

BDO'S RESTAURANT PRACTICE BENCHMARKING UPDATE

THE COUNTER:

Restaurant Industry Scorecard



SAME-STORE SALES

Although the third quarter tends to yield weaker performance for the restaurant industry with back-to-school, the service sector—and particularly restaurants—were hit especially hard this summer following the devastation of Hurricanes Harvey, Irma and Maria. Same-store sales were down 0.4 percent through the third quarter. As restaurants look to recover and capitalize on bullish expectations for the upcoming holiday season, businesses should focus on managing costs while offering customers what they truly want: convenience and a memorable experience.

As always, pizza saw the highest same-store sales increase of all segments at 3.2 percent through Q3. This growth is owed to Domino's continued domination as the company tailors its rewards program and improves digital experiences. For instance, the company recently announced a partnership with the office chat platform, Slack, which has 3 million daily active users, allowing hungry users to "slack" a pizza order without opening a browser. It's important to note that without the help of Domino's, the segment would have experienced a 0.8 percent decline. Looking to get a slice of Domino's success, Pizza Hut is reinvesting in advertising and restaurant technology to help drive sales. Last spring, Pizza Hut's parent company, Yum! Brands, [announced plans](#) to invest \$130 million to turn the brand around.

The only other segment that showed positive signs through Q3 was quick serve, posting an increase of 0.8 percent. The segment's quarterly gain can be attributed to Carrols Restaurant Group, a Burger King franchisee, and Taco Bell, posting 3.9 percent and 5 percent gains, respectively. Taco Bell credits this quarter's margin increases to franchising success, but caveated in the Yum! Brands Q3 earnings [press release](#) that food and labor cost inflation offset some growth.

Fast casual continued to slow this quarter with an overall 2.1 percent decrease, the largest change of any segment. Chipotle was an exception, however, leading the segment with an 8.3 percent gain through Q3. The company saw success with its new queso offering in September and ongoing efforts to make 2016's foodborne illness

The **pizza segment** experienced the most significant growth through Q3, with a same store sales increase of **3.2%**. However, without Domino's the segment would have experienced a 0.8% decline.



a distant memory. Pulling the segment down, fast casuals from Texas to Georgia had to close their doors due to this summer's hurricanes. In particular, Pollo Tropical of Fiesta Restaurant Group experienced a loss of 8.5 percent following closures in Florida and Atlanta.

Sales at casual and upscale casual restaurants fell 0.9 percent and 0.4 percent, respectively. Texas Roadhouse led the pack in the casual segment with a 4 percent boost through the third quarter due to higher traffic and a focus on operations, delivery and customer service. On the other hand, Applebee's contributed to losses with a 7.3 percent dip. In recent months, the company announced plans to double down on its "Middle America roots" by slimming menu options, taking the target off of millennial customers and downsizing their national store footprint. Combining this strategy with its effort to spur sales through promotions like the \$1 margarita special, Applebee's may emerge from the slump. For upscale casual brands, Eddie V's was on top again, posting a 3.5 percent gain through the quarter—a figure that reflects its commitment to guest experience and food quality. Sullivan's Steakhouse saw a 3.8 percent decline driven by the elimination of lunch at certain locations, starting in the second quarter.

COMMODITIES AND COST OF SALES

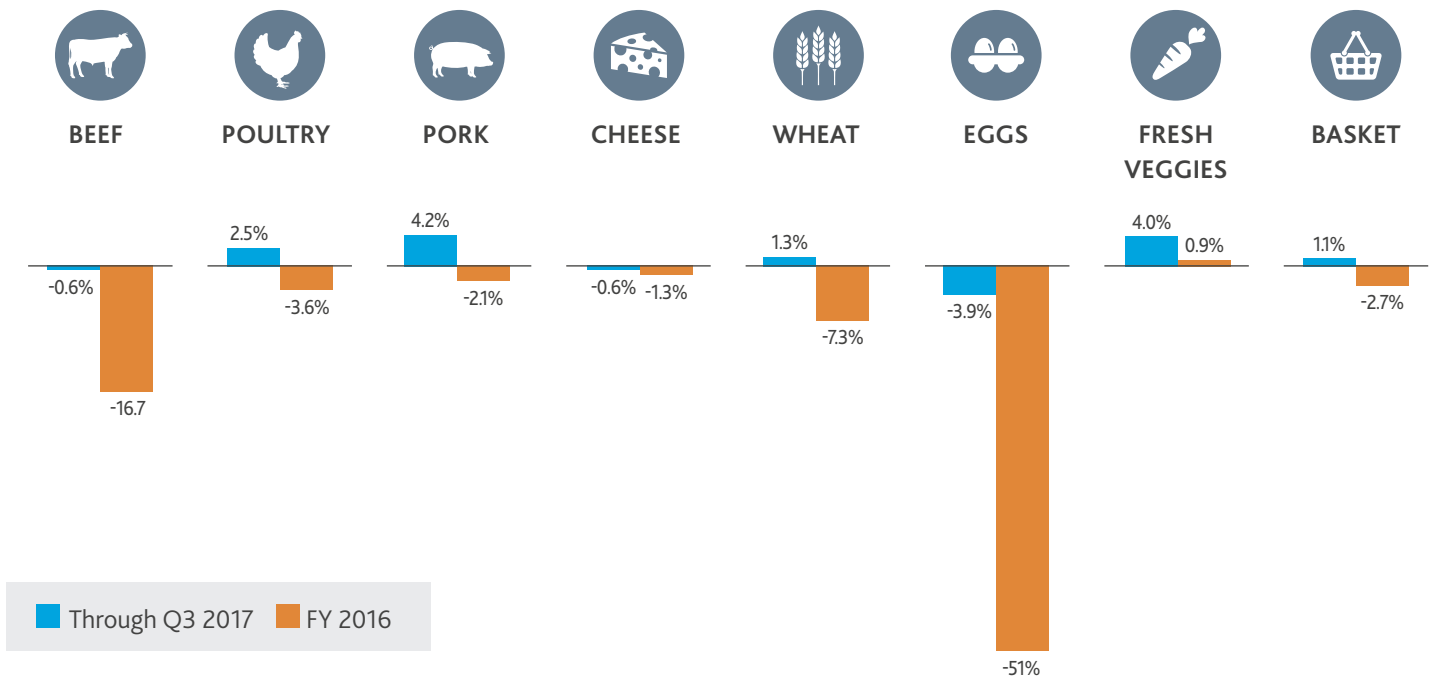
Cost of sales were largely up across the board at 28.9 percent, up 0.2 percent from 28.7 percent through Q3 2016. The only segment that did not experience a modest increase in cost of sales through this quarter was pizza, where lower cheese prices helped to offset other expenses.

Commodities fluctuated through Q3, with poultry, fresh vegetables and pork prices up 2.5 percent, 4 percent and 4.2 percent, respectively. On the other end of the spectrum, egg and beef prices were down 3.9 percent and 0.6 percent, respectively, through Q3. As companies work to cater to consumers' demands for high quality and freshness, restaurants will have to get creative with menu engineering to satisfy these cravings while managing somewhat unpredictable costs.

Cost of sales increased **0.2%** across all segments.



Commodities



LABOR

While cost of sales can be tricky to manage and commodities are often beyond a business’s control, labor is one area where operators can scrutinize cost hour-by-hour. In an industry characterized by low margins, every dollar counts. Labor costs were up across all segments through Q3, showing an average workforce price tag increase of 0.7 percent compared to FY 2016.

Though restaurants are impacted by external forces, including changing regulations and minimum wage laws, businesses can manage what trickles down to the bottom line by using labor management software to ensure better labor modeling. To combat minimum wage upticks, some restaurants are dissecting back-of-

the-house operations to see where they can cut prep time and make smarter staffing choices based on time of day and predictable traffic increases.

LOOKING AHEAD

Restaurants are realizing the detriments of explosive growth and striving to be a jack of all trades. As a result, many brands are working to improving sales and profitability at current store levels by investing in software and equipment as well as store remodels. For example, QSRs are seeing that more sales are coming from drive-throughs rather than the dining room. Thus, they’re downsizing store footprints and investing in drive-through efficiencies to reflect that.

For operators, pulling back on growth and reinvigorating current stores may also help combat encroachment from nontraditional players like meal kit services, grocery stores and retailers. We expect to see the industry try to level the playing field with a renewed focus on customer experience. The key will be to stay nimble and differentiated in a saturated market to keep customers coming back.

Labor costs increased 0.7% across all segments.

ABOUT THIS UPDATE:

Each quarter, we compile the operating results of publicly traded restaurant companies to provide you with timely benchmarking information.

Cost of sales includes food and beverage for all segments. Quick serve and fast casual segments also include packaging costs. Labor costs include restaurant level wages, payroll, taxes and benefits.

**Prior results have been restated to conform to current-year data availability.*

	Through Q3 2017	Through Q3 2016	Inc. (Dec)	FY 2016	FY 2015	Inc. (Dec)
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Quick Serve

Same Store Sales	0.8%			1.0%		
Cost of Sales	30.0%	29.5%	0.5%	29.5%	30.7%	-1.2%
Labor	29.4%	28.7%	0.7%	28.4%	28.1%	0.3%
Prime Costs	59.4%	58.5%	0.9%	58.2%	59.0%	-0.8%

Fast Casual

Same Store Sales	-2.1%			-0.9%		
Cost of Sales	30.7%	30.6%	0.1%	30.6%	31.2%	-0.6%
Labor	28.8%	27.9%	0.9%	28.2%	26.6%	1.6%
Prime Costs	59.5%	58.5%	1.0%	58.8%	57.8%	1.0%

Casual

Same Store Sales	-0.9%			-0.7%		
Cost of sales	28.2%	27.9%	0.2%	28.0%	28.5%	-0.5%
Labor	33.2%	32.4%	0.8%	32.7%	32.0%	0.7%
Prime costs	61.4%	60.4%	1.0%	60.7%	60.5%	0.2%

Upscale Casual

Same Store Sales	-0.4%			-0.1%		
Cost of sales	27.9%	27.7%	0.2%	27.6%	28.0%	-0.4%
Labor	31.0%	30.3%	0.7%	29.9%	29.3%	0.6%
Prime costs	59.0%	58.1%	0.9%	57.6%	57.4%	0.2%

Pizza

Same Store Sales	3.2%			4.6%		
Cost of Sales	26.2%	27.1%	-0.9%	25.7%	25.9%	-0.2%
Labor	31.2%	30.4%	0.8%	30.3%	29.8%	0.5%
Prime Costs	59.0%	59.5%	-0.5%	57.4%	56.8%	0.6%

Grand Average

Same Store Sales	-0.4%			0.1%		
Cost of Sales	28.9%	28.7%	0.2%	28.6%	29.3%	-0.7%
Labor	30.8%	30.1%	0.7%	30.1%	29.3%	0.8%
Prime Costs	59.9%	59.1%	0.8%	59.0%	58.8%	0.2%

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