RESTAURANT FINANCE MONITOR®

Volume 29, Number 8 • Restaurant Finance Monitor, 2808 Anthony Lane South, Minneapolis, MN 55418 • ISSN #1061-382X

August 20, 2018

What Do the Lists Tell Us About the Restaurant Industry

By Dennis Monroe

I have been studying a number of the restaurant industry rankings that come out this time of year and gleaning what they tell us about the current and future state of the industry.

Let's start with the Restaurant Finance Monitor's annual ranking of the Top 200 franchisees.

First, what struck me as interesting is that out of the top 20 franchisees, very few of these large multi-unit operators have a concentration in fast casual concepts. The exceptions are various investments in Panera and, to a lesser degree, La Madeleine. Clear in the top 20 is that most of the action still seems to be in quick-serve restaurants. This stat does run counter to the overall growth trajectory of fast casual in the industry.

Speaking of the top 20 companies in the Monitor 200 ranking, casual dining has obviously dipped in the number of units held by the operators. For example, the Flynn Restaurant Group operates 11 fewer Applebee's then it did in 2017. This is symptomatic of Applebee's overall decline. Even IHOP, another Dine Global Brands concept, has had some reduction in units operated by the top 200 franchisees.

Interestingly, and again probably at odds with the current trends, 33 of the top 100 companies in the Monitor 200 ranking this year were single-concept operators, approximately the same as last year.

Additionally, out of the top 50 companies on the list, 16 were YUM! franchisees, versus 18 last year. And while I'm on the subject of the top 50 companies: Wendy's seems to have taken the lead in that group over Burger King.

Moving on from the large franchise operators, as reflected in the Monitor 200, to the general restaurant industry: The segment that seems to be the hottest in terms of both growth in sales and number of units is the quick-pizza segment, with MOD and Blaze being the dominant forces.

Even more traditional pizza concepts like Marco's Pizza seem to be doing well. All three concepts are focused on a single type of fare. Other similarly focused concepts, the chicken-fingers maker Raising Cane's and breakfast purveyor First Watch, have shown tremendous growth. Clearly, what we can glean from these lists is that focused concepts seem to generate high growth and returns.

In the sandwich sector, the smaller rivals are certainly gaining ground over the Subway giant, which still shows unit expansion, but has slowed down markedly of late. A number of the sandwich competitors, particularly Jersey Mike's, are displaying reasonable growth.

I've made a couple of other observations from reviewing the Top 200 rankings. Chick Fil-A continues to be a concept with huge growth and consumer appeal, but those of course are run by single-unit operators.

I was surprised by the signs of resurgence on the part of Darden's Bahama Breeze and Bloomin' Brand's Outback, both of which are older concepts, and that of Chipotle, which had a very poor 2017, and is now rebounding. And, look at McDonald's: Things are picking up after slow results last year.

What trends may we infer from reviewing all of these rankings?

1. I think EBITDA multiples in casual dining are going to continue to go down, since there have been more dispositions than acquisitions. There may be an opportunity for someone to make acquisitions in the casual dining sector at these lower prices.

2. While large franchisees are typically not choosing fast casual concepts, it is still a place where most of the industry expansion is in terms of sales and unit growth.

3. Quick-serve restaurants are still attractive, particularly the concepts that are doing well, like those in the burger sector. It's in the more traditional sectors like that where multiples will continue to stay strong.

4. Some of the more specialized concepts that have what I would consider unique, but a little more narrow niche,

such as Raising Cane and Marco's, have produced great growth. The lesson their success teaches us is that if you do something really well, and keep doing it, then consumer will respond —and so will franchise sales.

Dennis Monroe is shareholder and chairman of Monroe Moxness Berg, a law firm specializing in multi-unit restaurant finance, M&A and taxation. Dennis and his partner John Berg will be conducting a pre-conference workshop for multi-unit restaurant operators at this year's Restaurant Finance & Development Conference on Monday, November 12. The topic is Tax-Efficient Structures After the Tax Cuts and Jobs Act of 2017. In the meantime, you can reach Dennis at 952-885-5999 or by email at dmonroe@mmblaw.com.