

Famous Dave's of America Inc.

Restaurants July 29, 2011

Company Description: Famous Dave's owns, operates and franchises BBQ centered casual dining restaurants. The company currently operates 52 restaurants while franchisees operate 129 units in 37 states. The restaurants offer a variety of barbeque items such as ribs, brisket, chopped pork, roasted chicken, sandwiches, sides and desserts. The company was founded in 1994 and is headquartered in Minnetonka, Minnesota.

2Q:11 results inline, disappointing outlook leads us to lower estimates

(DAVE - \$10.16) HOLD

Key Points

- Famous Dave's (DAVE) reported 2Q:11 results inline with our estimates.

	2Q:11 Actual	2Q:11 Estimate	Variance	2Q:10 Actual	YOY % Change
Total Revenue	\$41,290	\$40,961	0.8%	\$40,749	1.3%
Gross Profit	\$9,560	\$9,564	0.0%	\$9,492	0.7%
Operating Income	\$3,942	\$4,066	-3.0%	\$4,147	-4.9%
Net Income	\$2,415	\$2,497	-3.3%	\$2,543	-5.0%
Diluted EPS	\$0.30	\$0.30	\$0.00	\$0.29	\$0.01

- Same-store sales were mixed with company comps declining (1.2%) versus our (0.7%) estimate while franchised comps declined (1.4%), better than our (3.3%) estimate. Revenue of \$41.3mm was slightly better than our \$41.0mm estimate.
- Restaurant operating margin was 13.1% in 2Q:11 compared to our 13.4% estimate. Restaurant operating expenses increased 77 bps year over year. We think more should be done to contain restaurant operating expenses. Additionally, although food costs are currently contained with guidance for annual savings this year, we think 2012 could be problematic as contracts expire.
- Operating income of \$3.9mm missed our \$4.1mm estimate due to higher G&A expense. We view G&A expense rising faster than revenue growth unfavorably especially given the company-operated restaurant count is flat year over year.
- Management guided to fewer franchise restaurant openings this year. Management lowered the franchise-operated opening guidance from 9-11 units to 8 new units. Although we think the decline is largely due to timing delays, we are concerned with slower unit growth.
- We are lowering our 2011 and 2012 earnings estimates to \$0.69 and \$0.82, respectively, from \$0.73 and \$0.87.
- We are maintaining our HOLD rating and \$11.50 price target. Excluding the impact of share repurchases we think DAVE will have difficulty producing earnings growth in 2011 and early 2012 (we model flat EPS for the next three quarters with declining net income). We do not see sufficient upside to our target to recommend the shares, but would turn more positive if the company locked in food costs at lower costs than we expect, same-store sales growth accelerated or if the shares traded closer to \$9 with no change in fundamentals.

Financial Summary

Rev(mil)	2010A	2011E	2012E
Mar	\$32.6	\$37.1A	\$38.6E
Jun	\$40.7	\$41.3A	\$45.0E
Sep	\$38.7	\$38.3E	\$42.2E
Dec	\$36.2	\$36.6E	\$39.5E
FY	\$148.3	\$153.3E	\$165.3E
P/Sales	0.55x	0.53x	0.50x

EPS	2010A	2011E	2012E
Mar	\$0.14	\$0.16A	\$0.16E
Jun	\$0.29	\$0.30A	\$0.34E
Sep	\$0.17	\$0.17E	\$0.21E
Dec	\$0.07	\$0.07E	\$0.12E
FY	\$0.68	\$0.69E	\$0.82E
P/E	14.9x	14.7x	12.4x

Price:	\$10.16
52-Week Range:	\$12.20-\$7.86
Target:	\$11.50
Rating:	HOLD

Shares Outstanding:	8.1 mil
Mkt. Capitalization:	\$82 mil
Ave. Volume:	18,100
Instit. Ownership:	45%
BV / Share:	\$4.32
Debt / Tot. Cap.:	42%
Est. LT EPS Growth:	15%

DAVE's 2Q:11 results were roughly inline with our expectations. Revenue of \$41.3mm was slightly above our \$41.0mm estimate while net income of \$2.4mm was slightly below our \$2.5mm estimate. EPS of \$0.30 was inline with our estimate and above consensus of \$0.28. Restaurant operating margins of 13.1% were below our 13.4% estimate primarily due to higher restaurant operating expenses. We note that restaurant operating expenses have increased as a percent of sales every year since 2004 with guidance for a 45-50 bps increase this year. From 2007 through expected 2011 results, restaurant operating expenses have increased 250 basis points and account for nearly the entire 290 bps decline in restaurant operating margin during this period. We think that more should be done to contain these expenses. We note that food and beverage expense is expected to be slightly favorable in 2011 as a percent of sales, but we are concerned that new contracts later this year could be very unfavorable to 2012 margin. Concerning operating expenses, G&A expense of \$4.2mm was above our \$4.0mm estimate leading to operating income of \$3.9mm, below our \$4.1mm estimate. Net income of \$2.4mm was slightly below our \$2.5mm estimate, but EPS of \$0.30 was inline with our estimate due to a lower share count.

We are reducing our 2011 and 2012 earnings estimates. We are reducing our 2011 revenue estimate slightly to \$153.3mm from \$153.9mm due to expectations of lower company-operated same-store sales, but we are raising our 2012 revenue estimate to \$165.3mm from \$163.9mm. Management indicated the company will open two new company-operated restaurants in 2H:11 and one early in 2012. This was higher than our previous estimates for new company-operated restaurant openings and will lead to higher revenue. We think the new company-operated openings will impede near-term earnings due to pre-opening expense and prefer growth through franchisees. We are encouraged by management's plan to open a smaller-footprint, conversion unit that will operate as a counter service restaurant rather than full service. We think the unit economics could be very attractive in this platform as revenue is assumed to be lower than the system average, but higher margins and a very low cash investment could lead to cash on cash returns in excess of 30%. We don't expect this restaurant to "move the needle" on the company's earnings, but think it gives franchisees a new platform for future growth that may offer attractive returns and a lower barrier to entry given the low investment. Management reduced its opening guidance for franchise-operated restaurants in 2011 to 8 restaurants from 9-11 new openings. We think the reduction in guidance is primarily due to the timing of openings sliding into 2012, but would take a very unfavorable view on franchisees opting out of building new restaurants. We adjusted our 2H:11 estimates for management's line-by-line expense guidance and remain concerned regarding restaurant operating expenses in 2011 and potential increases to food and beverage expense in 2012 when the company re-prices its commodity contracts. We are lowering our 2011 and 2012 EPS estimates to \$0.69 and \$0.82, respectively, from \$0.73 and \$0.87. We note that we expect flat year-over-year EPS for the next three quarters with a slight decline in net income.

Investment Thesis

We are maintaining our HOLD rating and \$11.50 price target. Although 2Q:11 results were inline with our estimates, we are maintaining our HOLD rating given our outlook for the next 12 months. We model modest earnings growth over the next 12 months and think the company will continue to face headwinds from the macro-economic environment. We are maintaining our \$11.50 price target despite our lower expectations for earnings. We derive our \$11.50 price target by applying a 14x multiple to our new 2012 EPS estimate of \$0.82. We previously valued the shares at 13x our prior 2012 estimate of \$0.87. We think a 14x multiple is warranted given trading multiples of DAVE's casual dining peers and DAVE's highly franchised restaurant base (71%) which produces strong cash flow and typically has lower risk. With limited upside to our target and no catalyst for near-term earnings growth, we are maintaining our HOLD rating. We would turn more positive if sales improve more than we anticipate, the company is able to reduce operating expenses or if the shares traded closer to \$9 with no change in fundamentals.

Famous Dave's of America, Inc. Income Statement
 (Dollars in thousands, except where noted)

	2009	Mar	Jun	Sept	Dec	2010	MarA	JunA	Sept	Dec	2011E	Mar	Jun	Sept	Dec	2012E
Revenue																
Restaurant revenue	\$117,934	\$28,393	\$36,213	\$34,313	\$32,235	\$131,154	\$32,741	\$36,504	\$33,911	\$32,402	\$135,557	\$33,868	\$39,809	\$37,303	\$34,958	\$145,939
Franchise revenue	17,112	4,022	4,264	4,157	3,804	16,247	4,069	4,511	4,189	3,966	16,735	4,490	4,902	4,613	4,333	18,338
Licensing revenue	972	184	272	233	178	867	280	275	240	225	1,020	285	270	265	250	1,070
Total revenue	136,018	32,599	40,749	38,703	36,217	148,268	37,090	41,290	38,340	36,593	153,313	38,644	44,981	42,182	39,541	165,347
year-over-year % change	-3.1%	-3.5%	12.2%	16.2%	11.1%	9.0%	13.8%	1.3%	-0.9%	1.0%	3.4%	4.2%	8.9%	10.0%	8.1%	7.8%
Costs and expenses																
Restaurant expenses																
Food and beverage costs	35,489	8,327	10,617	10,177	9,633	38,754	9,653	10,632	9,902	9,494	39,681	9,957	11,696	10,967	10,260	42,881
Labor and benefits	37,016	9,249	11,024	10,944	10,135	41,352	10,437	11,124	10,818	10,433	42,812	10,855	12,162	11,806	11,134	45,957
Operating expenses	31,487	7,628	9,616	9,475	9,388	36,107	9,074	9,974	9,427	9,461	37,936	9,449	10,729	10,277	10,173	40,628
Total costs and expenses	103,992	25,204	31,257	30,596	29,156	116,213	29,164	31,730	30,147	29,388	120,429	30,261	34,586	33,051	31,567	129,465
Gross profit	32,026	7,395	9,492	8,107	7,061	32,055	7,926	9,560	8,193	7,205	32,884	8,382	10,395	9,131	7,974	35,882
Gross margin	23.5%	22.7%	23.3%	20.9%	19.5%	21.6%	21.4%	23.2%	21.4%	19.7%	21.4%	21.7%	23.1%	21.6%	20.2%	21.7%
Depreciation and amortization	5,191	1,292	1,377	1,401	1,477	5,547	1,375	1,375	1,425	1,510	5,685	1,575	1,610	1,675	1,725	6,585
Pre-opening expenses	0	27	54	219	0	300	0	45	245	275	565	195	65	215	125	600
General and administrative expenses	16,079	3,811	3,914	4,027	4,412	16,164	4,324	4,198	4,160	4,318	17,000	4,444	4,386	4,492	4,488	17,810
% of revenue	11.8%	11.7%	9.6%	10.4%	12.2%	10.9%	11.7%	10.2%	10.9%	11.8%	11.1%	11.5%	9.8%	10.7%	11.4%	10.8%
Total operating expenses	21,270	5,130	5,345	5,647	5,889	22,011	5,699	5,618	5,830	6,103	23,250	6,214	6,061	6,382	6,338	24,995
Operating income	10,756	2,265	4,147	2,460	1,172	10,044	2,227	3,942	2,363	1,102	9,634	2,168	4,334	2,749	1,636	10,887
Operating margin	7.9%	6.9%	10.2%	6.4%	3.2%	6.8%	6.0%	9.5%	6.2%	3.0%	6.3%	5.6%	9.6%	6.5%	4.1%	6.6%
Interest income (expense)	(1,314)	(261)	(242)	(219)	(247)	(969)	(273)	(274)	(250)	(230)	(1,027)	(225)	(200)	(190)	(165)	(780)
Other income (expense)	(1)	7	(12)	(8)	12	(1)	8	(8)	0	0	0	0	0	0	0	0
Gain (loss) from nonrecurring items	(751)	2,110	(10)	(16)	(144)	1,940	(172)	(10)	0	0	(193)	0	0	0	0	0
Pretax income	8,690	4,121	3,883	2,217	793	11,014	1,790	3,639	2,113	872	8,414	1,943	4,134	2,559	1,471	10,107
Pretax margin	6.4%	12.6%	9.5%	5.7%	2.2%	7.4%	4.8%	8.8%	5.5%	2.4%	5.5%	5.0%	9.2%	6.1%	3.7%	6.1%
Income tax expense (benefit)	2,989	1,414	1,347	759	276	3,796	608	1,238	719	296	2,861	661	1,406	870	500	3,436
% of pretax income	34.4%	34.3%	34.7%	34.2%	34.8%	34.5%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%
Net income (excl. nonrecurring items)	6,189	1,321	2,543	1,469	611	5,947	1,296	2,415	1,395	575	5,680	1,283	2,728	1,689	971	6,671
Net income (GAAP)	5,701	2,707	2,536	1,458	517	7,218	1,182	2,401	1,395	575	5,553	1,283	2,728	1,689	971	6,671
EPS	0.67	0.14	0.29	0.17	0.07	0.68	0.16	0.30	0.17	0.07	0.69	0.16	0.34	0.21	0.12	0.82
EPS (GAAP)	0.62	0.30	0.29	0.17	0.06	0.82	0.14	0.29	0.17	0.07	0.68	0.16	0.34	0.21	0.12	0.82
EPS growth rate	31.4%	-6.7%	11.5%	0.0%	-22.2%	1.5%	14.3%	3.4%	0.0%	0.0%	1.5%	0.0%	13.3%	23.5%	71.4%	18.8%
Diluted shares	9,211	9,162	8,810	8,631	8,535	8,784	8,302	8,183	8,155	8,130	8,193	8,150	8,125	8,150	8,100	8,131
Number of restaurants period end:																
Company-owned (incl joint venture)	45	52	52	53	52	52	52	52	53	54	54	55	55	56	56	56
Franchised	132	123	125	126	130	130	130	129	130	133	133	136	137	138	141	141
Total	177	175	177	179	182	182	182	181	183	187	187	191	192	194	197	197
Same-store sales (yoy pct. chg.):																
Company-owned	-6.3%	-3.5%	0.6%	2.4%	3.3%	0.7%	3.0%	-1.2%	-1.7%	-1.9%	-0.5%	-1.4%	2.5%	2.7%	2.6%	1.6%
Franchised	-8.5%	-3.4%	-0.6%	0.7%	-0.8%	-0.8%	-0.1%	-1.4%	-1.9%	0.1%	-0.8%	0.9%	2.5%	2.7%	1.0%	1.8%
EBITDA	15,947	3,557	5,524	3,861	2,649	15,591	3,602	5,317	3,788	2,612	15,319	3,743	5,944	4,424	3,361	17,472

Analyst Certification

I, **Mark E. Smith**, certify that the views expressed in this research report accurately reflect my personal views about the subject company and its securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation related to the specific recommendations expressed in this report.

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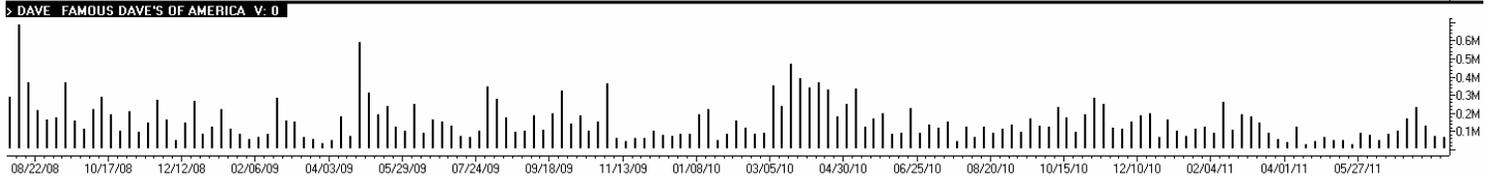
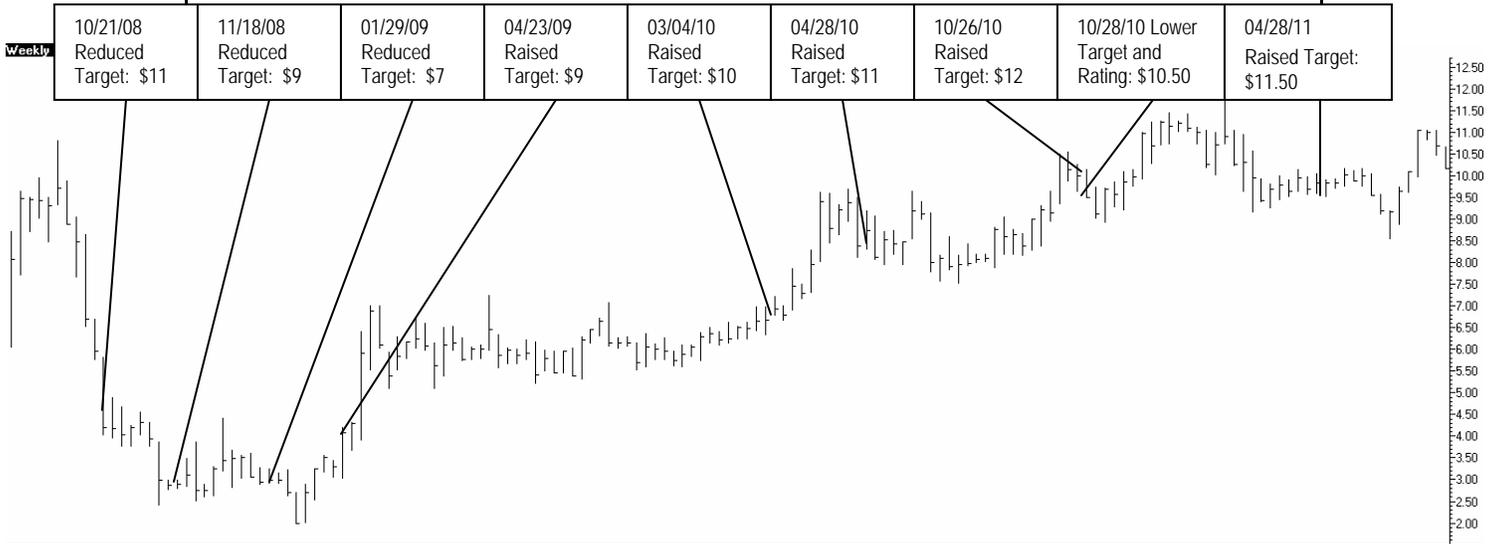
Sell: Expect a negative total return. Current positions may be used as a source of funds.

7/29/2011

Ratings Distribution for Feltl and Company

Rating	Investment Banking		Investment Banking	
	Number of Stocks	Percent of Total	Number of Stocks	Percent of Rating category
SB/Buy	40	67%	3	8%
Hold	20	33%	0	0%
Sell	0	0%	0	0%
	60	100%	3	5%

The above represents our ratings distribution on the stocks in the Feltl and Company research universe, together with the number in (and percentage of) each category for which Feltl and Company provided investment-banking services in the previous twelve months.



Date	Nature of Report	Rating	Price Target
05/30/07	Initiation @ \$20.13	Buy	\$26
01/24/08	Estimates and Target Reduced	Buy	\$19
04/16/08	Estimates and Target Reduced	Buy	\$16
04/24/08	Estimates and Target Reduced	Buy	\$15
10/21/08	Estimates and Target Reduced	Buy	\$11
11/18/08	Estimates and Target Reduced	Buy	\$9
01/29/09	Estimates and Target Reduced	Buy	\$7
04/23/09	Rating, Estimates and Target Raised	Strong Buy	\$9
03/04/10	Target Raised	Strong Buy	\$10
04/28/10	Target Raised	Strong Buy	\$11
10/26/10	Target Raised	Strong Buy	\$12
10/28/10	Estimates, Target and Rating Reduced	Hold	\$10.50
04/28/11	Target Raised	Hold	\$11.50

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Valuation and Price Target Methodology:

We derive our \$11.50 price target by applying a 14x multiple to our 2012 EPS estimate of \$0.82.

Risks to Achievement of Estimates and Price Target:

- Famous Dave's business may be impacted by consumers' discretionary spending and confidence. Macroeconomic factors such as increasing gasoline prices, unemployment and generally tough economic times may negatively impact consumers' restaurant spending. Changing customer tastes could also have a negative impact on sales.
- Severe weather may slow sales at the restaurants as customers and staff may not be able to travel to the restaurant, or customers may choose not to eat out due to inclement weather. The catering business may face more volatility due to inclement weather in summer months.
- Volatile commodity prices may affect earnings. DAVE's diversified menu exposes it to a variety of commodities, but may decrease the risks due to menu changes that are beneficial. Food and beverage costs are approximately 30% of restaurant revenue, and we think the company's largest commodity exposures are pork, chicken and beef. Approximately 85% of food costs are under contract which should, in our view, decrease risk. We project commodity price volatility to come primarily from high corn prices, disease and changing health trends and consumer preferences.
- There is no guarantee that Famous Dave's restaurants will be successful in new markets. Restaurants are currently operated in 36 states, but the company will continue to expand geographically in the future, including new franchised restaurants in international locations. In our view, this risk is lowered through growth in new markets from franchisees.
- The restaurant business is extremely competitive and competition for customers through lower prices may negatively impact DAVE's returns. DAVE operates in the casual dining segment of the restaurant industry which we think is the most competitive.
- Our growth projections are dependent on DAVE's ability to recruit and sign competent franchisees. Lower demand for franchised restaurants could slow restaurant development and expected returns.
- Readers should recognize that the risks noted here do not represent a comprehensive list of all risk factors or potential issues, nor all factors that may preclude achievement of our forecast or price target. Additional risk factors exist and are outlined in the Company's SEC filings

Other Disclosures:

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