

Restaurant Research Think Piece – February 2011

Private Equity Return Hurdles in the Restaurant Space

- We asked Trinity Capital for some color on current return benchmarks for private equity investments in the restaurant space. We believe Trinity's comments below are particularly timely for all restaurant industry players:
- According to Trinity, **private equity firms are generally looking for 25% compounded annual returns on equity capital invested in middle-market restaurant buyouts; this is down from 30% to 35% targets prior to the financial crisis of 2008.** Lower return goals reflect the new economic environment which has prevailed during the last two years, including: (1) smaller advance rates for leveraging buyout transactions; (2) more realistic assumptions about growth performance of buyout candidates; (3) a lower overall interest rate and investment return environment, and (4) a more conservative view of purchase price multiples when exiting an investment - generally, private equity investors no longer assume that they can sell an investment at a higher purchase price multiple than they paid at acquisition.
- Historically, private equity firms have earned money through five primary disciplines or market developments:
 - attaining market discounted acquisition price
 - aggressive use of financial leverage
 - operational optimization: enhanced unit economics; cost cutting, etc.
 - strategic guidance regarding acquisitions and divestitures
 - purchase price multiple expansion and recapitalization
- Private equity firms regularly concentrate on those disciplines in which they excel. Creative firms are known for their use of leverage or transaction structure to enhance the returns for their investors. Many institutions engage a management consulting firm to assist in their due diligence and to optimize operations once the transaction is closed. Some private equity concerns are known for acquiring distressed restaurant companies out of bankruptcy or otherwise averaging very low purchase price multiples in their portfolio. Other firms are well-known for their ability to continuously rollup restaurant concepts or segments or otherwise “add-on” complementary acquisitions in order to create more efficiency and larger critical mass for their investment. **In any case, the multiples private equity are willing to pay for restaurant companies and their return expectations will depend heavily on their skills and philosophy.**
- *About the Contributing Firm:* Trinity Capital is a boutique investment banking firm that provides financial advice to middle market businesses regarding mergers and acquisitions, leveraged and management buyouts, debt restructuring and private placements of debt and equity. Since our inception in 2000, the firm has completed nearly \$20 billion in successful transactions. Trinity is an internationally recognized industry leader in the restaurant, franchise and food sectors. The Firm has been engaged by such companies as Burger King Corp., Yum! Brands, Inc., Panda Restaurant Group, and Dunkin’ Brands, Inc. in multiple transactions with combined transaction values of several billion dollars. In addition, the Firm has been retained

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by some of the nation's most successful private equity organizations including Bain Capital, Thomas H. Lee & Company, The Carlyle Group, Goldman Sachs Capital Partners, Sun Capital and Lee Equity Partners LLC. Our client service philosophy is designed to provide each client, regardless of their size or transaction, the full complement of the firm's professionals, resources, expertise and experience.

- CONTACT INFO: Trinity Capital * 11755 Wilshire Blvd., Ste. 2450, Los Angeles, CA 90025 * 310.268.8330 * www.trinitycapitalllc.com

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