



QUARTERLY CHAIN RESTAURANT UPDATE

BELLWETHER FOOD GROUP, Inc.

DATE: October, 2013

TO: Manufacturing/Operator Friends and Colleagues

FROM: Bellwether Food Group

RE: Chain Restaurant Same Store Sales (SSS) 2nd Quarter, Calendar Year 2013

The 2nd Quarter 2013 Same Store Sales Reports

Cautious optimism began to emerge in the 2nd Quarter. There were more positives than negatives, with some brands showing traffic growth. The successful brands are doing a great job of engaging consumers in new, more relevant ways.

The familiar theme of new product news, excitement around the new products, combined with more contemporary tools, such as loyalty programs and digital apps, appears to be driving traffic and loyalty.

Regarding new product news, Taco Bell has had a big hit with the Doritos campaign - the most recent, the Fiery Doritos® Locos Taco - almost a brand within a brand. A 2% SSS increase isn't necessarily overwhelming on its own, but the important development is that the Taco Bell brand is healthy today. It wasn't all that long ago, 3-4 years, that many of the franchisees were struggling. Another one is IHOP's stuffed French Toast and pancake line extensions. These fit extremely well with what they're best known for and are *relatively* simple to execute.

In the cases of two other brands (Panera, Domino's), who had healthy quarters, we see more evidence that different groups of consumers want to feel a personal connection to their preferred brands *and/or* have all they need to order at their fingertips. At Panera, the loyalty program now has 14 million members, which represents roughly 45% of customer transactions - that's significant.

Meanwhile, Domino's projects \$2 billion in sales this year through its apps. The consumer sets up their own preferences in a "pizza profile." The operators like the apps for three reasons: (1) the ease and convenience for them; (2) they don't have to answer the phone as often; and (3) order accuracy is improved.

In our consumer insights work for chains - we are hearing consistently from consumers, across income levels, that they will spend discretionary dollars on restaurant meals. Eating out is still very much a part of most consumers' expectations. The key is that the entire experience has to

be "worth it" in the consumers' eyes. Meanwhile, unemployment and under employment numbers tell the story of a stressed consumer. So expectations are higher and there is less patience for an average or mediocre experience.

With a few exceptions, Casual Dining appears to be maintaining sales, and in some cases even growing traffic (Longhorn, Olive Garden), and experiencing what appears to be real growth. There are brands still struggling (Ruby Tuesday) - whose sales improvements have yet to rebound to pre-crash levels. Of course the key with any operator is growing traffic with current and lapsed users.

Most of the senior executives at casual dining chains see their biggest competitor as fast casual. Certainly, they recognize and respect the other players in casual dining, but fast casual is what keeps them up at night. The food offerings and environments are competitive, most are much newer facilities, and there's no tipping, leading to better overall value for the consumer. Those are real challenges for casual dining to overcome.

Ruby Tuesday's, led by Darden and Brinker alumni JJ Buettgen, has a relatively new management team, which appears to be focused on all the right things. As we all know, these changes take time to implement and have a measurable impact. We'll keep track of that one.

The higher end concepts, such as Ruth's Chris, Fleming's, and Capital Grill, are doing well. The higher end consumers are, for the most part, holding their own. We had the opportunity to chat with some of our friends in the higher end women's fashion sector, and they report strong traffic and sales.

2nd Quarter 2013 SSS Sales by Brand

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Limited/Quick Service				
Burger King	-0.5%			Closed 31 restaurants
Chipotle	+5.5%			
Domino's	+6.7%			
Dunkin Donuts	+4.0%			Agreement signed for 45 stores in Southern California
Jack in the Box	+0.1%			Qdoba +1.3% SSS
McDonald's	+1.0%			
Panera*	+3.8%			
Papa John's	+3.4%			
Popeye's	+4.4%			Lapping +8.4% from 2nd quarter last year
Pollo Tropical	+6.4%	+2.8%	+3.6%	

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Sonic	+0.1%			
Starbucks	+9%			Starbucks Card business appears to be a driver
Taco Cabana	+1.1%	-0.5%	+1.6%	
Wendy's	+0.4%			+0.3% franchised restaurants
Yum! Brands (US)	+1%			
KFC	+3%			
Pizza Hut	-2%			
Taco Bell	+2%			
Full Service Restaurants				
Applebee's	+1.3%			Higher check combined with slight traffic declines
BJ's	No change			
Bob Evans	-0.6%			
Bravo Restaurants	-1.6%			Plans to open 8 new restaurants this year
Brio Restaurants	-4.0%			
Buffalo Wild Wings	+3.8%			+4.1% (franchised) lapping +5.3% in 2012
Capital Grill	+4.5%			
Carrabba's	+0.3%			
Cheesecake Factory	+0.9%			
Chili's	-0.3%	-2.1%	+1.3%	
Chuy's	+2.1%	+0.2%	+1.9%	Portion of check increase appears to be favorable mix
Cracker Barrel	+2.6%	+0.6%	+2%	+1.9% price increase combined w/+1.1% mix growth
Denny's	+0.6%			
Famous Dave's	+3.8%			
Fleming's	+3.8%			
IHOP	+1.9%			Driven by traffic gains and check
Longhorn	+3.5%	+3.5%	+1.4%	Mix of negative 2%, offset by traffic & price increases
Olive Garden	+1.1%	+2.4%	+1.2%	Consumer check mix at -2.4%-equal to traffic gains
Outback	+2.8%			
Red Lobster	+3.2%	+4%	+1.2%	Mix negative-2.6%, offset by traffic & price gains
Red Robin	+4.3%	-0.7%	+5.0%	Some pricing, some positive mix shift
Ruby Tuesday	-3.1%			-5.1% at franchise locations
Ruth's Chris	+4.6%*	+2.1%	+2.5%	*Company stores, pricing primarily mix driven
Steak 'n Shake	+4.2%	+4%		
Texas Roadhouse	+4.5%			+5.3% at franchised restaurants

Implications for Manufacturers

One approach for a mature market is to pay more for better talent, which delivers better results over time. One of our manufacturing clients made the decision to ramp up their talent a couple of years ago. Today, they have five national accounts people doing the work that seven people used to do, and overall performance is much improved.

On the subject of talent, we are becoming advocates of re-thinking the sales coverage model that most food/beverage manufacturers use in covering the chain restaurant industry. Typically, most use a geography based model, or a relationship based model. Simply the accounts are divided based on geography (closest to where each NAM is based) or assignments are made based on who has historically had the strongest relationships with the key individuals in the power positions in the chain organization.

We're now recommending another, fairly different approach. The chain restaurant business is basically a mature business today. As such, we believe the legacy coverage models are outdated and no longer effective.

Today, we encourage clients to manage the business relationships based on the needs of the each specific customer, and the relative opportunity with that customer. Everyone has three types of accounts. They are transactional accounts, relationship driven accounts and non-customers or underpenetrated targets they believe can become customers. Simply put, our position is that these three types of accounts require a very different set of skills and characteristics.

We see three basic functional needs of sales talent in chain restaurants:

1. The entrepreneur, the **new business development** professional - someone whose assignment is to develop new business and relationships.
2. The **strategic relationship** manager - someone who can manage complexity, different buying influences and power levels within customer organizations, and internally as well.
3. The **tactical sales** manager - someone to work with purchasing, menu development and distribution.

The first group is the true business development professional, similar to an investment banker in knowledge, competence and skills. These individuals typically have no active customers, or very few. This is the person who is completely comfortable reaching out to the VP or C level, and having a conversation about their overall direction, focus, priorities, and strategy. These are the professionals who find the brand new opportunities, especially in a mature market. There's a group of successful manufacturers, who are already beginning to invest in this type of

talent. These are the firms who will be able to grow their business and margins in a mature market.

The second group is the strategic relationship manager, the typical NAM today. These individuals are capable, smart, accomplished, with the ability to manage complexity both internally and externally. They may be (if not, they need to be) completely comfortable starting a discussion with VP Marketing or concept President about the brand experience **they** strive to deliver, or the direction of the business.

The third group is the tactical salesperson. They think and talk about features, benefits, advantages, like a product seller. Based on your targeting and prioritization work, you know there are some accounts that are tactical and have very little chance of becoming true strategic partners. And....they pay their bills on time, the volume keeps the plant profitable and they're overall a good customer, one you want to keep running smoothly. They are those good people who are productive, but who won't ever evolve to developing the skills necessary to perform at a higher level. On the right pieces of business, they're the perfect fit, and they cost less than the higher performers.

Beyond industry maturity, we are invested in this approach for two other reasons. First, very few (if any??) sales people are good at all three of these functions. Second, it is very difficult to focus on all of these areas, and devote the time and necessary energy to do all three really well. Diligent hard working sales people will insist they can do it all!

Of course, these are three very different skill sets and compensation models as well. The new business development professional is focused exclusively on brand new customers, or new opportunities within existing customers. They are comfortable with the C level, and able to connect with, and resonate with, the C level executives. This is a unique, more comprehensive skill set than the typical NAM. As such, the compensation and overall strategy are much different.

Of course, when the business changes (like a transactional account evolving to a more strategically compatible opportunity), simply adjust the talent/resources accordingly.

We'll be publishing a white paper on this subject later this fall.

Regards,

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