                     |

Source: Company documents.

Note: Domino's 2012 year ended 1-31-13.

**EXHIBIT 3 Same Store Sales Growth (Percent)**

|      | U.S. company-owned stores | U.S. franchise-owned stores | International stores |
|------|---------------------------|-----------------------------|----------------------|
| 2008 | -2.2                      | -5.2                        | 6.2                  |
| 2009 | -0.9                      | 0.6                         | 4.3                  |
| 2010 | 9.7                       | 10.0                        | 6.9                  |
| 2011 | 4.1                       | 3.4                         | 6.8                  |
| 2012 | 1.3                       | 3.2                         | 5.2                  |

Source: Company documents.

**EXHIBIT 4 Growth: Total Number of Domino's Stores**

|      | U.S. company-owned stores | U.S. franchise-owned stores | International stores |
|------|---------------------------|-----------------------------|----------------------|
| 2008 | 489                       | 4,558                       | 3,736                |
| 2009 | 466                       | 4,461                       | 4,072                |
| 2010 | 454                       | 4,475                       | 4,422                |
| 2011 | 394                       | 4,513                       | 4,835                |
| 2012 | 388                       | 4,540                       | 5,327                |

Source: Company documents.

**Domestic Supply Chain**

Domino's domestic supply chain supplies franchisees with dough, vegetables, ovens, uniforms, and much more, enabling better control, pizza consistency, and timely delivery of products. This backward integration strategy enables Domino's to offer pizza at lower prices and allows store managers to focus on store operations rather than mixing dough on site, prepping vegetables, and bargaining with independent suppliers for ingredients. Domino's has 16 regional dough manufacturing and supply chain centers and leases a fleet of more than 400 trucks to aid in delivering products to stores twice a week. However, Domino's franchisees are not required to purchase supplies from Domino's, but interestingly more than 99 percent do purchase all its supplies from the company's domestic supply chain segment. To ensure this division remains viable, Domino's provides profit-sharing incentives to franchisees to buy its products from Domino's. In addition to the 16 domestic supply chain centers, Domino's also operates 6 supply chain centers outside the USA.

**Domestic Stores**

The company's domestic stores division includes a network of 4,540 stores operated by 1,026 franchisees and 388 company-owned stores in the USA. Domino's desires to have all of its stores owned and operated by franchisees, but if certain stores are underperforming, Domino's often will purchase these stores in hopes of turning them around and then refranchising them at a later date. Domino's uses company-owned stores as test sites for new products, promotions, new potential store layout improvements, and as test sites for prospective new franchisees. Although the typical franchisee of Domino's operates 4 stores, the nine largest franchisees operate more than 50 stores, including the largest domestic franchisee that operates 135 stores.

Currently, Domino's has 1,077 different domestic franchisees with the average franchisee being in Domino's system for an impressive 14 years. Much of this longevity can be attributed to Domino's requiring prospective franchisees to manage a store for 1 year before entering into a long-term contract with Domino's. Domino's feels this system is unique to the pizza industry and provides a competitive advantage over rival pizza firms.

**International Division**

Domino's has 5,327 franchise stores outside the USA. The company's international revenues as a percent of total revenues increased to 13.0 percent in 2012, up from 11.2 percent in 2010. Exhibit 5 provides a breakdown of Domino's stores in the top 10 markets, which account for more than 75 percent of all Domino's international stores. Note that the United Kingdom has the most Domino's of all countries, followed by Mexico. Among the company's six "international" supply chain centers, four of these are in Canada, one is in Alaska, and one is in Hawaii. (It is unclear why Domino's categorizes Alaska and Hawaii as international). As with Domestic franchisee stores, most of the company's revenue in the international division comes from royalty payments and advertising, as well as the sales of food and supplies to certain markets predominantly Canada, Alaska, and Hawaii). Note in Exhibit 5 the rapid growth in Domino's stores in India, Turkey, and Japan. The largest Domino's franchisee outside the USA operates 911 stores.

## EXHIBIT 5 Top 10 Countries Where Domino's Are Located

| Country        | Number of Stores, 2011 | Number of Stores, 2012 | % Change |
|----------------|------------------------|------------------------|----------|
| United Kingdom | 670                    | 720                    | 7.5      |
| Mexico         | 577                    | 581                    | 0.7      |
| Australia      | 450                    | 464                    | 3.1      |
| India          | 439                    | 522                    | 25.7     |
| South Korea    | 358                    | 372                    | 3.9      |
| Canada         | 354                    | 368                    | 3.9      |
| Turkey         | 220                    | 284                    | 29.0     |
| Japan          | 205                    | 245                    | 19.5     |
| France         | 195                    | 215                    | 10.3     |
| Taiwan         | 141                    | 140                    | –        |

Source: Company documents.

### Internal Issues

Domino's has a vertically integrated supply chain where they have backward control to some extent over many of its supplies such as dough, veggies, equipment, and uniforms and forward control over around 400 retail stores that are company owned. Domino's offers little to nothing in terms of healthy food options on the menu, such as salads or fruit. Although this approach enables Domino's to focus exclusively on pizza, this practice also increases the firm's vulnerability to the increasingly health-minded customer and possible government mandates for fast-food

restaurants to stop using certain ingredients and preservatives, and potentially forcing all restaurants to label all nutrition information on the menu at the point of sale. Such a law would not be favourable to Domino's.

Domino's attributes much of its success to an incentive-based system for franchisees in which it actively shares in profits through increasing demand for new stores and through purchasing supplies from the Domino's supply chain. Domino's individual franchisee stores and company-owned stores also enjoy a simple and effective store layout enabling pizza delivery and carryout orders to be processed and executed efficiently as compared to many competitors.

Unlike Domino's, many rival pizza firms use a dine-in business model, which is much costlier than Domino's strategy. Competitive advantages such as these make Domino's an attractive franchisee option in the quick-service restaurant (QSR) market because overhead and investment is generally cheaper than competing firms.

### Sustainability

Sustainability refers to the extent that an organization's operations and actions protect, mend, and preserve rather than harm or destroy the natural environment. Many firms today develop an annual sustainability report, similar to an annual report, to reveal to stakeholders its actions and commitment to sustainability. However, Domino's does not produce an annual sustainability report nor does the company have a sustainability statement on its website.

### Advertising and Sales Force

Dominos domestic stores contributed 5.5 percent of all retail sales to support national and local advertising campaigns. Domino's expects this rate to remain unchanged for the foreseeable future. Much of those monies are devoted to mass-mail flyers promoting specials at the local Domino's.

### Domino's Pulse Point-of-Sale System

To maximize efficiencies and provide timely financial and marketing data, Domino's requires all stores to install and use its PULSE system that now exists in all company-owned stores and 98 percent of franchisee-owned stores. The system enables touch-screen ordering that improves order accuracy and efficiency and provides the driver with directions and the best route to take for multiple deliveries, saving time and money. In addition, the PULSE system better enables Domino's to ensure it receives full royalties from all transactions in what is often a cash business, assuming the franchisees are honest and always use the PULSE system when receiving orders.

## Finance

Domino's recent income statements and balance sheets are provided in Exhibits 6 and 7, respectively. Note that Domino's revenues increased 2.6 percent in 2012 and the firm's long-term debt rose slightly to \$1.53 billion. Note the company has zero goodwill on its balance sheet.

**EXHIBIT 6 Domino's Pizza, Statements of Income (In thousands, except per share amounts)**

|                                          | 2010             | 2011              | 2012              |
|------------------------------------------|------------------|-------------------|-------------------|
| REVENUES:                                |                  |                   |                   |
| Domestic company-owned stores            | \$ 345,636       | \$ 336,349        | \$ 323,652        |
| Domestic franchise                       | 173,345          | 187,007           | 195,000           |
| Domestic supply chain                    | 875,517          | 927,904           | 942,219           |
| International                            | 176,396          | 200,933           | 217,568           |
| Total revenues                           | <u>1,570,894</u> | <u>1,652,193</u>  | <u>1,678,439</u>  |
| COST OF SALES:                           |                  |                   |                   |
| Domestic company-owned stores            | 278,297          | 267,066           | 247,391           |
| Domestic supply chain                    | 778,510          | 831,665           | 843,329           |
| International                            | 75,498           | 82,946            | 86,381            |
| Total cost of sales                      | <u>1,132,305</u> | <u>1,181,677</u>  | <u>1,177,101</u>  |
| OPERATING MARGIN                         | 438,589          | 470,516           | 501,338           |
| GENERAL AND ADMINISTRATIVE               | 210,887          | 211,371           | 219,007           |
| INCOME FROM OPERATIONS                   | 227,702          | 259,145           | 282,331           |
| INTEREST INCOME                          | 244              | 296               | 304               |
| INTEREST EXPENSE                         | (96,810)         | (91,635)          | (101,448)         |
| OTHER                                    | 7,809            | —                 | —                 |
| INCOME BEFORE PROVISION FOR INCOME TAXES | 138,945          | 167,806           | 181,187           |
| PROVISION FOR INCOME TAXES               | 51,028           | 62,445            | 68,795            |
| NET INCOME                               | <u>\$ 87,917</u> | <u>\$ 105,361</u> | <u>\$ 112,392</u> |
| EARNINGS PER SHARE:                      |                  |                   |                   |
| Common Stock—basic                       | \$ 1.50          | \$ 1.79           | \$ 1.99           |
| Common Stock—diluted                     | \$ 1.45          | \$ 1.71           | \$ 1.91           |

Source: 2012 Form 10K, p. 50.

**EXHIBIT 7 Domino's Pizza, Balance Sheets (In thousands except share and per share amounts)**

|                                                                                                   | 2011              | 2012              |
|---------------------------------------------------------------------------------------------------|-------------------|-------------------|
| <b>ASSETS</b>                                                                                     |                   |                   |
| <b>CURRENT ASSETS:</b>                                                                            |                   |                   |
| Cash and cash equivalents                                                                         | \$ 50,292         | \$ 54,813         |
| Restricted cash and cash equivalents                                                              | 92,612            | 60,015            |
| Accounts receivable, net of reserves of \$5,446 in 2011 and \$5,906 in 2012                       | 87,200            | 94,103            |
| Inventories                                                                                       | 30,702            | 31,061            |
| Notes receivable, net of reserves of \$324 in 2011 and \$630 in 2012                              | 945               | 1,858             |
| Prepaid expenses and other                                                                        | 12,232            | 11,210            |
| Advertising fund assets, restricted                                                               | 36,281            | 37,917            |
| Deferred income taxes                                                                             | 16,579            | 15,290            |
| Total current assets                                                                              | <u>326,843</u>    | <u>306,267</u>    |
| <b>PROPERTY, PLANT AND EQUIPMENT:</b>                                                             |                   |                   |
| Land and buildings                                                                                | 23,714            | 24,460            |
| Leasehold and other improvements                                                                  | 79,518            | 80,279            |
| Equipment                                                                                         | 171,726           | 168,452           |
| Construction in Process                                                                           | 6,052             | 9,967             |
|                                                                                                   | 281,010           | 283,158           |
| Accumulated depreciation and amortization                                                         | <u>(188,610)</u>  | <u>(191,713)</u>  |
| Property, plant and equipment, net                                                                | <u>92,400</u>     | <u>91,445</u>     |
| <b>OTHER ASSETS:</b>                                                                              |                   |                   |
| Investments in marketable securities, restricted                                                  | 1,538             | 2,097             |
| Notes receivable, less current portion, net of reserves of \$1,735 in 2011 and \$814 in 2012      | 5,070             | 3,028             |
| Deferred financing costs, net of accumulated amortization of \$25,590 in 2011 and \$5,201 in 2012 | 16,051            | 34,787            |
| Goodwill                                                                                          | 16,649            | 16,598            |
| Capitalized software, net of accumulated amortization of \$51,274 in 2011 and \$48,381 in 2012    | 8,176             | 11,387            |
| Other assets, net of accumulated amortization of \$4,070 in 2011 and \$4,404 in 2012              | 8,958             | 8,635             |
| Deferred income taxes                                                                             | 4,858             | 3,953             |
| Total other assets                                                                                | <u>61,300</u>     | <u>80,485</u>     |
| Total assets                                                                                      | <u>\$ 480,543</u> | <u>\$ 478,197</u> |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>                                                      |                   |                   |
| <b>CURRENT LIABILITIES:</b>                                                                       |                   |                   |
|                                                                                                   | 2011              | 2012              |
| Current portion of long-term debt                                                                 | \$ 904            | \$ 24,349         |
| Accounts payable                                                                                  | 69,714            | 77,414            |
| Accrued compensation                                                                              | 21,691            | 21,843            |
| Accrued interest                                                                                  | 15,775            | 15,035            |
| Insurance reserves                                                                                | 13,023            | 12,964            |
| Legal reserves                                                                                    | 10,069            | 5,025             |
| Advertising fund liabilities                                                                      | 36,281            | 37,917            |
| Other accrued liabilities                                                                         | 29,718            | 34,951            |
| Total current liabilities                                                                         | <u>\$ 197,175</u> | <u>\$ 229,498</u> |

**EXHIBIT 7 Continued**

|                                                                                                                                                 | 2011         | 2012         |
|-------------------------------------------------------------------------------------------------------------------------------------------------|--------------|--------------|
| <b>LONG-TERM LIABILITIES:</b>                                                                                                                   |              |              |
| Long-term debt, less current portion                                                                                                            | \$ 1,450,369 | \$ 1,536,443 |
| Insurance Reserves                                                                                                                              | 21,334       | 24,195       |
| Deferred income taxes                                                                                                                           | 5,021        | 7,001        |
| Other accrued liabilities                                                                                                                       | 16,383       | 16,583       |
| Total long-term liabilities                                                                                                                     | 1,493,107    | 1,584,222    |
| Total liabilities                                                                                                                               | 1,690,282    | 1,813,720    |
| <b>COMMITMENTS AND CONTINGENCIES</b>                                                                                                            |              |              |
| <b>STOCKHOLDERS' DEFICIT:</b>                                                                                                                   |              |              |
| Common stock, par value \$0.01 per share;<br>170,000,000 shares authorized; 57,741,208 in 2011<br>and 56,313,249 in 2012 issued and outstanding | 577          | 563          |
| Preferred stock, par value \$0.01 per share; 5,000,000<br>shares authorized, none issued                                                        | —            | —            |
| Additional paid-in capital                                                                                                                      | —            | 1,664        |
| Retained deficit                                                                                                                                | (1,207,915)  | (1,335,364)  |
| Accumulated other comprehensive loss                                                                                                            | (2,401)      | (2,386)      |
| Total stockholders' deficit                                                                                                                     | (1,209,739)  | (1,335,523)  |
| Total liabilities and stockholders' deficit                                                                                                     | \$ 480,543   | \$ 478,197   |

Source: 2012 Form 10K, pp 48-49.

## Competitors

Competition in both the USA and international pizza-delivery and carry-out business is extremely intense, with Pizza Hut (owned by Yum Brands) being the largest competitor in the industry. Pizza Hut's revenues are more than 60 percent greater than Domino's. Papa John's and Little Caesars are also fierce rivals in the industry. In fact, Little Caesars was listed as the fastest-growing pizza chain in 2010, with revenues up 13.6 percent over 2009, followed by Pizza Hut's 8 percent increase and Domino's 7.2 percent increase. In addition to the three main rivals, Domino's faces intense competition from many local mom-and-pop pizza stores, frozen pizzas from the grocery store, as well as hundreds of non-pizza fast-food options. Pizza Hut, Domino's, and Papa John's account for 51 percent of all consumer spending on pizza delivery stores in the USA, with the other 49 percent coming from regional or mom-and-pop establishments. Internationally, Pizza Hut and Domino's are the main players in the industry, but various countries have numerous national companies and thousands of mom-and-pop pizza and Italian restaurants vie for business as well. As with the domestic market, some customers consider local pizza stores to offer better quality products than large chains and are willing to pay marginally higher prices for this perceived quality.

Another competitor is Pizza Inn Holdings, Inc., based in The Colony, Texas. Pizza Inn owns 10 stores and franchises out 300 more stores.

### Pizza Hut

A division of Yum Brands, Pizza Hut is based in Plano, Texas, and operates more than 7,200 restaurants in the USA and more than 5,600 restaurants internationally in more than 90 countries. In contrast to Domino's, almost all Pizza Huts are dine-in restaurants. Pizza Huts serve pan pizza, as well as its thin n' crispy, stuffed crust, hand tossed, and sicilian. Other menu items include pasta, salads, and sandwiches. Pizza Huts offer dine-in service at its famous redroofed restaurants, as well as carryout and delivery service. About 15 percent of all Pizza Huts are company-operated, whereas the remaining stores are franchised. The world's largest fast food company, YUM Brands also owns and operates Kentucky Fried Chicken (KFC), Long John Silvers, and Taco Bell. Pizza Hut is Domino's major pizza rival outside of the USA.

### Papa John's International, Inc.

Headquartered in Louisville, Kentucky, and founded in 1985, Papa John's operates 3,883 pizza restaurants with 3,255 of these being franchisee-owned and 628 being company-owned stores. Papa John's has restaurants in all 50 U.S. states and 32 foreign markets. The company currently has 16,500 full-time employees and markets its pizza under the slogan "better ingredients, better pizza." Between 2001 and 2012, Papa John's was ranked number one (by the American

Customer Satisfaction Index) among national pizza chains for 10 of the 11 years during this period. The company reported revenue of more than \$1.2 billion for year-end 2011, and consistent with the industry, it shows no revenue allocated to research and development. Papa John's carries \$75 million in goodwill on its balance sheet; founder and CEO John Schnatter owns more than 20 percent of the chain. Papa John's offers several different pizza styles and topping choices, as well as a few specialty pies such as The Works and The Meats. Papa John's stores typically offer delivery and carryout service only.

Exhibit 8 provides a comparison between Domino's and Papa John's. Note that Domino's appears to generate more revenue with less employees, but that is not true because employees at franchised stores are not Domino's employees. Pizza Inn's 57 employees work at company owned restaurants, not franchised stores.

### Pizza Inn Holdings, Inc.

Pizza Inn is a relatively small chain of franchised quick-service pizza restaurants, with more than 300 locations in the USA and the Middle East. Pizza Inns offer pizzas, pastas, and sandwiches, along with salads and desserts. Most locations offer buffet-style and table service, whereas other units are strictly delivery and carryout units. The chain also has limited-menu express carryout units in convenience stores and airport terminals, and on college campuses. Pizza Inn's domestic locations are concentrated in more than 15 southern states, with about half located in Texas and North Carolina.

### Little Caesars

Headquartered in Detroit, Michigan, and privately held, Little Caesars is famous for its advertising slogan, "Pizza! Pizza!" which was introduced in 1979. The phrase refers to two pizzas being offered for the comparable price of a single pizza from competitors. In November 2010, Little Caesars introduced Pizza! Pizza! Pantastic, denying that the return of "Pizza! Pizza!" had any relationship to the recent success of Domino's. Little Caesars operates under its parent Little Caesars Enterprises and is estimated to be the fourth largest pizza chain in the USA. Little Caesars operates in 30 foreign countries.

## External Issues

Domino's competes in the Quick Service Restaurant (QSR) pizza category, which consists of two categories: 1) delivery and 2) carry-out. Delivery revenues for the industry in 2012 were \$9.6 billion, up only slightly the last few years. The delivery portion accounts for 30 percent of the total QSP pizza revenues. However, the carry-out portion of the industry grew revenues from \$14.1 billion in 2011 to \$14.6 billion in 2012. Domino's is the market leader in delivery and second largest in carry-out. Outside of the USA, pizza delivery is underdeveloped, with Domino's and one rival being the only firms.

**EXHIBIT 8 A Comparison Between Domino's and Papa John's**

|                       | Domino's | Papa John's | Pizza Inn Holdings |
|-----------------------|----------|-------------|--------------------|
| Revenue               | 1.65B    | 1.24B       | 43.5M              |
| Market Capitalization | 1.76B    | 1.16B       | 20.1M              |
| Gross Margin          | 0.29     | 0.31        | 0.12               |
| Net Income            | 98.99M   | 55.97M      | 888K               |
| EPS                   | 1.63     | 2.24        | 0.10               |
| Price/Earnings Ratio  | 18.67    | 21.69       | 24.51              |
| Number of Employees   | 10K      | 16.5K       | 57                 |

EPS, earnings per share.

Source: Company documents.

### Nutrition Concerns

An area of concern for all fast-food establishments, including pizza stores, is the growing health-minded customer, as well as the growing pressure from government agencies to label all products with nutrition information. There have been battles between the restaurant industry and government agencies for many years, but much like the tobacco industry (in respect to labeling its products). It appears the war is close to being lost for the restaurant industry. Domino's itemizes nutrition information on its website, but forces the customer to add the calories for crust, sauce, cheese, and topping, and then divide by the number of slices to derive the total calorie

count per slice. After doing the calculations, one large slice of hand-tossed pepperoni pizza for example has 300 calories and 12 grams of fat, and there are 8 slices in a pizza. To complicate matters for restaurants such as Domino's, it is difficult to provide accurate nutrition labels when there can be an almost endless combination of ingredients on a pizza. For example, someone may order a large sausage pizza with onions and olives whereas someone else might order extra cheese and tomatoes. Having to print out nutrition labels for all these combinations would be quite costly as opposed to a restaurant like McDonald's where it can print the nutrition label on the Big Mac because there is uniformity in ingredients and the label is understood to be for the base item. However, Domino's PULSE system could possibly be adjusted to resolve this potential issue.

Chipotle Mexican Grill claims to only use meat and dairy products from free-ranging cattle, as opposed to cattle injected with growth hormones. Domino's Pizza markets its pizzas as having gluten-free crust. This is an attempt to win over health-conscious customers, comply with government regulations, and make current customers feel a little less guilty about eating pizza. The tug of war between customers, governments, lawyers, and the restaurant industry on health issues is likely to continue for some time.

In response to these challenges, many restaurants have opted for healthy menu options.

Wendy's, for example, has promoted several meal combinations that contain less than 10 grams of fat. All of these items were originally on its menu, just not marketed in that manner. Wendy's has added side salads and fruit to help cut down on calories, fat, and sodium. Subway is also famous for marketing its products as healthy alternatives to other fast-food options. Domino's, and many pizza competitors, offer few to no menu options for the health-conscious consumer.

### **Barriers to Entry**

Barriers to entry are relatively low for the restaurant industry, but rivalry (competitiveness) among firms is exceptionally high. One large contributing factor for the low barriers to entry is many small entrepreneurs can open mom-and-pop establishments and bypass the franchise fees, royalties, selection process, and so on of owning a franchised restaurant and lease an existing building relatively cheap. However, even avoiding high fixed costs, variable costs are often high and small-scale entrepreneurs are not able to compete with larger franchise stores, who can better negotiate pricing on food, packaging, and other supplies. In the QSR industry, the bargaining power of consumers is quite powerful, availability of restaurant options in most places is abundant, and consequently there is intense price competitiveness among rival firms. Even if you are sure you want pizza for lunch or dinner, you likely have many options.

### **Economic Factors**

The current landscape in the QSR business is a bimodal population distribution with a large population of bargain-minded customers seeking deals on cheaper end fast food options, and another population of more affluent consumers targeting middle to higher-end restaurants. Domino's is well positioned strategically to target the first group of consumers because there are many more of them; Domino's often has excellent sales and discounts to target this group. Among the subset of customers who are value shoppers, many of these are also shoppers of quality and are willing to wait in line a little longer or pay a little more for better quality food products. Domino's has recently capitalized on this well with the introduction of its artisan pizzas and new recipes (or higher quality products) for its crust, sauce, and cheeses. In addition, Domino's offers many pick up specials. Although an inconvenience over delivery, many customers in today's climate are willing to tolerate a degree of inconvenience that they historically were not if they can get a better deal.

Similar to Domino's, many restaurant owners in the fast-food industry have experienced stronger growth in international markets than domestic markets. This trend is expected to continue, especially in China and other developing nations because many U.S. fast-food options are still novel, even in Europe. According to the S&P Industry Surveys, QSRs are expected to see a sales increase of 3 percent in 2012 and orders to increase 1.5 percent as a result in large part of consumers trading down to cheaper restaurant alternatives. There also is a steadily growing international appetite for U.S. fast food and an improving global economy. These positive trends are expected to continue into 2013 and should bode well for Domino's with its strong international presence.

### **Ethics and Corporate Citizenship**

Domino's has two extensive "Code of Ethics" documents on its website: one statement for its

employees and one statement for its executives. The documents outline matters such as: conflicts of interest, how to report unethical conduct, fair dealing with all employees, compliance with laws, proper way to use company assets, and much more.

In addition to Domino's Code of Ethics statements, the company is noted for its corporate citizenship record in particular with St. Jude Children's Research Hospital. Since 2006, Domino's has donated more than \$12 million to St. Jude and has hosted pizza parties for patients and its families on St. Jude properties.

In 1986, Domino's launched its Pizza Partners Foundation with a mission of "team members helping team members." The foundation is 100-percent funded by team member and franchise contributions and has disbursed nearly \$12 million to aid team members facing crisis situations such as fire, illness, or other personal tragedies.

## **The Future**

As CEO Doyle and his management team contemplate the future direction of Domino's, it has much to consider. Should the firm continue its aggressive market development strategies and accept the risk associated with expanding into markets it has little expertise operating within? What new geographic locations or regions should Domino's focus? Should Domino's simply follow Pizza Hut's international rollout of stores? How would this expansion affect the corporate structure of Domino's? Would restructuring by geographic division and thus establishing offices in Asia, the Middle East, and South America better enable them to manage these more risky environments? Can Domino's afford this financially? Should Domino's consider offering salads or a line of healthy menu options? Should Domino's purchase trucks to deliver its products rather than incurring such heavy leasing expenses?

**Domino's needs a clear three-year strategic plan. Prepare this document for the company.**