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Petco Health and Wellness Co., Inc. (NASDAQ: WOOF)

Consumer Discretionary – Specialty Stores

All Bark, No Bite?

April 14, 2023

Petco Health and Wellness Company Inc ('Petco') provides a wide variety of pet-related services, including veterinary care, grooming, training, telehealth, and pet health insurance services. It also sells pet supplies, consumables, and services through its various websites. Petco has over 1,500 pet care centers across the U.S., Mexico, and Puerto Rico.

Thesis

Several favourable trends over the past few years, including increased pet ownership driven by the COVID-19 pandemic, have contributed to the strong growth in the demand for Petco's products and services. The company has continually made efforts to retain its position as a major player in the US Pet Stores industry through consistently expanding its product and service offerings, aiming to serve as a definitive one-stop shop for all the needs of pet owners. However, the company has struggled as consumer spending has softened, and we believe the company is unlikely to experience strong growth in the near term.

Drivers

Fierce external competition to the US Pet Stores industry from big box retailers' and e-commerce stores and continued economic downturn will limit Petco's short-term growth prospects. However, the essential nature of some of the company's key product and service offerings will provide the business with stability even during periods of economic hardship.

Valuation

Our target share price of $10.02, with a total return of 5.1%, was derived from the equal weighting of our DCF Perpetuity Growth implied price, DCF Exit Multiple implied price, CCA EV/EBITDA implied price, and our CCA P/E implied price. We initiate a **HOLD** rating on Petco.

Equity Research	US
Price Target	**USD$ 10.02**
Rating	Hold
Share Price (Apr. 14 Close)	USD$ 9.54
Total Return	5.1%

Key Statistics	
52 Week H/L	$22.75/$7.59
Market Capitalization	$2.54B
Average Daily Trading Volume	2.58M
Net Debt	$2.96B
Enterprise Value	$5.50B
Net Debt/EBITDA	7.0x
Diluted Shares Outstanding	266.8M
Free Float	30.8%
Dividend Yield	N/A

WestPeak's Forecast

	2024E	2025E	2026E
Revenue	$6.41B	$6.92B	$7.44B
EBITDA	$346M	$491M	$528M
Net Income	$34M	$143M	$168M
EPS	$0.14	$0.55	$0.65
P/E	67.5x	17.2x	14.8x
EV/EBITDA	15.7x	10.8x	9.8x

1-Year Price Performance

Business Overview/Fundamentals

Company Overview

Founded in 1965 and headquartered in San Diego, California, Petco is one of the largest players in the US Pet Store industry with over 1,500 pet care centers across the U.S., Mexico, and Puerto Rico. The company offers one of the largest selections of both pet services and products. Over the past few years, Petco has transformed its business from a traditional retailer to a disruptive, fully-integrated, omnichannel provider that tends to all of a pet's needs. The foundation of Petco's current business model is the idea of treating the whole pet, including its physical, mental, and social well-being. The company went public for the second time in its history on January 14, 2021, with shares being sold at $18 each and raising roughly $864M in new funding. However, the company's share price has faced challenges since then, particularly over the past year, with shares experiencing a significant decline of 56.1%. This decline can be attributed to softness in consumer spending, which has been impacted by a decrease in demand following a strong stimulus-driven period in the prior year.

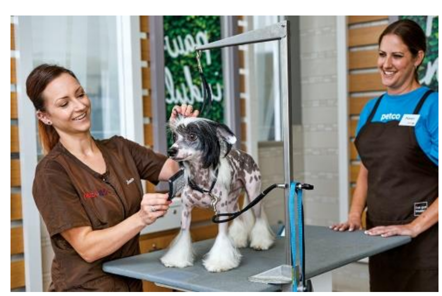
Products & Services

Consumables & Supplies

Petco originally started out as a veterinary supply company. To this day, it generates most of its revenue from selling pet consumables and supplies, which are sold both in-store and online. Although Petco has a wide range of products with high nutrition and quality standards, its offerings are weighted toward premium products. This is to capitalize on the growing number of health-conscious pet owners. Petco's product offerings leverage a wide variety of carefully curated partnerships with premium third-party brands to offer customers high-quality nutrition without artificial ingredients for their pets. Petco is also able to leverage its extensive physical network of pet care centers to create a last-mile advantage over its competition in its pet consumables and supplies offerings. They serve customers in a differentiated manner by offering the convenience of services such as same-day delivery, curbside pick-up, and buy online and pick-up in-store ("BOPUS").

Veterinarian Care

Petco offers various forms of veterinarian care, including Vetco mobile clinics and full-service veterinary hospitals. This is a more recent addition to their business model as they aim to provide pet owners with a single source for all of their pets' needs. Petco has a decade of experience running their Vetco mobile clinics and currently operates approximately 1,000 of them on a weekly basis. These mobile clinics offer affordable, preventive services to keep cats and dogs healthy. The

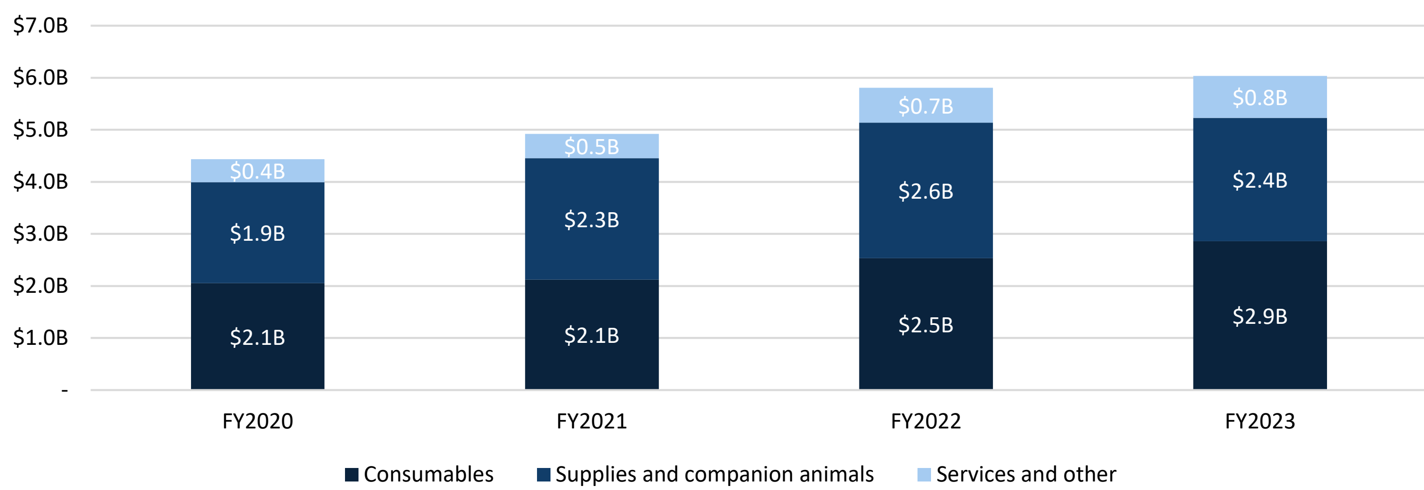


services they offer include vaccinations, deworming, microchipping, and heartworm testing. In addition to its Vetco mobile clinics, Petco opened its first full-service veterinary hospital in May 2017. Since then, they have expanded to operate 247 full-service veterinary hospitals. These state-of-the-art vet hospitals expand on the services provided by the Vetco mobile clinics, including, but not limited to, dental care, spaying and neutering, and surgeries.

Vital Care Membership

Originally launched in October 2020, Vital Care is a membership program that makes it easier and more affordable for pet parents to care for their pet's whole health in one place. The membership costs $19.99 per month for dogs and cats and $9.99 per month for birds, reptiles, fish, and smaller pets. Some benefits of a Vital Care membership include discounts on pet food, unlimited routine vet exams at Vetco Total Care locations, 20% off small pet supplies, and 20% off grooming for dogs. As of March 2022, nearly 160,000 pets were enrolled in a Vital Care membership. Petco is continuing to improve its membership; it revamped the program in March 2022 to make it more accessible and inclusive than ever before.

Revenue Segments FY2020 - FY2023 (USD)



Business Strategy

Petco has transformed over the past four years into the health and wellness space to truly become a single source for all the needs of pet owners. This transformation was led by CEO and Chairman, Ron Coughlin. Some of the significant operational and cultural changes that the leadership team has implemented include building leading omnichannel capabilities, creating a highly differentiated product offering, and implementing a performance culture led by data analytics.

Built Leading Omnichannel Capabilities

Petco believes they've entered a new era of retail called "Retail 3.0" in which customers seek a fully integrated experience of both physical retail and omnichannel digital offerings. This shift to "Retail 3.0" was further helped by the COVID-19 pandemic as customers of all demographics became more comfortable with online interaction. In order to climatize to this new era, Petco invested heavily in building an app with a specific focus on driving increasing spending per pet and has relaunched its e-commerce platform. To help drive traffic and engagement on their website, they specifically invested in improving attributes such as website speed, ease of navigation, and customer personalization. Furthermore, they've focused on increasing customer monetization, acquisition, and retention by leveraging advanced analytics and precision marketing on their website. These efforts have been rewarded as the company's app and website sales delivered double-digit growth for both Q4 and the full fiscal 2023 year.

Created a Highly Differentiated Product Offering

Petco offers an exclusive assortment of products that drives repeat purchasing and facilitates customer loyalty. Their three-core product differentiating capabilities are nutritional expertise, exclusive partnerships, and a robust in-house brand platform. In May 2019, Petco committed to better pet nutrition by no longer selling dog and cat food that contained artificial ingredients. They have also developed partnerships with some of the industry's most highly regarded premium food brands, including JustFoodForDogs, whom they expanded their partnership with in March 2022. Finally, Petco has established its own brands, WholeHearted and Reddy, in both the premium pet food and pet supplies spaces. These brands have been a success as Petco-owned brands saw double-digit CAGR between fiscal 2018 and 2021. Additionally, roughly 27% of sales in fiscal 2021 came from Petco-owned brands.

Implemented a Performance Culture Led by Data Analytics

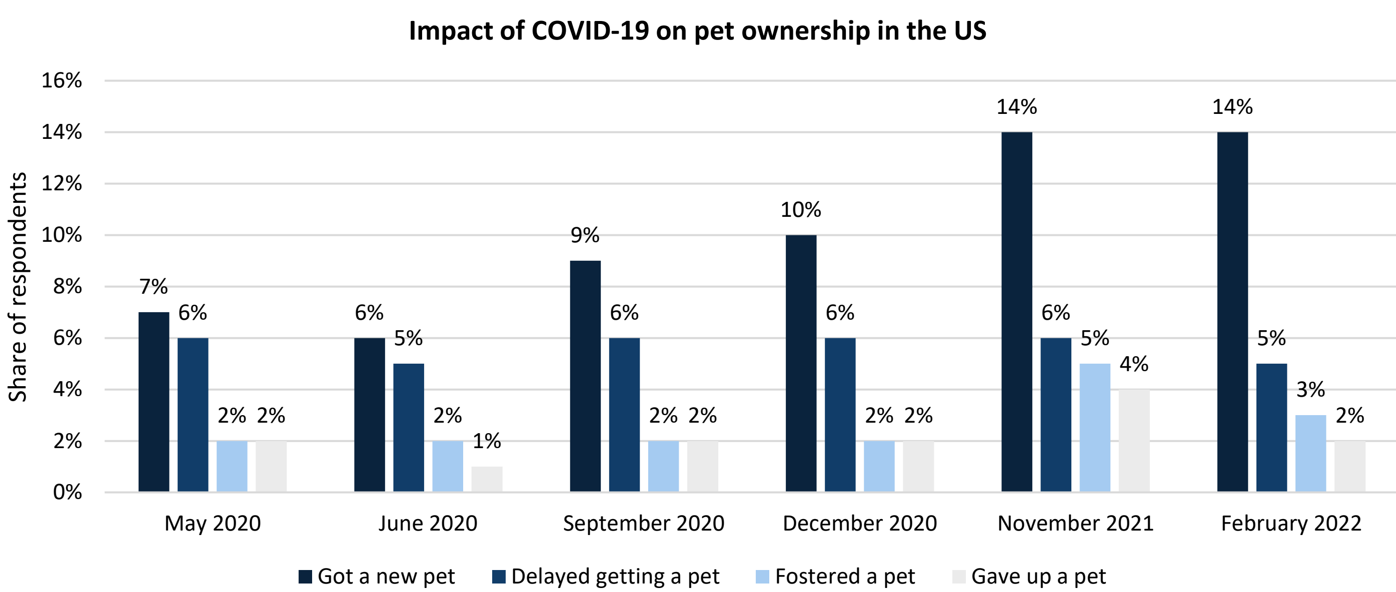
Petco has created a competitive advantage for itself by investing in talent and data analytics capabilities over the past two years. This investment has allowed them to drive sales and minimize costs through advanced capabilities, including dynamic pricing, inventory optimization, merchandising, and precision marketing. Additionally, Petco can generate a 360-degree view of its customers due to the use of tools that capture customer preferences such as purchases, searches, and services utilization. Furthermore, Petco is utilizing data analytics to enhance decision-making within the company. Managers are able to track performance across multiple dimensions, identify opportunities, and execute strategies to drive sales through a user-friendly, action-focused dashboard.

Industry Analysis

Petco operates in the US Pet Stores industry which had annual revenue of $23.5B in 2022. The primary activities of this industry are retailing pets, pet food, and pet supplies. Some of the major players industry include PetSmart, Petco, and Pet Food Express. The industry is currently in the growth stage of its life cycle, but growth is beginning to slow down. Between 2017 to 2022, annualized growth in the industry was 1.9% (IBIS World). Although forecasted annual growth is expected to remain positive over the next five years, it is expected to decrease to just 0.8% on an annual basis between 2022 to 2027 (IBIS World). One trend driving this continued growth is the increase in pet adoption throughout the country. Favourable trends caused by the COVID-19 pandemic and changes in population demographics have led to increases in pet adoption, driving the forecasted growth in the industry through 2027. However, this forecasted growth is hindered by increasing competition from supermarkets, mass merchandisers, and online retailers.

COVID-19

Although the COVID-19 pandemic negatively impacted many industries, the pandemic actually created some positive tailwinds for the US Pet Stores industry. Similar to other consumer cyclical industries, the industry was initially challenged by the decline in customer traffic as COVID-19 fears grew and more consumers opted to purchase products from online retailers instead. However, the US Pet Stores industry wasn't hit nearly as hard due to many pet stores being able to remain open despite the lockdown order in many states as they were classified among essential businesses that could remain operating. Additionally, the pandemic resulted in an increase in pet adoption. As people spent more time at home under strict orders from the government not to go out, many Americans sought companionship, leading to a huge increase in pet adoption. According to the 2021-2022 APPA National Pet Owners Survey, pet ownership reached on all-time high in 2020 with 70% of households owning at least one pet. A reported 23 million American households adopted a new pet during the pandemic (Washington Post). Not only has there been an increase in pet owners, but pet parents are spending more on their pets as well. 35% of pet owners surveyed stated that they had spent more on pet food and supplies in 2020 compared to the previous year (2021-2022 APPA National Pet Owners Survey). This higher spending was led by Gen Z and Millennial pet owners as 50% reported that they had spent more on their pets in 2020.



(Source: Statista)

As the world adjusts to a post-pandemic reality, with restrictions being lifted, the growth in new pet ownership is expected to decline. The factors that drove the surge in pet ownership during the pandemic, such as increased time at home and reduced social activities, will dissipate. Additionally, pet parents' spending is likely to return to pre-pandemic levels as the impact of COVID-19 stimulus checks from the US government subsides. However, there will be a growing demand for pet daycare services as millions of Americans return to the office, creating a need for convenient and reliable pet care solutions.

Industry Trends

Demographics

There are several favourable demographic trends in the American population that will continue to help drive growth in pet adoption over the next few years. One of the biggest trends is the growing number of Baby Boomers crossing the retirement threshold. As many Baby Boomers retire and are no longer occupied by full-time jobs, many opt to adopt pets as a way to keep themselves busy and active as they adjust to retirement. Baby Boomers are also getting divorced at a higher rate than any other age group making them more likely to seek companionship from pets. In a report from the U.S. Census Department from April 2021 found that 34.9% of all Americans who had a divorce in the previous calendar year were 55 or older; more than twice the rate of any other age group in the report. Additionally, pet parents who are Baby Boomers are more likely to pamper and spend more on their pets as they are in a better financial position than other age groups. Another trend that is helping the increase in pet adoption, is that more Americans are opting to start families later on in life and put a greater emphasis on their careers. According to a report from the U.S. Census Bureau in April 2022, the median age of U.S. women giving birth is now 30, the highest it has ever been. As a result of this delay in starting a family, many of these young couples are adopting pets instead. These young couples also have more disposable income to spend on their pets without the significant financial burden of raising a child.

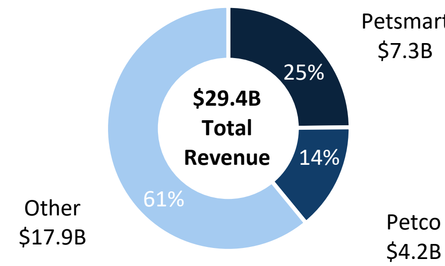
Increased Competition

In recent years, there has been increased competition from mass merchandisers. Major players within the industry have been put under pressure by discount retailers such as Costco and Walmart. These mass merchandisers tend to have a competitive advantage over the traditional major players in the industry as they are able to price their pet products more competitively due their ability to purchase directly from manufacturers in bulk. However, they usually don't sell any premium pet products as they are often restrained their manufacturers' restrictions. Mass merchandisers have been able to attract price-conscious consumers who don't put a lot of value on high-end, premium pet products, and their increase in popularity has negatively impacted industry growth over the past five years. There has also been increased competition from e-commerce alternatives as more consumers begin to purchase products online. Purchasing products online helps consumers save time, and companies such as Amazon provide them with added convenience as a one-stop shop for all of their needs. Amazon have even introduced their very own private-label brand called Wag. This new brand enables them to directly compete with traditional industry players when it comes to providing affordable pet food. Companies like Amazon will also benefit from the increase in demand for online purchasing options for pet food and supplies. This demand has increased at an annualized rate of 11.9% over the past five years (IBIS World).

Competitive Landscape

The US Pet Store industry is mainly dominated by two speciality supply retailers, Petco and PetSmart. These two retailers alone were responsible for 45.8% of the industry market share in 2022 (IBIS World). The rest of the industry is made up of family-owned stores and smaller pet store chains. The majority of sales in pet stores are made up by product purchases, as a result, companies' main area of competition is product range, price, and quality. Major players in the industry have been able to capture a large share of the market due to their ability to provide a variety of pet foods and supplies with diverse attributes at a wide range of prices. Petco and PetSmart are able capitalize on their ability to buy in bulk and produce their products at economies of scale. This allows them to sell products at low prices while still maintaining strong profit margins. Smaller stores often struggle to compete as they lack the purchasing power of the major industry players, but still try to offer products at similar prices in order to remain competitive. As a result, smaller stores are forced to differentiate themselves by catering to the specific needs of niche markets in their regional areas in order to survive. Although the industry is moderately concentrated, smaller stores have been able to successfully profit by serving more niche markets in their regional areas.

US Pet Store Industry Major Players 2022



Barriers to Entry

The barriers to entry in the US Pet Store industry are relatively high. Two of the biggest factors that would potentially hinder new entrants into the industry are the high industry concentration and the high level of regulation in the industry. The high industry concentration makes it hard for new entrants to establish market share as two of the national retail chains account for nearly half of the total industry revenue. The rest is left to smaller players who are often forced to differentiate themselves by providing niche and speciality product offerings or services in order to remain competitive. There is intense price competition within the industry from major players in the industry and external pressures from mass merchandisers making it hard for new, independent retailers. Prices established by Petco and PetSmart force new entrants to either obtain economies of scale or accept lower profit margins. Accepting these lower profit margins becomes even tougher when taking into account all the costs associated with opening a new pet store. New entrants have to factor in the costs of building brand awareness, purchasing new inventory to the required levels, and renting a location in a high-traffic area. Another factor that may discourage new entrants in the industry is the high levels of government regulation. When opening a pet store, you need to consider the various federal and state laws that regulate pet shops and the sale of animals. For example, the Animal Welfare Act of 1966 dictates how pets sold in pet stores must be maintained and kept, and this is just

the tip of the iceberg; there are many other laws and regulations that new entrants must consider. Pet stores need to address a range of issues and receive licenses in accordance with federal and state requirements before they can even begin operating.

Outlook

The US Pet Store industry is forecasted to continue growing, albeit at a slower rate, through 2027. This growth is mainly driven by the increase in pet adoption caused by favourable trends as a result of the COVID-19 pandemic and the demographic shifts in the population. However, increased competition from mass merchandisers and e-commerce will hinder the industry's growth as this external competition lures customers away through offering pet products at lower prices and with more convenient purchasing options. Major industry players will be forced to provide more online purchasing options in order to retain their market share as the demand for online purchasing options continues to grow though 2027.

Drivers

Wholistic Approach to Pet Care

Petco has undergone a significant transformation in recent years, shifting from a conventional pet retailer that sells a range of products and supplies to a fully integrated provider that addresses all the needs of a pet, including physical and social well-being. This transformation is demonstrated by the company's expansion into the veterinary care space through its Vetco mobile clinics and full-service veterinary hospitals. Offering pet owners the convenience of a one-stop-shop for all their pet needs will be critical in allowing Petco to retain customers in the face of competition from both major players in the US Pet Store industry and big box retailers. The company's wholistic offering of products and services is supported by Petco's Vital Care membership program further solidifying customer loyalty.

Premium Product Offering

One key factor that sets Petco apart from other players in the market is its premium collection of products. The company has made a deliberate effort to offer consumers only the highest quality pet food, including a commitment in May of 2019 to discontinue the sale of dog and cat food containing artificial ingredients. This premium offering is made possible through strong partnerships with leading pet food brands and Petco's own brands, WholeHearted and Reddy. The trend of increased humanization of pets in North America has rewarded Petco for its focus on high-quality products, and this will continue to drive growth for the company in the coming years. Despite economic fluctuations, there will be sustained demand for these premium offerings, and this will continue to distinguish Petco from its competitors.

Humanization of Pets

Consumers in the US are increasing treating their pets as family members, shifting their spending on pet products from discretionary to more essential and non-discretionary. Spending the extra money to purchase premium products is now viewed as a necessity, rather than a luxury; it's a crucial aspect of helping maintain the pet's health and increasing its lifespan. This will allow Petco to continue to compete with the increasing number of big box retailers entering the space who typically specialize in cheaper pet food as they are often restrained by their manufacturer's restrictions. Furthermore, this will allow Petco to generate stable revenue numbers even during periods of economic downturn as these health-conscious consumers will continue to purchase premium products regardless of the state of the economy.

Catalysts

Further Expansion into Veterinary Space

Petco has made notable strides in expanding its veterinary services offerings during fiscal year 2023. With veterinary services now available in 90% of their pet care centers and approximately 1.9 million pets treated in Petco clinics in 2022, these efforts have played a significant role in the impressive 20.2% growth witnessed in the company's services segment, the fastest-growing revenue segment in the past year.

Despite these achievements, we believe there is ample opportunity for Petco to further capitalize on the veterinary services market. The US Veterinary Service industry, valued at $62.2 billion in 2023, is more than double the size of the US Pet Store industry, according to IBIS World. Additionally, the veterinary services sector boasts considerably higher profit margins, averaging at 13.9% over the last five years, compared to a meager 1.9% for the US Pet Store industry. Furthermore, unlike some of Petco's other revenue streams, veterinary services are non-cyclical and recurring in nature, providing a stable and consistent revenue source. Given the market size, Petco's initial success in the veterinary services space, and the recurring nature of the service, we believe that a larger investment from Petco into the veterinary space has the potential to be a significant driver of revenue and cash flow growth in the coming years, ultimately leading to an increased share price.

More Severe Economic Downturn in 2023

2022 was a difficult year for the greater economy with the S&P 500 falling 19.4%, its worst year since 2008. This was mainly caused by the aggressive hiking of interest rates from the Fed and central banks around the world in an effort to tackle red-hot inflation. With inflation still sitting well above the Fed's target rate of ~2%, there is potential for more severe economic downturn in 2023. Although it's unlikely to have a massive impact on the spending of current pet parents on things such as pet food and veterinary services, it's likely to lead to a decrease in new pet owners. During this type of macroenvironment, many consumers may opt to not purchase new pets due to the significant financial cost. These consumers have not developed any sort of attachment to a pet; therefore, they view the purchase of one as non-essential. Furthermore, price conscious pet owners will reduce their expenditures, especially on more discretionary items such as toys and other pet supplies. Early signals of this impact can already be seen in the performance of Petco's supplies and companion animals revenue segment; the company's only revenue category that faced negative growth through fiscal year 2023. We predict that tougher economic conditions will limit the company's near-term growth.

Management Team

Ron Coughlin – Chief Executive Officer & Chairman

Ron Coughlin is Chief Executive Officer and Chairman of Petco and joined the company in June of 2018. He has 25 years of experience in consumer products, with expertise in transforming businesses through honing strategy, re-engineering cost structures, and cultivating high-performing teams. Prior to joining Petco, Coughlin served four years as President of HP's Personal Systems segment, a $33 billion global business. Before joining HP, Coughlin spent 13 years in a range of senior executive roles at PepsiCo. During his time as Chief Marketing Officer of PepsiCo International Beverages, Coughlin was responsible to marketing activities in all markets outside of the US across the Pepsi, Gatorade, 7 Up, and Tropicana brands. Coughlin holds a bachelor's degree in international marketing from Lehigh University and MBA from the Kellogg School of Management at Northwestern University.

Soumik Chatterjee – Chief Strategy Officer

Soumik Chatterjee joined Petco in October of 2018 as Chief Strategy Officer. He holds 20 years of experience across the US, EU, China, and India and is in charge of leading the company's long-term growth strategy, corporate development, and sustainability efforts. Before joining Petco, Chatterjee served as Head of Corporate Strategy at Qualcomm and prior to that he was also Senior Director of Corporate Strategy at HP. Chatterjee is currently an advisory board member of Santa Clara University's Retail Management Institute and a member of the Retail Industry Leaders Association. Chatterjee holds a bachelor's degree in computer engineering from the University of Mumbai and MBA from the University of Michigan's Ross School of Business.

Brian LaRose – Chief Financial Officer

Brian LaRose initially joined Petco in September of 2020 as Senior Vice President of Finance before being promoted to Chief Financial Officer in August of 2021. LaRose started his career in Deloitte's audit and M&A practice, working his way up to Senior Manger of Special Acquisition Services before leaving to join HP. He spent 17 years at HP, capping off his time there as Global Head of Digital Programs Office. Additionally, LaRose was appointed to the National Foundation for Autism Research's board of directors. LaRose holds a bachelor's degree from Colby College and master's degree in accounting from Northeastern University.

Management Compensation in 2021

Name	Title	Salary	Bonus	Non Equity Incentive Plan Compensation	All Other Compensation	Total Compensation
Coughlin, Ronald	Chairman of the Board & CEO	$1,100,000	-	$2,750,000	$175,740	$4,025,740
LaRose, Brian	Chief Financial Officer	$492,500	-	$628,711	$9,488	$1,130,699
MacDonald, Darren	Chief Customer Officer	$600,000	-	$5,040,094	$41,980	$5,682,074
Nuzzo, Michael M.	Former Executive Officer	$664,625	$1,000,000	$950,122	$47,173	$2,661,920
Tichy, Justin	Chief Pet Care Center Officer & COO	$600,000	$500,000	$960,000	$20,376	$2,080,376
Zavada, John M.	Chief Administrative Officer	$485,688	$1,000,000	$582,826	$31,006	$2,099,520
Total		**$3,942,813**	**$2,500,000**	**$10,911,753**	**$325,763**	**$17,680,329**

(Source: S&P Capital IQ)

Shareholder Base, Liquidity, Market Depth

Shareholder Base

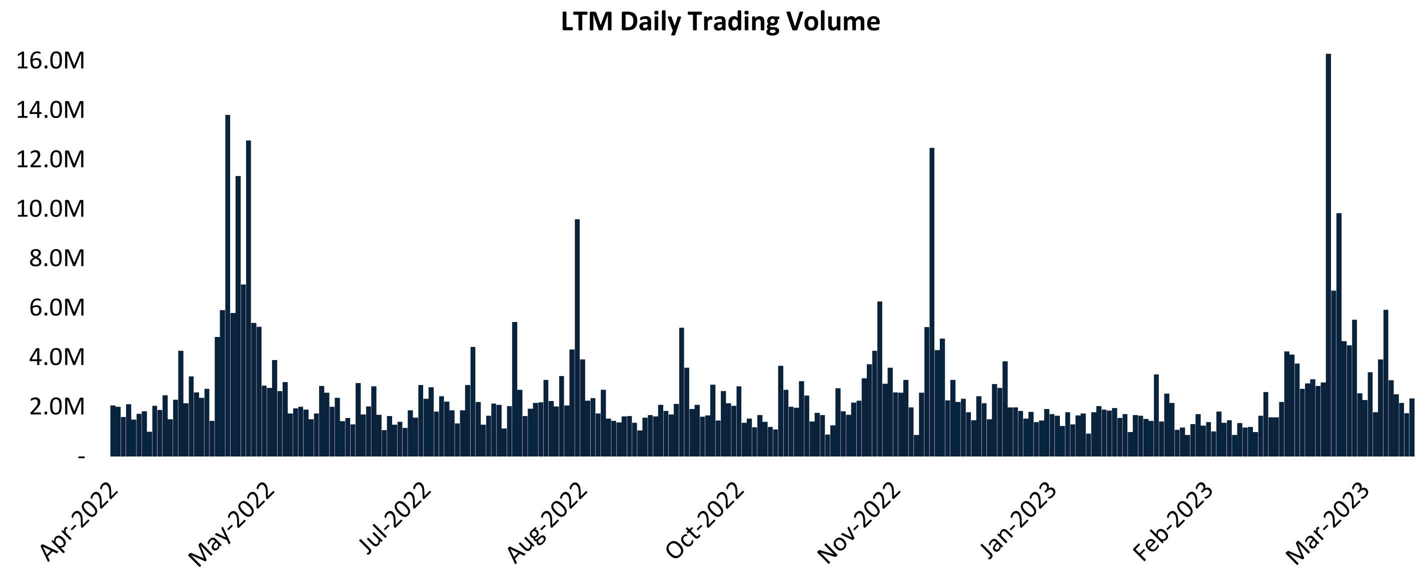
WOOF has a free float of 30.8% with 82,067,898 shares out of the 266,754,361 shares outstanding. The top 10 shareholders own 85.6% of the total shares outstanding; however, the majority of that is Scooby Aggregator, a private corporation owned jointly by CVC Capital Partners and CPP Investments.

Holder	Position	% of Shares Outstanding	Market Value (USD in millions)	Insider (Y/N)
Scooby Aggregator, LP	183,714,921	68.9%	$1,752.60	Y
Mackenzie Financial Corporation	8,214,994	3.1%	$78.40	N
The Vanguard Group, Inc.	7,202,909	2.7%	$68.70	N
Macquarie Investment Management Business Trust	4,880,462	1.8%	$46.60	N
ClearBridge Investments, LLC	4,460,592	1.7%	$42.60	N
J.P. Morgan Asset Management, Inc.	4,353,031	1.6%	$41.50	N
T. Rowe Price Group, Inc. (NASDAQ: TROW)	4,341,294	1.6%	$41.40	N
Millennium Management LLC	4,305,037	1.6%	$41.10	N
Franklin Resources, Inc. (NYSE:BEN)	3,509,659	1.3%	$33.50	N
BlackRock, Inc. (NYSE:BLK)	3,400,760	1.3%	$32.40	N
Top 10 Shareholders	**228,383,659**	**85.6%**	**$2,178.80**	

(Source: S&P Capital IQ)

Liquidity

The average daily trading volume over the last twelve months (LTM) was 2,580,697, with a high of 16,262,100 and low of 839,877. An LTM trading volume well above one million units is a good indicator of healthy liquidity; shareholders of WOOF shouldn't face any issues when attempting to exit positions.



(Source: S&P Capital IQ)

Valuation

Discounted Cashflow (DCF) Assumptions

Revenue Forecasts

Petco's revenue can be broken down by product type and services into three main categories; consumables, supplies and companion animals, and services and other. Consumables, which makes up the largest share of the company's net sales, performed well this fiscal year, posting an average year-over-year growth of 12.9% through the fiscal 2023. This growth was driven by Petco's strategic investment in customer acquisition and retention, and the company's continued expansion of its assortment of products with a specific mix shift to provide more premium consumables, including fresh and frozen food. We forecast that growth in this category will continue in fiscal year 2024, albeit at a slightly lower rate of 10.0% due to continued economic downturn leading to less discretionary spending on consumers. This forecast falls shy of the category's historical mean of 11.9% year-over-year growth.

Supplies and companion animals are responsible for the second largest share of Petco's net sales. Due to a strong stimulus driven period in the previous year, this category has faced negative growth through fiscal 2023, with year-over-year growth of -8.9%. We expect this negative growth to continue through fiscal year 2024 at a lower rate of -2.0% before rebounding to its historical mean of positive 7.0% year-over-year growth in fiscal year 2025 as we predict economic conditions will recover.

The final revenue category, services and other, experienced the largest year-over-year growth in fiscal 2023, posting growth of 20.2% through the year. This increase was mainly driven by growth in Petco's membership offerings, such as Vital Care, which grew 200% year-over-year according to the company's Q3 earnings call. Additionally, growth in Petco's veterinary hospital business aided the increase with the company now operating 247 veterinary hospitals as of December 31, 2022; 50 more compared to the previous year. We forecast this strong growth to continue throughout at fiscal year 2024 at a growth rate of 15% year-over-year. This estimate is derived from the assumption that sign ups for memberships such as Vital Care will taper off slightly from the explosive growth the program has experienced over the past year. However, we believe there will be sustained demand for services including veterinary hospitals as these services are deemed essential by the majority of consumers.

Cost of Goods Sold (COGS)

The cost of goods sold as a percentage of revenue was slightly higher through fiscal year 2023 at an average of 59.8% compared to its historical mean of 58.1%. This increase was mainly driven by the combined impact of strong sales in consumables and weak sales in supplies and companion animals. We forecast cost of goods sold to remain at 59.8% of revenue for fiscal year 2024 before tapering back down to the historical mean in the following year.

Selling, General, & Administrative Expenses (SG&A)

We forecast SG&A as a percentage of revenue at 34.8% for fiscal year 2024 and onwards, which was derived using the company's historical mean.

Capital Expenditures (CAPEX)

Capital expenditures have been much higher in fiscal year 2023, at an average of 34.6% of PP&E compared to the historical mean of 30.6%. This increase was predominantly driven by the expansion of Petco's veterinary hospitals, including a purchase of the remaining 50% stake of the company's veterinary joint venture for $35 million in May 2022, which is now a wholly owned subsidiary. We forecast that capital expenditures will return to the historical mean in fiscal year 2024.

Weighted Average Cost of Capital (WACC)

We calculated the weighted average cost of capital to be 6.8% for WOOF through taking the weighted average cost of debt and equity. The cost of debt was calculated by using a pre-tax cost of debt of 3.5%, based on the US 10-year Treasury note, and reducing it by the company's effective tax rate of 22.8%. This resulted in a cost of debt of 2.7%. To calculate the cost of equity, we used the market's expected rate of return of 10.4% and the company's adjusted beta of 1.19. The resulting cost of equity was 11.7%. The 2.7% cost of debt and 11.7% cost of equity was used to derive a weighted average cost of capital of 6.8%.

(Source: Bloomberg)

Perpetuity Growth Rate

We assumed a perpetuity growth rate of 2.8% as we believe this accurately reflects the maturity of the US Pet Stores Industry and Petco's position as one of the largest players in the space.

Terminal EV/EBITDA Multiple

A terminal EV/EBITDA multiple of 14.5x was calculated by taking the median multiple from our comparable companies analysis.

Comparable Companies Analysis Set

For our comparable companies analysis, we selected other publicly traded companies with similar business models that also operate within the Pet Stores industry. Our set retuned an EV/EBITDA implied price of $11.79 and P/E implied price of $6.41.

Bark, Inc. (NYSE: BARK)

BARK Inc., a dog-centric company, provides products, services, and content for dogs. It operates in two segments, Direct to Consumer and Commerce. The company serves dogs through monthly subscription services. It is also involved in the design of playstyle-specific toys, satisfying treats, personal meal plans with supplements, and dog-first experiences designed to foster health and happiness of dogs everywhere.

Tractor Supply Company (NASDAQ: TSCO)

Tractor Supply Company operates as a rural lifestyle retailer in the United States. The company offers a selection of merchandise, including equine, livestock, pet, and small animal products necessary for their health, care, growth, and containment; hardware, truck, towing, and tool products; seasonal products, such as heating products, lawn and garden items, power equipment, gifts, and toys; work/recreational clothing and footwear; and maintenance products for agricultural and rural use.

PetMed Express, Inc. (NASDAQ: PETS)

PetMed Express, Inc., together with its subsidiaries, operates as a pet pharmacy in the United States. The company markets prescription and non-prescription pet medications, health products, and other supplies for dogs, cats, and horses. It offers non-prescription medications and supplies, such as flea and tick control products, bone and joint care products, vitamins, treats, nutritional supplements, hygiene products, and supplies; and prescription medications.

Freshpet, Inc. (NASDAQ: FRPT)

Freshpet, Inc. manufactures and markets natural fresh meals and treats for dogs and cats in the United States, Canada, and Europe. The company sells its products under the Freshpet brand; and Dognation and Dog Joy labels through various classes of retail, including grocery, mass, club, pet specialty, and natural, as well as online**.**

Central Garden & Pet Company (NASDAQ: CENT)

Central Garden & Pet Company produces and distributes various products for the lawn and garden, and pet supplies markets in the United States. It operates through two segments, Pet and Garden. The Pet segment provides dog and cat supplies, such as dog treats and chews, toys, pet beds and grooming products, waste management and training pads, and pet containment; supplies for aquatics, small animals, reptiles, and pet birds, including toys, cages and habitats, bedding, and food and supplements. The Garden segment offers lawn and garden supplies products that include grass seed; vegetable; flower and herb packet seed; wild bird feed, bird feeders, bird houses, and other birding accessories; fertilizers; decorative outdoor lifestyle products; live plants; and weed and grass, as well as other herbicides, insecticide, and pesticide products.

Chewy, Inc. (NYSE: CHWY)

Chewy, Inc., together with its subsidiaries, engages in the pure play e-commerce business in the United States. The company provides pet food and treats, pet supplies and pet medications, and other pet-health products, as well as pet services for dogs, cats, fish, birds, small pets, horses, and reptiles through its www.chewy.com retail Website, as well as its mobile applications. It offers approximately 100,000 products from 3,000 partner brands.

Recommendation

Hold

We currently recommend a **HOLD** on WOOF. While the COVID-19 pandemic brought about positive trends for the US Pet Stores industry, including as a rise in pet ownership and a stimulus-fueled spending spree, the industry faces limited growth prospects due to intense competition from big box retailers and e-commerce stores. Additionally, Petco will find it challenging to substantially grow its net sales in its two largest revenue categories, consumables and supplies and companion animals, during this prolonged economic downturn. However, the essential nature of some of Petco's key products and services will provide the business with stability in the coming years. Favourable trends including an aging population and the humanization of pets in North America will further help to mitigate the negative effects of the broader economic environment in 2023. Furthermore, Petco is poised to maintain its position as one of the two major players in the industry, alongside PetSmart.

This resulted in a target price of $10.02 with a total return of 5.1%.

Risks

Product Recalls

An essential driver of Petco's success over the past couple of years is the humanization of pets within North America. With pet owners increasingly treating their pets like family members, they have been more willing to spend on premium products to maintain the health of their four-legged family members. However, this is increased focus on the well-being of their pets is a double-edged sword for the company as a product recall or controversy related product safety could be catastrophic for the company's sales. It is crucial that Petco maintains the high quality and safety as the company continues to grow.

Lawsuits

The company was sued in December of 2021 by William and Elma Hall over the death of their pet English Bulldog, Max. The couple claims that Petco was negligent in their care of Max; he died just a couple of hours after being dropped off for a routine grooming appointment. Although these types of incidents are sporadic for the company, and the Hall family is only suing them for $50,000, there is an increased risk of these incidents, especially as the company continues to expand their veterinary care offerings. Just due to the nature of the services veterinary practices provide, there is also the potential risk for the company to be wrongfully sued by distraught pet owners grieving over the death of their pet, even when Petco has done nothing wrong. It is imperative for Petco to do everything in its power to ensure that these types of incidents never occur, as any pattern of negligible behaviour could not only lead to a class action lawsuit but would be extremely damaging to the business as a whole.

Mass Merchandisers Increasing Product Ranges

As previously mentioned, major players within the industry have been put under pressure by mass merchandisers such as Walmart and Costco. Due to their ability to purchase directly from manufacturers in bulk, these discount retailers are able to price their products more effectively. However, their limited range of offerings, specifically lacking in premium pet products, has prevented them from truly disrupting the industry. Many of these mass merchandisers are limited by their manufacturer's restrictions. If these discount retailers figure out how to expand their product offering while maintaining their competitive pricing, this could pose a major threat to Petco's business.

Highly Concentrated Shareholder Base

The company is currently indirectly controlled by certain funds that are advised and managed by CVC Capital Partners and Canada Pension Plan Investment Board. These sponsors mainly exercise their control of the company through Scooby Aggregator which holds roughly 69% of the total shares outstanding. If these sponsors showed any interest in divesting their position, it could significantly impact Petco's share price.

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Appendix 1: Summary Page

Summary Page

(Figures in mm USD)	Jan-20 FY2020	Jan-21 FY2021	Jan-22 FY2022	Apr-22 Q1-2023	Jul-22 Q2-2023	Oct-22 Q3-2023	Jan-23 Q4-2023	Jan-23 FY2023	Jan-24 FY2024	Jan-25 FY2025	Jan-26 FY2026	Jan-27 FY2027	Jan-28 FY2028
Income Statement													
Revenue	4,434.5	4,920.2	5,807.1	1,476.0	1,480.8	1,501.2	1,578.0	6,036.0	6,411.4	6,920.0	7,435.5	7,807.2	8,197.6
EBITDA	284.1	369.3	438.5	96.9	98.6	96.1	127.8	419.4	346.2	491.3	527.9	554.3	582.0
Net Income	(104.0)	(31.7)	159.8	23.8	13.5	19.9	32.7	89.9	33.6	143.3	167.9	184.6	202.1
Earnings Per Share	$ (0.46)	$ (0.13)	$ 0.62	$ 0.09	$ 0.05	$ 0.07	$ 0.12	$ 0.34	$ 0.14	$ 0.55	$ 0.65	$ 0.71	$ 0.78
Cash Flow Statement													
Capital Expenditures	(156.9)	(159.6)	(239.1)	(65.9)	(70.3)	(75.9)	(65.9)	(278.0)	(247.7)	(250.8)	(255.9)	(261.1)	(266.4)
Acquisitions	(2.8)	-	(4.3)	-	(2.9)	(4.9)	(1.9)	(9.6)	-	-	-	-	-
Divestitures	-	-	-	-	(35.0)	35.0	-	-	-	-	-	-	-
Dividend Payment	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Dividend Per Share	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Dividend Payout to Earnings	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Dividend Payout to Core FCF	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Dividend Yield	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Balance Sheet													
Current Assets	711.0	777.5	1,070.8	1,048.9	1,013.8	1,019.0	1,016.0	1,016.0	1,133.6	1,267.5	1,471.1	1,676.3	1,900.6
Non-Current Assets	5,444.1	5,298.2	5,427.2	5,456.9	5,528.6	5,557.9	5,596.8	5,596.8	5,613.3	5,629.9	5,646.9	5,664.2	5,681.8
Assets	6,155.1	6,075.7	6,497.9	6,505.8	6,542.4	6,576.9	6,612.8	6,612.8	6,746.8	6,897.4	7,117.9	7,340.4	7,582.4
Current Liabilities	841.9	875.3	1,053.1	1,011.8	1,035.4	1,057.2	1,021.3	1,021.3	1,121.7	1,128.9	1,181.5	1,219.5	1,259.3
Non-Current Liabilities	4,752.1	3,145.1	3,189.0	3,206.3	3,227.9	3,191.8	3,210.1	3,210.1	3,210.1	3,210.1	3,210.1	3,210.1	3,210.1
Liabilities	5,594.1	4,020.4	4,242.1	4,218.1	4,263.3	4,249.0	4,231.4	4,231.4	4,331.8	4,339.0	4,391.6	4,429.6	4,469.4
Shareholders' Equity	569.4	2,068.8	2,274.0	2,306.8	2,279.1	2,327.9	2,381.5	2,381.5	2,415.1	2,558.4	2,726.3	2,910.8	3,113.0
Cash	148.8	111.4	211.6	190.9	125.2	148.7	201.9	201.9	212.3	321.8	459.4	617.1	791.5
Debt	3,825.9	2,990.3	3,024.2	3,031.8	3,064.3	3,089.9	3,109.0	3,109.0	3,109.0	3,109.0	3,109.0	3,109.0	3,109.0
Net Debt	3,677.1	2,878.9	2,812.6	2,840.9	2,939.1	2,941.1	2,907.1	2,907.1	2,896.8	2,787.3	2,649.6	2,492.0	2,317.6
Minority Interests	(8.3)	(13.6)	(18.2)	(19.1)	-	-	-	-	-	-	-	-	-
Debt/EBITDA	12.9 x	7.8 x	6.4 x					6.9 x	8.4 x	5.7 x	5.0 x	4.5 x	4.0 x
Operating Metrics													
Return on Equity (ROE)	-18.3%	-1.5%	7.0%	1.0%	0.6%	0.9%	1.4%	3.8%	1.4%	5.6%	6.2%	6.3%	6.5%
Return on Assets (ROA)	-1.7%	-0.5%	2.5%	0.4%	0.2%	0.3%	0.5%	1.4%	0.5%	2.1%	2.4%	2.5%	2.7%
Return on Invested Capital (ROIC)	2.0%	6.0%	6.3%	1.0%	0.9%	1.3%	1.5%	4.7%	3.1%	6.7%	7.9%	9.0%	10.3%
Valuation Metrics													
Stock Price (High)	n/a	$ 29.40	$ 28.05	$ 22.40	$ 20.37	$ 16.82	$ 9.54	$ 22.40	$ 9.54	$ 9.54	$ 9.54	$ 9.54	$ 9.54
Stock Price (Low)	n/a	$ 26.03	$ 17.43	$ 17.18	$ 13.44	$ 9.36	$ 9.54	$ 9.36	$ 9.54	$ 9.54	$ 9.54	$ 9.54	$ 9.54
Stock Price (Average)	n/a	$ 27.72	$ 22.74	$ 19.79	$ 16.91	$ 13.09	$ 9.54	$ 15.88	$ 9.54	$ 9.54	$ 9.54	$ 9.54	$ 9.54
Diluted Shares Outstanding (Average)	n/a	210.7	265.3	265.7	265.8	265.9	266.0	266.0	266.0	266.0	266.0	266.0	266.0
Market Capitalization (Average)	n/a	5,839.1	6,033.8	5,258.2	4,493.9	3,481.1	2,537.2	4,223.3	2,537.2	2,537.2	2,537.2	2,537.2	2,537.2
Enterprise Value (Average)	n/a	8,704.4	8,828.2	8,080.0	7,433.1	6,422.2	5,444.3	7,130.4	5,433.9	5,324.4	5,186.8	5,029.1	4,854.7
P/E	n/a	n/a	36.7 x	53.2 x	83.5 x	43.7 x	19.4 x	46.5 x	67.5 x	17.2 x	14.8 x	13.5 x	12.3 x
EV/EBITDA	n/a	23.6 x	20.1 x	20.8 x	18.8 x	16.7 x	10.7 x	17.0 x	15.7 x	10.8 x	9.8 x	9.1 x	8.3 x
FCF Yield to Market Capitalization	n/a	-3.3%	-5.5%	-2.1%	-2.9%	-1.4%	-1.2%	-7.6%	2.6%	6.5%	7.6%	8.4%	9.0%
FCF Yield to Enterprise Value	n/a	-2.2%	-3.7%	-1.4%	-1.8%	-0.7%	-0.6%	-4.5%	1.2%	3.1%	3.7%	4.2%	4.7%
Free Cash Flow													
EBIT	110.6	194.4	266.1	49.9	50.0	48.1	77.6	225.6	114.9	257.1	289.0	310.5	333.3
Tax Expense	35.7	3.3	(53.5)	(10.0)	(6.6)	(4.2)	(14.5)	(35.3)	(26.2)	(58.6)	(65.9)	(70.8)	(76.0)
D&A	173.5	174.8	172.4	47.0	48.6	48.0	50.2	193.8	231.3	234.2	239.0	243.8	248.8
Capital Expenditures	(156.9)	(159.6)	(239.1)	(65.9)	(70.3)	(75.9)	(65.9)	(278.0)	(247.7)	(250.8)	(255.9)	(261.1)	(266.4)
Changes in NWC	(421.2)	(404.6)	(475.7)	(133.5)	(153.1)	(63.2)	(77.4)	(427.2)	(6.8)	(17.2)	(13.3)	(9.6)	(10.1)
Unlevered Free Cash Flow	(258.3)	(191.6)	(329.7)	(112.5)	(131.4)	(47.2)	(30.1)	(321.2)	65.5	164.6	192.8	212.8	229.6

Valuation Summary

Current Price	**$ 9.54**
Target Price	$ 10.02
Total Return	5.1%
Recommendation	**HOLD**

DCF Valuation	
Perpetuity Growth Implied Price	$ 7.45
Exit Multiple Implied Price	$ 14.43
Comps Valuation	
Comps - EV/EBITDA Implied Price	$ 11.79
Comps - P/E Implied Price	$ 6.41

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Appendix 2: Discounted Cash Flow Analysis

Discounted Cash Flow Analysis

(Figures in mm USD)	*Jan-20* FY2020	*Jan-21* FY2021	*Jan-22* FY2022	*Apr-22* Q1-2023	*Jul-22* Q2-2023	*Oct-22* Q3-2023	*Jan-23* Q4-2023	*Jan-23* FY2023	*Jan-24* FY2024	*Jan-25* FY2025	*Jan-26* FY2026	*Jan-27* FY2027	*Jan-28* FY2028

WACC Calculations

Cost of Equity	
Risk-free rate	3.5%
Expected market return	10.4%
Market Risk Premium	**6.9%**
Beta	1.19
Cost of Equity	**11.7%**

Cost of Debt	
Pre-tax cost of debt	3.5%
Effective tax rate	22.8%
Cost of Debt	**2.7%**

WACC	
Market value of equity	2,537.2
Market value of debt	3,064.3
Total Capitalization	**5,601.5**
Cost of equity	11.7%
Cost of debt	2.7%
WACC	**6.8%**

Free Cash Flow

	FY2020	FY2021	FY2022	Q1-2023	Q2-2023	Q3-2023	Q4-2023	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028
EBIT	110.6	194.4	266.1	49.9	50.0	48.1	77.6	225.6	114.9	257.1	289.0	310.5	333.3
Less: Tax expense	35.7	3.3	(53.5)	(10.0)	(6.6)	(4.2)	(14.5)	(35.3)	(26.2)	(58.6)	(65.9)	(70.8)	(76.0)
Add: Depreciation and amortization	173.5	174.8	172.4	47.0	48.6	48.0	50.2	193.8	231.3	234.2	239.0	243.8	248.8
Less: Capital expenditures	(156.9)	(159.6)	(239.1)	(65.9)	(70.3)	(75.9)	(65.9)	(278.0)	(247.7)	(250.8)	(255.9)	(261.1)	(266.4)
Less: Change in net working capital	(421.2)	(404.6)	(475.7)	(133.5)	(153.1)	(63.2)	(77.4)	(427.2)	(6.8)	(17.2)	(13.3)	(9.6)	(10.1)
Unlevered Free Cash Flow	**(258.3)**	**(191.6)**	**(329.7)**	**(112.5)**	**(131.4)**	**(47.2)**	**(30.1)**	**(321.2)**	**65.5**	**164.6**	**192.8**	**212.8**	**229.6**
Discount factor									1.00	2.00	3.00	4.00	5.00
Present Value of Unlevered Free Cash Flow									**63.1**	**144.4**	**158.4**	**163.7**	**165.4**

Discounted Cash Flow Valuations

Perpetuity Growth Method		**Exit Multiple Method**	
Perpetuity Growth Rate	2.8%	**Terminal EV/EBITDA Multiple**	14.5 x
PV sum of unlevered FCF	695.1	PV sum of unlevered FCF	695.1
Terminal value	4,226.5	Terminal value	6081.8
Enterprise Value	**4,921.6**	**Enterprise Value**	**6,776.9**
Add: Cash	125.2	Add: Cash	125.2
Less: Debt	3,064.3	Less: Debt	3,064.3
Less: Other EV adjustments	-	Less: Other EV adjustments	-
Equity Value	**1,982.5**	**Equity Value**	**3,837.8**
Shares outstanding	266.0	Shares outstanding	266.0
Implied Share Price	**$ 7.45**	**Implied Share Price**	**$ 14.43**

Current Price	$ 9.54	Current Price	$ 9.54
Implied Price	**$ 7.45**	**Implied Price**	**$ 14.43**
Total Return	**-21.9%**	**Total Return**	**51.3%**

Perpetuity Growth Rate \ WACC	7.8%	7.3%	6.8%	6.3%	5.8%
1.8%	$ 1.52	$ 2.72	$ 4.17	$ 5.93	$ 8.14
2.3%	$ 2.48	$ 3.90	$ 5.63	$ 7.79	$ 10.57
2.8%	$ 3.63	$ 5.33	$ 7.45	$ 10.18	$ 13.81
3.3%	$ 5.04	$ 7.12	$ 9.80	$ 13.36	$ 18.34
3.8%	$ 6.80	$ 9.42	$ 12.92	$ 17.80	$ 25.10

Terminal EV/EBITDA Multiple \ WACC	7.8%	7.3%	6.8%	6.3%	5.8%
12.5 x	$ 10.30	$ 10.78	$ 11.28	$ 11.78	$ 12.31
13.5 x	$ 11.81	$ 12.32	$ 12.85	$ 13.40	$ 13.96
14.5 x	$ 13.31	$ 13.86	$ 14.43	$ 15.01	$ 15.61
15.5 x	$ 14.82	$ 15.40	$ 16.01	$ 16.63	$ 17.27
16.5 x	$ 16.32	$ 16.94	$ 17.58	$ 18.24	$ 18.92

Appendix 3: Comparable Companies Analysis

Comparable Companies Analysis

(Figures in mm USD)

Company	Ticker	Equity Value	Enterprise Value	EV/EBITDA Multiple 2022A EV/EBITDA	2023E EV/EBITDA	2024E EV/EBITDA	P/E Multiple 2022A P/E	2023E P/E	2024E P/E
Tractor Supply Company	(NASDAQ: TSCO)	26,150.7	30,218.4	17.0 x	15.4 x	14.3 x	24.5 x	22.6 x	20.5 x
Bark, Inc.	(NYSE: BARK)	218.6	188.1	n/a	n/a	n/a	(2.8 x)	(3.8 x)	(7.2 x)
Central Garden & Pet Company	(NASDAQ: CENT)	2,145.4	3,439.8	10.1 x	10.3 x	9.9 x	14.2 x	14.9 x	13.8 x
PetMed Express, Inc.	(NASDAQ: PETS)	318.9	216.5	7.6 x	13.6 x	9.7 x	15.1 x	38.3 x	21.2 x
Freshpet, Inc.	(NASDAQ: FRPT)	3,129.6	3,002.6	n/a	58.4 x	31.3 x	(50.5 x)	(123.0 x)	1,304.0 x
Chewy, Inc.	(NYSE: CHWY)	14,634.1	14,456.1	n/a	123.9 x	46.0 x	(190.4 x)	285.7 x	68.6 x
		-	-	-	-	-	-	-	-
		-	-	-	-	-	-	-	-
		-	-	-	-	-	-	-	-
		-	-	-	-	-	-	-	-
Petco Health and Wellness Company Inc.	**(NASDAQ: WOOF)**	**2,537.2**	**5,495.4**	**12.5 x**	**13.1 x**	**10.4 x**	**15.4 x**	**27.9 x**	**19.9 x**
Median					**14.5 x**	**12.1 x**		**18.8 x**	**20.9 x**
Mean					**35.9 x**	**14.9 x**		**39.1 x**	**236.8 x**
High					**123.9 x**	**46.0 x**		**285.7 x**	**1,304.0 x**
Low					**(6.2 x)**	**(21.7 x)**		**(123.0 x)**	**(7.2 x)**

	EV/EBITDA Impliled Price		P/E Implied Price	
Median	**$ 11.79**	**$ 13.02**	**$ 6.41**	**$ 10.03**
Mean	**$ 45.50**	**$ 18.60**	**$ 13.36**	**$ 113.68**
High	$ 184.22	$ 80.61	$ 97.53	$ 625.92
Low	-$ 20.94	-$ 54.47	-$ 42.00	-$ 3.47

Appendix 4: Operating Model

Operating Model

	Jan-20	Jan-21	Jan-22	Apr-22	Jul-22	Oct-22	Jan-23	Jan-23	Jan-24	Jan-25	Jan-26	Jan-27	Jan-28
(Figures in mm USD)	**FY2020**	**FY2021**	**FY2022**	**Q1-2023**	**Q2-2023**	**Q3-2023**	**Q4-2023**	**FY2023**	**FY2024**	**FY2025**	**FY2026**	**FY2027**	**FY2028**
Revenue Analysis - Growth													
Consumables revenue growth %		3.4%	19.3%	15.3%	12.3%	12.0%	12.1%	12.9%	10.0%	8.0%	7.0%	5.0%	5.0%
Supplies and companion animals revenue growth %		20.1%	11.8%	-9.0%	-9.5%	-9.4%	-7.8%	-8.9%	-2.0%	7.0%	7.0%	5.0%	5.0%
Services and other revenue growth %		6.1%	43.2%	18.1%	21.4%	24.6%	17.0%	20.2%	17.0%	10.0%	10.0%	5.0%	5.0%
Total Revenue Growth, %		**11.0%**	**18.0%**	**4.3%**	**3.2%**	**4.0%**	**4.2%**	**3.9%**	**6.2%**	**7.9%**	**7.4%**	**5.0%**	**5.0%**
Revenue Analysis - Segmented Breakdown													
Consumables	2,054.3	2,123.5	2,533.8	685.9	687.1	720.5	766.1	2,859.6	3,145.6	3,397.2	3,635.0	3,816.8	4,007.6
Supplies and companion animals	1,938.9	2,328.7	2,603.1	599.2	600.7	575.3	595.8	2,370.9	2,323.5	2,486.1	2,660.2	2,793.2	2,932.8
Services and other	441.3	468.0	670.3	190.9	193.0	205.4	216.1	805.5	942.4	1,036.6	1,140.3	1,197.3	1,257.2
									-	-			
Total Revenue, mm	**4,434.5**	**4,920.2**	**5,807.1**	**1,476.0**	**1,480.8**	**1,501.2**	**1,578.0**	**6,036.0**	**6,411.4**	**6,920.0**	**7,435.5**	**7,807.2**	**8,197.6**
Schedules - Property and Equipment													
Property and Equipment, beginning		**656.3**	**726.9**	**726.9**	**735.3**	**771.1**	**791.6**	**803.3**	**803.3**	**819.7**	**836.4**	**853.3**	**870.7**
Add: Capital expenditures		159.6	239.1	65.9	70.3	75.9	65.9	278.0	247.7	250.8427	255.9312	261.123	266.4201
Add: Acquisitions		-	4.3	-	2.9	4.9	1.9	9.6	-	-	-	-	-
Less: Divestitures		-	-	-	35.0	(35.0)	-	-	-	-	-	-	-
Less: Depreciation		(174.8)	(172.4)	(47.0)	(48.6)	(48.0)	(50.2)	(193.8)	(231.3)	(234.2)	(239.0)	(243.8)	(248.8)
Less: Other adjustments		(13.4)	(71.0)	(10.5)	(23.8)	22.7	(5.9)	(93.8)					
Property and Equipment, ending	**656.3**	**627.5**	**726.9**	**735.3**	**771.1**	**791.6**	**803.3**	**803.3**	**819.7**	**836.4**	**853.3**	**870.7**	**888.3**
Capex, % of Beginning P&E, %		**24.3%**	**32.9%**	**36.3%**	**38.2%**	**39.4%**	**33.3%**	**34.6%**	**30.8%**	**30.6%**	**30.6%**	**30.6%**	**30.6%**
Estimated P&E Useful Life, years		**3.8**	**4.2**	**3.9**	**3.8**	**4.0**	**3.9**	**4.1**	**3.5**	**3.5**	**3.5**	**3.5**	**3.5**
Schedules - Retained Earnings													
Retained Earnings, beginning		**(780.5)**	**142.2**	**142.2**	**166.9**	**180.3**	**200.2**	**233.0**	**233.0**	**266.5**	**409.9**	**577.8**	**762.3**
Add: Net income		(31.7)	159.8	23.8	13.5	19.9	32.7	89.9	33.6	143.3	167.9	184.6	202.1
Less: Dividends paid		-	-	-	-	-	-	-	-	-	-	-	-
Less: Other adjustments		790.0	(159.8)	0.9	-	-	0.0	(89.9)					
Retained Earnings, ending	**(780.5)**	**(22.3)**	**142.2**	**166.9**	**180.3**	**200.2**	**233.0**	**233.0**	**266.5**	**409.9**	**577.8**	**762.3**	**964.5**
Dividend Per Share, $/share	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**
Margin Analysis													
COGS, % of revenue, %	57.0%	57.2%	58.2%	58.8%	59.9%	60.2%	60.2%	59.8%	59.8%	58.1%	58.1%	58.1%	58.1%
Gross Profit, % of revenue, %	**43.0%**	**42.8%**	**41.8%**	**41.2%**	**40.1%**	**39.8%**	**39.8%**	**40.2%**	**40.2%**	**41.9%**	**41.9%**	**41.9%**	**41.9%**
SG&A, % of revenue, %	36.2%	35.3%	34.2%	34.6%	33.5%	33.4%	31.7%	33.3%	34.8%	34.8%	34.8%	34.8%	34.8%
R&D, % of revenue, %	-	-	-	-	-	-	-	-	-	-	-	-	-
OPEX, % of revenue, %	0.4%	-	-	-	-	-	-	-	-	-	-	-	-
EBITDA, % of revenue, %	**6.4%**	**7.5%**	**7.6%**	**6.6%**	**6.7%**	**6.4%**	**8.1%**	**6.9%**	**5.4%**	**7.1%**	**7.1%**	**7.1%**	**7.1%**
Income Tax Rate, % of EBT, %	**25.1%**	**8.0%**	**26.4%**	**32.6%**	**36.7%**	**19.4%**	**34.5%**	**31.5%**	**22.8%**	**22.8%**	**22.8%**	**22.8%**	**22.8%**
Working Capital Analysis													
Current Assets													
Accounts receivable, % of revenue, %	0.7%	0.9%	1.0%	0.7%	0.8%	0.8%	0.8%	0.8%	0.9%	0.9%	0.9%	0.9%	0.9%
Inventories, % of revenue, %	10.8%	10.9%	11.6%	11.6%	12.2%	12.0%	10.3%	10.8%	11.7%	11.2%	11.2%	11.2%	11.2%
Prepaid expenses, % of COGS, %	1.0%	1.4%	1.3%	1.5%	1.5%	1.2%	1.3%	1.4%	1.3%	1.3%	1.3%	1.3%	1.3%
Current Liabilities													
Accounts payable, % of COGS, %	11.6%	12.1%	12.0%	11.3%	11.8%	10.6%	10.0%	10.6%	12.3%	11.8%	11.8%	11.8%	11.8%
Accrued liabilities, % of revenue, %	3.3%	3.0%	3.6%	3.6%	3.7%	3.7%	3.4%	3.6%	3.5%	3.4%	3.4%	3.4%	3.4%

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