

14-Mar-2023

Portillo's, Inc. (PTLO)

BofA Securities Consumer and Retail Conference

CORPORATE PARTICIPANTS

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President, Chief Executive Officer & Director, Portillo's, Inc.

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OTHER PARTICIPANTS

Sara H. Senatore

Analyst, BofA Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Sara H. Senatore

Analyst, BofA Securities, Inc.

Good morning, everybody. Thank you for joining us. I'm very happy to have with me up here on the dais Mike Osanloo. Sorry, we just had a conversation about the pronunciation so I think I overcorrected. And Michelle Hook from Portillo's. And I'm sure many of you know Portillo's, but it's a fast-casual restaurant that specializes in Chicago specialties like Chicago-style hot dogs and Italian beef sandwiches, but also a more traditional limited service menu.

So, we're going to have a wide-ranging discussion because both Mike and Michelle bring a tremendous amount of history, both obviously at Portillo's, but the industry broadly. But if you do have questions, please don't hesitate to raise your hand. I think we have a mic or we'll have a mic circulating, and happy to have audience participation.

QUESTION AND ANSWER SECTION

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

So, with that, let me jump in here and let's start talking about the consumer, and in particular, the consumer in the context of your trends. So, what we have seen over the past, let's call it, four quarters is that, look to me like there was, demand was very strong. And then maybe, we as an industry hit a little bit of a softer spot in 2Q of last year. And then you've seen some steady improvement. I know you look at entrée counts. I think the cadence sort of follows that for you. But like I said, seems like a broader audience. I guess to what do you attribute that cadence, if you will? Because the macro environment doesn't feel like it's changed that much consumer sentiment. But so do you have any thoughts on that and how we should think about consumer demand going forward, given all the volatility?

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Well, first, thanks for having us here, Sara.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Oh, my pleasure. Thank you.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

I think the consumer is complicated, right? And I think there's – when you think about a consumer psyche, it's what's the next shoe to drop? What's the next shock? And I actually think that, for a period of time, for the last three, four quarters, it's been relatively – yeah, the macroeconomic environment hasn't dramatically improved, but it hasn't gotten worse. There haven't been some big shocks. And I think consumers are very adaptable. And so, I think the consumers said, okay, so now we're used to conflict in Ukraine, higher energy prices, inflation at 7%, 8%. We're used to this now. And so, I think that they started reacting to a new normal.

And the benefit for our industry is that, as much as inflation has affected us, it's affected the CPG companies worse. So, food away from home has not gone up nearly as much as food at home. And food away from home still tends to be something that human beings like to do. You like to go out. You like to go break bread with someone and interact. And the quality and the taste of food away from home continues to improve. 20 years ago, fast-casual didn't exist because the quality just wasn't there. So, I think the value propositions, the enthusiasm for going out, and I think getting adjusted to a little bit of a new norm has helped our industry, maybe more so than others.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

That's a good segue way to my next question, which is, I think the longer-term algorithm calls for low single-digit same-store sales. The implication, I think and to your point, we're not usually banking on 7% to 8% inflation and price increases. So, implicitly, the view, I think, is that transactions will be maybe flattish or slightly positive. How do we get there from here? Is it sort of we've reset now and go from here? Or what's the sort of transaction driver go-forward so that we can have that sort of low single-digit?

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah. Well, I'll talk about our company in specific because we're really, we're kind of two companies in one. So, when you think about Portillo's and we have committed to a low single-digit comp, it's a combination of we have a very strong base in Chicagoland and the outlying suburbs, right? We're a mature company there. We've been there for 60 years. And Chicago is not a growing market, population base is not growing. So, when we grow comp in Chicago, you're fighting tooth and nail, because transactions are actually organically declining. So, we think we can be flattish on transactions, which means we're taking share and we'll get a couple points of pricing on a regular basis.

So, the Chicago market and the core Midwest will be positive, low single-digits. We expect better out of our investments along the Sun Belt, places like Florida, Texas, and Arizona, where they will open up at AUVs below what the Chicago market has, but these markets have population growth, transaction growth. And so, we think that those will be better, better comp, and will continue to grow and be a really nice story for us. But Chicago is incredibly profitable for us, it generates a ton of cash, and we're taking that cash and deploying it to high-growth markets.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. And in terms of thinking about that traffic growth because, again, this past year, and we'll get to sort of channel shift and all the other dynamics, but the past year entrée count has been sort of flattish. But transaction growth I think has been modestly negative. So, I guess two things. One is should we be thinking about entrée growth? And then, two, how do we get from negative to flat or to positive? And that's I guess the crux of sort of are we reset lower because there have been so many adjustments in – related to COVID and now we grow from here.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

I think you've caught on to the point, I want to emphasize something about entrée growth. I think it's important for companies like us to look at entrée growth because channel mix clouds the story, right? I've explained this, like, when you have somebody who comes – when you have two people, two friends that go and dine in at your restaurant, they typically each are ordering for themselves, that counts as two checks, two people. If those same two people went through the drive-thru, it's usually one person paying. And it's one check, one bill. And then, if they did third-party delivery, come back, send it back to the office, it might be one check, but like five people.

So, when you look at transaction count, it's really check count, and it can be misleading when channel mixes are shifting so radically. And they have been. I think channel mix is starting to stabilize. And so, at that point, then I think you just go back and look at transactions traditionally.

Now, we have had very positive trends on both actually, transaction and check – sorry, sandwich count and transaction count over the last six, nine months. In fact, we announced this at our earnings. We are positive year-to-date on both transactions and on sandwich count. So, we think that the consumer, at least with our brand, is voting with their feet and we feel really good about where our value proposition is. And we made – we got some heat for it, we made very purposeful investments in the consumer in 2022. We did not raise prices as aggressively as almost any of our peers. And so, we invested in the consumer. That value proposition is paying back now.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. Right. In the form of a better transaction growth, in the form of [ph] brand (07:38). And I guess maybe just to put a finer point on that, relative to your underlying trends, the strength year-to-date, does it surprise you or it sounds like you view it as a continuation? Because I think for outside observers, it felt like the step change higher in January, February. But if I think about the underlying volumes, is that maybe less accurate characterization, it's much more consistent with trend?

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

I think it is a trend. I don't know if I'm old school or an analytic guy, but I pay attention to what I think are the underlying drivers of our business, right? You can – anybody – I can look at sales any given week and say, hey, we did great. I look at things that are leading indicators like our OSAT scores, our value perception. I see what guests are telling us. They're telling us – our overall satisfaction scores, our value perception, our speed of service metrics, these are really important in our industry. Those all reached multi-year highs in the third and fourth quarter of 2022.

I love when I see that because that means I'm going to have a good 2023, right? If people are saying, hey, this is the best, and by the way, the back half of 2022 wasn't an easy time to please guests, right? The bar was really high, they were very demanding. And so, when I see those things, it gives me a lot of confidence looking forward. Conversely, when I don't see those things, I get – I fret and we'd deal with them. But I think the leading indicators for our business have been very strong now for the last six to nine months, and we watch them assiduously and we make sure that we're giving guests a great experience. You do the right things, the sales come.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. Right. And I think those are the data that as an outside observer, we can't always see. But you're tracking the guest intention and the guest perception, which is so critical. I guess one dynamic, and we talked a little bit about this, in terms of mix shift that we've seen, is that off-premise sales have not – they've remained higher. They're not at peak COVID, but they're well above pre-pandemic levels.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

So, I guess maybe talk a little bit about what – to what you attribute that, and also what does that mean in terms of, as you think about going forward, whether it's your – whether it's how you build your restaurants or how you staff or whatever kind of changes to the operating model you might need.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah, it's – I confess to be a little confused. The person ordering through the third-party app off-premise remains stubbornly price-inelastic. You can't charge them enough for them to say no more. And I just don't – I don't get

that, except I see my daughter ordering from, like, Starbucks, like \$20 worth of coffee that costs \$10. I'm like, what are you doing?

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

You would be surprised how many executives I talk to point to their kids.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

And the kids are price-insensitive, to say the least.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Oh, but I nipped that in the bud the minute I saw that nonsense. I'm like, it's five blocks away. Go walk. So, I think that there is a segment of our society that is highly price-inelastic and greatly values the somebody-bring-it-to-me dynamic. I would have guessed that the growth in that would have stopped. It has not stopped. It's still a very healthy channel for us. It still grows dramatically and God bless them.

So, I'm not sure I get it. Whether or not I get it, I think it's important then to think about how do you design and build your restaurants for a stronger off-premise business? And so, we have been working on that in multiple ways. I'm going to let Michelle talk about this because she's leading, we have a project we call restaurant of the future, which is what the new Portillo's restaurants are going to look like. It's not going to happen this year, but hopefully it affects the class of 2024 or 2025. But I'll let Michelle talk about how we want to be omni-channel have-it-all.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

A

Yeah, I think when you think about Portillo's, to Michael's point, we are multi-channel. So we have double drive-thrus in all of our restaurants, and we have the capabilities for third-party delivery. We do pick-up where you can order in our app, pick up in the restaurant. And then we have a robust dine-in business as well. So, we're sort of QSR plus. We're fast-casual with QSR elements.

But the way that we think about the restaurant of the future is going where the consumer is going, which is we've seen more off-prem business. Before COVID, we were about 50% dine-in. And right now, we're about 35%, 40%. So, it's dine-in has bounced back, but not to pre-COVID levels. And we don't expect to get back to that. But our restaurants today are about, we're building about 7,800 square feet today, and how do we get that more in line with, again, the off-prem business.

I think there's opportunities as we look at that restaurant of the future to shrink the footprint a little bit further, Sara, as we look at, again, more robust off-prem business, but still have the experiential nature of a Portillo's and not losing that aspect of it. And then, again, providing the way the customer wants to order from us, and we're there to service that business.

So – but think about like restaurants as you have those third-party delivery folks coming into your restaurant, having dedicated doors, right, where they know where they're coming in and they're not going through the restaurant and looking around, where do I go, where do I go? So, having that dedicated entrance for them, having dedicated space for those pick-up shelves for the consumer who wants to order online and come in. Making it easier for our team members, right, as they're making the food and looking at those efficiencies in the kitchen, I think are important, too, because as they're making the food, right, they're going to have to deal with putting it on the shelves, dealing with the drive-thrus, dealing with the consumer inside.

We're used to all that today, but how do you design a kitchen as well that is efficient for our team members to work in, I think it's important too, because when you think about the labor, right, and we'll probably get into that, it's not easy to staff restaurants, right? And I think you – everyone's talking about the labor environment. Portillo's, we're able to staff our restaurants. We've never closed because of staffing. We've never had to shutter channels, et cetera. But it's a challenge. And so, how do we think about a restaurant of the future that maybe doesn't require as much labor because we can get more efficient in how we work in the kitchen.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Q

That's actually – so, yes, you're right. I am going to grill you on, pardon the pun, on margins and cost. But I do want to ask about that, because one of the things about off-premise is that you lose the gatekeeper in the cashier, right? Like, you could either infinite basically order [indiscernible] (14:42). So, how do you manage that? Like the [indiscernible] (14:46) what are you doing? Can you still actually reduce labor if you have the – what strikes me as a much more kind of hard-to-predict demand flow. So, how are you handling that?

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

A

Yeah, [ph] well, there (15:02) are opportunities. Now, Portillo's right where you see our AUVs on here. I think they're on there, are they, Michael?

[indiscernible] (15:09)

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

A

...\$8.5 million AUVs. Portillo's are busy. We're busy all the time.

Michael Osanloo*President, Chief Executive Officer & Director, Portillo's, Inc.*

A

Yeah. The demand flow is easy.

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

A

The demand flow is easy...

[indiscernible] (15:17)

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

A

It's always happening. There's always people in our restaurants. Of course, you have your peak periods during lunch and dinner. But for us to understand that demand flow is we do understand it. And we've been operating restaurants, as Michael mentioned, for 60 years. And so, how we schedule that labor, how we manage that labor is actually pretty surgical. [ph] So (15:43) we have a robust labor-scheduling tool that we utilize where we look at the demand within a specific restaurant. We can schedule our labor by shift, obviously, and by making sure we have coverage during those peak periods.

But how do we, as we we're talking about, get to a point where we don't need as much labor, right? And I think looking at just efficiencies in the kitchen, the equipment that we're operating with, I think there's some things we can do there that we're looking at in restaurant of the future with – a lot of people talk about ordering platforms too. I don't believe in putting kiosks in restaurants. I think the smart phone is a kiosk. So how do we use that to do maybe some QR codes at the table where people can order? And I think those type of channels will help with the labor as we move into, again, that restaurant of the future. So, I think there's a number of things that we can do.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

One simple thing, last year, we went from very distinct POS, using it on the outside versus the inside. So, we have inside order-takers. And we're not like, our drive-thrus are not like what you might think of in typical QSR. You drive up, you squawk into a box, go to a window, pay, go to another window, collect your food. That's not how ours work. You have menu boards, two people come out, and the person takes your order, collects payment right there. And then as you move forward in line, a runner comes out, runs your food to you, and then you can pop out of line when you get your food. So, it's a very different model than typical QSR.

We used to have two different POS systems, for outside and inside. Both those POS systems, they're antiquated, [ph] just the only way (17:30) to describe them. They're antiquated. If you wanted an ever dog, which is a hot dog with everything on it, you had to dog, add, add, add, which is insane...

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

...because this is a popular...

[indiscernible] (17:42)

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah. So, we refreshed the POS systems inside and outside. We aligned them around one common language. So, ever dog, there's a picture – literally a picture of a hot dog with an E, hit that button, you're good. You want to take something away, you can take stuff away, easier. It dramatically reduced the amount of time that we need to train people [indiscernible] (18:04). The other nice thing that it did is if you're super busy outside, you can move a cashier outside. They're already trained on how to do it. If you're slow outside, the weather is bad, but you pump it inside, you move a person inside. It's saved time, saved training, better accuracy, and it created labor flexibility. There's still a raft of opportunities like that for us, because on one hand, we're a 60-year-old brand. But we've been run professionally for like three, four years.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. Right. So, I mean, which is a nice place to be in the sense of you have all of the – you have the brand, equity, and all of the familiarity the 60 years brings with you.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah. That's right.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

But you have a lot of opportunity.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

We have all the opportunity that 60 years of entrepreneurship brings you.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. Right. So, you're in that good, sweet spot, if you will. So, I do want to just quickly talk about in this context, you talked about drive-thru. You've opened, I know you have a drive-thru-only location in Joliet.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

I think this format is more about infill markets and capturing that as opposed to new markets. But maybe you can talk about sort of the balance of non-traditional versus traditional, I think definitely leading towards the latter. But give us a sense of kind of what that footprint looks like.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah. I hesitate to say this because there's restaurant companies that say, well, we're a technology company. It makes me chuckle. We are an experiential restaurant company, right? I want people to experience Portillo's. Dick Portillo, when I first, like, came on board, I was visiting restaurants with him. And there's a genius to the way he thought about Portillo's. And one of his – one of the things that he said to me that really stuck with me is when you come into a Portillo's, it appeals to all of your senses.

There's something to that. When you come into our restaurant, there's a ton of stuff going on visually. Like, it's silly. But we have these LED stars in the ceiling that twinkle. It catches your eye. It's a beautiful restaurant, it's tricked out with all kinds of stuff. There's sounds, it's a loud restaurant. But that creates a sense of energy. You can smell a lot of stuff cooking. And I love the smell when you go in, my mouth, it's a Pavlovian response. I start salivating.

So, all those things are really, really important. And I want people to establish their love affair with Portillo's by going into the restaurant and eating at the restaurant. There's not – our fries are the best fries in the world, but even the best fries in the world, they spend 20 minutes commuting, die. And so, I want them to eat the food in the restaurant. So, we want beautiful restaurants. We want to engage people. We want you to bring your kids in so that your kids can go, wow, look at this thing. There's a Toyota truck hanging from the ceiling.

When you've got an established relationship with our brand, then we want to make the brand pervasive and easy to access. And then that's when it makes sense to have fill-ins. So, fill-in, the drive-thru-only makes a ton of sense in Chicago. Ton of sense in Chicago. So, don't be surprised if we build more drive-thru-only models in Chicago. People know us. They know how to use us. And so, that works.

And then, I think you go, you think about where will you saturate next and where does it make sense? And honestly, I think Arizona would be the next market for us. We've been in the valley now for a decade. We're building restaurant six right now. We'll have seven and eight next year. And then I think And honestly, I think Arizona would be the next market for us. We've been in the valley now for a decade. We're building restaurant six right now, we'll have seven and eight next year. And then, I think you can start thinking about some in-fills in Arizona, because those people also know our brand.

Sara H. Senatore

Analyst, BofA Securities, Inc.



Right. And I'm going to come back to that sort of how you know where your – the demand is [ph] and your direction (21:55). But before I do, I do want to – I promised you I would talk to you about margins. So, I'm going to do that. One of the things that sort of, as I was thinking about this drive-thru model, it's actually more – not more labor-intensive, there are more people involved than historically was the case, right? So, it used to be exactly what you said. You talk into a speaker box and maybe you do payment, maybe the same person might give you the food or somebody else.

Whereas now you're actually ordering with somebody and they're running the food to you. And so, in some sense, it's almost surprising how much more interaction you have than the traditional. So, I guess there are two things I'm getting at. One is, to what extent is there sort of an interactive component of that that is important? Because you talked about the Portillo's experience. And two, getting back to this sort of question, how should we think about the balance between technology and labor? Because as you said, it's been a really hard market to hire.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.



Yeah, I'll start and I'll let Michelle build. Here's the thing. There's a lot of companies that are moving more towards technological solutions, kiosks [indiscernible] (23:06) things like that. That's awesome. I love competing against them. You can become a glorified food kiosk and we'll still be a restaurant, because human beings still want to interact with – most do. You'll definitely find people who don't want to interact, but most do.

I love when you order at front cash with a Portillo's person because, Sara, what they'll say to you, if you order beef sandwich, they're going to say, would you like sweet or hot peppers on that? They help you curate the meal. If you don't order it, they'll say, by the way, have you ever tried our chocolate cake? We make homemade chocolate – literally homemade chocolate cake every day in-house. It's insanely good, right?

Sara H. Senatore

Analyst, BofA Securities, Inc.



It is.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

That is a curated dining experience. That still matters. And so, I think that having human beings who are doing things like that, who are helping you, is awesome.

Our drive-thrus are ridiculously fast. I mean, keep in mind, our drive – we're doing \$4 million just on the drive-thru side of our business, okay? That's people flying through there, and the reason you can do that is because you have human beings steering traffic. You got your food, you can just pop out right over there [indiscernible] (24:22) get out of the lane. And so, it's a win for consumers. It's a win for our team members. There's people who enjoy being outgoing and engaging. And so, I think we have a model that works really, really well, and it's a little bit unique, and I'm okay with that.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. Right. And to your point, unique can be good. It's a differentiator. And you think having a somebody, a front cash or whomever say, would you like to try a chocolate cake versus a machine that's going to try to upsell you? You think there's a qualitative difference between hearing it from a person and...

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yes. What is a consultative sale because it's somebody who's helping you solve a problem. Anybody who's been a consultant, you know you've got to find a problem before you can sell something. The other one is just a machine redirecting you to some algorithm on how other people order.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right. I see. Okay.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

A

And I think we can do both though, Sara, right? Because, as Michael mentioned, people do like to interact with other people. But those that don't, I think the opportunity is there to do that upselling in other formats. One of the things we invested in in 2022 was installing digital menu boards in all of our restaurants, both in the drive-thru and in the dine-in experience. So, we can upsell on that. We can feature our – we do some LTOs with shakes and desserts. We can do that.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

A

If we want to upsell a certain product, we can do that. So, we do have a format to do that, and talking about technology and how we weave that in. That is another method we can do that, if you so choose to not interact,

right, with a human being. But I think having that option is what makes the Portillo's experience different and unique, and why people do want to come and dine in our restaurants. And we've seen, as I mentioned, dine-in bounce back, not quite to 50%, but it's bounced back. And I think it can go a little bit further. And Michael and I believe that can be largely incremental to the brand as people continue to want to come into restaurants.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Q

Right. Okay, that makes sense. And sitting here as a New Yorker, I'm one of those people [ph] who doesn't (26:29) want to talk to anybody.

[indiscernible] (26:30)

Michael Osanloo*President, Chief Executive Officer & Director, Portillo's, Inc.*

A

I get that, yes.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Q

[indiscernible] (26:34). Okay. So, on the margin piece, I wanted to sort of talk about this kind of the economic model. And I think new units have come in at higher volumes, and the Sun Belt in particular has been very attractive. Can we talk about kind of how to think about margins because last year was sort of, I would say, an investment year in terms of people?

Michael Osanloo*President, Chief Executive Officer & Director, Portillo's, Inc.*

A

Yeah. That's right.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Q

[indiscernible] (27:04) you've been a price laggard. How do we think about the sort of traffic versus incremental price as a way to sort of get the margins maybe back to a more normal?

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

A

Yeah. I mean, Michael and I are both committed to growing margins in 2023 versus 2022. We purposefully made investments in 2022 because we didn't want to do long-term damage to this brand and we wanted to make sure we balanced out price-taking with – not at the expense of significantly reducing our traffic. And so, as we move into 2023, absolutely, even though we have 13 new restaurants coming online, four as part of the class of 2022, and then nine as part of the class of 2023 into our portfolio, so, despite that, we still believe we can grow margins and we're going to continue to use the pricing lever. And we've already announced we've taken 2% more pricing in mid-January.

And as we look into the future, Michael and I will continue to look at the landscape and pull the pricing lever as necessary as we have to continue to offset inflationary costs in the business with both food and labor. I think those will be mid-single digits this year on those two high input costs for us. And so, we need to offset that, but I

think catch up a little bit on some of the pricing that allows us to grow the margins. And that's what we're committed to this year.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Laggard – I want to clarify something, laggard doesn't mean won't take pricing.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Right.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Laggard just means we'll – I believe that the cross-elasticity effect of pricing is typically worse than the direct elasticity effect. So, like, after everybody else has taken their pricing and shocked the system, then it's time to take pricing.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

And actually it's a good question, but it's a good point about cross-elasticity. But I guess in that context, how are you thinking about relative value, right? So, if everybody took, and this is obviously a [ph] stylized view (29:02), but 10 points of price last year, and you took less or they took, in some cases, mid-teens, and you took less. And now, your gap narrows a little bit. You're not worried about that. We'll see. And we'll see whether others actually hold the line on price.

But if that were the case, you'd still be about value, but perhaps slightly less so, or the gap would be slightly narrower. So, when you're thinking about value, are you looking at increases year-over-year or are you like actually measuring what can I get for my money? And I'm looking at a broad kind of group of whether it's food at home or other fast-casual, fast food. Maybe how is your [indiscernible] (29:42)?

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah. So, it's honestly pretty – I won't say complicated, I'll say thorough, it's thorough. So, we absolutely track pricing year-over-year, us versus them. We track the most popular bundle that we sell versus their most popular bundle for a series of different restaurant companies. And so, we know that, right now, our most popular bundle, beef sandwich, peppers, fries and a drink is anywhere from \$1 to \$7 or \$8 cheaper than the people we typically compete with. And so, so we say just on prices, at what you get for the money, we're in a really good spot.

I think when you're making these decisions, you also need to look at what are your guests telling you about your value proposition, about how satisfied they are with you, and your speed of service, because those are all parts of the value that you provide them. All three of those metrics, value proposition, speed of service, overall satisfaction

are at multi-year highs for us, so that what the guest is getting from us at that price point is about as good as it's ever been, which tells us that we have [indiscernible] (30:54) price.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Right.

Q

Michael Osanloo*President, Chief Executive Officer & Director, Portillo's, Inc.*

If they're telling you, you might be below everybody else on pricing. But if your guest satisfaction scores aren't good, if they're telling you your value scores aren't good, you actually don't have any power of price.

A

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Right, right. Right, to your point, the guests will determine, yeah, the value. That makes sense. Secondly, on margins, we talked about mid-single-digit, which would be still up but much less [indiscernible] (31:22) nice disinflation. It seemed to me last year that labor was -predictable's probably the wrong word, but we kind of saw a trend with labor, whereas the commodities just there was a tremendous amount of volatility. So, how are you thinking about this year? Mid-single-digits is your best estimate. But as you look at the commodities market, are you seeing anything that surprises you or are you still anticipating volatility? Maybe talk about also where you're locked and how much visibility you have?

Q

Michelle Hook*Chief Financial Officer, Portillo's, Inc.*

Yeah. I mean, look, we don't know what's going to happen, but as we sit here today, we think that some things have started to stabilize. For us, beef is about 35% of our total basket. And then when you add in chicken and pork, those proteins make up about 50%. All three of those in totality. So, as those move, that's going to have an outweighed impact on our basket.

A

I think we all know what happened in beef last year. We saw some highs that started to come down in the back half of the year. It remains okay right now, but I think that could be pressured in the back half of the year. I think chicken and pork have largely come down from highs of last year. So, that's been a good sign for us. And so, that's balancing some of the increases on beef I think we'll see this year.

And then, French fries for us, which is about [ph] 7% to 8% (32:42) of our basket. We're seeing pretty significant increases on that this year. And so, when you blend those together, Sara, I think we'll see some deflation, I believe, on chicken and pork, but offset by fries and the beef costs is how we get to mid-single-digits.

But again, last year, I didn't think when the year started, we'd be at 15% commodity inflation. And so, the world just kind of fell apart. But I don't see that happening this year. I think it's stabilized a bit. And on the labor front, we were up about 11% on hourly rates last year. And so, I think it's a reasonable mid-single-digits this year, knowing that we still have investments that we want to make in our team members. But we've, over the course of the last two years, made significant investments in our team members and in labor. So, I think that will largely stabilize as well this year, but still be up.

Sara H. Senatore*Analyst, BofA Securities, Inc.*

Q

And, Michael, you mentioned sort of a surgical approach. When I think about pricing, presumably it's not you take the same price increase across all menu items. You're sort of – yeah, so how does that look? Are there certain SKUs you want to protect? You talked about the bundle, I guess how – maybe talk about your approach to pricing.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

It is – look, we try to be very thoughtful. We have some very popular baskets. You're not pricing everything in the basket ever. So, beef sandwich, fries, and a soft drink. You're not pricing sandwiches, fries, drinks. You might price sandwiches, you might price sides, you might price drinks. You might say I'm just pricing off-premise channel. I might just price catering. But we take a very surgical look to the pricing. And we do – when we price, we compare. What do our fries cost versus everybody else's fries? How good of a deal is our fries? How good those are portioned versus theirs? How about our sandwiches? Where do we stack up?

And so, when we price, we also – Michelle and I have said this, that we like to price in small chunks. We don't take big chunks of price and we take small – I'd rather take multiple small bites of pricing than a couple of big bites.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

There's, I guess, less sticker shock.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

Yeah, to the customer. Yeah, that makes sense. I want to – you've mentioned like how much food you get. That was – when I first went to Portillo's, that was what was so surprising is just the sheer volume.

[indiscernible] (35:12)

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Well, that's true, Sara.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

I know.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

We like to eat.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

I know. I was just, I remember thinking, oh, surely, this is going to cost me like my whole per diem [indiscernible] (35:23) \$25, was just crazy. So, and to your point about Midwestern, let me use that as a sort of stepping stone.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

Yeah.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Q

The question always comes up about portability of the brand. I think it's – at this point, your volumes in new markets are very high, but how do you think about this sort of 600-plus target in the context of, there are only so many Chicago ex-patriots, I think, so that we can – and so, we know that some of your biggest markets, I think Arizona you mentioned, there's some of that culture that gets carried with you. So, how do we think about the portability of the brand? And in the existing markets where you are very successful, is that enough of a market, a TAM for the total count that you're thinking about?

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

A

I got to tell you, I think it's the most exciting element of the Portillo story, right? So, like, I kind of feel like I'd bet my career on the portability of Portillo's. Like, there's a lot of places I could have gone to, but I'm here because I think that I'm [indiscernible] (36:29) I am privileged to lead a sleeping giant. And I think Portillo's is going to be portable. I've recruited a team that's like-minded in that sense.

We – I get this question all the time and I think underlying that question is that, hey, your food is kind of different, right? It's not very typical. So, an Italian beef sandwich. It's not Italian, it's Italian beef sandwich. Or a hotdog. What's so different about your food and what people eat it? So, I'd say my favorite proof point is our average restaurants in Midwest, in Chicagoland does \$10 million. We now have \$9-million, \$10-million restaurants in Arizona and Florida.

We opened at The Colony in Texas, which is just past Frisco, north side of DFW. Since it opened, and it opened in early January, it's been the number one restaurant in our system. It's averaging \$48,000 a day, which would trend it to be a [ph] 17-plus million-dollar (37:35) restaurant. Don't model that number. Don't bank on that. But you know what it is going to do? It's going to smoke our underwriting expectations. And people say, why do you think The Colony is doing so well? I'm like, because people like beef and bread in Texas. It's not that complicated. It's a really good sandwich. And it's selling a ton of Italian beef. And we're getting phenomenal feedback. And it's been a home run of an opening.

We're going to open a boatload of restaurants in Texas, in Florida, in Arizona. We'll go to Georgia, we'll go to these other states. I think that it's a very conservative 600 restaurants as our TAM. I think that I'm very comfortable that our food is enjoyed, loved, and eaten. You don't do – the volumes we're doing at The Colony, it's not ex-Chicagoans who have found their way there. It's locals, right? You can't sustain that kind of a bit. You certainly get a lot of ex-Chicagoans the first couple of days, they're excited. It's a nostalgic thing. It's a taste of home. They're not driving \$17-million trend.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Right. Right.

Q

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

So, I think it's – and then I challenge people like, look, it's a fair question, can you guys truly be a nationwide restaurant chain? Very fair question. Because we're iconic, we're unique. No one does what we do. The logical corollary to that is if I can prove to you that we're going to be nationwide, we should get the fattest multiple in the restaurant industry, because we're iconic, we're unique, and no one does what we do.

A

Sara H. Senatore

Analyst, BofA Securities, Inc.

Right. No, that – I think, and you mentioned people in Texas like beef and bread. People everywhere like beef and bread.

Q

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

People like beef and bread.

A

[indiscernible] (39:19)

Sara H. Senatore

Analyst, BofA Securities, Inc.

It's delicious...

Q

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

Yeah. It's going to work everywhere.

A

Sara H. Senatore

Analyst, BofA Securities, Inc.

Yeah. I think that's right. I'm just going to see if there are any questions from [ph] I think from the (39:28) audience. So, in our last, I guess 24 seconds, maybe I'll ask Michelle as we think about to your – to Mike's point about blowing through underwriting expectations, sort of how should we think about going, or sort of what the hurdle is and to the extent that there's probably upside, where is it going to come from?

Q

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

Yeah, I think we continue to think about our targets as a class of restaurants, Sara. And so, when we talk about classes, we are going to have restaurants that are going to be homeruns in the class, like The Colony. We're going to have restaurants that are going to be at the rates we thought they were going to be at. And so, our targets still remain that, by year three, we want the class of restaurants to do \$6 million and 22% margins, and that will deliver a 25% cash-on-cash return. And that remains our targets.

A

Now, Michael and I want to build as many homerun restaurants as we can. And him and I are very competitive people. And so, we are not happy with those numbers that I stated to you. So, our goal is to continue to outperform those numbers and continue to build restaurants that are going to perform above our underwriting expectations.

Sara H. Senatore

Analyst, BofA Securities, Inc.

I think investors would be happy to hear that.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

Yes.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

Yes.

Sara H. Senatore

Analyst, BofA Securities, Inc.

All right. Well, thank you so much for joining me.

Michael Osanloo

President, Chief Executive Officer & Director, Portillo's, Inc.

Thank you.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

Thanks.

Sara H. Senatore

Analyst, BofA Securities, Inc.

Yeah.

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