



December 6, 2011

Business Assessment

Objectives: Operations review, Income & cost opportunities, Market & competitive survey, Management structure, Renovation elements

Executive Summary

***** presents itself as a mature business in need of revitalization from both an operations and facilities perspective. While the validity of requisite capital investment is unquestionable, the spend level, in conjunction with specific operational objectives, needs to be derived via relatively conservative estimates of annual revenue and guest count gains, perhaps in the 4%-6% range. It is likely that the 2009 downturn in the macro environment changed the dining habits of a large segment of the original guest base who may have initially abandoned the brand due to personal financial conditions and have either not returned or not been replaced with a new guest base (along the lines of "out of sight, out of mind"). There is a confluence of factors involving real estate, value, facility and operations playing into the attrition.

From a competitive performance standpoint, the trade area appears to be strong with chain business ***** Ave relatively robust. The ***** site is disadvantaged, being located a ½ mile off of the main traffic artery and main food destination area with no retail drivers to entice people into the immediate vicinity. I would rate the real estate a "B" (as opposed to a "C") due to the heavy local concentration of office and industrial business in close proximity to the building coupled with decent weekday daytime traffic on the adjacent cross roads, good potential for curb appeal, easy access, great parking and some visibility from Highway ***** , which should improve by January with the completion of the road improvement project. Current visibility has been diminished from its prior level with the construction of the rise mound which completely obscures the restaurant from east bound freeway traffic. The good news is that ***** should be highly visible on the home bound drive. For weekend and post 6pm weekday dinner occasions, the site is destination, re-enforcing the importance of as much visibility as possible (i.e.: signage and lighting) and local store marketing. Lunch can generate strong business from a convenience standpoint as long as there remains adequate day pop and occupancy within the local businesses and there is a strong value proposition with a quick pace of experience.

Operationally, the management has hits and misses. In general the food is good. Any inconsistencies are minor and can be addressed with the use of proper training and recipe procedures. Collectively the staff appears to be positive , willing to perform and vested in the success of the business. There are also a significant number of loyal, higher frequency guests. On the opportunity side, the facility is worn and managed to the status quo with a loss of pro-active management and attention to detail. Upside presents itself in day to day leadership, organization, cleanliness and implementation with adherence to systems that will deliver better consistency in financial and operations performance. In the financial arena there is opportunity in food cost, back of house labor and operating expenses. Operationally there are many systems absent that help insure QSC. The specifics are addressed in the detail commentary following.



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Revenue

Of the four methods for building sales: price, merchandising, frequency and new guests; merchandising and new offer the most long term upside. Looking at competitor's menus, there is little room for price and the current guest base does not appear to be sufficient to generate meaningful income gains via frequency at regular pricing. With average weekly counts at ***** and ***** for lunch and dinner respectively, dinner appears to have the larger upside. Though one would want to suspend any heavy investment in outside marketing and advertising until completion of a facility upgrade, there are a few moves that may boost check and new trial utilizing internal promotion. The ability to drive check and margin should be significantly guided by promotional products.

- 1) If the "*****" proposition delivers a good margin and presents itself as a competitive value, it may benefit from more prominent panel positioning within the menu. Placing it on the back side of the third panel would make it immediately apparent upon opening the menu. This would be wise only if the margin is strong and one wants to purposely raise the mix and/or it holds promise for generating frequency in the short term.
- 2) The quarterly promotion with the *****. Once again, if the food cost is attractive, purposefully increase mix. Pre-shift meetings, contests, etc. Seems like guests enjoy it and the ones that are willing to part with the additional cash send a message that they are more interested in quality than price (thus the importance of bountiful portioning and perfect execution). The premium opportunities balance out the value oriented meal deal. Goes back to communication and training of the service staff.
- 3) Dessert menus should be presented by servers to each table at the appropriate time. They were just placing them on every table which, with the bar menu, was cluttering and taking up too much space. A lot of them were ripped and in poor condition. Shoot for a 6% dessert mix. An assigned person in the BOH is critical to the ticket time.
- 4) Looking at the other restaurants in the area, patios are in demand. The ***** has added or expanded their patio capacity at what looks like considerable expense and ***** patio is packed every night. The ***** patio should be clean, completely set for business and proactively offered on a daily basis at those times of the year when it is feasible to use it. Lots of opportunity with the cabana bar if it gets fixed up. Dedicated staffing would be key as well.
- 5) Lunch price points may be an opportunity. The major players on *****^h Ave ***** , ***** , ***** , *****) have many items in the \$7 to \$8 range. Either reducing pricing by \$1 on a few key items or adding more in the \$7 range may be a thought for the next iteration of the lunch menu.
- 6) Business cards. Though cliché, it's tried and true. Utilizing the fishbowl and business card program to put butts in seats Mon-Thu in the bar or on the patio via "bar parties" will make the restaurant look busier, potentially expose new guests and possibly generate meaningful income on their own if handled properly.
- 7) Fundraisers. There was a small fundraiser Sunday evening. Quantifying the goals and getting after this "higher quality discounting" will bring in a crowd that is at least willing to spend full price as opposed to coupons. Another avenue to expose new people to the brand.



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Competition

Over the course of the week we took a look at some of the major players located on ***** Ave. during lunch and dinner, weekday and weekend. In almost all cases table counts during peak hours were generally double or more compared to *****. When ***** had 12-15 tables for lunch, others had 28-35. Smaller restaurants such as ***** were at capacity. Larger footprints were 50% full. On weekend nights all concepts were on a wait ranging from 20 minutes to one hour extending to at least 9:30pm. It is hard to verify comp store sales but some relay positive low to mid single digits. I did hear from one ***** team member, who has the ***** as a common employer, that they were still down for the month year over year. ***** a new independent fast casual in-line, opened this week in the mall next to ***** with price points starting in the \$5.50 range (they do go way up for *****s-probably no purchasing power). Food does not appear to be a significant advantage for most the competitors but their facilities present themselves as superior to ***** from a total experience/value perception. Service is hot and cold. I ate at *****. The place was packed at 10pm and none of the staff was particularly friendly or engaging. Host staff at the other restaurants were rather perfunctory though I think that ***** had a good team and the bartenders at the ***** were working the crowd at the bar top. In absence of the ability to compete on media, service is a big opportunity for ***** to differentiate itself and create an advantage.

Income Statement

With a 27.3% restaurant operating profit there appears to be 1.5%pts available in two lines.

- 1) **Food Cost** running 29.3%. Traditionally ***** restaurants have run at a 3.5%-4.0%pt deficit to ***** units, mostly due to *****. If the ***** is at 23%, one would look for 26.5%-27% on the *****. Add in a potential additional cost for ***** versus ***** of about 1% and one should see food cost in the 27%-28% range. Of course, this is all dependent on the costs of current promotions, seasonal commodity costs, the price of ***** vs. ***** and the ***** base food cost. I would recommend asking for a department breakdown for food cost for several ***** restaurants as a comparison. It looks like ***** is running around \$5.50/lb which is likely a 35% premium to *****. Some aspects to monitor are ***** waste, line production waste and prep. An example would be ***** which has a shelf life of 3 days but had not been made all week as of Friday night. This product would need to be tossed. There are other products that are being made too often, having labor implications. Utilizing prep sheets and a waste report on a regular basis will aid in reducing waste. From what I could see on the P&L, comps seem to be reasonable, so excessive freebies do not seem to be playing a significant role.
- 2) **Back of House Labor** at 12.4% of food sales is a difficult comp as ***** ***** uses ***** and includes BOH lead hourly. One would have to request current performance numbers but would likely look for 8.5% to total sales with lead; a 0.5%pt opportunity from current year. Another factor is that, with soda into food, most ***** are probably running an 80/20 food/liquor mix. ***** runs much higher. There should be a prep program that semi automates the prep production, indicating when items should be produced based on shelf life in



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addition to designating specific hours to allocate to prep on a daily basis by department. One day this week, prep was being performed without prep sheets filled out ahead of time. Looking at the sheets, it does not look like the norm but if occurring a few times per week, it can have a material impact.

- 3) **Repair and maintenance.** Implementing a written and regularly updated prioritizing R&M list reviewed at each week's manager meeting will help prioritize spending. Cannot quantify savings without cost detail.
- 4) **Operating supplies inventory.** Perform a small wares inventory once per month to gauge needs more accurately.
- 5) **Budget.** Moving soda from liquor to food will raise liquor cost and drop food cost with a net wash. Also, recommend seasonalizing budget costs by the month, especially labor otherwise the managers miss the labor during low sales months and then hit it during busy ones when they should be beating it. It's just good to have realistic, true targets based on sales volume.
- 6) **Scheduling.** The schedule entered into ***** should match the budget goal. For example, the week of 11/14-11/20 the FOH was scheduled a forecast of 11.37% on \$***** in sales and ran 7.85% on \$***** in sales. It's good that they ran the labor but over projecting the hours leaves open a large margin of error and does not give the shift managers much guidance as to what to run in daily hours if sales are achieved.

Service

Though the service and host staff have a good grasp of hospitality and guest interaction for the most part, there are a number of key components that, if addressed, will improve the service levels. #1 is pace of experience, particularly as it relates to larger tables, especially important during lunch.

- 1) From observation, servers are given large parties in excess of 10 persons leading to drawn out waits for completion of order taking, ticket time, pre-bus, etc. Any table over 10 persons should have 2+ servers assigned. One is better off with 2 servers assigned to a large party and having 2 additional tables each than 1 server with 20 and another with a 4 table station. The "I'll help" position does not really work out.
- 2) Incomplete trays. This is a kitchen communication and training issue. The ***** are out with the *****s dragging 5 minutes. Visibly awkward for the guests. This also includes ***** which need someone assigned and dedicated on ***** during the rush otherwise servers are producing after ***** arrive (small point but large service impact).
- 3) Though ticket times were generally good, we had a few at 20+ with one running 28 min for a 12 top Sunday night. Due to new cook.

#2 is making sure that host desk is manned 100% of time during peak hours and front manager is out front watching tables, body language, eye contact, music, lighting, etc. In the event that there is only one host, this is a good position for the manager to work into the floor management. What is currently happening is the front manager is spending too much time on expo and leaving the front unattended during peak business. This is because the CHEF has to jump behind the line and that in turn is because the training program for new cooks is not organized and regimented and not everyone in the kitchen seems



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to be able, or maybe not directed, to jump on the line prior to the rush. Some of this may be prep oriented which goes back to prep sheet planning.

#3 Training program. It's very loose with no final exams, CT review, etc., etc. Implementing will improve service, build credibility and reduce <60 day turn which also has financial implications related to hard costs and soft costs. Goal should be 20% or lower for less than 60 day turn for new hires. Managers using "interview assistant" and formalizing the anointment process for each position will save money and improve service, both front and back. As an example, if a restaurant with a staff of 80 @ 70% annual turn hires 56 people per year at an average cost of \$750 each and loses 20% vs 50% in first 60 days, the savings are about \$12,600. That is hard cost only.

Establish seasonal pars for each department and hire to the par 60 days in advance using the aforementioned interview and training process. Currently there are 26 staff including 16 servers in the front with lots of doubles. Probably need 20-22 servers though it is apparent they are attempting to cover the income requirements of the more senior staff and recent sales do not require the increased par. BOH has 15 on the schedule which may be 2 short of where a \$*. *M unit needs for complete coverage and flexibility.

Product

Overall, food tasted very good. Found a couple of items out of spec all of which were due to no reference to recipe book. The kitchen needs an updated book out, available and referred to regularly. Guest comments received tableside were all positive on food.

Management Structure

The restaurant needs full time daily leadership. We reviewed an example schedule that reflects strong coverage with either a GM or CHEF in the building and presence during peak volume periods with adequate back-up to accomplish administrative and staff development functions. Pre-shift, training follow-up, sanitation, manager meetings, P&L review, assistant manager development (working with the GM two shifts per week), etc. BOH coverage is supplied via lead hourlies which gives flexibility in cost management and also provides a pipeline for bench strength. Cost as written is \$234k annually which is in line with current year but adds management capability. Administration and office organization are opportunities. Schedules should be complete, approved and posted by Friday morning at the latest.

Facility: Operations

The kitchen needs a thorough cleaning. Reach-ins, racks, equipment, ***** holders, walls, etc. There are no side work/sanitation sheets in place and no weekly rotation of equipment cleaning. Front of house tables and chairs are OK but chip stations, back bar, areas where one starts looking behind and under all need attention. Restroom checks are not performed regularly, not specifically assigned and need detail cleaning in toilet areas.



Facility: Capex

With respect to a remodel, it would be best to accomplish the operations initiatives prior to refreshing the physical plant. We reviewed a timeline that would accomplish a complete operations plan, implementation and follow-up by mid January.

A refresh could be accomplished in stages starting with exterior paint, lighting, signage, landscaping (trim palms) and patio. ***** has a call into the city regarding regulations pertaining to pole sign height and size limitations. There are a lot of exterior lights not functioning. Removal of the awnings is an option, replacing with some sort of trellis and down lighting with the possible addition of one large glass window replacing the individual frames which would showcase the dining room much better from the outside (cost prohibitive?). New front door. Interior paint. Tables and chairs could follow. Finalize with restrooms, back bar, lots of glass shelving and lighting. Remove interior dining "barn doors" and turn the area in front of ***** more into a plaza. ***** would have a stand-up style bar with stools and 1' top glass partition. Maybe an additional entrance into the bar from the dining room. This would be problematic with the Friday DJ but the music may have eroded some of the Friday night dining business during the past few years which has made itself more apparent with the economic downturn. I do not think there is a lot of value in resurfacing the parking lot right now unless it can be done inexpensively. ***** spent \$50k doing *****. There is also some equipment repair/replacement needed on the kitchen line and behind the bar in addition to new chip warmers. Repair all interior lighting, rheostats and music.

Would probably add fresh uniforms to the list as well.

Miscellaneous for Review

- | | |
|-------------------------------------|--|
| Server check cards | Tray use |
| Ticket time awareness | Restroom checks |
| Staffing levels 90%+ | Hourly reviews |
| All team members pass position test | Coupon procedures |
| Interview procedures | Lights, music, air co (make sure not running while closed) |
| Food safety program | Pre-shift meetings |
| BOH side work & sanitation | Dessert menus |
| Server order pads | Plumbing system |
| Check delivery & timing procedures | Operating supplies inventory |
| Plate ware | |



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Conclusions

The key to improved sales will be GM/RM leadership concurrent with development of the managers prior to initiating a remodel. Once a plan of action has been established by the GM and CHEF, the assistants and keyhourlies should be brought up to speed on the operations initiatives related to management. After a period of practice and follow-up (such as training, kitchen communication, preparing the shift, systems for ticket times/*****/cross training/sanitation) for a week or two, institute staff training refresh (food knowledge, sequence of service, organization, etc). Two or more additional weeks of follow up required. Produce a written, agreed upon budget for all training. Cost should be minimal, perhaps 0.5% of total sales over a two month period.

One scenario on a \$***,*** remodel investment would require an approx. 8.5% lift on \$*.*M in sales to return \$***k, or 50% of the investment, the first year on current cost structure at the restaurant CP line (before rent). Gains in food and labor costs would improve flow reducing the requisite sales gain. 4.5% of the gain would have to come from ops with the remaining 4% from the improved facility.

SAMPLE



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Exhibits

Exhibit A		Purch \$Mix	Cost prem
Food Cost	US Region base base	23.0%	
Prem. Meat commodity analysis	Produce	1.3%	28.3%
	(Brand proprietary product)	0.9%	19.6%
	Other	0.9%	37.0%
	Premium meat	1.0%	15.2%
	Unit with soda in	27.1%	

Exhibit B		Old	Soda	New		
Soda impact						
Data: YTD Nov. 2011	Sales Food	\$1,515,174	\$128,500	\$1,643,674		
	Sales Liq	\$838,085	(\$128,500)	\$709,585		
	Total	\$2,353,259	\$0	\$2,353,259		
	Food Cost	\$444,608	\$8,995	\$453,603	29.3%	27.6%
	Liq Cost	\$210,384	(\$8,995)	\$201,389	25.1%	28.4%
	COGS	\$654,992		\$654,992	27.8%	27.8%

Exhibit C		M	T	W	T	F	S	S	Annual
Management Schedule & Cost	GM	X	X	OPEN	OPEN	10-10	10-10	10-10	\$60,000
	AM	OPEN	OPEN	X	X	OPEN	CLOSE	CLOSE	\$35,000
	AM	CLOSE	CLOSE	CLOSE	CLOSE	CLOSE	X	X	\$35,000
	KM	OPEN	OPEN	X	OPEN	10-10	10-10	X	\$50,000
	LH@\$12/hr	4-12	4-12	4-12	X	7-3			\$19,868
	LH@\$12/hr				4-12	4-12	4-12	4-12	\$19,868
	LH@\$12/hr			7-3			7-3	7-3	\$14,901
									\$234,637

GMKM schedule can alternate. Goal is to have at least one in the building
AM schedule can be flipped so one is not always closing.
LH can pick up hourly positions on none lead hourly days-good development position



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Exhibit D
Revenue-Remodel

	Shift Tbls	Tbl Occ Cts	Day turn	Cts		Days	Chk	Revenue	%	COGS	%	Labor	%	Other	%	CP	%
Total				165,860	100.0%	362	16.52	2,740,000	100.0%	802,820	29.3%	830,220	30.3%	358,940	13.1%	748,020	27.3%
Lunch M-F	27	81	3.2	66,300	40.0%	258	11.27	747,201	27.3%								
Lunch Sat-Sun	27	81	2.6	22,100	13.3%	104	11.65	257,465	9.4%								
Lunch Total	27	81	3.0	88,400	53.3%	362	11.37	1,004,666	36.7%								
Dinner	34	102	2.1	77,460	46.7%	362	22.40	1,735,334	63.3%								
Patio use	11	33	1.0	4,004		121	14.00	56,056	2.0%	16,424	29.3%	3,363	6.0%	-	0.0%	36,268	64.7%
Cantina parties		10	1.0	2,080		208	10.00	20,800	0.8%	10,171	48.9%	1,248	6.0%	-	0.0%	9,381	45.1%
(Lunch price)	27	81	3.2	49,725	75.0%	258	(1.00)	(66,300)	-2.4%	-	0.0%	-	0.0%	-	0.0%	(66,300)	100.0%
(Dinner price)																	
Lunch Ct+	30	90	0.5	12,605	19.0%	258	10.52	132,600	4.8%	38,852	29.3%	7,956	6.0%	-	0.0%	85,792	64.7%
								2,883,156	105.2%	868,267	30.1%	842,787	29.2%	358,940	12.4%	813,161	28.2%
Remodel														200,000			
				5,410	3.3%		15.85	85,746	3.1%	25,823	30.1%	25,065	29.2%			34,859	40.7%
2012								2,968,902	108.4%	894,090	30.1%	867,852	29.2%	358,940	12.1%	848,020	28.6%
								228,902								100,000	1.3%