COMPASS™
RESTAURANT CONSULTING & RESEARCH

EOM Report // April 2020

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COMPANIES MENTIONED IN THIS REPORT:

CORE COVERAGE

*Charts on pages 4-23 "Mean" Source – Company Filings

SUMMARY OF INDUSTRY BUSINESS CONDITIONS:

SAME STORE SALES (SSS) (Includes Independents):

	SSS
Total Industry-wide avg.	<55%>
QSR	<42%>
Casual Dining	<73%>
Fine Dining	<51%>

- April top performers: Popeye's, Domino's, Wingstop.
- April bottom performers: Applebee's, IHOP, Red Robin.

CONSUMERS AND OPERATORS PROVIDE THEIR TAKE:

- CONSUMERS: Quarantine fatigue, pent up demand, concerns and fears over social distancing and personal income are all impacting the consumer's mood as 19 States begin lifting/easing Shelter at Home rules.
- OPERATORS:
  - Apprehension over future is taking its toll.
  - They are overwhelmed by logistics to re-open.
  - Up to 30% of Independents are closed.
- SUPPLY CHAIN: As of 4/29/20, the Covid-19 pandemic's far reaching impact on the supply chain's potential meat shortage is looming and/or at least a gap in availability.

HEADLINE NEWS:

I. **BREAKING NEWS: Scattering of Wendy's locations in KY and OH temporarily out of beef. Could be up to 15% of all U.S. stores.**

II. Several States begin allowing controlled re-opening of businesses and public places.

III. Federal Government Passes 2 large stimulus packages for individuals and small businesses.

MAY OUTLOOK

- **Brands we expect to outperform the Industry**
  - Burger King
  - Chipotle
  - Domino's
  - Popeyes
  - Wingstop
- **Brands we expect to underperform the Industry**
  - Casual Dining Sector
  - Pizza Hut

Please see Page 24 for Important Disclosures.

CONSUMERS – WHAT WE HEARD IN APRIL 2020:

Consumer confidence has taken a beating over the last 6 weeks. One key looming concern is the rate and number of people losing their jobs or have a reduction in hours (reduction in income) during the Covid-19 Crisis. As of April 23, 2020, the Department of Labor reported 30 million Americans have applied for unemployment benefits. This represents approximately 19% of the labor force (source: Pew Research August 29, 2019).

This unprecedented loss of jobs is also generating a higher level of concern among those still employed of which 25% fear they will lose their job within the next 12 months (Gallup Poll – 4/22/20). This amount of layoffs and rapid rate at which it is occurring has shaken consumers' confidence in the job market. The ripple effect will be an impact on their spending as the economy begins to re-open – what they purchase, when, why and where, as well as the rate at which they return to the labor force.

The University of Michigan's recent Sentiment Survey of April 30, 2020 showed April's sentiment at 71.8; a 17.3 point drop from March.

While the initial impact in mid-March was the concern regarding the Covid-19 virus (62% stated it was their top concern with personal finances coming in at 38%), by end of April the concern levels began to shift with Covid-19 at 60% and consensus over personal finances at 40%. As more people get impacted financially, their concerns begin shifting. The restoration of consumers' confidence in the job market will be difficult and likely take longer to achieve than many had earlier estimated.

Survey by Lending Tree (April 24, 2020): on consumers' plans for spending stimulus funds:

- 45% on groceries
- 29% on rent
- 22% on debts
- 10% on restaurants/splurge

OPERATORS – WHAT WE HEARD IN APRIL 2020:

According to our latest discussions, as many States and municipalities lift or ease their Shelter at Home restrictions, operators are facing overwhelming obstacles to re-open their businesses or open their dining rooms – implement new sanitizing and food safety policies and procedures, rehire and retrain employees, and evaluate current menus are just a few of the myriad of tasks to begin a re-opening process.

Create and implement new standards, policies and procedures for food safety and restaurant cleaning/sanitizing practices would include employee health evaluations and practices, rehire and retrain employees on those new policies as well as new social distancing best practices. Work stations will need to be reconfigured as well as dining rooms to create more distance between customers and employees, limiting the number of customers – logistics will have to be worked out. Masks and gloves for employees will have to be procured and policies put in place, additional hand sanitizer dispensary points will have to be set up in the restaurant, ensure restaurant is capable of handling "cashless transaction" payment options (might require new software upgrades), remove customer access to any Self Service items to avoid cross contamination. In the case of most QSR's which offer self-serve drinks, an additional employee will need to be stationed to fulfill that function. In some instances installing plexiglass shields at the cashier station to limit their exposure. Continue to focus on the Off-Premise model. Another whole set of issues has emerged regarding obtaining supplies to re-open – to include food and packaging as well as cleaning supplies, face masks, etc. Operators will need to ensure their distributors have the needed items for re-opening and possibly have to establish some degree of credit for their initial order.

Once all of this has been established and other State and Federal mandates have been met, then operators have to hope the consumer returns.

Commodities

Covid-19 Impact on Supply Lines

According to the latest report from the CDC, as of May 1, 2020 thousands of U.S. workers in meat processing plants have been infected with Covid-19 and at least 20 have died. Workers in 115 plants in 19 States have been diagnosed with Covid-19 resulting in 25 meat processing plants closing or partially closing. This will create a disruption in the supply line. According to the USDA, these closed or partially closed plants represent 15% of the beef and 30% of the pork production. However, the USDA was quick to respond that this does not mean there will be a meat shortage. However, for the consumer, they can expect to see higher prices and absence of some selections of beef and pork. As of this weekend (5/3/20) several grocery store chains are limiting consumer purchase of meats to 1 package.

For the operator/restaurant industry, it will mean higher prices – especially for chains that feature fresh beef like Wendy's and McDonald's Quarter Pounder.

The USDA stated that once these plants begin to re-open it is estimated to take 8 to 12 weeks to get the system back up to 90% production.

The Chairman of Tyson Foods sent an open letter to the Sunday New York Times, Washington Post and several other media outlets on Sunday, April 26, 2020 warning that the food supply chain is breaking due to these closures and that millions of pounds of meat supply from cold storage will be depleted. Tyson further stated, "If we hold where we are, with the same number of plants down but no further closures, then we estimate there should be enough processed meat in storage to last through the beginning of May." Since Mr. Tyson's letter, there have been 2 more major closures of beef processing plants. So the timetable will no doubt be accelerated.

Another critical component to the supply chain is hog and beef ranchers have been withholding supply to processors since mid-March because beef and hog prices were down approximately one-third since the beginning of the year. This has created another bottleneck in the supply chain. Even if meat processing plants were ready to go to 90% production today, they do not have enough raw product available to meet production demands. This will also slow output from producers.

Yet another factor that is creating turmoil with the supply chain has been reductions in manpower as many workers refuse to work in the current environment. Another piece to this conundrum is the introduction of more stringent safety measures such as bigger gaps between shifts and physical distancing between workers. These changes in protocols have reduced production by as much as 10-25% from normal.

Bottom line, there are numerous elements that are generating disturbances to the food supply chain due to the Covid-19 Crisis and will impact available supply.

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