



QUARTERLY CHAIN RESTAURANT UPDATE

BELLWETHER FOOD GROUP, Inc.

DATE: April 24, 2015

TO: Operator Friends and Colleagues

FROM: Bellwether Food Group

RE: Chain Restaurant Same Store Sales (SSS) 4th Quarter, Calendar Year 2014

The 4th Quarter 2014 Same Store Sales Reports

The positive momentum began with the November 2014 election results, combined with gas prices which are one-third less than what they were one year ago. As much as anything, this immediately impacts consumer confidence and behavior. The feeling of extra cash has a favorable impact on the willingness to go out for a meal.

The incremental disposable income, combined with better execution and raising the performance bar, made a big difference in the 4th Quarter. In taking a closer look at the brands that have done well, each has “upped its game” in one way or another. That is imperative today, regardless of gas prices.

With the exception of McDonald's, there were encouraging results all the way around. In family dining, most of the players had positive SSS (Cracker Barrel, Steak N' Shake, Bob Evans, Denny's and IHOP). IHOP (+6.1%) and Cracker Barrel (+7.9%) stand out especially. Of course Cracker Barrel primarily depends on car travel, so the lower gas prices impacted them immediately.

IHOP, a legacy brand (54 years old), has done a remarkable job of creating interest within the framework of their brand. They've taken pancakes and made them fun with line extensions, etc. We were in a meeting recently with a group of millennials recently, and many of them described the food at IHOP as “fun.” Now, that's progress! They added Belgian Chocolate Moosecake as an LTO dessert - which at least one of our partners made it a point to try. It is better than pretty good - who would ever have expected that in the past at IHOP?

Casual dining had a strong quarter as well, with a number of chains showing positive trends (Applebee's, Buffalo Wild Wings, Longhorn, Outback, and Texas Roadhouse). Again, a key factor was lower gas prices, combined with better execution. Two examples - Chili's continues to upgrade their menu with new offerings (Margarita Chicken Fresh Mex Bowl, Top Shelf Tacos) and they have renewed their focus on lunch. Outback has done it with seemingly small things - more contemporary plate ware, new menu design, and enhanced wait staff training. All those details matter.

On the subject of gas prices, Sonic Drive-In posted an +8.5% SSS quarter. Give Sonic credit for their innovations such as Lil' Doggies® and Lil' Chickies™. These initiatives hit three important points - it's a smaller portion (making it a "safer" trial decision), the price points are competitive, and it fits within the brand positioning. Very successful strategy on "new product news" targeted to the core Sonic consumer.

Emerging Fast Casual has drawn traffic primarily from Casual Dining (we're hearing that from the consumers). That's not really news - what is news is that those emerging fast casual brands are impacting how many of the legacy, established Brand management teams are thinking about their business. That's essentially the opposite of just a few years ago when the emerging brands were tracking the more established brands.

We believe the consumer transition to caring much more about ingredients is permanent. We hear this in almost every project now. This consideration is evolving into information consumers will expect and demand, and is happening way ahead of any legislative or regulatory compliance requirements. California consumers cared about calories, fat, sodium, etc., and some brands were leading the trend (CPK, Panera). This was well before the nutritional posting requirements became California state law.

It is interesting to observe how consumers behave on specific occasions. The dynamics of how individual consumers actually make a restaurant or menu decision based on the source/quality of the menu items, nutritional factors and all of the other considerations continue to evolve. We will be looking at that issue.

One poignant example is the continuing decline of diet soft drinks. That segment is declining faster than the full calorie products. Surprisingly, full calorie soft drinks still outsell the low/no calorie products. While that is an interesting observation, what really matters here is that fewer consumers are regular, high volume consumers of those carbonated products. This will mean margin and profit pressure over time, as operators work on ways to recapture the revenue in some other category.

Italian Casual Dining continues to struggle. Ignite threw in the towel in on Macaroni Grill, selling the brand for some \$8 million to a management led investment group. When a chain restaurant brand suffers that much for so long, the single most difficult challenge is keeping talented staff. This is especially true in casual dining, where tips really matter to the employees. Lower volumes mean fewer tables, which directly impacts their income. The talented wait staff professionals seek out the higher volume, higher check (Cheesecake Factory, Outback, etc.) brands. It is simple economics.

While on the subject of staffing and labor, that topic is a subject of conversation with each of our chain restaurant clients, and the investment community. The challenge is how to attract and keep the best employees in a tightening labor market. We already see Walmart and McDonald's taking action on wages, and many will be following if they haven't already done so.

Also, tip credits are at risk in states that still allow tip credits. So, many are looking at server and table top technology, and menu engineering to figure out ways to maintain high levels of service, but protect labor costs. It will be interesting to follow these changes over the next year.

4th Quarter 2014 SSS Sales by Brand

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Limited/Quick Service				
Burger King	+4.2%			(Includes Canada)
Chipotle	+16.1%			
Domino's	+11.1%			
Dunkin Donuts	+1.4%			
El Pollo Loco	+7.6%			
Jack in the Box	+4.4%			
McDonald's	-1.7%			
Panera	+3.0%			
Papa John's	+4.1%			
Popeye's	+6.3%			6 th year of positive SSS
Pollo Tropical	+7.7%	+3.8%		
Pot Belly	+3.7%			
Qdoba	+14.0%			
Sonic	+8.5%			
Starbucks	+5%	+2%		
Taco Cabana	+6.1%	+1.6%		
Wendy's	+1.9%			+1.6% Franchise stores
KFC	+4%			
Pizza Hut	+2%			
Taco Bell	+7%			Increase driven by new breakfast sales
Zoe's	+7.8%	+3.9%	+1.2%	Additional 2.7% increase in product mix
Full Service				
Applebee's	+2.8%			
BJ's	+1.2%			
Bob Evans	+3.8%			
Bonefish Grill	+0.7%			
Bravo Restaurants	-3.9%			Traffic declines of -3.8% (both brands)
Brick House Tavern	+5.7%			
Brio Restaurants	-4.2%			Traffic declines of -3.8% (both brands)
Buffalo Wild Wings	+5.9%*			+5.1% at (591)franchised stores, *491 co. stores
Capital Grill	+6.1%			

Brand	Same Store Sales Versus Prior Year	Traffic Change	Pricing	Comments
Carraba's	+0.3%			
Cheesecake Factory	+1.4%			
Chili's	+3.5%	+2.1%		
Chuy's	+3.8%			
Cracker Barrel	+7.9%	+4.7%	+3.2%	
Denny's	+4.7%			
Famous Dave's	-4.0%			
Fleming's	+3.4%			
IHOP	+6.1%			Highest Quarterly SSS increase in over 10 years
Joes' Crab Shack	-4.5%			
Longhorn	+5.4%			
Macaroni Grill	-2.8%			Sold to Red Rock Partners
Olive Garden	+2.2%			
Outback	+6.4%			
Red Robin	+3.1%			
Ruby Tuesday	-1.0%	-1.3%		
Ruth's Chris	+5.0%			
Steak 'n Shake	+4.8%	+2.7%		
Texas Roadhouse	+7.0%			
Yard House	+5.4%			

Implications for Operators

We are at an interesting point in the development of the chain restaurant industry. We have a large number of new concepts and new entrants that are well designed, well thought out and well financed. As a result consumer behaviors are changing and there is even more blurring of the lines between segments, occasions, and how consumers use brands. If you have been following our updates, you know that we recently reviewed the top emerging brands and outlined some of the consumer's favorites.

We work with many brands every year, and are consistently surprised by how few of them have reached out to understand their consumers over the past several years. With new entrants, and changing consumer behavior, it is more important than ever to talk to your consumers; and more importantly those consumers who no longer use your brand – lapsed users – to understand how your brand compares to the competition. What needs you are or are not meeting, and what aspects of your brand (if any) truly differentiate you, and drive consumer loyalty.

The tool we see that works well to understand consumers in this context is the Attitude Awareness and Usage study (AA&U). In this study we talk to consumers to understand which brands they are using today and why, how those brands meet their expectations or don't,

review performance of a range of attributes, and what elements of the brand drive guest satisfaction, intent to revisit and intent to recommend. There are a growing number of brands we work with that conduct these studies annually, to see how marketing, advertising, menu changes, and operations performance are improving their scores with consumers relative to the competitive set. We strongly encourage you to talk to your consumers and gain a better understanding of why and how they are using your brand today, and if they have stopped using your brand, where are they going and why.

As always we look forward to your thoughts and insights.

Regards,

Mac Brand, Dallas	mbrand@bellwetherfoodgroup.com ,	773-255-6466
Rob Hardy, Boston	rhardy@bellwetherfoodgroup.com ,	617-281-5175
Jon Jameson, North Carolina	jjameson@bellwetherfoodgroup.com ,	843-422-4285