OUTLOOK

Q2/2023

Are Happy Days Here Again?

Optimistic report demonstrates restaurants are finding their footing

While it's hard to know what normal times feel like anymore, the National Restaurant Association's newly released 2023 State of the Restaurant Industry report sounds more optimistic than it has in a long time. After a few years of many unwelcome surprises, nearly three out of four restaurant owners now say their business has found a positive pattern that feels like a new normal.

The wide-ranging report, which considers views from restaurant owners, operators, chefs and consumers, addresses topics such as the state of the economy, restaurant business operations, and trends related to food and employment. Several themes emerged from the report:

Many changes forced upon restaurants by the pandemic are here to stay – and have made restaurants more resilient. The specific changes vary by restaurant category, but whether it's the addition of drive-thru lanes, delivery service, year-round outdoor dining options, or (where permitted) alcohol to-go, restaurants that made changes to boost business after the start of the pandemic have seen evidence that these approaches make good sense for the long-term health of their business.

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Long-Term Challenges Require Flexibility and Reinvention

Agricultural commodities update

The confluence of climate change-related challenges, supply chain snags, inflation and ongoing geopolitical tensions is making for interesting times in agriculture. All of these elements are having an impact on the long-term outlook for the supply, demand and trade of agricultural commodities, both within the U.S. and worldwide.

Here is an overview of key commodities according to recent research from the USDA and other industry sources:

Wheat: Not long ago, U.S. wheat farmers increased plantings of winter wheat to an eight-year high, encouraged by expanded crop insurance programs and high wheat prices as a result of restricted supplies coming from Ukraine. However, ongoing drought conditions in the Plains have damaged prospects. U.S. wheat exports are expected to drop to a 51-year low in the current marketing year and, according to a Reuters report, are unlikely to improve significantly in the next season despite efforts from the Biden administration to increase U.S. food production after the start of the war in Ukraine. (Last summer, the USDA expanded the number of U.S. counties where farmers can get crop insurance on a second crop planted after wheat.) The International Grains Council and USDA have conflicting forecasts for the global wheat trade, with the council anticipating total world ending wheat stocks to increase 3 percent over last year and world wheat trade to decrease by 1.3 percent, which suggests a price decline. The USDA expects world wheat stocks to decrease 2.6 percent and trade to increase 5 percent, which suggests a price boost.

Corn and Soybeans: The latest 2022-23 U.S. corn outlook is for lower exports and larger ending stocks, according to the USDA. Exports are down 75 million bushels, which reflects the poor pace of sales and shipments despite relatively competitive U.S. prices. With no other use changes, ending stocks are up 75 million bushels from last month. Still, price trends indicate better profitability for U.S. farmers to plant corn over soybeans this year, and the USDA believes corn acres will surpass levels from a year ago. Corn and soybean production was expected to rebound in South America this year after drought harmed crops in Brazil and Argentina last year, but conditions in Argentina have only worsened and hampered recovery of global supplies. The USDA reports higher exports, lower crush, and reduced ending stocks by 15 million bushels for U.S. soybeans compared with its previous report.

Commodities
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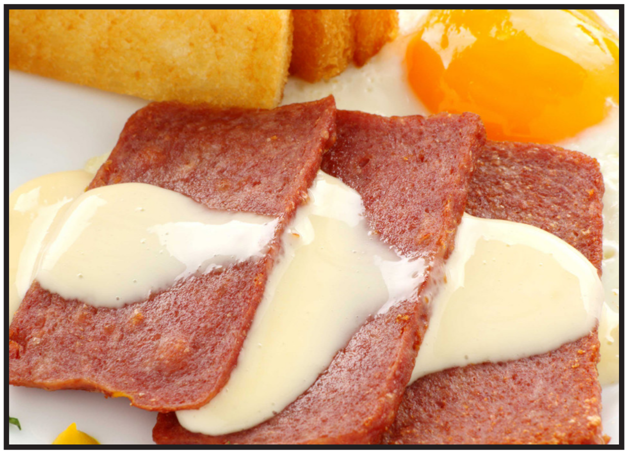

Pork: The agency also expects commercial pork production to increase over the 10-year projection period, as a result of rising hog inventories as producers increase supply to meet processor demand. Total commercial production of pork is projected to grow from 28 billion pounds in 2024 to a record 31 billion pounds in 2032. The U.S. is also a major importer of pork, though exports outweigh imports. Imports are expected to grow to a record 1.683 billion pounds by 2032, elevated by a strong U.S. dollar and an influx of Canadian pork that had historically been exported to China..

Beef: The USDA expects commercial beef production to contract this year and next, following a higher-than-normal rate of slaughter in 2022 during drought conditions, before growing through 2032. Commercial slaughter volumes and weights are expected to increase, expanding production to record levels by 2032. The U.S. imports beef in volumes often similar to the volumes it exports. To support domestic consumption, U.S. beef imports are expected to rise to 3.6 billion pounds in 2024 but decrease after, hovering around 3.1 billion to 3.2 billion pounds annually.

Inflation Strain

Times are improving, but steep increases in food and labor costs continue to be a strain on restaurants. Here's what most restaurants are experiencing. How do your costs compare?

· Wholesale food prices are up nearly 13.2%.

· The typical small business restaurant runs on a 3-5% pre-tax margin. Food and labor, the two most significant budget line items for a restaurant, each account for about 33 cents of every dollar in sales.

· Other expenses – including rent, utilities, and other direct operating costs – generally represent about 29% of sales. For the vast majority of restaurant operators, these three categories comprise a larger share of sales than they did before the pandemic.

Source: National Restaurant Association

Themes

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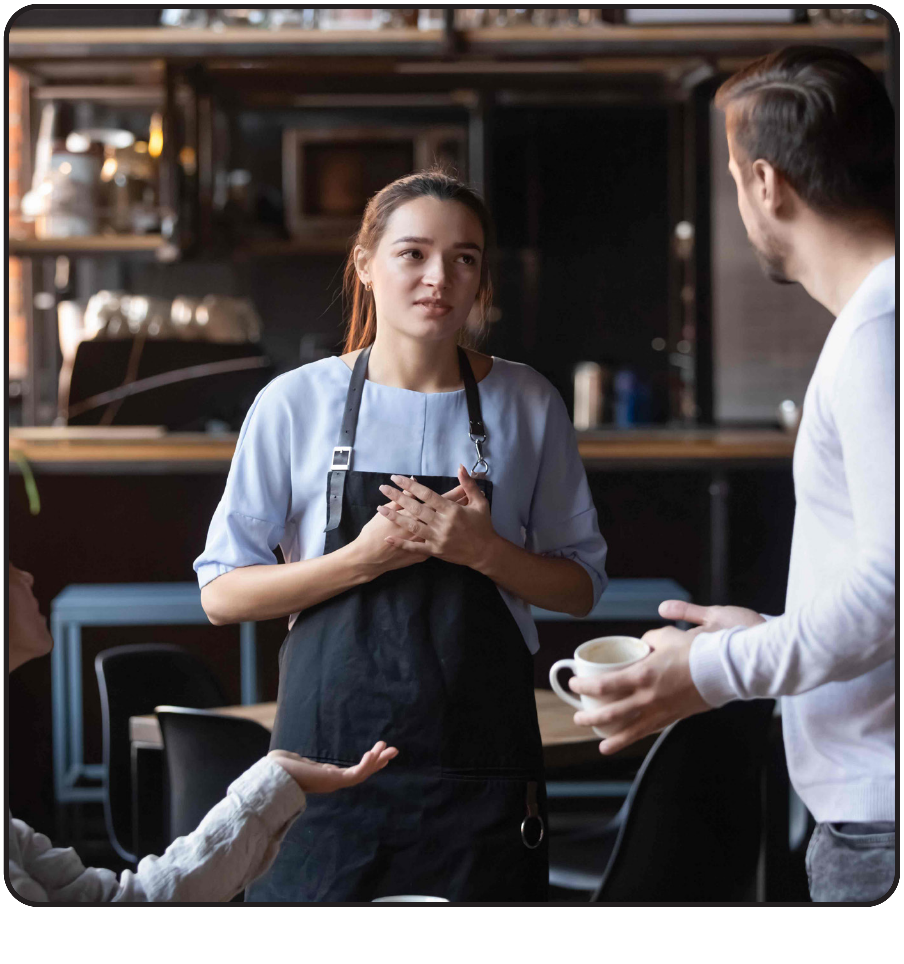
Restaurants have been hiring – and want to keep it up. The restaurant and foodservice workforce is forecast to grow by 500,000 jobs, for total industry employment of 15.5 million by the end of this year. The anticipated growth of the sector this year, due in part to rising menu prices, is likely going to continue to elevate hiring levels. In the next seven years, the foodservice industry is expected to add approximately 150,000 jobs a year on average, with total staffing levels projected to reach 16.5 million by 2030.

While more than half of operators say new technology and automation tools will become more commonplace this year, they generally see them as resources to support their people – not take their place. This indicates that restaurant jobs themselves are evolving to provide new opportunities for staff.

Restaurants have invested heavily in new technology to support their operations, but the industry is still far from being tech-forward. More than 40 percent of operators plan to invest in technology to boost productivity, though largely in areas such as ordering and payment systems as opposed to leading-edge automation tools. Consumers are expecting to be able to use technology to order, pay and earn rewards at restaurants, so their behavior is driving restaurants' focus.

Restaurants are demonstrating the value of the restaurant experience. A clear majority of consumers who responded to the survey – 84 percent – said going to a restaurant with others is a better use of their spare time than cooking and cleaning up at home. More than two-thirds of respondents consider restaurants essential to their lifestyle.



Of course, industry challenges remain. The vast majority of operators say the rising cost of food remains a major hurdle, while nearly half of operators expect competition to intensify this year. The report points to a number of potential opportunities to increase revenues, including chef's tastings, cooking classes, sales of branded apparel, meal kits, meal subscriptions and the promotion of locally sourced foods. Beyond that, careful management of inventory and food costs, recipe flexibility, and marketing ingenuity will continue to be important to making the restaurant experience feel worthwhile to consumers.