QUARTERLY CHAIN RESTAURANT UPDATE

BELLWETHER FOOD GROUP, Inc.

DATE: April 2016

TO: Manufacturing Friends & Colleagues

FROM: Bellwether Food Group

RE: Chain Restaurant Same Store Sales (SSS) 4th Quarter, Calendar Year 2015

The 4th Quarter 2015 Same Store Sales Reports

Overall, the industry was fairly healthy in the 4th Quarter. Many brands continue to do well, while some are struggling. Pizza continues to grow with Domino's leading the way with a +10.7% increase, which comes on top of +11% in 2014. Papa Johns (+2.2%) and Pizza Hut (+2%) also delivered positive results. Papa Murphy's didn't fare as well, reporting a -3.1%.

In Hamburger QSR, McDonald's sales increased 5.7%, benefiting from the October launch of all day breakfast. Wendy's continues to gain traction as evidenced in the +4.8%, and Burger King continued their positive trends posting +2.8%. In what has to be one of the best turnarounds in recent times, Arby's has turned positive, showing an +8.1% for the calendar year 2015, on top of a +5.7% in calendar year 2014. All benefitted somewhat from the unseasonably mild weather.

Sonic posted a +5.3% increase (on top of +8.5% the previous year). Besides the product news and integrated customer engagement, they've continued with menu enhancements. Recently, "The Soda Pop Shoppe" was introduced. Among the offerings - cream sodas made with flavored syrups or soft drinks mixed with sweet cream, ½ price after 8 PM. This plays into one of their strengths as a combined 40% of their sales come in the afternoon or after dinner.

New product news and limited time offers are established tools in QSR. More recently, coffee continues to evolve as an important driver of breakfast differentiation. Sonic, not one of the brands typically part of the discussion in QSR breakfast, now has a branded coffee program (Green Mountain), and they're using that with a $3 breakfast delivered in 2 minutes.

Starbucks continues to hit on all cylinders reporting +9% SSS, 4% of which is incremental traffic. They lead in many ways, none the least of which is the technology platform. Over the Christmas Holiday, $1.9 billion was loaded on Starbucks Cards in the U.S. and Canada - 1 in 6 American adults received a Starbucks Card over the holidays, up from 1 in 7 in 2014. Their loyalty program is an industry benchmark, Starbucks Rewards ™has more than 11 million active members.

Technology's role in the consumer experience will continue to increase. Domino's recently described itself as a technology company that delivers pizza. The acceptance rates across the consumer spectrum, including baby-boomers is unprecedented.

The flagship Darden brands all had positive results. We see Olive Garden's new focus on take out (up 20%) and the value oriented Cucina Mia ($9.99). Recently, Olive Garden started a national delivery program for any home or office event for a minimum of $125. They've seen all the local independents enjoy that business for some time.

Cracker Barrel has focused on a value platform, with a $5.99 lunch plate, and a $7.69 Country Dinner plate, combined with the "Wholesome Fixins" line with entrees under 600 calories in all three dayparts. They've decided to give fast casual a try, opening Holler & Dash, a "biscuit inspired" menu. The first unit opened last month in Birmingham, Alabama. The menu includes innovation - organic apple juice, beer, wine, beignets, and a biscuit with bacon, guacamole and a fried green tomato. Interesting menu, we're anxious to give it a try.

Elsewhere in casual dining the environment continues to be tough. Bloomin Brands had negative sales and traffic at all three flagship brands. They've announced a number of initiatives including a "Re-Invigorating the Experience," remodeling the restaurants, along with plans to relocate potentially 100 Outback locations to better sites. Early reports are that the new location moves are generating a 20-40% lift in traffic during dinner. This makes sense, as local trade areas can change over time. Also, work with app upgrades include ordering/paying online, combined with waitlist and reservation enhancements are recent enhancements.

Casual dining has embraced the order and pay at your table concept. Pay at table has always been the case, but it is now using technology to do so, which is rapidly becoming the industry standard. Consumer expectations are shaped by the entirety of their collective experience with all the places they shop. Today, the consumer can track their package coming across the country thru Amazon, so now they expect the kitchen to know where their order is, in real time, and when it will be at the table. The standard "it should be here soon" response is no longer an acceptable answer.

If you're working with Brio/Bravo we advise caution. Traffic declines of 17% over the past three years, and no clear plan for reversing the decline, will mean issues for some of their vendors.

The amount of work and money to support declining sales with a customer strains all concerned. For Brio/Bravo, the challenge for now is keeping the best talent in the store. The best servers, bartenders, and others are going to go where the best tips are. For managers, who earn bonus on sales increases, this makes life very difficult. So the guest experience suffers. The same realities apply to Famous Dave's.

Wage increases are happening, and for the time being the trends are going in that direction. Both the chain operators and the manufacturers are looking for unique ways to reduce labor. Of course, technology will play a significant role, especially in full service restaurants.

We don't see that technology will completely replace servers in full service, although that may evolve over time. What we do see is the servers using the pads to communicate internally to input customer orders (and then only once - the kitchen and bar get the orders at the same time the waitperson actually takes them).

This saves time and labor and improves the customer experience. In most full service restaurants today, the server takes the customers' order and then has to enter all that information **again** manually, into the back of the house system in the restaurant. The tablet technology eliminates that second step. This will minimize errors, speed up the overall dining experience, and allow the server to cover more tables at a time. A separate food and beverage delivery person will bring most of the orders to the tables. For operators working to maximize throughputs during a busy lunch or breakfast rush, this can really help. We've already seen how well the right technology can improve both the customer experience and operations at Starbucks.

Over time, the servers will handle more tables and therefore make more in tips. The operator will have less people, which will save labor expense and health insurance costs. We don't make predictions, but the evidence so far strongly suggests that the minimum wages are going in only one direction for the next few years - up. California recently signed legislation that raises the minimum wage to $15 over a period of years.

4th Quarter 2015 SSS Sales by Brand

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Limited / Quick Service				
Arby's	+8.1%*			*full year 2015 performance
Bojangle's	+0.6%			
Burger King	+2.8%			US and Canada
Chipotle	-14.6%			-30% SSS in December; -29% in February
Del Taco	+5.8%			
Domino's	+10.7%			
Dunkin Donuts	-0.8%			
El Pollo Loco	+1.8%			
Habit Burger	+3.3%	-0.2%	+3.5%	
Jack in the Box	+1.4%			
Jamba Juice	+3.9%			
KFC	+1%			
McDonald's	+5.7%			All day breakfast a key driver
Noodle's	-1.1%			
Panera	+2.3%			

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Papa John's	+1.9%			
Papa Murphy's	-3.1%			
Pizza Hut	+2%			
Popeye's	+2.0%			Lapping +10.4% SSS
Pollo Tropical	+0.4%	-1.1%		
Pot Belly	+3.7%			
Qdoba	+1.8%			
Shake Shack	+11%			
Sonic	+5.3%			Lapping +8.5%
Starbucks	+9%	+4%		
Taco Bell	+4%			
Taco Cabana	+3.3%	-0.7%		
Wendy's	+4.8%			
Wingstop	+5.9%			
Zoe's	+7.7%	+2.8%	+0.4%	+4.5% product mix
Full Service				
Applebee's	-2.5%			
BJ's	+0.7%	-2.5%		
Bob Evans	-3.6%	-6.5%	+2.9%	
Bonefish Grill	-5.4%			
Bravo Restaurants	-5.2%			Combined traffic decline of -8.2% for both brands
Brick House Tavern	-2.8%			
Brio Restaurants	-4.3%			
Buffalo Wild Wings*	+1.9%*			*@ 596 Company stores, +0.1%% @ (579) Franchised
Capital Grill	+4.3%			
Carraba's	-4.0%			
Cheesecake Factory	+1.1%			
Chili's*	-2.1%			
Chuy's	+3.2%			
Cracker Barrel	+0.6%			
Dave 'N Busters	+6.0%			Lapping a +10%
Denny's	+2.9%			
Famous Dave's	-10.6%			Lapping -4.8%, on top of -2.6% in '13, -6% in '12
Fleming's	-0.3%			
IHOP	+1.4%			
Joes' Crab Shack	-2.9%			
Longhorn	+2.7%	-0.7%		
Olive Garden	+4.9%	+3.0%		

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Outback	-2.2%			
Red Robin	-2.0%			
Ruby Tuesday	+0.8%	-2.2%	+3.0%	
Ruth's Chris	+3.2%	-0.3%	+3.5%	
Steak 'n Shake	+0.8%			
Texas Roadhouse*	+4.5%			*392 Co. Stores ;+4.0% @ 82 Franchise Stores
Yard House	+3.9%			

Implications for Manufacturers

The challenges for the manufacturing community in casual dining are well known. Even with the more successful brands, it's a share capture game at best - for both the chains and the manufacturers.

One example is BJ's. The fact is that the 3 year trends with the brand are not encouraging for their supplier base. Simply, they're stuck in the casual dining conundrum. Given the maturity of casual dining overall, and the emergence of fast casual, how many more units can be built? The stated goal is to open 18-19 restaurants this year. The stated upside is a potential 425 restaurants on a base of 172 restaurants today. That seems aggressive - but even if they open 20 per year, that timeline is still at least 10-12 years.

For the suppliers, this means very limited growth opportunities, combined with pressure from procurement (which of course they get from the management team and their investors) to "manage costs" - which is code for "lower prices."

There's another discussion we've been having lately with our friends and clients in the manufacturing community. It revolves around one simple question. Is your sales and marketing organization focused primarily on demand fulfillment or demand creation? They're not necessarily mutually exclusive, but they both matter. Demand fulfillment is all about operating the business smoothly and keeping things moving in the right direction.

However, future success and revenues are much more a function of demand creation. To survive, every business has to invest in demand creation. This of course means new customers or additional penetration with existing customers, both of which are challenging endeavors.

What we're advising our clients to focus on is new, new business. The best place to look - regional brands that are on a growth trajectory (Habit Burger, Zoe's) or in fast casual. Admittedly, the volumes are much less today, but that is where we believe the future growth will be. You don't want to be where many Chipotle suppliers are today, experiencing 30% declines in sales from their largest customer, with a turnaround at least 1-2 years away.

We're happy to share our perspective in more detail, just give us a call.

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