



# Mid-Year Review of the Restaurant Industry & Economy

## July 31, 2008

### Introduction

This report provides a summary of current conditions in the restaurant industry and key economic indicators. The restaurant industry faced a challenging business environment in the first half of 2008, with food and energy costs rising at their strongest rates in nearly three decades. Overall, despite a sluggish economy and softer consumer spending, the restaurant industry is expected to post positive sales growth in 2008.

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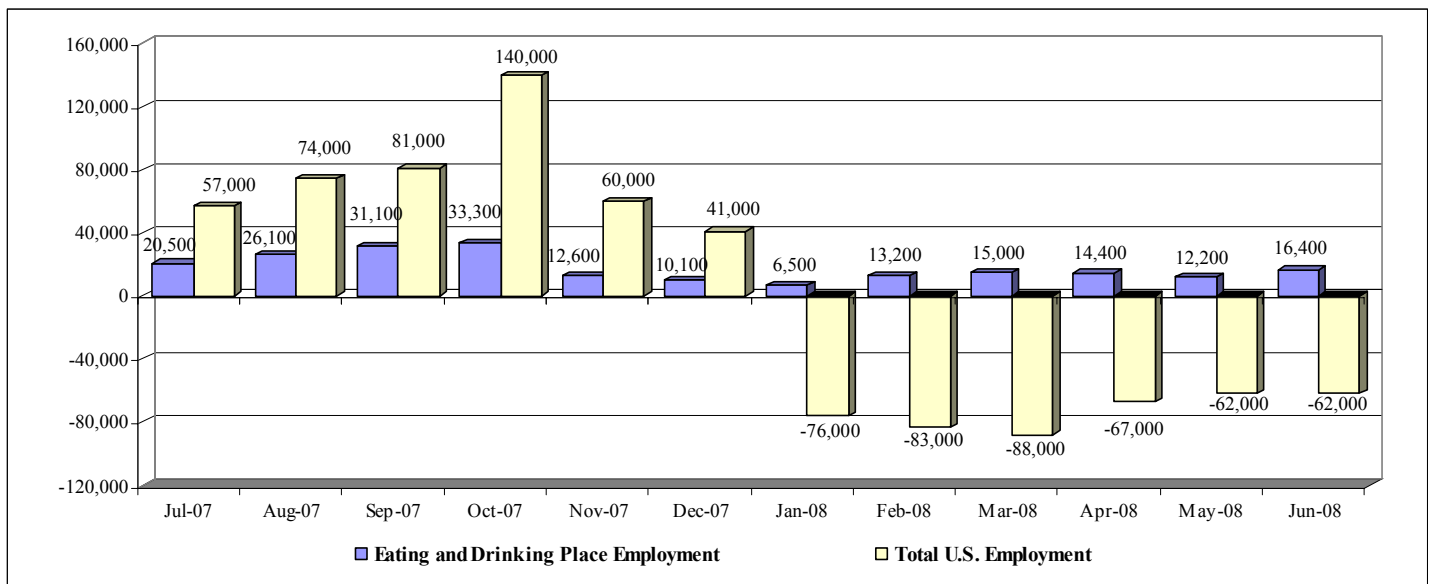
## National Economy Shed Jobs in Each of the First Six Months of 2008

- The national economy lost jobs for the sixth consecutive month in June, a sign that the economy is most likely in a jobs recession. The economy shed 62,000 jobs in June on a seasonally-adjusted basis, bringing the total job losses during the last six months to 438,000. The losses in the first six months of 2008 came on the heels of 52 consecutive monthly gains, during which the national economy added nearly 8.3 million jobs.
- Job losses during the first half of 2008 were concentrated in the nation’s private sector. The private sector lost 564,000 jobs during the first six months of 2008, while 126,000 government jobs were added. Within the private sector, goods-producing employers cut 471,000 jobs, while service-producing employers cut 93,000 jobs. This indicates that the economic weakness is spreading beyond the goods-producing sectors.

## Restaurant Industry Job Growth Continues

- In contrast to the trends in the overall economy, the restaurant industry continues to add jobs, according to figures from the Bureau of Labor Statistics. Eating and drinking places – the primary component of the restaurant industry which accounts for roughly three-fourths of the total restaurant and foodservice workforce – added 16,400 jobs in June on a seasonally-adjusted basis, their 21st consecutive monthly gain. Overall, during the last 21 months, eating and drinking places added 466,000 jobs.
- Employment gains in the restaurant industry are being driven by continued consumer spending, albeit at reduced rates.

### Monthly Job Growth: Eating and Drinking Places vs. Total National Economy

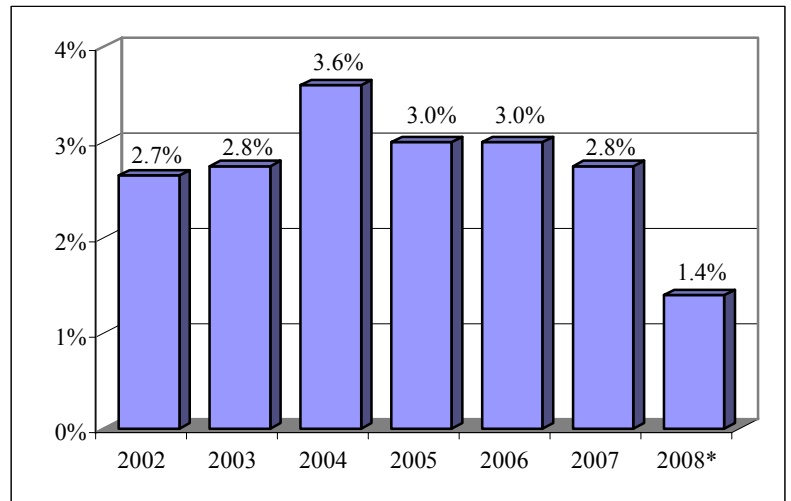


Source: National Restaurant Association analysis of Bureau of Labor Statistics data; figures are seasonally-adjusted

## Consumer Spending on Pace for Slowest Growth in 17 Years

- Despite the national job losses, overall economic activity expanded in the first half of 2008, albeit at a sluggish pace. Real gross domestic product (GDP) – the value of goods and services produced in the United States – grew at a 1.9 percent annualized rate in the second quarter, which followed a 0.9 percent gain posted in the first quarter.
- Personal consumption expenditures, which account for over two-thirds of total economic activity, grew at a modest 1.4 percent rate on a year-to-date basis through June 2008. If the trend continues, it would represent the slowest consumer spending growth since 1991.

## Real Growth in U.S. Personal Consumption Expenditures



Source: Bureau of Economic Analysis; NRA \*Year to date growth through June

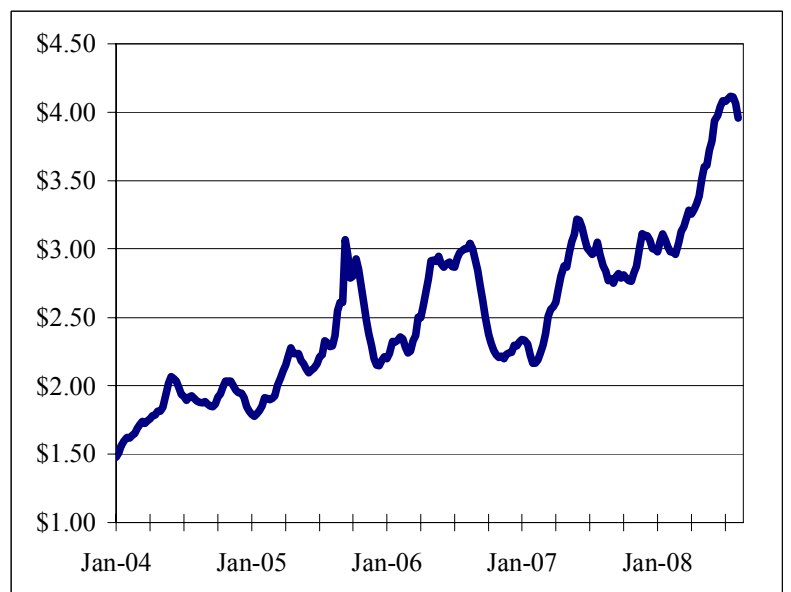
## Disposable Personal Income Jumped in the Second Quarter as Stimulus Checks Arrived

- A positive development was the sharp rise in disposable personal income in the second quarter as stimulus checks began to arrive. Real disposable personal income increased at an 11.3 percent annualized rate in the second quarter, its strongest quarterly gain in more than six years. This is positive news for the restaurant industry, as a large proportion of the industry's growth is driven by cash on hand.

## Gas Prices Fell Below \$4 for the First Time in Eight Weeks

- After hitting a record high of \$4.11 on July 7, gas prices fell for the third consecutive week, according to figures from the Energy Information Administration. The nationwide average retail price for a gallon of regular gasoline fell to \$3.95 on July 28, which represented the first reading below \$4 in eight weeks.
- However, it is now likely that average pump prices in 2008 will be more than \$1 higher than they were in 2007. This will cost consumers more than \$100 billion, which will essentially gobble up much of the tax rebate checks that were sent to households beginning in May, and will likely have an overall dampening effect on the economic stimulus package.

## Average Price per Gallon of Regular Gasoline

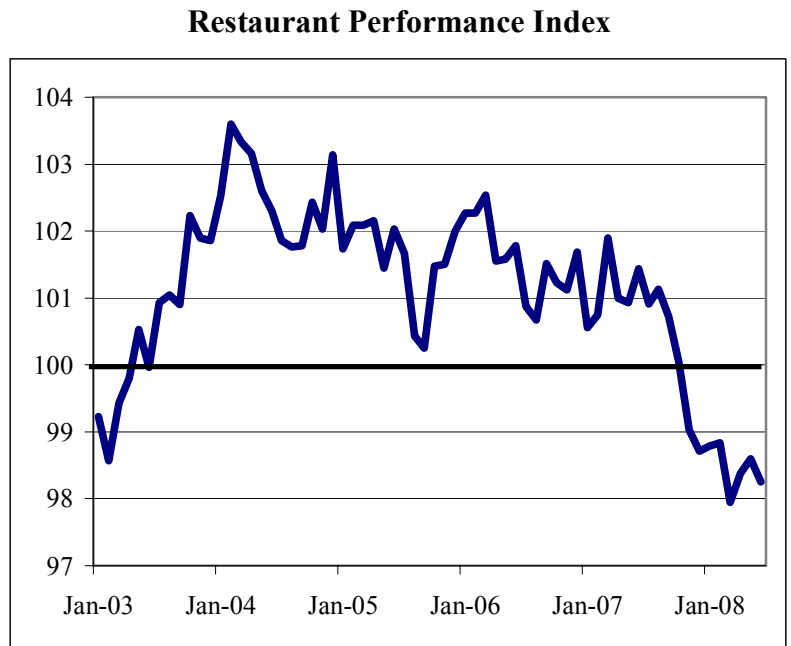


Source: Energy Information Administration; NRA



## Restaurant Performance Index Averaged 98.5 during the First Half of 2008

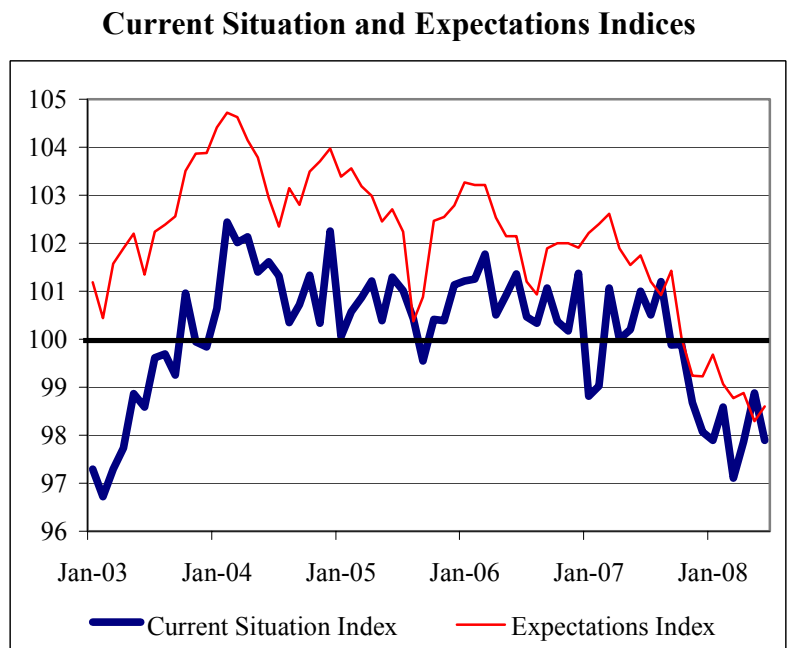
- Restaurant industry performance softened in the first half of 2008, according to the National Restaurant Association’s comprehensive index of restaurant activity. The Association’s *Restaurant Performance Index (RPI)* – a monthly composite index that tracks the health of and outlook for the U.S. restaurant industry – had an average level of 98.5 during the first half of 2008, the lowest six-month average in the six-year history of the index. This included a record-low level of 97.9, registered in March 2008.
- The *Restaurant Performance Index* is constructed so that the health of the restaurant industry is measured in relation to a steady-state level of 100. Index values above 100 indicate that key industry indicators are in a period of expansion, while index values under 100 represent a period of contraction for the key industry indicators.



Source: NRA; Values Greater than 100=Expansion, Less than 100=Contraction

## Current Situation and Expectations Indices Remained Below 100 in the First Half of 2008

- The *Restaurant Performance Index* consists of two components – the Current Situation Index and the Expectations Index.
- The Current Situation Index, which measures current trends in four industry indicators (same-store sales, traffic, labor and capital expenditures), had an average level of 98.0 during the first half of 2008, which signifies contraction in the current situation component.
- The Expectations Index, which measures restaurant operators’ six-month outlook for four industry indicators (same-store sales, employees, capital expenditures and business conditions), had an average level of 98.9 during the first half of 2008, including a record-low level of 98.3 in May. This indicates that operators expected continued contraction on the six-month horizon.

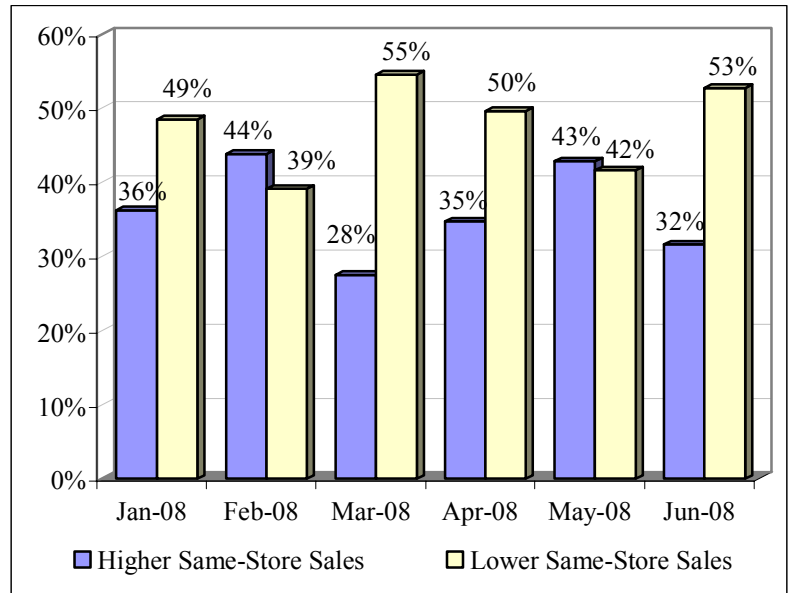


Source: NRA; Values Greater than 100=Expansion, Less than 100=Contraction

## Restaurant Operators Reported Negative Same-Store Sales in Four of the First Six Months of 2008

- Restaurant operators reported negative same-store sales in four of the first six months of 2008, according to the National Restaurant Association's monthly Restaurant Industry Tracking Survey. February sales were bolstered by the extra day as a result of Leap Year.
- In June, 32 percent of restaurant operators reported positive same-store sales, while 53 percent reported a sales decline.
- In addition to softer sales results, restaurant operators reported negative customer traffic levels each month during the first half of 2008. Twenty-one percent of restaurant operators reported an increase in customer traffic between June 2007 and June 2008, while 58 percent of operators reported a traffic decline in June.

## Restaurant Operators' Reporting of Same-Store Sales

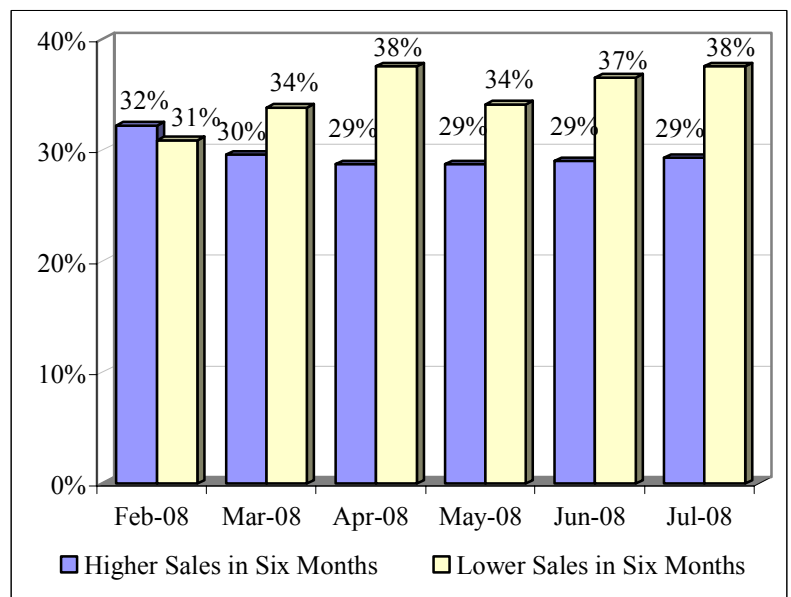


Source: National Restaurant Association; Restaurant Industry Tracking Survey

## Restaurant Operators Remain Pessimistic about Sales Growth and the Economy

- Restaurant operators were relatively pessimistic about short-term growth in sales and the economy during the first half of 2008.
- In the July Tracking Survey, 29 percent of restaurant operators said they expect to have higher sales in six months (compared to the same period in the previous year), matching the proportion who reported similarly in each of the previous three months. Meanwhile, 38 percent of operators said they expect their sales volume in six months to be lower than it was during the same period in the previous year.

## Restaurant Operators' Outlook for Sales in Six Months



Source: National Restaurant Association; Restaurant Industry Tracking Survey

- Restaurant operators also remain pessimistic about the direction of the economy. In the July Tracking Survey, just 15 percent of operators said they expect economic conditions to improve in six months, while 43 percent of said they expect economic conditions to worsen in six months.



## Total Eating and Drinking Place Sales Outpaced the Overall Retail Sector during the First Half of 2008

- Despite the sluggish sales performance on a same-store basis, total eating and drinking place sales registered positive growth during the first half of 2008. Total sales continued to grow due to overall industry expansion.
- Total eating and drinking place sales increased at a 4.5 percent rate on a year-to-date basis through June 2008, according to figures from the U.S. Census Bureau. In comparison, overall retail sales (excluding foodservice) increased at a 2.9 percent rate during the same period, while grocery store sales grew at a stronger 6.1 percent rate.

Total Sales: Year to Date Growth Through June 2008



Source: U.S. Census Bureau; NRA

## Restaurant Industry Expected to Post Positive Real Sales Growth in 2008

- The National Restaurant Association expects eating and drinking place sales to grow in the 4.2 – 4.5 percent range on an annual basis in 2008. With menu prices projected to increase in the 3.9 – 4.1 percent range in 2008, real sales growth (adjusted for inflation) is expected to remain positive. However, real sales growth in 2008 will likely be the lowest growth since a 0.2 percent decline in 1991.

## The Economy and Food Costs Top the List of Concerns for Restaurant Operators

- The uncertain economy and rising food costs continue to create a challenging business environment for restaurant operators. For the fifth consecutive month in July, the sluggish economy topped the list of challenges reported by restaurant operators in the Association’s Restaurant Industry Tracking Survey. This followed 29 consecutive months in which recruiting-and-retaining employees was the number-one challenge reported by operators.
- A record 29 percent of restaurant operators identified the economy as the number-one challenge facing their business in July, followed by food costs (22%), building-and-maintaining sales volume (14%), recruiting-and-retaining employees (11%), and gas and energy prices (11%).

## Top 10 Challenges Reported by Restaurant Operators

1.	The Economy	29%
2.	Food Costs	22%
3.	Building/Maintaining Sales Volume	14%
4.	Recruiting & Retaining Employees	11%
5.	Gas and Energy Prices	11%
6.	Operating Costs	7%
7.	Labor Costs	2%
8.	Competition	2%
9.	Taxes	1%
10.	Insurance Costs	1%

Source: National Restaurant Association, July Tracking Survey



## Wholesale Food Prices Continue to Rise Sharply

- Food prices continue to rise sharply, according to the latest data from the Bureau of Labor Statistics. On a year-to-date basis through June, wholesale food prices jumped 8.2 percent. These strong gains are coming on the heels of a 7.6 percent increase in 2007, which represented the strongest food price increase in 27 years.
- While the overall food price index registered strong growth recently, several individual commodities are posting even more dramatic gains. Flour (73%), fats and oils (56%), eggs (55%), milled rice (51%), cheese (21%) and milk (14%) all rose sharply on a year-to-date basis through June. What is more, these increases are all coming on top of double-digit growth rates in 2007.
- Food costs are one of the most significant line items for a restaurant, accounting for approximately 33 cents of every dollar in sales. With average margins of roughly 4 – 6 percent, an increase in food costs can have a dramatic impact on a restaurant’s bottom line.
- Several factors have contributed to the dramatic rise in food prices in recent years, including higher oil and energy prices; the growing global demand from rapidly developing economies such as China and India; a weak U.S. dollar; and a larger share of the grain market being diverted to ethanol production.

### Wholesale Price Growth for Selected Food Commodities

<u>Commodity</u>	2007	2008	<u>Commodity</u>	2007	2008
	<u>Annual</u>	<u>YTD</u>		<u>Annual</u>	<u>YTD</u>
Fruits & melons, fresh/dry vegetables & nuts	10%	5%	Processed poultry	13%	3%
Fresh fruits and melons	11%	5%	Eggs	61%	55%
Fresh vegetables (excluding potatoes)	11%	0%	Unprocessed & packaged fish	2%	4%
Processed fruits and vegetables	6%	4%	Unprocessed fin fish	-5%	-12%
Cereal and bakery products	7%	17%	Fresh packaged fish & seafood	12%	8%
Bakery products	4%	8%	Frozen packaged fish & seafood	3%	8%
Flour	22%	73%	Canned and cured seafood	4%	1%
Milled rice	14%	51%	Unprocessed shellfish	-1%	7%
Other cereals	8%	12%	Sugar and confectionary	1%	4%
Meats	3%	-2%	Refined sugar	-12%	-7%
Beef and veal	3%	-1%	Confectionary materials	13%	14%
Pork	4%	-7%	Alcoholic beverages	0%	4%
Other meats	0%	0%	Soft drinks	2%	4%
Dairy products	19%	12%	Coffee (whole bean, ground & instant)	7%	10%
Milk	20%	14%	Tea	3%	5%
Butter	10%	-1%	Fats and oils	17%	56%
Cheese	22%	21%			

Source: National Restaurant Association analysis of Bureau of Labor Statistics data

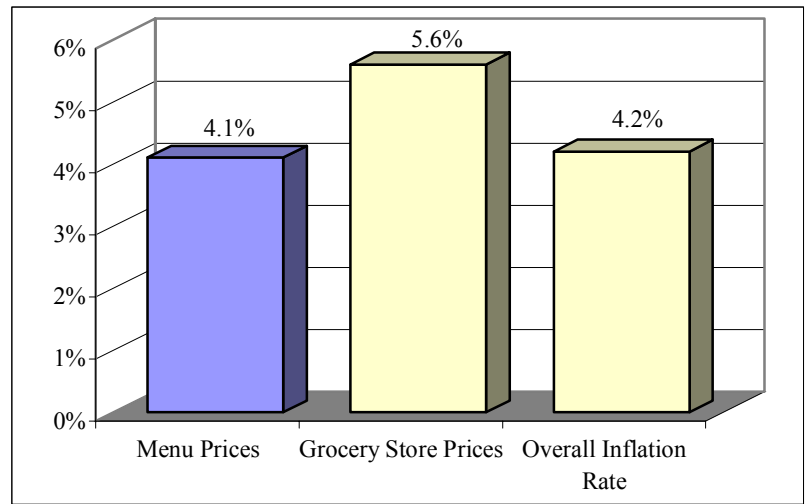
Note: 2008 figures represent year-to-date growth through June



## Menu and Grocery Store Prices Are on Pace to Post Their Strongest Growth in 18 Years

- Although menu price growth accelerated in recent months, it still remained below gains in grocery store prices, according to data from the Bureau of Labor Statistics. On a year-to-date basis through June 2008, menu prices grew at a 4.1 percent rate, well below the 5.6 percent gain in grocery store prices. Both menu and grocery store prices are on pace for their strongest gain since 1990.
- During the same period, overall consumer prices increased at a 4.2 percent rate.
- Within the food-away-from-home sector, the quickservice segment registered slightly stronger menu price growth in recent months. On a year-to-date basis through June 2008, quickservice restaurant menu prices rose 4.3 percent, compared to a 4.0 percent gain in fullservice menu prices.

## Consumer Prices: Year to Date Growth Through June 2008

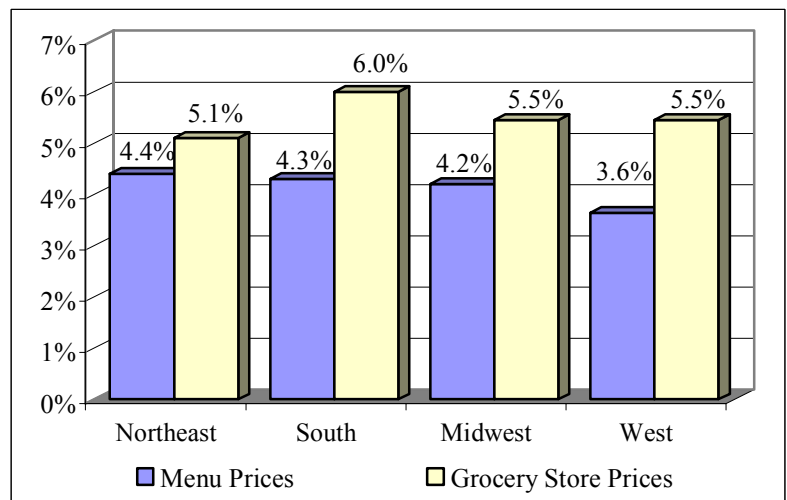


Source: Bureau of Labor Statistics; NRA

## Grocery Store Prices Outpaced Menu Price Growth in Each of the Four U.S. Regions

- On a regional level, the Northeast region led the way with a 4.4 percent menu price gain on a year-to-date basis through June 2008. The South and Midwest regions followed closely behind with gains of 4.3 percent and 4.2 percent, respectively. In the West, menu prices increased at a lower 3.6 percent rate during the first half of 2008.
- In each of the four U.S. regions, grocery store prices outstripped menu price growth during the first half of 2008. The South region set the pace with a strong 6.0 percent increase in grocery store prices on a year-to-date basis through June 2008. Grocery store prices increased at 5.5 percent rates in the Midwest and West regions, and a 5.1 percent rate in the Northeast.

## Regional Prices: Year to Date Growth Through June 2008



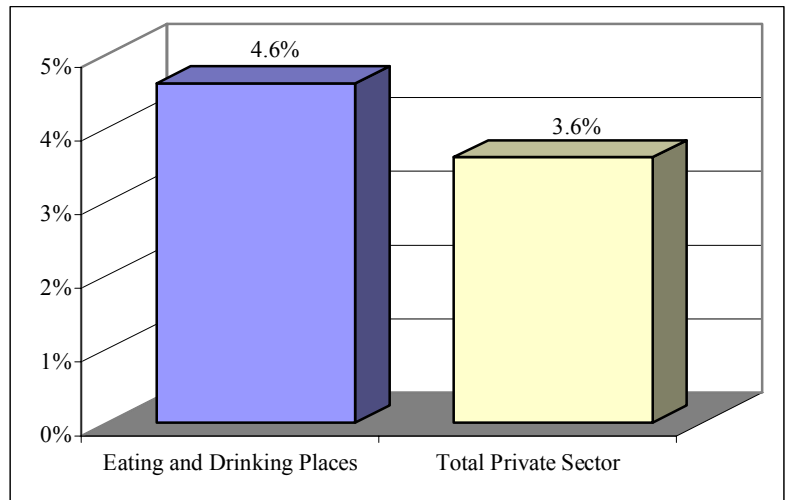
Source: Bureau of Labor Statistics; NRA



### Restaurant Industry Wage Growth Outpaced the Overall Economy During the First Five Months of 2008

- Growth in the earnings of non-supervisory restaurant employees outpaced the overall economy in recent months, according to figures from the Bureau of Labor Statistics.
- The average hourly earnings of non-supervisory eating and drinking place employees increased at a solid 4.6 percent rate on a year-to-date basis through May 2008, a full percentage-point above the 3.6 percent gain in the average hourly earnings of total private sector non-supervisory employees during the same period.

### Average Hourly Wages of Non-Supervisory Employees *Year-to-date growth through May 2008*

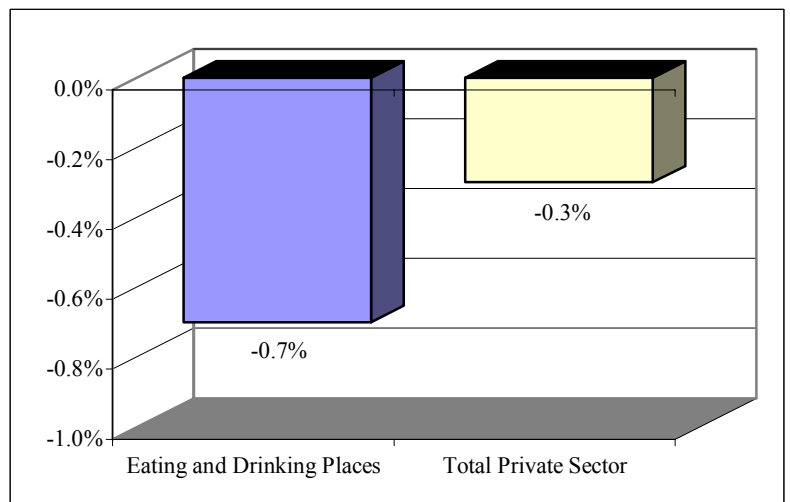


Source: Bureau of Labor Statistics; NRA

### Average Workweek of Restaurant Employees Declined During the First Five Months of 2008

- The average workweek of restaurant industry employees became shorter in recent months, according to figures from the Bureau of Labor Statistics.
- The average weekly hours worked by non-supervisory employees at eating and drinking places declined 0.7 percent on a year-to-date basis through May 2008. During the same period, average hours worked by non-supervisory employees in the total private sector declined 0.3 percent.

### Average Weekly Hours of Non-Supervisory Employees *Year-to-date growth through May 2008*



Source: Bureau of Labor Statistics; NRA

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### Produced by the National Restaurant Association’s Research Group

Contacts:

Hudson Riehle, Senior Vice President of Research and Information Services, [hriehle@restaurant.org](mailto:hriehle@restaurant.org)

Bruce Grindy, Chief Economist, [bgrindy@restaurant.org](mailto:bgrindy@restaurant.org)

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