Trinity Capital

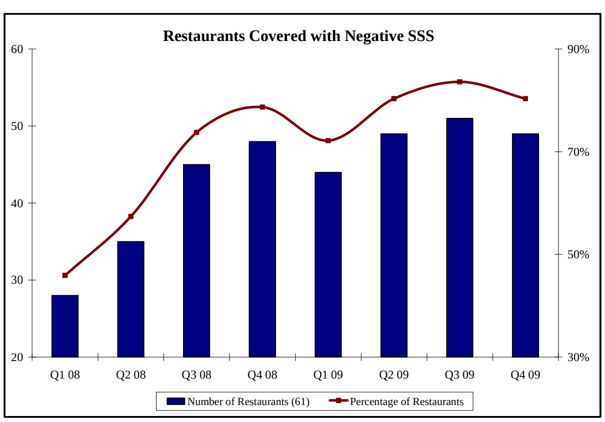
4th Quarter 2009 Restaurant Industry Commentary

What's Inside This Commentary

Same-Store Sales Discussion and Analysis

By Joshua L. Brannan

Despite extensive promotional activity, couponing, and trading down by customers, restaurant sales continued to decline in the fourth quarter of 2009 due to the continued softness in the economy and the record-breaking harsh winter weather. In fine dining, the companies we track were down by an average of (10.4%) for the fourth quarter of 2009. Both corporate and high-end users continue to cutback materially on occasions resulting in eight straight quarters of same-store sales declines for the fine dining category. In casual dining, 24 of the 26 concepts that we track were negative for the fourth quarter with the segment down by an average of (4.1%). Buffalo Wild Wings continues to be the star of the segment reporting same-store sales growth for the eighth consecutive quarter. All six family dining concepts we track were negative during the quarter with the segment down by an average of (5.6%). The fast casual segment ended the quarter with the best performance in the restaurant industry. The segment was positive by 0.2% for the fourth quarter, with four of the eight concepts we track reporting same-store sales growth.



* For purposes of comparison, excludes concepts that do not have SSS Data for all 8 qtrs.

In the QSR segment, 12 of the 17 concepts we track were negative during the fourth quarter of 2009 with the segment down by an average of (3.9%). This fact is perhaps the most disturbing as the QSR segment has been the biggest beneficiary of trading down, discount limited time offers ("LTOs"), couponing, value menus, extensive promotional campaigns and new product introductions. Unfortunately, the current economic woes and unemployment in the U.S. continue to depress QSR sales despite all efforts to drive traffic and sales.

2009 was challenging for the restaurant industry; with operating cost inflation, consumer spending pressures, tight credit markets and negative same-store sales trends. Despite macroeconomic headwinds, strong brands and operators that adapt to the changing market conditions and consumer trends can still perform well.

Many restaurant operators and concepts have continued to find ways to control costs in this "new" environment and have minimized the impact of declining sales on their bottom lines. Beyond general control enhancement and increased operational rigor, the key cost cutting measures are: rent concessions by landlords, the negotiation of more favorable contracts with suppliers and aggressive cuts to G&A. The operators that continue to be mindful of their costs will be the ones that survive and even flourish in 2010.

Contributing Editor Joshua L. Brannan is a Vice President for Trinity Capital.

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Same-Store Sales ("SSS") Data

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	Q4 09
Fine Dining:								
Fleming's	-6.8%	-8.4%	-9.7%	-20.8%	-19.9%	-22.4%	-18.0%	-5.7%
McCormick & Schmick's	-5.8%	-4.9%	-5.5%	-13.5%	-13.9%	-17.3%	-18.8%	-12.9%
Morton's Rest. Group	0.7%	-1.9%	-7.6%	-12.0%	-24.1%	-26.1%	-16.8%	-11.6%
Ruth's Chris	-6.9%	-7.1%	-6.9%	-18.5%	-18.5%	-23.4%	-24.0%	-11.2%
Mean	**-4.7%**	**-5.6%**	**-7.4%**	**-16.2%**	**-19.1%**	**-22.3%**	**-19.4%**	**-10.4%**
Same Store Negative Count[1]	**3**	**4**	**4**	**4**	**4**	**4**	**4**	**4**
Casual Dining:								
Applebee's	0.5%	-1.7%	-3.1%	-4.6%	-3.0%	-4.3%	-6.5%	-4.5%
Benihana	-1.0%	-4.9%	-6.5%	-11.1%	-10.4%	-10.1%	-9.9%	-5.9%
Big Boy & Golden Corral	0.0%	-0.2%	0.4%	-0.1%	1.1%	4.6%	-2.4%	-2.0%
BJ's Resturants	0.0%	0.6%	-1.0%	-0.7%	-0.1%	-1.3%	-1.6%	-0.2%
Bonefish	-3.9%	-8.0%	-10.2%	-11.5%	-10.0%	-8.2%	-5.8%	1.0%
Buffalo Wild Wings	2.8%	5.7%	3.8%	3.2%	6.1%	3.4%	1.5%	2.2%
California Pizza Kitchen	0.4%	1.4%	-2.4%	-7.2%	-5.9%	-6.5%	-8.0%	-5.8%
Carrabba's Italian Grill	0.7%	-5.0%	-5.7%	-6.5%	-7.3%	-5.9%	-7.5%	-3.6%
CEC Entertainment	3.6%	5.7%	1.1%	-1.5%	-0.1%	-5.4%	-3.1%	-2.0%
Cheesecake Factory	-1.8%	-4.1%	-4.7%	-7.0%	-3.2%	-3.0%	-2.4%	-0.7%
Chili's Grill & Bar	1.6%	3.4%	-3.0%	-4.2%	-5.2%	-9.4%	-6.0%	-3.2%
Dave & Buster's	3.8%	1.2%	-6.0%	-10.2%	-7.9%	-6.5%	-7.4%	-
Famous Dave's	3.6%	1.7%	-4.7%	-8.3%	-5.5%	-9.4%	-6.8%	-3.4%
Granite City	1.8%	0.5%	-	-	-11.2%	-13.2%	-12.7%	-8.1%
Landry's	0.2%	-2.5%	-2.0%	-4.7%	-9.0%	-8.0%	-6.5%	-5.0%
LongHorn Steakhouse	-3.3%	-3.1%	-4.9%	-5.7%	-5.4%	-6.5%	-6.2%	-
Macaroni Grill	-3.2%	5.7%	-9.0%	-10.6%	-	-	-	-
Maggiano's	-0.4%	-0.5%	-3.3%	-6.9%	-9.5%	-9.2%	-6.6%	-1.6%
O'Charley's	-4.7%	-1.4%	-4.0%	-6.1%	-2.9%	-6.9%	-7.6%	-7.3%
Olive Garden	5.7%	5.8%	2.4%	0.8%	-1.4%	-0.6%	-2.9%	-1.4%
On The Border	-1.8%	-2.3%	-3.3%	-3.7%	-5.0%	-5.8%	-5.1%	-4.7%
Outback	-2.6%	-5.3%	-7.9%	-9.1%	-8.4%	-10.2%	-10.7%	-5.9%
PF Chang's Bistro	0.1%	-2.3%	-3.1%	-7.1%	-6.6%	-6.8%	-8.5%	-5.2%
Real Mex	-0.2%	1.4%	-3.7%	-6.5%	-9.1%	-	-	-
Red Lobster	-2.0%	-0.2%	-3.7%	0.3%	-4.6%	-0.6%	-7.9%	-8.4%
Red Robin	4.0%	-0.8%	-2.4%	-6.7%	-7.8%	-11.1%	-14.8%	-10.9%
Ruby Tuesday	-12.7%	-10.3%	-10.8%	-10.8%	-6.8%	-3.2%	-3.1%	-1.7%
Stoney River	-3.2%	6.4%	-8.1%	-18.2%	-17.2%	-20.4%	-17.1%	-10.3%
Taco Cabana	0.7%	-0.6%	-0.9%	0.5%	-1.6%	-3.8%	-4.3%	-4.5%
Texas Roadhouse	-1.2%	-0.3%	-3.2%	-4.9%	-1.4%	-3.7%	-4.4%	-2.3%
Mean	**-0.4%**	**-0.5%**	**-3.8%**	**-5.8%**	**-5.5%**	**-6.1%**	**-6.6%**	**-4.1%**
Same Store Negative Count[1]	**11**	**17**	**21**	**21**	**23**	**23**	**24**	**23**
Family Dining:								
Bob Evans	1.7%	2.0%	-2.5%	-1.3%	-1.6%	-3.0%	-2.8%	-4.2%
Cracker Barrel	1.1%	-0.8%	-3.2%	-1.5%	-0.9%	-1.4%	0.6%	-0.2%
Denny's	-0.4%	-2.8%	-5.1%	-6.1%	-1.1%	-4.2%	-7.2%	-7.0%
IHOP	3.7%	2.6%	0.2%	-1.0%	2.0%	-0.6%	-1.1%	-3.1%
Luby's	-3.3%	-2.0%	-6.7%	-3.2%	-8.9%	-13.6%	-13.3%	-12.5%
Ninety Nine	-2.2%	-3.1%	-8.1%	-8.4%	-4.5%	-10.0%	-7.1%	-6.5%
Perkins	-1.7%	-1.9%	-3.7%	-3.9%	-4.9%	-8.3%	-7.5%	-
Mean	**-0.2%**	**-0.9%**	**-4.2%**	**-3.6%**	**-2.8%**	**-5.9%**	**-5.5%**	**-5.6%**
Same Store Negative Count[1]	**3**	**4**	**5**	**6**	**5**	**6**	**5**	**6**

[1] For puposes of comparison, excludes concepts that do not have SSS data for all 8 quarters

* Source: Piper Jaffrey Companies, Restaurant Research LLC, Capital IQ and company filings

SSS Data (Con't)

	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	Q4 09
Fast Casual:								
Chipotle	10.0%	7.1%	3.1%	3.5%	2.2%	1.7%	2.7%	2.0%
Cosi	0.3%	2.2%	-0.1%	-6.9%	-11.3%	-12.2%	-10.7%	-11.9%
Einstein Noah Bagel	3.6%	1.0%	-1.7%	-3.3%	-5.7%	-2.2%	-3.1%	-1.4%
Panera Bread	2.4%	5.5%	3.3%	2.7%	0.7%	-0.4%	2.8%	5.4%
Qdoba Mexican Grill	2.4%	0.5%	-1.0%	-1.1%	-2.3%	-2.8%	-3.1%	-1.7%
Rubio's Restaurants	-3.3%	-3.9%	-2.1%	-0.2%	1.9%	0.9%	-2.7%	-2.7%
Steak n Shake	-6.3%	-5.8%	-7.4%	-1.4%	2.4%	5.0%	10.1%	10.0%
Tim Horton's (US)	1.0%	3.1%	-0.6%	-0.1%	3.2%	3.3%	4.3%	2.1%
Mean	**1.3%**	**1.2%**	**-0.8%**	**-0.9%**	**-1.1%**	**-0.8%**	**0.0%**	**0.2%**
Same Store Negative Count[1]	**2**	**2**	**6**	**6**	**3**	**4**	**4**	**4**
QSR:								
Chicken:								
Church's	2.4%	3.3%	4.0%	2.1%	1.5%	-5.6%	-	-
El Pollo Loco	1.8%	1.9%	0.0%	-2.5%	-5.9%	-6.8%	-10.1%	-
KFC	-2.0%	-3.0%	-6.0%	-3.0%	-7.0%	3.0%	-2.0%	-8.0%
Pollo Tropical	-1.0%	0.1%	-1.9%	-3.6%	-3.0%	-3.1%	-0.1%	0.3%
Popeyes	-1.8%	-1.7%	-2.8%	-2.8%	-0.3%	4.3%	-0.3%	-1.0%
Mean	**-0.1%**	**0.1%**	**-1.3%**	**-2.0%**	**-2.9%**	**-1.6%**	**-3.1%**	**-2.9%**
Same Store Negative Count[1]	**3**	**2**	**3**	**3**	**3**	**1**	**3**	**2**
Coffee/Snack:								
Caribou Coffee	-2.3%	-1.7%	-4.7%	-5.1%	-5.0%	-3.3%	-0.5%	0.2%
Jamba Juice	-4.2%	-7.3%	-10.3%	-12.0%	-13.8%	-13.7%	-5.3%	-
Krispy Kreme	-3.9%	-9.2%	-11.8%	1.9%	2.1%	5.9%	5.1%	-
Starbucks	-5.0%	-5.0%	-8.0%	-10.0%	-8.0%	-6.0%	-1.0%	4.0%
Mean	**-3.9%**	**-5.8%**	**-8.7%**	**-6.3%**	**-6.2%**	**-4.3%**	**-0.4%**	**2.1%**
Same Store Negative Count[1]	**2**	**2**	**2**	**2**	**2**	**2**	**2**	**0**
Mexican:								
Taco Bell	7.5%	7.3%	9.0%	9.0%	2.0%	1.0%	-2.0%	-5.0%
Mean	**7.5%**	**7.3%**	**9.0%**	**9.0%**	**2.0%**	**1.0%**	**-2.0%**	**-5.0%**
Same Store Negative Count[1]	**0**	**0**	**0**	**0**	**0**	**0**	**1**	**1**
Pizza:								
Domino's	-5.2%	-5.4%	-6.1%	-3.0%	1.0%	-0.7%	0.0%	1.4%
Papa John's	1.7%	2.4%	1.7%	-2.0%	0.3%	0.1%	0.0%	-0.5%
Pizza Hut	2.0%	5.0%	5.0%	-1.0%	-3.0%	-8.0%	-13.0%	-12.0%
Sbarro	0.3%	0.0%	-1.0%	-8.0%	-4.8%	-5.1%	-5.2%	-
Mean	**-0.3%**	**0.5%**	**-0.1%**	**-3.5%**	**-1.6%**	**-3.4%**	**-4.6%**	**-3.7%**
Same Store Negative Count[1]	**1**	**1**	**1**	**3**	**1**	**2**	**1**	**2**
Sandwich:								
Arby's	0.4%	-3.3%	-5.0%	-8.5%	-8.7%	-6.9%	-9.0%	-11.0%
Burger King	5.6%	5.6%	3.0%	1.7%	1.6%	-4.5%	-4.6%	-3.3%
Carl's Jr.	3.9%	3.8%	0.5%	-0.6%	-5.1%	-6.1%	-5.2%	-8.7%
Hardee's	-0.6%	3.3%	1.3%	1.5%	2.5%	-2.7%	-1.8%	-2.5%
Jack in the Box	-0.1%	-0.4%	-0.8%	1.7%	0.4%	-1.0%	-6.0%	-11.1%
McDonald's	2.9%	3.4%	4.7%	5.0%	4.7%	3.5%	2.5%	0.1%
Sonic Drive-In	3.2%	-0.4%	-0.6%	-3.6%	-3.6%	-5.4%	-4.5%	-6.5%
Wendy's	-1.6%	0.9%	0.1%	3.7%	1.0%	-0.4%	-0.1%	-3.0%
Mean	**1.7%**	**1.6%**	**0.4%**	**0.1%**	**-0.9%**	**-2.9%**	**-3.6%**	**-5.8%**
Same Store Negative Count[1]	**3**	**3**	**3**	**3**	**3**	**7**	**7**	**7**
Mean Total QSR	**0.2%**	**0.0%**	**-1.4%**	**-1.8%**	**-2.3%**	**-2.8%**	**-3.0%**	**-3.9%**
Same Store Negative Count - QSR[1]	**9**	**8**	**9**	**11**	**9**	**12**	**14**	**12**

[1] For puposes of comparison, excludes concepts that do not have SSS data for all 8 quarters

* Source: Piper Jaffrey Companies, Restaurant Research LLC, Capital IQ and company filings

The Impact of Artificially Low Interest Rates on Your Business

By David E. Stiles

In our ***"3rd Quarter 2009 Restaurant Industry Commentary"***, we reviewed trends to observe in various economic indicators, particularly those to which the restaurant industry is most sensitive. We also provided guidance on how restaurant operators should use caution in navigating the current economy given these trends. One of the economic issues receiving significant attention has been what we have referenced as, "artificially low interest rates." Here we explore in greater detail the significance that prevailing interest rates could have on your business and why it is so important to carefully analyze your business's exposure to variable rate interest expense.

Since the credit crises in October 2008, interest rates have been extremely volatile compared with historical results. The 6 month LIBOR has dropped an incredible 480 basis points while 30 year Treasury Notes, which started at 4.6% as of July 2008 dropped to 2.87% by year end, only to run back up to 4.5% within six months and currently stands at 4.62%. There is a measure in the marketplace commonly referred to as, "Short-term implied interest rate volatility", an annualized measure of the market's uncertainty regarding future movements in interest rates. Prior to the crisis, the reading was under 10%. Since then, it has climbed to more than 80%, at times even spiking above 100%. Uncertainty remains around when interest rates will finally settle into a trade-bound range, but it is easy to argue that there is only one way for LIBOR rates to travel, given they stand at an all time low. The tremendous supply of treasury's which we brought onto the market to fund the rollover of the outstanding US debt as well as the current year deficit will continue to pressure interest rates upward. A related note, it's interesting that Berkshire Hathaway bonds now trade through U.S. Treasury securities

Consider that the 30-Day LIBOR rate's 20-year historical mean is approximately 4.45% compared to the average rate of 0.57% over the last 12 months of your business operations and averaged 3.00% in 2008. The current rate stands at almost 1/5th of 2008 levels and 1/8th of the 20-year historical mean. That is quite the savings in interest expense, provided that your variable rate index and margin are not subject to a floor or your lender has not cited you in technical default of your loan covenants and has since imposed the default rate of interest.

A clear threat we believe franchisees now face is rising interest rates. Consider the impact on unit-level profitability from an increase in interest rates. Assume that your restaurant with $19,000 weekly sales in 2008 and comps down 2.5% for two consecutive years, now generates 5 percent earnings before interest, taxes, depreciation and amortization (*EBITDA*) margin (*after overhead allocation*) and has annual occupancy expense of $85,000. Today, that same restaurant with weekly sales of $18,000 that is encumbered by a 15-year, $500,000 variable rate mortgage indexed to the 30-day LIBOR, plus a 2.25% margin (*for an effective interest rate of 2.48 percent*) would result in a Fixed Charge Coverage Ratio of 1.07x (*lender covenants generally require an FCCR maintained above at least a 1.15x*). An increase in LIBOR to its historic 20-year average would increase the effective interest rate to approximately 6.70%. The store in this scenario with the higher interest expense no longer covers its debt service (*before capex*) with an FCCR of .95x. Consider that 30-day LIBOR was at 5.01% right before the credit crisis. With the same 2.25% margin, the effective cost of funds would increase by 422 basis points to 6.70%.

This store's debt service has now increased by approximately $13,500 per year. Now, suppose you lose 100 basis points in EBITDA margin from the impact from an increase in gas prices (*lower traffic*), increase commodity prices from 2008 all-time highs or enduring LTOs (*increasing food prices*) and you would be confronted with a serious cash flow shortfall with an FCCR of 0.88x.

Franchisees exposed to variable rate debt have options to mitigate this exposure. Depending on the size of debt obligations, entering into interest rate swap agreements (*converting variable rate debt to fixed rate* debt) has been an effective way to hedge against rising interest rates. This, of course, is predicated on a substantial and credit worthy performing loan. Alternatively, preparing your company to refinance or convert to a fixed rate may also be a viable solution. In this effort, it is critical that franchisees demonstrate effort and actions preserving profitable operating margins. Also critical is assembling projections and budgets that are realistic and credible for lenders to support. Having all of your financials and documentation in order will increase your chances of a successful financing. This is equally important in obtaining financing for any purpose.

Another tool which is classically suited to hedge against significant interest rate increases includes purchasing an interest rate cap from a brokerage dealer. In these transactions, much like the purchase of an option, you pay an up-front premium to protect against increasing interest rates beyond a strike point. The variety of terms that can be structured into pricing these derivatives makes interest rate caps a flexible alternative to interest rate swap agreements. The premium can be higher or lower depending on the term and strike rate. It may be the case that purchasing a long term interest rate cap at a low strike price may be prohibitively expensive. However, if the objective is to protect the company against extraordinary swings in interest expense, an "insurance policy" of capping rates may well be worth the investment.

As we mentioned in our third quarter commentary, we believe it is critical at this juncture for restaurant operators to analyze their debt obligations, capital structure and evaluate their potential risk exposure. The results of this analysis, at the very least, will be an eye-opener for some restaurant executives. We also take note that, given the state of the economy and our perspective on what may transpire with interest rates, now is the time to acquire a complete understanding of the on- and off balance sheet obligations and future working capital requirements. Trinity Capital has helped companies review loan covenants and evaluate performance for covenant compliance. Trinity has worked with companies to ensure they have ways to meet their reimaging requirements, pay down debt or even exploit opportunities that may exist with their lenders. If you feel you are at risk, we encourage you to contact us so we can guide you through evaluating your exposure. Starting with a clear understanding of your company's true exposure is the prudent and sound action for protecting your franchise in the current economic climate.

Contributing Editor David E. Stiles is a Senior Vice President for Trinity Capital.

4th Quarter 2009 Restaurant Market Commentary and Economic Outlook

By Kevin T. Burke

Many readers and clients have contacted us regarding our third quarter research report and indicated they agree with us that the economy is a mess and the rate of improvement is very spotty at best. Therefore, the question is, "When will the economy improve enough to drive consistently higher levels of traffic into the nation's restaurants?". It is very important to note that improvements are spotty because economic performance is very geographically skewed and we still have both high unemployment and under-employment. For example, five states (CA, FL, AZ, MI and NV) represent 75% of the nationwide home price decline and about half of all mortgages with negative equity. These same states lead the nation in unemployment as well. Considering residential housing alone, it is clear that economic recovery is not uniform geographically throughout the United States.

As we said in our last report, three obstacles currently overshadowing economic recovery are unemployment levels, the ailing regional banking system and the distressed real estate (residential and commercial) markets. Once these items begin to show steady improvement, we believe consumer confidence will then follow shortly thereafter and recovery will take hold. In the meantime, there's simply not enough consumer confidence to drive the consumption we need to repair the economy. Another issue plaguing consumers is their clear lack of faith in Washington - politicians are not trusted and therefore have lost their ability to provide leadership in this crisis. We believe the elections in November may very well change the composition of Congress and therefore attenuate the White House to more pressing popular sentiments like federal deficit reduction and jobs creation as opposed to health care, Card Check or cap and trade legislation.

So what is the long-term outlook for restaurant traffic in the United States? We believe it is very good; however, the next two years may still be very challenging for many restaurant companies as consumers save more and are thriftier on menu selections. Nonetheless, our faith in the US economy rests in many aspects of US hegemony particularly economic, infrastructure, education and military. The $14 trillion US economy is approximately 25% of a global $56 trillion world economy. In perspective, the US economy is 3 to 4 times as large as any of the next five economies in the world. Some of the elements that contributed to this strength are an abundance of natural resources, infrastructure, immigration (formerly) and free markets. For example, United States is the leader in producing many foodstuffs on either a gross or per capita basis including beef, pork and chicken as well as grains such as wheat, corn and soy. In addition, the United States has the largest bastion of freshwater in the world within the Great Lakes and our river system. The US navigable river system includes a dozen dependable transportation veins which have facilitated unrivaled commerce during the past 100 years.

The United States has fair state and federal courts, GAAP accounting standards, and the SEC, CFTC and other regulatory bodies which are regarded as leaders in their disciplines around the world. In spite of the financial crisis of 2008, we have capital markets and a money center banking system, which are at the forefront of securities trading, banking and commerce throughout the world

Even today after the financial crisis, our money center banks lead the world in profitability and other important measures of financial prowess. United States infrastructure is also unique in that our airlines, railway and US interstate and highway systems move more goods per mile than anywhere in the world. All 50 states trade with each other without tariff, trade barriers or customs and they all speak the same language.

The US primary educational system takes on a lot of criticism, yet our universities still manage to be the destination of choice for foreign students around the world. In 2009 the *Times of London* ranked US higher education the best in the world as the US had 18 of the top 50 global institutions of higher learning (36%) while we only have 4% of the world population. The fact is, there are more laboratories, PCs, universities and books in New England alone than in all of Eastern Europe - it's not even close.

Finally, it is impossible to have a discussion about the US economy without referencing the hegemony of the United States military which includes five branches of service (Air Force, Navy, Army, Marine Corps, and Coast Guard) as well as substantial national and state guard units. The lessons of the Cold War made it clear that if you want to be a military superpower, then you must be an economic superpower. As far as military superpowers go, there is only one: the United States. For example, the United States Navy is larger than all of the combined navies of the other 350 countries in the world. The US Navy features 12 carrier groups; only three other countries even have a carrier and none have two. The United States Navy has complete rule over the high seas by design since to be a trade power you must control the sea lanes. The US ballistic missile, ballistic missile submarine and air superiority are virtually unchallenged by any other country. Furthermore, the weapon systems for US missiles, ordinance and remotely piloted vehicles are generally two generations superior to any other systems operated by our allies or adversaries.

So we believe that whatever political and governmental budget shortcomings the US is experiencing right now, the US is clearly in the best position to emerge from the global financial crisis as the only global military and economic superpower: two necessary linchpins for sustainable economic recovery and political stability. Accordingly, we believe that will lead to good long term prosperity for the economy and this restaurant industry.

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Restaurant Deal Activity – A Tale of Two Cities

By Robert J. Woolway

We all know the restaurant industry in general has had a rocky last 12 months. For most operators, traffic count and same-store sales have declined materially. Most restaurant executives we speak with characterize this period as the toughest they have seen in their careers. These difficult market conditions have led to a number of restaurant bankruptcies, liquidations and distressed sales. At the same time, some restaurant companies are experiencing growth, at least in profits resulting from cost cutting, and M&A activity involving restaurants has actually picked up. We appear to be in an environment of "haves and have-nots". There has been increased activity at each end of the deal spectrum: more bankruptcies/distressed transactions on one hand with a pick-up in M&A deals on the other.

Many observers have noted that there have been fewer bankruptcies and debt restructurings involving restaurants than one would expect given the economic and financial meltdown that has occurred. In part, this can be explained by creditors' seeming willingness to "pretend and extend" in the hopes of an economic recovery and a desire to avoid unnecessary asset write-downs. We are seeing in 2010, however, that in numerous cases it is no longer viable to delay the inevitable. Many companies are just too leveraged as the result of easy lending in early years and significant EBITDA declines since 2007. Our debt restructuring practice has picked up considerably as restaurant borrowers and lenders have concluded that the problems can no longer be postponed. For some restaurants, bankruptcy has become the only option. Recent filings include:

- McGrath's Fish House
- Fili Enterprises (parent company of Daphne's Greek Cafés)
- Taco Del Mar
- The Oceanaire
- Uno Restaurant Holdings
- Max & Ermas Restaurants

With the frequent negative news about restaurant bankruptcy filings and debt challenges, it is somewhat surprising to observe a modest increase in restaurant M&A activity. In the fourth quarter of 2009, there were 94 restaurant company transactions versus 88 in the fourth quarter of 2008 and an average of 76 for the first three quarters of 2009. In addition to numerous smaller transactions, several significant company sale or acquisition efforts have been announced including:

- CKE Restaurants – Acquisition agreement with Thomas H. Lee Partners
- Church's Chicken – Acquired by Friedman Fleischer & Lowe
- Papa Murphy's – Put up for sale
- Captain D's Seafood Kitchen – Put up for sale
- Rubio's – Received takeover offer
- Hooters – Talking to potential investors
- Ruth's Chris – Recapitalization

Several factors have contributed to this increased M&A deal flow. In general, buyers of businesses in this market appear to be demonstrating an increased tolerance for risk as the economy and capital markets show signs of stabilizing if not improving. For much of the latter half of 2008 and the first half of 2009, most deal participants appeared to be paralyzed with uncertainty. Many buyers believe this is an attractive time period to acquire businesses and/or market shares at relatively low valuations. At the same time, a number of sellers have concluded that with the likelihood of higher capital gains tax rates in 2011 and beyond, a sale in 2010 may generate higher net proceeds. Furthermore, some private equity funds feel pressure to liquidate portfolio companies where possible after an extended period during which such sales were not feasible. Finally, some restaurants have decided, either voluntarily or involuntarily, that their only choice is to sell-out as high leverage and/or sale declines have eliminated other strategic alternatives.

Obstacles remain for a robust M&A deal environment. Many sellers have not adjusted their valuation requirements to the realities of the current capital markets and lending environment, and many lenders remain relatively conservative in their borrowing ratios and advance rates. However, we anticipate the forces described above will contribute to a continued pick-up in activity in 2010. This trend stands in contrast to the higher level of debt restructurings and bankruptcies the industry will continue to experience. This juxtaposition highlights that in virtually every environment there will be operators who excel and those who struggle, those with healthy balance sheets and those with no financial flexibility. The recent crisis has accentuated these differences and created something of a "barbell" effect on the industry deal activity.

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Trinity Capital provides a unique combination of world class financial professionals providing exceptional boutique-style service. Whatever the assignment, you can be sure of receiving proactive, value-added advice from experienced investment bankers.

We are industry acknowledged experts at managing and executing all aspects of your transaction with senior level attention produces superior results. With dealmaking experience of approximately $20 billion in transactions since 2000, Trinity Capital has a broad range of industry experience with a focus on entrepreneurs and specialization in the restaurant, food and energy sectors. www.trinitycapitalllc.com