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Darden Restaurants, Inc. (DRI)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Darden Fiscal Year 2022 Third Quarter Earnings Call. Your lines have been placed on listen-only until the question-and-answer session. [Operator Instructions] The conference is being recorded. If you have any objections, please disconnect at this time.

I will now turn the call over to Mr. Kevin Kalicak. Thank you. You may begin.

Kevin Kalicak

Senior Vice President-Finance and Investor Relations, Darden Restaurants, Inc.

Thank you, Jess, and good morning, everyone, and thank you for participating on today's call. Joining me on the call today are Gene Lee, Darden's Chairman and CEO; Rick Cardenas, President and COO; and Raj Vennam, CFO.

As a reminder, comments made during this call will include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements are subject to risks and uncertainties that could cause actual results to differ materially from our expectations and projections.

Those risks are described in the company's press release, which was distributed this morning and in its filings with the Securities and Exchange Commission. We are simultaneously broadcasting a presentation during this call, which is posted in the Investor Relations section of our website at darden.com. Today's discussion and presentation includes certain non-GAAP measurements, and reconciliations of these measurements are included in the presentation.

Any reference to pre-COVID when discussing third quarter performance is a comparison to the third quarter of fiscal 2020. This is because last year's results are not meaningful due to the pandemic's impact on the business and the limited capacity environment that we operated in during the third quarter of fiscal 2021. We plan to release fiscal 2022 fourth quarter earnings on Thursday, June 23, before the market opens, followed by a conference call.

This morning, Gene will share some brief remarks, Rick will give an update on our operating performance, Raj will provide more detail on our financial results and an update to our fiscal 2022 financial outlook, and then Gene will have some closing comments.

Now, I'll turn the call over to Gene.

Eugene I. Lee, Jr.

Chairman & Chief Executive Officer, Darden Restaurants, Inc.

Thank you, Kevin, and good morning, everyone. Our third quarter was one of stark contrast, and I'm pleased with our performance in this highly volatile environment. Our team did a great job controlling what they could control. In fiscal December, we achieved record sales while meeting our internal profit expectations that were contemplated in the guidance we provided in December.

However, in fiscal January, which is a high-volume period for us, the Omicron variant significantly impacted consumer demand, restaurant staffing and operating expenses. We also experienced substantial weather impacts, all of which resulted in significantly lower sales and earnings than our internal expectations.

Finally, as COVID cases declined and the operating environment normalized, sales improved throughout fiscal February, and we had strong results that exceeded our internal expectations. Sales strength has continued into March. Quarter-to-date, our average weekly sales are slightly ahead of our February actuals, and these trends are incorporated in our guidance.

When we talked last in December, we could not have predicted the impacts Omicron would have on our business. In fact, the dramatic spike in cases created the most difficult operating environment since the initial onset of COVID two years ago. Rick will provide more details on the impact it had on our staffing levels in a moment.

Omicron also created additional pressure on expenses at the restaurant level as we saw higher levels of sick pay and we incurred significant overtime costs due to staffing shortages caused by exclusions. The January spike also caused further supply chain disruptions, and we now expect inflation to be higher in Q4 than when we talked in December. We have implemented pricing actions to mitigate the impacts of rising costs, and Raj will provide more detail in his remarks.

We recognize that all of us in the industry faced additional risk due to the current geopolitical environment such as higher inflation and further supply chain disruptions. However, I'm confident that Darden can compete effectively in any operating environment. We have a strong balance sheet and the right strategy in place, driven by our four competitive advantages of significant scale, extensive data and insights, rigorous strategic planning, and our results-oriented culture. And our brands are relentlessly focused on executing our back-to-basics operating philosophy anchored in food, service, and atmosphere.

Now, I'll turn it over to Rick.

Ricardo Cardenas

President & Chief Operating Officer, Darden Restaurants, Inc.

Thanks, Gene, and good morning, everyone. Our restaurant [ph] teams (04:53) are focused on executing at the highest level in creating exceptional experiences for every one of our guests. That's why we are committed to doing what it takes to have the people we need and the products our guests expect when they choose to dine with us.

From a people perspective, we are seeing positive momentum in applicant numbers, and we feel much better about where we are now in terms of overall staffing. Our focus will continue to be on hiring and, more importantly, training our new team members to reach the productivity level required to enable us to operate at optimum staffing levels.

Our biggest staffing challenge during the quarter was managing the impacts of team member and manager exclusions due to Omicron. To provide some context, at the peak, team member exclusions in January were three times higher than the monthly peak we experienced with Delta.

While we did get some help as the CDC guidelines for exclusion were reduced from 10 to 5 days, 8% of our total workforce was excluded at some point during January. To put a finer point on this, in the month of January, we had over 13,000 team members excluded for a total of more than 65,000 exclusion days.

I am really proud of how our teams managed through the impacts of Omicron. As it moved across the country, we had some restaurants that were down as much as 40% of their staff and others that needed to limit their hours were temporarily moved to takeout only in order to operate effectively.

As Omicron began to fade, our teams kept the same level of focus on staffing and training to provide a great guest experience, which resulted in record sales for fiscal February. Valentine's Day was strong across all our brands, and that is a testament to the excellent job our operators are doing to ensure their restaurants are staffed and ready to serve our guests. In fact, on Valentine's Day, Olive Garden served more than 1 million guests with approximately 35% of sales off-premise.

On the product side, our supply chain team is working hard leveraging our scale to ensure our restaurants have the products they need to serve our guests. Our inventory levels remained strong and some of the logistical challenges we had been dealing with began to improve in December. However, Omicron impacted staffing for our supply chain partners in January as well.

For labor-intensive food production, this resulted in reduced supply and increased cost at a time when protein prices typically shift down from the heavy holiday buying season. Our distribution partners also experienced warehouse staffing challenges and driver shortages. Thus, we had expedited shipping costs and utilized more spot rate haulers in the quarter.

Between those impacts and dealing with back-to-back winter storms, our team did an admirable job of maintaining supply continuity for our restaurants. Together, all of these factors increased our expected annual inflation, and Raj will provide more color on that in a moment.

To Go sales remained strong during the quarter as our brand and our guests continue to benefit from the strength of our digital platform. Off-premise sales accounted for 30% of total sales at Olive Garden and 16% of total sales at LongHorn Steakhouse. Digital transactions accounted for 63% of all off-premise sales during the quarter and 12% of Darden's total sales.

Before I turn it over to Raj, I want to thank all of our team members who have shown tremendous resiliency and dedication in the face of constant change. Two years ago, we closed our dining rooms and did not know when we would be able to reopen them. Since then, we have dealt with multiple COVID waves, and our teams continue to demonstrate incredible flexibility and perseverance while creating exceptional guest experiences.

Today, we are hopeful that we are near the end of the COVID-19 as a pandemic and that we will be able to live with it like we do with other viruses. As I visit our restaurants and talk with our team members, they say each day feels a little more normal, and they are invigorated by the energy that has returned to our dining room. Our team members are the best in the business. I'm inspired by their winning spirit and confident that Darden's best days are ahead of us.

Now I'll turn it over to Raj.

Rajesh Vennam

Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

Thank you, Rick, and good morning, everyone. Before I get into our results for the quarter, I want to expand on Gene and Rick's comments regarding the impact of Omicron and winter weather on our third quarter results. When looking at the fiscal months, actual sales for December and February were close to our internal expectations that were contemplated in the financial outlook we provided in December. And we met our profitability expectations in December and exceeded them in February.

In fiscal January, however, we were significantly below our sales and profitability expectations as COVID cases surged, causing increased staffing shortages and reduced demand. We also experienced more severe winter weather than historical averages. As a result, sales were negatively impacted by over $100 million. This sales slowdown, coupled with additional expenses related to sick pay, overtime and increased inflation, negatively impacted EPS by approximately $0.30 and was more than 100 basis points drag on EBITDA margins for this quarter.

Now turning to the detailed results for the quarter. Total sales for third quarter were $2.4 billion, 41% higher than last year, driven by 38% same-restaurant sales growth and the addition of 33 net new restaurants. Diluted net earnings per share from continuing operations were $1.93. Total EBITDA was $395 million, resulting in EBITDA margin of 16.1%, 50 basis points better than pre-COVID.

We continue to return significant cash to shareholders, paying $141 million in dividends and repurchasing $382 million in shares for a total of over $520 million cash returned to investors in the quarter. We ended the quarter with $555 million of cash on the balance sheet. We continue to see increasing cost pressure with total inflation of 7% this quarter, which was higher than our previous expectations.

As I mentioned last quarter, we began taking additional pricing in the third quarter and have also implemented additional actions to further preserve the strength of our business model while balancing the impact to our guests. For the third quarter, total pricing was 3.7% and for the fourth quarter, we expect our pricing to be approximately 6% compared to last year.

As a result, we now expect pricing to be just over 3% for the full fiscal year. This is well below our updated total inflation expectations of 6% for the year as we continue to execute our strategy of pricing below overall inflation to strengthen our value leadership position.

Turning to our P&L and segment performance for the third quarter. We are comparing against pre-COVID results in the third quarter of 2020, which we believe are more comparable to normal business operations and with how we've been framing our margin expansion opportunity.

For the third quarter, food and beverage expenses were 270 basis points higher, driven by elevated commodities inflation as well as investments in food quality, portion size and pricing significantly below inflation. Our commodity inflation this quarter was 11%. Restaurant labor was 50 basis points higher, driven by wage inflation, higher sick pay and overtime expense as a result of Omicron. Hourly wage inflation during the quarter was just over 9%.

Restaurant labor as a percent of sales in fiscal December and February was better than pre-COVID as these months did not experience the same scale of headwinds from Omicron. Restaurant expenses were 80 basis points lower, as our teams continue to manage controllable expenses. Marketing spend was $44 million lower, resulting in 190 basis points of favorability.

As a result, restaurant-level EBITDA margin for Darden was 19.4%, 50 basis points below pre-COVID levels for the quarter. However, both in December and February, restaurant-level EBITDA margins grew by almost 100 basis points compared to pre-COVID. G&A expense was 90 basis points lower, driven by savings from the corporate restructuring in fiscal 2021, a decrease in mark-to-market expense, lower travel expenses, and sales leverage.

Turning to our segment performance. Sales and segment profit margins significantly increased versus last year for all of our segments. As we compare to pre-COVID, all segments, other than Olive Garden, grew sales. Olive Garden sales were slightly lower due to disproportionate impact Olive Garden experienced from the significant increase in COVID cases. This is because Olive Garden's geographic footprint and guest demographics make it more sensitive to COVID case counts.

Additionally, Olive Garden continues to have significantly less marketing and promotional activity, which is a headwind to sales growth when comparing to pre-COVID. The January impact from Omicron I discussed earlier resulted in all of our segments experiencing lower segment profit margin in the quarter relative to pre-COVID.

Finally, turning to our financial outlook for fiscal 2022. We updated our outlook for the full year to reflect our performance year-to-date and our expected performance for the fourth quarter.

We now expect total sales of $9.55 billion to $9.62 billion, driven by same-restaurant sales growth of 29% to 30% and approximately 35 new restaurants; capital spending of approximately $425 million; total inflation of approximately 6%, with commodities inflation of approximately 9% and total restaurant labor inflation between 6% and 6.5%, which includes hourly wage inflation approaching 9%; EBITDA of $1.53 billion to $1.55 billion; an annual effective tax rate of approximately 13.5%; and approximately 129 million diluted average shares outstanding for the year, all resulting in diluted net earnings per share between $7.30 and $7.45.

This outlook implies full year EBITDA margin growth versus pre-COVID of roughly 200 basis points, still within our previous expected range. This outlook also implies fourth quarter sales between $2.52 billion and $2.59 billion and EPS between $2.13 and $2.28, which is higher than what was contemplated in the previous outlook we provided in December. As Gene said, our quarter-to-date average weekly sales are slightly ahead of February, and that is incorporated in this guidance.

Looking forward to fiscal 2023, we're providing some preliminary guidance for a few items. We expect to open approximately 60 new units in fiscal 2023. We project total capital spending between $500 million and $550 million. We anticipate an effective tax rate of approximately 14% for fiscal 2023.

Now, I'll turn it back to Gene.

Eugene I. Lee, Jr.

Chairman & Chief Executive Officer, Darden Restaurants, Inc.

Thanks, Raj. This morning marked my 31st and final earnings call in my 8 years leading Darden. To all the analysts who support us, thank you for believing us, our vision and our ability to execute. And for those of you who didn't always believe in us, thank you as well. You motivated me more than you will ever know.

I want to thank our shareholders for the trust they have shown us and by investing in Darden. I will miss our time together, whether it's a one-on-one meeting, a group meeting or one of the many dinners we shared over the years. And finally, thank you to all the team members in our restaurants and our support center who are the lifeblood of our company. I look forward to seeing you in our restaurants in my new role as Chair.

I began this journey 45 years ago as a high school kid bussing tables. I've learned a lot of lessons throughout my career, but two in particular have served as guiding principles for me.

First, when it comes to making decisions, you have to make sure both your guests and team members win. When those two critical stakeholders win, it's a good decision. Second, it's a simple business. Malcolm Knapp says it best. The [ph] restaurant business (18:16) is simple, but simple is hard. To be successful in the restaurant industry, you must have great people who consistently serve outstanding food in an engaging atmosphere.

So I may have bored you with my back-to-basics operating philosophy, running great restaurants will always require intense focus on the fundamentals. As I transition into my new role as Chair, I'm confident Darden is set up for success. Rick is ready to lead the company, and he and his team will do a great job.

Now, we'll open it up for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We'll take our first question from David Tarantino with Baird. Your line is open. Please go ahead.

David E. Tarantino
Analyst, Robert W. Baird & Co., Inc.

Q

Hi, good morning. My question's about the margin outlook given the inflation environment you're facing. And I think you had previously guided to 200 to 250 basis points of margin expansion relative to pre-COVID levels. And it looks like you're going to [ph] come in (19:46) on that range for the fiscal year. But as you think about the forward-looking outlook beyond this year, do you think that is still in play as you think about the inflation as you move into fiscal 2023, or do you think that needs to change?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

Hi David. Good morning, this is Raj. So, let me just step back and talk about margins – when we began the year, obviously, things have changed quite a bit from the environment today relative to how we started the year is very different. We started the year with 3% inflation assumption and pricing closer to 1.5%. And here we are, three quarters in, we're looking at 6% total inflation, and our pricing has only gone up by about 1.5%.

So, we started with 1.5% and now we're just over 3% for the full year and still are able to get to that 200 basis points. So, we really feel good about where we are getting to by the end of this year. We'll share more details in June call in terms of how we're thinking about fiscal 2023. But I think in the current environment, considering the situation we're in, we feel good about where we expect to be for this fiscal year.

David E. Tarantino
Analyst, Robert W. Baird & Co., Inc.

Q

Got it. And then just a follow-up on that. You are – sounds like you're leaning in a bit more on pricing with the fourth quarter being up 6%. I guess how did you arrive at the decision to take that much pricing? And how do you feel about the consumers' ability to absorb that level of pricing?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

Yeah, I think if you actually look back to what we've done over the last few quarters and actually last couple of years, we've taken very little pricing. We said all along that we wanted to preserve the flexibility. We wanted to – we approach pricing very conservatively. And so we've been trying to hold off on pricing as much as the inflation would have dictated.

And I think where we are now is 6% – while 6% seems high in terms of how historically we price, considering the environment and considering what we're pricing over two years, we don't think it's too much. Obviously, we're going to continue to look for opportunities to price below inflation. And like I said earlier, this year, we're pricing [ph] 300 basis points (22:16) below. And as inflation creeps up, we're going to have to try to manage through that, but it's going to be a combination of pricing and productivity initiatives.

David E. Tarantino
Analyst, Robert W. Baird & Co., Inc.
Q

Great. Thank you. And Gene, congrats again on a great run as CEO.

Eugene I. Lee, Jr.
Chairman & Chief Executive Officer, Darden Restaurants, Inc.
A

Thank you, David.

Operator: We'll go next to Brian Bittner with Oppenheimer & Company. Your line is open. Please go ahead.

Brian Bittner
Analyst, Oppenheimer & Co., Inc.
Q

Thank you. Good morning. Congratulations, Gene. We seem to be sitting here at a point in time when operators and investors are increasingly concerned about lapping stimulus and doing so at a time when gas prices are surging. And this does not seem to be impacting your outlook based on your comments around March and based on the implied 4Q revenue guidance, which implies very strong trends. So, can you just comment on the environment out there and maybe why Darden seems to not be prone to it?

Eugene I. Lee, Jr.
Chairman & Chief Executive Officer, Darden Restaurants, Inc.
A

Brian, I think – this is Gene. I think one comment – and I'll let Rick jump in here, too, but one of the things that gives us confidence around pricing – increasing [ph] our (23:28) pricing level to 6% is that our wage rate at the lower end are increasing higher than that. So we're seeing almost double digit when you look at our direct labor. So we believe that wage inflation throughout the country is rising at a pretty rapid rate. And so we believe that the consumer can handle that right now based on where things are today, right.

The environment can shift pretty quickly on us here. But what we're seeing today is that consumer demand remains fairly strong. And this environment seems to be very different than a lot of other environments we've operated in the past, where we've got a lot of headwinds impacting the consumer, but wages are increasing rapidly and especially more so on the lower end.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.
A

Yeah, Brian. And I'll add to the current environment. As you think about what's going on in Ukraine, first of all, I want to say our thoughts and prayers are with the people of Ukraine, but the fact is we don't know how long the conflict is going to last. And so we don't know how long that's going to do anything to the environment itself. We're focused on controlling what we can control, confident in our ability to manage our business effectively in any operating environment.

The other thing to think about is restaurant supply is down 13-ish percent, 14% from pre-COVID. And so that gives people that want to go out – and people do want to go out – fewer options, and we are a great option for them.

So – and then last thing I'll say is you'll notice that our guidance range is a little bit wider than it normally would be in a quarter [ph] at the end, (25:14) and that's just because of the uncertainty that we're feeling. But we feel good about the guidance we gave, we just gave a little bit bigger range just because of what we're going through today.

Brian Bittner
Analyst, Oppenheimer & Co., Inc.

Q

Great. Thank you, Gene and Rick.

Operator: We'll go next to Brett Levy at MKM Partners. Your line is open. Please go ahead.

Brett Levy
Analyst, MKM Partners LLC

Q

Great. Thanks for taking the question. And Gene, your comments will be surely missed over the next few years as we come out of these more challenging times. When you think about your operating model and all of the [audio gap] (25:52) with inflation, labor shortages, all of the rising pressures on the consumer, how should we think about what you can implement in terms of technology? How conservative you want to be in terms of newness to the menu over the next, we'll say, two to six quarters? How should we think about what you can really monitor on the controllables to drive productivity versus your need to stay front-footed? Thanks.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, Brett, it's Rick, and – couple things on that question. So on the technology front, we continue to have the same goal. It's implementing technology that reduces friction across the value chain, wherever that friction is, and responding to guests' growing needs for personalization. We don't anticipate using technology to take people out of the system because this is a full-service restaurant and full service company, and we believe that consumers want human interaction.

In terms of menu, we've been clear that we really like the reduction in menu and what it's done to provide our guests with the dishes they want – high-value dishes that they want and make it easier for our teams to produce them. And we continue to get better. If we add new items, we take another item off. And so we're going to be consistent on making sure our menus stay at the levels they are today within a very small percentage up or down.

On the controllables front, we still have some costs that will be coming in over time. But as we look to the future and project, as we think about sales going forward, we would expect to get some productivity. But we don't think margin's going to be moving very much from where it is today. We'll talk more about that in June as we think about our fiscal 2023.

But just if you think about our long-term framework that we've had, it was 10 to 30 basis points of margin improvement. We got seven years of margin improvement in two years. And so we have to make sure that we manage that and consider that margin improvement we've made over the last couple years.

Brett Levy
Analyst, MKM Partners LLC

Q

And then just one quick follow-up. When you think about the mix of your consumers right now shifting either to a higher value product or the pursuit of value, have you seen any material movement in the mix, I guess, by Olive Garden, by LongHorn and then just across [ph] for consolidated? (28:35)

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

No, Brett, we haven't seen any movement.

Brett Levy
Analyst, MKM Partners LLC

Q

Thank you.

Operator: We'll move next to John Glass with Morgan Stanley. Your line is open. Please go ahead.

John Glass
Analyst, Morgan Stanley & Co. LLC

Q

Hi, thanks. Good morning, Gene. I don't think you bored any of us. I think, actually, you taught us all a lot about the industry. So thank you for that. Raj, on commodities specifically, I know you've provided some insight on the deck here about through May. Do you have [ph] at least (29:08) started to contract beyond that or do you think it's too early given the volatility? Do you have any visibility, I guess, into 2023 on at least that expense item?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

John, we are obviously starting to have conversations. We have – we are – I would say, from a – compared to historical situation, we're probably less contracted and we're working through those over the next few months, and we'll have more to share in June. But the forward premiums are too high to contract that far out.

John Glass
Analyst, Morgan Stanley & Co. LLC

Q

Thank you for that. And then just related to your comments about pricing and the consumer can tolerate that pricing, how are you thinking about your promotional tactics in 2023?

Do you start to come up with alternative plans if the consumer is weaker than you expect? Are you starting to revisit your thoughts about the marketing spend in the business? How are you preparing if, in fact, consumer demand starts to weaken? And what are some of the tactics, just broadly, that you think you could employ to continue the sales momentum?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, John, it's Rick. Thanks for the question. I will say we're not going to talk too much about 2023. But I will say, we've got contingency plans for anything. If the economy slows down, we've got some plans. We won't talk about what they are. If the economy stays strong, then we'll continue what we're doing. And so until we see what that is and where it is, we don't really want to comment on what we would do.

John Glass
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Thank you.

Operator: We'll go next to Brian Mullan at Deutsche Bank. Your line is open. Please go ahead.

Brian H. Mullan
Analyst, Deutsche Bank Securities, Inc.

Q

Hey, thank you. Thanks for the development color on fiscal 2023. Just wondering if you could speak to how that pipeline is building beyond that on a multiyear basis. And it would be great to hear your thoughts on what you're seeing from a competition for site perspective. Are you seeing other large chain casual diners out there looking at these same sites? Just anything different or notable that's worth calling out versus how the environment was prior to COVID when there were more restaurants.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, Brian, we're continuing to build our pipeline for fiscal 2024 and beyond. And as we've said before, we'd like to get closer to the higher end of our long-term framework in the future.

As we're seeing competition for sites, we aren't seeing as many people competing for sites, but there are still brands that are out there growing and competing for site. And so as we continue to build the pipeline, we will continue to compete for some of those sites. I will say, add to that, we are taking over some sites and building some restaurant and converting some to our brands at an economical rate. And they're really great sites. Those brands just didn't stay through.

So we'll continue to build our pipeline. We still have some cost inflation in there, but our business model has improved so much that is offsetting that by more than enough. And we feel good that we'll continue to build our pipeline.

Brian H. Mullan
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you.

Operator: We'll go next to Peter Saleh of BTIG. Your line is open. Please go ahead.

Peter Saleh
Analyst, BTIG LLC

Q

Great. Thanks. Thanks for taking the question and congrats again, Gene. Gene, I think several quarters ago, you had mentioned that you were seeing about 10% fewer units in casual dining versus pre-pandemic, but there was, I think, a lot of speculation still in the category and people opening up restaurants.

Are you still seeing that? Is it still fairly competitive out there in terms of development, or has the inflationary environment kind of pushed that down a little bit and made that subside a little bit?

Eugene I. Lee, Jr.
Chairman & Chief Executive Officer, Darden Restaurants, Inc.

A

Yeah. I think if you go back – and what I was trying to say back then was that there was a lot of speculation, especially by some of the big REITs out there that were willing to take on some real estate and leave it vacant for a while, the carry costs were less. We haven't seen any real change in that. My expectation would be, as interest rates rise, there'll be less speculation in the real estate market and people will be less likely to allow their buildings to sit dark for a period of time.

And so, as Rick said before, in the prior question, we're building our pipeline. There's competition out there. Not a lot of chain restaurants out there competing, there's a lot of smaller regional players out there competing for space. At the end of the day, most landlords want a Darden guarantee signature on their property. We get to look at most of the real estate out there in the United States, and we get first look at it. And if we can make it work, we're going to – we'll sign a lease and we'll try to put the right brand on there to maximize the opportunity.

Peter Saleh
Analyst, BTIG LLC

Q

Thank you for that. And then, just on the development for 2023, can you give us a sense on how much of that development is coming from Cheddar's?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah. It's going to be somewhere in the low single digits, maybe as much as 10, but lower single digits to as much as 10.

Peter Saleh
Analyst, BTIG LLC

Q

Great. Thank you very much.

Operator: We'll go next to Jeffrey Bernstein at Barclays. Your line is open. Please go ahead.

Jeffrey A. Bernstein
Analyst, Barclays Capital, Inc.

Q

Great. Thank you. Gene, thank you for your steady leadership and friendship over the years and for setting an example for the industry to follow. So a question on the off-premise business. It seems like it's stickier than we would have thought, I think you said 30%, Olive Garden; 16% at LongHorn. Just wondering if you can maybe share the split between delivery and pickup within that current To Go sales and maybe where you think that's going to settle.

I mean it just seems like a lot of this is here to stay. I'm just wondering whether there's any chance you guys would reconsider opening up to maybe third-party delivery aggregators. It seems like the consumer expects it and the consistency's improved, the fees have eased. I don't want to see you guys lose out if this is kind of where the future is going. So, any thoughts on that would be great. Thank you.

Eugene I. Lee, Jr.
Chairman & Chief Executive Officer, Darden Restaurants, Inc.
A

Hey, Jeff, this is Gene. I thought you'd wait till I leave the room to ask about third-party delivery. I'll let Rick take that.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.
A

Hey Jeff, thanks for the question. Gene and I are in the same place on what we believe with third-party delivery. We still don't like that model. We don't think it's the right thing for having someone get in between us and our guests. And a couple of points, Olive Garden has grown their To Go business significantly and, in many ways, faster than others that have grown it with third-party delivery without that margin hit.

Now, our takeout sales increased in Q3 from Q2, partly because of the influx of Omicron. And so people shifted again back to a To Go experience. We're seeing a little bit of a shift back to on-premise in Q4. We don't know where the equilibrium's going to be. And when we get there, it will probably be higher than where we were before COVID, but it's not going to be at the levels they are today. And so we'll continue to make investments that we need to take the friction out of the order, pick up and pay experience so that people don't consider getting delivered.

Now, you did ask about our delivery. We do have large party delivery for Olive Garden and that's a good business for us. It's a minimum order size. It gives us enough time to prep the order and deliver it to our guests and actually do a little bit more of a setup for it. I mean, so we really feel good about that business, but we never say never, but the likelihood of us getting into third-party delivery anytime soon is pretty low.

Jeffrey A. Bernstein
Analyst, Barclays Capital, Inc.
Q

Thank you.

Operator: We'll go next to Dennis Geiger at UBS. Your line is open. Please go ahead.

Dennis Geiger
Analyst, UBS Securities LLC
Q

Great. Thank you and, Gene, congrats on a remarkable run. Wanted to ask on the staffing situation a bit more. Where are you now on staffing levels relative to where you'd like to be? And kind of related to that, as it relates to wage inflation, recognizing there's a lot of moving pieces out there, has that stabilized in your mind or is it too soon to make that call?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.
A

Yeah, Dennis, it's Rick. Thanks for the question on the staffing side. We feel – as I said in the prepared remarks, we feel much better about where we are in our staffing today than we did three months ago and three months before that. We continue to add around 10,000 people working per quarter, basically at the end of the quarter from the quarter before.

Our staffing levels are greater than 95% of pre-COVID staffing levels. We don't need as many people as we did before because of our productivity enhancement. That said, we want to make sure that our team members that we have are fully trained and productive. And as we said, exclusions were pretty tough in the month of January, especially.

In terms of wage inflation, we are, as we said, seeing a continued increase on applicant flow. And so while it hasn't reversed kind of the starting wage trends, it's actually starting to stabilize, but we don't know where that's going to land. But right now, it's starting to stabilize a little bit. And we'll know more as that applicant flow continues to pick up and people feel more comfortable working again after – as Omicron, hopefully, become more of an endemic versus a pandemic.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Great. And just one more there, Rick. As it relates to the competitive environment and the industry, you spoke to it some, I think, as it related to real estate opportunities. As it relates to market share, perhaps, how are you thinking now about the small chain independent situation? Has it gotten better or worse as you look ahead? Has the opportunity for you to pick up share, because of closures, permanent closures, maybe more challenges that are coming, given all the inflation, has that – have your thoughts there changed at all on what that means for Darden's brands? Thank you.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Dennis, our thoughts haven't changed. As the economic environment continued to struggle over time, as Omicron picked up, more restaurants closed. I mean, so there are fewer restaurants today than there were last month and the month before and the month before that. They'll eventually get filled. And our – what we want to do is be there to fill some of those restaurants and pick up that market share.

As we think about the future, we've said that we're going to increase – hopefully get to the high end of our framework in new unit. But those restaurants will eventually come back and be better than they were before. Our restaurants will be better than maybe the ones that were closed.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Thanks very much.

Operator: We'll go next to Chris O'Cull at Stifel. Your line is open. Please go ahead.

Chris O'Cull
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thanks. My question relates to just consumers' value perception of Olive Garden. Rick, I'm curious if you've seen any change in the value perception as more orders have shifted to off-premise over the past couple of years? Or if your strategy of pricing below inflation, as others have taken more aggressive pricing, has had any impact on Olive Garden's value perception?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, Chris, we haven't really seen a big impact in our internal data on a change in value perception at Olive Garden. We track both on-premise and off-premise. Olive Garden continues to increase their overall satisfaction from five years ago. There's a slope up versus most customers are actually more dissatisfied across the American Consumer (sic) [Customer] (41:20) Satisfaction Index. We're bucking that trend. All of our brands are bucking that trend.

And so we haven't seen a big change in value ratings for Olive Garden, and we'll continue to monitor that. We don't think the pricing actions that we have taken are going to change that dramatically because we're still, as Raj had mentioned, much lower than most full-service restaurants combined over a two-year period.

Chris O'Cull
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That's helpful. And then just with marketing dollars down about 60% from pre-COVID levels, and other chains are starting to spend more on advertising, is there any concern at all that Olive Garden may lose top my mind awareness if marketing spend doesn't increase more aggressively?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Chris, as you mentioned, we are lower in marketing spend than we were pre-COVID. We're going to continue to wait for the equilibrium. I'm really proud of the work that Dan and his team has done, keeping with our strategy. And so we have been marketing. But we're marketing our Never Ending First Course to remind everybody about the value they get every day at Olive Garden. We're not doing promotional marketing, but we're talking about the value they get every day. And we'll continue to look at our marketing spend over time. And if the time we bring that back up, we would expect to earn a return on that, as we said on the last call.

We feel – Olive Garden is large and one of their advantages is their scale, means that we will be marketing at Olive Garden. We just want to find the right time to continue to increase that, but it probably won't get all the way back to pre-COVID levels, but we'll see where equilibrium comes.

Chris O'Cull
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. Thanks, guys.

Operator: We'll go next to Eric Gonzalez at KeyBanc Capital Markets. Your line is open. Please go ahead.

Eric Gonzalez
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey, thanks for the question. And Gene, congrats on a fantastic career. It's really been a pleasure to follow your success over the years. My question is about the consumer environment. You talked about the rise in low-end wages being an offset to some of the cost pressures out there. I'm also wondering if we might be experiencing some post-Omicron pent-up demand in March. Will the consumer might be less sensitive to price increases? So perhaps you could talk about how sustainable you believe the current momentum might be and maybe what factors might contribute to that sustainability.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Eric, this is Rick. I'll talk about the sustainability. We've guided where what we think our Q4 will be, and that includes everything we know today. And it talks about what our comp sales will be and what our total sales will be, which was higher than what we would have guided in December for Q4.

There might be some pent-up demand for Omicron, but there's pent-up demand for COVID. And it might have been Omicron, but it's other things. And so we're going to continue to see what the equilibrium is. We keep coming back to that word, equilibrium. What do we look like when everything is back to a more normal state, and is a steady state. And we're not there yet. We've got geopolitical risk and other things, which is, again, why we have a wider range in our outlook for Q4 than we normally would at this time.

Eric Gonzalez
Analyst, KeyBanc Capital Markets, Inc.

Q

Fair enough. And maybe on labor costs quickly, you mentioned the heavy exclusion costs due to Omicron. I'm just wondering if you can comment on turnover levels and then maybe quantify how much of a drag, if you're seeing any excess staff training relative to normalized levels.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, turnover levels in the last – you think about turnover the way we manage it, it's over a 12-month period, and you've got a lot of kind of fluctuation over time. But turnover levels are getting a little bit better for us in [ph] the long – (44:56) versus where we were just a few months back and months before that.

We still have 90-day turnover at a higher level than we'd like it to be. So that's why we're focusing more on training, even more and specifically on our new team members to make sure they get up to speed and they understand what our business is all about. And I'll let Raj talk about the other part.

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

Yeah. On the expense side, I'd say just, purely, the expense part of it probably impacted our margins by about 20 to 30 basis points related to all the Omicron impact, whether it's overtime, sick pay or training, all that stuff is probably in that 20 to 30 basis points range. I remind you, that doesn't include the deleverage from sales [ph] mix. (45:37) So that's the other part of it that impacts the margin, too.

Eric Gonzalez
Analyst, KeyBanc Capital Markets, Inc.

Q

That's helpful. Thanks.

Operator: We'll go next to Nicole Miller at Piper Sandler. Your line is open. Please go ahead. I apologize. We lost your line. We'll go to Andy Barish with Jefferies. Your line is open. Please go ahead.

Andy Barish
Analyst, Jefferies LLC

Q

Yeah, one quick follow-up. Just, Raj, on the $100 million sales impact you quoted, I was a little confused. Was that the Omicron impact and the winter weather impact? I just wanted to make sure I heard that okay.

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.
A

Yeah, it was the impact of both in January. We're specifically referring to the impact in January, yeah, from both.

Andy Barish
Analyst, Jefferies LLC
Q

Okay. and then, Gene, if you could kind of publicly impart a little bit of final wisdom on – I mean, what would you be looking for? What would typically show up in consumer behavior if the consumer was starting to feel stressed from environmental factors?

Eugene I. Lee, Jr.
Chairman & Chief Executive Officer, Darden Restaurants, Inc.
A

Yeah. I think – I mean, obviously, we've been trying to regress a bunch of different variables back in the past recessions to try to – to give us a chance to understand what the leading indicator may be. I think this one's so different because of the geopolitical risk involved, because of a pandemic that, hopefully, we're going to switch to endemic and we're able to live with this virus going forward. I think that it's going to take a fairly solid recession to really have some impact on the consumer. I think the consumer balance sheet is stronger than it has been previously.

And I think the biggest variable going forward that as I think about it, it's different than every other recession or a period that we had a real slowdown is that there's so many open jobs today. And when you think about what really causes a recession, it's employment.

And as things slow down a little bit, it's just – I just don't see companies, especially where the supply chains have been somewhat broken and inventories levels are low, I don't see us getting to a higher – a significantly higher unemployment level anytime in the near term, barring something really happens bad with what's going on overseas.

And so I just think this one is different, because of where employment is. It's not like we've perfectly matched everybody that's willing to work with a number of open jobs. We have so many open jobs today. And I look at our shop here and say, boy, if we had to come in and cut some more overhead, it would be almost impossible to do, because we have a fair number of open jobs here. So that's the one variable that I think is so different in this environment. I don't know how it's going to play out.

But remember, we're in a business where, like in an Olive Garden, if three or four tables don't come in tonight [ph] and that (49:04) 12 to 16 guests, it's going to have a pretty big impact on the business over time. So we're fighting – I always say we're fighting for that last [ph] four top. That last four top (49:13) is so profitable, and we need to make sure that we continue to create great value and we got to operate well.

And I think that's the big thing out there today is that the – I think casual dining restaurants and full-service restaurants in general is we just need to operate better. I think we got sloppy during COVID. We've had to do things to just stay open and get by. We got to get sharp again. And I think our teams are doing a great job. But I think as an industry, we've got to earn the right from the consumer to pay what we're asking them to pay. And we've got to provide a really true full-service environment.

Andy Barish
Analyst, Jefferies LLC
Q

Thanks again.

Operator: And we'll return to Nicole Miller with Piper Sandler. And Nicole, your line is open. Please go ahead.

Nicole Miller Regan
Analyst, Piper Sandler & Co.

Q

Thank you so much. I hit the hang-up button versus on mute, so I apologize. Two quick ones. On Olive Garden, in, let's say, a normalized environment, you had mentioned the sales and marketing. Can you talk about and reconcile a little bit marketing in the framework of discounting? Because it seems like a lot of investment has gone back into the store and into the plate, really consumer-facing areas. And so it also seems like it would be tempting with sales just down a smidge to go back to discounting, but maybe that isn't the right strategy. Could you just talk about that a little bit?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Nicole. We are really pleased with the strategy that we have. We believe that it's better to provide an experience with a great guest experience that people, our core guests that are willing to pay for that experience. And we would rather not discount. We took out all discounting out of Olive Garden – in all of our brands at COVID. I mean we haven't added that back. Others have started to add that back, but we are continuing to maintain our strategy of keeping the discounts out of our brand.

Again, as the environment changes, if the environment changes, we will consider anything, but we have a lot of options. Our biggest option is to increase our marketing spend, whether it's – even it's undiscounted just to get our strategy, our message out at Olive Garden of a Never Ending First Course. That is a great value. And as we think about limited time offers in the future, if we have them, they'll be at a different construct than we had before. But again, when equilibrium comes and we know which way we go, that's when we'll act.

Nicole Miller Regan
Analyst, Piper Sandler & Co.

Q

And then if that equilibrium does not come, I'm curious about Cheddar's. Not that anyone would or could move this quickly, but if it's a weaker macro period, do you press on value and marketing the value of Cheddar's and/or even grow the units as fast as possible? It seems like that's one of the best or better value propositions in the portfolio.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Nicole, Cheddar's is a great value. That is their advantage as well, value. And we're continuing to improve the experience at Cheddar's, improve the food, improve the service experience while keeping prices much lower and pricing much lower than our competition, which is just going to improve the value perception even more. Cheddar's doesn't have as much scale to do kind of the TV kind of advertising.

Our best advertising at Cheddar's is when you get your check and you see the price that you're paying and you tell your friends. We're going to continue to do that and find other ways with digital and other things if we need to, to ramp up marketing in our brands.

And in terms of new unit growth, those pipelines take a while to build, right. So, we're building them now. You can't kind of turn on a dime if the consumer gets a little weaker and say we're just going to open that quite a few more of one brand versus the other. But we believe in Cheddar's and we believe that they have a lot of growth ahead of them. And we're going to continue to build the pipeline of people and of restaurant to capture that opportunity.

Nicole Miller Regan
Analyst, Piper Sandler & Co.

Q

Thank you.

Operator: We'll go next to Andrew Charles at Cowen. Your line is open. Please go ahead.

Andrew M. Charles
Analyst, Cowen & Co. LLC

Q

Great. Thank you. Gene, best wishes on a well-deserved retirement and Rick, best of luck to you in your new role. The mix of digital sales as a percent of off-premise grew this quarter to 63% from 60% of sales previously. And Rick, I know you said the equilibrium [indiscernible] (53:57) where the off-premise mix can go is unclear relative to that prior 20%-plus target. But is there an upper boundary for how high that digital mix of off-premise can go? And then I have a follow-up.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, I don't think there's a limiter of how high the digital mix will go other than 100%. But there are still people that want to call in and dial in and pick up their order. They may not be as comfortable with the technology. We're trying to make it as seamless and smooth as possible. But we're even making that experience better for the people that dial in, how they pay and how do they pick up. So, we're doing things on the technology front that maybe they don't see as much, but that we can get better so that they can still do the dial-ins for us.

We would like to see the digital percentage continue to grow as part of off-premise. It just simplifies the operation in the restaurant. There's fewer things that the team members have to do to pick up the phone, et cetera. But there are some long-standing guests that just like to call and we'll continue to offer that service to them. We will not eliminate dial-in to get the percentages up. These percentages have grown because of the investments that we've made and will continue to make. And hopefully, they'll continue to grow.

Andrew M. Charles
Analyst, Cowen & Co. LLC

Q

Great. And then just relatedly, can we expect to see a higher mix of digital marketing in 2023 versus 2022 to drive a higher digital off-premise mix and help increase data collection? Or will the focus of the 2023 marketing message pivot back to driving more dine-in sales?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Andrew, we're not going to talk as much about what's going on in 2023. I will say that whatever the environment looks like, whether we need to drive more dine-in sales versus off-premise, we'll do. We don't really do a lot of digital marketing on the off-premise, so most of our marketing is for on-premise. And so if we do any off-premise marketing, it will be an increase. So pretty much most of our marketing is for – I'm sorry, if we do any off-premise marketing, it will be [ph] to increase. (56:01) Most of our marketing is on-premise.

Andrew M. Charles
Analyst, Cowen & Co. LLC

Q

Thank you.

Operator: We'll go next to Lauren Silberman at Credit Suisse. Your line is open. Please go ahead.

Lauren Silberman
Analyst, Credit Suisse Securities (USA) LLC

Q

Thank you. And Gene, I also echo everyone's comments about your leadership. So on the accelerating commodity pressures, beyond additional price, can you talk about any other levers you're looking at in the supply chain to help offset some of the commodity pressures, any flexibility in some of ingredients and sourcing?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Lauren, we really like the way our menu works right now and the taste in our food. So we don't have a – we don't expect to go in there and change ingredients significantly to offset some of these costs. We'll continue to work with our supply chain partners to get the best prices that we can get for the product.

I will say, as I said in my prepared remarks, we're going to do whatever it takes to get the products that our consumers value and that our consumers expect to have when they come in to eat with us. We're hoping that eventually this inflation environment gets a little bit better, but we think we can compete in whatever environment there is.

Lauren Silberman
Analyst, Credit Suisse Securities (USA) LLC

Q

Thank you.

Operator: We'll go next to Chris Carril at RBC Capital Markets. Your line is open. Please go ahead.

Christopher Carril
Analyst, RBC Capital Markets LLC

Q

Thanks and good morning. Gene, congratulations and wish you all the best going forward. So just on the additional pricing you'll take beginning this quarter, can you provide any further detail on how you're planning to implement this additional pricing across the portfolio, maybe specifically at your largest brands versus your higher end brands?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

Yeah. I think, Chris, the way we've talked about before is our philosophy is generally to price less at casual dining. And obviously, that can vary from quarter-to-quarter. So I don't want to get into the exact specifics because these numbers change monthly, quarterly because it's a function of what we're wrapping on and how this goes. But generally speaking, there's a lot of science that goes into how we go about pricing and there are – and that is very analytical, but there's also a lot of art that we've gained over time, the intuition that we've developed looking at data over time being in this business for a long time.

Christopher Carril
Analyst, RBC Capital Markets LLC

Q

Got it. And then, I guess, as a follow-up, Raj. You mentioned productivity initiatives to also help offset these incremental cost pressures that you're seeing. So can you expand maybe on what some of these productivity initiatives look like? Is this just more related to new employee training?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

I think it goes back – some of that is that, but I think it goes back to the things that we did through COVID. A lot of the stuff is a continuation of what we've done with simplification. We continue to find opportunities to simplify. And then as Rick said in his comments, as we're hiring new people, our focus is on training them to be more productive. So there is a lot of new people in our system right now, and we want them to be at their best. And that takes time.

Christopher Carril
Analyst, RBC Capital Markets LLC

Q

Got it. Thank you.

Operator: We'll go next to John Ivankoe with JPMorgan. Your line is open. Please go ahead.

John Ivankoe
Analyst, JPMorgan Securities LLC

Q

Hi. The question was also just on the staffing, and I guess who the applicants are in 2022 relative to 2019. It was curious – or good to hear that your overall turnover levels, I guess, on an annual basis are beginning to improve. But how would you I guess, [ph] I think, you'd (59:39) described the overall productivity and the hospitality elements of your employees, I mean, is this still basically the type of employment class that you expect to get back to fiscal 2019 hospitality levels? Or have there been some changes, including your menu simplification that might actually allow the calendar-2022-and-beyond class to actually execute better than what you've done in the past based on some of the process changes that you've made?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, John, to answer the question directly, I think we can get better, continue to get better with this class because of the menu simplification we've made. Reducing our menus the way we did has made it a lot easier to run a restaurant. The managers spend a little less time on individual items and teaching people on these items that we didn't produce very often. I mean we just get better at producing the same things over and over again, which are the things that our guests want.

We've had a couple of things that have happened through COVID that have been good for us. One is we've hired some folks that maybe we wouldn't have looked at before, maybe it's their first job. But giving someone their first job and teaching them to do the things the way we do it is a good thing for us. Maybe in the past, we would have said, you needed to have a lot of experience in a restaurant before you come to work for ours. But we're seeing that some of these folks that we're hiring that are new to work, we're teaching them how to work the way we want them to work and it's actually working out for us pretty well.

We also have seen a lot of rehires. A lot of people are coming back to work for us that have left us over time. And a lot of our managers are rehires. And so while people may have left the industry during COVID, a lot of them are coming back. And we feel really good about the fact that they're coming back to work for us.

John Ivankoe
Analyst, JPMorgan Securities LLC

Q

That's helpful. Congratulations again, Gene.

Operator: We'll go next to David Palmer with Evercore ISI. Your line is open. Please go ahead.

David Palmer
Analyst, Evercore ISI

Q

Thanks. Congrats, Gene, on a heck of a career. All the best to you in retirement. I have a question about Cheddar's and Darden's acquisition strategy going forward. Cheddar's has gone through a lot of change before COVID. I think some of that was more painful and slow than you would have expected, but it seemed to have reached pretty transformational levels with labor productivity during COVID. So could you talk about Cheddar's new unit returns today and what that unit growth could possibly look like going forward for that brand? How fast can it ramp? And I have a quick follow-up on that.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, David, let me just say how proud I am of John Wilkerson and his team and what they've done over COVID over two years of significantly changing the business model at Cheddar's to make it a much more investable proposition for us. As we said in one of the earlier questions, kind of the new unit opening range of low single digits to high – to up to 10, we'll probably open more than we've had since we bought them. And we'll continue to build that pipeline as we continue to strengthen the team.

The great thing that they have done is build the team to be ready to open restaurant. And that wasn't ready when we got them. And so, I can't tell you how big Cheddar's will be, but I can tell you that they have a big addressable population. The value that they provide for the consumer and the food that they have means there's a lot of Cheddar's that can be built out there.

How many? Can't tell you until we get some more of these open. I will say, the restaurants that we've opened through COVID had done really well for us, and we feel really good about the fact that we can open more Cheddar's.

David Palmer
Analyst, Evercore ISI

Q

And, I mean, I don't know, maybe you want to circle back on the unit returns part of that. But I also have a follow-up just on sort of what that means, as you're getting past Cheddar's, are acquisitions going to be even more in focus for you?

And I just think it's worth just noting how unusual it would be if Darden were to become, sort of, get an acquisition premium, if you will. Because right now, there's not many play – not many companies out there you can see an acquisition strategy paying off in an accretive way, where the multiple reflects that, like that rinse-and-repeat credibility on acquisitions. So maybe you want to comment on that capability and how much of this is going to be a focus for you going forward? And thank you.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, David. If you think about our acquisition strategy, we've made four big acquisitions since 2007. And that should still be part of our strategy going forward. We've proven that we can get synergies. And we've proven over time, it takes a while, that we get these brands up and running and ready to go and grow. But our management team and board regularly evaluate that, and nothing is going to change as we go forward. We believe Darden is a platform, a platform that can add brands that help Darden grow and continue to build our biggest advantage, which is scale.

David Palmer
Analyst, Evercore ISI

Q

Thank you.

Operator: We'll go next to Jared Garber with Goldman Sachs. Your line is open. Please go ahead.

Jared Garber
Analyst, Goldman Sachs & Co. LLC

Q

Hi. Thanks for taking the question. And certainly, appreciate all the great color on the quarter, and I think on the consumer as we think, I think, ahead for the rest of the year. Many of the questions have certainly been asked and answered, but I wanted to get a sense of maybe some other strategies that you're thinking about in terms of making the consumer value proposition stronger outside of the price dynamic.

So wondering if you can comment on how loyalty plays into your thinking here, whether that's a brand-specific program or something across the platform. Or are there any other, sort of, strategies that you're thinking through that might improve that value proposition outside of just stronger menu and sort of better value pricing?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, Jared. As we think about our strategy and value proposition, it's really what we've been talking about for years in our basic, simple operating philosophy: food, service and atmosphere.

We're going to continue to invest in food, make it better and make it more consistent every time you come into one of our restaurants. We're going to continue to improve our service and we're going to make sure our atmospheres are great. In terms of – while we, again, price – continue to price, is our expectation, below our competition and below inflation. We believe that that is the best way to build value.

Loyalty, we've looked at that before. We may look at it again. I'm not quite sure that that's where the value comes from is to give a discount to your highest core consumers. Our goal is to build an additional visit to our core consumers, and we've been doing that without discounting because we're giving them what they want at a price that they think is a fair value for them and a great value for them. And we'll continue to do that going forward.

Jared Garber
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thanks for the color.

Operator: We'll go next to Jake Bartlett with Truist Securities. Your line is open. Please go ahead.

Jake Rowland Bartlett
Analyst, Truist Securities, Inc.

Q

Great. Thanks for sneaking me in here and, Gene, congratulations, just to echo all the thoughts there. My question was on the idea that there's a pent-up demand post-COVID itself and not just Omicron, and given all the – how [ph] data-intensive (01:07:38) you are, I'm wondering if you can share any data on how many – whether you're seeing consumers come back in that haven't come in, in a couple of years, maybe how material that is, whether you're really seeing a shift in consumers kind of more post-COVID.

And then a separate question is just on regionality. I think as investors are a little concerned about what gas prices might be doing to consumers, [ph] maybe (01:08:08) it's higher prices in different regions and specifically in the West Coast, whether you're seeing any kind of more pronounced near-term impact as you think about maybe your quarter-to-date trends, whether there's much variability there.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Hey, Jake, in terms of kind of this pent-up demand over – for COVID versus Omicron, yeah, we're seeing some consumers that haven't been with us for a couple of years in our dining rooms and are dining, right. So, there were – there are still a percentage of people that didn't feel comfortable going out even as Delta kind of waned and people thought maybe COVID was kind of done at that time.

And so we're still seeing guests that are coming back and there'll probably be some more that come back. We're still a little skewed. If we think about our skew of demographics, we're still a little bit lower in our mix of those over 65 because, I think, they felt a little bit less comfortable, but that mix is getting better.

And in terms – I forgot the second part.

Kevin Kalicak
Senior Vice President-Finance and Investor Relations, Darden Restaurants, Inc.

A

Geogrpahy.

Jake Rowland Bartlett
Analyst, Truist Securities, Inc.

Q

[indiscernible] (01:09:17)

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, in terms of geography, we're – the geography piece – I'm sorry – yeah, I don't think we're going to get into the geography in just three weeks, right, quarter-to-date. I will say that the geographic impact in Q3 were much more related to Omicron than they were for anything else, depending on what that geographic region felt about COVID versus not, but not getting into kind of the gas prices in just a really short period of time because they're already – the gas prices kind of moved up and moved down a little bit over those three weeks.

Jake Rowland Bartlett
Analyst, Truist Securities, Inc.

Q

Got it. And just a quick follow-up. I think there's more concern about the lower-income consumer. And Gene, you mentioned [ph] just that's with the low-income (01:10:01) consumer seeing the most wage inflation. So, I appreciate that offset. But are you seeing any differences in maybe in quarter-to-date or February in terms of the types of consumers that you're exposed to? Any insight there as to whether there's – one is a little more wobbly than the other or whether they're kind of all performing about the same?

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Yeah, Jake, we're not really seeing a big material difference in consumers through February, March based on anything that's going on in the geopolitical environment or what's going on with inflation.

Jake Rowland Bartlett
Analyst, Truist Securities, Inc.

Q

Great. I appreciate it. Thank you.

Ricardo Cardenas
President & Chief Operating Officer, Darden Restaurants, Inc.

A

Sure.

Operator: We'll take our final question from Nick Setyan with Wedbush Securities. Your line is open. Please go ahead.

Nick Setyan
Analyst, Wedbush Securities, Inc.

Q

Thank you and thank you, Gene, for all of your wisdom throughout the years. My question is specifically on just lead costs, given the importance of pasta and bread. It would be just very helpful if you could frame your exposure in some way, whether it's a percentage of the food basket or this is the kind of pricing we would need to take to offset it. Is there any way you can frame your exposure if we should be worried about it?

Rajesh Vennam
Senior Vice President, Chief Financial Officer & Treasurer, Darden Restaurants, Inc.

A

Yeah. Nick, maybe I'll just dimensionalize it for you. When you look at our food basket, wheat makes up about 7%; call it, 2% to 3% is pasta related; and then the rest is bakery and bread. So that's really where the exposure to wheat directly is. We're continuing to see what happens in that market, and we'll work with our vendors to just make sure we get the best price we can in the environment we're in.

Nick Setyan
Analyst, Wedbush Securities, Inc.

Q

Great. Thank you.

Operator: And with no other questions holding, Mr. Kalicak, I'll turn the conference back to you for any additional or closing comments.

Kevin Kalicak
Senior Vice President-Finance and Investor Relations, Darden Restaurants, Inc.

Thank you, Jess. That concludes our call. And I'd like to remind you that we plan to release fourth quarter results on Thursday, June 23, before the market opens, with a conference call to follow. Thank you all for participating in today's call.

Operator: Ladies and gentlemen, that will conclude today's conference. We thank you for your participation. You may disconnect at this time.