COMPASS™
RESTAURANT CONSULTING & RESEARCH

Restaurant Pulse Report // October 2021

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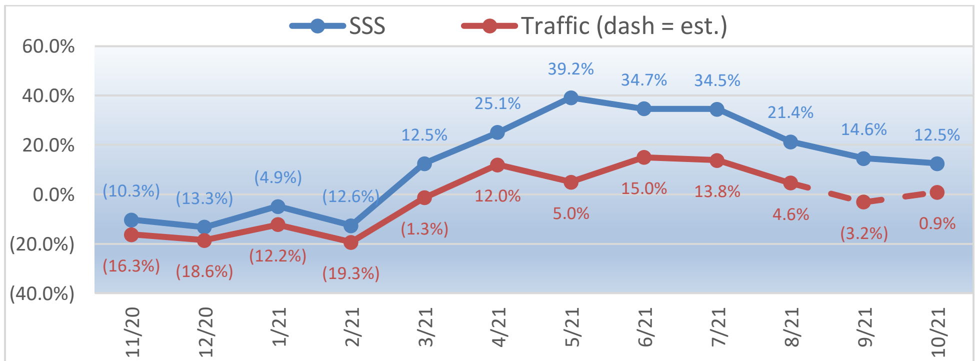
INDUSTRY: HEADLINES / BUSINESS CONDITIONS/TRENDS

HEADLINE NEWS:

- Off premise sales expected to increase during holidays.
- Supply Chain Issues – multiple causes (see pg. 5 for details).
- Store staffing improves but at a cost.

SALES & TRAFFIC: (Compass RCR coverage average):

Industry avg. SSS	+12.5%
Industry avg. Traffic	+0.9% (estimated)



ECONOMIC HEADLINES:

- Inflation hitting middle and lower income the hardest.

BRAND HEADLINES:

- QSR – McDonald's leads the way, others doing well but Burger King and Popeyes lagging far behind.
- Fast Casual – All performing reasonably well. Chipotle light years ahead.
- Casual Dining – Sector performed well; Darden seems to have figured it out.

OPERATOR HEADLINES:

- What's the future of Virtual Kitchens? Must be pretty good as Krogers Grocery Store chain is opening "Virtual Grocery Stores" in Florida.
- Operator optimism contradicts results.

SUPPLY CHAIN HEADLINES:

- Multiple large companies reporting product shortages.
- Bottleneck in port cities delaying products and raw materials.

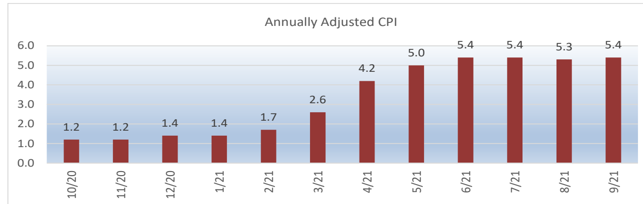
CURRENT TRENDS:

- Off premise sales are expected to increase during the holidays. With the growth of omnichannel shopping, off premise options for restaurant purchases will increase during the holidays driven by higher gas prices, the desire to avoid the crowds, and ease of use vs. cooking at home. Even though October saw a spike in domain preferences, there will be a reverting back by many to off premise dining.

Please see Page 27 for Important Disclosure

ECONOMIC NEWS (BREAKDOWN):

- CPI/Inflation Rate - Annualized 5.4%
- Commodities wholesale prices rose 12.9%
- Unemployment 4.8%



SOURCE: TRADINGECONOMICS.COM US Bureau of Labor Statistics

CPI/12 Month % Change: Overall (annualized) increase of 5.4%; Major Categories: All items rose 5.4%. Food at Home 4.6%; Food Away From Home 4.7%; Energy 24.8%

INFLATION – According to multiple sources (Federal Reserve and several top economists) inflation is not expected to ease until late 2022 or early 2023.

UNEMPLOYMENT – Rate dropped to 4.8%, lowest since March 2020. Many believe this happened because more people are less concerned over the Covid virus and are re-entering the job market.

WHOLESALE COMMODITIES UPDATE	October 2021	September 2021
Beef	$3.60	$2.85
Dairy	$2.08	$2.07
Pork	$3.39	$3.45
Poultry	$3.01	$2.95
Produce	$29.25	$23.50
Seafood	N/A	N/A
Chicken Wings	$3.11	$3.15
Thighs	$0.72	$0.65
Basket (limited)	$6.45	$5.91

SOURCE: Commodities: USDA / Gasoline: AAA

According to the USDA Outlook Report – protein prices are expected to rise until Spring 2022. Wholesale prices YOY on several major commodities: Beef 57.7%, Eggs 39.2%, Processed Poultry 30.3%, Pork 27.2%, Seafood 16.6%.

NATIONAL GAS AVERAGE - PER AAA									
1/21	2/21	3/21	4/21	5/21	6/21	7/21	8/21	9/21	10/21
2.25	2.68	2.87	2.9	3.04	3.09	3.17	3.19	3.18	3.38

Gas prices are expected to continue to rise through Winter 2022.

RETAIL COMMODITIES UPDATE	October 2021	October 2020	September 2021
Ground Beef	$6.79	$4.08	$6.18
Milk	$3.59	$3.44	$3.56
Bacon	$7.22	$5.61	$7.10
Bread	$1.58	$1.49	$2.08
Coffee	$4.73	$4.49	$4.73
Whole Chicken	$1.50	$1.54	$1.47
Eggs	$1.84	$1.35	$1.71
Potatoes	$0.80	$0.80	$0.80
Basket	$3.50	$2.85	$3.45

- **OPERATORS:**
  - Current Month Sales (nationally):
    - 76.0% ⇧ Increase over last year
    - 24.0% ⇧ Decrease over last year
  - Current Traffic:
    - 70.0% ⇧ Increase over last year
    - 30.0% ⇧ Decrease over last year
  - Future Outlook for Business Conditions over the next 6 mos.
    - 46% expect business conditions to improve
  - Future Outlook for Sales:
    - 47.0% ⇩ Increase over last year
    - 53.0% ⇧ Worse than LY
  - Margins Impact:
    - 83.0% ⇩ Reported food cost increase (rose 6.1% YOY)
  - Menu Prices:
    - 89.0% ⇧ Higher than LY
    - Menu prices increased 5.4% over last 12 months
  - Staffing Issues:
    - 49.0% ⇧ Fully Staffed
    - 51.0% ⇩ Understaffed
  - Top Concerns:
    - 74% Recruiting/retaining employees
      Specifically 89% are concerned w/recruiting quality employees
    - 81% Inflation
    - 62% Government vaccine mandate

According to the NFIB Monthly Survey:

- Outlook for Better Business Conditions over the next six months decreased to a negative <33%>.
- 51% reported job openings that could not be filled – a record 48-year high.
- 42% reported raising compensation.
- 35% reported supply chain disruptions that have had a significant impact on their business.
  32% reported moderate impact.
  21% reported mild impact.

SUMMARY: October operator results indicate a strong shift away from confidence in the current and future business conditions; this is declining rapidly. It also indicates that general situations with staffing, inflation, and supply chain disruptions are not looking good through the holidays. The frustration with staffing grows as the search goes beyond "warm bodies" to finding qualified workers.

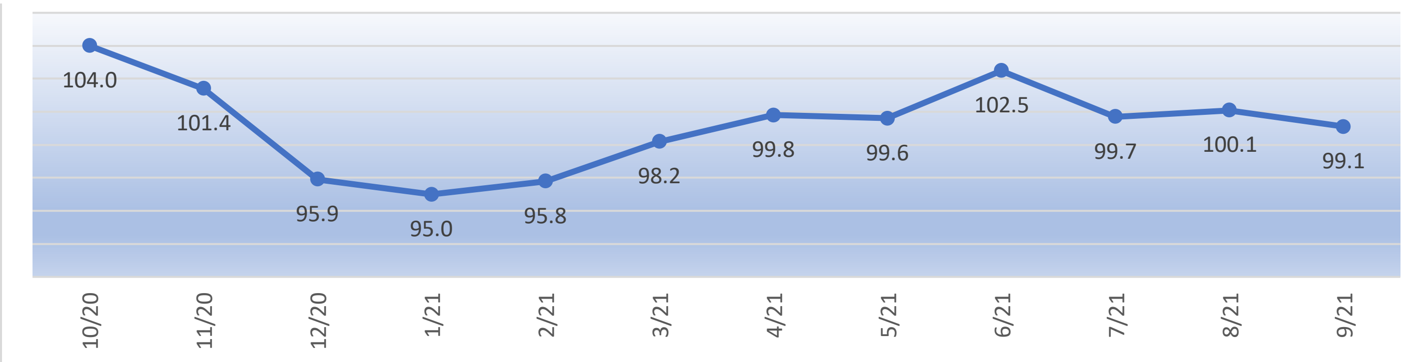
When comparing SSS to 2019, operators reported the following. By segment:

	CURRENT MONTH		LAST MONTH	
	Higher	Lower	Higher	Lower
QSR	67%	17%	75%	17%
Fast Casual	71%	14%	50%	17%
Casual	56%	39%	47%	42%
Fine Dining	32%	68%	38%	50%

SSS 2-Year Comparison (Higher)

	June	July	August	September	October
QSR	71%	47%	64%	75%	67%
Fast Casual	71%	67%	50%	50%	71%
Casual	38%	50%	75%	47%	56%
Fine Dining	5%	80%	50%	38%	32%

SMALL BUSINESS OPTIMISM INDEX (Source: NFIB and Compass RCR)



RESTAURANT PERFORMANCE INDEX: (Source: National Restaurant Association)

	2/21	3/21	4/21	5/21	6/21	7/21	8/21	9/21
RESTAURANT PERFORMANCE INDEX	100.1	105.1	106.3	105.5	105.6	105.2	104.2	102.9
CURRENT SITUATIONS								
$ SSS Increase/Decrease	73%/27%	77%/23%	97%/3%	95%/5%	84%/16%	85%/15%	73%/11%/16%	76%/24%
Capital Spending	53%	58%	74%	68%	72%	73%	63%	59%
EXPECTATIONS:								
$ Sales Outlook Improvement	63%	78%	77%	75%	75%	71%	53%	47%
Economy Outlook Improvement	66%	69%	64%	74%	68%	32%	36%	16%

CONSUMER SENTIMENT: (Source: University of Michigan Sentiment Poll)

	11/20	12/20	1/21	2/21	3/21	4/21	5/21	6/21	7/21	8/21	9/21	10/21
Consumer Sentiment	74.1	80.4	81.8	76.9	80.7	84.9	82.9	85.5	81.2	70.3	72.8	71.7
Current Economy	82.9	87.8	85.9	87.0	90.0	87.7	89.4	88.6	84.5	78.5	80.1	77.7
Consumer Expectations	68.5	75.6	79.2	70.5	74.6	73.8	78.8	83.5	79.0	65.1	68.1	67.9

- Consumer Sentiment remains relatively unchanged from September. However, according to the Survey of Consumers by the University of Michigan, the positive impacts of higher income expectations and receding Covid 19 has been offset by falling confidence in government economic policies and high rate of inflation. Consumers also expressed greater uncertainty about the coming year's inflation rate than anytime in nearly 40 years of these surveys. Declining living standards, due to inflation, were mentioned by 20% of households.
- Online Shoppping remains very high (30% over pre-pandemic levels) in September according to a recent study by McKinsey & Company (U.S. Consumer Sentiment & Behaviors During the Covid Crisis / Oct. 18, 2021). And according to the report, Omnichannel is here to stay (something we predicted last year).
- Also worth mentioning, a recent study by Acosta Shopper Community Survey – "The Why Behind the Dine" (published 10/2021) key notes are:
  - Food Trucks, Pop-Up Restaurants, and Ghost Kitchens are increasing in popularity.
  - 60-70% stated eating out several times a month (more than pre-Covid).
  - Food quality trumps everything else when choosing where to eat.

Consumer Conerns:

	October 2021	September 2021	August 2021
Health concerns as related to Covid variant	36%	50%	26%
Financial concerns – (Inflation) increased cost of goods	72%	58%	16%
Immigration	76%	52%	11%

SOURCE: September 24, 2021 Gallup Poll

SUPPLY CHAIN NEWS:

SUPPLY CHAIN

After a broader investigation into the current supply chain crisis, we have concluded there are multiple causes to the dilemna rather than the one or two single causes many reports focus on. (Similar to the ancient parable of "The Blind Men and the Elephant".)

The supply chain was already strained pre-Covid but manageable. However, the impact of the Covid crisis on the world economics revealed the vulnerabilities of the chain; and how weak all the links were. The entire infrastructure proved to be tenuous.

Prior to the Crisis, the focus from businesses and the supply chain was on lean and efficient stock levels leaving little or no buffer or margin for error. The accepted inventory practice was "just in time" restocking policies.

- **THE COVID 19 CRISIS –** and its subsequent repercussions on shutting down economies around the world; this event was the proverbial straw that broke the camel's back. Businesses of all types closed, employees were let go, production of most non-essential goods ceased, and people saved their money (according to the Bloomberg report on March 3, 2021). They estimated "consumers in the world's largest economies amassed $2.9 trillion in extra savings during Covid lock downs. A vast cash hoard that creates the potential for a powerful recovery from the pandemic recession."
- **INCREASE IN CONSUMER DEMAND** – as the world economies began to reopen, consumers' demands for goods exceeded everyones expectations. The supply chains' logistic systems were not capable and were not designed to handle this surge. The money saved is now being spent as part of the consumers releasing the pent up demand.
- **SHIFT IN CONSUMER PREFERENCE** – For approximately the last 60 years (prior to the Covid Crisis), U.S. households share of spending on products such as cars and kitchenware had been decreasing and spending on services such as eating out and travel had increased. However, with the consumers spending time during the lockdown on DIY projects and homebound activities, the pandemic interrupted the long term spending trend on services back to spikes in demand for products. Spending on durable goods increased 32% YOY from March 2020 to March 2021 while spending on nondurable goods increased only 8%. During this same period, consumer spending on services such as restaurants, hotels, and travel dropped 3%. All down the supply chain, this surge on durable goods found businesses scrambling to meet the demand. The surge in demand created bottlenecks that slowed production.
- **CURTAILED PRODUCTION** – With economies worldwide shut down, creating less demand; thus manufacturers scaled back and in some cases ceased production thereby generating a gap in the availability of many products.
- **SHORTAGE OF WORKERS** – Every step of the supply chain, from raw material to supplier to manufacturer to distributor to storage to retailer to consumer has been impacted by the labor shortage. (As to what caused the workforce shortage, we refer the reader to our past reports on the "labor crisis".)

  The biggest direct impact of worker shortages on the supply chain is in transportation. Not enough truckers to drive supplies from ports and depots to the other links in the supply chain. According to the American Truckers Association, they are short 80,000 truckers which means a lot of cargo can't go anywhere. So it doesn't matter how many widgets a manufacturer can make, if they can't ship it, the production process is stalled. But again the worker shortage is impacting every stage of the supply chain.
- **GOVERNMENT REGULATIONS ON PORTS AND TRUCKERS** – Current regulations for ports state their hours of operations can only be 16 hours per day; roughly 8 A.M. to midnight and closed on Sundays. Even though President Biden recently anounced relief by allowing two ports to go to 24/7 hours of operations, there are three major problems with this. (1) There are over 20 major container ports along the U.S. coastlines. So only opening two for 24/7 operations isn't going to provide much relief. (2) With the trucker shortage, unloading more cargo only increases the bottleneck at the ports storage facility. And (3) According to the Container Port Performance Index 2020 published in May 2021 by World Bank Group, the port of Los Angeles and Port of Long Beach scored 338 and 333 out of 351 as far as efficiency rating worldwide. So granting these two ports 24/7 operating status might be the most efficient effort.

  For truckers, currently the regulations state they cannot drive more than 11 hours in a 24 hour period and a required 30 minute break every 8 hours. The American Truckers Association is asking for some latitude with these regulations during the current supply chain crisis. (Some suggestions: allow drivers to extend and increase breaks.)

  According to the most recent Manufacturers Report from the Kansas Qtrly Fed – 95% of manufacturers reported supply chain disruptions and shortages in October 2021. 82% of manufacturers reported paying more for materials than prior month.

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