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# First Watch Restaurant Group, Inc. (FWRG) Q2 2024 Earnings Call Transcript

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## Q2: 2024-08-06 Earnings Summary

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EPS of \$0.18 **beats by \$0.06** | Revenue of \$258.56M (19.54% Y/Y) **beats by \$914.14K**

First Watch Restaurant Group, Inc. (NASDAQ:[FWRG](#)) Q2 2024 Earnings Conference Call August 6, 2024 8:00 AM ET

### Company Participants

Steven Marotta – Vice President-Investor Relations

Chris Tomasso – President and Chief Executive Officer

Mel Hope – Chief Financial Officer

### Conference Call Participants

Patrick Johnson – Stifel

Brian M. Vaccaro – Raymond James

Andy Barish – Jefferies

Pratik Patel – Barclays

Gregory Francfort – Guggenheim Securities

Ali Arfstrom – Piper Sandler

Katherine Griffin – Bank of America

Karen Holthouse – Citi

## Operator

Thank you for standing by, and welcome to the First Watch Restaurant Group, Inc. Second Quarter Earnings Conference Call occurring today, August 6, 2024, at 8:00 AM Eastern Time. Please note that all participants are currently in a listen-only mode. Following the presentation, the conference call will be open for analyst questions and instructions on how to ask a question will be given at that time. This call will be archived and available for replay at [investors.firstwatch.com](https://investors.firstwatch.com) under the News & Events section.

I would now like to turn the conference over to Steven Marotta, Vice President of Investor Relations at First Watch to begin.

## Steven Marotta

Hello everyone. I am joined by First Watch's Chief Executive Officer and President, Chris Tomasso; and Chief Financial Officer, Mel Hope. This morning, First Watch issued its earnings release for the second quarter of fiscal 2024 on Globe Newswire and filed its quarterly report on Form 10-Q with the SEC. These documents can be found at [investors.firstwatch.com](https://investors.firstwatch.com).

This conference call will include forward-looking statements that are subject to various risks and uncertainties that could cause the company's actual results to differ materially from these statements. Such statements include, without limitations, statements concerning the condition of the company's industry and its operations, performance and financial condition, outlook, growth plans and strategies, and future expenses.

Any such statements should be considered in conjunction with cautionary statements in the company's earnings release and the risk factor disclosure in the company's filings with the SEC, including our Annual Report on Form 10-K and quarterly reports on Form 10-Q.

First Watch assumes no obligation to update these forward-looking statements, whether as a result of new information, future developments, or otherwise, except as may be required by law. Lastly, management's remarks today will include references to various non-GAAP measures, including restaurant-level operating profit, restaurant-level operating profit margins, adjusted EBITDA and adjusted EBITDA margin. Investors should review the reconciliation of these non-GAAP measures to the comparable GAAP results contained in the company's earnings release filed this morning.

During today's call, references to same-restaurants sales and traffic growth compares the 13-week periods ended June 30, 2024 and July 2, 2023 in order to compare like-for-like periods. Otherwise, any reference to percentage growth when discussing second quarter performance is a comparison to the second quarter of 2023 unless otherwise indicated.

And with that, I will turn the call over to Chris.

### **Chris Tomasso**

Thanks, Steve. Good morning. I'm pleased to report another quarter of solid operating results and adjusted EBITDA growth, and I thank everyone in our organization for their hard work. I remain extremely proud of our teams for continuing to control what we can control and delivering exceptional customer experiences both of which are key factors in sustaining our profitability improvements as evidenced by our adjusted EBITDA performance.

As expected, traffic was challenging during the quarter given the macro headwinds throughout most of our industry. Despite that, we are operating at a very high level and are comfortable reiterating our fiscal year 2024 total revenue and adjusted EBITDA guidance.

In Q2, we generated \$299 million in system-wide sales, \$258.6 million in total revenues and \$35.3 million in adjusted EBITDA, the latter of which represented a 37% increase versus last year.

Additional second quarter highlights include sequentially better same restaurant traffic compared to the first quarter, positive mix, improved labor productivity and better than expected contributions from both our new restaurant openings and strategic franchisee acquisitions completed over the past year.

We opened seven total new restaurants in six states during the second quarter, six of which are company-owned and one that's franchise-owned. We also completed our largest First Watch franchisee acquisition on April 15 when we purchased 21 restaurants along with the development rights in the Raleigh-Durham, North Carolina DMA.

Our results in our internal KPIs demonstrate that we continue to operate our restaurants with remarkable efficiency. Our NROs by vintage and across geographies have been outstanding, performing at or above their sales expectations, and our pipeline for future growth is stronger than ever.

As of today, we have more than 130 new restaurant projects in our pipeline and we are on track with our long-term target of delivering annual new restaurant growth in the low-double digits as a percentage of our system. As we continue to expand the system, the pipeline remains a significant driver of long-term value creation and earnings growth.

As we stated on our last earnings call, we believe our traffic headwinds are more macro than micro and our insights indicate that one much of the industry-wide pressure is occurring primarily during the weekday breakfast and lunch dayparts as consumers look to trim weekday occasions. Two, that the behavior and frequency of our repeat customers remain relatively consistent, which is encouraging. And three, that occasions from our infrequent customers, those who average a single visit annually have declined, as have visits by lower income consumers.

While it's evident that our customer is under some pressure, our business is strong and our long-term strategy remains intact and compelling. In the second quarter, our customer experience scores improved versus the same period last year. Growth in our per person average check exceeded carried pricing as a result of positive mix through menu innovation.

Our ticket times were more than 20% faster than last year. Our employee turnover improved again, marking six straight quarters. It's clear that our investments in technology both customer facing and our enhanced business intelligence tools for our operations teams are bearing fruit, exemplified by a record Mother's Day that featured positive 1.8% same restaurant traffic, positive 5.4% same restaurant sales, better than 20% faster ticket times and higher customer experience scores. And in the second quarter, Placer.ai data indicates that First Watch's traffic share increased against the direct daytime dining competitive set.

As I've shared with investors and our teams, our approach in the current environment is to double down where we already excel. Through our investments in technology, data capture and analytics, we now know and continue to learn more about First Watch customers than ever. We're putting those insights to work.

We've accumulated an opt in database of roughly 7 million customers and are analyzing and segmenting customer information by visitation patterns to deliver the appropriate communication to the appropriate audience at the appropriate time. Whether we're delighting our repeat customers, reengaging a lapsed customer or reaching a competitive user, we are focused on targeting demand generation across our own communication channels as well as paid digital media.

Our approach is in stark contrast to the broad based discounting that many in our industry are deploying. It's our opinion that while aggressive promotions drive short-term traffic in some instances, we view that tactic as sacrificing margin from loyal customers while also attracting temporary discount motivated customers with low recurrence rates.

We will lean into traffic driving marketing initiatives the First Watch way, focusing on profitable growth with messages that lever our core brand attributes to increase the frequency of targeted customer groups. We realize that some may not fully appreciate our approach, but our industry has a history littered with brands that lost their way during challenging times. First Watch has always played to win the long game.

First Watch restaurants deliver exceptional everyday value featuring a culinary forward menu using fresh, high quality ingredients, and consistent customer service that creates memorable experiences. We're very measured when it comes to pricing actions in any environment and our conservatism, which is guided by our goal of preserving our value proposition is well documented.

The modest 1% price action we implemented during the last week of the second quarter is merely a continuation of our conservative pricing philosophy and is consistent with the multi-year strategy we implemented upon exiting COVID.

As I stated earlier, our growth engine continues to hum and is a particular point of strength for us and our long-term growth outlook remains in place. Inclusive of the 40 company-owned NROs combined with the 45 franchise acquisitions completed, we've added nearly 4,500 additional annual operating weeks to our operating model since the second quarter of 2023. Our new restaurants as a group and by vintage are meeting or exceeding our targets.

New restaurant third-year AUV targets have increased by more than 40% since 2019 and our capital return criteria continues to be achieved. We had 538 restaurants in operation at the end of the second quarter, representing only a quarter of our total addressable market of 2,200. And encouragingly, no DMA is completely built out. The 130 new restaurant projects currently under development reflect nearly 25% of our current system. Our future growth opportunities abound and our manager ready bench is as robust as our real estate pipeline.

Since May 2023, our franchise acquisition strategy has resulted in our conversion of 45 restaurants from franchise operated to company owned, including our largest First Watch acquisition, which took place in the second quarter. Restaurants we have acquired from our franchisees have added nearly \$100 million in annual restaurant sales and 17 new DMAs for corporate development.

We're delighted with how these restaurants, leaders and employees have integrated into our corporate operations. We successfully retained 94% of leaders, manager and above across our 2024 acquisitions, including 100% of directors of operations. In short, times are good for us, just not in the usual way. Our most loyal customers expect a consistently high experience and are maintaining frequency. We're delivering on their high expectations.

Furthermore, both our restaurant and enterprise level profitability is exceptional. While we're not immune to macro headwinds, we are managing through these times by playing to our strengths, which is paying off in restaurant level profitability and the continued rapid growth in the number of well run First Watch restaurants.

And with that, I'll turn it over to Mel.

### **Mel Hope**

Thank you, Chris, and good morning everybody. We're pleased to report strong second quarter profits. We are controlling the controllables, and as a result, our teams continue to generate higher restaurant level operating profit margin and improved adjusted EBITDA margin. Total second quarter revenues were \$258.6 million, an increase of 19.5%. Our top line growth in the second quarter was driven by our new restaurant openings and the franchise restaurants we acquired over the past year.

Same restaurant sales slipped 30 basis points on negative same restaurant traffic of 4%. Our food and beverage costs were 21.8% of sales in the second quarter, compared to 22.4% in the same period last year. As a percent of sales, costs benefited from carried pricing of 3.5% and positive mix partially offset by commodity inflation of 4.2%.

During the quarter, restaurant level labor inflation was 4.6%. Nevertheless, labor and other related expenses were 32.8% of sales in the second quarter, a 40 basis point improvement from 33.2% in the second quarter of 2023. The improvement in labor efficiency illustrates the success of our operators who have also been building on our reputation for great service.

For the quarter, our customer experience scores have strengthened by roughly 10% versus last year. In short, and in the spirit of controlling what we can control, our restaurants continue to successfully serve our customers more efficiently, at the same time, our customers are reporting that our service is even better. The improvements in food and labor helped lift restaurant level operating profit margin by 100 basis points versus the prior year and income from operations margins by 110 basis points.

General and administrative expenses were \$27.2 million, approximately \$1.9 million higher than in the prior year, primarily due to additional headcount. G&A expenses were actually lower than the first quarter of 2024 and at 10.5% of sales they were 120 basis points lower than last year.

Adjusted EBITDA was \$35.3 million, a \$9.5 million increase versus the \$25.8 million reported last year. We're pleased to report this significant year-over-year growth in adjusted EBITDA as we continue to open and acquire restaurants in the execution of our strategic long-term growth plan.

Adjusted EBITDA margin was 13.7% versus the 11.9% margin we realized in the second quarter of 2023. The improvement was primarily attributable to the increase in restaurant level operating profit margin we discussed, as well as lower general and administrative expenses as a percent of sales.

Net income was \$8.9 million and net income margin was 3.4%. We opened seven new system-wide restaurants during the second quarter, of which six are company-owned and one is franchise-owned. So at the end of the second quarter, the First Watch system has now grown to 538 restaurants.

For your financial modeling purposes, the net effect of acquisitions, which includes only the impact of purchases made within the last 12 months, increased both second quarter revenue by about \$21 million and adjusted EBITDA by about \$5 million. For further details on the second quarter, please review our supplemental materials deck on our Investor Relations website beneath the webcast link.

Again, we're proud of our restaurant teams who have continued to improve the experience in our restaurants while delivering strong profitability. To provide you with more insight on our planning for the rest of the year, third quarter to date same restaurant traffic growth has been below our second quarter results, and we're anticipating the second half of the year to be at least as challenging as the first half. We took about 1% of additional price, the last week of June and so will carry about 3.5% of price in the third quarter.

Furthermore, our third-party off-prem channel remains volatile and we expect it to continue to weigh on our overall traffic for the balance of the year. To update our full year outlook for 2024, we are adjusting same restaurant sales growth to a range of negative 2% to flat, with a mid-single-digit decline in same restaurant traffic. We expect a total of 52 to 56 net new system-wide restaurants updated to reflect 45 to 48 company-owned restaurants, 9 to 10 franchise-owned restaurants and the two system-wide closures.

Our 2024 development pipeline remains heavily weighted in the second half of the year, the fourth quarter in particular similar to our cadence in 2023. We now expect a blended tax rate between 31% and 33%. The outperformance of our non-comp restaurants is largely offsetting our negative same restaurant sales growth, and as such, we're maintaining our total revenue growth guidance in a range of 17% to 19%, excluding the impact of the 53rd week last year, approximately 7% of the growth is expected to be the net contribution from the 23 restaurants we acquired in 2023 and the 22 restaurants acquired in 2024.

We're also maintaining the adjusted EBITDA guidance range of \$106 million to \$112 million. The net impact from acquisitions is now expected to contribute about \$13 million to current year adjusted EBITDA. Our expectation of commodity inflation for the year remains unchanged at 2% to 4%, as does our expected restaurant level labor cost inflation in the range of 5% to 7%. Finally, we continue to plan capital expenditures of \$125 million to \$135 million, not including the capital invested in the franchise acquisitions.

And with that operator, would you please open the line for the questions?

## **Question-and-Answer Session**

### **Operator**

Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] The first question comes from the line of Chris O'Cull with Stifel. Please go ahead.

### **Patrick Johnson**

Great. Thanks, guys. This is Patrick on for Chris. Good morning.

### **Chris Tomasso**

Good morning, Patrick.

### **Patrick Johnson**

Morning. I know you guys called out last quarter that Florida was a region of weakness for the system. And I'm curious if you've seen that remain the same and if there's been a change when you look geographically across any other regions of the country that you have a relatively good penetration in.

### **Chris Tomasso**



Yes. We saw the gap between Florida and the rest of the system widen a little bit, again, but our position hasn't changed. I mean, we still see that as a normalization of trends in the state kind of coming out of COVID and normalizing, but we're still all in on Florida from a growth perspective. I mean, Florida is still one of the top states for net migration in the U.S. And we continue to see it as an excellent opportunity for us to continue to operate and grow there. And still with the tourist destination aspect of it, we just – we believe that – the presence that we have in Florida is strong and we'll continue to focus on it.

### **Mel Hope**

And we don't have any other regions of the country that we'd call out as being weaker than the rest of the – our development process is really data driven. And so our – when we select a site, the success of the site really performs pretty predictably within a narrow band.

### **Patrick Johnson**

Got it. That's helpful. And then, Chris, I know the company utilizes digital channels to drive greater frequency among current users, and you called some of that out in your prepared remarks. But I was curious how you're thinking more about what you might call top of the funnel tactics that you can deploy from a marketing perspective that maybe can help reach consumers who have never used First Watch.

### **Chris Tomasso**

Yes. I think we look at and segment the consumer based on, obviously, demographics, psychographics, but probably more importantly, the frequency. And we do have a focus on all the channels that I mentioned on the call. So our infrequent users, lapse users, and even users of competitors, so – and we're doing that, again, what we're just calling the First Watch way, which is through the owned channels that we have and then through social and digital.

### **Patrick Johnson**

Helpful. Thanks, guys.

### **Chris Tomasso**

You're welcome.

### **Operator**

Thank you. Next question comes from the line of Brian M. Vaccaro with Raymond James. Please go ahead.

**Brian M. Vaccaro**

Hi. Thanks and good morning. Back on the sales, I was also curious to what degree you think maybe return to office dynamics could be impacting your business. Could you elaborate on what you're seeing weekday versus weekend? Or are there any other data dynamics that you analyze to try to answer that questions?

**Chris Tomasso**

Yes. We don't have any data that suggests that it's due to return to work. We do know that the weekday occasion is the – weekday lunch specifically is where we're seeing the most softness, weekday breakfast and weekday lunch. And so we just think it's maybe a factor of the consumer just choosing to treat that occasion as one that they can have at home or something like that in this environment. Again, we didn't see any check management steps prior to what we're seeing in the traffic pressure. So we believe it's actually a – and then when we look at industry data, we also see that those day parts are down across full service QSR and whatnot. So that kind of leads us more, Brian, towards hypothesis that it's the occasion.

**Brian M. Vaccaro**

All right, that's helpful. Thanks, Chris. And on the labor front, another quarter of solid cost controls evident in your Q2 results. Could you just remind us what some of the new tools and processes you've deployed and any benchmarks or data points you could provide on the efficiencies that that's driving in your restaurants?

**Mel Hope**

So, good morning, Brian, by the way. The tools that we created, really, last year and have rolled out in the system continue to improve, basically help the managers in the restaurant actually see their kind of real time labor costs, which helps them with scheduling and staffing during weekdays and during their peak hours. They also have just better hourly management, I would say, in terms of labor and better scheduling.

They're also successful in more throughput during our peak hours, which makes our labor look a little bit better. I don't have any metrics that I can give you or to share with you, but it's really just the attention to the management of the restaurant, the scheduling, and the labor management that our operators have been attentive to as they learn to use the new tools and apply some of the strengths of those.

**Chris Tomasso**

And then, Brian, I'll add that we – just to give you an example, we had been testing a digital scheduling platform, and the test went extremely well. And we're rolling it out here in Q3 – excuse me, in Q3. And that's a typical platform where the servers can look at their schedules, actually, all employees can look at their schedules. They're a lot – they can trade schedules on their trade shifts, things like that, things that we had to do very manually and, frankly, through the manager before. So this will again, improve our efficiency and free up the manager to focus on other things.

**Mel Hope**

And make it easier for the crews.

**Chris Tomasso**

Yes.

**Brian M. Vaccaro**

Okay. Well, I'll pass it along. Thank you very much.

**Chris Tomasso**

Thanks.

**Operator**

Thank you. Next question comes from the line of Andy Barish with Jefferies. Please go ahead.

**Andy Barish**

Hey, guys. Good morning. Wondering, as you kind of tease out the traffic impact, does discounting kind of in the breakfast category, some of the legacy players, obviously, that's a subject we're hearing a lot about across the restaurant industry right now. Do you think that's having a near-term impact? Are you able to kind of tease that out of what you're seeing?

**Chris Tomasso**

Andy, I'd say that we worked really hard years ago to differentiate ourselves from that segment through our brand repositioning and things like that. That's not an area that we choose to kind of operate in. What I'll tell you is that back to my comment, if we were seeing check management and things like that, and looking at our own menu pricing compared to others in our space and saw that there was something that we were – that was self inflicted, I think we would address that. But that's really not what we're seeing. It really seems to be an occasion issue right now.

So we are focused on our everyday value. What we are, what we have launched here recently is really stepping up the communications and focusing on our brand attributes and reminding people why they love First Watch so much. And so that's kind of our take there. We won't – I would say, at the discounting level, that's out there right now, that's just not something that we would do.

**Andy Barish**

Got it. And where are you on sort of seasonals? And I think last call, you may have mentioned, we've got some things that maybe mix really well, maybe a little bit lower on the price point. Is that starting to kind of work into the seasonals in the back half of the year?

**Chris Tomasso**

Yes. Well, first of all, I know everybody's excited that we're almost to pumpkin season, so we'll get there with our pumpkin pancake breakfast soon. But, yes, I mean, we had positive mix in Q2 and in Q1. And I think a lot of the favorability you're seeing on the profit line in the restaurants was a result of that. I talked about the shrimp and grits and some other items that we brought back and put on. And so that strategy has actually helped us a lot.

And then variation in mix for us, as you know, is kind of a quarter-to-quarter function because of the LTOs and the menu modifications. But there's really been no discernible change in customer behavior in mix or attachment this year. But we are able to flex up a little bit sometimes with favorites like the shrimp and grits and when the pumpkin pancake breakfast comes back.

**Andy Barish**

Got it. And then just finally, the 130 projects in the pipeline for growth, obviously that's multiple years of new unit growth, even assuming absolute level of pickup. How does that – how should we frame that versus the past? I mean, I know some new territory obviously, is now flowing into that through the franchise acquisitions, just yes, any help on that would be great.

**Chris Tomasso**

I think the point being made there is that we are on track, like we have been for many years to meet our development goals. And so that stat is really to provide some comfort that we're well on our way. That's been one of our hallmarks is the consistency of the openings and then also the outperformance of the new restaurants. So that's really what we were trying to convey there.

**Mel Hope**

Right. And we know that our 10% growth in the system, long-term guidance is a big number, and we want people to be comfortable that we're actually curating enough projects that we can fill that pipeline.

**Andy Barish**

Yes. Looking forward to a couple of those coming out of the pipeline in Massachusetts. Thanks, guys.

**Chris Tomasso**

That's right. Get ready.

**Operator**

Thank you. Next question comes from the line of Jeffrey Bernstein with Barclays. Please go ahead.

**Pratik Patel**

Hi, good morning. This is Pratik on for Jeff. Thanks for the question. I just wanted to get a sense of what you're seeing in your sales trends by income cohorts. What buckets are you seeing strength from? And where might you be seeing a little bit of softness? You did call out the weekday breakfast day part as a little bit weaker. And is that really just a function of consumers choosing food at home rather than losing traffic share? And if you can call out any particular consumer segment where you're seeing that as most prevalent. Thanks.

**Chris Tomasso**

Yes. So we talked about the lower income consumer, us seeing less visits by that group. I don't think that's very different than what you're hearing pretty much across the industry as far as a pressure point. And for us, that's defined as 70,000 household income or below. And then the only other insights I can give you that we've shared is that the infrequent customer is one that we're seeing less visits by as well, based on our credit card data analysis.

**Pratik Patel**

Got it. That's very helpful. And then I apologize, if you already gave it, but are you contemplating any potential weather impact from Debby in 3Q, is that baked into your guidance?

**Chris Tomasso**

We really had, I think yesterday, we might have had three restaurants with partial day closures, something like that. So I don't know that it's going to be all that meaningful, if that changes, we'll update.

**Mel Hope**

What we're really looking for is the mobility of the consumer right now, I can tell you, as I'm sure everybody on the call heard, where we're based, Sarasota got the worst of it. And there's a lot of folks not able to get to our office today. So whether we're open or not, we're – I think we're going to see some impacts, but we don't expect it to be significant as it relates to the whole company.

**Pratik Patel**

Got it. Thank you. Very helpful. Appreciate it.

**Operator**

Thank you. Next question comes from the line of Gregory Francfort with Guggenheim Securities. Please go ahead.

**Gregory Francfort**

Hey, good morning, guys. I had two questions. The first is just from a same-store sales perspective, I guess, as we look to the back half, what can you guys do to maybe have an impact on the comps? I mean, are you guys thinking about deploying a little bit more marketing from a calendar perspective? Is there something you can do or is this just going to be more kind of bouncing around with the industry in terms of what's going to happen?

**Chris Tomasso**

No. I think we are taking steps to, again, reach out to our consumers again, just I know I keep saying the same targets, but really focusing on our owned audiences, which as we said on the call, we've got an opt in database now of close to 7 million that we've been curating over a period of time and just really cutting that data in ways that we can be more efficient and more effective in the way we communicate with them. I'd say you'll probably start to see us increase the frequency of the communications as well with that group and then also stepping up our digital and social activity as we do that simultaneously.

**Mel Hope**

Yes, but I mean, to your question, we do not – absolutely do not bounce around with the system. I mean, we'd go straight at the audiences that, where we have the most touch and we know people are listening.

**Gregory Francfort**

I mean, just on the G&A side of things, how much of that was lower incentive comp versus belt tightening versus project timing? Just trying to think about that for the rest – the next couple quarters.

**Mel Hope**

Yes, for the most part, it's just unspooling the timing of our G&A realization for the year. I don't think the incentive comp differences were all that meaningful. And then the timing of new restaurant openings tends to drive some other costs into the back half of the year too.

**Gregory Francfort**

I said two, but maybe I'll sneak in one last one. Just can you give us an update, Mel, on where new store returns look, right now, I know you said new store AUV sounded becoming really, really strong and I think the CapEx guidance is unchanged. Just maybe the update on what those numbers look like.

**Mel Hope**

Yes. They're tracking with the unit economic model that we have in the investor deck that's attached to the – to our website.

**Gregory Francfort**

Thank you guys. Appreciate it.

**Operator**

Thank you. Next question comes from the line of Brian Mullan with Piper Sandler. Please go ahead.

**Ali Arfstrom**

Hi, this is Ali Arfstrom on for Brian Mullan. Thank you for taking the question. Wondering if you could share comp trends directionally or by month in Q2. Thanks.

**Mel Hope**

We don't typically share by month. We share by quarter. And so I can tell you that quarter-to-quarter, you have both those comps. And what we did say is exiting the quarter into the third quarter, our traffic was running somewhat below the full quarter of Q2.

**Ali Arfstrom**

Thank you.

**Operator**

Thank you. Next question comes from the line of Sara Senatore with Bank of America. Please go ahead.

**Katherine Griffin**

Hi, thank you. This is Katherine on for Sara. First, I wanted to ask just about the traffic trend in the quarter, which was sequentially stable versus the first quarter. So just curious if you can opine on what that means about the operating environment right now. It would seem to suggest that it's relatively stable.

**Chris Tomasso**

Yes, I'd agree with that.

**Katherine Griffin**



Okay. And then, yes, I guess, just another question on demand. I think given that weekend brunch generally has a lower average check than other daypart occasions in full-service broadly. So I would think that First Watch could be a beneficiary of a kind of shift in that occasion. Are you still seeing that?

**Chris Tomasso**

Yes. I think obviously for us, weekend brunch is our highest check average occasion and it's still an area where we have demand. And so I think our general commentary here is that weekends are helping to offset the softness that we're seeing during weekdays, which is why our focus has been on throughput optimization, in that we can serve more people when we have the demand rather than trying to create an occasion that maybe the consumer's not open to at this point.

So that's been our focus, and I think that's why we delivered the results we did this quarter and last quarter, because we're really, really optimized as it relates to the peak sales hours and the time when we have the most demand.

**Katherine Griffin**

Great. Thank you.

**Operator**

Thank you. Next question comes from the line of Jon Tower with Citi. Please go ahead.

**Karen Holthouse**

Hi, this is Karen Holthouse on for Jon. Thanks for taking the question. I wanted to dig a little bit into the commentary on stronger non-comp store performance. Is there anything you would point to in particular that's helping that whether that's just improving site analytics, better developer relationships, the mix of info versus new market, just anything your own data is telling you.

**Mel Hope**

Over the course of the last few years, our non-comp restaurants, new restaurants have all fairly predictably outperformed the legacy system. Some of that is because the legacy system includes a number of restaurants that might be occupied in smaller footprint and that sort of thing. And our shift to more premium real estate in about 2017 or so has served us well in terms of accommodating more interest from the customers and greater volumes.

**Karen Holthouse**

And then just on the modeling front, this is two quarters in a row now that we've seen sub 22% COGS, which is below where historically you've tracked. Is that sustainable and driven by some of the benefits of, like, alcohol in the juicing platform, or are you worried about working that number too low, that you're going to get off-sides on a value proposition for the consumer?

**Mel Hope**

Yes, not worried about it. Sometimes that number changes around when you have a heavier load of new restaurants coming on Board in the back half of the year, we might see some of the labor margins tick up a bit as we have more of a larger cohort of new restaurants who have some built in inefficiency when they first open.

But I would say, it does show the success of our operators in terms of managing their crews better. And I think if we can see that hover in the 22% area, that's something to be proud of over a long period of time.

**Karen Holthouse**

And there's one final one for me, and apologies if I missed this in the prepared remarks. The last couple of quarters you've shared, your performance versus Black Box. Do you have that for this quarter?

**Mel Hope**

We do. I think we said that we hadn't, that in terms of performance, that the Black Box data on the metrics that we measure, we're slightly below the cohort. There's a lot of participants in that group that are pressing on aggressive advertising, promotions and discounting. So there's we look closely at the traffic number, and so this would be a period where, for, relative to the casual dining category that our traffic hasn't – has not met Black Box. We do continue to take share, however, in the against the category in the second quarter. Our Placer.ai, which I know people are using more and more these days, indicates that our traffic shares increased against the direct daytime dining competitive set.

**Karen Holthouse**

Okay. Thanks. I'll pass it on from there.

**Operator**

Thank you. Next question comes from the line of Brian M. Vaccaro with Raymond James. Please go ahead.

**Brian M. Vaccaro**

Hi, thanks for the quick follow-up. I just wanted to circle back on the second half guidance and could you elaborate on some of the assumptions you embedded on both sales and margins? You mentioned the software quarter-to-date. Many have seen that in the industry as well. Did you assume that continues? Or maybe there were some calendar or other seasonal factors impacting July and really on the margins as well.

I understand you have less pricing, but following the very strong Q2 EBITDA performance, just curious kind of what some of the margin dynamics that could be different in second half versus first half. Thanks very much.

**Mel Hope**

Yes. For the back half of the year, I've already alluded to the fact that as we bring on, we've got a great deal of new restaurant openings that are calendared to enter the mix in the back half of the year. And as I mentioned earlier, that their immature margins can sometimes affect the overall margins of the company.

We also have heavy up on expenses that occur in the back half of the year. Our fourth quarter, for example, we have our national conference and some of those more seasonal type things. And there's a sort of a natural tendency to make sure that we onboard staff and complete projects before the end of the year. So there's a tendency, sort of call it human nature, that we tend to experience an uptick in our G&A expense during the fourth quarter. So those are kind of some of the seasonal kind of items.

**Brian M. Vaccaro**

Thank you.

**Operator**

Thank you. Ladies and gentlemen, we have reached the end of question-and-answer session. I would now like to turn the floor over to Christopher Tomasso for closing comments.

## Chris Tomasso

I want to personally thank our teams for their efforts in this and every quarter with a special shout out to our operations leaders for the exceptional results they delivered in these interesting times. And while I'm proud of what we accomplished, I'm even prouder of how we did it. We're guided by our You First philosophy. It's at our core and it defines who we are. Our achievements have been and our future growth is underpinned by standing shoulder to shoulder, rolling up our sleeves, putting others first and being kind. Thanks everybody for your time today.

## Operator

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.

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