



Market Brief

Tracking and interpreting restaurant trends

THE ECONOMY

The "S" curve of the recession seems to be flattening out, although it's too soon to say whether the economic trendline is turning into a "U" curve and heading back up. GDP dropped 5.5% in Q1, but that's not as bad as the fourth-quarter plunge. Real DPI—the best predictor of consumers' spending habits—continues to inch up thanks to federal stimulus funds. Restaurant chains report nominal revenues up slightly (excluding the impact of global currency fluctuations on McDonald's). Same-store sales are still down, but not as much as last quarter's comps. There are many unknowns, but there are also signs that it may be time for restaurants to position themselves to profit in the coming recovery.

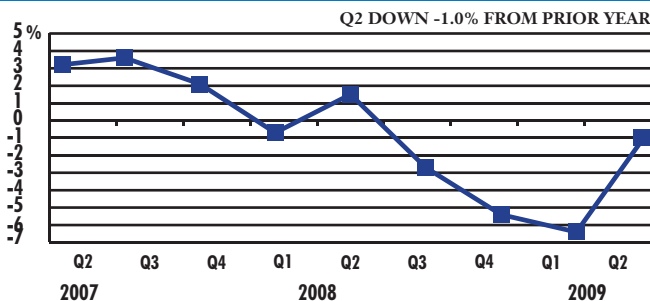
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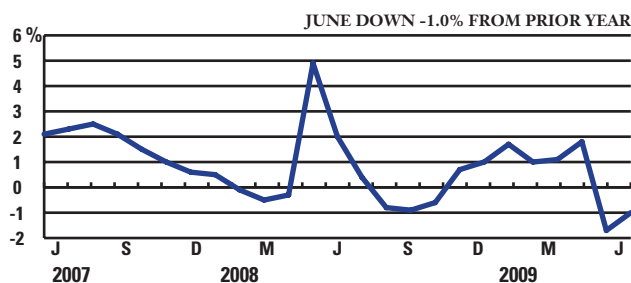
Gross Domestic Product Quarterly Rate of Increase



Source: Bureau of Economic Analysis

U.S. real gross domestic product (GDP) decreased at an annual rate of 1.0% from the first quarter to the second, according to Bureau of Economic Analysis advance estimates. That was considerably less than analysts had expected, and far less than the 6.4% Q1 GDP drop or the 5.4% drop for Q4 2008. Those two quarters were the worst in 26 years.

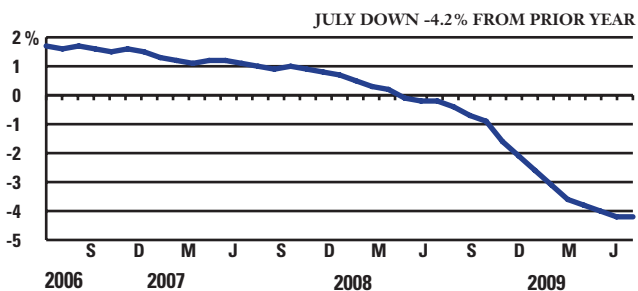
Real Disposable Personal Income Growth



Source: Bureau of Economic Analysis

U.S. consumers' real disposable personal income (DPI) fell 1.0% in June from year-before levels. In addition, DPI changes for every month since January 2007 were revised downward. Real DPI fell 1.8% from May, partly because consumers benefited more from federal stimulus funds in May. Real personal consumption expenditures were down 0.1% from May.

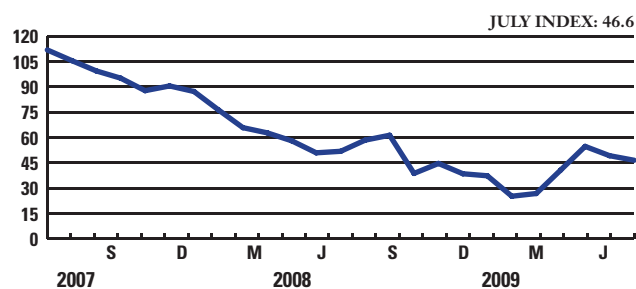
Employment Growth: Total Non-Farm



Source: U.S. Dept. of Labor

Nonfarm payroll employment (not seasonally adjusted) was down 4.2% from the prior year in July; this is the same performance as in June. The unemployment rate, at 9.4%, is also little changed from June, when it was 9.5%. In July, 247,000 additional jobs were lost and the number of unemployed persons was 14.5 million. The number of long-term unemployed (those jobless for 27 weeks or more) rose by 584,000 over the month to 5.0 million.

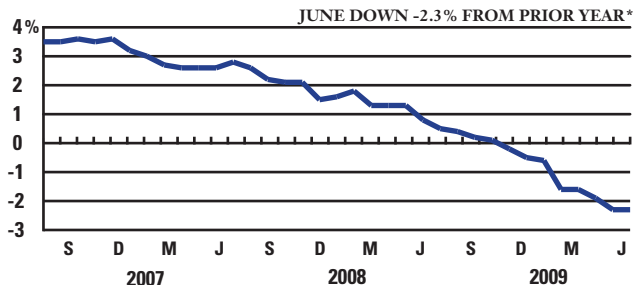
Consumer Confidence Index (Base 1985=100)



Source: The Conference Board

The Conference Board Consumer Confidence Index, which had retreated in June, declined further in July. The Index now stands at 46.6 (1985=100), down from 49.3 in June. Consumer confidence, which had rebounded strongly in late spring, has faded in the last two months as more consumers are pessimistic about their income expectations and overall short-term outlook.

12-Month Moving Average (Foodservice & Drinking Places Real Sales)



Source: U.S. Census Bureau; Technomic, Inc.

June's moving average for sales of foodservice establishments (including restaurants, bars and taverns, and onsite foodservice) was 2.3% below year-before figures in real dollars, the same year-to-year decline tallied in May. In a Technomic poll, 31% of full-service operators and 23% of limited-service operators said they expected their 2009 sales to be below those of 2008; 73% of full-service operators and 53% of limited-service operators said they did not expect to see an economic recovery before 2010.

Q4 KEY FINANCIAL METRICS – PUBLIC COMPANIES

Nominal quarterly global revenues of U.S.-based public restaurant chains were lower than those of a year ago. In sum, quarterly revenues of 69 public companies that had reported by mid-July showed a top-line total of \$25,423 billion, down 1.6% from almost \$25,830 billion for the first quarter of 2008. However, excluding McDonald's, the 68 remaining chains showed a very small 0.1% increase—to not quite \$19,776 billion from just over \$19,754 billion. McDonald's reported global revenues down by \$537.4 million (though it noted that in constant currencies, first-quarter results reflected an increase in revenues). The fact that 2008 was a leap year also distorted comparisons, since the first quarter of 2008 contained an extra business day.

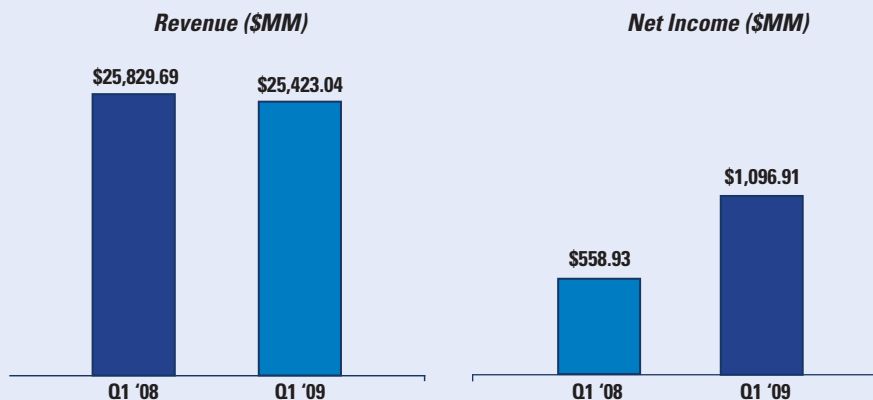
All revenue growth was in the limited-service sector. FSR revenues declined 3.0%. LSRs' total revenues were down by 0.8%, though they were up 2.9% with McDonald's excluded.

Food-away-from-home annual inflation was 4.7% in the first quarter, however, turning all the positive numbers into negatives.

► **Bottom line: Overall, public chain restaurants were still showing nominal revenue increases in the second quarter, though income and margins were down. A few standout chains pulled up sector averages in both full service and limited service, showing that solid management, savvy innovation and cautious growth can still pay off.**

Public Company Fourth Quarter 2008 Industry Summary Results*

	QUARTERLY REVENUES (\$ MM)			QUARTERLY NET INCOME (\$ MM)			MARGINS %	
	2009	2008	% CHANGE	2009	2008	% CHANGE	2009	2008
GRAND TOTAL – 69 companies								
LSR total – 36 companies	16,380.58	16,504.92	-0.8%	1,796.56	1,559.02	15.2%	11.0%	9.4%
<i>Excl. McDonald's</i>	<i>10,733.38</i>	<i>10,429.62</i>	<i>2.9%</i>	<i>702.86</i>	<i>368.52</i>	<i>90.7%</i>	<i>6.5%</i>	<i>3.5%</i>
FSR total – 33 companies	9,042.46	9,324.77	-3.0%	394.05	190.41	107.0	4.4%	2.0%
GRAND TOTAL	25,423.04	25,829.69	-1.6%	2,190.61	1,749.43	25.2%	8.6%	6.8%
<i>Excl. McDonald's</i>	<i>19,775.84</i>	<i>19,754.39</i>	<i>0.1%</i>	<i>1,096.91</i>	<i>558.93</i>	<i>96.3</i>	<i>5.5%</i>	<i>2.8%</i>



* Calendar quarter; number of chains reporting varies each quarter
Source: Public Company Reports

SAME-STORE SALES Q4 2008

Public chains' Q1 U.S. same-store sales comparisons showed more losers than winners. Of 91 chains and franchisees reporting, only 31—just over a third—tallied nominal increases from Q1 2008. Weighted average comps came to -2.0%; without McDonald's, the weighted average decline was -2.9%.

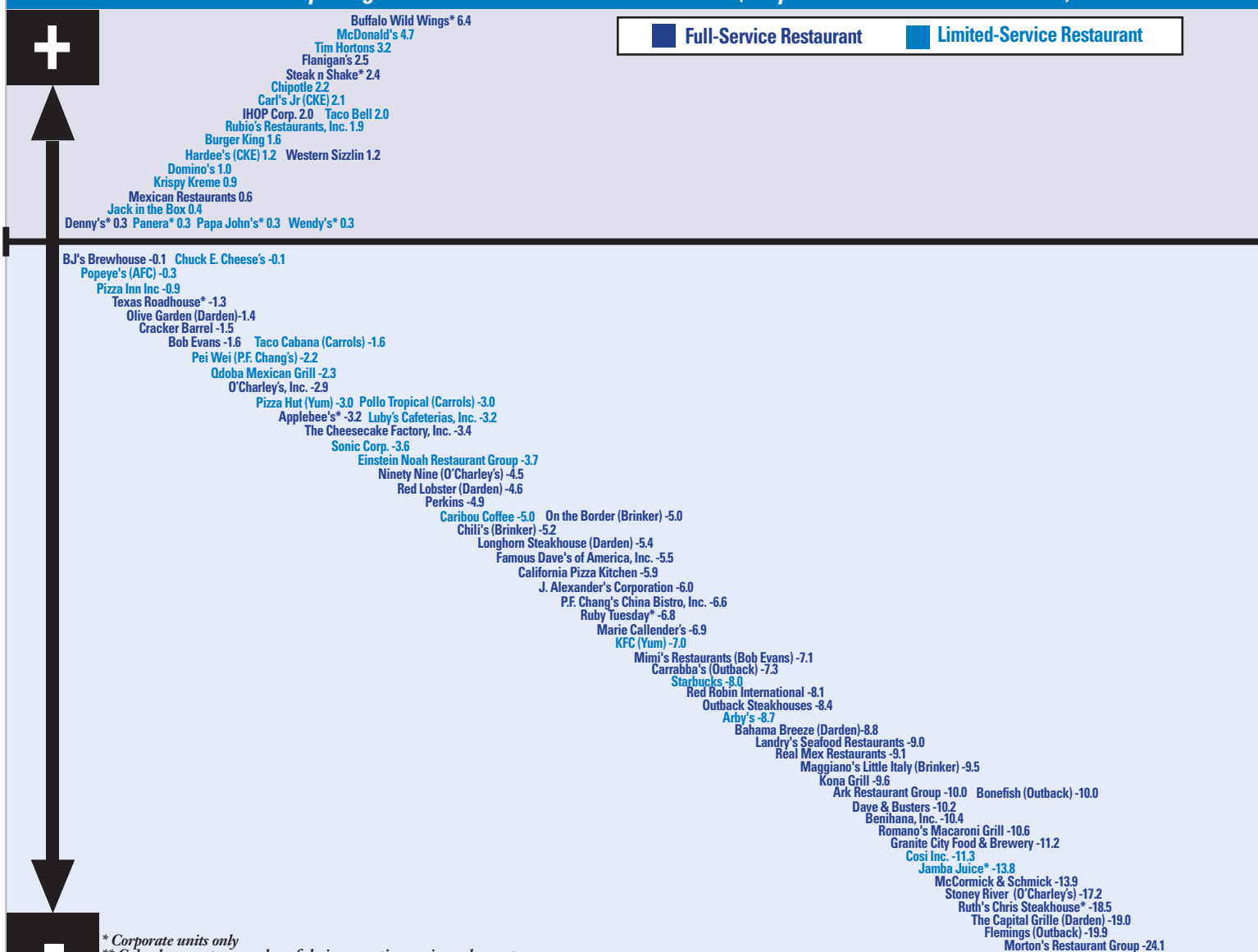
LSRs fared far better than FSRs, with half reporting growth. Of 36 LSR chains, 18 were up and 18 down. The LSR chains with positive comps represented 58% of all chains with same-store sales growth in Q1. The LSR weighted average was actually up, by a tiny 0.1%, though it was down 1.7% with McDonald's excluded. LSR results were bookended by McDonald's 4.7% domestic increase and by double-digit declines at Cosi (-11.3%) and Jamba Juice (-13.8% for company units).

While 46 FSRs saw declines, 13 showed growth. FSRs' weighted average showed a 4.1% drop in SSS compared to the year-before period. Best results came from Buffalo Wild Wings, with SSS up 6.4% at company units. The worst-performing companies were all upscale steakhouses; bringing up the bottom was Morton's Restaurant Group, with a 24.1% drop.

SSS dips are slightly smaller than in the last quarter. The 2.0% decline was a modest improvement from the fourth quarter of 2008, when the weighted average was -2.1%. Without McDonald's, the weighted average was -2.9% in Q1, compared to -3.0% in the previous quarter.

▶ Bottom line: While comps show stark differences by sector and menu cluster, the chains that managed to pull off increases represent full service as well as limited service, with a range of menus, ambiance and price points. Growth in this difficult economic climate depends more on successful execution and attention to basics (including input costs) than it does on a segment or menu "sweet spot."

Chains Reporting 1st Quarter 2009 U.S. Same-Store Sales (% up or down from 1st Quarter 2008)**



* Corporate units only
 ** Calendar quarter; number of chains reporting varies each quarter
 Source: Public Company Reports

SOCIAL MEDIA: BEST PRACTICES

Last month's MarketBrief explored consumers' behaviors and perceptions surrounding social media. More than four out of five of those surveyed said they had visited a social networking site such as Twitter, Facebook, MySpace or YouTube within the previous month. Our study found that consumers who connect with restaurants via such media are motivated by the unprecedented access they get to coupons, promotions, member-only deals and, to a lesser extent, news about the menu and restaurant. We also found that consumers decide to try new restaurants based more on promotions and discounts—including those they find out about via social media—than on any other factor.

This month, we take a look at social media from the operator's perspective, exploring how savvy restaurant companies are leading the way and how independent restaurants with fewer resources can adapt some of these innovations.

REVOLUTIONIZING RESTAURANT MARKETING

Marketing may be the fastest-changing aspect of running a restaurant today. Print marketing is on life support—Baby Boomers still clip coupons, but Millennials find them a hassle. Television is just part of the mix, often used most effectively in conjunction with social media, including corporate and viral websites, blogs, Facebook and MySpace pages and 140-character “tweets” via Twitter. Email marketing is losing its effectiveness because of the clutter factor—consumers don't have the time to read emails even if they've “opted in.” Mobile marketing (alerts, promotions and coupons via cell phone) is picking up speed because of its relevance to on-the-go, often planning-resistant Millennial consumers

A well-thought-out social media presence provides a face and “personality” for a restaurant company. It facilitates rapid response to customer inquiries and to quickly developing issues. It may help companies gain insight on their customers in a way never possible before. Interactive and viral marketing makes customers partners in the business. Viral media opportunities include company websites offering “send it on to a friend” videos, games or coupons, as well as jokey “stealth” websites that may not even identify the sponsoring chain. (Consumers who receive marketing messages from a “trusted source”—a friend—are more likely to respond favorably than if they received the message from a faceless corporation.)

Restaurant operators are using social media in many ways, including mixed campaigns, social-media exclusives, quick-response programs and local initiatives.

- **At Denny's, a presence on Facebook,** MySpace and Twitter is key to the Allnighter campaign aimed at younger-generation night owls, along with a microsite, webisodes and TV commercials.
- **Papa John's targeted Facebook-exclusive** free-pizza deal for NCAA basketball's “March Madness” added 170,000 new fans in 24 hours.
- **Pizza Hut hired a summer “Twintern”** to collect and share insights and experiences via blog, Twitter, Facebook, YouTube and emerging media.

TAPPING INTO IPHONE, IPOD AND OTHER MOBILE DEVICES

Hardee's is one chain leading the way in appealing to its young, hip customer base via social media. Among its many recent initiatives is an “iBurger” application promoting its Western Bacon Thickburger. When fans download the app onto their iPhones or iPod Touch units, it creates a burger photo on the screen. Using sound recognition technology, the iBurger app “hears” the munching sound whenever the iPhone or iPod user eats a burger, whereupon the burger photo gradually disappears as it is virtually “eaten.” Hardee's is also offering coupons via Microsoft's new Tag It! couponing application. After downloading the free Tag It! app, users can snap a picture of the special Tag It! symbol located on Thickburger boxes to receive a coupon on their phone screen, which they can show to the cashier at a Hardee's counter to receive free fries and a Coke with purchase of a Thickburger.

HELPING CUSTOMERS HELP YOU

Giving customers a chance to form a relationship with your brand and join a conversation can deepen their bond with your concept and also provide valuable ideas. Your customers and the dining public in general can be a source of great suggestions, and they're very generous in sharing with the restaurants to which they feel loyal. One of the best practices in this area is Starbucks' MyStarbucksIdea.com, which invites Starbucks customers to help improve the chain and its offerings. In March, Starbucks celebrated the one-year anniversary of its MyStarbucksIdea.com community. Starbucks said that in the first year, users shared some 70,000 ideas on the site about what the chain could do to improve customer loyalty, food and beverage offerings, and the overall in-store experience. Of those ideas, Starbucks considered implementing 94 and eventually launched 25, including ideas that led to VIA instant coffee, Venti travel cups, new tea lattes and improved Wi-Fi service. A number of suggestions for improving the microsite itself were also employed.

In addition, Starbucks is now posting updates on Twitter and has already reached 250,000 fans. In late July, Starbucks announced that it's now the most popular brand page on Facebook, with more than 3.5 million fans. Because of its diverse and successful efforts, Starbucks was recently named the #1 brand in a social media engagement report developed by Altimeter Group and Wetpaint. "The key here is that we are connecting directly with our loyal customers, who will be driving our future growth," Starbucks chairman Howard Schultz told analysts during the company's second-quarter conference call

THE LOCAL ANGLE

Although it might seem that only chains with deep pockets and media-savvy professional marketers can take advantage of new media, nothing could be further from the truth. Compared to traditional forms of marketing and advertising, social media provide quicker, cheaper, more effective communication with customers than operators could ever dream of before. A social media presence is such an ideal marketing medium for a local, independent restaurant that even some chains are making their online presence felt at the unit level rather than as a faceless corporation. For instance, each individual unit of the Smokey Bones barbecue chain has its own website, Facebook and MySpace page. An employee is designated as "web host," tasked with updating the sites regularly with photos and news about the restaurant and its events—along with his or her own personal information and opinions. It's a great way to put a human face on the restaurant and present its employees as customers' friendly peers.

Local marketing efforts can be tied to local pride. Rubio's Fresh Mexican Grill tied a localized quick-response promotion in its home market of San Diego to residents' obsession with the local pro football team. Its online offer of a "Free World Famous Fish Taco If the Chargers Win" the AFC divisional playoff in January led to a 50% increase in web traffic along with thousands of coupon downloads and signups for its online Beach Club. The promo targeted to football-crazed San Diegans was picked up by local TV and radio as well as other Twitter, Facebook and MySpace sites, generating invaluable free publicity. At the unit level, Rubio's tracked a 100%-plus increase in transactions and a 40% increase in sales even as it gave away 25,000 fish tacos.

TOO MUCH OF A GOOD THING?

The Rubio's football tie-in in San Diego was one of many promotions that have "gone viral," multiplying the restaurant's reach in a way that might once have been unbelievable. Rubio's response was manageable—but before making any offer, restaurants must consider carefully whether they can deal with the likely response. Great offers can take on a life of their own. Quiznos Sub found that out in February when it announced it would give away a million free subs to underscore its new lower prices. Customers could sign up at a MillionSubs.com microsite to instantly receive a coupon good for a free sub sandwich at participating stores. A million coupons were downloaded within three days, but some customers were angered when they visited units that did not honor the promotion or that had run out of product. In the end, Quiznos had to reimburse franchisees as well as disgruntled customers. Poor communication between the chain and franchisees, along with an over-ambitious promotion and a failure to anticipate the likely response, caused the promotion to backfire.

► **Bottom line:** *Social media won't wait until your company is ready. The question is not whether you should be using social media avenues, but how. Restaurant operators are focusing relentlessly on ROI in every aspect of their business, and an investment in social media can have a better return than almost any other marketing expenditure. There's no going back; the conversation with your customers will be an ongoing one, no matter what the social media platform of tomorrow turns out to be.*

BUSINESS-BUILDING IMPLICATIONS

- **If you're new to social media marketing, your first urgent step is to sign up on the major sites** including Facebook, YouTube, MySpace and Twitter. If you don't register your company name, anybody can.
- **Observe and listen in on your competitors and customers.** Monitor conversations about your brand, note likes and dislikes, and respond to any negative postings or inaccurate information. Check out the websites and social media presence of other restaurant brands, including the deals they are offering.
- **Don't proceed further before you make a plan**—how to present your brand, how you will interact with customers, who will lead the effort, what you have to say, how you can maximize links. Designate and empower a web host.
- **Consider which forms of social marketing best suit your purposes.** Evaluate custom tools and applications (such as iPhone custom apps)
- **Have something interesting to say**, and update content frequently.
- **Build in customer support.** Find ways to interact with your customers and get them involved online—selectively. Don't give customers free opportunities to bash your brand online, but recognize the customer's role as a marketer of your brand—customers who love you will sell your brand for you.
- **Think links.** Identify opportunities to organize your online content (and particularly coupons and promotions) with a variety of links and approach points. Consider including links to positive information about your brand on other sites. Link your Facebook or Twitter presence to an identifiable corporate presence so users know you're legitimate.
- **Continuously monitor your social media presence and how many people are responding.** Social media effectiveness is a learning curve, so traffic and data are essential.
- **Don't try to be controlling.** The online conversation is already going on. It's about people coming to you, not you going to them. Speak in a human voice, not an institutional voice. Customers want to know that people in your company are authentic, honest human beings.
- **Think of your online media presence as an ongoing process**, not a product that can be finished once and then displayed. Don't be afraid to make mistakes and learn from them. Respond quickly to problems before they get out of control. When you do make mistakes, admit it.

About MarketBrief *Through MarketBrief, American Express provides chain restaurants with research-based analysis of key industry developments. Data is collected and analyzed by Technomic, Inc. Past issues of MarketBrief are available online at: www.technomic.com/operator/amexmarketbriefs. If you have questions, comments or topic suggestions, please contact Kimberly Perman at kperman@technomic.com or directly at (312) 506-3831.*

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