

Restaurants Industry

Commodities update: cont'd deflation ex-sugar, coffee; beef now expected lower

Industry Overview

Deflation cont'd in 4Q; sugar, cattle, coffee inflationary

The fourth quarter of the year saw meaningful deflation for natural gas (-44.6%), wheat (-29.4%), corn (-22.4%) and soybean oil (-18.4%). Sugar saw the highest y/y inflation of 41.3%. Beef prices saw disinflation, at 4.2% vs 17.3% in 3Q while coffee turned inflationary from -24.7% in 3Q to 6.5%.

Expect disinflation in 1Q for sugar, coffee; cattle stable

Futures forecast continued deflation in 1Q24 for most commodities; greatest declines are forecasted for wheat (-24.4%), corn (-24.2%) and dairy (CME cheese -13.6%, CME milk -11.3%). Sugar and coffee are expected to increase 8.8% and 2.6% respectively, indicating a slowdown in y/y inflation from 41.3% and 6.5% y/y in 4Q. Notably, cattle prices expectations have moved from inflationary to stable (+0.1% y/y). Natural gas, oil prices are forecasted to decline y/y.

Vs. Oct, price expectations mostly lower; best for pizza

Expectations for 1Q24 commodities prices have been largely lower compared to 3 months ago. Expectations have fallen significantly for cheese (-14.9%), milk (-14.0%), sugar (-12.1%), soybean oil (-10.2%), and corn (-8.8%). Expectations for cattle prices have fallen (-3.4%). Exceptions to the trend are coffee and wheat, which have seen expectations rise 15.0% and 2.9% respectively. Versus 3 months ago, expectations have fallen meaningfully for gas prices (-30.0%) and oil (-9.1%).

Proteins: Egg deflation; chicken and beef elevated

Retail egg price y/y growth has continued to decline from its Jan 2023 peak. In 4Q23, prices declined -40%, and declined -48% in Jan 2024. Chicken breast price growth has reaccelerated after its most recent trough of 0% in Nov 2023 to 15% y/y in Jan 2024. Chicken wing price y/y growth began to reaccelerate in 2H23 and was stable in January vs December at 83%. Beef prices continue to see y/y inflation and have accelerated in January.

Baskets and contracts determine exposure

Animal proteins (beef and chicken) account for the largest share of input costs for most restaurants (ex dessert, coffee, pizza), generally accounting for 25-35%+ of COGS. In our coverage, TXRH and PTLO are at the high end of the range and restaurants with big breakfast mix (FWRG, MCD, and CBRL) at the low end. Because of contracts, however, P&L impact tends to lag by ~2 quarters (contracts can be as long as a year).

Restaurants have historically priced for food inflation

Food inflation is closely correlated with industry SSSG because: 1) consumers tend to benchmark against FAH (eating at home is always less expensive in absolute, but relative matters); and 2) as the marginal cost, food prices dictate prices.

06 February 2024

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Restaurants

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Glossary:

DD – double digit
HSD – high single digit
NTM – next twelve months
COGS – cost of goods sold
FWRG – First Watch
PTLO – Portillo's
TXRH – Texas Roadhouse
MCD – McDonald's
CBRL – Cracker Barrel
WEN – Wendy's

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Timestamp: 06 February 2024 05:00AM EST

Deflation cont'd in 4Q; sugar, cattle, coffee inflationary

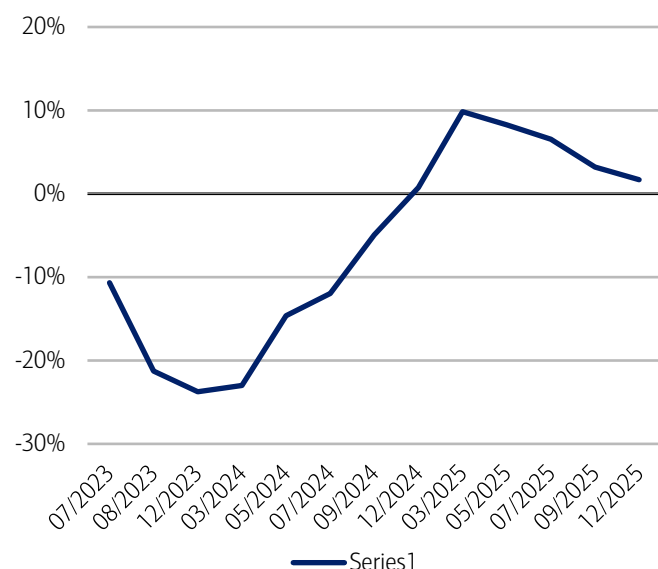
The fourth quarter of the year saw meaningful deflation for natural gas (-44.6%), wheat (-29.4%), corn (-22.4%) and soybean oil (-18.4%). Sugar saw the highest y/y inflation of 41.3%. Beef prices saw disinflation, at 4.2% vs 17.3% in 3Q while coffee turned inflationary from -24.7% in 3Q to 6.5%.

Expect disinflation in 1Q for sugar, coffee; cattle stable

Futures forecast continued deflation in 1Q24 for most commodities; greatest declines are forecasted for wheat (-24.4%), corn (-24.2%) and dairy (CME cheese -13.6%, CME milk -11.3%). Sugar and coffee are expected to increase 8.8% and 2.6% respectively, indicating a slowdown in y/y inflation from 41.3% and 6.5% y/y in 4Q. Notably, cattle prices expectations have moved from inflationary to stable (+0.1% y/y). Nat. gas, oil prices are forecasted to decline y/y.

Exhibit 1: For 1Q24, average corn price inflation is expected to be -24.2%

Corn futures y/y change

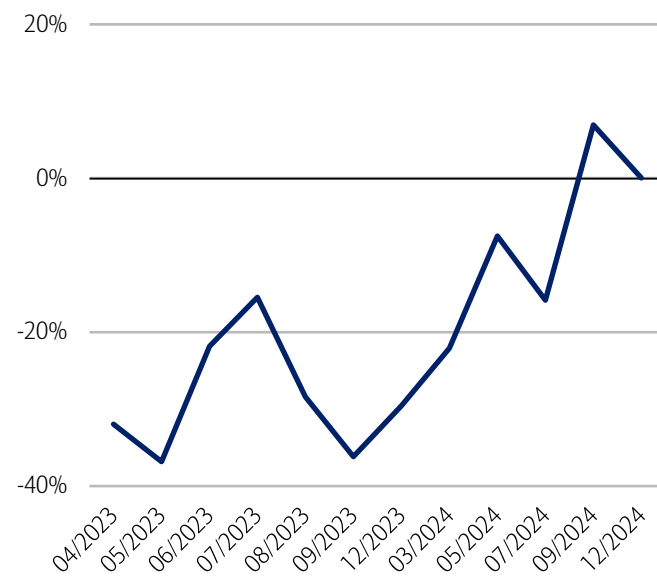


Source: Bloomberg

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Exhibit 2: For 1Q24, average wheat price inflation is expected to be -24.4%

Wheat futures y/y change

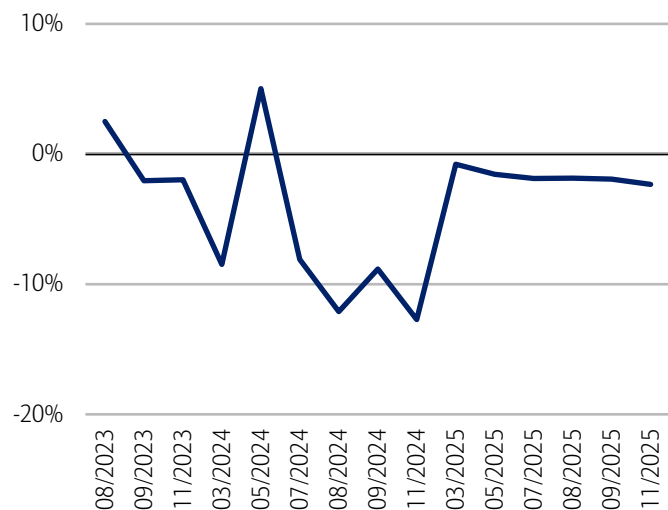


Source: Bloomberg

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Exhibit 3: For 1Q24, average soybean price inflation is expected to be -10.1%

Soybean futures y/y change

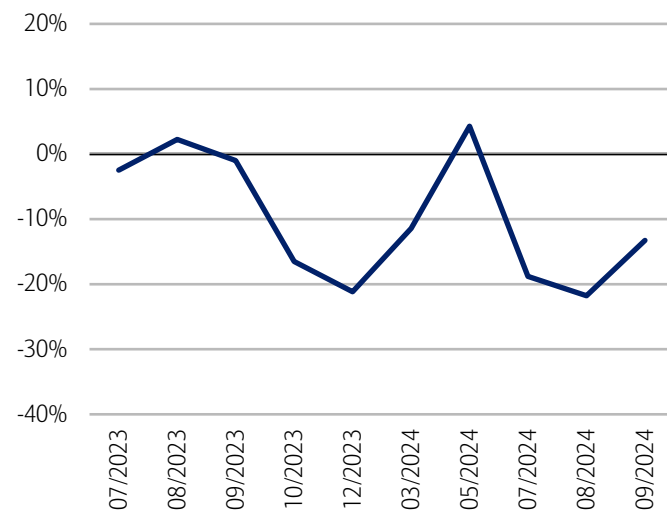


Source: Bloomberg

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Exhibit 4: For 1Q24, average soybean oil price inflation is expected to be -16.0%

Soybean oil futures y/y change

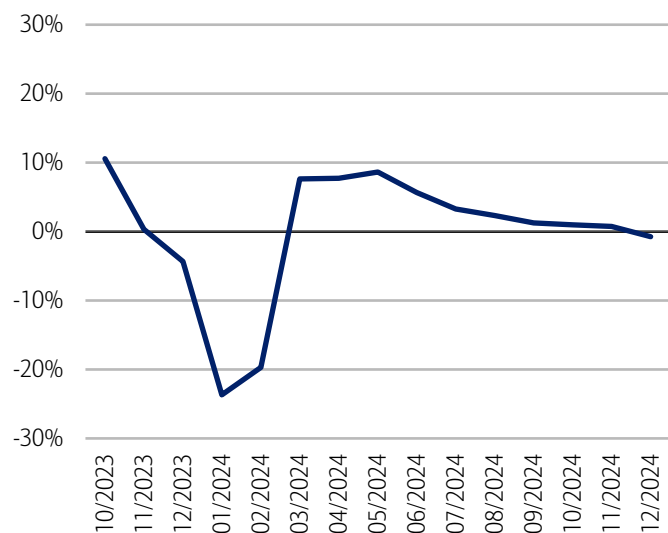


Source: Bloomberg

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Exhibit 5: For 1Q24, average CME cheese price inflation is expected to be -13.6%

Cheese futures y/y change



Source: Bloomberg

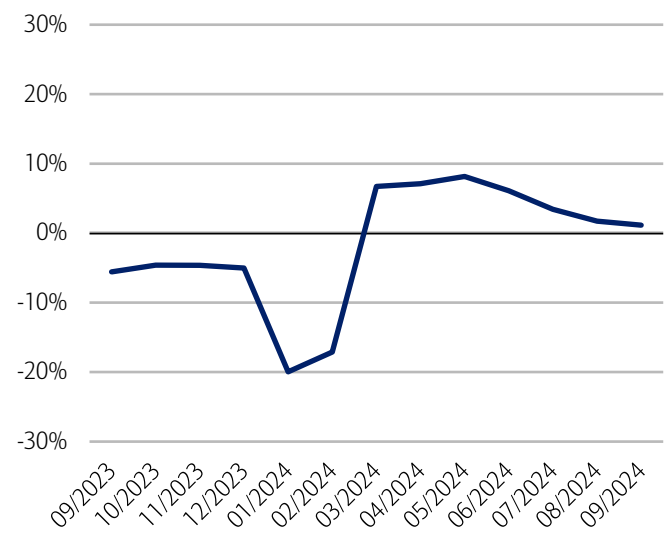
CME- Chicago Mercantile Exchange

USDA monthly weighted avg price uses both 40lb cheddar block and 500lb barrel prices

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Exhibit 6: For 1Q24, average CME milk price inflation is expected to be -11.3%

Class III Milk futures y/y change



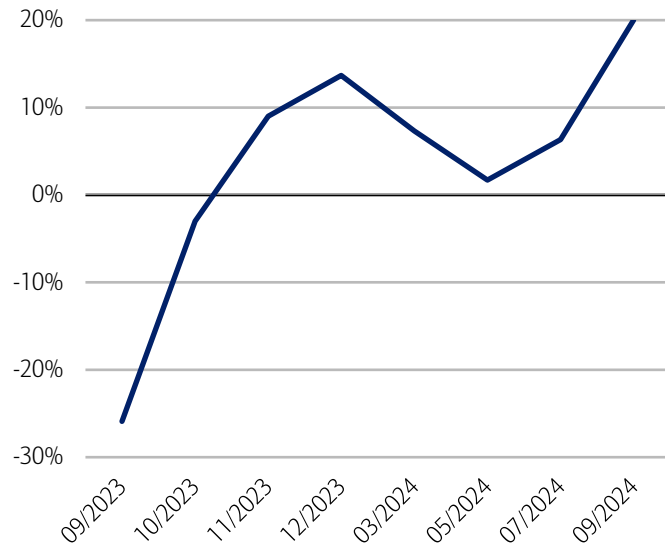
Source: Bloomberg

Class III Milk is typically used for cheese manufacturing

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Exhibit 7: For 1Q24, average coffee price inflation is expected to be 2.6%

Coffee futures y/y change

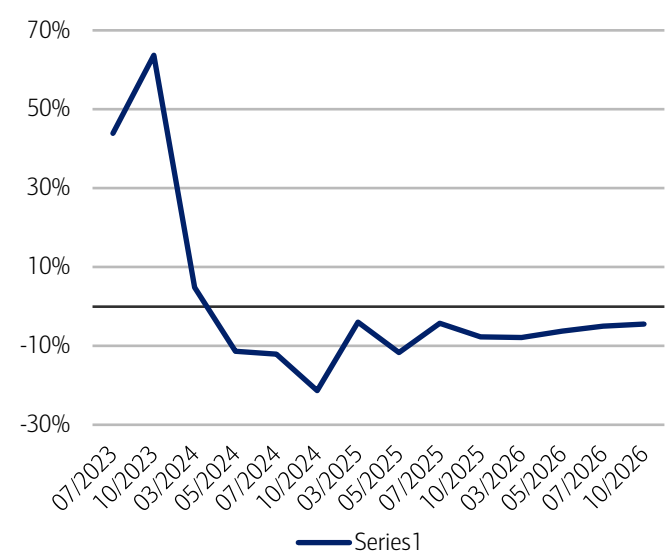


Source: Bloomberg

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Exhibit 8: For 1Q24, average sugar price inflation is expected to be 8.8%

Sugar futures y/y change

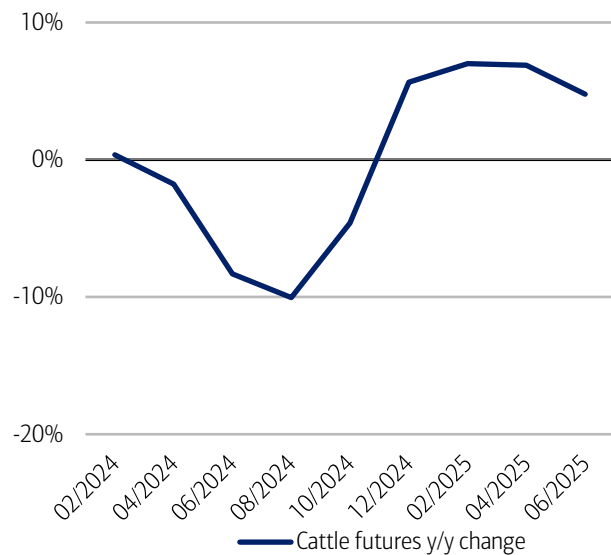


Source: Bloomberg

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Exhibit 9: For 1Q24, average cattle price inflation is expected to be 0.1%

Cattle futures y/y change

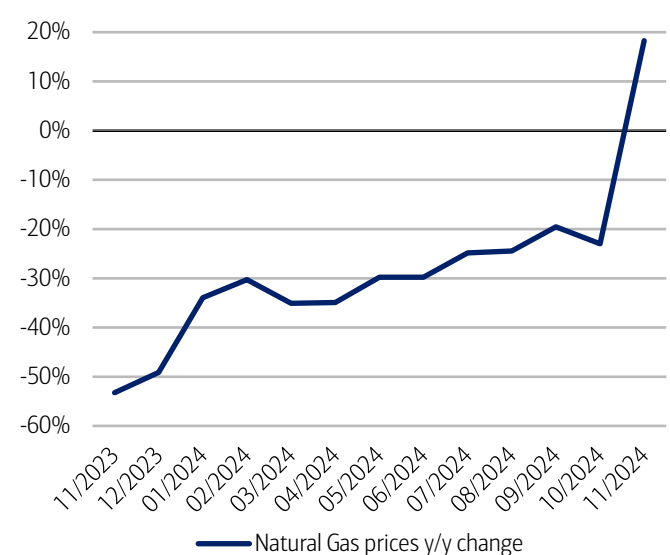


Source: Bloomberg

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Exhibit 10: For 1Q24, average natural gas price inflation is expected to be -32.3%

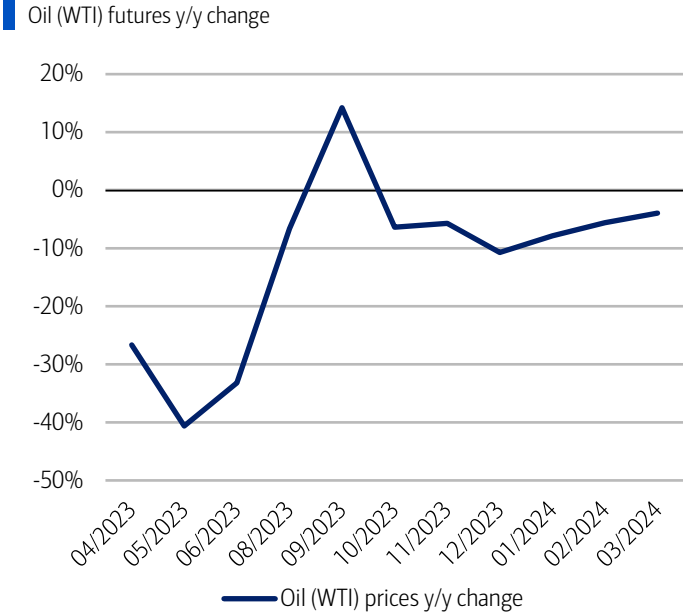
Natural gas futures y/y change



Source: Bloomberg

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Exhibit 11: For 1Q24, average oil (WTI) price inflation is expected to be -5.8%



Source: Bloomberg

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Exhibit 12: We expect to see cattle, coffee and natural gas price inflation in the next twelve months from November while other commodities deflate

One year forward inflation rate

Cattle	Coffee	Wheat	Soybean Oil	Corn	Soybeans	Natural Gas
May-23 11.0%	2.9%	-13.1%	-26.6%	-21.6%	-17.7%	-37.6%
Aug-23 13.8%	-7.3%	-5.2%	-5.0%	-21.3%	-8.0%	-7.8%
Nov-23 2.6%	4.1%	-3.4%	-19.0%	-15.3%	-7.2%	16.4%

Source: BofA Global Research, Bloomberg

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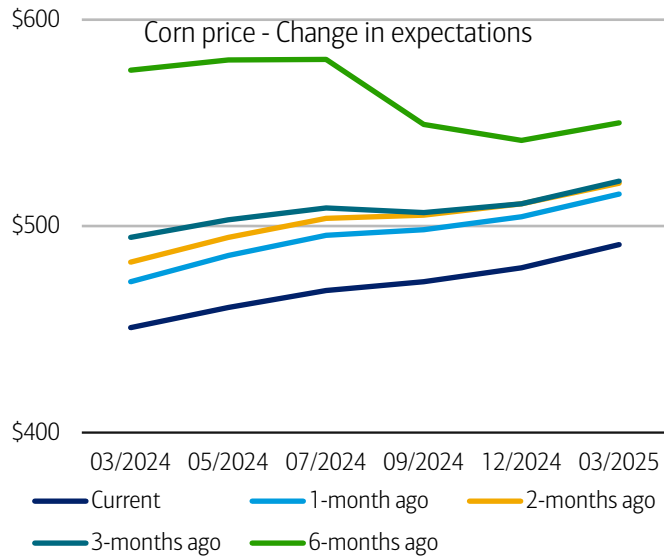
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Expectations for 1Q24 commodities prices have been largely lower compared to 3 months ago. Expectations have fallen significantly for cheese (-14.9%), milk (-14.0%), sugar (-12.1%), soybean oil (-10.2%), and corn (-8.8%). Expectations for cattle prices have fallen (-3.4%). Exceptions to the trend are coffee and wheat, which have seen expectations rise 15.0% and 2.9% respectively. Versus 3 months ago, expectations have fallen meaningfully for gas prices (-30.0%) and oil (-9.1%).



Exhibit 13: Near-term corn price expectations are lower than 1, 2, 3 and 6 months ago

Corn futures – Change in expectations

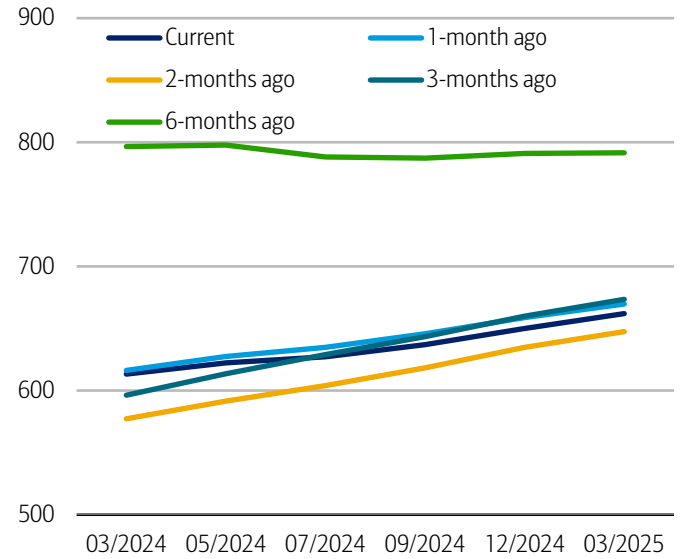


Source: Bloomberg

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Exhibit 14: Wheat price expectations are higher than 1, 2, 3, and 6 months ago

Wheat futures – Change in expectations

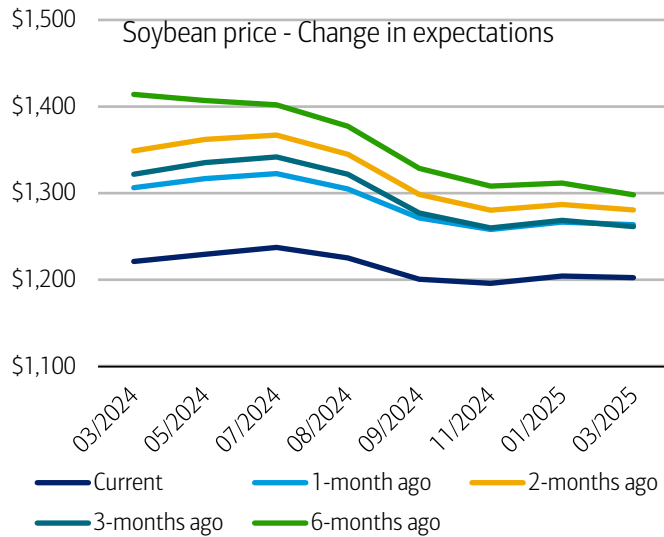


Source: Bloomberg

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Exhibit 15: Near-term soybean price expectations are lower than 1, 2, 3, and 6 months ago

Soybean futures – Change in expectations

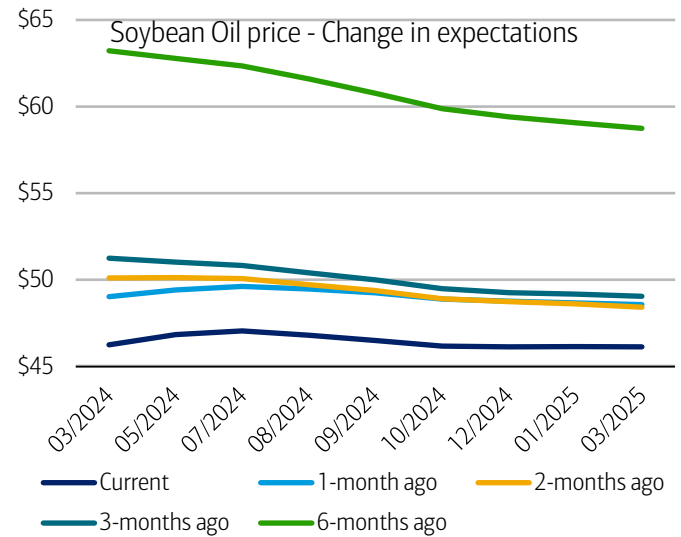


Source: Bloomberg

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Exhibit 16: Soybean Oil price expectations are lower than 1, 2, 3, and 6 months ago

Soybean Oil futures – Change in expectations

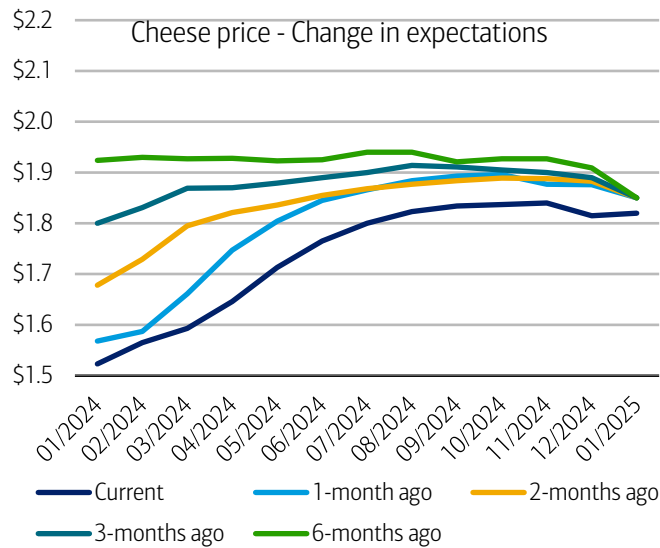


Source: Bloomberg

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Exhibit 17: Cheese price expectations are lower than 1, 2, 3, and 6 months ago

Cheese futures – Change in expectations

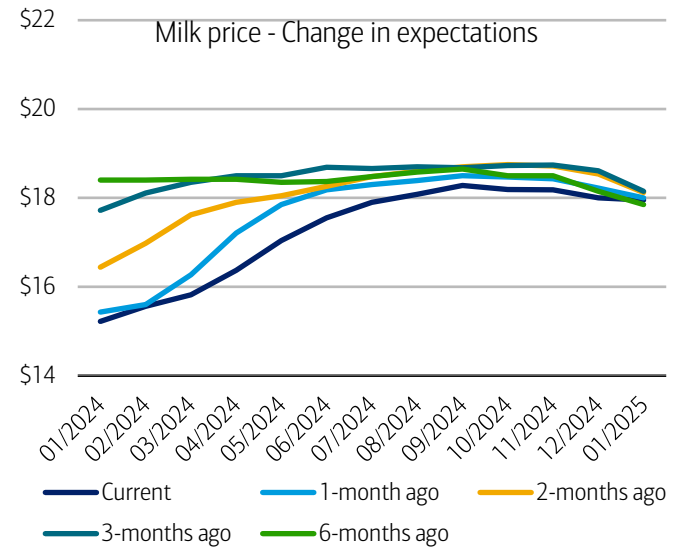


Source: Bloomberg

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Exhibit 18: Milk price expectations are lower than 1, 2, 3, and 6 months ago

Milk futures – Change in expectations

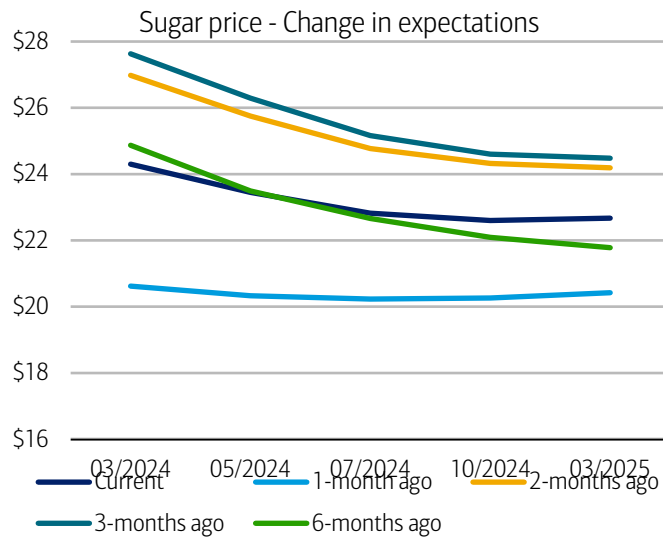


Source: Bloomberg

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Exhibit 19: Near-term sugar price expectations are higher than 1 month ago but lower than 2,3, and 6 months ago

Sugar futures – Change in expectations

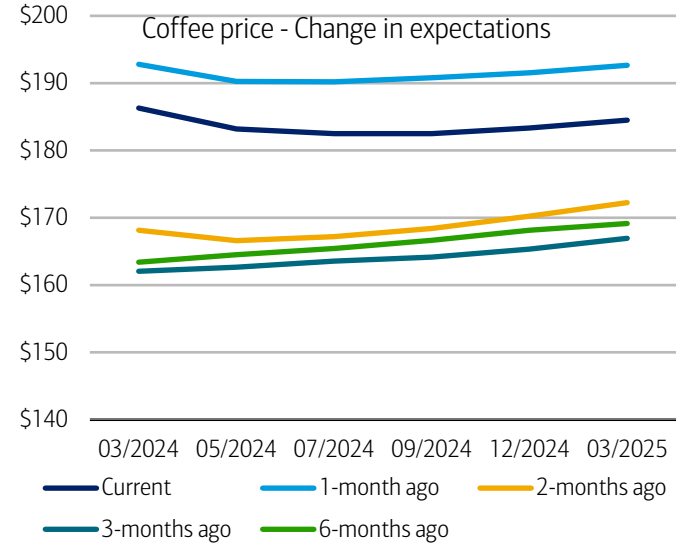


Source: Bloomberg

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Exhibit 20: Coffee price expectations are lower than 1 month ago but higher than 2, 3, and 6 months

Coffee futures – Change in expectations



Source: Bloomberg

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Exhibit 21: Natural gas price expectations are in-line with 1 month ago and lower than 2, 3, and 6 months ago

Natural gas futures – Change in expectations

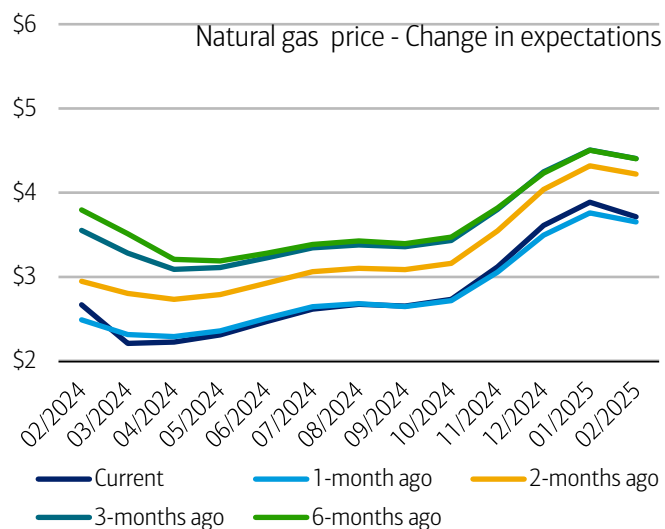
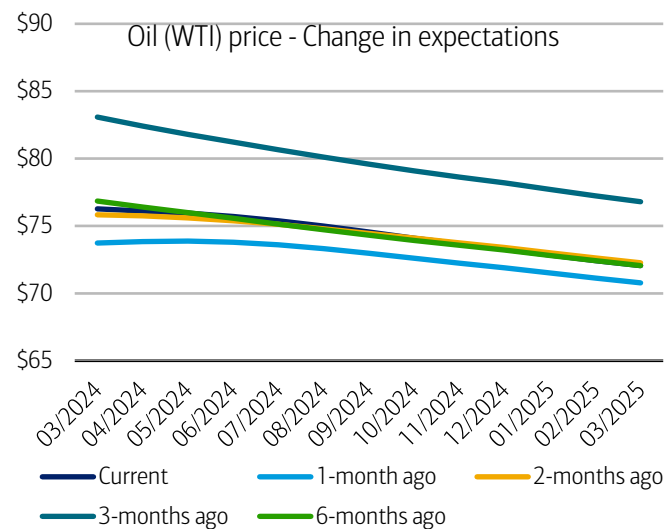


Exhibit 22: Near-term oil price expectations are higher than 1 month ago, lower than 3 months ago, and in-line with 2 and 6 months ago

Oil futures – Change in expectations



Proteins: Egg deflation; chicken and beef elevated

Retail egg price y/y growth has continued to decline from its Jan 2023 peak. In 4Q23, prices declined -40%, and declined -48% in Jan 2024. Chicken breast price growth has reaccelerated after its most recent trough of 0% in Nov 2023 to 15% y/y in Jan 2024. Chicken wing price y/y growth began to reaccelerate in 2H23 and was stable in January vs December at 83%. Beef prices continue to see y/y inflation and have accelerated in January.

Exhibit 23: Egg prices continue to decline y/y

USDA Eggs Grade A Retail Price USD/dozen – Y/Y growth %

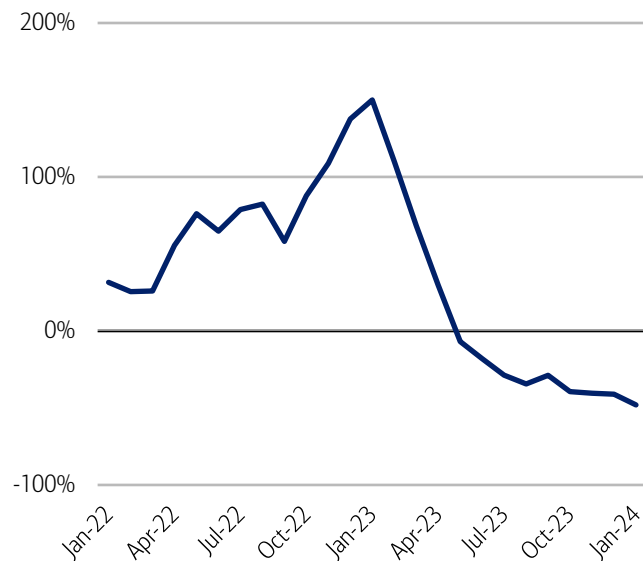


Exhibit 24: Chicken breast prices have increased y/y since Nov 2023

USDA Northeast Broiler Fryer Breast B/S Weighted Avg Spot USD/lb – Y/Y growth %

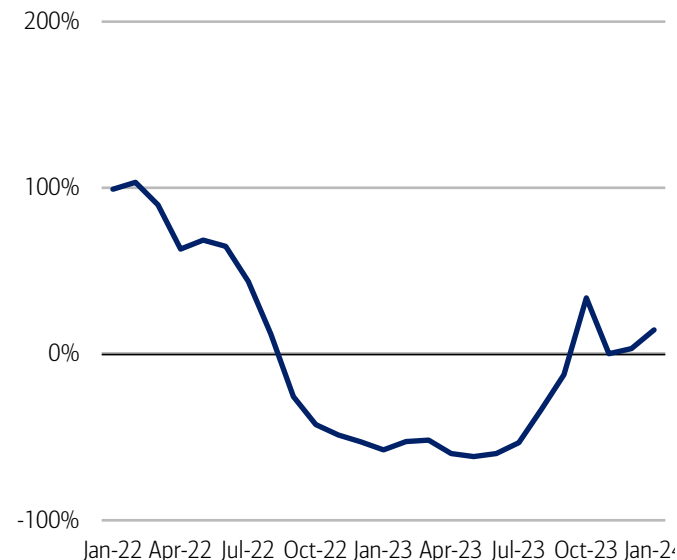
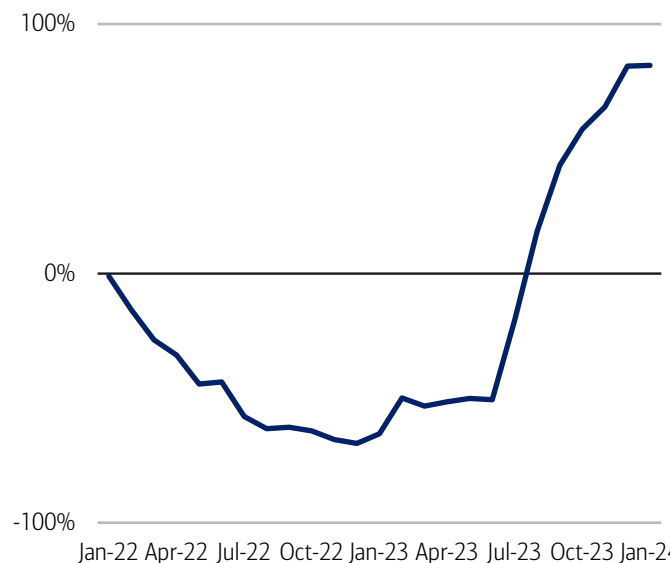


Exhibit 25: Chicken wing prices troughed at the end of 2022, recent y/y prices have been elevated

USDA Northeast Broiler Fryer Wings Whole Weighted Avg Spot USD/lb – Y/Y growth %

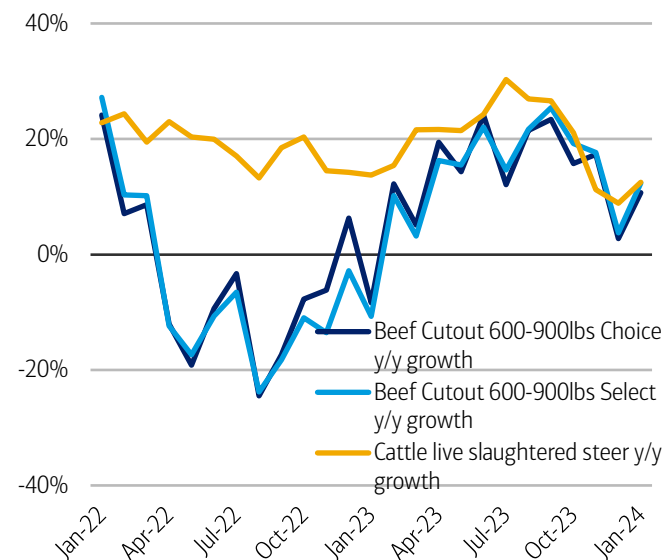


Source: Bloomberg

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Exhibit 26: Beef continues to see y/y inflation

USDA Beef Prices – Y/Y growth %



Source: Bloomberg

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Baskets and contracts determine exposure

Animal proteins (beef and chicken) account for the largest share of input costs for most restaurants (ex dessert, coffee, pizza), generally accounting for 25-35%+ of COGS. In our coverage, TXRH and PTLO are at the high end of the range and restaurants with big breakfast mix (FWRG, MCD, and CBRL) at the low end. Because of contracts, however, P&L impact tends to lag by ~2 quarters (contracts can be as long as a year).

Exhibit 30: The significant breakfast business for the full service restaurants in our coverage mitigate their protein exposures

Company commodity baskets (inputs as % of COGS)

	QSR						Coffee/Treats	
	MCD	QSR	WEN	YUM	DPZ	SBUX	BROS	DNUT
Beef	15%	15%	20%	20%	10%		0%	
Chicken	15%	15%	20%	20%	15%		0%	
Dairy	10%			15%	30%	10%	23%	
Eggs	8%		7%		0%	2%	0%	
Coffee	6%				0%	18%	11%	8%
Wheat					20%	3%		20%

Source: Company filings, BofA Global Research estimates

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Exhibit 31: The significant breakfast business for the full service restaurants in our coverage mitigate their protein exposures

Company commodity baskets (inputs as % of COGS)

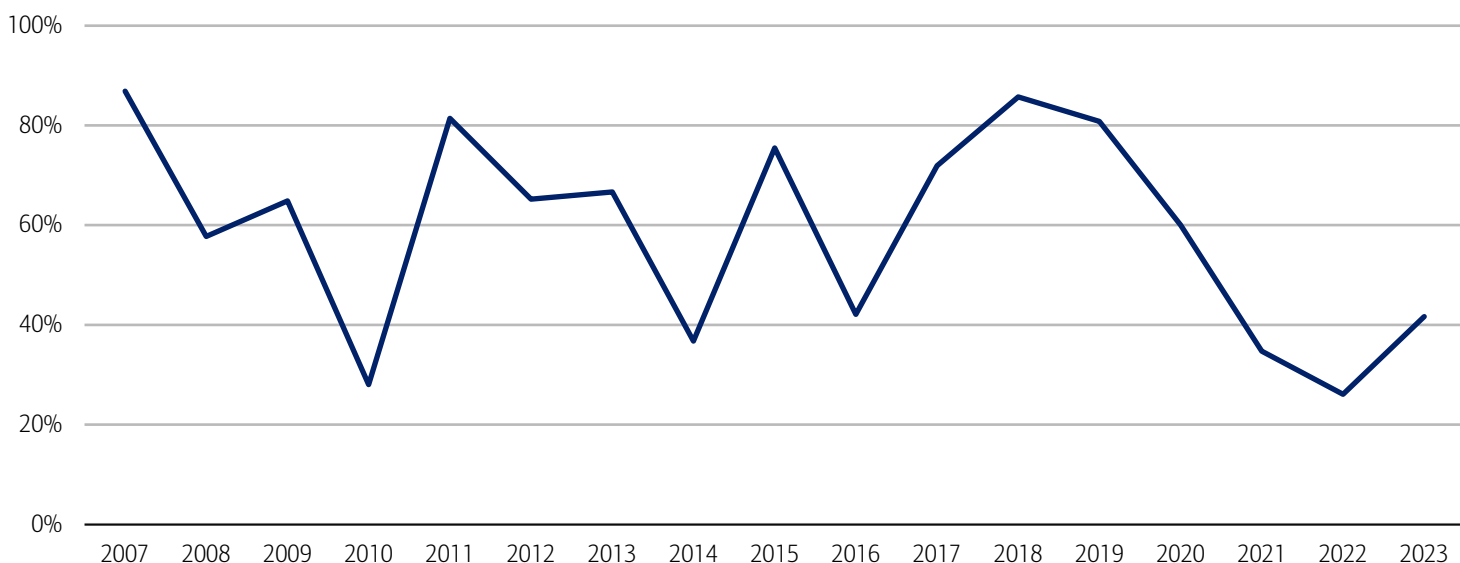
	Fast Casual					Casual Dining				
	PTLO	CMG	SG	SHAK	FWRG	CBRL	EAT	DRI	TXRH	
Beef	28%	20%	0%	28%	11%	14%	18%	22%	48%	
Chicken	8%	10%	20%		11%	11%	18%	8%	15%	
Dairy	8%				10%	6%		10%	8%	
Eggs					10%	6%				
Coffee	1%				4%	4%				
Wheat	0%				6%	6%		7%		
Produce							18%	12%	8%	
Bread mixes, oils									8%	
Beans		5%								
Avocado		9%	9%							
Cheese		5%								
Pork		2%								
Seafood								9%		
Non-Perishable / Other								32%		

Source: Company filings, BofA Global Research estimates

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Exhibit 29: Starbucks fixed price contracts have been lowest when coffee prices are highest, as coffee prices come down, we expect the share of fixed price contracts to increase

SBUX fixed price contracts share of total inventories



Source: Company reports

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SBUX fixed price contracts share of total inventories

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Food inflation is closely correlated with industry SSSG because: 1) consumers tend to benchmark against FAH (eating at home is always less expensive in absolute, but relative matters); and 2) as the marginal cost, food prices dictate prices.

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Underperform	N/A	≥ 20%

^{R1} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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