

Efficient Research Solutions & Value-Added Insight

Restaurant Research Think Piece – January 2012

Brand Strength Trumps Macroeconomics

"Restaurant Theory" always has held that eating out propensity was a function of convenience (consumers stretched for time), flavor profile, price, along with growth in disposable income, urbanization, travel and mobility. Restaurant success then supposedly followed these broad macroeconomic waves. But an important addition to the theory now apparent is that **brand matters**.

While macroeconomics is important, it doesn't explain the following:

- **McDonald's**: a 64 year old concept that just recently delivered an 8th year of strong worldwide sales, unit growth and profitability performance has managed to build AUV, customers and unit locations almost every year, despite the macroeconomic waves.
- **Subway**, which now outnumbers even McDonald's store counts world-wide, was able to post double digit same store sales gains in 2008/2009, realized in the utter depths of the Great Recession.
- How some restaurant institutions (**think: Howard Johnson's, Burger Chef, Bill Knapp's, Steak N Ale/Bennigan's**) have totally or almost totally disappeared despite rising incomes, and the rising food away from home consumption? Even some current fast casual names (**like Pat and Oscar's and Daphne's Greek Café**) have struggled despite all their press buzz.
- How **Chipotle**, a phenomenon in its own right, has gone from an AUV of \$652,000 in 2000 to almost \$2 million today, despite a vastly oversaturated domestic restaurant market and lingering economic weakness marked by high unemployment and underemployment in its core customer ranks.

The DNA and composition of the brand, which transcends macroeconomics, is responsible. Beginning in 2005, and especially since 2008, we see much less that individual company trends move in lock step with the macroeconomics. There are more outliers, more bifurcation.

Strength of brand DNA shows up with consumer interest, loyalty and frequency. It shows in the M&A world, affecting EV/EBITDA multiples. It shows up in the stock market via PE multiples. And it shows up in credit risk and interest rates.

To be sure, same store sales, return on capital invested, unit growth - the classical three drivers of restaurant company value - is important. So too is store level economics, and new product news.

However, restaurant success is not just about "new wave" companies, management strengths, company culture, board governance, amount of leverage and debt, privately held v. public or private equity motivations, marketing budget size and efficiency, number of media GRP points, coupons, pretty restaurants, geographical development zone, stock valuation, CAPEX and remodeling, company owned v. franchising and management skills. Nor is it only about taste quality, service value and other differentiators.

Rather it seems that a holistic sum of all these influences is needed for success - it's not just what

Restaurant Research ChainRestaurantData.com

the consumer sees or believes, but literally a stew of these factors that drives brand value. For investors, it is complicated. But restaurants are the sum of thousands of moving pieces.

Our special thanks for this insightful *Think Piece* to author John A. Gordon who is an independent chain restaurant analyst, and his firm, Pacific Management Consulting Group 100% focuses on chain restaurant analysis and advisory engagements. John can be contacted at

jgordon@pacificmanagementconsultinggroup.com, www.pacificmanagementconsultinggroup.com.

Restaurant Research's *Concept Reports* provide clients with detailed brand assessment as revealed by unit level data and analysis which is useful for benchmarking, lending and investing due diligence and competitive intelligence. For information on how to order our *Concept Reports* (coverage includes the 22 largest brands), please contact us at (203) 405-1901 or info@ChainRestaurantData.com.

www.ChainRestaurantData.com

RR Clients

Includes major lenders, investors, major US restaurant chains, operators and industry consultants. Please check www.ChainRestaurantData.com for a partial client list and customer testimonials.

More About Us

Restaurant Research LLC leverages an extensive network of industry players as part of its annual Concept Benchmark Analysis due diligence process for 22 large US restaurant chains. Also, RR tracks store level data for all major chains with system-wide sales in excess of \$1B across all major restaurant segments in order to produce 11 key Industry Data Topic reports.

Copyright 2012 Restaurant Research® LLC. All rights reserved.

Disclaimer of Liability: Although the information in this report has been obtained from sources Restaurant Research® LLC believes to be reliable, RR does not guarantee its accuracy. The views expressed herein are subject to change without notice and in no case can be considered as an offer or solicitation with regard to the purchase or sales of any securities. Restaurant Research's analyses and opinions are not a guarantee of the future performance of any company or individual franchisee. RR disclaims all liability for any misstatements or omissions that occur in the publication of this report. In making this report available, no client, advisory, fiduciary or professional relationship is implied or established. This report is intended to provide an overview of the restaurant industry, but cannot be used as a substitute for independent investigations and sound business judgment.