Restaurant Same Store Sales Display Changes Needed

We all know the single number in the restaurant world that tends to drive the most commotion-- career upside and aggravation, fortunes made and lost, investor excitement and confusion and both good and bad tactical solutions launched is the same store sales trend number. It is a very sensitive metric. Yet restaurant operators explanation of the moving pieces behind the number is not what it could be; restaurants have some flexibility to display explanations to avoid perception problems.

As the world fills up with restaurants, three factors are seen everywhere:

•With restaurant expansion as the magic elixir of life for this business, both generally smaller, urban infill and non-traditional restaurant sites become important in order to find a site at all or the source the right site in the first place.
•Land, buildouts and equipment relating to restaurants have grown more and more expensive. Smaller footprint and asset light franchisors sites are quick to get into sites and to hold down the capital cost of the buildout.
•As a result of Wall Street's short term focus, the restaurant same store sales number is slapped into the restaurant brand like a pass/fail bumper sticker. No matter what the same store sales number is, it is never high enough or good enough (1).

One of the issues affecting same store sales results is the size and footprint of stores that are being developed (typically franchisee pays the CAPEX) and built (company pays the CAPEX). As real estate and rents have gotten more expensive, and sites more difficult to find, all kinds of variations of store footprints have emerged. This is healthy and reflects the reality of the real estate marketplace and required restaurant economics. Consider the following examples:

•In 2012, Chipotle (CMG), then in its prime buildup phase, announced it was developing its slightly smaller Type A store with a bit less kitchen and a smaller footprint. The company pointed out 50% of sales was take out anyway, and a large footprint wasn't required everywhere. The analysts and markets could not understand it, fearing somehow that sales potential was falling. That did not happen for four more years, for different reasons not relating to store size.
•In late 2017, almost the same thing happened with Dave and Buster's (PLAY), when it announced its movement to some 16,000 to 20,000 square feet stores, versus the larger 30,000 square feet store basic model. Some analysts were concerned that the AUV would be lower. Likely so, but time will tell, but Dave and Buster's noted that if the CAPEX is lower, the capital returns likely would be better.
•In the franchise space, both Dunkin Donuts (DNKN) and Sonic (SONC) franchisees are being encouraged to develop locations based in gasoline stores and some convenience stores. These stores have much lower AUV—sometimes only half that of a traditional store.

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(1) For some brands that reported same store sales increases in the past of over plus 10%, when the next quarter comes in at plus 8 or 9%, there is inevitable disappointment on the part of some observers, despite the fact that sustaining a plus 10% comp over a long period of time is impossible. Both Dominos (DPZ) and Chipotle (CMG) come to mind.

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The problem comes about when these different format stores enter the same store sales database—some 12 months to two years out as the brands define it. For example, with AUVs running in the $1.2M range, when AUVs in the $500K range come in, the average typically will fall.

The solution for restaurant operators is simple: as the mix of new store types materially change, simply breakout and restate separate values for the store types. If necessary, a weighted average same store sales number for the system as a whole can be shown, given the unit types can be done.

See the following as an example:

QSR Brand XXXXXX Same Store sales

Same stores sales, Traditional Stores: X.XX %

Same store sales, oil and gas store type: X.XX%

Weighted System Total: X.XX%

Another option is to convert same store sales (and potentially store level profit) to a per square footage basis and include that as a side display or as a footnote.

This really isn't that difficult, all the numbers typically exist. As a precedent, McDonalds (MCD) did this in the late 1990s as the number of smaller and limited menu McCafe's in the system were material, and were different enough from the traditional store types. Restaurant operators should be able to find and build economically viable sites, not bound by the intricacies of being beaten up on static same store definitions.

It is important to note that a same store sales number is a non GAAP number (non-generally accepted accounting principles); non GAAP conventions are typically defined in the 10Q/10K and audited financial statements. The federal and state regulatory comes out in favor of more disclosure, but it simply cannot be false or misleading. The Financial Accounting Standards Board (FASB) provides guidance and the SEC (2) encourages disclosure so long as it is not false and misleading.

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(2) Good background reading is the FASB opinions, at http://www.fasb.com, and the Securities and Exchange Act of 1934; and its associated Rule 10b5, enacted under 17 CFR 240.10b-5.

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