

Consumer

KOL Highlights: Food, Distribution, and Restaurant Themes

CONCLUSION

The Piper Sandler Packaged Food, Transportation Technology, and Restaurant analysts hosted a call with Marc Wulfraat, Founder & President of MWPVL International, a supply chain, logistics & distribution consulting firm. Key highlights included: 1. Digital is an increasingly important capability in the forms of delivery, rapid pick-up, click and collect. 2. Consumers are reluctant to pay for delivery, forcing a push for efficiencies, and... 3. ...higher online prices, as much as 10%+ in grocery and 20% at restaurants. 4. Supply chain disruptions are here, especially for meat plants; higher protein prices are possible. 5. Consumers are shifting from fresh/prepared foods to shelf-stable, center store categories. 6. Despite rising unemployment, labor inflation is real, fueling automation efficiencies.

- E-commerce gains likely structural; scale requires efficiencies.** E-commerce as a share of grocery sales has increased from 4-6% to ~40% during COVID-19, and a level around 20-25% may be likely once COVID-19 subsides as consumer behavior shifts. Greater efficiencies are needed to drive profitability, as unprofitability at greater scale is unsustainable. Grocery delivery requires 6-10x the paid labor as retail, with roughly 50% of labor costs from "last mile" delivery. Companies can drive efficiencies by promoting click & collect, investing in automation, micro-fulfillment, and inventory management.
- Center store takes center stage; consumers shift gear.** Prior to COVID-19, consumer demand was growing for fresh and prepared foods at the expense of center-store categories, which has reversed now as food at home takes share from restaurants. We view our covered food names in three groups: Meal and meal ingredient skewed (biggest beneficiaries), snacks skewed (less upside from shifts from restaurants), and those with heavy foodservice exposure (risk from lower restaurant sales); details inside note.
- COVID-19 hits protein supply chain; shortages likely.** COVID-19 has closed a third of US meat production (18 plants closed), with ~2,200 known cases across 48 US plants. These processing plants contain thousands of workers that operate in tight conditions, and it could be difficult to adjust operating procedures without slowing output, or risking food safety. We expect supply chain disruptions may reduce supply, driving prices up.
- UBER-like delivery has a long-term role; the math needs work.** Food delivery is 22% of UBER's (N) gross bookings and ~11% of adjusted net sales. With COVID-19, demand has skyrocketed, but we don't think margins are necessarily improving, as the industry is too inefficient to handle this unexpected demand surge. Wulfraat pegs the true labor cost at \$11-12/delivery (even up to \$20); how many consumers are willing to add that to their bill? The solution: combine higher prices with higher delivery volume and a more efficient (automated?) pick-up process. Automating delivery, though, looks far-fetched.
- Restaurants/Branded Hospitality Conclusions:** Human capital and access to capital are keys to the restaurant industry's future. We expect labor inflation ahead, with the potential for relaxed rent as an offset. Digital is a valuable asset in the form of delivery (up 2x-3x across industry) and builds a loyal, direct relationship with the end user, but comes at a cost that must be addressed, as we expected elevated levels to persist. As protein plants face broad closures, commodity inflation is a growing risk (see p. 9 for commodity-specific exposure by company). We expect scale to prevail and maintain our narrowed focus investment list: OW-rated CMG (+digital) and WING (+ digital/- chicken exposure).

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BGS	18.67
BYND	88.46
CMG	882.26
CPB	50.80
GIS	60.19
HAIN	27.19
HRL	48.40
HSY	143.28
K	64.68
KHC	28.76
MDLZ	52.22
POST	91.03
TSN	59.92
UBER	28.24
WING	112.44

INDUSTRY RISKS

Risks include currency moves, commodity costs, supply chain constraints, and shifting consumer preferences

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The Food world has been turned on its head

Grocery (Food at Home) is regaining share from restaurants (Food away from Home)

- Prior to COVID-19, there was a decades-long trend of restaurants and food away from home gaining share of consumers' wallet
- The Food away from Home spend crossed 50% of the total in recent years
- Latest estimates had Food at Home at 47% of total food spend
- Now, restaurant sales are down 60-70% and grocery sales are up 20-35% or more

Center-store categories are taking center stage

- Meal and meal replacements have the most upside, taking share from restaurants
- Categories that have benefitted the most include categories under long-term pressure
 - Canned soup, pasta/pasta sauce, canned vegetables, cereal are up significantly

Fresh, perimeter-store, prepared foods, etc. have fallen out of favor

- Shifts appear to have two dimensions: channel shift (foodservice to grocery) and product shift (within grocery purchases), based on latest retail scanner data
- Consumer concerns about fresh foods that may be handled by someone else and/or food that could be exposed to the open air have added headwinds to these categories
- Suppliers of foodservice outlets could be impacted by restaurant closures

Three phases: Stockpiling surge, restaurant closures, and afterwards

The first initial retail surge was stockpiling (roughly 2 weeks ended March 22)

- Consumers were panic buying necessities for staying home
- The US Department of Homeland Security recommended enough supplies for 2 weeks
- In this period, retail sales for some suppliers were up over 100% (details on next slide)
- Favored categories were often canned or frozen foods (i.e. non-perishables)

Restaurant closures drive the near-term dynamics

- Our scanner data now runs through April 5th with very different trends in the 2 weeks ended April 5th vs. the 2 weeks ended March 22nd
- Most suppliers sales lift was closer to a 30-40% gain in the 2 weeks ended April 5th
- We consider this period to likely be indicative of trends until restaurants reopen (details on slide 5)

Afterwards? Trends for any 'new normal' not yet known, but survey suggests upside

- Our consumer survey (detailed on slides 6-7) points to sustainable upside for Food at Home (i.e. grocery sales)
- Some consumers are reluctant to return to restaurants
- Broadly, consumers indicated more expected Food at Home consumption to continue

Greater consumption of food at home is driving sales lifts

Recent US retail data show a strong lift during COVID-19

- Stronger demand at retail and shifting meal occasions from restaurants is lifting sales for packaged food companies
- Stockpiling appeared likely during mid-March, when retail sales grew 55-115%
- Measured US retail sales growth was up 30-40% in the recent two weeks (ending April 5, per IRI)
- E-commerce sales are likely up even more, as consumers take fewer trips outside
- Hormel, Tyson, Campbell, and General Mills are tracking to ~20% C2Q20 retail growth

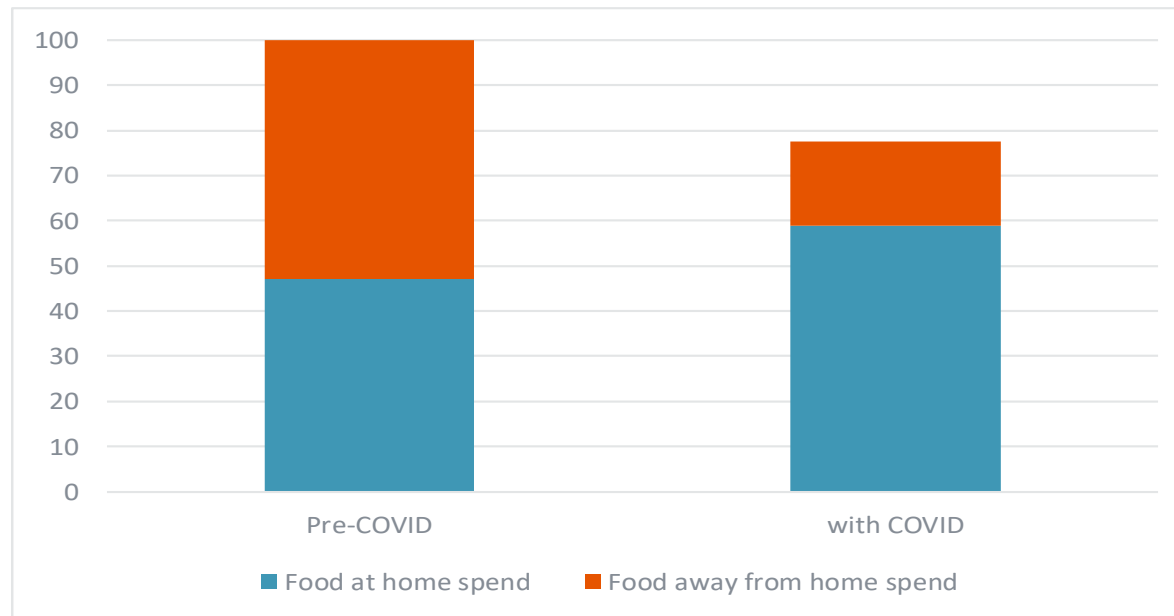
	3/1/2020	3/8/2020	3/15/2020	3/22/2020	3/29/2020	4/5/2020	Latest 2 weeks	C1Q20
B&G Foods	-1.0%	1.4%	88.4%	107.3%	35.9%	42.8%	39.4%	13.9%
Hormel Foods	4.8%	14.9%	111.3%	113.9%	38.0%	35.6%	36.8%	21.9%
General Mills	2.2%	11.0%	97.1%	101.8%	30.3%	35.0%	32.6%	19.7%
Tyson Foods	1.1%	6.5%	88.5%	101.2%	27.5%	33.0%	30.3%	20.1%
Campbell	3.8%	15.2%	110.7%	105.3%	27.4%	27.5%	27.5%	19.5%
Kraft Heinz	-2.4%	3.0%	72.3%	82.7%	22.6%	29.9%	26.2%	12.1%
Post Holdings	-3.1%	-1.2%	68.1%	72.5%	17.1%	22.0%	19.5%	11.9%
Mondelez	0.2%	5.7%	61.8%	59.5%	13.3%	14.3%	13.8%	10.0%
Kellogg	-3.0%	4.2%	63.8%	64.9%	6.9%	11.5%	9.2%	10.0%
Hershey	0.9%	5.0%	20.0%	16.0%	1.2%	11.7%	6.4%	4.6%
Hain Celestial	-3.4%	4.8%	65.4%	52.1%	5.3%	7.4%	6.4%	5.9%

Source: IRI, Piper Sandler Co.

Restaurant closures could drive a ~25% baseline lift in grocery sales

- We believe a shift to at-home food consumption from restaurants and cafeterias could drive a ~25% lift in grocery food sales until they reopen
- Before COVID-19, just over half of US food spend was on food away from home (though the volume consumed at home is more, as it is cheaper)
- If foodservice sales fall ~65% (consistent with recent metrics), grocery sales could be up by ~25%, even as total spend falls sharply (chart below)
- We expect food consumption to primarily occur at home until restaurants reopen and consumers feel comfortable eating out again, which could get underway in May

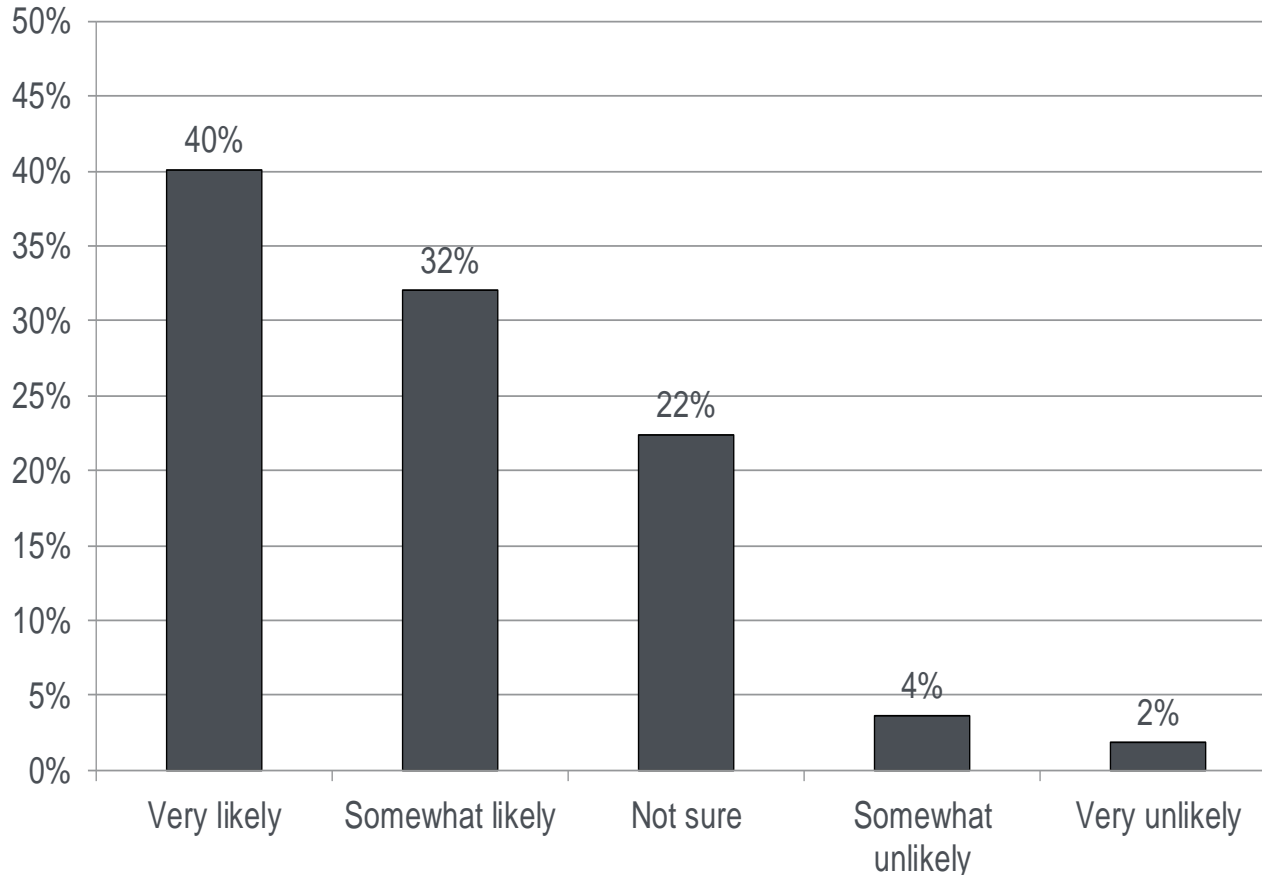
Estimated increase in at-home food consumption during COVID-19



Source: Piper Sandler Co.

Our proprietary consumer survey suggests sustainable sales lift ahead

“Do you expect to cook at home more than you used to once COVID-19 concerns are over?”



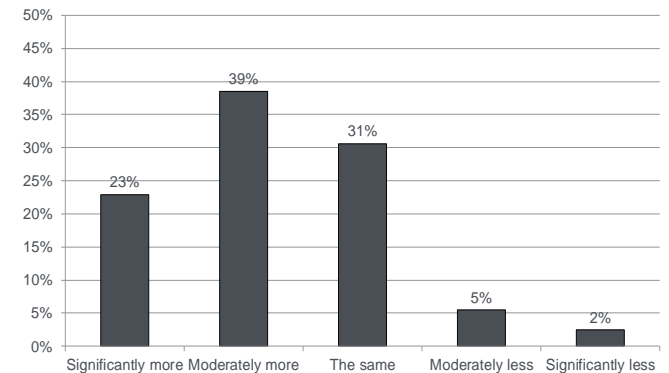
67%

Net More Likely to Cook at Home

- ~450 consumers surveyed
- Expectations for cooking at home more often once COVID-19 concerns are over are strong, with 72% of respondents saying they are “Very likely” or “Somewhat likely” and just 5% saying “Very unlikely” or “Somewhat unlikely”

- Spending for groceries has increased as food consumption shifts from restaurants to at-home
- 40% of survey respondents are unlikely or not sure if they will return to restaurants as soon as they reopen (**next slide**).
- A net 67% of respondents expecting to cook more at home, which suggests to us that some sustainable lift from recent shifts is likely

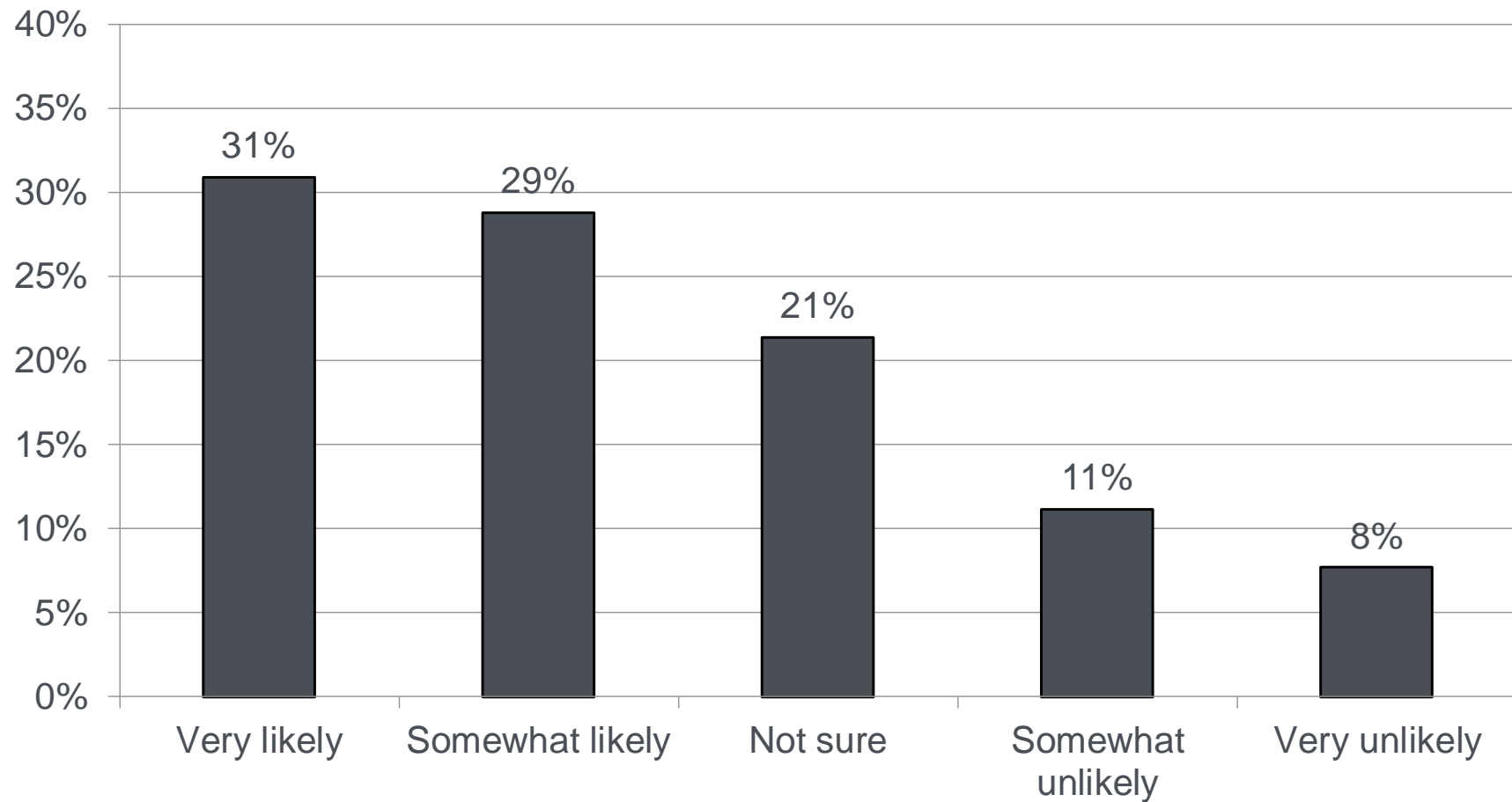
“Amidst COVID-19, roughly how much have you spent on groceries vs. normal?” (bottom chart)



Source: Piper Sandler Consumer Survey

Cooking at home likely to continue after COVID-19 concerns subside

“What is your likelihood of going back to restaurants as soon as they reopen following COVID-19?”



- 60% of respondents are likely to return to restaurants as soon as they reopen
- 40% are unlikely or not sure if they will return to restaurants as soon as they reopen

Food Manufacturer portfolio composition matters

Not all benefit equally; we see portfolios in three buckets:

- **Skewed to meals and meal ingredients**
 - Meal and meal replacements have the most upside, taking share from restaurants
 - Likely the biggest beneficiaries of sustained shifts to Food at Home
 - Companies include: General Mills (OW), Campbell (OW), B&G Foods (N), Kraft Heinz (N)
- **Skewed to snacks**
 - Snacks sales are less likely to replace a restaurant purchase
 - Still strong demand, little downside risk, but less upside benefit likely
 - Companies include: Mondelez (OW), Kellogg (OW), Hershey (OW), Hain (N)
- **Heavy dependence on foodservice sales**
 - Suppliers of foodservice outlets could be impacted by restaurant closures
 - Most companies have ~10% or less of sales to foodservice; relatively manageable
 - Exposure to foodservice above these levels poses risk
 - Companies include: Beyond Meat (N; 50% foodservice), Post (OW; 30%), Tyson (OW; 30%) and Hormel (OW; 30%)

Commodity-Specific Concentrations Across PSC Restaurant Coverage

Limited Service	COGS Margin	As a % of COGS Basket									
		Proteins					Dairy	Coffee	Grains & Produce	Paper/Packaging, Transportation, & Other	All Other
		Beef	Pork	Poultry	Seafood						
Restaurant Brands International	nm	nm	nm	nm	nm	nm	nm	nm	nm	nm	
Del Taco Restaurants, Inc.	28.4%	19.0%	nm	9.5%	nm	9.5%	nm	19.0%	10.0%	33.0%	
Dunkin' Brands Group, Inc.	nm	nm	nm	nm	nm	nm	nm	nm	nm	nm	
McDonald's Corporation	31.8%	15.0%	nm	15.0%	nm	15.0%	4.5%	22.5%	4.5%	23.5%	
Wendy's	31.9%	20.0%	2.0%	20.0%	2.0%	8.0%	nm	10.0%	nm	38.0%	
Starbucks Corporation	32.5%	nm	nm	nm	nm	7.0%	17.0%	18.0%	34.0%	24.0%	
QSR Average	31.2%	18.0%	2.0%	14.8%	2.0%	9.9%	10.8%	17.4%	16.2%	29.6%	
Chipotle Mexican Grill, Inc.	32.8%	15.0%	2.0%	15.0%	nm	7.0%	nm	19.0%	nm	42.0%	
Fiesta Restaurant Group, Inc.	31.9%	5.9%	3.3%	24.8%	nm	4.9%	nm	7.6%	nm	53.5%	
Noodles & Company	26.3%	3.9%	3.3%	13.6%	4.5%	9.8%	nm	38.9%	19.7%	6.3%	
Potbelly Corporation	26.5%	12.5%	na	12.5%	nm	11.0%	1.0%	12.0%	10.0%	41.0%	
Wingstop	36.1%	0.0%	0.0%	65.0%	0.0%	0.0%	0.0%	20.0%	nm	15.0%	
Shake Shack, Inc.	29.0%	31.0%	3.0%	nm	nm	18.0%	nm	27.0%	12.0%	9.0%	
Fast Casual Average	30.4%	11.4%	2.3%	26.2%	2.3%	8.5%	0.5%	20.8%	13.9%	27.8%	
Limited Service	30.8%	14.7%	2.2%	20.5%	2.1%	9.2%	5.6%	19.1%	15.0%	28.7%	
Full Service	COGS Margin	As a % of COGS Basket									
		Proteins					Dairy	Coffee	Grains & Produce	Paper/Packaging, Transportation, & Other	All Other
		Beef	Pork	Poultry	Seafood						
BJ's Restaurants Inc.	25.8%	16.0%	nm	11.0%	12.0%	12.0%	nm	19.5%	11.5%	18.0%	
Cheesecake Factory Incorporated (The)	23.0%	nm	nm	14.0%	9.0%	13.0%	nm	28.0%	nm	36.0%	
Darden Restaurants, Inc.	28.3%	18.0%	nm	7.0%	10.0%	10.0%	nm	19.0%	nm	36.0%	
Dave & Buster's Entertainment, Inc.	26.3%	11.0%	11.0%	16.0%	8.0%	7.0%	nm	47.0%	nm	0.0%	
Brinker International, Inc.	26.7%	15.0%	5.0%	15.0%	2.0%	9.0%	nm	15.0%	nm	39.0%	
Casual Dining Average	26.0%	15.0%	8.0%	12.6%	8.2%	10.2%	nm	25.7%	11.5%	25.8%	
The ONE Group Hospitality, Inc.	26.6%	36.0%	nm	nm	17.5%	5.0%	nm	10.0%	27.0%	4.5%	
Ruth's Hospitality Group, Inc.	29.9%	40.0%	nm	nm	17.5%	5.0%	nm	10.0%	25.0%	2.5%	
Fine Dining Average	28.3%	38.0%	nm	nm	17.5%	5.0%	nm	10.0%	26.0%	3.5%	
Full Service	27.1%	26.5%	8.0%	12.6%	12.9%	7.6%	nm	17.9%	18.8%	14.7%	

Source: Company filings, Piper Sandler estimates

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- I: Initiating Coverage
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- T: Transferring Coverage
- D: Discontinuing Coverage
- S: Suspending Coverage
- OW: Overweight
- N: Neutral
- UW: Underweight
- NA: Not Available
- UR: Under Review

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Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [OW]	478	58.58	125	26.15
HOLD [N]	319	39.09	51	15.99
SELL [UW]	19	2.33	1	5.26

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