Nation's Restaurant News

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The Next 20: NRN's new look at emerging brands

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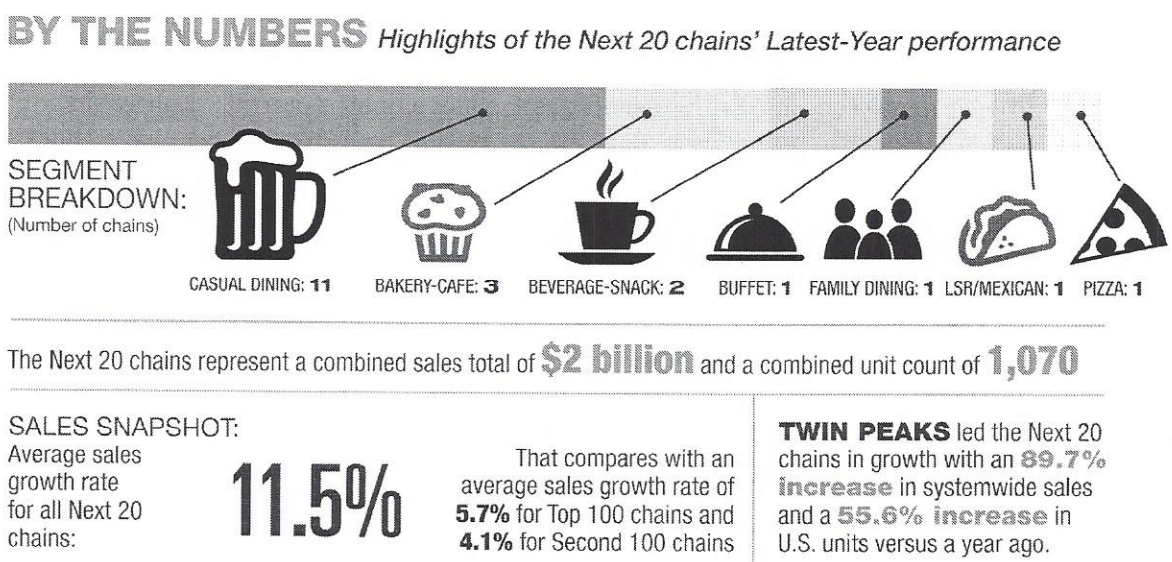
In a business where differentiation is key to success, strong positioning is driving the momentum of The Next 20 — a group of restaurant chains among which some are poised to crack into the ranks of Nation's Restaurant News' Top 200 by virtue of their sales volumes.

The inaugural Next 20 roster includes chains as varied as the Red Mango frozen yogurt system, with Latest-Year U.S. systemwide sales of $64 million from estimated sales per unit, or ESPU, of $357,500, and the high-end Del Frisco's Double Eagle Steak House, with domestic system sales of $124.7 million and ESPU of $13.1 million.

Though the list was pulled together while researching NRN's annual Top 100 and Second 100 censuses, these chains are not ranked No. 201 through No. 220 by reported or estimated Latest-Year U.S. systemwide sales. Instead, they were culled from that list, as some former Top 200 chains that contracted off the roster would have been ranked ahead of them in a straight sort. The Next 20 have not been featured in the Top 200 in the past.

The Next 20 chains — more than half of which offer polished or conventional casual-dining experiences — had average Latest-Year system sales growth of 11.5 percent, eclipsing the Top 100 chains' average of 5.7 percent and the Second 100's 4.1-percent average.



Smaller chains can be more agile than larger ones, fueling their growth, said Wallace B. "Wally" Doolin, a veteran chain operator who is now chairman of Thomas Doolin and Associates LLC, the holding company of People Report and Black Box Intelligence.

"For a couple of years now, I've been stuck on a quote by Rupert Murdoch, a man who built his fortune through amassing companies to create scale," he said. "His comment was, 'Big no longer beats small; fast beats slow.' That starts to speak to companies of all sizes, but clearly some smaller companies can move quicker and make adjustments that appear more local than they might be, even though they are a chain."

Particularly potent sales builders included Twin Peaks, a casual-dining chain largely associated with halter-top-and-shorts-clad female servers, counter-service Red Mango and fast-casual Cafe Rio Mexican Grill. That trio had year-over-year increases in Latest-Year U.S. systemwide sales of 89.7 percent, 30.6 percent and 25.9 percent, respectively.

But not all of the Next 20 concepts are relative newcomers in high-growth mode. Some are alternatively named clones of Top 200 chains, including the Souplantation brand, associated with the Second 100's Sweet Tomatoes, and Saint Louis Bread Co., the concept from which sprang now-larger sibling and Top 100 notable Panera Bread.

Other Next 20 chains are distinctly positioned operations that have added few restaurants in recent years — and may have even lost locations to lease expirations — but continue to be forces to be reckoned with in the markets where they compete. Within that circle are celebrity steakhouse concept The Palm and Il Fornaio, an early entrant into the polished-casual arena that is nearly as well-known for its frequency-building Festa Regionale loyalty program as it is for its upscale decor and authentic Italian food.

Recipes for growth

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Just how imperative growth might be for Next 20-type chains can depend on their ownership structure, according to John Gordon, principal at Pacific Management Consulting Group of San Diego.

"Where they are publicly traded or where there is a private equity flip envisioned, some growth needs to be shown [unless] it is a secondary brand that is totally overwhelmed by a larger strategic growth concept," Gordon said.

Regardless of ownership, he continued, all viable chains must be able to service their debt and generate enough free cash flow to fund unit remodels and rebuilds, if not new unit development.

"As quickly as the United States is changing — demographically, politically, socially and culturally we're such a broad country now — there does have to be some unit movement," Gordon said.

He said chains that resist the pressure to add units or simply are not in a position to do so must still strive to improve unit performance to counter inflation in commodities or operating costs, such as labor and utilities.

"A lower average ticket strategy can work for a period of time, but from a longer-term average-unit-volume standpoint, these [chains] have got to get AUV growth to maintain the unit economics model," Gordon said.

A full 75 percent, or 15 chains, of the Next 20 roster showed growth in Latest-Year ESPU, ranging from 0.2 percent to 19.6 percent. As a group, they had average growth in Latest-Year ESPU of 2.3 percent, which was lower than the Top 100's average increase of 3.2 percent but an improvement over the Second 100's 2.2-percent average rise.

HIGHEST SALES TOTAL:
$126.6 million
la Madeleine Country French Café

LOWEST SALES TOTAL:
$38.2 million
The Ultimate Stevi B's Pizza Buffet

MOST UNITS: **209**
red mango

FEWEST UNITS: **10** (tie)
Del Frisco's Double Eagle Steak House
Smith & Wollensky

ESTIMATED SALES PER UNIT:
15 of the 20 chains showed growth in ESPU.

Highest: **$13.1 million** Del Frisco's Double Eagle Steak House

Average: **$3.7 million**

Lowest: **$357,500** red mango

A strong bar component is an important part of today's hottest casual-dining chains, according to industry observers like research firm Technomic Inc. The Next 20's Rock Bottom Brewery, Gordon Biersch Brewery Restaurant and Brick House Tavern + Tap all have a sharp focus on beer. And the list's four steak-centric chains — Del Frisco's, Smith & Wollensky, Sullivan's Steakhouse and The Palm — are known for their full lines of libations.

A study by the Washington-based Hudson Institute think tank released earlier this year, "Lower-Calorie Foods: It's Just Good Business," found that between 2006 and 2011, 17 of 21 casual-dining and quick-service chains that offered lower-calorie foods and beverages saw sales of those products outpace those of traditional menu items.

First Watch and Gordon Biersch are among the Next 20 chains playing off the greater consumer interest in healthful fare. Breakfast and lunch chain First Watch has offered a Quinoa Power Bowl with chicken, kale and roasted tomatoes, while Gordon Biersch has sold a kale-quinoa pilaf and Superfood Salad with kale, blueberries, almonds and dried cranberries.

Growing consumer interest in foods perceived as more healthful has contributed to the rapid growth in franchised units at frozen yogurt purveyors Red Mango and Yogurtland, both of which in the Latest Year added net new U.S. units at rates above the Next 20 average.

Red Mango had Latest-Year and Preceding-Year growth in total U.S. units of 40.3 percent and 49 percent, respectively, while Yogurtland saw its domestic store base rise by 8.9 percent in the Latest Year after achieving blistering growth of 56.5 percent in the Preceding Year.

"I think there is enough wind in the sails from this [health] issue that early adopters who are truly genuine are going to do well," Doolin of People Report said.

He added, "I think what we will find routine at some point, like nonsmoking, is [a focus on] calories."

Other Next 20 leaders in domestic new store development included Twin Peaks and Cafe Rio, with Latest-Year growth of 55.6 percent and 23.9 percent, respectively.

Among all Next 20 chains, the average rate of Latest-Year growth in net new domestic locations was 6.6 percent, or more than double the average rate of growth for the Top 100, 2.7 percent, and the Second 100, 2.5 percent. Despite that relatively high overall average performance, just nine of the 20 chains showed an increase in net units, as six registered no change and five lost stores.

Nine of the Next 20 chains franchise their concepts to others. Two-thirds of the Next 20 chains that franchise showed Latest-Year growth in units, compared with a little more than a quarter, or 27.3 percent, of the chains that do not franchise.

Pacific Management's Gordon indicated that franchisors interested in spurring new unit growth or accelerating the pace of unit makeovers, including Next 20 licensors trying to bull their way into the Top 200, may want to take a page from Burger King's playbook.

"They have to get a big line of credit, backstopped by the company, so that franchisees can get money," he explained.

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Methodology and key terms

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METHODOLOGY

The Next 20 is the third installment in a series of exclusive NRN reports, including the recent Top 100 and Second 100, covering the performance of the largest organizations in foodservice.

NRN seeks to present relevant comparisons of the largest foodservice competitors by tracking U.S. consumer foodservice sales.

Figures are compiled using corporate documents and research studies as well as information from NRN news coverage, government agencies, chain officials, franchisees, industry analysts and peer-group tendencies.

Chains in The Next 20 are those tracked by NRN as part of its Top 200 research and that booked U.S. systemwide sales below the $134.4 million threshold for this year's Second 100. Next 20 chains have never been ranked in the Top 200, as former Top 200 qualifiers that have dropped in ranking because of declining sales were not eligible.

KEY TERMS

Estimated sales per unit: Sales-per-unit figures calculated using a proprietary formula that considers systemwide sales and change in year-end number of units. Units with atypical sizes or sales capacities may be excluded.

Fiscal year-end: The ending month of the fiscal year that corresponds to the study's Latest Year, between July 1, 2012, and June 30, 2013. If a fiscal year's ending date occurs in the first half of a month, the preceding full month is shown as its fiscal year-end.

Latest Year and Preceding Year: The consecutive fiscal years that ended just before and two years before the Latest-Year fiscal period, respectively.

U.S. systemwide foodservice sales: Foodservice sales at all domestic restaurants, stores or other outlets in a chain, including company-owned, company-managed, franchised and licensed units. Sales from merchandise, video games, facilities rentals and other nonfood sources, when discernable, are excluded.

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