REPORT FROM "MUST ATTEND" RESTAURANT FINANCE & DEVELOPMENT CONFERENCE - TAKEAWAYS

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RESTAURANT FINANCE & DEVELOPMENT CONFERENCE - TAKEAWAYS

I just returned from John Hamburger's RFDC, the must attend conference for restaurant industry professionals, in Las Vegas. Something approaching 3,0000 attendees spent two days networking, listening to panels focused on critical industry developments, and getting macro-economic updates from keynote speakers such as Arthur Laffer (Ronald Reagan's economic guru) and Guy Adami (daily CNBC stock market commentator).

Three major takeaways:

(1) There is still a huge amount of capital available to finance restaurant growth as well as renovation. Valuations are high on a historical basis, but interest rates are still low, investors of all stripes are "reaching for yield" so institutions have money to invest in pizza, burgers, and tacos. All of this is cyclical. Those of us who have been around for a while have lived through several similar periods, and this too shall pass. From a macro standpoint, very low interest rates spawn "misallocation of capital" as investors (and institutions in turn) underestimate the risk side of the equation. The music is playing so the dance goes on. As Warren Buffet famously said: "When the tide goes out, we will find out who is swimming naked".

As a corollary, the question is always asked at this conference and elsewhere: "How big does my operation have to be to raise capital from institutions?" And most private equity investors, will respond sagely with something like "We like to see upwards of $5 million of EBITDA at the store level". To that I say: "Beauty is in the eye of the beholder". It depends on "what you've got" and "who's running it". For example: If Danny Meyer, or Howard Schultz, had one location, in his mind, he could raise money from institutions and/or individuals. Away from the restaurant industry, look at the billions of dollars that Tesla and Uber have raised. They are losing billions, breakeven is years away, but they tell a good story. Bringing it back to home for us, it depends on the unit level economics (existing, or even planned) and the credentials of management. Size matters, but not always.

(2) By far the issue of the day for the industry is DELIVERY. The workshops and panels dealing with delivery were standing room only. Virtually everyone is evaluating it, testing it, trying to offset lower dine-in traffic by re-capturing the customer with delivery. The big names are pretty well known: Grubhub, DoorDash, Postmates, Uber Eats. Everyone knows by now that profit margins on the delivered food is lower than within the store, due to the commissions paid to the delivery agent. It's also obvious to most of us that loss of control over "the last mile" provides an element of risk to

the brand. However, the really big stumbling block as described by many of the conference speakers is that the delivery agents retain the customer information, therefore compromising the restaurant's degree of exclusivity with the customer. Therefore: any restaurant chain of substance, who can afford the time and money to develop it, is intent on developing an in-house capability to control the process, at least to the degree of controlling the customer information. It will likely turn out that the most customers for the delivery companies will be independents and multi-unit operators too small to afford in-house delivery capabilities.

(3) Profit margins for restaurant operators, even the best of breed, are severely challenged, with labor costs (especially) rising as far as the eye can see. Traffic continues to be challenged, in spite of delivery, mobile apps, curbside pickup and the other operating initiatives. Franchisees are increasingly unhappy with franchisors marketing leadership that focuses on discounted deals. The traditional "conflict of interest" between franchisors, driven by royalty generation, and franchisees, who fight the daily battle for unit level profit, has been exacerbated by the current environment which gives every indication of continuing. Franchise associations at Tim Horton's, Dunkin' (forget the Donuts), Jack in the Box, and even McDonald's are becoming "Activists". This week, flying to Las Vegas, TV commercials came across my screen for "All you can eat fries" at Wendy's, and "Ten chicken nuggets for $1" at Burger King. A day later, the Burger King commercial for "Three pancakes for $0.89" hit my TV screen. So the key promotional price point has become ONE DOLLAR. So now, at Burger King you can get ten nuggets and three pancakes for $1.89. I personally wouldn't want to make a habit of it, but it might get me through the lunch hour:) Seriously, while the franchisor will make the case that these deals are traffic builders, only one end of the barbell, etc., it's hard to believe that profitability will be enhanced for the franchisees, and they are making their feelings known.

I would welcome input from any of you relative to other important issues, explored at the Conference, that could be worthy of discussion here.

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