Turbulence Ahead for Restaurants-Strategies for Navigating the Storm and Beyond

Company Participants

- Gary Levy, CPA - Hospitality Industry Practice Leader, CohnReznick
- Michael Halen, Consumer Analyst, Bloomberg Intelligence
- Mike Lukianoff, Chief Analytics Officer, Fishbowl
- Pete Bell, Senior Vice President of CRM, Fishbowl
- Unidentified Speaker

Presentation

Michael Halen {BIO 18797919 <GO>}

Welcome to the Bloomberg Intelligence and Fishbowl Analytics Restaurant Webinar; Turbulence Ahead for Restaurants-Strategies for Navigating the Storm and Beyond. I have the pleasure of being -- my name is Michael Halen, I'm a Restaurant Analyst here at Bloomberg Intelligence, and I have the pleasure of being joined by Mike Lukianoff, who is the Chief Analytics Officer at Fishbowl; Pete Bell, Senior VP of CRM at Fishbowl; and Gary Levy, CPA. He is the Head of the Hospitality Industry Practice at CohnReznick.

So, quickly a few housekeeping notes. Today's presentation will be recorded and will be available for playback. At the bottom of the slide window, you'll notice that you can adjust the volume and maximize your screen. We recommend you do so for best quality. Feel free to ask questions using the Q&A panel to the right of the slides. We will address questions at the conclusion of the presentation. And a copy of the slides will be distributed via email following the presentation. Additional questions can be sent to bievents@bloomberg.net.

So, for those of you that aren't familiar, Bloomberg Intelligence provides analysis and context on different industries, companies, government, litigation, economic and credit factors. It's Bloomberg's in-house research product. We provide broad coverage and tons of data for our clients. BI EATS GO is where you can find our restaurant analysis.

So, I'll give a quick industry backdrop before looping in our esteemed panel. So, according to MillerPulse data, restaurant industry sales have been in a slide since posting a strong weather-aided result back in January. Two-year stacked same-store sales have fallen sequentially in five out of the last six months as consumer budgets are crimped by higher rent, healthcare, student loan and mobile and Wi-Fi costs. On top of that, the gap between eating at home versus away from home hit a record high.

This is motivating cost-conscious consumers to cook for themselves and bag their lunches instead of visiting restaurants. The gap is being fueled by higher wage rates across the country. Restaurants are labor-intensive as we all know, so this puts them at a disadvantage to packaged food manufacturers that can aggressively pass cheaper commodity costs onto their consumers.

Many restaurants faced with a higher waste cost, opted to raise menu prices, and we think that's a large reason why we are seeing this drop in restaurant traffic.

Discounting is persistent and shows no signs of slowing. Some fast food chains that have been trying to move away from low price value deals like Wendy's and McDonald's are seeing an immediate slip in traffic. And finally, baby boomers, they're retiring, and they're starting to live on fixed budget, so this is creating another headwind. It should curb discretionary spending from this mash -- from discretionary spending from this generational cohort, putting greater pressure on restaurants and, in particular, casual dining.

So, Mike, it doesn't look great out there. How did restaurant chains survive downturns in the past and what's different this time?

Mike Lukianoff

I think that if we look at the industry and we sort of separate out, say, the large national chains from, say, regional and local independents, if we think of how the large national brands have reacted to downturns in the past, really the playbook was, go on national media with big discounts, backfill some of your weaker markets to prop up traffic, and do some cost-cutting, right. And really that national media would really help them to be able to keep their head above water. Meanwhile, the local and regionals who's more of a defensive play, so, yeah, they didn't have those kinds of budgets to be able to compete, so they've really batten the hatches, play cost control.

What was different was -- what's interesting is that the other -- in the past, it's been really -- it was really the age of the big national brands, and what we've been seeing is that a lot of the small chains and regionals have gotten lot more prominence, largely because of so much more localized media. So, through whether it's social or local, digital and so on and so forth, they're able to compete more at a local level, which I think is going to be interesting to see how chains are going to be able to use this -- if they use the same playbook, or are they still going to be able to prop themselves up, or are they going to continue to lose more share to these, say, super-regionals and locals.

Gary Levy {BIO 17914334 <GO>}

And then if I could just add to that, I mean, consumer tastes are changing and I think it's all about staying relevant, right. When was the last time you haven't been in an independent restaurant where they didn't have (inaudible) on the menu, right. And that's what consumers are wanting. The demographics are all changing as you were saying. So, you have to stay relevant or you are going to lose market share to people who are on top of it.

Michael Halen {BIO 18797919 <GO>}

And which is also the question of the discounting, right. So we still see, for about 10% of the population, they're very active in responding to discounts, but call it 90%, maybe 80% of the population may -- everybody likes some price off, but it's not necessarily the primary motivating factor.

When the chains, especially locally that are looking more at what the experience is and changing the experience and adapting to tastes, aren't as subject to having to do with the price discounting, which really commoditizes these brands. So, when you see the big discounting across the board, single message nationally, they're really commoditizing themselves and leaving themselves open to those change that you're talk about, Gary, that are much more relevant within their local trade areas.

Gary Levy {BIO 17914334 <GO>}

I agree. And discounting takes all forms. There are discounting available for the independents, so that large chains can do it for the 2 for 10s, but you see companies like Groupon as a way to get discounts in independents. Sorry for going off topic.

Michael Halen {BIO 18797919 <GO>}

No, no, it's great. So, to continue on that topic, Mike, it seems that, like I had mentioned, most fast food chains are having trouble moving away from these low price points, but we all know this isn't sustainable. So how do restaurants manage their pricing and promotions to kind of gain some share in this type of an environment?

Mike Lukianoff

Well, I think it starts with recognizing who your customers are, who will respond to the discount. Brands that get in trouble are the ones that try to rip off the band aid all at once and say, oh, we're too dependent on the discount, so let's go cold-turkey, right. That's a sure formula for disaster, because the truth is, years of doing the discount, you've trained your customers into a certain behavior, and in fact you've increased the customer mix that responds to the discount.

If you can get more attuned with, say, contextual advertising on these kinds of things, understanding what people want to buy, what their tastes are, and go more to the total experience, and bifurcate who is responding to what kinds of discounts versus who is responding to experiential offers and that kind of thing, new -- be the first to taste our new limited time offer product, these kinds of things. New technologies and new media channels are enabling this. So, you don't have to do the blanket across the board 2 for 20 or what have you, where everybody gets a discount just for continuing their normal habits.

Michael Halen {BIO 18797919 <GO>}

So, Gary, in your experience, what are the best practices for restaurants when the market turns?

Gary Levy {BIO 17914334 <GO>}

When I think about that, to me best practice is the best practices. You should be doing that consistently throughout your business, right. And, since we come from the math side, staying on top of the numbers on a regular basis, having your team all growing in the same direction, being very conscious and aware of what your core values are in the marketplace.

The differentiators may be, if the market turns, I'm not going to be as experimental, maybe looking at what's really performing well on the menu, not add things that are different or new, maybe looking closer at cutting back a position where I can just to pay more attention to strategy of where I can maximize dollar. If I have the menu item that the chef loves or -- but no one is buying it or it's labor-intensive, maybe I eliminate that to focus more on the dollars. Where -- when things are really well, all right, we'll leave that on. So, you got to stay true to best practices, good governance, good communication. No matter what's going on in the macro environment, you just may have to sharpen the pencil a little bit more as you go.

Mike Lukianoff

Yeah. And, I think, Gary, the thing that you also need to focus on, as you said, you got to stay to your best practices. The worst mistake, though, you can make is when the quality of the product you're delivering, because of the size of the menu, is not what the guest expects, as well as the service, because in these downtimes, when people have limited dollars to spend each month to dine out, they want to make sure that that experience is a great experience. They don't want to have buyer's remorse, because the service was off or the quality of the food was not what they expected.

Michael Halen {BIO 18797919 <GO>}

Pete, during sales slumps, marketing spending tends to get cut, especially in franchise system, so how can restaurant companies most effectively target their customers and optimize their ad budgets?

Pete Bell {BIO 18904324 <GO>}

Yeah, I think the first thing that restaurants need to do today is really understand who their guests are. And when I look back in my career, even going back five years ago, we didn't have the data resources we have today or the analytics companies that could help us to pull that data together and to understand it to truly understand who our guests are. So, I hope -- I feel that that's a starting point. Before you just go in and start slashing budgets or optimizing budgets, just make sure who the guest is.

It's not just that media buying demo like adults 25-54, today we can understand not only demographics, psychographic, life stage, media, channel preferences, et cetera.

So, by understanding this, instead of slashing budgets, we can go in and really optimize the budgets, right. We can still use television and radio, but the right channels are right day parts that our guests are interacting with, and also with all these new channels that are available to us making sure we're on those channels that our key guest segments are engaged with.

Michael Halen {BIO 18797919 <GO>}

And with the declining sales, do you think some of these chains should look at cutting their marketing budgets or should they focus more attentively on getting that media mix optimized?

Pete Bell {BIO 18904324 <GO>}

No, I definitely think it's getting that media mix optimized. I mean, what we've seen in the past is that the brands that continue to spend can improve market share versus those that cut the budgets. And, I mean, cutting the ad spend, basically you're taking yourself out of the guest consideration set, right, you've gone dark on it.

I think really what it comes down to is, reevaluating your media mix, so you can get more effective and efficient in reaching them. So, again, as I said, it's, are you buying the right stations on television or radio or the right day parts. Move dollars out of some of those traditional mediums and move them into the non-traditional new channels that are out there on the digital online world. Even when you think about what you do as a company with SEO and keeping yourself out there, I mean, all generations, young and old, they're all using the Internet to research purchases. So, you need to constantly be out there in front of your guests or someone else is going to grab them.

Mike Lukianoff

The old adage in media is, I know that half of my marketing budget is working, I just don't know what half, right. That's in an age of lack of data and information, right. The whole world has changed, right, that's not an excuse anymore, right. I mean, people have started building media mix models 20 years ago, right, and the data has just improved over time. As we get new channels with more robust datasets, it becomes predictive. There is no longer the excuse to say, I don't know what my media budget is doing, right.

So, I think that -- and there are chains that do it very well, but there's a huge swap of the industry that really isn't even collecting the data, having the discipline to analyze it, to really understand what the return on one of their largest expenditures is. So, I think that that's a huge opportunity. Downturn or upturn, it's a big opportunity to optimize.

Pete Bell {BIO 18904324 <GO>}

Right. And I mean, I think, Mike, most brands today don't have the kind of budgets that -- if you look back 10 or 15 years ago that they had to even going with that mentality of half of my advertising is working, I just don't know which half, right. So, the more kind of laser focus you can get in reaching your guest is the approach that's going to get you the best results.

Gary Levy {BIO 17914334 <GO>}

And, Pete, you said earlier, know your guests, right, to stay on top of what your guests is? There were some great data analytic tools or something with the POS systems or some other companies that do this that can provide you great data on your guests, who that guest is, his frequency, when his birthday is, what bottle of wine he likes, so you can do strategic marketing to them. And without the media vibe of more strategic like in social media, and even email, if you're collecting that data, all right. I guess email is outdated now, so Instagram or whatever (multiple speakers) Snapchat.

Pete Bell {BIO 18904324 <GO>}

It's still in use, but I mean that's a perfect example. Today versus five, six years ago, think about all the different sources of data we can pull via online reservations. We have our POS, our payment data, we have loyalty program data, we have email data, right. So, we're pulling all of this data together, which some of it existed years ago, but we mostly looked at POS, we looked at things like menu mix where we're looking at high level traffic by day part, by day of week et cetera, we weren't really taking that data, pulling it together, and drilling down to understand who the guest is.

Knowing that guest, and when I talk to CMOs, most CMOs say their biggest pain point is they don't know who their guests are. Knowing that guest then offers up what you said, should I -- are we doing stuff on Snapchat, what media, what online channel should I be on, because if I know where my guests are, those are the channels on --

Gary Levy {BIO 17914334 <GO>}

And what strategies can I implement to draw them back in.

Michael Halen {BIO 18797919 <GO>}

Absolutely.

Gary Levy {BIO 17914334 <GO>}

It's more expensive to capture a new guest and to keep one that consistently comes back. And I think that puts candidly the independents at an advantage, because they know the community better than no one in the community. They know they're -- they are there saying hello to people who is working. If the chains can get the training to the staff about treating the guest that way, I think that evens the playing field, because they do have more dollars to spend on the strategic marketing.

Mike Lukianoff

I think the advantage of what you see with how people are messaging and the mediums they are using, think about it, the locals or these small regionals because of size of budget, they're forcing these new local channels, right. They have to do more non-traditional because they can't afford to do broadcast buys.

Pete Bell {BIO 18904324 <GO>}

I mean, let's face it, people aren't looking at their mobile device, standing in front of a Chili's to see what the rating of that Chili's is, right. They're looking at it to see if there's something better down the street, right. And now you can know that and you can trust it by these other -- whether it's Yelp or whatever the channel is, or Facebook or what have you, and what are my friends saying about something that's half a block away. And that's a challenge that used to be, I've got enough media to blanket the whole nation and say, I am this brand, and this is what I stand for. But now that's being accomplished at a very local level, right, a resurgence of the local independents.

Gary Levy {BIO 17914334 <GO>}

You are right. (multiple speakers) tremendously influential when someone is trying to make a decision, especially if they -- from out of town and they don't know that restaurant brand or name, right.

Pete Bell {BIO 18904324 <GO>}

Right. So, when you can actually get to people when they're going to make a decision, right, which is more and more becoming mobile, then you can influence that. Instead of just going to the TV and radio and saying, here's my blanket message across everywhere and I can get it for cheap, well, one thing I can predict, right, there's a few things that are predictable on restaurants, right, I can predict when you're going to get hungry almost every day, right, pretty well.

Gary Levy {BIO 17914334 <GO>}

(multiple speakers) much as 12 to 2, right.

Pete Bell {BIO 18904324 <GO>}

And I also can predict that if you're not within a certain proximity of a restaurant, it's not your consideration set, right. And those are the two most simple things that a lot of restaurants just aren't getting right and you're not going to accomplish that with the TV and radio, right, but you can accomplish this through phone.

Gary Levy {BIO 17914334 <GO>}

That's right, but that I think we are very in the infancy of where that's going to go and how that's going to happen, right.

Mike Lukianoff

But I think that again is getting to a point where restaurant companies are using data to understand who the guests are, because that's how you're going to reach them in that mobile device. You're going to reach them on the channels that they engage with every day on that mobile device.

Gary Levy {BIO 17914334 <GO>}

I agree with that.

Michael Halen {BIO 18797919 <GO>}

Gary, with so much of the industry being run by sophisticated investors, how do you think that's going to change the equation this time? From what you're hearing from your contacts, do you think chains are going to cut that cost and other expenses to hit quarterly targets, or are they going to continue to invest in the long-term health of the brand?

Gary Levy {BIO 17914334 <GO>}

I think that's a double-sided answer. I mean, if you're focusing on maximizing the return, because you are a public company and you've got to meet quarterly earnings for what you told the Street, you may make decisions to focus on meeting that short-term goal. The more sophisticated investors, the private equity funds, even the large independents that are multi-unit independent companies, they're focusing on the long-term, right, and we are not going to sacrifice to hurt our brand. We will invest back into our company if it's investing in human capital or reinvesting back in the site.

And we'll absorb a lower EBITDA return, almost like a hockey stick approach, because we know the long-term play is to keep the brand strong, take advantage of what's going on in the marketplace, and when things turn, we're going to be even better off, right. And I think that's the right strategy. Absolutely, the way -- if you want to be standing whenever the same-store sales come back, you have to do that, right.

Michael Halen {BIO 18797919 <GO>}

Do you think the private equity owned firms have an advantage over the publicly held, the portfolio backed by private --

Gary Levy {BIO 17914334 <GO>}

The ones, I would say like this, there are a bunch of private equity funds that really, really understand this business and they're investing in right now. They love the fast casual arena that are growth concepts. And when they make these investments in these growth concepts, they realize there's going to be a dollar investment in technology, human capital systems, because they are investing in the foundation of the business, no differently when you build a house.

You want a great foundation so that the thing can grow on its own. The great example I will think about is, you may have enough people to run a 20-unit restaurant company, do you have enough people to run a 200-unit restaurant company? And are those the right people and the right seats on the bus, right? And if you do that right in the beginning, think how easy it will be to open up more stores. Some restaurant chains, they open up 100 stores a day. I have clients that take some three years to open one restaurant. So that's a human capital, right, intellectual capital equation?

Michael Halen {BIO 18797919 <GO>}

So I would imagine this would create some opportunities for long-term investors in this space. So I guess what kind of opportunities can people with a long-term view look for in a downmarket?

Gary Levy {BIO 17914334 <GO>}

Okay. So, I don't know if there is a some way to answering that, there is a lot of talk about same-store sales being down absolutely. But I don't know if we're necessarily in a down market when you look at the valuations of privately-held companies that are doing transactions in the arena, because there's still a -- valuations are high, driven by the fact that there's still a lot of capital sitting on the sidelines.

So, from that side, I don't know how long that's going to take for that to change. I think that is going to change, because if the economics aren't working, people are going to pull back on the valuations, right. I've never seen a spreadsheet that doesn't go straight up. Projections, I'm still waiting for the one that shows the (inaudible) going back, right. You all think they don't. [ph] But the --

Mike Lukianoff

I am guilty of it too.

Gary Levy {BIO 17914334 <GO>}

I am aware of this -- everything is beautiful, which is a nice way to look at the world. But the -- what opportunities are there? And there are a lot of them. I mean, there is definitely an opportunity on human capital, finding great people, right, because they're out there, compensation is going to change, there's going to be an influx in that. So, there will be an opportunity, and you will see, I think, people who want to have great careers that are passionate about the brand that want to be part of a winning strategy and an exit -- leave to go to those brands that get it right, what's really relevant, what's hot.

Millennials, they wouldn't -- I don't want to -- they don't go to casual dining restaurants, because they don't want anyone know they are in there, right. But they'll go to the cool hip (inaudible) or a Tender Greens or any of those things that are really -- can seem to be really relevant and cool. They want everybody to know they are there. I see that with my kids all the time and they will never -- so, I think that's it.

The other thing is real estate. You'll see definitely some opportunities in real estate. Right now rents are astronomical. It's almost like, what, how much should I have to pay per square foot. That math doesn't work. But you will see those opportunities absolutely come out there in the marketplace, and you will see, I mean, there's still a lot of lenders in the space, there are lot of them.

And so I think you'll still see some opportunities to that. But you'll be able to renegotiate deals even with your vendors and go on and on about like these are the 10 things you should be really thinking about, but you can go back to your vendors, you can go back to your landlords, you can go back to your investor group and say, we have to make a strategy that aligns with (inaudible) core values and the economic platform, because we're building good to great, a quote of Jim, I'll just keep quoting him as a model [ph].

Michael Halen {BIO 18797919 <GO>}

Actually the clients will appreciate that. Mike, so off of that point, is 5% to 10% unit growth smart in light of today's real estate market? It would have been -- would some of these chains be better served maybe to pull back a little bit in light of sales sliding [ph]?

Mike Lukianoff

Yeah, I think, and especially as Gary was mentioning about leases, build-out cost and all that, there's such pressure for new unit growth, right, because everybody's projection these days, and to support the valuation, you got to have a lot of new units out there. We've done a lot of site modeling and what I'll say is that, it's looking a lot more like, I hate to say, but 2007 out there in terms of seeing the same chains, all the chains looking at the same sites and lot of competition to get into A, B and even C locations.

So I would say, be realistic about, first of all, what your projection would be for a new unit, and don't be afraid -- don't be afraid to pass on a unit where if you sit down and do the math on it, pass on it. I would venture to guess that in -- if you think of the people who signed leases in 2007 versus the people who signed leases in 2010, it was a lot more -- a lot easy to sustain something that was signed in 2010, right, and I think that things are looking a little top-heavy in terms of leases right now.

So, I think the smarter brands are going to figure out how to slow some of the unit growth right now, pass on the deals and wait for some of these that are going to -- I think it may come back to them when you start seeing some units that never made box economics sense start to close.

Pete Bell {BIO 18904324 <GO>}

I agree with that. I think you should be strategic in your site selection. You do have, and you also have the ability to go back to these landlords and say, especially in the larger shopping areas (inaudible). You want me in this place, right, you're going to give me TI money to build it out, sort of $20 a square foot, I want $100 a square foot.

So, it's going to lower my CapEx to get back into the store and help improve that return on invested capital, and I'm going to go back to the smart portfolio backed restaurants. The management teams are going to be very selective about what site to check. The thing is, they do have -- they want to grow, they have to grow, right. So, bunch of guys, similar brands competing for the same spot. And the smart landlords are like, yeah, we'll have this brand, if you don't want it, I'll give it to him, done. (inaudible)

Mike Lukianoff

Yeah, what I find interesting (inaudible) food chains publicly traded anyway are talking about cutting back on developmental or even, for example, Buffalo Wild Wings. Marcato, I thought did a nice job with their presentation, their Activist presentation for Buffalo Wild Wings, but that wasn't even brought up, which I found curious.

Pete Bell {BIO 18904324 <GO>}

Yeah, but if you read the M&M, which I'm sure you do, there's a lot of companies that are shuttering stores, a lot of them, which is normal course of business. I think that'll be a good thing in the long-run. I mean, I never like to see a business close, but I think that's the right thing and market share will be won by the more -- I think, relevant brands is what the consumers want.

Mike Lukianoff

And that's an important thing to think about too, right, is the relevance, right. When we start talking about -- so talking -- speaking of like box economics, right, so when we talk about wage rate increases and minimum wage and healthcare and all that kind of stuff, it makes full service dining, especially the -- as if casual dining and casual dining bar and grill didn't have enough to worry about, that makes the economics of that business even tougher.

Gary Levy {BIO 17914334 <GO>}

But also in fast casual, if you -- if we may, on the minimum wage, if you think about that, we're going to go from $9 an hour now in three and a half years or about three and a half years, it will be $15 an hour, minimum wage. So, most of those employees are fast-casual quick-serve restaurant people. Fine dining or upscale casual dining, most people in those restaurants will make more than that, and they may have to get (inaudible)

You're somebody -- if you were in today's world somebody working 55 hours at the minimum wages making like $5.60 an hour, I think is that number, three years from now that same person is going to be making over $900 an hour. That I've -- never in the history of the minimum wage have we seen such dramatic increases.

I don't know, Halen, we could spend some time talking about this too. How does a restaurateur or any business for that matter absorb such a high increase? You were going to have to pass on price. I don't know how you can pass it. We talk about technology, right, which gives a whole bunch of (inaudible). So, we're going to have that and I said this on our phone call, we're going to have the age of the Jetsons where you walk in, someone comes on the screen to take your order and it comes out by conveyor belt, which is not any place I want to go either, at least not now, but --

Mike Lukianoff

I think along the lines of passing on price, right, I mean, 10 years ago, any time there was a minimum wage, we kind of knew and have done a lot of price work over time, kind of knew when minimum wage increases were happening. It was a great time to actually pass on price. And more often than not, you could pass on 80%, 90%, even close to 100% of the wage increases through to price, because what was happening was that that lowest economic consumer was actually a big consumer particular to QSR and so forth. So, they had money -- more money in their pocket while prices were going up, so the economics kind of worked out kind of well, right, depending on where you were in the spectrum of food service.

What we're seeing now is a much different environment and we've seen -- we work with a lot of different chains, and even within the same chain, somebody who tries to pass on minimum wage one of these days and does it traditionally across the board pricing, all units going up at the same amount, they're getting pounded with traffic erosion, right. It's a more -- we've also seen, though, that if they can really strategic, not try and pass on all of the minimum wage, figure how to stage then over time, they can mitigate a lot of the potential traffic erosion and keep some of that. But the problem is, they still can't get a 100% of that through. So there's got to be other strategies that need to be employed.

Gary Levy {BIO 17914334 <GO>}

Especially your point that you made earlier that consumers are going to say, all right, I'm not going to go out, I'll make it at home, because there's such a big differentiator or I'll trade down from table service to fast-casual.

Pete Bell {BIO 18904324 <GO>}

Yeah, that's what we saw in 2009, right, fast-casual bled casual dining, because people traded down. And I think part of that, Mike, is not just what we took in price, right, that eroded traffic, but the other areas where you could start to cut cost in the quality of the food, right, the food cost, lower those and the labor. So, the service -- so it's sort of a double-edged sword, right. If you don't want to take it all and pass it through on price, and you cut other areas where the quality and the service now begin to deteriorate, it's going to erode the traffic as well.

Mike Lukianoff

Well, and you start to homogenize the line between fast-casual and casual dining, right, because the more -- if I walk into a fast-casual, I sit down at the table and I can order there and the food comes out to me, what a great experience, I'm real happy, right, you are just elevated and I might even be willing to pay a little bit more for that, right. But if I walk into a full service, place where I expect the waiter to come in, I sit down and I place my order on a tablet, right, and then I pay on the tablet, if I want my server, I've got to press the button that lights up and says, somebody wants you over here, right, that just -- that was just a major step down (inaudible) with it. Yeah.

Pete Bell {BIO 18904324 <GO>}

Right. That's like, right, the exponential differential.

Mike Lukianoff

And in fact, you may -- the service may also -- may still be a little bit better, right, one or the other, but in terms of what your expectation is --

Gary Levy {BIO 17914334 <GO>}

Guy on the tablet screen is politer.

Mike Lukianoff

And what the price differential is, right. And that's going to be a real challenge. People who are going to get hit, going back to relevance right, are the people who can't culinary keep pace, right, decide to battle minimum wage and overtime rules and so forth, is going to have all part-timers, right. So, okay, so now instead of having 25 full-timers who know what they're doing, I'm going to get 50 people who don't know what the heck they're doing, right, lower my service and to get around --

Gary Levy {BIO 17914334 <GO>}

Unemployment is pretty low right now, right, unemployment is 5% below. I think one of my clients said, they got the problem with 5% of unemployment, that 6% of the population should be working anyway. Not my quote, someone else's.

Michael Halen {BIO 18797919 <GO>}

So what do you think we'll see, between proposals for $15 federal minimum wage and one of the candidates wants to see the tip wage rate eliminated completely, how well these -- if these policy changes are made, what do you think the impact is going to be? Are we going to see more technology in the restaurants or are there going to be capital investments in kiosks and server handhelds and the like?

Gary Levy {BIO 17914334 <GO>}

The answer to that is, you're going to see a lot. Yes, absolutely technology will be in the marketplace. Somebody sent me a link to a video of a robot flipping burgers, and I was thinking, wow, right. That burger can -- it shows up, never calls in sick, don't have to give him benefits, right. I don't know how expensive it is to buy the robot, but I think that's something you'll see.

And I don't know what's going to happen with the tipping. It's still like there are some restaurateurs that are trying very hard to change that mix, and I think they're getting very mixed results from the consumers that just are not ready for it. But the difference between what a server makes and what a cook in the back of the house makes, there is a big differential there. And I don't know how much longer that's going to -- I think at some point that's going to change, because the millennials who order on their phone, they're not used to tipping, the people who are used to tipping are the baby boomer generation, right.

Mike Lukianoff

The smart brands, right, are the ones who use technology to enhance their surface, right, and enhance the --

Gary Levy {BIO 17914334 <GO>}

And run their business, right.

Mike Lukianoff

This is so much me-too in this industry that people say, oh, they just got this loyalty program or this app or this whatever, and they're not really thinking about what the features are that are actually improving the experience for the customer, because at the end of the day, that's who is going to win, right. If they actually know what their customer experience is from beginning to end and figure what those pain points are and alleviate those, but then invest in the areas that actually elevate the experience, they're going to do better, right.

The nice thing about the kiosks and so forth, so if you eliminate that pain point at the end of the meal, where's my check, right, I got to go, right. That's a nice pain point that's being alleviated, but if I can't find my server until I press a button that sends up the flare to say, please come and help me, because I can't figure out how to order another --

Gary Levy {BIO 17914334 <GO>}

Pete was talking about, I don't think any of us know how to work the kiosk when it's (multiple speakers)

Pete Bell {BIO 18904324 <GO>}

But that's generational, Gary.

Gary Levy {BIO 17914334 <GO>}

I give the credit card to my son; please, pay. So I think who knows what's going to happen. I think the minimum wage is going to be a very big issue that's going to cause inflation for the industry, but that's not just for the restaurant industry, that's every industry, right. So commodity, of course, I assume are going to have to go up too, because the guy is providing me my meat, or my linens.

Mike Lukianoff

But it affects us more, right, because when -- to Michael Halen's point about the lowering food at home, right, grocery prices are going down, because they don't have as much (multiple speakers)

Gary Levy {BIO 17914334 <GO>}

We want [ph] that go up, because -- we want that go up too, because they're buying from suppliers, they'd also have to pass on increases?

Mike Lukianoff

Not by as much because it's being held down by the commodity deflation. Right now we see wheat prices are at record -- excuse me, wheat supplies are forecasted to be at record levels, right. So this unusual food deflation, the more it increases the gap between eating at home and restaurants. When there's a narrow gap, there's not really a choice, but especially when you get into that lowest economic segment, right, the QSR discount responders, they're going to eat more at home, right. But even if you get into some of the --

Gary Levy {BIO 17914334 <GO>}

-- casual or fine dining, I was with one of my clients, went to a couple of restaurants and we were talking about this. I guess, look, eating out is expensive. It's like -- it's not like I'm making any more money, I have no choice. That is, it's expensive to go out and eat. (multiple speakers)

Mike Lukianoff

So, you look at the NPD report that came out yesterday on lunch, right, our department (inaudible) people are cutting back on lunch, right, some of (inaudible) deciding that it is pricing, they're doing more bag lunches, these kinds of things. It's going to be -- it's not necessarily going to be across the board, but you need to be able to recognize it as an operator as to what's price related, what's service related and what do we do to combat it.

Because if we just (inaudible) on what the competitor across the street is doing, and doing what's right for you and your customer, it comes right back to what (technical difficulty) know who they are, know what motivates them to come in and tap into those things, because this (inaudible) message doesn't work anymore.

Pete Bell {BIO 18904324 <GO>}

Well, I think the other thing too, Mike, is, with brown-bagging it or not coming in and I also think especially the larger chains (technical difficulty) to step back. And you touched on this earlier, you talked about the culinary capabilities in the restaurants, it's, are you offering today relevant food items, right. And then there's different flavor profiles, healthy items, right. Items that are good for you. We hear this all the time, farm to fork.

Is that another reason why people are trading off with a brown-bag because they want something that's (technical difficulty) these younger millennials are more food (technical difficulty). They are looking for something that's more flavorful and more relevant to what they're searching for versus going into a casual dining chain is not really going to have those offerings.

I mean, it seems like, just a couple of years ago, it was like groundbreaking that casual dining chains put sriracha on the menu. I mean that's a sauce, come on, we are behind the time. That's where fast-casual, I think to your point, Gary, the independent chains are doing so well, right, because they're developing and creating those relevant good-for-you, healthy items.

Mike Lukianoff

But there's also -- when you look at the big chains, right, it's also got to be about execution. Can they execute it in scale, right, and can they execute it well in their individual locations? I wish that half of these brands would stop -- go back to serving just iceberg lettuce as a salad, right, because they don't know what to do with mixed baby greens. You can taste the biggest -- popped open a bag of (inaudible) and dumped it in a bowl or you can taste the detergent on it, because they don't know how to execute it well, right. Whereas these local concepts that specialize in it, they can give you something that's actually appealing, not just looks like it's what you've heard about.

Gary Levy {BIO 17914334 <GO>}

Let us focus on just -- sometimes the economics won't come into play. The foodies, the chefs that create these things, they are about, I want the best salad possible. They are going to eat that salad and go, wow. Then I'm thinking about what to charge you, what it cost to make. As I'm lucky to be at some of the best kitchens or put some of the best chefs in it, I watch them sometimes throw out, they go right into the salad bowl and they would throw out lettuce that they don't think is fresh enough or good enough, right. They're not thinking. I am like you just threw out a lot of money. I'm like, get out of my kitchen. They just want -- it's got to be the best.

Mike Lukianoff

Well, again, I think one of the things you will find with the larger chains is that the days of having chefs in the kitchens, scratch kitchens, for the most part are gone. In 2009, and the recession did, and we started cutting costs. I mean labor, who's in the kitchen, we leaned on vendors for value-added items. So, as product comes in, we warm it, slice the bag, plate it and send it out into the dining room. You wouldn't see that in an independent.

You don't see that when you're standing in line at a fast-causal and you're actually customizing the meal with fresh ingredients that are laid out in front of you. So, there's a big difference when you think about what the independents are doing. I mean, it's tough for them too in these times, but the product and the quality they're delivering and the experience as well as what fast-casual is doing, right, that same experience and the quality of the items and the broad flavor profiles they're delivering are definitely eroding like casual dining segment.

Pete Bell {BIO 18904324 <GO>}

You know it's funny you talk about it, because you think about how much the media has played into creating chefs that are celebrities now and how much they're driving taste. They are really taste change agents, is that the right word? Tastemakers to the consumer's (inaudible)

I forget who said this, but I remember (inaudible) someone has said to me people think about eating more than anything else in the day, right. They think about -- eating is like the number one thing, which most men will like, sure. But -- and so that's very relevant. They think about what they're going to eat, they're going to care about it, it's no longer (inaudible). And then the other thing you said, you're thinking about how the kitchen has changed and you don't have chefs and they truly -- if you think about a technology shift, the chains traded cooks or chefs for microwave, right. So now that's at play and you see how that worked out.

Mike Lukianoff

And a lot of hotel don't have the kitchen. (multiple speakers). They don't have the kitchen or the expertise or anything else to actually be able to execute something that's a more aspirational menu, right. So they put it out there, because it tested well on a focus group, but then when they try and roll it out to the system, it's a disaster.

Gary Levy {BIO 17914334 <GO>}

But (inaudible) this webinar is about what can you do when sales are dropping, declining. What can you do? And I think the message we're talking about is, you got to be relevant, what's the relevant food, and how do you communicate that to your guest. And I'm using the word guest, not customer. How do you communicate that to them, to have them come, to continue to come in, right, that's really the strategy.

Mike Lukianoff

Absolutely. But know what you can do, right, not -- know what your brand is capable of executing, right, because at the end of the day, that's where you're going to win is at the location level, the days of top-down management of a large chain. It's not working that way anymore, you've got to really know what you're doing down at the location level and execute.

Gary Levy {BIO 17914334 <GO>}

And you can get that (inaudible) you can get everyone rowing in the same direction.

Mike Lukianoff

Absolutely.

Michael Halen {BIO 18797919 <GO>}

We spoke about it a little bit before offline, but even bad chains can generate some cash flow, right. So, what smart strategies can restaurants implement immediately to kind of free up cash flow, and outside of the tech investments that we spoke of, what should they be doing with their excess cash?

Gary Levy {BIO 17914334 <GO>}

When I used to run a seminar about like how to maximize cash flow on a restaurant, I would be like, what's the quickest way to -- what's the quickest way to pick sales or raise sales -- raise prices, right. That's simple, no-brainer, what's the quickest way to cut labor cost. People can mail the suggestions like, fire people, right. That's quick. That is not the right answer clearly. There are things you can do strategically. I talked about it earlier, knowing what's labor-intensive, what doesn't make money and produce, trim your menu. I remember Julia Stewart talking about when Applebee's had so many menu items, you really got to keep it simple, so you can execute really what's good and cravable.

Some of the things to think about in reality is, some restaurants carry decent size inventories, trim your inventories, see what's out there. Look at your budgeting and cut back on your spending, but also -- and this, a lot of people don't do this, communicate with your vendors, your investor group, your partners, your landlord and be very clear, hey, this is where we're going, you need to support me through this, right.

If you have a policy of making X dollar distributions to your partners every month or every quarter, maybe go back to them and say, we're not going to do that now. You go back to your landlord and say, you know what, I'm really tight this month, I got to choose between making payroll and making rent. Can I take that rent and make it up to you over in the next couple of months as a tail of the lease. Cutback on maybe some CapEx.

Those are the general things you can think about, but you need to have really good core communication. I'm always going to go back to -- you got to have the teamwork, but if you're running the business using the numbers as a beacon, right, you're going to have -- I always am a big fan of flash reports, every week they get a flash report and they talk to management about 15 minutes about what's happening, and people are very aware. If we're trying to hit a targeted throughput, this is how much you get to spend this week. If you need to go over, we need to approve it, don't just haphazardly do it. Trim the things that you can, trim the (inaudible)

Mike Lukianoff

But I think you also need to keep in mind when you're doing that trimming is, what is the impact of those cuts going to have on the guests coming through your door.

Gary Levy {BIO 17914334 <GO>}

Absolutely.

Mike Lukianoff

Right, because I have been with brands where we cut and we cut deep, and traffic declines have just escalated. And so it's one of those things that I think you'd always have to keep in mind that guest, because there's so many choices today.

Pete Bell {BIO 18904324 <GO>}

All right. I absolutely agree. You need to be -- you are going to have to have a -- you got to be strategic in all the decision you're making here. This is -- we talk about it like it's so easy. Honestly, this is time-consuming. No one -- everyone, at least my clients, they don't want to talk about money. It creates anxiety for them, right. Even I get anxious talking about their money. So, it's something you have to pay attention to because this is a business.

Then, if everybody is rowing in the same direction, you make that focused choices; some will work, some won't. But make sure -- it's always important, and I think that communication is good. If you have lenders, communicate with them, because they may be a source of cash when you need it. If you have that great hire that you really want, right, go find the dollars to hire that guy, because he'll payoff in the long run. I have no magic -- no magic bullet for --

Mike Lukianoff

No, I'm a data guy, so I'm going to have a bias, but I really do believe that the companies that are making fact-based decisions based on data are making better decisions, right. You're not guessing whether, oh, was it the weather, was it that promotion, was it our service levels, all this stuff is knowable, right. The data is out there. And, in fact, a lot of those sophisticated models aren't that tough to execute if you've got the data. So, it all comes down to making sure that you've got the right strategy around accumulating the right data that's going to -- and you set up the whole -- your whole data program with certain goals in mind that you're trying to -- that you can actually know you can get a return on investment on, right.

So, whether it's optimizing your media, whether it's price optimization, right, these are things that are very tangible and measurable, right. And once you've got the datasets that can actually help to fuel that, then you can apply that sort of a data-driven culture across the entire company.

Gary Levy {BIO 17914334 <GO>}

I agree with that. That's a -- I mean, I think that just goes to best practices, pick the right data, use it efficiently, pay attention to both macro and micro. Some people have always said to me, I can't really worry about the macro issues. I'm like, that's like taking a sailboat out when there's hurricane coming in and saying, I can't worry about that hurricane, right. You've got to pay attention to both and then implement with the right team.

Pete Bell {BIO 18904324 <GO>}

And I think, Mike, to your point with the data, it's really understanding your guest behavior when they're in your restaurant, what they order, when they come, how they use your brand. Gary, you talked about these restaurants getting huge menus. Look at casual dining, it's become the sea of sameness. It was probably a dozen at least menu items on casual dining restaurants, so they're not selling menu but a competitor has in one of their menus that they have. Those are the areas you can cut, but you need to understand your key guests, who they are, what those segments are in your restaurant, and what they're ordering. You don't want to cut those items.

But if you have items that have low sales, those are the items that you want to start to eliminate. And the problem is, everybody in casual dining has become just like everybody else. Mike and I've talked about it. If you took the trade dress off the menus and you look at the menus you probably wouldn't know what brand you're in.

Unidentified Speaker

And then the commodity, everything is commoditized and that's like [ph] -- and then that goes to -- that's a formula for not being there anymore. And that's in any business, mostly from the commodity and price wins, I mean, like what am I doing here in a zero-sum game.

But that's what casual dining does, right. As CFO of that I used to work with, used to call them T.G.I. Chilibees, because, you know, and no matter which one you went to is --

And then it's just -- then it's like a site selection, right. And that's why you see these great growth brands coming up, because they're really differentiated, right, specialized in salads, specialized in Mediterranean, specialized in burrito, right. You see that, because that's what the consumer of today and tomorrow is going to really want.

And we see the Boomers not eating out as much and you talked about, you know, these chef-driven culture. Well, millennials view themselves as foodies, right. We call them foodies, right. They are the ones that are searching out things that you're not going to necessarily find in casual dining, but you're going to find in these emerging brands.

You haven't noticed and you go to like some of these cooler, hipper places, while the kids are on their phone taking pictures of food and next minute it's like all over the web.

Yes. Does -- does a place like Blue Apron, is that a real threat?

Maybe to some of the brands out there.

(inaudible) replacement has been -- Mike talked about forever. So this is just maybe a smarter way to getting it out there. So Blue Apron is the smart there. There is another company called Home Chef, that's also getting that traction. So, it's been -- I think those things are out there.

You know, I mean, I often sit with my (inaudible) my oldest uses Blue Apron, and really it comes down to -- she is in law school, it's -- she is a foodie, she likes to eat out, she's a kid that's snapping, you know, she wants to have her own food Instagram site. But for her, you can order meal-specific, right, so she's not having leftover produce, leftovers that she's not going to use again.

So for her, it's affordable, but it's really that one-time meal all the ingredients aren't there. So, her cupboards aren't stocked with spices and she doesn't have all the produce that maybe a big household would carry. So for her, it's a really affordable way to have a very good meal at home without having to deal with grocery shopping.

Yes, it's easier.

It's like actual versus theoretical software for your own cupboard, right.

Exactly. It's almost like having the Jetsons in your own cupboard. I had the CEO of Ogo [ph] wants to do a webinar for me, and we made -- we were going to call the webinar, The Drones are Coming, and they say, you do order something on your phone and a drone would drop it off at your house fully cooked.

Chipotle and Virginia Tech.

Yes.

Chipotle is going to -- Chipotle grew on Virginia Tech, they're going to run an experiment.

Where you won't deliver by drone?

Exactly, I mean, I can only imagine the first time drones crash and fall out of the sky, but --

What's going to happen is you're going to have a bunch of beans and rice on your head.

My son says, it's absolutely going to happen. Like I just want the car that when I have to go pick him up late in that I can just send the car and I don't have to go again. That's called Uber I guess.

Michael Halen {BIO 18797919 <GO>}

Yes. All right. So, we'll take -- we'll take a couple of questions from our listeners before we wrap up here. So how different is the weight of labor cost in the overall structure of fast-casual versus full-service dining? So is the impact -- you know, is the rising minimum wage is going to -- is that going to be much more onerous on casual dining versus fast-casual.

Unidentified Speaker

I know the gentlemen who entered the question is that -- usually that's really bright and typically hard ones, but I think my opinion, I think that's going to be a more costly exercise for the quick-service fast-casual, because those are the people that are really making at the minimum wage more so than I think in the fine dining arena. But if I'm raising -- if I'm raising, Michael and you are above Michael in seniority and now you're going to expect an increase too, right. So --

So the tip wages problems will be something more, and tip [ph] credit could really change the entire economics (multiple speakers) casual dining that's --

And then the waiters make so much more than that, the ones in casual dining. I mean, they're making 20,000 30,000, 40,000 an hour. Remember, years back when no one was reporting tips or (inaudible), I was thinking, well, why am I going to college if I can make more money being a waiter. That's changed. But you know the tip credit I don't think there is any reason to take that away that hard.

And we spoke -- we spoke about -- talking about, you know, first, speaking with your landlord about rents, and one of our listeners said that, they've tried going to their landlord and -- who told them to pound sand. Do you have any recommendations or any magic words he could use next time he goes back to that landlord?

Landlord sounds like a wonderful guy, right, because internally [ph] you think about what he did, he probably levered up his building and needs your rent to pay his -- to pay down the mortgage. But I don't know enough about that situation, but you know this is almost like a game of who is going to chicken, who is going to bluff first, (inaudible) first.

If you have the -- I would check my lease and then be very clear with him about your financial situation is going to be like and if it's really, really tight, right, be slow on paying the rent, don't pay all of it. I mean, it depends what strategy you really want to take. I don't know if there is a magic word, if somebody just told you to go pound sand or jump in a lake.

And how can restaurant management and restaurant leadership help increase the emotional intelligence of their employees?

First thing, it would come down to -- to training, right, and making sure -- I think, make sure your employees understand what the brand stands for. You know like create that passion amongst the employees for the brand. I think, you know, we've all experienced going into a restaurant where you know that, that server is not just passing through, but it's a career and they're passionate, they're knowledgeable, they understand the brand and how many times have we walked out of one of those experiences, and we just keep talking about what a great experience we had. So, I think, you know, investing into the employees in the restaurant and really understanding the front-line is critical.

And hiring in the first place, right, getting the right people, the right people on the door and whole other [ph] --

Which means that you need to be the employer of choice, right, in your area. The ones who are going to get hit the most with say the minimum wage increases, right. So, paying all your employees a minimum wage, you're probably not the employer of choice to begin with, right. You know, the industry needs to do some hard thinking about, how do we figure out how to actually make restaurants a career again like it was (inaudible)

(inaudible) we're trying to do by eliminating tipping and sharing rents with the house, that it's now a career. And you think about that, I mean the labor question, the General Managers are the ones who really drive the successful restaurant.

You take a good General Manager and put him in a bad store, he'll make that store good. You take a great location and you put a bad manager who will own it [ph]. So, incredibly important. And there's such a bifurcation of what you're supposed to pay and be relevant in that arena and that's attractive. We're actually working on with a really large hotel chain right now to do a global compensation study to understand what's relevant in the local marketplace.

We've just started it. I can't wait to see what the data shows like, what is the differentiators of being able to attract people to come work with them, because I think at the end of the day, the food is got to be great, right. The service is got to be spot on. And if you have the right team that buys into your core value with great training, that's a huge win, right. You're going to go back there where that server knows you, that bartender knows you, rather than, you know, you notice, and I always notice this in the mornings. When I get up and I go to the men's room, and if there's a server like crossing my path, and I'm the guest, does he let me walk through first, does he walk in front of me.

Not that -- I'm just noticing and I see I know which restaurants where the server will say, please, they will always say, please go. (inaudible) no, no you go especially if you have a lot of food with you, but, to think you notice that stuff and most guests do, not just me, sorry.

All right. That was great. I want --

No question?

I think so. I think so. So, want one more?

There were some good questions, I'll take three, you're going to comment on three, maybe, Peter? Michael, we are out of time?

Michael Halen {BIO 18797919 <GO>}

Yes, I think we're -- I think our -- I think we hit our limit. So I want to thank you guys. This was absolutely phenomenal. Just to put a bow on everything. Number one, know your customer, serve relevant food that you can execute in your restaurants, and if we do see a downturn, you know, use it as an opportunity and get the best employees that you can possibly find. So once again thanks, Mike, Pete. Gary, this was great. Look forward to doing it again.

Unidentified Speaker

Thank you.

Thanks, Michael.

Michael Halen {BIO 18797919 <GO>}

This would be available via a transcript and audio and we will be emailing this out to all our listeners. So, thanks for joining us.