

Check, please: Restaurant M&A slumps as consumers' habits shift

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Restaurant deal making activity over the last year has been largely quiet, as private equity plays a wait-and-see game with the state of the economy and changing consumer spending habits, several industry sources told *Mergermarket*.

Over the last 18 months it's been difficult for deals to get done because of extremely high valuation expectations from founders and increased interest rates that have made it more difficult to borrow money, said Andrew Smith, managing partner at Utah-based private equity firm **Savory Fund**.

"There's really been pressure on both sides of the equation to make the deals pencil like they used to," Smith said. "A lot of people just sat on their fingers and just thought, 'as soon as interest rates come down, LBO will pick back up, and I can start doing transactions again.'"

Smith said, however, over the past three months multiple have started to soften a bit and there has been a bit of "a shift in the tide."

A handful of those concepts that could be ripe for acquisition in the future include **Swig**, **Smalls Sliders**, and **Dave's Hot Chicken**, Smith said.

Dave's Hot Chicken grew almost 100% in 2023 and has roughly 950 locations in development, 100 of which will be added this year. Swig started franchising last year and now has 16 in the pipeline, in addition to 25 corporate locations to add to its existing 62. 10 Point Capital-backed Smalls Sliders signed a deal with Tampa-based Purple Square Management to open 22 locations in the Phoenix metro area.

Smith said it's critical for restaurant brands to be reaching 18%-25% store-level profit to scale and attract investors.

Recent bankruptcies

Many struggling concepts have had to file for Chapter 11 bankruptcy this year. Most notably, **Red Lobster** filed for bankruptcy protection in May, citing a "difficult macroeconomic environment," but Smith said the chain's struggles are not necessarily reflective of the current environment

The chain recently exited Chapter 11 restructuring, appointed a new CEO, and completed its acquisition by RL Investors Holdings, which plans to invest more than USD 60m in funding to help buoy the struggling company.

Other restaurants to file for bankruptcy this year include **Roti**, **Buca di Beppo**, **Tijuana Flats**, **Kuma's Corner**, and **Sticky's Finger Joint**. West Palm Beach, Florida-based **AUA Private Equity Partners** sold Tijuana Flats to **Flat Holdings LLC** as part of the restructuring.

Even in the current environment, there can be a market for underperforming restaurant concepts for investors who see opportunity to take costs out of the business or implement a specific plan to re-engage consumers and drive positive traffic, said Kenny Kraft, managing director at **Houlihan Lokey**.

"Given the current macro environment, even restaurants with strong brands and loyal customer followings are having to manage through operating challenges and traffic declines," Kraft said. "It's just a matter of weathering some of the near-term operating headwinds and getting back to a track record of same-store sales comp growth, and overall profitability. The market is even stronger for those who have outperformed peers."

Where deals are happening

M&A activity hasn't come to a full halt, but the concepts attracting attention from private equity have unique characteristics that allow deals to close easier and faster.

Tropical Smoothie Cafe and **Playa Bowls**, both whose locations are mostly franchised, are examples of fast-casual brands that are innovators in their respective spaces, which is a draw for private equity now, Kenny Green, director at **Capstone Partners**, told *Mergermarket*.

“A digital component as well labor and cost of goods sold are big things in restaurants,” Green said. “If you have a digital setup that can minimize your labor, I think those are going to get some attention too.”

Earlier this month, **Sycamore Partners** completed the acquisition of Belmar, New Jersey-based acai chain **Playa Bowls** for an undisclosed amount. *Mergermarket* previously reported in August that the company generates around USD 20m-USD 25m EBITDA and was looking for a multiple in the mid-high teens. The chain’s sales grew more than 44% in 2023 to USD 225m, according to [Technomic](#).

In April, **Blackstone** [NYSE:BX] entered an agreement with Los Angeles-based **Levine Leichtman Capital Partners** to acquire Tropical Smoothie for a reported deal value near USD 2bn, including debt, according to *The Wall Street Journal*.

Tropical Smoothie has more than 1,400 locations across 44 states, growing from roughly 800 in 2020 when Levine acquired the asset. During this growth stage, the company’s investors contemplated taking the fast-casual franchisor public, but last year settled to pursue a sale process, hiring Baird for the mandate.

Prior to the deal, Tropical Smoothie was purported to be valued at around 20x of EBITDA, according to a December 2023 Reuters report.

In this environment, a deal like Tropical Smoothie at that purported EBITDA multiple is truly a “gem,” Green said, adding that franchisor models typically go for higher multiples, as opposed to company-owned stores, which are seeing far fewer deals.

Earlier this month, **Thrive Restaurant Group** announced the acquisition of Denver-based **Modern Market Eatery**. Thrive has been a franchisee of Modern Market since 2022, previously purchasing three locations in Austin, Texas, and building two in the Kansas City area. The acquisition expands Thrive’s portfolio to seven states with 24 restaurants and five licensed locations.

“There’s some pressure from a franchisee front to where some of the big brands—Wendy’s, Burger King, Taco Bell—they’re limited what you can do to grow, so they’re capping you both in terms of number of units as well as competing concepts in the franchise space,” Green said. “So by buying a brand, you can get around that a little bit.”

Capstone currently has a regional pizza franchisor in the market, which Green anticipates will close within the next 30 days. Capstone brought the asset to market last November, and despite the category relying on discretionary spending, Green said the buyer is comfortable with the deal since the franchisor dominates a region and there are opportunities for consolidation.

“There’s been some pain points internally,” he said. “I think buyers are generally more diligent on various items and more sensitive to things where, in the past, they’d let it slide, and now they’re really digging in.”

by Katishi Maake in New York



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