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EXECUTIVE SUMMARY

Chipotle Mexican Grill (NYSE: CMG) is the pioneer of what is now called the fast-casual restaurant industry. Started in Denver, Colorado Chipotle now operates 1,084 stores in 38 states in the US as well as operating stores in Canada and now London, England. Chipotle serves a simple menu that is highly customizable. They pride themselves on serving high quality, fresh ingredients that are grown in a sustainable and human manner in accordance with their 'Food With Integrity' initiative. Since its inception in 1993 Chipotle has enjoyed rapid growth and increasing success. In 2010 alone, revenues exceeded \$1.835 billion. Chipotle has seen its revenues and net income increase in each of the past five years. It has expanded rapidly even through national economic hardships and uncertainty and has seen its profit margins grow healthily the past three years.

While Chipotle has had great success, Cambrian Group believes that they can help Chipotle continue and enhance that success. Chipotle should continue its growth in the United States both increasing density in current locations as well as expanding into areas that, as of now, are untapped by Chipotle. Also, after achieving initial success in Europe Chipotle should continue to test the western European market by slowly entering other major cities such as Paris and Munich but keep their focus on domestic expansion. With this stated expansion, Chipotle should continue and increase its use of the smaller, more efficient A-Model style restaurant. Chipotle has recently run into troubles with illegal workers in its restaurant and is the current target of ICE probes in multiple states. Cambrian would also recommend that Chipotle tighten its hiring policies and possibly help sponsor individuals to help them gain the legal right to live and work in the United States. The last recommendation is to continue its 'Food With Integrity' initiative but also to advertise the initiative more heavily as it is a major differentiating factor between CMG and its competitors.



PART I

INTRODUCTION



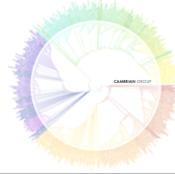
COMPANY OVERVIEW

Chipotle Mexican Grill is a fast-casual restaurant business with the idea that food served fast doesn't have to be typical fast food. They currently operate over 1,000 restaurants and employ over 25,000 people. With an emphasis on having fresh, high-quality all natural ingredients Chipotle has created a unique experience for consumers. They have a very focused menu, the food is assembled in front of you, and all their locations have a unique, distinctive ambience. They strive to be a hip company and so they offer online ordering and even have an iPhone application to keep with current trends. Chipotle is a very strong, widely-recognized brand that now dominates the Mexican fast-casual restaurant sector with over twice as many restaurants as their closest competitor, Qdoba Mexican Grill.

History

Chipotle (CMG) was founded in 1993 by then-Chef Steve Eells, who is still Chairman and co-CEO of Chipotle. The first location was in Denver, CO and was converted from an old ice cream parlor. Needing to sell about 100 burritos per day to see profits the location was quickly selling over 1,000 burritos per day and so in 1995 and 1996 seven more Denver area stores were opened. Up until this point Chipotle's expansion was funded mostly by Eells' father with a total of \$1.5 million invested. The rest of the funding came from cash flows and a Small Business Administration loan, but in 1998 Eells created a Board of Directors and raised \$1.8 million in outside capital. This influx of money funded CMG's move into two new markets in Minneapolis and Columbus. From there, Chipotle enjoyed fast expansion from the 16 restaurants that existed in 1998 to 500 by 2005 and to the 1,023 that exist today: all owned by CMG with no franchising. Chipotle now covers most of the United States, with several locations in Canada and a recently opened location in London, England.

In 2006, Chipotle went public with an IPO price that had to rise twice because of a high perceived demand and the stock price still doubled on its first day. The money raised from this funded new store growth.



McDonalds was one of Chipotle's initial minority investors and by 2001 it was its largest investor. McDonalds fully divested from Chipotle in 2006 but they had invested \$360 million in Chipotle over the years. They also helped strategically by providing help in the supply chain as Chipotle rapidly grew geographically. Over the past five years, Chipotle has still enjoyed significant growth with its overall revenue more than doubling in that period to \$1.74 billion in the most recently reported twelve months and growing by almost 65% from year end 2008 to 2009. On January 26th, 2006 CMG's stock price was at 42.2 and in 2011 it has yet to dip below 217 and has reached as high as 246.3. This represents a 158% positive change in price over the last year. CMG stock has outperformed the S&P500 over the past year, as well as outperforming competitors Yum! Brands, Inc. who run Taco Bell and It has a market cap of \$7.62 billion which sits at a premium above its enterprise value of \$7.11 billion. All this has led to some speculation that CMG stock may be slightly overvalued, or at least won't experience similar growth, but Chipotle's has expanded financially safely and plan on larger growth in the coming year.

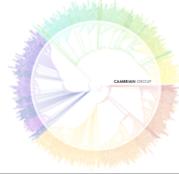
Current Situation

In 2010, Chipotle had revenues exceeding \$1.8B which was up almost 21% above 2009 numbers. Net income increased by 41.1% over the previous year which is a very healthy growth rate. Over the last four years CMG's revenues and net income have grown by 22.4% and 46.1% on an annualized basis respectively which are both great growth rates to sustain for that period. Chipotle also has a very stable financial situation. Currently, their balance sheet contains \$301 million in cash and just \$3.81 million in debt exhibiting a high coverage ratio. They also operate at margins much higher than most of the restaurant industry with a profit margin of 9.43%. Average restaurant sales have stayed somewhat consistent over the past three years with a very slight increase to about \$1.8 million, but restaurant and company level margins have been increasing consistently since 2005 with restaurants now operating at a 26.4% margin. All this has lead Chipotle to believe that they will open about 140 new restaurants in 2010 which is a significant jump from the 67 openings in the year ending September 30, 2010.



Chipotle is unique in the restaurant business for several reasons. First it has a very distinct plan for its ingredients. In 1999, Steve Ells started Chipotle's emphasis on 'Food With Integrity' by serving naturally raised pork in 2000 and naturally raised chicken in 2002; now 100% of Chipotle pork and chicken is naturally raised. In 2004, Chipotle also started using zero trans-fat frying oil. Emphasis was also put on naturally raised beef in 2009 and so now 85% of beef is naturally raised and by 2007 all sour cream and cheese products were rBGH-free. Ells' crusade for more humane and eco-friendly food supply starts taking off and as of 2010 40% of the black beans served are certified organic. Chipotle stands against the use of any unnatural hormones or antibiotic usage as well as other additives with the raising of its meat products and is striving towards 100% compliance with its corporate goals. Chipotle also prefers buying from family farms and also in buying locally. In 2010 Chipotle planned to serve at least 50% of its produce from local farms (within 300 miles of the restaurant) when seasonally available. Because of this Chipotle has had to raise prices somewhat but sales have not been hurt by these changes.

Another reason that Chipotle is a unique brand is its architecture and advertising. Each new restaurant aims for a hip and urban feel. Each Chipotle location has industrial, but little, décor which consists of halogen lighting, metal tabletops, wooden benches and seats, concrete floors, arched metal ceilings, and exposed ductwork with all artwork inside each Chipotle being designed by sculptor Bruce Gueswell. It costs the company approximately \$850,000 to open a new restaurant and they have started putting a heavy emphasis on sustainable construction with some of their restaurants featuring solar panels or even wind turbines. On the advertising side Chipotle has been remarkably absent. During its rapid expansion in the early years advertisement was solely by word-of-mouth. Now the company advertises on billboards and radio advertisements and currently has a witty, edgy campaign going poking fun at typical marketing campaigns, which fits in with the wanted style of their restaurants. Other advertising outlets include giving out burritos on Halloween for costumes that look like burritos or processed foods and even sponsoring screenings of Food, Inc to spread appreciation of their 'Food With Integrity' initiative.

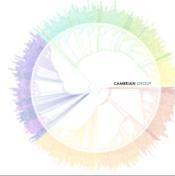


Chipotle plans on strong growth in the future as well with the noted plan to introduce 135 to 145 new restaurants in the 2011 calendar year in current markets as well as planned expansion further into Europe. CEO Eells, and 1.25% owner, is also planning on starting an Asian fast-casual restaurant chain in the future as well. They are a major buyer in food supply market and have already started using that power to improve their supply chain. Chipotle stands very financially secure with solid prospects for future growth, amidst some doubt about the relative value of Chipotle Mexican Grill's stock price.



PART II

ANALYSIS



FINANCIAL ANALYSIS

Chipotle Mexican Grill is a high growth casual restaurant chain serving a menu of tacos, burritos, salads and burrito bowls made with fresh ingredients. The company has a market capitalization of \$8.504 billion and grossed \$1.836 billion in revenue with a net income of \$179 million in fiscal year 2010. Chipotle's most similar and direct competitors are Mexican fast food chains such as Qdoba Mexican Grill and to a lesser extent Taco Bell, Del Taco, and similar locations, however Chipotle also competes directly against other mid-sized casual dining chains offering similar services- relatively cheap food, quick service, casual dining experience- including: California Pizza Kitchen, Panera Bread Company and P. F. Chang's China Bistro. While these firms span the casual dining spectrum, the Vector Group believes that Chipotle's most direct competitor, in terms of consumer dining experience, is Panera Bread Company with \$1.542 billion in gross and \$111.6 million in net income. In addition to larger regional and national competitors, Chipotle's competition also includes a variety of smaller locally owned restaurants and markets.

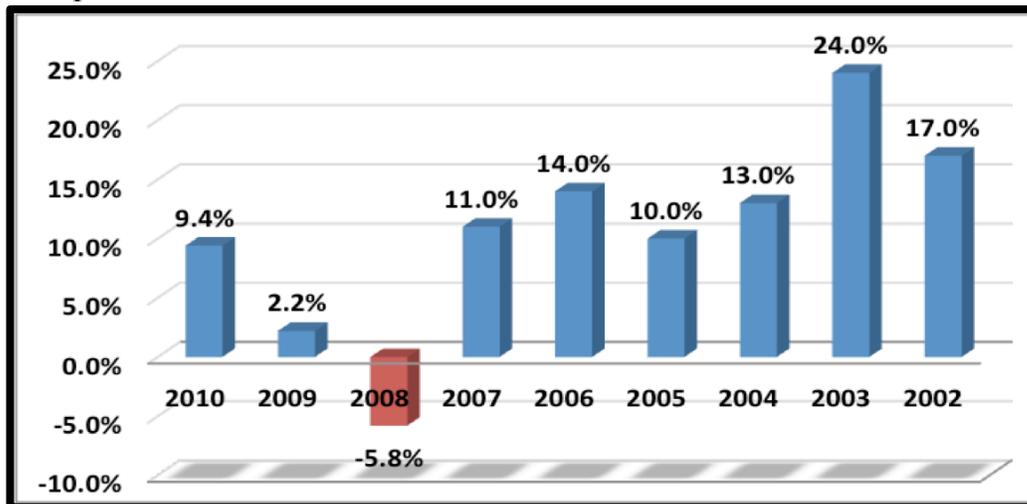
Chipotle's financial success is contingent upon management's continued ability to offer a high quality product that utilizes organic ingredients at a reasonable cost. This strategy subjects the company to market forces that may result in supply challenges as happened in the second quarter of 2010 when supply shortages forced Chipotle to stop serving naturally raised chicken in some markets. While this reduced food and beverage cost as a percentage of revenue, it poses image challenges for a company whose trademark is 'Food with Integrity.' In line with ingredient costs, labor and occupancy costs have also decreased as a percentage of net revenue primarily due the higher average restaurant sales. It should be noted that Chipotle has recently faced increased scrutiny over the immigration status of its workers. Immigration and Customs Enforcement recently notified the company that it would be undertaking an in-depth audit of the company's I-9 forms, which verify employment eligibility. This may result in significantly higher labor costs and/or fines if the company is found to be in violation of federal/state employment laws. The observed decreases in the percentage costs of inputs driven primarily by higher same store sales highlight the importance of Chipotle's continued growth to the continued



success of the company, while their new emphasis on A-model stores has also contributed to this financial success. Moving forward, especially with some increased cost concerns over labor and the possibility of supply challenges makes it all the more important for Chipotle to continue growing to offset these possible worries.

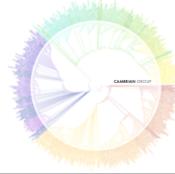
Chipotle's management has also staked the financial viability of the company on an aggressive growth strategy and its two principal elements: an increase in existing same store sales and the continued expansion of stores throughout the United States. Although Chipotle currently has three restaurant locations abroad, with two in Canada and one in the United Kingdom, the Cambrian Group will primarily focus on domestic operations as those data are most readily available. The chart below depicts the growth of sales at comparable restaurants from FY2002 to 2010.

Comparable Restaurant Sales Growth



Source: S&P Stock Report

In addition to the explosive same store growth, expansion has also been a key revenue driver. The company has expanded from 227 stores at the beginning of 2003 to 1,084 at the end of fiscal year 2010. After adding 129 stores in 2010, the company plans to add 135 to 145 new locations in 2011 with about 25-30 percent being lower cost "A-Model" stores which are simply a smaller version that will be explained in more detail later. This expansion strategy translates into about 22 percent compound annual



growth rate (CAGR). In the past, the market has placed a large emphasis on Chipotle's continued ability to grow same store sales while also expanding into new markets as this strategy combines market penetration and saturation strategies. Even through the tough economic environment of the past couple of years Chipotle has expanded their top-line and bottom-line revenue figures at an average annual rate (five-year compound annual growth rate) of 20.95 percent and 41.1 percent, respectively. This suggests that Chipotle's management has an effective job of targeting consumers that are willing to spend on discretionary purchases even in times of financial distress.

Balance Sheet/Income Statement Analysis

Five-Year Sales, Operating and Net Income and Growth

(\$ 1000s)	2010	2009	2008	2007	2006	CAGR
Sales	1,835,922	1,518,417	1,331,968	1,085,782	822,930	
Growth	20.91%	14.00%	22.67%	31.94%		22.38%
Operating Income	287,831	203,705	124,039	108,183	61,952	
Growth	41.30%	64.23%	14.66%	74.62%		48.70%
Net Income	178,981	126,845	78,202	70,563	41,423	
Growth	41.1%	62.2%	10.8%	70.3%		46.1%
<i>Source: Chipotle 10K</i>						

Chipotle's balance sheet and liquidity positions remain strong. Free cash flow, defined as operating cash flow less capital expenditure, has increased from \$152 million in 2009 to \$176 million in 2010. This increase in cash flow has allowed Chipotle to continue their aggressive growth campaign without relying on incremental growth capital, short-term capital infusion, thereby reducing the costs of expansion. Chipotle's capital expenditures have increased to \$113.2 million in 2010 from just over \$48 million in 2002 with the primary use of that capital relating to the construction of new restaurants. It is important to note that the average development and construction costs per restaurant, net of occupancy, have decreased from \$850,000 in 2009 to \$795,000 in 2010. This is primarily due to the utilization of Type A model stores as well as simpler restaurant design.



Funding sources have included the proceeds from the company's January 2006 initial public offering and cash from ongoing operations. As of December 31, 2010, Chipotle had no debt. In addition to a marked decrease in average development costs, Chipotle has leveraged their growth through the economic downturn to seize advantageous contractual terms such as lease agreements and build-out terms.

Since Chipotle operates in an industry in which customers pay using cash or credit and debit cards, there are almost no accounts receivable. In addition to the absence of accounts receivable, the fresh nature of Chipotle's food ingredients has resulted in the absence of any significant inventories further enhancing Chipotle's liquidity position. The company's decision to lease substantially all of their properties, owning only 16 of the 1,084 current locations, represents another aspect of management's overall liquidity strategy. The company uses a variety of lease terms that vary between five to twenty year initial agreements with several five-year extensions depending on location and type of restaurant.

Analysts expect earnings of \$1.43 per share for the most recent Q1 FY2011. This estimate is slightly lower than the \$1.47 earnings per share that Chipotle posted for Q4 FY2010 and implies that profits will be adversely impacted by the anticipated rise in commodity costs. For FY 2011, analysts are generally bullish with respect to earnings per share with a consensus estimate of \$6.74 compared to the reported FY2010 earnings per share of \$5.64. In line with these expectations, analysts see Chipotle's operating margin increasing as same store sales are expected to increase relative to operating costs offsetting the rising cost of food ingredients and other operating costs.

Overall, Chipotle saw increases in almost every major income category. As mentioned before, revenues, operating income, and net income all rose over the previous year. Their continued aggressive expansion in 2010 led to increases in supply costs (20.4% over PY) and labor costs (17.8%) which contributed to total operating costs rising 17.75%. While this does seem like a high number their total revenues rose by the aforementioned 20.9% which contributed to an increase in net income as well as their margins. Since Chipotle's revenues come exclusively from their restaurants' sales they don't break total revenues down.



Stock Performance Analysis

Five-Year Stock Performance: Chipotle vs. Panera Bread, Yum! Brands, and S&P 500



Source: Google Finance

Chipotle's stock price is currently trading at \$269.64 down from its yearly high of \$278 that was reached in April 2011. The share price decline is largely attributable to the recent correction seen in world equity markets and may also be attributable to ongoing concerns of rising input costs for Chipotle. While analysts are mixed on the stock, when the Cambrian Group applies a price to earnings estimate of 31 times, the average of trailing twelve months high and low price to earning ratios, to consensus FY 2011 earnings per share estimate of \$6.74 we have a target price of \$208.94. This indicates that the equity may be overvalued as it is currently trading at a price to earnings multiple of 47.80X as calculated from the trailing twelve months of earnings as reported by S&P.



COMPETITIVE ANALYSIS

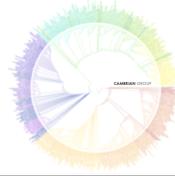
Force	Strategic Impact
Internal Rivalry	High
Buyer Power	Moderate
Supplier Power	Moderate
Entry	Low
Substitutes and Compliments	High

Under the Standard Industrial Classification system, fast casual restaurants fall into the category of Eating Places, code 5812. Under the NAICS definitions, fast-casual restaurants would be considered a limited service restaurant, code 722211. This category is part of the larger industry category of Accommodation and Food Services.

Internal Rivalry

Chipotle operates in a highly competitive industry, in which they compete both with other fast casual restaurants, as well as less directly with fast food restaurants and casual-dining chains.

In the sub-category for fast-casual Mexican restaurants, Chipotle competes with Qdoba, Moe's Southwest Grill, Baja Fresh, and El Pollo Loco. Many of these competitors have been attracted by Chipotles success in the industry. Fast-casual Mexican restaurants account for close to \$5 billion of the \$20 billion fast casual market. Chipotle is the largest player in the fast casual Mexican category, with \$1.8 billion in sales last year, and along with Panera Bread and Panda Express is one of the largest companies for fast casual restaurants. Other examples of restaurants in the fast casual category include Benihana Inc., California Pizza Kitchen and P.F. Chang's China Bistro.



Chipotle also competes within the larger market for fast food restaurants. While the company's focus on higher quality ingredients differentiates it from many of the other fast food restaurants, many of the fast-food chains, including McDonalds are increasingly focusing on healthier and higher quality food. In addition, many other fast food restaurant chains are looking to improve the quality of their food and restaurant décor. At the same time, there has been a push in the fast-casual market towards keeping prices low and providing better value to consumers. These two forces serve to bring Chipotle and other fast-casual restaurants in more direct competition with the larger fast-food chains. In this larger industry, Chipotle is a much smaller player, with a market cap of just over \$8.2 billion, about one tenth the size of the largest company in the industry, McDonald's Corp.

Chipotle has recently opened a store in London. This market will likely have much less internal rivalry than in the domestic market. In this region, Mexican food is much rarer, which gives their product an advantage. Chipotle's new Asian-themed restaurant chain will operate within the fast-casual category. This will make their most direct competition other fast-casual Asian restaurants, such as Panda Express.

The company's store-by-store sales are helped by the fact that the market is not fully saturated with Chipotle branches. Chipotle does not franchise their stores, making them an anomaly in the industry. Currently, Chipotle operates just over 1000 stores domestically. In its most popular markets, namely Denver, Cincinnati, Columbus and Cleveland, Chipotle has achieved a density of one restaurant for every 50,000 residents. It is estimated that if a similar density could be supported across the country, Chipotle could profitably operate up to 3,000 locations. Some analysts place this number as high as 3,500 domestic locations. As market saturation rises, average restaurant sales will fall. While more bullish analysts are confident that the domestic market is capable of supporting a significant increase in the number of branches, others feel that Chipotle is already close to saturating the market.

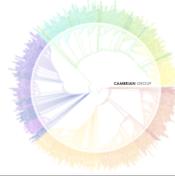


Supplier Power

Chipotle's tag line is 'Food With Integrity.' This refers to the fact that all their ingredients come from sustainable sources, and they use, "organic and local produce when practical," "dairy from cows raised without the use of synthetic hormones," and whenever possible use, "meat from animals raised without the use of antibiotics or added hormones." Since 2001, Chipotle has sourced 100% of their pork from producers who feed the pigs vegetarian diets, give them no antibiotics, and provide adequate living space. 85% of the beef the restaurant uses meets these same naturally raised standards, and they're attempting to bring this up to 100%. Finally, 100% of the chickens they use are raised without antibiotics or other additives.

Chipotle finds suppliers for their ingredients market-by-market and ingredient-by-ingredient. When available in a given location, they look for local, organic and family farmed ingredients. This past year, Chipotle committed, "To serve at least 50% of at least one produce item from local farms when it is seasonally available." While this commitment to naturally raised and sustainable ingredients provides a way for the company to differentiate itself from its peers, it creates a larger degree of supplier power that that faced by others in the industry, since Chipotle can only draw from a much smaller pool of suppliers. As a result, Chipotle has less ability to control the price of its inputs, and subsequently pays more for inputs in some regions than in others.

Since there are a limited number of suppliers of ingredients that meet Chipotle's standards, the potential for food shortages presents a serious risk. This substantial business risk gives further power to their suppliers to set prices. Chipotle as part of their 'Food With Integrity' movement have tried to source from smaller family farms and make sure to personally meet all of their suppliers. They communicate to make sure that Chipotle's standards for their ingredients are being upheld. In the past they've made voluntary concessions to farmer's in order to improve working conditions and to make sure that the growing methods are organic and sustainable. Because of Chipotle's size they are a major buyer of ingredients and especially with their penchant for finding family farms as sources their buying represents a



large portion of many of these farms' business and so they do wield a significant amount of power with their suppliers. There remain possible volatility issues with supply because of the smaller pool of suitable suppliers but because of Chipotle's high quantity buying and methodology for finding suppliers Chipotle influences its suppliers much more than vice versa.

Buyer Power

Consumers of fast-casual and fast food restaurants have a large degree of buyer power. Switching costs in the industry are non-existent. Further, most of the domestic market is highly saturated with comparable restaurant options. As a result, individual stores cannot rely on Hotelling's law to provide customers but must actively attract consumers. In addition, a meal at a restaurant is a discretionary good, since consumers always have the option of cooking at home. Chipotle's business model of healthy food and environmental sustainability attracts a niche of customers who would not readily substitute away to other fast-food chains.

While the large number of readily available substitutes creates buyer power, the large number of potential consumers reduces buyer power. The companies' profits are the result of high volume, and so no individual consumer has much buyer power.

Entry

There are relatively low barriers to entry in the restaurant industry. Little specialized equipment is necessary and relatively low capital requirements mean that there will be a constant inflow of entrants to the market. In fact, Chipotle holds virtually no debt, further attesting to the low capital requirements in this industry. Despite this, Chipotle has competitive advantages in several areas that serve to create an economic moat. The most notable of these come from Chipotle's status as the largest fast-casual Mexican restaurant chain, providing benefits from economies of scale. The greatest benefit of their size is Chipotle's brand recognition and brand image. The name and uniform store architecture create this brand



recognition and hopefully also brand loyalty, even in the absence of direct advertising.

Interestingly, in 2010, Chipotle announced that they were moving away from traditional advertising. Over the past five years, Chipotle has employed four different advertising agencies. Chipotle has decided to bring all advertising in house, and rely primarily on word-of-mouth promotions. According to Chipotle's chief marketing officer, "the chain hasn't added a menu item in 17 years and it also does not have a regular cadence of pricing promotions. For those reasons, he said, agencies' experience with other fast food chains is irrelevant." The data supports this assertion that Chipotle's advertising had been largely ineffective. Part of the problem was that the company spent less than \$10 million a year on advertising, which is quite small for a chain of their size. However, the advertising that they did was less effective than that of their peers. McDonalds, a notoriously successful advertiser, got 20% more sales revenue per dollar spent on advertising compared to Chipotle.

Chipotle's relative size in the industry allows them to rely on word of mouth advertising, instead of more traditional means of advertising. Further, their large number of stores in high traffic areas effectively serves to market the entire chain, not just the individual location.

Since Chipotle is attempting to expand their primary chain internationally as well as open a new Asian-themed restaurant chain, they must understand the barriers to entry in these new markets. The brand has considerably less recognition abroad than it does domestically. The companies' size allows it to support international expansion even if it is not initially profitable. For international expansions, the companies' challenge will be to publicize their business model in a new location. The main challenge for entering the fast-casual Asian restaurant market is to effectively publicize the new brand in a market dominated by highly recognizable chains such as Panda Express.

Substitutes And Compliments

The high degree of internal rivalry stems from the wide availability of substitutes. For a certain portion of consumers, those interested



exclusively in fast-casual Mexican food, the available substitutes for Chipotle include Qdoba and Baja Fresh. To the larger group of consumers interested just in fast-casual food, the number of available substitutes rises, and now includes Panera Bread and Panda Express among others. Finally, for the most inclusive group of consumers, those interested in either fast-casual or quick-service restaurants, the number of substitutes increases substantially. Finally, there is the demographic for consumers interested in any sort of Mexican food, for which Chipotle competes with the other fast-casual Mexican restaurants as well as with companies such as Taco Bell. Similarly, Chipotle's new Asian-themed restaurants are a direct substitute for restaurants such as Panda Express and P.F. Chang's. In addition, there are far fewer direct substitutes in the European market.

Further, all consumers in the industry can substitute away from restaurant food to cooking their own food. The degree of substitution towards home cooked food is driven largely by macroeconomic factors, such as overall consumer spending. Compliments for Chipotle are any nearby stores that attract potential consumers to the area. Many branches are located in shopping malls where there is high foot traffic.

SWOT ANALYSIS

Strengths

- Strong brand name, image, and loyalty
 - Current customers continue coming back
 - Promotions/advertising support trendy image
 - Rapid expansion across United States and starting into Europe
 - Plans to open 135+ stores in 2011 after opening 100+ in 2010
 - Largest chain in industry with over 1,000 stores
 - Almost double the size of next competitor
 - Owns all locations
 - Very strong balance sheet (high cash/debt ratio)
 - Extensive supply network
 - Amicable relationship with suppliers
 - 'Food with Integrity' initiative
 - Sustainability very popular societal movement
-



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- First mover advantage
 - Pioneered Mexican fast-casual industry
 - Distinctive restaurant environment
 - Design and décor are unique
 - Bags and cups have messages/stories about Chipotle

Weaknesses

- Competitors have wider variety of menu options
 - Chipotle is limited in its variety of food options
- Slowing of revenue/store growth
 - Revenues per store have somewhat plateaued in past several years
- Competitors have nutrition information available online
- Questionable hiring practices
 - Recent audits could lead to lawsuits

Opportunities

- Ability to invest in expansion
 - Over \$300 million in cash
 - Very low debt/liabilities
- Expansion into European market
 - Plans to move into Paris in 2011 and Munich also a target
- Increase variety of options
 - Healthier choices, smaller portions
- Continue 'Food with Integrity'
 - Increase awareness
- Asian fast-casual restaurant concept
 - New style would benefit from Chipotle's expertise and supply network

Threats

- Current reliance on US market
 - Very exposed to US consumer tastes
 - Nutrition value concerns
-



-
- Nutritional information not readily available
 - High calorie food
 - Possible overexpansion
 - CMG is very ambitious with new store plans
 - Supply Issues
 - Amicable relationship now but Chipotle has given in to demands previously which could lead to further issues because of 'Food with Integrity'
 - Prices
 - 'Food with Integrity' movement could lead to higher supply costs and move food prices above competitors



PART III

RECOMMENDATIONS

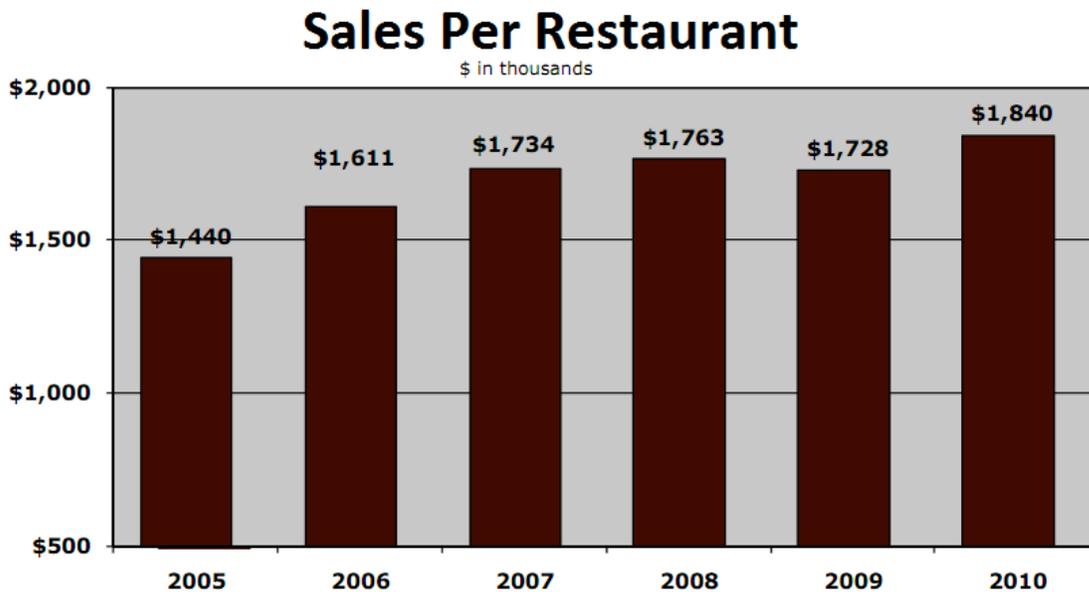


STRATEGIC RECOMMENDATIONS

1. Focus on US expansion with focus on A-model, continue slow entrance into Europe
2. Tighten up hiring policies
3. Increase awareness of 'Food With integrity'

Continued Expansion

Chipotle Mexican Grill now operates over 1,080 stores in 38 states and Washington DC within the United States. They have expanded fiscally responsibly by using revenues from current stores instead of utilizing possibly costly means of debt. Even with Chipotle's rapid expansion in the past several years, CMG was listed as the 8th fastest growing company in 2009 and moved up to 3rd in 2010; the chain has not seen significant dips in revenue per store as evidenced by the following chart. In fact, they saw a



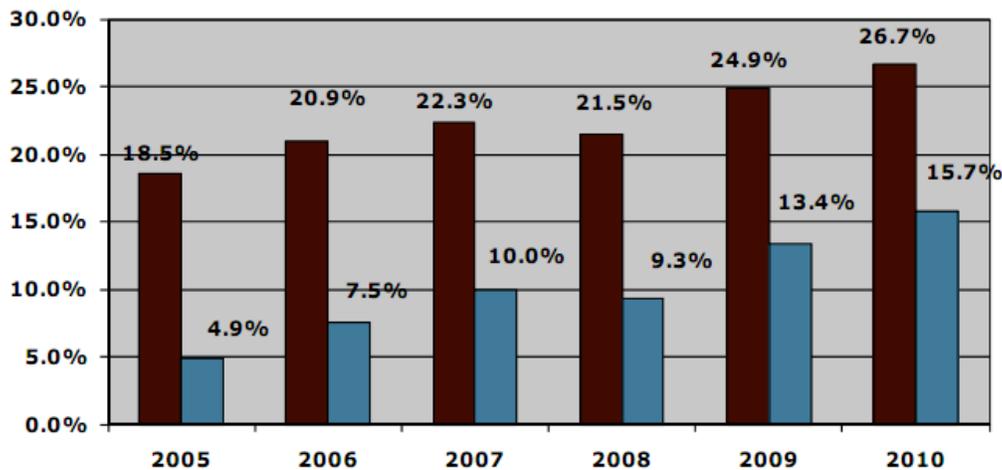
Source: Chipotle Investor Conference 1

6.5% rise from 2009 to 2010 after a brief dip the previous year. On top of this, Chipotle's restaurant level, as well as company level, margins



increased for the third straight year as shown in the following graphic. These signs point to the fact that even though Chipotle operates so many stores in the United States, that the marginal stores being opened are at least as profitable as the existing set of Chipotle locations.

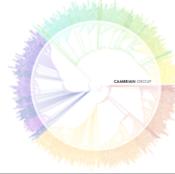
Restaurant and Company Level Margins



Source: Chipotle Investor Conference 2

The reason that Chipotle has enjoyed this success is for multiple reasons. First, Chipotle is in very high demand with over 750,000 customers per day. This demand can easily support more stores within the US especially considering that CMG can still expand geographically within the US so as not to hurt revenues of existing stores. The second reason that Chipotle has had increased success recently is its emphasis on what it calls its “A-Model” stores. Chipotle’s A-model is simply a smaller restaurant design. It lowers development costs from \$850,000 to \$700,000 while still supporting the same volume as a typical Chipotle restaurant. This also leads to lower occupancy costs and the smaller restaurants are more energy efficient. In 2010 roughly 25% of new locations were of the A-model and Chipotle looks to bump that up to at least 30% of new stores in 2011. Co-CEO Montgomery Moran believes that with just a couple years of sales increases the A Model strategy could generate cash-on-cash returns of more than 50%.

Chipotle should continue its very prosperous expansion in the United States. They still have room to expand into its current geographic areas as



well as moving into new areas that are currently unserved by Chipotle. With this expansion Chipotle should continue and expand its A-Model buildings. Serving the same demand at a much lower cost has really helped Chipotle not only maintain its margins and revenues per store but actually increase them.

In 2010 Chipotle opened its first store outside of North America in London, England. So far the location has been a great success and CMG already has plans to open a location in Paris later this year. After achieving initial success Chipotle should be careful not to expand too quickly in Europe as demand there would likely not be as high as it is in the United States, but this is not a concern as of yet. It should be noted that, while initially successful, Chipotle should make sure to not lose focus on its domestic market. It seems as though Europe is a viable market for the US, albeit at probably reduced density, but Chipotle's principal market is the United States and it should be sure to not lose focus on completing its expansion in the US before moving abroad.

Chipotle's expansion into Europe should be eased by the cultural awareness of Europeans. Europeans are much more aware of the origins of their food and so much of the farming and ranching is more sustainable and fits Chipotle's 'Food With Integrity' initiative very well. Sustainable, hormone-free growing is much more common in the EU and so CMG would have a much easier time securing suitable ingredients.

As mentioned, Chipotle needs to continue its expansion in the US. It has achieved great success and is still increasing its margins even with this aggressive expansion. The increased use of the A-model has proven successful and should be expanded. At present, Chipotle is enjoying initial success expanding into Europe and CEO Steve Eells is considering opening a similar fast-casual Asian style restaurant. While these endeavors may be in the long term benefit of Chipotle they should not distract from domestic expansion now. Over 99.7% of Chipotle's stores are in the US and that is where Chipotle's, and co-CEO Steve Eells', focus should remain until they deem their expansion in the USA to be completed.



Hiring Policies

Recently, Chipotle's hiring practices have come under close scrutiny. In 2010, the Immigration and Customs Enforcement agency started investigating the legal status of immigrant Chipotle workers in Minnesota and Wisconsin. This led to 450 illegal immigrant workers being fired in Minnesota which represents almost 40% of their workforce. Now, the ICE has announced and begun investigating all of Chipotle's stores in Virginia and Washington DC. While these investigations do not represent a significant portion of Chipotle's 1,084 restaurants nor has it happened in a high profile location yet but these investigations and subsequent firings do embody a very troubling concern should the ICE's inquiry continue and expand to a national level, especially considering how accurate these allegations have been thus far.

Chipotle has been known as a company that keeps labor costs very low and this will obviously change that. There is really no reason that Chipotle needs to try and circumvent the law in order to keep costs low though. They already have practices in place to place recent transplants to the US in their workforce as well as a whole team devoted to bringing employees from different cultural and linguistic backgrounds together. They even have an English education program offered to all employees who request it. They need to expand these offerings and even help possible employees gain the legal right to work and live in the United States. Over the past three years they have seen their profits rise by great amounts and their margins have increased as well. With other new profitability measures, such as the A-Model, in place Chipotle needs to clean up their hiring practices and make sure that workers are legal to be working in the United States. The current system is too risky and is frankly unnecessary at this point in Chipotle's development. Changing their employee hiring practice will most likely lead to higher costs in terms of switching as well as higher wages but Chipotle is a very profitable company with very high margins and changing their workforce over to legal workers would be less costly than continued legal trouble from these investigations and Chipotle's margins can absorb the elevated costs.



Food With Integrity

Chipotle's movement called 'Food With Integrity' is a major part of their business model. It is Steve Ells' ideological view that all ingredients in the food we eat should be raised naturally with respect for the animals, environment, and the farmers. This means supporting family farmers who grow crops and animals sustainably and also attempting to reduce the amount of antibiotics, hormones, and other chemicals used in the raising of Chipotle's ingredients. Chipotle also makes this stand with produce meaning buying local, organically grown produce whenever possible. Chipotle started this idea more than a decade ago and there is no end in sight. Currently, 100% of pork is naturally raised without antibiotics, fed a vegetarian diet, and live outside or in deeply bedded pens. Also, 85% of their beef is naturally raised as well as over 35% of their dairy products coming from pasture-raised cows. 40% of their beans are grown certified organic which may not sound like a lot, but this alone reduces the amount of chemical pesticides by 110,000 pounds per year.

This 'Food With Integrity' movement even extends to the farmers themselves. Chipotle has policies in place to make sure that none of the ingredients they buy come at the cost of exploiting people in the supply process. They also try to buy from family farms whenever possible because of the belief that family-owned farms are run more sustainably because they depend on the land that they own for their continued livelihood. This sustainability motive also leads Chipotle to use as much local food as possible so as to reduce the overall carbon footprint of their ingredients. Overall, Chipotle has a close, personal relationship with suppliers that many other restaurants do not. CMG meets and converses with each of its suppliers to make sure that Chipotle's 'Food With Integrity' guidelines are being followed as closely as possible.

While many people have heard of Chipotle's 'Food With Integrity' ideology, most don't know the extent to which it permeates Chipotle's business. With climate change a serious issue, Chipotle's emphasis on sustainable, organic, and local food supply is a major cultural anomaly in the restaurant, and especially fast food, industry. Many chains look to cut costs in any way possible such as buying inhumanely raised meat from major factory farms



that use all sorts of hormones, antibiotics, and other chemicals in the raising of produce and animal products. This ‘Food With Integrity’ initiative is a major differentiating factor for Chipotle versus its competitors in the industry, especially given the recent ingredients scandals at Taco Bell.

Chipotle is very much in line with a strong societal movement towards sustainability but Chipotle doesn’t advertise this enough. CMG should start an advertising campaign highlighting their efforts to save the family farm and inform the general public about what actually goes in to the food they are eating along with the starkly different methods that Chipotle uses. Chipotle even agreed to pay more for their tomatoes simply to improve the working conditions of tomato farm workers. Aligning them with this powerful and seemingly long-lasting cultural drive and informing the general public the extent to which Chipotle is willing to go for this philosophy would greatly increase brand loyalty and secure more customers away from other large chains.



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