SEPTEMBER 30, 2015

Cara Operations Ltd.

CAO-T: $32.75 | Rating: Buy | Target price: $38.00

Primed for a Turnaround

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Investment Highlights

Cara Operations Ltd. is a multi-banner full-service restaurant company with 10 banners in operation. Approximately 89% of its 827 units are franchised, with 72% of restaurants located in Ontario. Their two largest banners by location count are Swiss Chalet (213 restaurants) and Harvey's (262 restaurants). Current system sales are just over $1.7 billion.

Source: BigCharts.com

Market and Company Data

Ticker	CAO-T	FD Shares O/S (M)*	53.8
Rating	Buy	Market Cap (M)*	$1,763
Risk	High	Float O/S (M)*	11.8
Price	$32.75	Float Value (M)*	$384.9
1-Yr Target	$38.00	Avg Daily Volume (k)	115.8
Dividend	$0.37	Enterprise Value (M)	$1,820
Yield	1.1%	Equity Ownership:	
1-Yr ROR	17%	*Fairfax:*	*40.5%*
52 Wk High-Low	$36.99-$29.52	*Phelan Family:*	*35.6%*
Valuation	14x 2017e EBITDA	Net Debt/EBITDA	0.7x
Year End	Dec. 31	Next Reporting	Nov-15

EPS (FD)

	Q1		Q2		Q3		Q4		Annual		P/E
2014	*$0.19*	A	*$0.23*	A	*na*	A	*na*	A	*$0.90*	A	36.4x
2015	*$0.20*	A	$0.30	A	$0.29		$0.28		$0.99		33.2x
2016	$0.28		$0.33		$0.34		$0.32		$1.28		25.6x
2017									$1.45		22.6x

Adjusted EBITDA ($M)

	Q1		Q2		Q3		Q4		Annual		EV/EBITDA
2014	*$17.8*	A	*$22.0*	A	*$21.7*	A	*$22.1*	A	*$83.6*	A	21.8x
2015	*$24.9*	A	$28.4	A	$29.3		$28.3		$110.9		16.4x
2016	$28.3		$32.0		$32.6		$31.3		$124.3		14.6x
2017									$136.5		13.3x

*Cara's IPO was April 10, 2015; 2014 and Q1/15 figures (*italics*) are pre-IPO

Source: Company reports; Thomson; Bloomberg; LBS estimates.

All pricing as of September 28, 2015.

Initiating Coverage: Buy, $38.00 Target Price

- We highlight the following aspects from an investment standpoint:
  1. Opportunity embedded in the ongoing turnaround at Cara's corporate stores and focus on improving profitability and margins (i.e. H1/15 margins of 10.5% vs. H1/14 at 4.0%);
  2. Benefits from renewed efforts to improve franchisee profitability through more active promotional activity in order to reduce the number of franchisees receiving assistance (i.e. 178 restaurants receiving assistance at Q2/15 versus 203 at Q4/14);
  3. Near-term momentum on store openings to turn materially with management forecasting 24 net new openings in H2/15 vs. 10 net closures in H1/15;
  4. A strong balance sheet with leverage at 0.7x net debt/EBITDA and aided significantly with the recent IPO;
  5. New management team with a strong track record, in particular CEO Bill Gregson who is well-regarded among institutional investors due to his past success with The Brick and Forzani Group.
- Aggressive growth targets outlined; Low-end of revenue / EBITDA target range attainable with organic growth / new openings. With its IPO, Cara outlined in detail its growth objectives over the next five to seven years. The ultimate goal is for the company to reach $2.5 to $3 billion in system sales, with operating EBITDA of $175M to $240M (or 7-8% of system sales). Assuming management executes at the lower end of the target range in terms of net new store openings (i.e. 35 per year versus 30-50 target) and SSSG (i.e. 2.5% versus 2.5%-4.0% target), we see them hitting the low end of the target EBITDA range of $175M in five years (i.e. 2020). In such a scenario, with the stock holding our target multiple of 14x, this would imply a $50 valuation in 3-4 years, providing a return CAGR of +12-16% using a conservative forecast.
- Balance sheet allows for incremental growth through M&A, with leverage of approximately 0.7x net debt / EBITDA. In terms of acquisition criteria, Cara management has outlined several criteria in order to determine a fit for the organization, which include: (1) Establishing a presence in the fast-casual market; (2) Offers potential for expansion of existing brands in Quebec; (3) Appropriate valuation (which we would estimate at 8-10x EBITDA); (4) Looking for concepts with potential to achieve minimum annual system sales of $150-200M. While we are often questioned regarding the availability of such targets, we would note that several potential candidates are out there (we outline several in this report). In our view, the challenge is more often convincing the seller (who will often still be looking to build the business) that Cara is the right partner to grow with.
- In determining our $38.00 target price, we have selected a target multiple of 14x 2017E EBITDA. This is effectively the same multiple used to price the April IPO (which was priced at $23 per share), and also represents a significant discount to the current LTM multiple which is closer to 18.7x. Additionally, while we acknowledge that 14x is at a premium to North American peers, our view is that current consensus financial forecasts remain conservative. We also have a view that investors are paying a premium in the expectation that the company will be able to complete a large and meaningful acquisition.

Company/Recent IPO/History

Large scale operator in the Canadian restaurant market

Cara is Canada's third largest restaurant operator, with over $1.7 billion in system sales generated across 827 restaurants (as of Q2/15). The company is a multi-brand operator with 10 distinct banners (as illustrated in Exhibit 1), with the largest being Swiss Chalet at ~$550M in system sales.

Cara is primarily a franchisor, with 89% of restaurants operating as a franchise, with the restaurant footprint skewed heavily into Ontario (72% of units). Additionally, apart from Harvey's and pending acquisition of New York Fries (both of which would classify as quick-service restaurants), **Cara's portfolio is primarily full-service / casual dining restaurants** (> 80% based on system sales).

Exhibit 1: Overview of Cara Brands as at Q2/15

Brand	Year Founded	Current Units	2014 System Sales (M$)	AUV (M$)	Percent Franchised	B.C	AB	SK	MB	ON	QC	Atl
						Geographic Location Breakdown						
Swiss Chalet	1954	213	546	2.5	*97%*	*4%*	*11%*	*0.5%*	*0.5%*	*76%*	*-*	*8%*
Harvey's	1959	262	267	1.0	*94%*	*0%*	*7%*	*0.4%*	*1%*	*69%*	*18%*	*4%*
Montana's	1995	92	234	2.6	*88%*	*11%*	*20%*	*3%*	*4%*	*54%*	*-*	*8%*
Milestones	1989	54	169	3.2	*54%*	*31%*	*9%*	*-*	*-*	*56%*	*-*	*2%*
East Side Mario's (Prime)	1980	75	168	2.1	*96%*	*1%*	*7%*	*1%*	*-*	*77%*	*7%*	*7%*
Kelsey's	1978	71	157	2.2	*77%*	*1%*	*1%*	*-*	*-*	*97%*	*-*	*-*
Prime Pubs (Prime)	1996	29	63	2.1	*86%*	*-*	*17%*	*0%*	*3%*	*79%*	*-*	*-*
Casey's (Prime)	1980	21	59	2.4	*95%*	*-*	*-*	*-*	*-*	*71%*	*29%*	*-*
Bier Markt (Prime)	1999	7	27	3.9	*0%*	*-*	*-*	*-*	*-*	*86%*	*14%*	*-*
The Landing Group	2011	3	18	6.0	*0%*	*-*	*-*	*-*	*-*	*100%*	*-*	*-*
		827	1,708		*89%*	*5%*	*9%*	*1%*	*1%*	*72%*	*7%*	*5%*

Notes:
Harvey's AUV (average unit volume) excludes non-traditional / smaller-format locations
Cara acquired 55% of the Landing Group in December 2014. The 45% balance was acquired in June 2015.

Source: Company reports; Laurentian Bank Securities

Details of Recent IPO

On April 10, 2015 Cara raised $230.1M gross proceeds ($216.6M net) in an initial public offering of 10M subordinated voting shares priced at $23 per share. The listing price of $23 represented an LTM EBITDA multiple of 14.2x. The IPO was very well received by investors and the market (i.e. priced above the high end of the range), with the stock gaining +42.7% to $32.83 on the first day of trading (representing an LTM EBITDA multiple of 20.1x).

The use of proceeds from the IPO was effectively allocated to paying down debt, with net debt / EBITDA dropping to 0.7x post-IPO from 3.1x just prior.

Some Historical Perspective

Pre-IPO financial flexibility was constrained

While we will not give a detailed history of Cara (and Prime) in this report, some notes regarding the events leading up to the IPO are important. In particular, we would note that in 2012, Cara's "predecessor" company (which consisted of Swiss Chalet, Harvey's, Montana's, Milestones, and Kelsey's) was **facing "severely constrained financial flexibility" with leverage hitting 6.4x net debt / EBITDA at the end of that year.** This financial pressure was driven by multiple factors including:

1. Significant debt taken on during the 2004 going-private transaction initiated by the founding Phelan family (who still remain significant shareholders);
2. An overall inflated cost structure; and
3. Lack of meaningful recovery in the underlying restaurants from the slowdown experienced during the 2008 financial crisis.

Along comes Fairfax

Given the ongoing financial pressure and need for capital, in October 2013 Fairfax invested $100M in Cara while also vending in its interest in Prime Restaurants (East Side Mario's, Prime Pubs, Casey's, and Bier Markt) at a value of approximately $69.6M (note that Fairfax privatized Prime in January 2012 at a cost (enterprise value) of $65M). In return for the investment, Fairfax received preferred shares, warrants and subordinated debt.

Alongside this capital investment, Fairfax also put a new management team in place, which included Chief Executive Officer Bill Gregson and Chief Financial Officer Ken Grondin. We would note that both Mr. Gregson and Mr. Grondin worked with Fairfax on its prior (and quite successful) investment The Brick, which was acquired by Leon's Furniture in March 2013. Additionally, in September 2014 the management team was bolstered by the addition of Ken Otto as President, Family Dining and Chief Development Officer. Mr. Otto was previously with Boston Pizza as Chief Operating Officer, and held several executive roles throughout that company's rapid growth phase from 2004-2014.

With the new management team focused on improving the cost structure and operating profile, leverage for the combined Cara/Prime entity had dropped to a more manageable 3.1x at the end of 2014 (i.e. just prior to the IPO).

Dual Class Share Structure and Ownership

In Exhibit 2, we provide a snapshot of the current share structure and ownership of Cara, which consists of multiple voting (25 votes) and subordinate voting (1 vote) shares. We also illustrate some of the pre-IPO share structure changes that took place with the transaction.

Exhibit 2: Capital Structure of Cara Pre and Post Closing of Initial Public Offering

	PRE-IPO Share Structure and Changes				POST-IPO Share Structure	
Shareholder	Security	Number	Ownership post pre-closing capital changes Exercise of Warrants	Ownership post pre-closing capital changes Conversion to MVS/SVS	Current Ownership	*Voting Percentage*
Fairfax Group Shareholders (1) (2)	Class A Preferred Shares Class A Warrants Class B Preferred Shares Class B Warrants Subordinated Debt Warrants	27,848,425 27,848,425 17,418,503 17,418,503 8,564,596	55,530,426 Voting Common Shares	19,903,378 MVS	19,903,378 MVS	*52.56%*
Phelan Group Shareholders (1) (3)	Voting Common Shares	48,805,209	48,805,209	17,492,906 MVS	17,492,906 MVS	*46.20%*
Prime Shareholders	Class A Preferred Shares Class A Warrants	4,327,065 4,327,065	2,628,163 Voting Common Shares	941,994 SVS	941,994 SVS	*0.10%*
Robinson Holders	Voting Common Shares	1,662,500	1,662,500	595,878 SVS	595,878 SVS	*0.06%*
Landing Group Issuance (4)	Voting Common Shares	-	-	-	209,526 SVS	*0.02%*
Public Shareholders (3)	Voting Common Shares	-	-	-	10,005,000 SVS	*1.06%*
Total Multiple Vote Shares Outstanding (MVS)					37,396,285 MVS	
Total Subordinated Vote Shares Outstanding (SVS)					11,752,398 SVS	
Total shares outstanding (MVS and SVS)					49,148,683	

Options	Average Strike	Number
Director Options	$0.01	86,022
CEO Stock Option Plan	$5.89	3,494,624
Employee Stock Option Plan	$9.43	1,110,371
Total	$6.62	4,691,017
Fully Diluted Shares Outstanding		53,839,700

Notes:
(1) MVS represent Multiple Voting Shares with 25 votes each; SVS represent Subordinate Voting Share with 1 vote each
(2) All MVS automatically convert to SVS when Fairfax Group Shareholders own less than 50% of their original amount (or 9,951,688 MVS)
(3) Phelan Group MVS automatically convert to SVS when they own less than 50% of their original amount (or 8,746,452 MVS)
(4) On June 26, 2015 Cara issued 209,526 SVS as part of the purchase of remaining 45% of the Landing Group.

Source: Cara IPO Prospectus; Laurentian Bank Securities

Before discussing the growth strategy being communicated by Cara management, we will provide an overview of the Canadian restaurant industry.

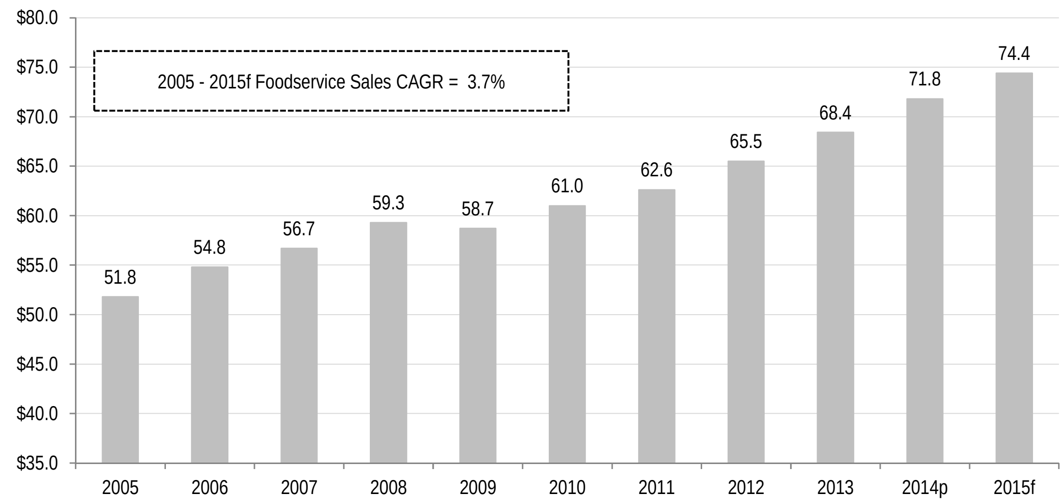
Brief Industry Overview - Canadian Foodservice

Industry exhibits stable and consistent growth trend

According to data from Restaurants Canada, in 2014 total Foodservice sales in Canada were an estimated $71.8 billion (Exhibit 3), which represented growth of +5.0% over 2013. Over the 2005-2015f time period (10 years), the industry is anticipated to have grown at a +3.7% CAGR, with the only down year coming during the economic slowdown of 2009 where growth was -1%.

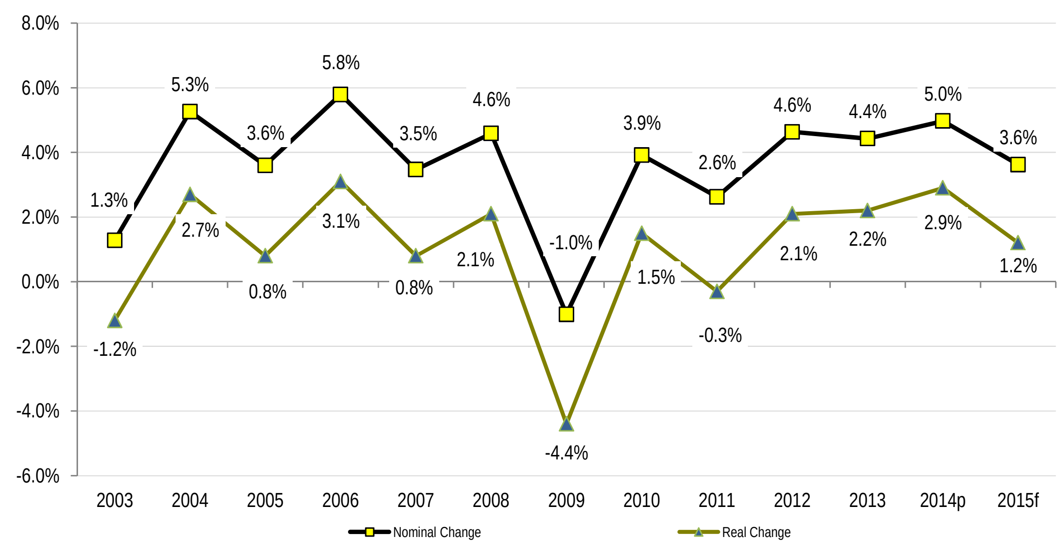
In terms of real growth rates, 2015 is forecasted to grow at +1.2% which represents a downtick from the three previous years (see Exhibit 4). This slower rate of growth is related to a “noticeable” dip in economic activity seen towards the end of 2014, with job creation and consumer confidence both falling. As expected, a lot of this slowdown is related to trends in Western Canada, namely Alberta and Saskatchewan.

Exhibit 3: Total Foodservice Sales in Canada ($ billions)



Source: Restaurants Canada, Foodservice Facts 2014, 2015; Laurentian Bank Securities

Exhibit 4: Total Foodservice Sales in Canada - Nominal / Real Growth Rates



Source: Restaurants Canada, Foodservice Facts 2014, 2015; Laurentian Bank Securities

Breaking Down Canadian Foodservice Sales

Exhibit 5 presents a detailed breakdown of Canadian Foodservice Sales. Overall, the largest category is Commercial Foodservice, which represents approximately 80% of total Foodservice sales. Within Commercial, Quick-service restaurants (QSR) and Full-service restaurants (FSR) are the largest categories with a combined $50 billion in sales. As illustrated, both categories continue to show consistent growth, with Restaurants Canada forecasting +3.7% and +3.4% respectively over the 2016-2019 timeframe. As discussed in the next section, most of Cara's banners (except Harvey's and New York Fries (pending closure of acquisition)) would fall within the FSR category.

Exhibit 5: Canadian Foodservice Sales and Forecast (per Restaurants Canada)

	2010 Final (M$)	y/y Growth	2011 Final (M$)	y/y Growth	2012 Final (M$)	y/y Growth	2013 Final (M$)	y/y Growth	2014 Preliminary (M$)	y/y Growth	2015 Forecast (M$)	y/y Growth	5yr avg nominal growth	2016-2019 growth forecast
Quick-service restaurants (QSR)	21,220	5.4%	21,962	3.5%	23,140	5.4%	24,138	4.3%	25,536	5.8%	26,532	3.9%	4.6%	3.7%
Full-service restaurants (FSR)	20,931	1.2%	21,486	2.6%	22,631	5.3%	23,722	4.8%	24,916	5.0%	25,813	3.6%	4.3%	3.4%
Caterers	3,998	7.1%	4,214	5.4%	4,444	5.5%	4,600	3.5%	4,904	6.6%	5,085	3.7%	4.9%	4.7%
Drinking Places	2,468	-3.4%	2,362	-4.3%	2,356	-0.3%	2,311	-1.9%	2,296	-0.7%	2,312	0.7%	-1.3%	1.2%
Total Commercial Foodservice	48,616	3.2%	50,024	2.9%	52,570	5.1%	54,772	4.2%	57,652	5.3%	59,742	3.6%	4.2%	3.6%
Total Non-Commercial Foodservice	12,138	4.7%	12,369	1.9%	12,721	2.8%	13,643	7.2%	14,197	4.1%	14,707	3.6%		
Total Foodservice	60,755	3.5%	62,393	2.6%	65,291	4.6%	68,415	4.8%	71,849	5.0%	74,449	3.6%		
Menu Inflation		na		2.9%		2.5%		2.3%		2.1%		2.4%		

Source: Restaurants Canada, Foodservice Facts 2011, 2012, 2013, 2014 and 2015; Laurentian Bank Securities.

Competitive Positioning of Cara Brands

Skew towards Family Dining segment … Notable absence from Fast Casual

In Exhibit 6 we present an overview of the various restaurant segments, showing the competitive positioning of Cara's brands within the market. As illustrated, **the majority of sales** (~53%) **fall within the category "family dining"**, which is very much a value-oriented / table-service offering. Additionally, Cara has taken a barbell-type approach with its two most recent acquisitions, with The Landing Group at the far right within the premium casual category, and New York Fries (pending acquisition) at the other end of the spectrum. **Cara is notably absent from the fast casual segment**, and we believe that the company would like to get more exposure to this portion of the market given that it currently represents the fastest growing part of the North American restaurant market.

In terms of M&A, which we will discuss in more detail later in this report, we anticipate Cara will be active in effectively all segments of the market, but with some emphasis on family/casual dining.

Exhibit 6: Restaurant Segmentation in Canada

	Quick Service (QSR)	Fast Casual (FC)	Family Dining	Mid-Casual	Premium Casual	Fine Dining
Characteristics	Lowest Cheque No table Service Plastic Seats No alcohol	Value priced Fresh ingredients No table service Made to order Alcohol rare	Value-oriented Table service Buffet Limited alcohol	Moderate cheque Table service Eclectic décor Alcohol served	Higher cheque Richer décor Few families* Social atmosphere* Alcohol served	Highest cheque Fine cuisine White table cloth Alcohol served
Examples	A&W **Harvey's** KFC McDonalds Taco Bell Tim Hortons **New York Fries**	Five Guys Burgers Hero Certified Burgers Freshii Chipotle Mucho Burrito	Denny's **Eastside Mario's** Humpty's **Montana's** Perkins Pizza Hut **Swiss Chalet**	Boston Pizza **Casey's** Elephant & Castle Jack Astor's **Kelsey's** Original Joe's **Prime Pubs**	Baton Rouge **Bier Markt** Cactus Club Earl's Keg **The Landing Group** **Milestone's** Moxie's	Hy's Morton's Ruth's Chris Shore Club
Typical Spend	Less than $8	$10-15	$8 - $12	$12 - $25	$20 - $50	More than $50
*% f2014 Cara System Sales**	*19%*	*0%*	*53%*	*16%*	*12%*	*0%*

* We have assumed New York Fries has system sales of $75M in this analysis (QSR percentage would be 15% excluding New York Fries)

Source: Cara IPO Prospectus, Diversified Royalty Corp 2015 AIF, Boston Pizza Management Information Circular (filed March 27, 2014); Laurentian Bank Securities

The Primary Challenge: Traffic Levels are Stagnant

Despite the positive overall growth forecast outlined by Restaurants Canada, some more granular data provided from NPD Group (Crest) **shows that traffic levels within the Commercial segment have been extremely stagnant since 2009.** As illustrated in Exhibit 7, **traffic levels from 2009 to 2014 have increased a mere +1% in aggregate**, with the past two years extremely challenging (Exhibit 8).

Dinner segment very challenging in Canada

Of all of the segments highlighted within the restaurant segmentation (Exhibit 5), traffic losses within the full-service (family / casual dining) have been most acute, with fast-casual restaurants and improved retail / home-meal-replacement offerings (i.e. Costco) the benefactors in most cases. **In particular, over the 2009-2014 timeframe, the dinner segment (47% of full-service traffic) has been very difficult, with overall visits down 4%, with "evening snack" (which mainly consists of bar occasions) visits down 7%.** Full-service chains have been able to partly offset the latter day traffic declines with increases in both the lunch and breakfast dayparts.

U.S. trends in Family Dining even more dire

While the trends for full-service restaurants in Canada have not been strong, **the negative traffic trends within the U.S. have been more pronounced**, with NPD estimating that traffic levels have declined 8% from 2005 to 2014, versus fast-casual dining where traffic levels are up +103% from 2005 to 2014. **We would note that the proliferation of fast-casual restaurant chains in the U.S. is currently much more advanced than in Canada.**

Exhibit 7: Canada Commercial Foodservice - Traffic Trends Among Restaurant Segments

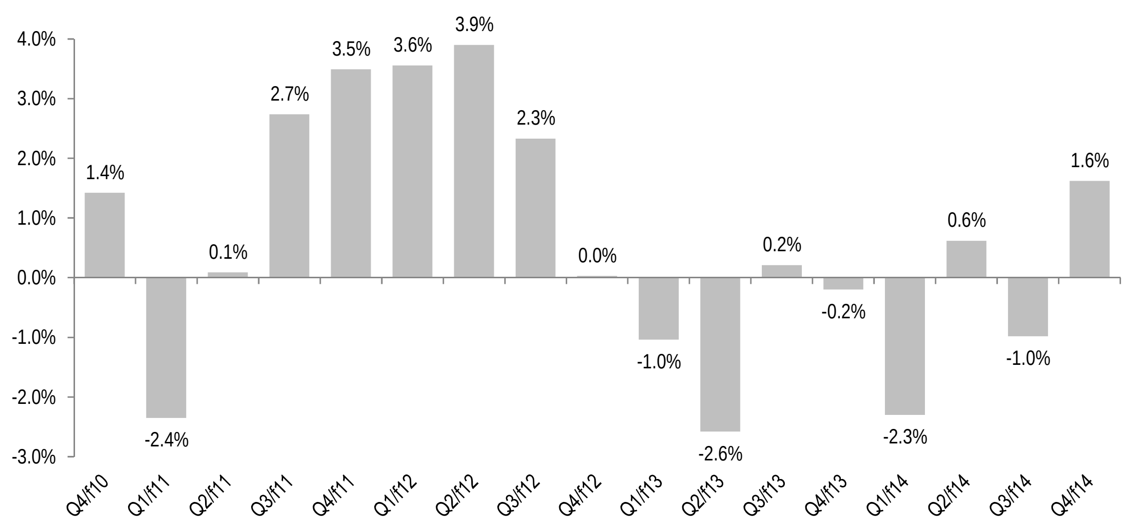
Segment	Visits 2009 (B)	Visits 2014 (B)	*09-14 Delta*	*Dollar Share*
Quick-Service (QSR)	4.10	4.30	*1.0%*	*47.0%*
Full-Service (FSR)	1.62	1.58	*-1.0%*	*39.0%*
Home Meal Replacement	0.47	0.5	*1.0%*	*7.0%*
Convenience	0.30	0.20	*-4.0%*	*7.0%*
Total Market	6.4	6.6	*1.0%*	*100.0%*

Note: Data in table presented as per NPD presentation

Source: NPD Group (CREST YE Feb 2015); Laurentian Bank Securities

Even though trends are tough and getting tougher, all is not lost. **The long-term viability of today's restaurant brands will be determined by the efforts made to reposition themselves to cater more towards a younger demographic**, which we discuss in more detail below.

Exhibit 8: Quarterly Traffic - Total Canadian Commercial Foodservice (2010-2015)



Source: NPD Group (CREST) (Note that Q4 ends in November)

"Winning the Year" by Attracting Millennials

Boomers diminishing need for family dining

At a recent restaurant industry conference we attended, **the focus on the millennial generation and the necessity for brands to actively engage this customer group was overwhelming.** This is particularly true given that this generation (ages 14-34 per NPD) is set to surpass (or has already surpassed) the baby boomer generation (ages 49-67 per NPD) in terms of both size and consumption. Several ideas were offered at this conference as to what the millennial generation is seeking in terms of a restaurant offering. That said, **one of the clear messages given was that what the generation is not seeking is what we refer to as traditional casual / family dining.**

Exhibit 9: Share of Total Foodservice Visits

Mature Traditionalists	*11.0%*
Boomers	*27.0%*
Gen X	*17.0%*
Millennials	*28.0%*
Post-Millenials	*17.0%*

Source: NPD Group (CREST YE Feb 2015)

In Exhibit 9 we illustrate the estimated foodservice visits per generation across all segments.

User-generated content becoming increasingly important

At this conference, there was also a significant amount of discussion surrounding how best to reach millennials in order to market and create brand awareness. While the answer was perhaps unsurprising overall (i.e. via mobile devices or through engaging digital content), some of the underlying nuances were quite interesting. In that regard, versus other generations, millennials are much more likely to produce and upload user-generated content and also trust other user-generated content obtained through social networks, peer reviews and conversations.

This becomes a critical aspect of the client equation as millennials are not only more likely to share a particular restaurant experience among peers, the dissemination is rapid, and the potential reach is significant. **As such, it is simply not enough to "win a particular customer visit from a competitor". More than ever, that single customer experience has potential consequences across a very broad group of consumers.** As such, the quality of the entire restaurant experience (i.e. food, service, value) needs to be high and encourage a repeat visit.

Strategies to Steal/Maintain Market Share

Within the context of largely flat traffic conditions (within both the U.S. and Canada), the industry has evolved into an ongoing "battle for market share". This battle is clearly being won by fast casual restaurants in particular, and boosted by their appeal among the Millennial generation. Examples of some of the more well-known and successful fast-casual concepts include Panera Bread, Chipotle Mexican Grill, Panda Express and Five Guys Burgers. These concepts offer consumers a higher quality product vs. quick-service-restaurants at a slightly higher price point, while providing a less-formal and lower price point vs. casual dining.

In terms of some specific thoughts regarding how the top chains in all segments gain share, the following ideas were offered at the industry conference:

1. Regular menu innovation for food and beverage – which includes adding new menu items (i.e. Swiss Chalet chicken wings, Tim Horton's creamy chocolate chill) and especially using limited time offers (LTOs) to drive incremental traffic and consumer interest. The use of LTOs is increasing rapidly as studies clearly show that the consumer response is favourable (i.e. A&W Spicy Guacamole, The Keg seasonal menu offerings).
2. Premiumization of core menu items – this can be accomplished through the use of higher quality ingredients (i.e. locally-sourced or hormone/steroid-free (A&W)), adding different types of proteins (i.e. steak, seafood), or offering more made-from-scratch / fresh / healthier items (i.e. McDonald's recent salad bowl enhancement).
3. Allowing customers more control of the menu – achieved primarily through made-to-order offerings, which is the hallmark of fast-casual restaurants. Another interesting approach to customized menu items is through the use of mobile apps. An example of this is the recent release of an app from Taco Bell that allows custom orders and pre-payment, while also informing the restaurant when the customer enters the store so food preparation can begin.
4. Expanding beyond core dayparts – with increased snack (in particular between lunch and dinner) offerings being a popular way to grab share (i.e. McDonald's and Tim Horton's snack wrap and smoothie offerings).
5. Renovating and upgrading restaurants – this relates almost entirely to renovation activity with most franchise agreements asking for a renovation cycle of once every seven or eight years. Tired, dirty and out-dated décor reflects poorly on the brand and leaves consumers disinterested.
6. Maintaining a strong balance between value and price – particularly in Canada, most consumers are value conscious and want to feel that they received a good product for the dollars spent.
7. Introduction of loyalty programs – interestingly, restaurants in both the U.S. and Canada have been slow to embrace loyalty programs.

Need to differentiate is critical

With an intensifying "battle for market share" coupled with a muted outlook in terms of traffic growth, investors will need to increasingly focus on identifying those restaurant concepts which resonate positively with consumers on the criteria of food quality, service/experience, value and convenience. This will become increasingly critical within the quick-service-restaurant space and at the lower end of casual-dining, particularly among those concepts offering a product viewed by consumers as largely homogenous across brands (i.e. pizza, burgers, chicken).

Within the casual/full-service space, while value always remains important, food quality and service/experience are more of the differentiating factors that need to be exploited to keep customers returning. In particular, full-service restaurants need to evolve their product offering to cater more readily to the millennial cohort as it becomes the most influential consumer group in the market.

Growth Avenues

With its IPO, Cara outlined in detail its growth objectives over the next five to seven years. The ultimate goal is for Cara to reach $2.5 to $3 billion in system sales, with operating EBITDA of $175M to $240M (or 7-8% of system sales). In this section we provide an overview of the key strategies outlined to reach its goals.

1. Achieve Annual SSSG of +2.5-4.0%

Multiple levers available to support organic growth

As discussed earlier, in the context of stagnant traffic trends, attaining consistent SSSG above 2.5% will be challenging. That said, Cara management has outlined several initiatives to support ongoing organic growth, namely:

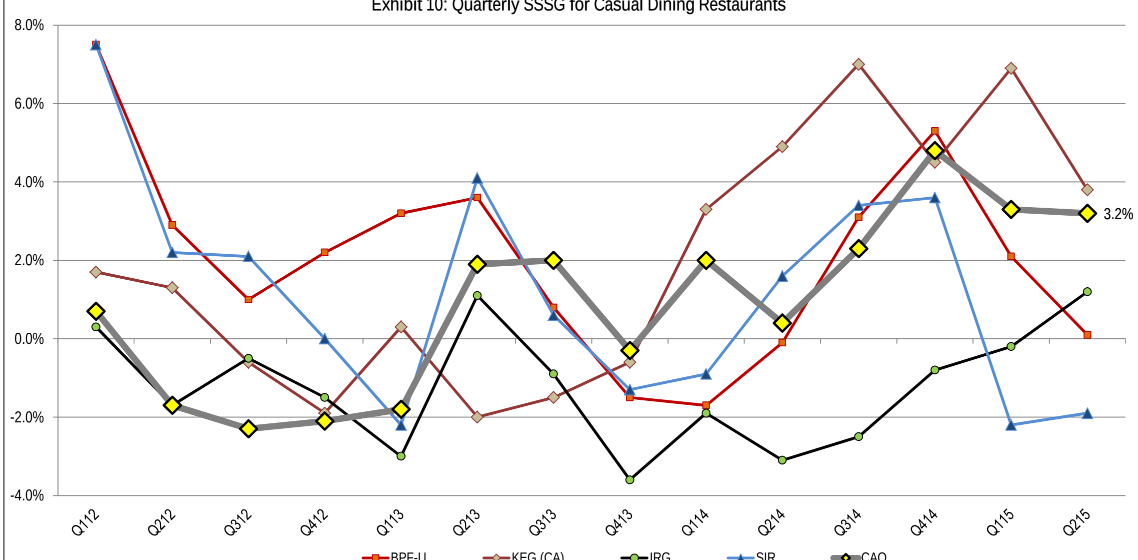
- Regular menu innovation and offering compelling product;
- Monitor guest experience and improve customer experience;
- Keep restaurant concepts up to date;
- Pursue effective media spend and promotion activity with a "win-the-week" mindset;
- Leverage strategic / cross-promotional programs with third parties (i.e. SCENE and CAA);
- Expand off-premise (take-out / delivery) programs (with East Side Mario's and Montana's indicated as opportunities to expand; Swiss Chalet is the benchmark at 43% of sales off-premise).

In assessing these initiatives, it is clear that there is tremendous opportunity to boost the organic growth rates of the restaurants. In particular, with a store-base where there has been less focus on the aforementioned, any real efforts to improve along these criteria should be met with a favourable customer response.

In Exhibit 10 we illustrate Cara's historical SSSG versus other Canadian casual dining peers (namely Boston Pizza, The Keg, Imvescor, and SIR Corp.). **More recently we have seen Cara's SSSG trend move within the target range as management has focused in particular on the marketing and promotional activity.** This coincides with the "Win the Week" sales culture that the Cara management team has implemented within the organization. Additionally, in supporting these efforts, we would note that Cara is currently "over-investing" in the advertising fund with quarterly payments of $2-2.2M. While we have some expectation the level of payment will taper off over time, this level of over-investment is expected to continue over the near term (note that Cara is under no obligation to make these payments and has the option to discontinue at any time).

In terms of quantifying the impact of a +1% increase to SSSG (on the franchise business), we estimate this would add ~$15M to system sales with an associated EBITDA lift of ~$600,000 (i.e. 4% margin). In terms of our forecast, we have modelled +3% SSSG in H2/f15 and 2016, with +2.5% in f2017e.

Exhibit 10: Quarterly SSSG for Casual Dining Restaurants



Source: Company reports, Laurentian Bank Securities.

2. Target +30-50 net new locations annually

While management has outlined a strategy to reach this target, we continue to view this goal as quite aggressive. In particular, the company has stated that they will open 24 net new locations in H2/f2015. **This will represent a significant turnaround from the more recent trend of net store closures** (10 since the end of 2014), which has been more concentrated in the East Side Mario's and Casey's banners (importantly, the +30-50 net opening target excludes Casey's closures and conversions as that banner is restructured and phased out). **We are under the impression that the vast majority of the new store openings will be franchises (i.e. 85-90%).**

Good real estate at a reasonable price is critical to a restaurant's long-term success

In our conversations with restaurant executives, while the success of any particular franchise is driven by multiple factors (which obviously includes the operating ability and capitalization of the franchisee), **the real estate, location, and level of rent are very critical factors which play an important role in the viability of a particular store** (particularly in a period of weakness). Within its presentation, Cara management highlights a disciplined approach to growth, **with an appropriate occupancy cost and return on investment for franchisees.**

As can be seen in Exhibit 11, the all-in investment for many of Cara's restaurants is sizeable (i.e. $1.3-1.8M), and would generally require a substantial amount of borrowed capital on the part of the franchisee at the outset. While a unit in a subpar location may perform well during its honeymoon period (i.e. first 6-9 months), the longer-term viability needs to be analyzed. In that regard, we are aware that Cara senior management closely scrutinizes each and every real estate deal to ensure it encompasses an appropriate level of return for all parties involved.

Exhibit 11: Cara Operations - Franchise Cost by Banner

	Franchise Fee	Estimated Total Investment	Franchise Royalty	Franchise Advertising	Restaurant Concept
Swiss Chalet	$60k	$1.3-1.8M	5%	5% [1]	Family Dining
Harvey's	$25k	$600k-950K	5%	4%	Quick Service
Montana's	$60k	$1.6-2.3M	5%	3%	Family Dining
Milestones	$60k	$2.5-$3.5M	na	na	Premium Casual
East Side Mario's	$50k	$1.3-1.6M	5%	4% [2]	Family Dining
Kelsey's	$60k	$1.3-1.6M	5%	3%	Mid-Casual
Prime Pubs [3]	$40k	$1.3-1.6M	5%	4% [4]	Mid-Casual (Bar/Pub)
Casey's	$50k	$1.3-1.6M	5%	4%	Mid-Casual
Bier Markt	na	na	na	na	Premium Casual
The Landing Group	na	na	na	na	Premium Casual
New York Fries	$30K	$0.2-$0.3	6%	2%	Quick Service

Notes:
1) 4% nationally (on premise), 2% nationally (off premise), 1% locally
2) 3% nationally, 1% locally
3) Group includes Fionn MacCool's, Darcy McGee's and Paddy Flaherty's
4) 1% nationally, 3% locally

Note: Advertising rates are standard and may vary.

Source: CFA Franchise Source Guide 2015, Company reports, Laurentian Bank Securities

In terms of target markets (circling back to Exhibit 1), Cara banners remain underrepresented in Western Canada, with B.C., Alberta and Saskatchewan all representing possible areas of expansion. In particular, we would anticipate some level of push for Swiss Chalet and Harvey's franchises in Western Canada (which includes possible combination restaurants). **One of the fastest ways to approach this expansion would be to sign an area development agreement with a well-capitalized local group to build out multiple locations.** On the corporate side, focus will be on Milestones, Bier Markt and The Landing Group.

In terms of the potential system sales contribution from new openings, Cara's average unit volume in f2014 was just over $2M. At the low end of the range for net new openings (i.e. 30 restaurants), this has the potential to add $60M in system sales and ~$2.4M in EBITDA (i.e. 4% EBITDA margin at the franchise level). With corporate units the expected contribution margin is 10-15%, so to the degree net openings skew toward corporate (we believe will represent ~10% of net new openings), there would be some upside to this estimate.

3. Pursue acquisitions and new concepts

With a clean balance sheet and leverage of approximately 0.7x net debt / EBITDA, we anticipate that Cara will be active in Canadian restaurant M&A. In terms of acquisition criteria, Cara management has outlined the following in order to determine a fit for the organization:

- Brands that complement the existing restaurant portfolio;
- Add selective limited-service concepts;
- Establish presence in "fast casual";
- Offer further expansion of existing brands into Quebec;
- Opportunity to realize synergies;
- Appropriate valuation (which we would estimate at 8-10x EBITDA);
- Prepared to own less than 100% (allowing incumbent management to continue owning equity).
- Looking for concepts with potential to achieve minimum annual system sales of $150-$200M.

In terms of the expansion of existing brands into Quebec, we would note that there has been a suggestion that St-Hubert and Imvescor (IRG-T; Not Rated) could be potential targets.

In terms of St-Hubert, the fit is quite logical and attractive given the product offering and market position of Swiss Chalet. That said, the St-Hubert business is controlled by its founding family, and the timing of any potential transaction remains uncertain.

Regarding Imvescor, it is a more interesting situation given the ongoing turnaround under the (relatively) new CEO Frank Hennessey, coupled with Fairfax's history with the business. Recall Fairfax invested $25M in late 2011 as part of a recapitalization transaction at Imvescor. Fairfax subsequently exited this position in April 2012. While we believe such a combination with Imvescor does provide an opportunity for significant synergies, we would view it more as a medium-term opportunity.

Apart from the above mentioned chains, Exhibits 12 and 13 illustrate a sampling of some of the larger restaurant chains in Canada. We do not believe there is any shortage of acquisition candidates or investment opportunities for Cara. In many cases it is more a function of convincing the owner that Cara is the right partner to continue growing the business.

In a situation where an owner is looking to fully exit their business, we would view MTY (MTY-T, Buy; $40 target) as a potential competitor on certain transactions, particularly anything within the QSR space. Additionally, while private equity is not nearly as active in Canada versus the U.S., there is always potential for a group to bid and participate on deals.

In terms of the possibility of a master franchise agreement, we are not under the impression that Cara has much interest (at this point) in acting as the representative for a large U.S. brand within the Canadian market. We are not necessarily surprised by this given that such arrangements typically distribute a large portion of the economics back to the parent company.

Regarding deals completed by Cara under its new management team, we would note the October 2013 acquisition of Prime Restaurants for $73.5M, December 2014 acquisition of a 55% interest in The Landing Group (subsequent 45% interest acquired June 2015) for total proceeds of $39.5M, and the announced acquisition of New York Fries (expected closing in fall 2015) for which no purchase price was disclosed.

Exhibit 12: Canadian QSR / Coffee / Ice Cream / Frozen Yogurt Chains (Focusing on chains over $30M in system sales)

Name	Total Units	Recent System Sales (M$)	Restaurant Concept	Parent Company / Owner / Ticker
Restaurant Brands International	4,119	5,563		Publicly Traded (QSR CN; QSR US)
Tim Hortons Canada	3,819	5,210	Coffee/Baked Goods	
Burger King Restaurants Canada	~300	354	Hamburgers	
McDonald's Restaurants of Canada	1,440	3,888	Hamburgers	U.S. Publicly Traded (MCD US)
Subway	3,154	1,400	Sandwiches	U.S. Private Company
Yum Restaurants Canada	1,211	1,013		U.S. Publicly Traded (YUM US)
Pizza Hut	383	313	Pizza (Full-service)	
Taco Bell	182	76	Mexican	
KFC	646	624	Chicken	
Starbucks Coffee	1,445	1,318	Coffee/Baked Goods	U.S. Publicly Traded (SBUX US)
A&W Food Services Canada	837	1,004	Hamburgers	Canadian Publicly Traded (AW-U CN)
MTY Food Group	2,792	983	Various	Canadian Publicly Traded (MTY CN)
Wendy's Restaurants Canada	360	638	Hamburgers	U.S. Publicly Traded (WEN US)
International Dairy Queen	617	558	Ice Cream / Other	U.S. Publicly Traded (BRK/a US)
Pizza Pizza Limited	739	519		Canadian Publicly Traded (PZA CN)
Pizza Pizza	637	426	Pizza	
Pizza 73	102	93	Pizza	
Domino's Pizza Canada	384	257	Pizza	U.S. Publicly Traded (DPZ US)
Pita Pit	200	226*	Pita Sandwich	Private company (Ontario)
Quiznos Canada[1]	392	225*	Sandwiches	Private company (U.S. based)
Chairman's Brands	434	211		Family-owned private company (Ontario)
Eggsmart	41	44	Breakfast (Full-service)	
Coffee Time Donuts	110	61.6*	Coffee/Baked Goods	
Robin's Donuts	143	43	Coffee/Baked Goods	
241 Pizza	90	43	Pizza	
New Orleans Pizza	50	19	Pizza	
Second Cup	337	180	Coffee/Baked Goods	Canadian Publicly Traded (SCU CN)
White Spot Limited	64	172	Hamburgers	Private company (B.C.)
Panago Pizza	183	154	Pizza	Private company (B.C.)
Booster Juice	311	139*	Juice / Smoothies	Private company (Alberta)
Pizza Nova	148	112	Pizza	Private company (Ontario)
Arby's of Canada[2]	109	91	Sandwiches	Private company: Roark Capital (Georgia)
Mary Brown's	120	85		Private company (Ontario)
New York Fries (Cara Operations)[3]	120	75	Fast Food	Public Company (CAO CN); acquired Aug.31/15
Edo International[4]	115	68	Asian (Japanese)	Private company (Alberta)
Gino's Pizza	98	52	Pizza	Private company (Ontario)

Notes:
1 Figures from 2014 Foodservice and Hospitality Top 100 Report.
2, 4. Figures from 2013 Foodservice and Hospitality Top 100 Report.
3. We estimate system sales of $75M for New York Fries and $10M for South St. Burger
* indicates that figures include some international store counts and sales

Source: Foodservice and Hospitality Magazine; Company Reports and Websites; Laurentian Bank Securities;

Exhibit 13: Canadian Casual Dining and Full Service Chains (Focusing on chains/groups with over $50M in system sales or over 30 locations)

Name	Total Units	Recent System Sales (M$)	Restaurant Concept	Parent Company / Owner / Ticker
Cara Operations	827	1,708		Canadian Publicly Traded (CAO CN)
Swiss Chalet	213	546	Family Dining	
Harvey's	262	267	Hamburgers (QSR)	
Montana's	92	234	Mid Casual	
Milestones Grill and Bar	54	169	Higher End Casual	
East Side Mario's	75	168	Family Dining	
Kelsey's	71	157	Family Dining	
Prime Pubs	29	63	Bar/Pub	
Casey's Grill and Bar	21	59	Mid Casual	
Bier Market	7	27	Higher End Casual	
The Landing Group	3	18	Higher End Casual	
Boston Pizza Canada	366	1,023	Family Dining	Boston Pizza International/Royalty (BPF-U CN)
Keg Restaurants Canada	88	501	Higher End Casual	Keg Restaurants/Royalty (KEG-U CN) Fairfax owns 51%
Northland Properties Corporation[1]	153	309		Northland Properties (B.C.)
Denny's Restaurants	55	103	Breakfast	
Moxie's Restaurants	64	206	Mid Casual	
Shark Club	11		Higher End Casual	
Bar One Urban Lounge			Bar / Pub	
Chop Steakhouse			Higher End Casual	
Rockford Wok / Bar / Grill			Higher End Casual	
St. Hubert[2]	117	387	Family Dining	Private company (Quebec)
Imvescor Restaurant Group[3]	229	369		Canadian Publicly Traded (IRG CN)
Pizza Delight	88	67	Family Dining	
Mikes	74	102	Family Dining	
Scores	43	106	Family Dining	
Baton Rouge	29	96	Higher End Casual	
SIR Corp	55	261		SIR Corp./Royalty (SRV-U CN)
Jack Astor's Bar and Grill	38	196	Mid Casual	
Canyon Creek Chop House	8	27	Higher End Casual	
Alice Fazooli's / Scaddabush	5	16	Mid Casual	
Reds, Far Niente, Four, Petit Four	4	21	Upper End Casual	
Franworks	89	229	Mid Casual	Franworks/Royalty (DIV CN)
Original Joes	63	156	Mid Casual	
State & Main	14	29	Mid Casual	
Elephant and Castle	12	41	Mid Casual	
Joey Restaurant Group	23	159	Family Dining	Private company (B.C)
Cora Franchise Group	130	145	Breakfast	Private company (Quebec)
Smitty's Canada	100	140	Family Dining	Private company (Alberta)
Mandarin Restaurant Corp	23	125	Family Dining	Private company (Ontario)
Sportscene Group	50	107	Bar/Pub	Canadian Publicly Traded (SPS/a CN)
Red Lobster[4]	27		Mid Casual	Private company (U.S.) - Golden Gate Capital
Darden Restaurants				U.S. Publicly Traded (DRI US)
Olive Garden	6		Mid Casual	
Obsidian Group[5]	110			Private company (Ontario)
Crabby Joe's Tap & Grill	41	83	Family Dining	
Coffee Culture Café[3]	58		Baked Goods/Café (QSR)	
Union Burger	11		Hamburgers (QSR)	
Sunset Grill Restaurants	118	94	Breakfast	Private company (Ontario)
Browns Socialhouse (Browns Restaurant Group)	38	70	Bar/Pub	Private company (B.C.)
Oliver & Bonacini[6]	11	68	Upper End Casual	Private company (Ontario)
Shoeless Joe's	34	61	Bar/Pub	Private company (Ontario)
Cactus Club Café	27	59	Upper End Casual	Private company (B.C.)
Firkin Group of Pubs	34	56	Bar/Pub	Private company (Ontario)
Red Robin Restaurants	18	56	Hamburgers (QSR)	Private company (B.C.)
Lone Star Texas Grill	23	54	Mid Casual	Private company (Ontario)
Pickle Barrel	11	52	Family Dining	Private company (Ontario)
Brewsters Brewing Company	14	50	Bar/Pub	Private company (Alberta)

Notes:
1, 5. Figures from 2013 Foodservice and Hospitality Top 100 Report.
2. Estimated system sales figure, based on figures from 2013 Foodservice and Hospitality Top 100 Report.
3. System sales data and restaurant count per banner based on fiscal 2014.
4, 6. Figures from 2014 Foodservice and Hospitality Top 100 Report.

Source: Foodservice and Hospitality Magazine; Company Reports and Websites; Laurentian Bank Securities;

4. Further improve network health and profitability

There are several initiatives being pursued in order to improve overall profitability of the network.

One of the primary focal points in this endeavour will be to monitor the number of franchisees receiving assistance from Cara. This assistance is generally offered through the franchise royalty fee (i.e. discount off of the 5% standard) and comes in two separate forms:

- Restaurants paying less than 5% royalty rate per corporate conversion agreements. At the end of Q2/15 there were 96 such restaurants under this category (versus 115 at Q4/14 and 132 at Q4/13). The lower royalty rate in this instance is typically used to incent a prospective franchisee to purchase an existing corporate restaurant. These discounts are typically contractual in nature and designed to scale towards the 5% normalized rate as sales at the purchased restaurant ramp higher (of note the bulk of this assistance is expected to expire at the end of 2018).
- Restaurants paying less than 5% for temporary assistance due to cash flow issues. At the end of Q2/15 there were 82 such restaurants under this category (versus 88 at Q4/14 and 108 at Q4/13). We would note that in addition to royalty assistance, such restaurants may also receive rent assistance. Our understanding is that such payments accrue over time, and represent an obligation owed to Cara by the franchisee if and when the restaurant returns to a suitable level of profitability. Under a situation where the franchisee profitability does not return to suitable levels, the store could then be closed or be subject to a corporate takeback.

Cara's goal is to raise the franchise royalty rate as a percentage of system sales closer to 5% versus 4.46% currently (LTM basis). Such a delta would increase franchise royalty income by ~$7.5M. That said, as we see the royalty percentage tick higher, we would also anticipate a reduction in the franchisee rent assistance and bad debt expense, which was $8.5M on an LTM basis. In Exhibit 14, we illustrate the progress Cara has made during H1/15 in terms of improving the franchise business profitability. As shown, the majority of margin gains recorded have come through a reduction of rent assistance and bad debt expense to $3.9M in H1/15 versus $6.2M in H1/14. At least part of this improvement would be associated with the reduction in franchise stores over the past year (i.e. unprofitable franchises), some of which were closed and some of which were subject to corporate takeback.

Exhibit 14: Change in Franchise Profitability

				LBS Forecast		
	H1/14	H1/15	Delta	2015e	2016e	2017e
Number of franchise restaurants	752	735		751	781	811
Franchise system sales	732,812	753,353		1,540,556	1,642,691	1,749,322
Franchise royalty income	31,913	33,565		68,989	75,165	80,469
As a percentage of franchise system sales	*4.35%*	*4.46%*	*0.10%*	*4.48%*	*4.58%*	*4.60%*
Franchise rent assistance and bad debt	-6,169	-3,909		-8,239	-8,706	-9,096
As a percentage of franchise system sales	*-0.84%*	*-0.52%*	*0.32%*	*-0.53%*	*-0.53%*	*-0.52%*
Total franchise contribution (EBITDA)	25,744	29,656		60,751	66,459	71,372
As a percentage of franchise system sales	*3.51%*	*3.94%*	*0.42%*	*3.94%*	*4.05%*	*4.08%*

Source: Company Reports; Laurentian Bank Securities

Shifting over to the corporate side, there is also an opportunity to increase profitability, with management targeting a corporate EBITDA contribution margin of 10-15% versus 8.9% on an LTM basis. The primary mechanisms being pursued to achieve this are:

- Food cost control. Per the 2015 Bottom Line Report, the average food cost as a percentage of sales was 29.4% for Canadian restaurants across all restaurant types (463 respondents);
- Labour cost control. Per the 2015 Bottom Line Report, the average labour cost as a percentage of sales was 30.6% for Canadian restaurants across all restaurant types (463 respondents); and
- Leveraging fixed costs (rent, utilities, overhead) through SSSG. This line item is running at ~$15-15.5M per quarter. We expect this to increase as the number of corporate restaurants moves higher, but we recognize some portion should be fixed (we currently estimate 20%).

In Exhibit 15 we illustrate the progress Cara has made in terms of improving its corporate restaurant profitability. As illustrated, during H1/15 food cost as a percentage of sales was 29.9% versus the *Bottom Line Report* benchmark of 29.4%. Given Cara's scale and buying power, we would anticipate this percentage to drop below the Canadian average over time. In terms of labour, this is where the majority of gains have been made y/y, and based on the 30.6% benchmark illustrated within the *Bottom Line Report*, it would appear that there are still gains to be made. We would note that our (fairly conservative) forecast has food cost as a percentage of sales dropping to 29.6% in 2017E, with labour cost as a percentage of sales dropping to 32.4%.

Exhibit 15: Change in Corporate Profitability

	H1/14	H1/15	y/y Delta	LBS Forecast 2015e	2016e	2017e
Number of corporate restaurants	83	92		100	105	110
Corporate Restaurant Sales	94,640	113,738		232,660	258,355	277,701
Food Cost (Cost of inventories sold)	29,034	33,977		69,219	76,731	82,200
As a percentage of corporate restaurant sales	*30.7%*	*29.9%*	*-0.8%*	*29.8%*	*29.7%*	*29.6%*
Labour Cost	35,015	37,659		75,927	83,965	89,975
As a percentage of corporate restaurant sales	*37.0%*	*33.1%*	*-3.9%*	*32.6%*	*32.5%*	*32.4%*
Other operating costs	26,765	30,123		60,723	64,444	66,640
As a percentage of corporate restaurant sales	*28.3%*	*26.5%*	*-1.8%*	*26.1%*	*24.9%*	*24.0%*
Total corporate contribution (EBITDA)	3,826	11,979		26,791	33,214	38,886
As a percentage of corporate restaurant sales	*4.0%*	*10.5%*	*+6.5%*	*11.5%*	*12.9%*	*14.0%*

Source: Company Reports; Laurentian Bank Securities

5. New retail licensing opportunities

With a limited retail presence (predominantly Swiss Chalet products), Cara sees opportunity to leverage its brands in order to sell product at grocery. While the payoff from launching a product at retail can be significant, with a pure licensing deal allowing an opportunity for a third party to invest the capital necessary for product development and manufacturing, we have seen some mixed results in terms of retail product launches over the past few years. At one end of the extreme we have seen Imvescor (IRG-T; Not Rated) successfully launch its Baton Rouge rib product, which has attained a very high market share and provides the company an estimated incremental royalty stream in the $3-$4M range. On the other hand, we saw MTY Food Group (MTY-T; Buy; $40 Target) struggle with its launch of Thai Express frozen products at retail.

Organic Growth and New Unit Growth Enough to Hit System Sales Target

As previously discussed, while growth via M&A is an important element of Cara's growth strategy, we would note that the company can reach its system sales target of $2.5-$3.0 billion over the next 5-7 years through simply executing on growth strategies 1 and 2 (net new store openings and SSSG).

In particular, looking at Exhibit 16, using 2015e system sales of $1.77 billion as a base, we show the various 5-7 year scenarios that are feasible. As illustrated, hitting the midpoint of the SSSG target and net new store opening target yields system sales at the low end of the range (i.e. $2.5 billion) in five years.

Exhibit 16: Estimated Cara System Sales Under Various Scenarios ($ billion)

Using 2015e system sales of $1.77 billion as a base year

				SSSG		
	5 years	*2.5%*	*3.0%*	*3.25%*	*3.5%*	*4.0%*
	30	2.31	2.36	2.38	2.41	2.46
Annual	35	2.36	2.41	2.43	2.46	2.51
# of New	40	2.41	2.46	2.48	2.51	2.56
Builds	45	2.46	2.51	2.53	2.56	2.61
	50	2.51	2.56	2.58	2.61	2.66

				SSSG		
	7 years	*2.5%*	*3.0%*	*3.25%*	*3.5%*	*4.0%*
	30	2.53	2.60	2.64	2.68	2.75
Annual	35	2.60	2.67	2.71	2.75	2.82
# of New	40	2.67	2.74	2.78	2.82	2.89
Builds	45	2.74	2.81	2.85	2.89	2.96
	50	2.81	2.88	2.92	2.96	3.03

Source: Laurentian Bank Securities Estimates

Financial Forecast

In this section, we will discuss some specific details with respect to our financial forecast. A snapshot of our forecast is in Exhibit 17.

Restaurant growth

In 2014, Cara added four net new restaurants (three added through the acquisition of The Landing Group, five new openings, four closures, and including 10 corporate take-backs). In the first half of 2015, there were 10 net closures (predominantly East Side Mario's and Casey's). **For the second half of 2015, we are forecasting 24 net new openings** (20 franchise/four corporate) which is in line with management's guidance and represents a significant reversal in the new opening trend. Additionally, we are forecasting 35 new openings in both 2016 and 2017 (five corporate/30 franchise), which is towards the lower end of management guidance of 30-50 net new openings.

Consolidated SSSG

Cara reported consolidated SSSG of +3.3% in Q1/15 and +3.2% in Q2/15, and we are forecasting consolidated SSSG of +3.0% through the balance of 2015. The consolidated number includes both corporate and franchise locations. For 2016 and 2017, we are forecasting +3.0% and +2.5% respectively. Similar to our forecast on net new store openings, our SSSG forecast is at the lower end of management's guidance of +2.5-4.0%.

System sales

In 2014, system sales (which includes corporate and franchise sales) increased +24.5% over 2013. This growth was essentially driven by the late 2013 acquisition of Prime. We are forecasting system sales growth of +4.6% to $1,773.2M for 2015, +7.2% to $1,901.0M in 2016 and +6.6% to $2,027.0M in 2017. We have yet to factor the New York Fries acquisition into our numbers, but this would add approximately $75M to our annual system sales.

Corporate segment

For the Corporate restaurant segment, we are forecasting EBITDA of $26.8M in 2015 versus $10.8M in 2014, which represents an 11.5% margin versus 5.5%. Looking ahead, we are forecasting $33.2M in 2016 (12.9% margin) and $38.9M in 2017 (14.0% margin). In terms of the margin expansion, we see continued modest improvement on the cost of goods sold line and cost of labour line (as these numbers trend towards Canadian averages communicated in The Bottom Line Report), with the potential for significant leverage on the other operating cost line (which has a meaningful fixed cost component embedded as it relates to rent, utilities and overhead).

Franchise segment

For the Franchise segment, we are forecasting EBITDA of $60.8M in 2015 versus $55.3M in 2014, which represents a margin of 3.94% of franchise system sales versus 3.69% in 2014. For 2016, we are forecasting a margin of 4.05% of franchise system sales ($66.5M EBITDA) and 4.08% of franchise system sales in 2017 ($71.4M of EBITDA). We view these forecasts as quite conservative overall from a margin expansion perspective.

Central segment

For the Central segment, we are forecasting EBITDA of $23.4M in 2015 versus $17.4M in 2014, which represents 1.3% of total system sales versus 1.0% in 2014. For 2016 and 2017 we see the margin within this segment as stable at the 1.3% level. Similar to our forecast at the franchise level, we view this as quite conservative overall.

Taxes, net earnings and EPS

We are forecasting a 26% tax rate, which is in line with management's guidance. However, given the expected tax loss carry forwards, Cara is not expected to have cash taxes until 2017. For 2015, we are forecasting adjusted net earnings (from continuing operations) of $53.1M and fully diluted EPS of $0.99 per share. In 2016, adjusted net earnings are forecasted to grow +29.8% to $68.9M (EPS of $1.28), and +13.2% to $78.0M in 2017 (EPS of $1.45).

FCF profile

Using the traditional calculation for free-cash-flow (FCF), cash flow from operating activity minus CAPEX, we calculate FCF for 2014 of $70.7M. In terms of CAPEX, we are forecasting spending of $24.5M in 2015 and $25M in both 2016 and 2017, which is in line with management's guidance (and excludes potential incremental corporate takebacks). As such, our FCF estimate is $58.2M in 2015, $97.8M in 2016 and $82.6M in 2017. Note the reduction in FCF in 2015 versus 2014 is related to our working capital forecast (i.e. -$5.5M in 2015 versus +$11.6M in 2014), with the 2017 reduction versus 2016 related to the elimination of tax loss carry-forwards.

Balance sheet

At the end of Q2/15, net debt was $63.6M, with net debt / EBITDA of 0.7x. For 2015, we are forecasting net debt of $12.4M which implies net debt / EBITDA of 0.1x. Looking into 2016 and 2017, we are forecasting that Cara will have a net cash position, with an estimated net debt / EBITDA of -0.7x and -1.2x respectively. This net debt calculation excludes the $24.5M gift card liability that was on Cara's balance sheet at the end of Q2/15.

As of Q2/15, Cara has a $150M term credit facility (with a $50M accordion feature) upon which $41M has been drawn. The current effective interest rate on the facility is 2.6%. In the case of a large M&A transaction, we believe the company could easily get its current credit facility upsized.

Dividend growth expected

The current annualized dividend is $0.37 per share (1.1% yield). The company can clearly afford a higher payout and we would anticipate dividend increases over time. Cara also offers investors a dividend reinvestment plan (which comes with a purchase price discount of 3%).

Exhibit 17: Cara Operations Summary Financial Forecast

All amounts in $M unless otherwise indicated	f2013	f2014	f2015e	f2016e	f2017e
Number of Restaurants					
Corporate	77	91	100	105	110
Franchise	756	746	751	781	811
Total	833	837	851	886	921
Consolidated SSSG	*0.5%*	*2.6%*	*3.1%*	*3.0%*	*2.5%*
System Sales					
Corporate	185.0	195.4	232.7	258.4	277.7
Franchise	1,177.1	1,500.6	1,540.6	1,642.7	1,749.3
Total	1,362.1	1,696.0	1,773.2	1,901.0	2,027.0
y/y growth		*24.5%*	*4.6%*	*7.2%*	*6.6%*
Total Cara Revenue	270.6	281.8	318.4	348.9	373.8
y/y growth		*4.1%*	*13.0%*	*9.6%*	*7.1%*
EBITDA					
Corporate	-2.2	10.8	26.8	33.2	38.9
as a percentage of corporate system sales	*-1.2%*	*5.5%*	*11.5%*	*12.9%*	*14.0%*
cost of goods sold	*30.4%*	*30.4%*	*29.8%*	*29.7%*	*29.6%*
cost of labour	*42.2%*	*38.3%*	*32.6%*	*32.5%*	*32.4%*
Franchise	41.7	55.3	60.8	66.5	71.4
as a percentage of franchise system sales	*3.5%*	*3.7%*	*3.9%*	*4.0%*	*4.1%*
average royalty rate	*4.5%*	*4.4%*	*4.5%*	*4.6%*	*4.6%*
franchise rent assistance and bad debt	*-1.0%*	*-0.7%*	*-0.5%*	*-0.5%*	*-0.5%*
Central	8.4	17.4	23.4	24.6	26.3
as a percentage of total system sales	*0.6%*	*1.0%*	*1.3%*	*1.3%*	*1.3%*
Total EBITDA	47.9	83.6	110.9	124.3	136.5
as a percentage of total system sales	*3.5%*	*4.9%*	*6.3%*	*6.5%*	*6.7%*
as a percentage of sales	*17.7%*	*29.7%*	*34.8%*	*35.6%*	*36.5%*
Tax rate	*na*	*na*	*20.3%*	*26.0%*	*26.0%*
Adjusted Net earnings (continuing operations)	-42.2	5.4	53.1	68.9	78.0
Adjusted EPS (Fully Diluted)	na	$0.90	$0.99	$1.28	$1.45
Operating cash flow	61.7	76.8	88.2	124.3	109.1
Delta working capital	-22.4	11.6	-5.5	-1.5	-1.5
Cash flows from operating activities	39.3	88.4	82.7	122.8	107.6
CAPEX	-17.9	-17.7	-24.5	-25.0	-25.0
Free cash flow	21.4	70.7	58.2	97.8	82.6
FCF per Fully Diluted Share	na	na	1.08	1.82	1.53
Net Debt	295.49	274.6	12.4	-83.2	-163.6
Net Debt / EBITDA	6.2x	3.3x	0.1x	-0.7x	-1.2x

Note: In Oct. 2013, Cara acquired Prime Restaurants Inc. (4 brands) which contributed $44.0M to total sales in 2014f (versus $5.2M in 2013f).

Source: Company Reports; Laurentian Bank Securities Estimates

Valuation and Recommendation

We compare Cara Operations with a group of publicly-traded North American restaurants, which includes full-service restaurants, quick-service restaurants and fast casual restaurants. These restaurants also contain different levels of franchising which influences capital intensity and return on invested capital. We would note that most of the companies in this list have a much larger market capitalization than Cara and lower banner diversification (Cara's 10 compared to the peer group average of two).

Exhibit 18: North American Restaurant Comparables (Quick Service, Full Service, Fast Casual)

Ticker	Short Name	Year End	Price ($)	Div. Yield	Shares Out (M)	Market Cap (M$)	Net Debt (M$)	EV (M$)	P/E 2014a	P/E 2015e	P/E 2016e	P/E 2017e	EV/EBITDA 2014a	EV/EBITDA 2015e	EV/EBITDA 2016e	EV/EBITDA 2017e	EBITDA CAGR 14-16e	Restaurant Type	Percent Franchised	# of Brands
Full-service Restaurants, >50% Franchised																				
DIN US	DINEEQUITY INC	Dec	90.16	2.5%	19	1,701	1,345	3,046	19.1x	15.3x	14.5x	na	12.3x	11.1x	10.8x	na	6.8%	FSR	99%	2
DENN US	DENNY'S CORP	Nov	11.05	na	83	920	155	1,076	29.9x	25.1x	22.6x	na	13.7x	11.2x	10.5x	na	14.0%	FSR	91%	1
BWLD US	BUFFALO WILD WIN	Dec	193.19	0.0%	19	3,673	-92	3,582	38.0x	34.5x	27.1x	21.9x	15.3x	12.6x	10.1x	8.6x	23.0%	FSR	54%	3
RUTH US	RUTH'S HOSPITALI	Dec	16.11	1.2%	35	567	-5	562	21.8x	19.0x	17.3x	na	10.6x	9.9x	9.2x	na	7.6%	FSR	53%	1
									27.2x	**23.5x**	**20.4x**	**21.9x**	**13.0x**	**11.2x**	**10.2x**	**8.6x**				
Full-service Restaurants, <50% Franchised																				
EAT US	BRINKER INTL	June	51.93	2.2%	60	3,121	919	4,040	16.8x	14.4x	12.9x	11.7x	8.9x	7.9x	7.6x	7.0x	7.9%	FSR	45%	2
RRGB US	RED ROBIN GOURME	Dec	74.89	0.0%	14	1,061	122	1,184	28.2x	23.2x	20.0x	16.7x	10.8x	8.0x	7.2x	6.6x	22.8%	FSR	19%	1
TXRH US	TEXAS ROADHOUS	Dec	37.20	1.6%	70	2,607	-20	2,593	30.2x	27.0x	22.4x	19.0x	13.7x	12.0x	10.2x	9.1x	16.0%	FSR	17%	2
BLMN US	BLOOMIN' BRANDS	Dec	18.53	0.3%	123	2,272	1,188	3,490	16.8x	14.5x	12.6x	10.8x	9.1x	7.5x	6.9x	6.3x	14.9%	FSR	11%	4
(7) RT US	RUBY TUESDAY INC	May	6.15	0.0%	63	385	170	555	*nm*	*43.9x*	*32.4x*	*38.4x*	6.9x	7.2x	7.1x	6.7x	-1.6%	FSR	11%	2
DRI US	DARDEN RESTAURAN	May	68.11	3.2%	128	8,697	763	9,459	25.9x	21.1x	18.6x	17.4x	13.8x	9.9x	9.2x	8.7x	22.4%	FSR	1%	8
BJRI US	BJ'S RESTAURANTS	Dec	42.14	na	26	1,079	49	1,128	*40.9x*	28.1x	23.5x	20.1x	12.4x	9.8x	8.5x	7.5x	21.1%	FSR	0%	4
(5) CAKE US	CHEESECAKE FACTO	Dec	53.44	1.1%	49	2,623	-37	2,586	27.1x	22.8x	19.9x	18.4x	11.4x	10.1x	9.2x	8.8x	10.9%	FSR	0%	1
CBRL US	CRACKER BARREL	July	143.58	4.9%	24	3,440	135	3,574	25.5x	21.1x	19.7x	18.2x	12.9x	10.9x	10.2x	9.7x	12.3%	FSR	0%	1
DFRG US	DEL FRISCO'S RES	Dec	13.55	0.0%	23	318	-2	316	16.5x	15.9x	13.9x	11.5x	8.5x	6.8x	6.0x	5.2x	19.0%	FSR	0%	3
CHUY US	CHUY'S HOLDINGS	Dec	26.45	0.0%	16	436	-8	428	*38.3x*	*31.0x*	27.0x	25.2x	16.3x	12.6x	10.9x	9.8x	22.5%	FSR	0%	1
									23.4x	**20.9x**	**19.0x**	**16.9x**	**11.3x**	**9.3x**	**8.5x**	**7.8x**				
Quick-service Restaurants																				
DNKN US	DUNKIN' BRANDS G	Dec	48.78	1.9%	95	4,646	2,174	6,820	28.0x	25.4x	21.7x	19.2x	17.7x	16.5x	15.3x	14.2x	7.6%	QSR	100%	2
(2) QSR US	RESTAURANT BRAND	Dec	36.14	na	467	16,894	8,340	30,530	36.5x	35.1x	28.7x	24.4x	19.8x	19.1x	17.4x	15.9x	6.6%	QSR	100%	2
PLKI US	POPEYES LOUISIAN	Dec	55.20	0.0%	23	1,264	100	1,364	33.5x	29.0x	24.9x	na	18.6x	16.1x	14.2x	na	14.2%	QSR	97%	1
DPZ US	DOMINO'S PIZZA	Dec	108.54	0.9%	55	5,960	1,502	7,462	37.4x	31.0x	26.8x	23.1x	19.6x	17.1x	15.6x	14.1x	12.2%	QSR	97%	1
SONC US	SONIC CORP	Aug	23.49	0.4%	52	1,220	443	1,663	28.0x	21.5x	18.6x	16.5x	11.8x	10.2x	9.5x	9.2x	11.4%	QSR	89%	1
KKD US	KRISPY KREME	Jan	14.87	0.0%	63	936	-33	903	21.2x	18.8x	17.3x	na	14.8x	12.1x	10.4x	na	19.1%	QSR	89%	1
WEN US	WENDY'S CO/THE	Dec	8.78	2.3%	290	2,549	1,200	3,748	25.8x	27.7x	24.9x	21.3x	9.1x	9.4x	9.7x	9.7x	-3.2%	QSR	87%	1
PZZA US	PAPA JOHN'S INTL	Dec	67.72	0.8%	39	2,672	212	2,905	38.7x	32.5x	27.9x	24.6x	18.4x	16.6x	15.0x	14.0x	10.8%	QSR	85%	1
MCD US	MCDONALDS CORP	Dec	95.96	3.4%	942	90,376	13,903	104,279	19.9x	20.4x	18.6x	17.0x	10.9x	12.1x	11.5x	11.0x	-2.7%	QSR	81%	1
(1) YUM US	YUM! BRANDS INC	Dec	76.00	2.1%	431	32,772	2,763	35,599	24.6x	21.6x	18.6x	16.8x	15.5x	11.9x	10.5x	9.7x	21.3%	QSR	79%	3
JACK US	JACK IN THE BOX	Sept	77.37	0.5%	37	2,830	641	3,471	31.6x	25.6x	21.7x	20.8x	13.7x	12.0x	10.9x	10.2x	12.2%	QSR/FC	74%	2
(3) SBUX US	STARBUCKS CORP	Sept	55.77	1.0%	1,484	82,774	722	83,498	*41.9x*	35.2x	29.7x	25.7x	21.8x	18.5x	16.1x	14.2x	16.5%	QSR	0%	4
									29.6x	**27.0x**	**23.3x**	**20.9x**	**16.0x**	**14.3x**	**13.0x**	**12.2x**				
Fast Casual Restaurants																				
HABT US	HABIT RESTAURA-A	Dec	21.27	0.0%	26	553	-52	557	*236.3x*	*81.5x*	*65.2x*	*64.5x*	32.1x	22.6x	17.7x	15.2x	34.7%	FC	88%	1
PNRA US	PANERA BREAD-A	Dec	189.27	0.0%	26	4,882	-25	4,857	29.0x	30.6x	28.2x	22.7x	12.1x	12.3x	11.7x	10.2x	1.9%	FC	51%	3
NDLS US	NOODLES & CO	Dec	13.70	0.0%	28	389	28	417	36.1x	49.3x	40.8x	35.1x	9.5x	9.4x	8.2x	7.3x	7.5%	FC	14%	1
PBPB US	POTBELLY CORP	Dec	10.79	0.0%	30	326	-54	272	*49.0x*	39.1x	31.9x	25.7x	10.1x	7.8x	6.7x	5.6x	22.8%	FC	8%	1
ZOES US	ZOE'S KITCHEN IN	Dec	36.53	0.0%	19	708	3	711	*nm*	*493.6x*	*259.1x*	*105.3x*	*125.4x*	38.2x	30.5x	24.7x	102.8%	FC	2%	1
CMG US	CHIPOTLE MEXICAN	Dec	708.03	na	31	22,049	-879	21,170	50.1x	40.8x	34.3x	28.7x	25.8x	20.8x	17.7x	15.1x	20.8%	FC	0%	3
(4) SHAK US	SHAKE SHACK IN-A	Dec	47.94	0.0%	36	1,738	-65	1,676	*299.6x*	*191.0x*	*155.1x*	*126.2x*	*185.0x*	*57.9x*	*48.4x*	*40.3x*	95.5%	FC	0%	1
									38.4x	**39.9x**	**33.8x**	**28.0x**	**17.9x**	**18.5x**	**15.4x**	**13.0x**				
Average, all companies above									**28.3x**	**26.4x**	**22.9x**	**20.5x**	**14.3x**	**12.7x**	**11.2x**	**10.2x**				
MTY CN	**MTY FOOD GROUP**	**Nov**	**31.23**	**1.1%**	**19**	**597**	**7**	**604**	**21.6x**	**19.4x**	**18.2x**	**na**	**14.2x**	**12.1x**	**11.3x**	**na**	**11.7%**	**QSR**	**98%**	32
(6) **CAO**	**CARA OPERATIONS**	**Dec**	**32.75**	**1.2%**	**54**	**1,763**	**57**	**1,820**	**36.4x**	**33.2x**	**25.6x**	**22.6x**	**21.8x**	**16.4x**	**14.6x**	**13.3x**	**21.9%**	**FSR/QSR**	**89%**	10

Notes:
(1) YUM Brands consists of Taco Bell (QSR), KFC (QSR) and Pizza Hut (FSR).
(2) 2014 EBITDA is a pro-forma number provided within BKW Q4/14 presentation.
(3) ~50% of SBUX locations are licensed.
(4) ~49% of SHAK locations are licensed.
(5) ~4% of CAKE locations are licensed.
(6) CAO Net debt and shares outstanding estimated pro-forma offering.
(7) Ruby Tuesday's EBITDA is adjusted for impairment charges.

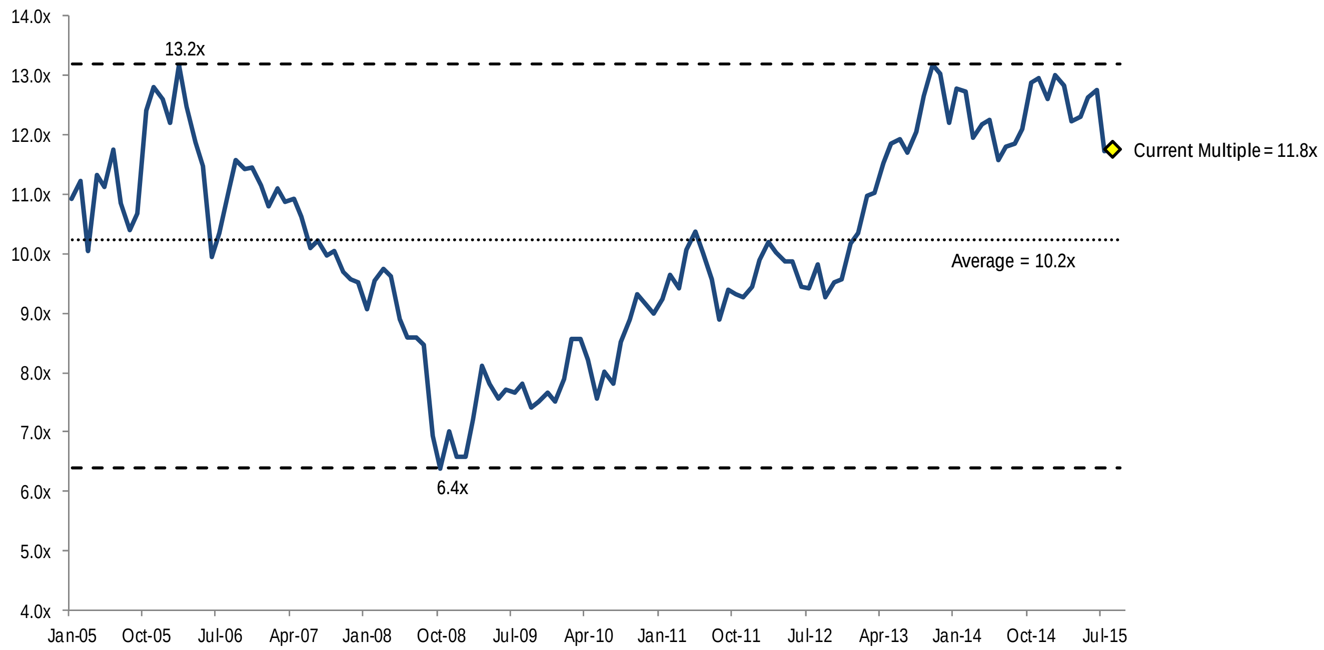
Numbers in italics are excluded from averages.

Source: Bloomberg; Laurentian Bank Securities

Cara is trading at an EV / EBITDA multiple of 16.4x our 2015 estimate, 14.6x our 2016 estimate and 13.3x our 2017 estimate. Our comp group trades closer to 12.7x 2015, 11.2x 2016 and 10.2x 2017. On a P/E basis, Cara is trading at 33.2x 2015, 25.6x 2016 and 22.6x 2017. Our comp group trades closer to 26.4x 2015, 22.9x 2016 and 20.5x 2017. Cara is clearly trading at a premium to its restaurant peers, and if we narrow in explicitly on full-service restaurants, that premium becomes even more meaningful.

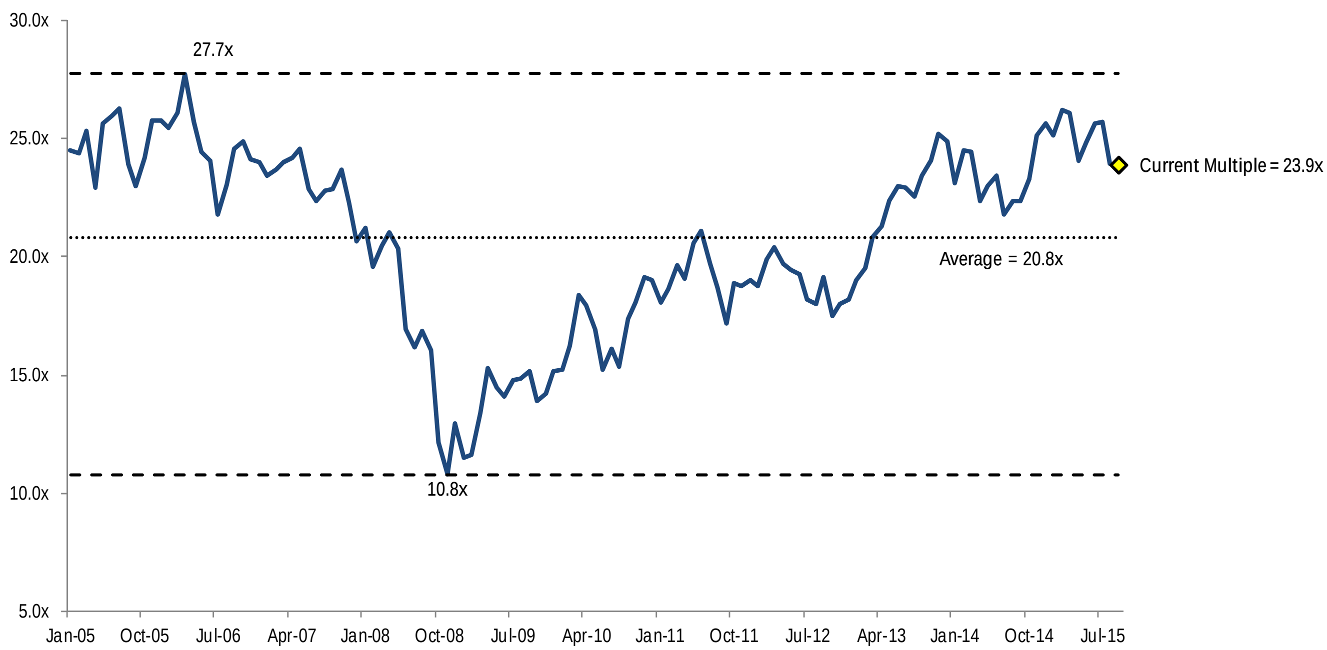
In Exhibits 19 and 20 we illustrate the average 1-year forward (i.e. 12 month forward) historical trading multiple for the peer group outlined in Exhibit 18. As illustrated, on a long-term basis, U.S. peers are trading above their respective 10 year average for both EV / EBITDA (11.8x versus 10.2x) and P/E (23.9x versus 20.8x).

Exhibit 19: U.S. Restaurants - 1 year Forward EV/EBITDA Multiple (Jan/05 to Present)



Source: Bloomberg, Laurentian Bank Securities.

Exhibit 20: U.S. Restaurants - 1 year Forward P/E Multiple (Jan/05 to Present)



Source: Bloomberg, Laurentian Bank Securities.

As we look at our timeframe for determining our target price, our view is that investors should focus on the longer-term profile for Cara. In determining our target multiple for Cara, we take into consideration:

1. **Strong balance sheet (0.7x net debt/EBITDA)** and the ability for Cara to deploy capital towards accretive M&A (note that our forecast does not include any potential M&A activity or the acquisition of New York Fries which was announced on August 31, 2015).
2. **Potential upside to our forecast**, given our estimates which factor in net new store openings and SSSG at the low end of management's target range. Of note, Cara has targeted 30-50 net new openings per year and we have forecast 35 in 2016 and 2017 (mix of 5 corporate / 30 franchised). Regarding SSSG, we are forecasting +3% in 2016e and +2.5% in 2017e, versus management guidance of +2.5-4.0%.
3. **Multiple growth opportunities available to expand the business.** As we have previously discussed, beyond growing SSSG and new locations there is a significant opportunity to grow the business through acquisitions of new banners and from improvements to the network's profitability.
4. **Significant investor demand for the stock.** Cara's IPO was significantly oversubscribed with pricing above the high-end of the initial indicated range. Additionally, the stock traded up +42.7% on its first day of trading highlighting significant interest in the name (where the float remains relatively small at just under $400M).

Management team with a turnaround track record. Cara's CEO Bill Gregson is extremely well-regarded among institutional investors due to his association with The Brick and Forzani Group.

We have selected a target multiple of 14x 2017e EBITDA, which is effectively where the IPO was priced at $23 per share. This multiple also represents a discount of 2.4x on the current 2015 trading multiple and a discount of 0.6x on the current 2016 trading multiple. While we recognize this is a large premium versus its peers, we believe this is justified for the aforementioned reasons. **We also have a view that investors are paying a premium in the expectation that the company will be able to complete a large and meaningful acquisition.** We have also opted to include Cara's forecast Gift card liability as an obligation in our valuation for conservatism and nuances underlying the obligation for this particular item.

In Exhibit 21, we present our target price derivation. **Our one-year target price for Cara is $38.00, which reflects an all-in return of 15% from current levels. Therefore, we rate the shares a Buy.**

Exhibit 21: Cara Target Price Derivation

	2015e	2016e	2017e
EBITDA	110,928	124,261	136,513
Multiple	14.0x	14.0x	14.0x
Enterprise Value	1,552,994	1,739,649	1,911,177
Net debt (net cash)	-18,642	-114,242	-194,697
Gift card liability	49,535	49,535	49,535
Equity value	1,522,101	1,804,356	2,056,339
Target price	28.27	33.51	38.19
Shares outstanding (fully diluted)	53,840	53,840	53,840

Note: Net debt figure includes option proceeds.

Source: Laurentian Bank Securities Estimates

Risks

Franchisee recruitment

Cara's store growth is contingent on its ability to continue to recruit new franchisees to open new restaurants. Successful franchisees are generally well capitalized with some level of operating experience at the restaurant level. If Cara is not able to recruit franchisees, this may lead to a slowdown in new store openings which could negatively impact the company's ability to grow its royalty revenues.

Real estate market

The Canadian real estate market continues to perform well and lease rates on high quality locations remains high. High lease rates can impair unit economics over the medium-term as a new store matures and/or a period of slower sales occurs (i.e. recession). If earnings become depressed at a particular unit, this may prompt the franchisee to close the store and cease operations. In the case of a corporate store, the same situation could occur.

Head lease exposure

Cara is on the head lease for a large number of franchise locations. This implies that if a franchisee walks away from their business, or has an inability to pay rent, Cara is obligated to pay that franchisees' rent to the landlord. In a period of prolonged economic weakness, if a large portion of franchisees walk away from their restaurants, this could create a significant financial burden for the company.

Forecast predicated on a turnaround

While Cara's balance sheet is currently in good condition, the underlying restaurant operations are in a turnaround situation and management has communicated a plan to investors. As at Q2/15, 178 franchised restaurants (or 24.2% of all restaurants) were receiving some form of royalty assistance from the franchisor. Our forecast is predicated on a steady reduction in the number of franchisees receiving assistance over time. If management's plan to turn around the restaurants does not occur, this would have negative implications for our financial forecast.

Highly competitive environment

The foodservice industry and the full-service restaurant segment are extremely competitive in terms of market share, quality, brand, customer service and location. While Cara's brands are diversified to some degree, multiple brands overlap in terms of average cheque and style.

Multiple voting share structure

The voting of Cara is controlled by Fairfax through ownership of multiple voting shares. Fairfax owns ~40% of the equity of CAO-T which through multiple voting shares provides 52.56% of voting power. This ownership can influence the outcome of shareholder votes. Additionally, Fairfax has the ability to appoint one additional Director to the Board in the case of a deadlock.

Acquisition strategy

Part of Cara's growth strategy involves the pursuit of acquisitions and new concepts. This strategy exposes the company to various integration risks, including potential complications in terms of quickly and efficiently integrating acquired operations and realizing anticipated synergies. Additionally, we believe there is an expectation in the market that Cara will be successful completing a large M&A transaction. If no such transaction comes, we could see Cara's multiple get rerated lower.

Challenges of multiple banners

Cara offers franchises in eight of its ten banners. While multiple concepts and formats helps to diversify the portfolio overall, it could also lead to distractions and underperformance among banners where less emphasis may be placed. In that regard, it is necessary that each banner and brand have appropriate management at the corporate level to ensure it remains relevant in the market.

Economic conditions, discretionary spending, changes in sales tax

A weak economy and specifically, a decline in consumer confidence / discretionary spending could negatively impact sales. This is likely to be more visible among the higher-end banners (i.e. "Premium Casual") compared to those in the Family Dining or QSR segment. Additionally, an increase in sales tax rates can have a negative effect on consumer spending and consequently the same-store sales growth of a restaurant or group of restaurants.

Regulatory environment

The company is subject to various government laws and restrictions. Significant changes or the introduction of new laws and regulations related to product safety, nutritional content, labelling and sanitation could increase the cost of compliance and increase exposure to litigation and agency investigations.

Food safety and raw material availability

Negative publicity with respect to food safety and food-borne illness could adversely affect brand reputation and traffic. Outbreaks of food-borne disease, at a Cara brand or that of a competitor, could reduce traffic and result in the temporary closure of restaurants and negatively impact system sales.

Management Profiles

Bill Gregson, Chairman and CEO. Mr. Gregson has held the role of CEO since October 2013 and is also the Chairman of the Board of Directors. Prior to joining Cara, Mr. Gregson was the Executive Chair of the Board of The Brick (January 2012 – March 2013), The Brick's President and CEO (July 2009 – December 2011), as well as President and COO of Forzani. Mr. Gregson is currently a director of Keg Restaurants Ltd.

Ken Grondin, CFO. Prior to joining Cara as CFO in October 2013, Mr. Grondin was the CFO and President Financial Operations of The Brick (August 2011 – April 2013), Senior Vice President and CFO of Parkland Fuel Corporation (2009 – 2011), CFO and Board Member of Nygard International (2001 – 2009) and Partner – Head of Tax Division (Winnipeg) for Arthur Andersen (1997 – 2001). Mr. Grondin is a Chartered Accountant, Certified Management Accountant and a Chartered Business Valuator.

Kenneth Otto, President, Family Dining Division & Chief Development Officer. Prior to joining Cara in 2014, Mr. Otto was with Boston Pizza as COO (June 2011 to August 2014), where he also held other senior executive roles (from June 2004 to May 2011).

Grant Cobb, Senior Vice President, Casual Dining Division. Mr. Cobb has held his current role since 2014, prior to which he was Senior Vice President, Brand Management (2009-2014) and Senior Vice President, Casey's and Pubs (2008-2009). Before joining Cara, Mr. Cobb managed large food service businesses including Casey's and Pat & Mario's, and was a primary shareholder of Prime prior to its acquisition by Cara in 2013.

Stephen Gunn, Director. Mr. Gunn is the Chair of Sleep Country Canada Inc. and previously served as its CEO from 1997 to 2014. Mr. Gunn is also the Lead Director of Dollarama (since 2009) as well as a director of Golfsmith International Holdings GP Inc. and Mastermind Toys.

Christopher Hodgson, Director. Mr. Hodgson is the President of the Ontario Mining Association and previously served as Lead Director for The Brick.

Michael Norris, Director. Mr. Norris has been a director with Cara since 2012 and served as interim Chairman from October 31, 2013 until closing of the IPO. Previously, Mr. Norris was Deputy Chair of RBC Capital Markets (2003 – 2012) and also held multiple positions there including Head of Global Investment Banking (1998 – 2003).

John Rothschild, Director. Mr. Rothschild has been a director since October 2013 and was previously Senior Vice President, Restaurant Development from October 2013 to his retirement in November 2014. Prior to Cara, Mr. Rothschild was the CEO of Prime (1992 – 2014).

Sean Regan, Director. Mr. Regan has held the role of President of Cara Holdings since October 2013, prior to which he was the Senior Vice President, Corporate Development (2013) and head of the IT Group (2009 – 2013).

Financial Statements

Exhibit 22: Cara Operations Financial Statements

Income Statement ($000) - Year End Dec 31	f2013	f2014	Q1/2015	Q2/2015	Q3/2015e	Q4/2015e	f2015e	Q1/2016e	Q2/2016e	Q2/2016e	Q2/2016e	f2016e	f2017e
Consolidate same-store-sales growth (SSSG)	*0.5%*	*2.6%*	*3.3%*	*3.2%*	*3.0%*	*3.0%*	*3.1%*	*3.0%*	*3.0%*	*3.0%*	*3.0%*	*3.0%*	*2.5%*
Number of Corporate Restaurants	77	91	92	92	98	100	100	100	102	104	105	105	110
Number of Franchised Restaurants	756	746	742	735	743	751	751	756	766	778	781	781	811
Total Number of Restaurants	833	837	834	827	841	851	851	856	868	882	886	886	921
Corporate Restaurant Sales	184,991	195,424	53,146	60,592	62,475	56,446	232,660	59,826	69,193	68,289	61,047	258,355	277,701
Franchised Restaurant Sales	1,177,114	1,500,616	376,991	376,362	383,869	403,333	1,540,556	394,564	402,088	414,011	432,028	1,642,691	1,749,322
Total System Sales	1,371,943	1,696,040	430,137	436,954	446,345	459,780	1,773,215	454,389	471,282	482,300	493,075	1,901,046	2,027,023
y/y sales growth	*4.7%*	*23.6%*					*4.6%*	*5.6%*	*7.9%*	*8.1%*	*7.2%*	*7.2%*	*6.6%*
Revenue													
Sales	194,829	205,073	55,784	62,786	64,779	58,866	242,215	62,232	71,646	70,815	63,682	268,375	288,547
Franchise revenues	74,306	71,754	18,196	18,070	18,524	19,400	74,190	19,203	19,545	20,294	21,123	80,165	84,869
Development revenues	1,511	4,979	1,686	81	100	100	1,967	100	100	100	100	400	400
Total revenue	270,646	281,806	75,666	80,937	83,403	78,366	318,372	81,535	91,291	91,209	84,905	348,941	373,816
Cost of inventories sold	56,285	59,379	16,021	17,956	18,514	16,727	69,219	17,768	20,550	20,282	18,131	76,731	82,200
SG&A	142,603	139,532	35,045	36,646	37,715	35,482	144,889	37,618	41,017	40,647	37,834	157,116	165,712
Franchisor overcontribution to advertising fund	886	1,493	2,199	2,229	2,045	2,045	8,518	2,045	2,045	2,045	2,045	8,180	7,580
Depreciation of PP&E	23,747	17,413	4,689	4,732	4,700	4,700	18,821	4,700	4,700	4,700	4,700	18,800	18,800
Amortization of other assets	302	2,503	1,009	957	1,000	1,000	3,966	900	900	900	900	3,600	3,600
Other	5,072	1,756	-2,395	-2,988	-2,600	-2,678	-10,660	-2,669	-2,768	-2,833	-2,896	-11,167	-12,008
Development expenses	1,520	4,451	1,645	76	100	100	1,921	100	100	100	100	400	400
Restructuring	16,929	11,495	-205	436	0	0	231	0	0	0	0	0	0
Operating income	1,803	43,784	17,658	20,893	21,928	20,989	81,468	21,073	24,747	25,368	24,092	95,281	107,533
EBITDA													
Corporate	-2,241	10,826	3,927	8,052	8,357	6,455	26,791	6,531	9,757	9,554	7,372	33,214	38,886
as a % of corporate system sales	*-1.2%*	*5.5%*	*7.4%*	*13.3%*	*13.4%*	*11.4%*	*11.5%*	*10.9%*	*14.1%*	*14.0%*	*12.1%*	*12.9%*	*14.0%*
Franchise	41,716	55,324	14,916	14,740	15,163	15,932	60,751	15,861	16,164	16,850	17,584	66,459	71,372
as a % of franchise system sales	*3.5%*	*3.7%*	*4.0%*	*3.9%*	*4.0%*	*4.0%*	*3.9%*	*4.0%*	*4.0%*	*4.1%*	*4.1%*	*4.0%*	*4.1%*
Central	8,434	17,416	6,102	5,584	5,753	5,948	23,387	5,926	6,071	6,209	6,382	24,587	26,254
as a % of total system sales	*0.6%*	*1.0%*	*1.4%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*
Total EBITDA	47,909	83,566	24,945	28,376	29,273	28,334	110,928	28,318	31,992	32,613	31,337	124,261	136,513
EBT		9,864											
Income taxes	-21	4,511	1,519	1,132	5,561	5,317	13,529	5,339	6,294	6,455	6,123	24,211	27,397
Tax rate	*0.0%*		*19.6%*	*6.6%*	*26.0%*	*26.0%*	*20.3%*	*26.0%*	*26.0%*	*26.0%*	*26.0%*	*26.0%*	*26.0%*
Adjusted net adjusted (continuing operations)	-42,236	5,353	6,228	15,949	15,827	15,132	53,136	15,195	17,913	18,373	17,428	68,909	77,975
EPS		0.96	0.35	0.32	0.32	0.31	1.08	0.31	0.36	0.37	0.35	1.40	1.59
EPS - Fully Diluted		0.90	0.20	0.30	0.29	0.28	0.99	0.28	0.33	0.34	0.32	1.28	1.45
Shares outstanding - Basic				49,149	49,149	49,149	49,149	49,149	49,149	49,149	49,149	49,149	49,149
Shares outstanding - Fully Diluted				53,840	53,840	53,840	53,840	53,840	53,840	53,840	53,840	53,840	53,840

Note: CAO completed their IPO on April 10, 2015.

Source: Company reports; Laurentian Bank Securities Estimates

Financial Statements (Cont'd)

Exhibit 23: Cara Operations Financial Statements

Cash Flow Statement ($000) - Year End Dec 31	f2013	f2014	Q1/2015	Q2/2015	Q3/2015e	Q4/2015e	f2015e	Q1/2016e	Q2/2016e	Q2/2016e	Q2/2016e	f2016e	f2017e
Adjusted net earnings (continuing operations)	-42,236	5,353	6,228	15,949	15,827	15,132	53,136	15,195	17,913	18,373	17,428	68,909	77,975
Restructuring	*16,929*	*11,495*	*-205*	*436*	*0*	*0*	*231*	*0*	*0*	*0*	*0*	*0*	*0*
Depreciation of property plant and equipment	*23,747*	*17,413*	*4,689*	*4,732*	*4,700*	*4,700*	*18,821*	*4,700*	*4,700*	*4,700*	*4,700*	*18,800*	*18,800*
Amortization of other assets	*302*	*2,503*	*1,009*	*957*	*1,000*	*1,000*	*3,966*	*900*	*900*	*900*	*900*	*3,600*	*3,600*
Lease cost and tenant inducement amortization	*394*	*674*	*142*	*143*	*145*	*145*	*575*	*145*	*145*	*145*	*145*	*580*	*580*
Net gain on disposal of PPE	*18,555*	*-275*	*-636*	*327*	*0*	*0*	*-309*	*0*	*0*	*0*	*0*	*0*	*0*
Losses on early buyout / cancellation of rental contr	*1,781*	*4,400*	*1,135*	*34*	*0*	*0*	*1,169*	*0*	*0*	*0*	*0*	*0*	*0*
Net interest expense and other financing	*44,036*	*33,404*	*8,311*	*2,012*	*540*	*540*	*11,403*	*540*	*540*	*540*	*540*	*2,161*	*2,161*
Change in fair value of derivitive	*24*	*516*	*1,600*	*1,800*	*0*	*0*	*3,400*	*0*	*0*	*0*	*0*	*0*	*0*
Stock-based compensation	*-886*	*6,142*	*1,655*	*1,497*	*1,500*	*1,500*	*6,152*	*1,500*	*1,500*	*1,500*	*1,500*	*6,000*	*6,000*
Income taxes paid	*94*	*-775*	*-5,008*	*0*	*0*	*0*	*-5,008*	*5,339*	*6,294*	*6,455*	*6,123*	*24,211*	*0*
Change in onerous contract provision	*1,605*	*-792*	*-29*	*-216*	*0*	*0*	*-245*	*0*	*0*	*0*	*0*	*0*	*0*
Net change in non-cash working capital	*-22,443*	*11,564*	*-27,500*	*-1,520*	*-750*	*24,250*	*-5,520*	*-24,500*	*-2,250*	*-500*	*25,750*	*-1,500*	*-1,500*
Cash flows from operating activities	41,609	88,502	-11,808	24,310	22,962	47,268	82,732	3,818	29,742	32,113	57,087	122,761	107,616
Cash flow from operating activities and discontinued ope	-2,354	-139	-13	-13	0	0	-26	0	0	0	0	0	0
Cash flows from operating activities	39,255	88,363	-11,821	24,297	22,962	47,268	82,706	3,818	29,742	32,113	57,087	122,761	107,616
Business acquisitions	*-3,085*	*-28,656*	*-3,312*	*-11,861*	*0*	*0*	*-15,173*	*0*	*0*	*0*	*0*	*0*	*0*
Purchase of PP&E	*-17,876*	*-17,673*	*-2,168*	*-4,288*	*-8,000*	*-10,000*	*-24,456*	*-6,250*	*-6,250*	*-6,250*	*-6,250*	*-25,000*	*-25,000*
Proceeds on disposal of PP&E	*1,798*	*348*	*10*	*190*	*0*	*0*	*200*	*0*	*0*	*0*	*0*	*0*	*0*
Proceeds on early buyout of equipment rental contr	*1,433*	*2,765*	*369*	*83*	*0*	*0*	*452*	*0*	*0*	*0*	*0*	*0*	*0*
Additions to other assets	*-324*	*-109*	*-17*	*-68*	*0*	*0*	*-85*	*0*	*0*	*0*	*0*	*0*	*0*
Change in long-term receivables	*3,885*	*5,020*	*3,033*	*986*	*0*	*0*	*4,019*	*0*	*0*	*0*	*0*	*0*	*0*
Cash flow used in investing activities	-14,169	-38,305	-2,085	-14,958	-8,000	-10,000	-35,043	-6,250	-6,250	-6,250	-6,250	-25,000	-25,000
Change in bank indebtedness	*-1,581*	*-6,926*	*5,288*	*-3,064*	*0*	*0*	*2,224*	*0*	*0*	*0*	*0*	*0*	*0*
Issuance of long-term credit facility	*396,855*	*108,000*	*44,000*	*317,811*	*0*	*0*	*361,811*	*0*	*0*	*0*	*0*	*0*	*0*
Issuance of various securities	*100,001*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
Repayment of notes	*-200,000*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
Repayment of long-term credit facility	*-272,855*	*-127,000*	*-24,000*	*-527,811*	*0*	*0*	*-551,811*	*0*	*0*	*0*	*0*	*0*	*0*
Issuance of subordinate voting shares	*0*	*0*	*0*	*216,557*	*0*	*0*	*216,557*	*0*	*0*	*0*	*0*	*0*	*0*
Change in finance leases	*-1,283*	*-1,928*	*-361*	*-558*	*0*	*0*	*-919*	*0*	*0*	*0*	*0*	*0*	*0*
Interest paid	*-25,536*	*-19,853*	*-3,115*	*-7,144*	*-540*	*-540*	*-11,339*	*-540*	*-540*	*-540*	*-540*	*-2,161*	*-2,161*
Dividends paid on common shares	*-10,624*	*0*	*-11,000*	*-3,044*	*0*	*0*	*-14,044*	*0*	*0*	*0*	*0*	*0*	*0*
Other	*-10,049*	*-119*	*0*	*-168*	*0*	*0*	*-168*	*0*	*0*	*0*	*0*	*0*	*0*
Cash flow used in financing activities	-25,072	-47,826	10,812	-7,421	-540	-540	2,311	-540	-540	-540	-540	-2,161	-2,161
Net change in cash and equivalents	14	2,232	-3,094	1,918	14,422	36,727	49,973	-2,972	22,952	25,323	50,297	95,600	80,455
Cash and equivalents beginning of period	1,562	1,576	3,808	714	2,632	17,054	3,808	53,781	50,809	73,762	99,084	53,781	149,381
Cash and equivalents end of period	1,576	3,808	714	2,632	17,054	53,781	53,781	50,809	73,762	99,084	149,381	149,381	229,836
FCF	21,379	70,690	-13,989	20,009	14,962	37,268	58,250	-2,432	23,492	25,863	50,837	97,761	82,616
FCF per FD Share	na	na	na	0.37	0.28	0.69	1.08	na	0.44	0.48	0.94	1.82	1.53

Note: CAO completed their IPO on April 10, 2015.

Source: Company reports; Laurentian Bank Securities Estimates

Financial Statements (Cont'd)

Exhibit 24: Cara Operations Financial Statements

Balance Sheet ($000) - Year End Dec 31	f2013	f2014	Q1/2015	Q2/2015	Q3/2015e	Q4/2015e	f2015e	Q1/2016e	Q2/2016e	Q2/2016e	Q2/2016e	f2016e	f2017e
Cash and equivalents	1,576	3,808	714	2,632	17,054	53,781	53,781	50,809	73,762	99,084	149,381	149,381	229,836
Accounts receivable	42,412	33,108	24,446	25,118	25,618	26,618	26,618	27,118	27,618	28,118	28,618	28,618	30,618
Inventories	2,722	4,223	3,209	4,878	5,128	5,128	5,128	5,378	5,378	5,628	5,628	5,628	6,128
Prepaid expenses	1,995	2,556	3,772	1,776	2,026	2,026	2,026	2,026	2,026	2,026	2,026	2,026	2,026
Total current assets	48,705	43,695	32,141	34,404	49,826	87,553	87,553	85,331	108,784	134,856	185,653	185,653	268,608
Long-term receivables	69,368	50,173	46,565	45,505	45,505	45,505	45,505	45,505	45,505	45,505	45,505	45,505	45,505
Property, plant and equipment	76,416	86,597	84,609	83,374	86,529	91,684	91,684	93,089	94,494	95,899	97,304	97,304	102,924
Brands and other assets	153,113	163,650	163,229	162,277	161,277	160,277	160,277	159,377	158,477	157,577	156,677	156,677	153,077
Goodwill	18,059	43,051	45,981	45,981	45,981	45,981	45,981	45,981	45,981	45,981	45,981	45,981	45,981
Deferred tax asset	2,161	671	341	0	0	0	0	0	0	0	0	0	0
Total assets	367,822	387,837	372,866	371,541	389,118	431,000	431,000	429,283	453,241	479,818	531,120	531,120	616,095
Bank indebtedness	6,926	0	5,288	2,224	2,224	2,224	2,224	2,224	2,224	2,224	2,224	2,224	2,224
Accounts payable	63,459	81,352	64,645	61,287	61,537	61,787	61,787	62,037	62,287	62,537	62,787	62,787	63,787
Provisions	4,894	6,904	5,158	5,104	5,104	5,104	5,104	5,104	5,104	5,104	5,104	5,104	5,104
Gift card liability	43,069	49,461	26,954	24,535	24,535	49,535	49,535	25,535	23,535	23,535	49,535	49,535	49,535
Income taxes payable	364	3,991	68	594	594	594	594	594	594	594	594	594	594
Current portion of long-term debt	16,794	17,702	17,750	2,730	2,730	2,730	2,730	2,730	2,730	2,730	2,730	2,730	2,730
Discontinued operations	408	184	174	164	164	164	164	164	164	164	164	164	164
Total current liabilities	135,914	159,594	120,037	96,638	96,888	122,138	122,138	98,388	96,638	96,888	123,138	123,138	124,138
Long-term debt	273,346	260,661	280,808	61,240	61,240	61,240	61,240	61,240	61,240	61,240	61,240	61,240	61,240
Preferred shares	126,289	135,545	136,536	0	0	0	0	0	0	0	0	0	0
Provisions	7,814	7,630	7,885	7,432	7,432	7,432	7,432	7,432	7,432	7,432	7,432	7,432	7,432
Other long-term liabilities	76,804	62,448	61,120	57,984	57,984	57,984	57,984	57,984	57,984	57,984	57,984	57,984	57,984
Total liabilities	620,167	625,878	606,386	223,294	223,544	248,794	248,794	225,044	223,294	223,544	249,794	249,794	250,794
Common share capital	29,285	29,285	29,285	433,442	434,942	436,442	436,442	443,281	451,075	459,030	466,653	466,653	472,653
Warrant certificates	17,913	18,490	18,490	0	0	0	0	0	0	0	0	0	0
Contributed surplus	852	7,204	8,859	10,356	10,356	10,356	10,356	10,356	10,356	10,356	10,356	10,356	10,356
Deficit	-300,640	-308,040	-304,781	-295,172	-279,345	-264,213	-264,213	-249,018	-231,105	-212,732	-195,304	-195,304	-117,329
Total shareholders equity	-252,590	-253,061	-248,147	148,626	165,953	182,585	182,585	204,618	230,326	256,653	281,705	281,705	365,680
Non-controlling interest	245	15,020	14,627	-379	-379	-379	-379	-379	-379	-379	-379	-379	-379
Total equity	-252,345	-238,041	-233,520	148,247	165,574	182,206	182,206	204,239	229,947	256,274	281,326	281,326	365,301
Total liabilities and equity	367,822	387,837	372,866	371,541	389,118	431,000	431,000	429,283	453,241	479,818	531,120	531,120	616,095
Total debt	297,066	278,363	303,846	66,194	66,194	66,194	66,194	66,194	66,194	66,194	66,194	66,194	66,194
Net debt	295,490	274,555	303,132	63,562	49,140	12,413	12,413	15,385	-7,568	-32,890	-83,187	-83,187	-163,642
Net debt / LTM EBITDA	6.2x	3.3x	3.3x	0.7x	0.5x	0.1x	0.1x	0.1x	-0.1x	-0.3x	-0.7x	-0.7x	-1.2x

Note: CAO completed their IPO on April 10, 2015.

Source: Company reports; Laurentian Bank Securities Estimates

Appendix I – Important Disclosures

Company	Ticker	Disclosures*
Cara Operations	CAO-T	U, V

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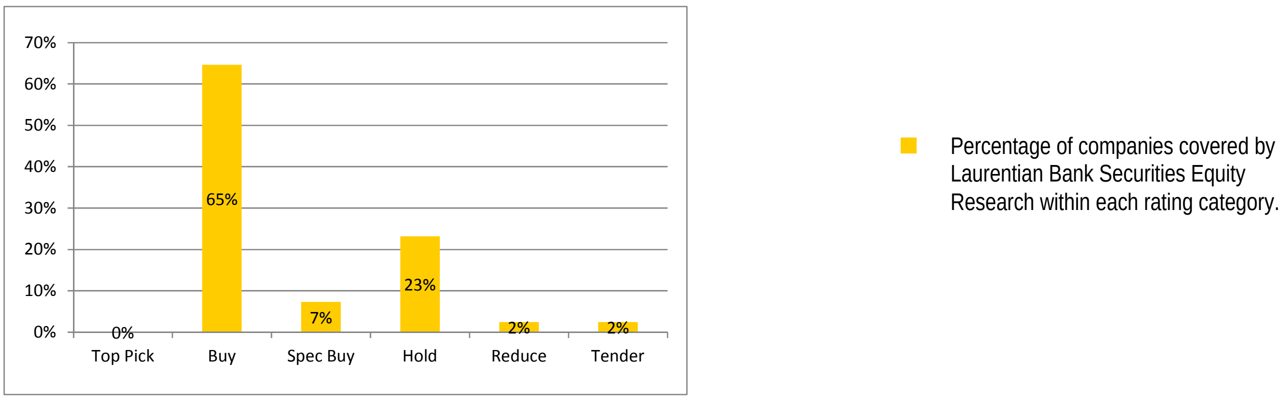

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