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MANAGEMENT DISCUSSION SECTION

Dennis Geiger
Analyst, UBS Securities LLC

Good morning. I'm Dennis Geiger, restaurants analyst at UBS. And I'm pleased to welcome and excited to have on stage with us, Michael Osanloo, Portillo's CEO; and Michelle Hook, CFO; and also representing Portillo's today is Barbara Noverini, Director of Investor Relations.

Quick intro for the team. Portillo's is best known for its Chicago-style hot dogs, Italian beef sandwiches, char-grilled burgers and delicious and famous chocolate cake, among other delicious items on the menu. Portillo's now has more than 80 restaurants across 10 states, while maintaining one of the industry's strongest growth opportunities.

And with that, I want to welcome Michael, Michelle and Barbara. Thanks so much for being here with us today.

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

Thank you, Dennis, and thank you for that introduction. So for those of you who are not familiar with us, that is our food up there. That is our Italian beef sandwich with peppers, our Chicago-style hot dog. Do not sleep on our fries or burgers, Dennis. They're amazing. So we're very, very proud of our food.

I'm going to talk for just a few minutes and share with you a little bit of who we are and what we do before we dive into the Q&A part.

Here's how I would describe us at a glance. We are incredibly proud of our food. We think there's something craveable for everyone and I mean for everyone. We have vegan offerings that are fantastic. That is one of our new salads that's coming on market at the end of this month, the new spicy chicken chopped salad. We – our Spicy Chicken Sandwich has been a home run. It's on trend. We think this is a fantastic, delicious salad that creates incrementality and visitation.

We're experiential, differentiated dining. If you haven't visited our restaurants, I'd encourage you to take a look at them. They are beautiful. It's the place you'd be fine and happy to take your family, take kids, go with a friend. It's a gorgeous layout. It's a beautiful box with engaging decor.

We are available any way you want it. We were multichannel before multichannel became a thing. We have very robust double lane drive-thrus where people come out, curate your order with you, run your food out to you. So it's very different than a typical drive-thru.

We have fantastic dining rooms. We do third-party delivery. We do our own delivery on orders over $100. We have a robust catering business, and we also ship food all across the country. All 50 states, we ship Portillo's to. So we've been doing this for a long time, multichannel for a while.

We have obsessed fans. I'll share with you some NPS scores. People who know us don't just like us, they tend to love us. We think we have an unmatched value proposition. That's not just price point. Our price points are incredibly good, but we also have abundant quantity, amazing quality and a great experience.

Our unit economics are – they will speak for themselves. I'll show you the numbers. You can judge what you think of them. And then we are growing very, very fast. Dennis is right on our growth trajectory. We think we're on the road to over 900 restaurants. We opened restaurant 85 two days ago. So we're really happy with where we are, but it's just the tip of the iceberg for us in terms of growth.

And then we have – we will talk about our strategies. We think we are very surgical in what we do, and it pays out. So there's something craveable for everyone. Our menu mix is a little unique. It has a little bit of complexity, but we also think with that complexity comes veto-proof dynamic. If you're going with the family, the kids want to eat something specific, your partner says, look, I just want a salad today. We have it all.

I actually like to talk about our salads. We sell per restaurant $650,000 of salads that are fresh made when you order. They're hand-tossed out. You want a chopped salad, you don't want green onions and blue cheese, no problem. You want what I think is the best commercially available Caesar salad, you're going to get it from us at a really good price point. So our sales mix is both an advantage and creates a little bit of a competitive moat for us.

This is our Orlando restaurant. And I show you this picture because I think that it's easy to build a really inexpensive box that looks like every other box that has no soul. This is a restaurant where you will see families. This restaurant is a little over a mile away from the front door of Disney, and it works exceptionally well.

Our restaurants are cookie-cutter when it comes now to the kitchen line, the footprint, et cetera, but they're all uniquely designed so that for every local market, it feels like this is your Portillo's, right? This is unique. Nobody else has this giant guitar on the ceiling with LED light. It's a gorgeous – we think it's a point-in-time look. This is our diner style. It's a point-in-time diner. It doesn't actually go out of style because it's targeting a point in time, which means that maintenance and upkeep is relatively easy. You – it's seatbacks, it's tables, it's floors. I'm not redesigning the entire restaurant at any point.

We're available anyway you want. This is our sales for 2023. We did $3.5 million per drive-thru. That's roughly the equivalent of [ph] two-plus (00:05:28) McDonald's in the drive-thru. We did $4.2 million dine-in. That's a Chipotle. We did $1.2 million in delivery. That's a Domino's. So you're getting the benefit of two McDonald's drive-thrus, a Chipotle and a delivery – a Domino's delivery business all under one roof.

That channel mix provides us all kinds of defensive protection depending on how the economy goes, offensive opportunities. We can push different channels at different occasions. We also have this off-premise thing where we have a lot of people doing carryout, catering and direct shipping. And I think that that's important, again, because it gives you growth opportunity.

I love – we talk about the catering business. I love the catering business. I view the catering business as a paid sampling exercise. Somebody is paying you to go get your food and to serve it to 20, 30, 40, however number of people. It's paid sampling. It's marketing that I'd almost do for free, except we can make good money off of it. And so we love the catering business. We especially love it and as it grows outside of Chicago. And we've pivoted to an outbound team that does call to generate sales side.

Can I get a little help with the slides? Thank you. Our NPS study that we monitor, we care. How do people think about us, and we compare our NPS to what I think are some world-class companies. Objectively, these numbers are actually very good. NPS scores of 50 or above are outstanding scores. We feel really proud and privileged to be near the top of that list with some amazing names, right? These are In-N-Out, Chick-fil-A are world-class operators. I think they're just world-class operators. It's a source of pride and privilege to be lumped in with them. So we feel very, very good about how we're viewed.

This isn't like a homer thing. This isn't – we're not just talking to people in Chicago. This represents people all across our geographies. So this is people in Texas, it's people in Florida, it's Arizona, all the 10 states that Dennis referred to.

Where we compete, we have remarkably high level of fandom. That's very important because, again, if you haven't experienced us, this is like an intellectual exercise. Go visit our restaurants, see how people engage with us, see how people are engaging with our food.

We think we have an unmatched value proposition. This is a very specific thing. So we look at what we believe is an indicative restaurant. This restaurant happens to be in Elmhurst, Illinois, a suburb of Chicago. We take our most popular bundle, which is the beef sandwich, small fries and a small drink. It's $13.37 at Elmhurst.

We then go within a three- to five-mile radius, and we look at all of our competitors and see how they price. And you can see what the prices are based on what we believe is their most popular bundle. We think that that creates – that is an unmatched value.

I'm not even talking about the quantity of our food because our food is abundant. Our burger isn't a quarter of a pound. Our burger is a third of a pound. The Italian beef sandwich is loaded with beef. Our fries – our small fries are huge. I'm not talking about that. I'm not talking about the quality of what we do or the quantity or the experience. This is just purely price. And just purely on price, we are really, really strong.

But to be fair, we said what consumers experience now, when you all go to a restaurant and that little POS flips around and the order takers says, oh, you just have to hit a button before you can finish, right? The tip button. And so you have to be there looking at this person across the aisle and go, I'm going to tip because I don't want anything bad to happen to my food. So that's that arm-twisted pricing that is a little disingenuous, but it's there. We don't do that. Chipotle doesn't do that. The other people that we identified here, they all do that.

So this is what their recommended tip is. If you want to hit the fewest number of buttons and just get out of there, that's actually what you're paying. Suggested tip is pricing in our opinion. And so we think that when you look at the suggested tip, our value is exceptionally good versus everyone else.

This is our – this is just a quick slide on unit economics. Our average unit volumes were $9.1 million. We generated $102 million of adjusted EBITDA. Our restaurant-level EBITDA margins were 24.3%. And I would tell you, we opened 12 new restaurants last year. Our restaurants as they mature, obviously, versus everyone else, as they mature, tend to have better margins. So on a base of 72, we opened 12 and generated 24.3% margin. Okay.

That's – I will let you fill in the pieces on what that implies, but we are very, very proud of that performance. I'm especially proud of the fact that we are a well-regarded employer for our team members, our frontline team members, right? 20 points, 20 percentage point lower turnover than the fast-casual segment.

That pays dividends in multiple ways. We have happier team members. Happy people make better food. Happy people churn a lot less. There's hard costs and soft costs associated with turnover. We're very proud of the turnover in our restaurants. We think it's one of the reasons why our NPS score is high, why other metrics within our ecosystem performed so well. We love being a good employer. We think that's a huge difference to us.

We're growing faster and further than ever, right? So you can see we have, obviously, a very strong core in Chicagoland and Illinois in general, but we're now in 10 states. We recently announced that we are growing. We're going to be building restaurants in Atlanta, Georgia, in Denver, Colorado and Las Vegas.

Our pipeline, when we announce that, that's not – don't expect those this year, not even necessarily next year because what we like to do is scout out regions. And when we go and build in a market, we want to build very quickly six to eight restaurants to achieve local scale. When we achieve local scale, you see better margins, better revenue performance. The whole business performs better once we achieve scale.

So as we look at markets, we want to identify six to eight restaurants that we are really good – excited to build, and then we like to hit go. So we're in that process in Atlanta, in Denver and Vegas to scout sites, get letters of intent to start the deal flow so that we can hit go and then very quickly achieve scale in those markets.

I'm super proud of the fact that within 14 months, we went from zero restaurants to we opened our fifth restaurant in [ph] DF (00:12:29), Dallas-Fort Worth area last week. I'm extremely proud of that. That's very fast for us. Those restaurants, we think, are going to be home runs, and we think that as we achieve scale in Dallas, it's better.

We did announce that we're going to be building in Houston this year. That's the next new metropolitan area that we're going into. And we have publicly said multiple times that 80% of all of our growth is coming along the Sun Belt, which is really more of a nomenclature for where is America moving to. Where is the growth in America? Three fastest-growing states in America are Texas, Florida, Arizona. Not surprisingly, we're building a lot of restaurants in those states.

A question people ask very frequently is how is your performance different? And so we have, obviously, exceptionally high brand awareness in Chicago, relatively good brand awareness in the rest of the Midwest. It tends to be a little bit lower in the Sun Belt, but we know that the Sun Belt has the highest growth rate.

But what's interesting is that when you look at these restaurants and you look at the AUV performance – Dennis, this thing jammed again. Can you advance it? Thank you. When you look at the AUV performance, we do really well in Chicagoland, $11.4 million AUV. We do $5.8 million in the rest of the Midwest.

What I think surprises people is that we actually do $6.8 million in the Sun Belt because I think it's a little counterintuitive that the farther afield we go, the better we do. People think, well, you must – are you a Chicago concept? Are you a Midwest concept? This personally gives me comfort thinking that this concept is portable. This concept performed exceptionally well in the Sun Belt. If we were only here talking about a $6.8 million AUV restaurant concept with our margins, people would be giddy. That's where our growth is, the Sun Belt.

And so – go back a slide. So last thing I'd say, we talk about long-term algorithm, and we're – we feel really comfortable with these numbers, unit growth of 12% to 15%, same-restaurant sales in the low single digits, combining to get to mid-teen revenue growth and adjusted EBITDA growth in the low teens.

People ask why is your EBITDA growth lower? Just think of it this way. You have such fulsome margins in Chicagoland, where we have a big core because these restaurants have been open for 60 years. We have great margins.

As you build new restaurants, they're fantastic. They're accretive. They generate a lot of cash flow. They generate margin, but they're margin dilutive until they fully mature. So that's the simple answer to why adjusted EBITDA growth doesn't grow quite as fast.

So I think that's the formal stuff, Dennis.

Dennis Geiger
Analyst, UBS Securities LLC

That's great. Thanks. Thanks for that, Michael. Terrific growth. Just phenomenal snapshot numbers when you look at them. And then obviously, the pictures, I think, are making us all hungry.

QUESTION AND ANSWER SECTION

Dennis Geiger
Analyst, UBS Securities LLC

Q

But I want to dive into a few of the points that you just outlined in a little bit more detail. Maybe we start with development, given how impressive the trajectory is. You maintain one of the best expansion stories in the sector with a minimum addressable market of 800 full scale.

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

A

Right.

Dennis Geiger
Analyst, UBS Securities LLC

Q

You just spoke to the 900 number. Can we talk a little more about the key drivers of that growth perhaps?

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

A

Yeah. Look, the – we went through and did a whole bunch of – I could have quoted you a ridiculously high number if I said that the density in Chicago is something that we're going to replicate everywhere. What we do is we did a massive regression study, have an algorithm on where does Portillo's perform exceptionally well, plug it into a model, and then say, where do we think we can build full-size restaurants that will achieve certain hurdles, right?

Hurdles have to be – it's got to be a certain revenue number. We don't want it to cannibalize other restaurants. And so we want them to be as accretive as possible. And that's where we get to the 800 number based on a multivariate regression.

There's another 120 that are – I would describe it as opportunistic, right? Like we're doing pickup-only locations in Chicagoland. We're really excited about them. They're smaller footprints, smaller restaurants, but still pretty darn good AUVs and returns.

They just don't have a dine-in. And we think that's a wonderful infill strategy right now in Chicago. But when you think about those, you think about potential airport locations, you think about dense urban walk-up only locations, that's where we get to the 920 number.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Terrific. Very exciting. And you showed the states, you showed sort of where you're going, which makes perfect sense. Maybe a little more visibility into that pipeline that you kind of started to address and sort of that site selection process and the perspective there if you could.

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

A

Yeah. So it's funny. We've done a lot of work on the pipeline, and it just is starting to show because when you're doing development, you need 18, 24 months to get the machine roaring, right? So – and here's what we've had to think about differently.

Like in Chicago, we can pretty much build anywhere, and that's going to be successful. But we have to approach new markets with a certain level of humility. And you've seen other restaurant concepts going to different markets not appreciating the fact that like we do really well, but outside of Chicago, I'd like to be at an intersection. I want great ingress and egress. We need great parking. We need great signage. We like to be near other traffic drivers.

We will ultimately be a massive traffic driver to a power center or a mall, whatever you have. But in the near term, we want to be near other great traffic drivers, right? So like when you think about the state of Texas, we tend to – we have sites that are really close to an H-E-B, those of you who know the state. We are really close to Buc-ee's, which is amazing. We're – we pick sites that are close to other traffic drivers so that as we're building, people are finding us without having to hunt us down. That takes time.

When we map out a market, we map out Dallas-Fort Worth. We're looking at what full potential looks like. And I've said this publicly multiple times. We think Dallas could be 16 to 20 restaurants for us. But we've mapped out where we want to be, and then we don't hit go until we know we have five or six locations locked in because then we want to achieve scale as quickly as possible.

And then we believe that given the traffic that we drive to centers, we should be at worst, paying market rates. In general, we should be better than market on rents because we're a traffic driver. So we feel really good about that.

And then the other constraint for us is on growth. We try to be very methodical about having a general manager identified for our restaurants well in advance, right? Portillo's at our volumes is a really unique piece. And what we find is that a general manager who has not experienced a $6,000 hour kind of – it's a real shock to the system when the first time you're doing that.

And in a lot of concepts, if you have five, six, seven, eight people working, the general manager can fix things by rolling up their sleeves and getting involved. At a busy Portillo's, you have 20, 25 people working. The general manager rolling up their sleeves doesn't help. They need to coach and lead. So it's a slightly different skill set.

So we have – we're very proud of building a bench and a pipeline, having the training programs in place so that now Michelle and I can say, for the class of 2024, we know every single general manager that's going in. For the class of 2025, we know every single general manager who's going in, and they're experienced Portillo's GMs.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Terrific. Given the importance of sort of that new store performance to the broader growth story, maybe you could talk about new opens over the last couple of years and how those have performed.

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

A

Yeah. I've been very public about a couple, right? So we opened in Orlando. And if you think about it, Orlando is not like – it's not a huge ex – Chicago expat population. It is more of a tourist location. But that restaurant opened, and it performed exceptionally well the first year. It did $10 million-plus in its first year, and that's with managing volume.

So we actually tamped down demand. We did not have third-party delivery open. We did not have catering. We did not have any off-premises, just dine-in and drive-thru open in Orlando for the first year. We wanted that restaurant to get its legs under it to have a good experience. And so Orlando opened exceptionally well.

We – early on, we knew there was going to be a lot of demand for that restaurant. We did a number of things to sort of take some of the pressure off of the grand opening, right? We had friends and family invited. We had people who signed up for our loyalty program. We had them come visit. We did first responders. We did the local mayor, shook hands, kiss babies, that kind of stuff.

So we took a lot of pressure off before we actually opened so that when the restaurant opens, the team is ready, the restaurant can perform. It can come out of the gate strong, and it can then have really good experiences for our guests.

We've seen the flattest curve in recent openings. That restaurant dipped a little bit and is right back up to sort of gaudy numbers by year three. We did turn on off-premises channels in year two and year three. We think that is the right paradigm for when we go into a new market and first to open.

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

A

I'd also just add, Dennis, one of the proof points we put out there for the class of 2022. So there were seven restaurants in that class. And when we did our Development Day deck back in September, we snapshot of that class and said in year one, it's – it was on pace at that point to average 8 million AUVs and 22% margins.

Now keep in mind, when we talk about a class of restaurants, like year one, you're targeting high-teens margins, right? And so looking at that class and saying the performance in year one was already above that, we felt really good about the performance of that class.

Dennis Geiger
Analyst, UBS Securities LLC

Q

That's terrific. Another one that I think we still get questions on even with the strong results that we've seen from these new stores in new states, new markets in recent years, just thinking about the portability of the brand and then sort of which markets you're targeting. But that portability, you talked about the Net Promoter Score, but just how you think about portability and what gives you – what has given you this confidence in the portability?

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

A

I think the numbers are sort of undeniable, right? There's not enough ex Chicago into Orlando to do $10 million. I publicly said that the first restaurant in Dallas did 13 million in its first 12 months. There aren't enough ex Chicago to do $13 million. You don't do those volumes without becoming part of a routine of locals. And we work really hard to do that.

Like our entire marketing support is designed to make – that Orlando restaurant, it's not a Chicago restaurant. It is Chicago food in an Orlando restaurant. We don't want to be carpet baggers going to Florida or Texas. We want to feel like a local restaurant company.

And so I think the numbers themselves say, you're not doing those volumes, you're not getting that kind of traffic without it becoming part of the local fabric.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Great.

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

A

It is a question everyone asked, and it's one of the great debate points. At some point, it will be so proven that we'll be past it.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Certainly well on your way without a doubt. I want to talk about new build costs and obviously, there's been some work that you've been doing. You've talked about that. Maybe if we talk about new build costs historically versus currently and sort of at the end of the day, what that means for new store returns. I think you've had a 25% [ph] store (00:24:47) return historically, looking to bump that a bit going forward, if we could touch upon that a little bit.

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

A

Yeah. Go ahead.

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

Yeah. When you look at – when I mentioned the class of 2022, right, that average build cost for that class was at $7 million. So what we're building today and what we built in the class of 2023 and what we're currently building in the class of 2024 is $6.2 million to $6.5 million build costs.

One of the things that we've been working on over the last 18 months is a new prototype that we're calling Restaurant of the Future. We believe that that restaurant can shave another $1 million off the build cost, so bring it down to $5.2 million to $5.5 million.

And to your point, Dennis, old targets 25% cash-on-cash returns with the assumption that we get the build cost down, that would bolster the returns closer to 28% cash-on-cash returns. And we will build our first Restaurant of the Future in Willowbrook, Texas, which is a suburb in Houston in Q4 of this year.

So every build starting with Willowbrook and beyond will be in the new Restaurant of the Future prototype. It's in for permitting right now. We're getting the construction cost and all that in, but that's what we believe that can do to the build costs alone.

We haven't even talked about or included within the modeling in those return numbers any other additional benefits we believe are out there in terms of labor efficiencies, et cetera, in the restaurants. So from that standpoint, I'd say we're probably more conservative in terms of the estimates there. But those are things that we still have to understand and prove out as this restaurant gets built, and we operate it. But we feel really good about where we sit today.

And look, we're already working on Restaurant of the Future 2.0 and what that looks like. And just to level set everyone, these new restaurants, so today, we're building 70, 100 square foot restaurants. So a new Restaurant of the Future is closer to 6,000 square feet. And we're not giving up the ability to do the volume, right? It's still going to be able to do $10-plus million. And so I don't want anyone to think, hey, you're shrinking the box, and you're not going to be able to do those volumes. That's not going to be the case. And so we feel good about that and our ability to continue to perform at the volumes that you see.

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

Can I just add one thing to what Michelle said because Michelle is co-leading this project with our Head of Marketing. But there – we created a nice constructive tension with operations, right? They hired world-class partners to help us with this, people who've done this for other restaurant concepts.

We've done time motion studies. We've seen how many people sit in our dining rooms at different times. There's a lot of analytics behind what they've done. But when push came to shove, the operators – I look at [ph] our operator in the eye, I said (00:27:30), can you do $10 million in this? But it's not like, yeah, I can. It's – which means $200,000 a week, which means you need to do $40,000 on Friday, which means you have $6,000 hours at 11:00, noon and 1:00. Can you do a $6,000 hour in this space?

And we map out the kitchen. We have an innovation center where we have the kitchen laid out. And in the first iteration, the operator is like, yeah, there's no chance. This isn't enough space. And the consultants say, well, no, that's 26 inches is enough for two people to work. Like that's not normal human being anymore. I need more space.

And so it's been iterative to get to a kitchen with these many beef wells and these many fryers for that and so on to then the operator say, yes, in this space, we can do $6,000 an hour. And then that's how you get to, did you capacity constrain yourself? Did you cut off your nose despite your faith? And we're pretty confident that we didn't.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Great. Very exciting opportunity. I wanted to just touch on the new pickup and delivery-only location. And Michael, you spoke to it some. But just how are you thinking about the potential for more of those over time, where and ultimately, what that opportunity looks like perhaps?

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

A

Look, we love it. It's a fraction of the cost of a regular restaurant and a bigger fraction of a regular restaurant in terms of revenue. So that means the cash-on-cash returns, all of the other numbers look really good. So we love it.

I especially love it as an infill strategy right now in a market that is full. So in Chicagoland, like you're pretty much within 12 to 15 minutes of a Portillo's wherever you are. I'd like it to be 10 to 12 minutes. And I think there's an infill strategy. It's like the super fortressing strategy that some other concepts do. So I think it's a brilliant infill strategy, and that's how we see that it works really well.

The first one we built, honestly, Dennis, was to take pressure off of a restaurant that it was at capacity and to take pressure off their drive-thru. That was literally the only reason we did this. And now we're seeing, wow, there's a lot of incrementality here. It's filling in and it's – the uplift is really good.

So I think you can think of this as a great infill strategy once you've achieved a certain level of density and maturity in a market. So Chicago, this is a no-brainer. And then you can imagine in other markets as we achieve density and penetration, then you continue to infill with pickups.

Dennis Geiger
Analyst, UBS Securities LLC

Q

That's great. Mike, I want to touch on omni-channel, and you spoke to this some in your prepared remarks. Just as far as the core advantages that the omni-channel approach has, where you've got a pretty balanced business across those channels. What that does for the brand, the opportunity from here across all of those channels, if you could touch on that a little bit?

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

A

Yeah. Perversely, I would say the best example is the COVID year. So being omni-channel during COVID when dining rooms were shut down, we were down 8% on comp, up 8% on adjusted EBITDA. We're down 8%. That's it, because we're a very easy – very quick and effective in pivoting to all of our off-premise channels, where before we might have had two people taking orders outside, two people running food, we went to four, five outside order takers, four, five running food.

I don't know what kind of bizarre black swan event happens. But so I love the idea of being flexible and agile. And so that's one element. If QSR gets crazy promotional, that has an impact on our drive-thrus because that's the –

QSR customer is essentially drive-thru customer, but it actually benefits our dining rooms because in our dining rooms, we tend to compete against a sit-down occasion, casual dining, high-quality, fast casual.

So I think that it sort of insulates us from massive swings on comp. They protect us. And then some of those channels like, look, I'm not sure I understand the pricing sensitivity of the third-party delivery channel. We're taking it – it's growing. It continues to be robust for us. Let's – we'll jump on that gravy train for as long as it works.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Absolutely. I want to touch on customer satisfaction metrics and some of the key metrics, if you could touch on sort of where those are and what that tells you about the brand and how the brand is positioned right now.

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

A

Yeah. By and large, I'd tell you I feel really good about it. I mean as a matter of fact, we are at five-year highs in overall satisfaction score on every one of our channels right now. Now I can tell you that with one hand and tell you that we're a little slower in the drive-thru than we were five years ago, and that upsets me.

So I think that guest satisfaction is really, really important. I believe it tends to be a leading indicator in our business. If you think about why all of you go to a restaurant and the last time you went to that restaurant, I'm going to guess that the number one reason is you had a good experience. You said I had a really good experience. That's why I went back. So that's a great metric.

But there's an – there's still opportunities for us to be better. And so I'm vexed that we got slower in the drive-thru, and I intend to claw back some of that time.

Dennis Geiger
Analyst, UBS Securities LLC

Q

How about as it relates – speaking of that, I guess, to the operational improvements, and you kind of both have touched on this a little bit. But what are sort of some of the biggest opportunities from here? And as – Michael, as you talked about maybe throughput and speed, how we think about that or how you think about that opportunity?

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

A

I think operational improvement in this business is a – it's a never-ending journey, right? Like you can always get better. And there's a combination of technological improvements and – that enable you to become more efficient and improve. Like the operational metrics that I care about the most is probably items per labor hour. How much are we producing in a given labor hour? And we did a lot to make that easier, right? So we use machine-cut tomatoes and onions.

I get perfect, beautiful red onions, machine-sliced, vacuum-sealed. Now you pay a tiny bit more on cost of sales, but I get less waste, less yield loss. I don't have as many prep hours. I don't create some – I don't make some poor person like put on a cut glove, sharpen knives, spend hours cutting onions. And by the way, those onions are great the first hour, and they start to deteriorate over time. So that you always have fresh, perfect onions. You've eliminated the prep time, and there's a little bit of arbitrage there.

So I think we need to be smart and continue to do things like that. We need to use technology and machines where it doesn't negatively affect the guest experience, but it makes our teams more efficient.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Great. You talked on technology. I want to maybe shift over to digital and how you think about growing that digital business in 2024 and sort of maybe what are some of the key initiatives to further enhance digital engagement with your customer base?

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

A

I think – so I think digital, in some ways, is a little bit of a red herring conversation. And here's what I mean by that. Most people who talk about digital, it's satisfying an off-premise need, right? Because that – people say, well, I like digital because I don't want to go sit in your restaurant and eat. I want to use a different way.

So like it's less relevant for people with a robust drive-thru because that's like if you want our food in an off-premise setting, the drive-thru is phenomenal, okay? And so we still do just purely digital app based. I think it's over 20% of sales.

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

A

Yeah, it's around 22%.

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

A

So we feel good about that. Obviously, what we want to do is be as frictionless of an environment for a customer as possible. So Dennis, if you're a guy who's like, no, I only order on an app, I just want to do pick up on an app, that's it. No problem. We have totally enabled that.

And so I want to make it a frictionless environment for any guest for however they want. And then we are selectively looking at ways of being better, smarter, faster. So we are testing QR code ordering in a couple of restaurants.

You're sitting, you've come in with a group of like two families with six kids. It's mayhem. You don't want to try to go order. There's a QR code, you can QR order, and we'll actually call your number. You don't have to get up out of your table. We're testing that.

We are testing other sort of things that best-in-class companies are doing to figure out what's right for our brand. The balancing act is we still believe that it's important to be an experiential brand and have value-added human interaction, but we're also going to be very, very responsive to our guests and what they want.

Dennis Geiger
Analyst, UBS Securities LLC

Q

That's terrific. I want to touch on value. You showed really attractive price points, especially for the size and the quality that you're getting versus some of your competitors. So I want to talk a little more about how you think about value for the brand. And even to some extent as you talk about drive-thru and the environment that we're in, that maybe is getting a bit more promotional, what that means for the brand and for strategy potentially?

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

A

I think somebody else asked me this question. I think that pricing to cover up ills in your P&L is not a good idea. That's a mark of weakness. And so I think value – a lot of people conflate value with price. Value is quality, quantity, experience and price.

And so I think playing offense, if you're providing great quality, which we are, we have not like rightsized our commodities or done any of that nonsense. We have actually improved the quality of some of our ingredients. We serve the best commercially available bacon in the world. If you haven't had a bacon burger at Portillo's, go try. Don't sleep on our bacon burger. So we're very proud of the quality of what we do.

We have not played any games with quantity. You get the same number of fries in a Portillo's, small or large fry as you did five years ago, four, three, two, one. We – our burgers are a third of a pound. They've always been a third of a pound. Our beef sandwiches are ridiculously heavy with beef. They've always – so we're not playing any of those games. We work really hard on our experience. We hope people have a great experience.

On top of that, our price points are really low. So – but I think it's reasonable to tell consumers that as I increase value, my price should go up a little bit. And so I think we need to be thoughtful about a value proposition that makes sense, that is accretive to the business and does not negatively impact the consumer.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Right. I want to shift over to thinking about some of the comp trends and maybe competition at least at a high level. And maybe as we think about traffic as well as mix this year, Michelle, anything to kind of – that investors should be thinking about on those two components of the comp for this year?

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

A

Yeah. For this year, Michael showed our long-term growth algorithm. And I had the question, I think, Dennis, at our Q4 call is do we think that we can achieve that this year from a comp standpoint, low-single digits with a "choppy first quarter", right, which you see in the industry. And my answer is yeah, I think that's achievable this year. I think that's achievable over the long term.

But when you think about the comp as whether it's this year as we move forward, think about it in two different buckets, right? You have the Chicagoland restaurants, right? There are generally 40 restaurants. That's going to be a good chunk of what's in your comp base today, right?

And then you have the other outer market restaurants that are – we'll talk about those dynamics in a minute. So you talk about the Chicagoland restaurants, where generally in that market, you have a shrinking population base, right? And so to take – to have traffic growth in that market, you're going to have to take share, right?

And so we think we have a very strong brand. Do we think we can do that? The answer is yes. We think we can do that. But I think you'd see more of that being more of a challenge in that market. And our ability, to Michael's point, we still have pricing power. So the ability to grow ticket, whether it's through pricing or add-ons to the ticket, we think is there in Chicagoland, right?

Outside, it's a little bit of a different dynamic when you think about those high-growth markets in the Sun Belt. I think there's more ability for traffic growth because you just have those natural comp tailwinds with the population growth in those Sun Belt markets, and we still have pricing power in those markets.

So I think that when those restaurants begin to come into the comp base, there is potential. And Michael and I talk about this all the time. We want to put out targets that we think are achievable, right, not some pie in the sky targets. But do I think over the long term, we have the ability to outperform it as those come into the comp base? I think the answer to that is yes. But we have to continue to get those restaurants into the comp base, get scaled quickly so that that starts to mature. But that's how I think about the comp, not just in the short term, but over the long term.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Right. Terrific. That's very helpful. I want to touch on marketing and the company's approach to marketing, particularly as we think about what that means for the longer-term strategy. You saw some good success recently in Chicago. So what did that tell you and maybe what -might that mean for the future?

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

A

I think it's a great question, and it's on people's minds. So it certainly – we felt really good about the marketing. The creative was brilliant, highly efficient, right? We didn't use an outside agency. We did it ourselves. Almost every penny that we spent went into media buy. And so highly efficient because of that.

And it – I always think the marketing guys are going to tell you how well it [ph] performed, so you (00:41:14) got to measure that a little. But it – no matter what they say, it obviously performed well. I think it's an important arrow in our quiver, and it is something that we should use as appropriate.

I think the best marketing – I learned this from another marketing officer. He said the best marketing in a restaurant company is great operations, right? Again, when you go to a restaurant and you have a great experience, you're going to go back. And so I think focusing on great operations and value as being the driver of frequency is a really solid strategy.

There might be times when you want to get out of a doldrum, when you want to like juice up the business just a hair, I think that makes sense. Getting hooked on marketing is a dangerous tack because once you're hooked on it, you have to do it. And then it's no longer a tool, then it's like something that you're reliant on.

Dennis Geiger
Analyst, UBS Securities LLC

Q

Yeah. Makes sense. I want to shift over to margins. And I think, Michael, you touched on this. Michelle, you kind of talked about Chicago and non-Chicago from a sales perspective to some extent. Lots of questions from investors about the longer-term margin trajectory and ultimately, that dynamic of kind of Chicago versus non- and some of that structural impact going forward. So anything for investors to think about on kind of that longer-term restaurant margin trajectory?

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

A

Yeah. I think over the long term, we expect to be what you see today, right, which is that mid-20% margins. And so obviously, I said to you before, Dennis, when restaurants over the first couple of years, the trajectory is going to be high teens, and then they get to that 22% margin in year three.

But it doesn't stop there. It's not all of a sudden when you hit 22%, wow, [indiscernible] (00:42:59). No, that's not the case. And can you get there quicker? I think the answer is yes. And it's the reason why we're building scale as quickly as possible.

And Michael mentioned us getting to five restaurants in the DFW market over the span of [ph] our (00:43:14) past 14 months is important because we know there's scale advantages to margin. And it's not just a cost advantage to margin. The scale doesn't just benefit your cost structure, but it also benefits frequency.

So as we get more restaurants in a market, we start to get in the decision set of consumers, where Portillo's becomes not just that destination restaurant, but it becomes just part of whether it's called QSR, fast casual, but it gets into your routine. And so you start to build that frequency. And that has margin benefit as you continue to grow that top line.

So that's the way that we're viewing the world as we move forward. But I think from a margin standpoint, even when we look at this year, we don't expect margins to degrade 100 basis points, right? We're still expected to be within that, call it, 23%, 24% range this year.

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

We're really proud of the fact, Dennis, that last year, on a base of 72 restaurants, we opened 12 new restaurants and we improved restaurant-level margins by 170 basis points, right? Because those 12 are not margin accretive out of the gate. And so we think that that speaks volumes of what we can accomplish.

Dennis Geiger Q
Analyst, UBS Securities LLC

Great. I want to get one more in while we have time. Just as it relates to the compelling growth algorithm that you spoke to, off of, again, a current snapshot of already really gaudy and impressive numbers. As we think about that kind of mid-teens growth, Michelle, and then the low teens EBITDA growth, can we just talk about a little more what's sort of baked into that low teens EBITDA growth, some of the moving pieces within that over the longer term?

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

Yeah. I think when you think about G&A, and this is something that I even mentioned earlier in the week, right now, we're targeting 75% of the revenue growth, right, is the current target for G&A growth. And so our goal is to get that down to 50% of the revenue growth over, call it, the next three to five years, Dennis. It's not going to be immediate, right? But I think we'll start to stair step that down.

And as Michael and I look at our ability to lever that line, I think that provides some of the upside that we can see in the long-term growth algorithm when you talk about that adjusted EBITDA growth being in the low teens versus getting it up more into the mid-teens.

Dennis Geiger

Analyst, UBS Securities LLC

That's great. Well, we're out of time. So Michael, Michelle, Barbara, thank you so much for your time, sharing these insights. We really appreciate it.

Michael Osanloo

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

Thank you, Dennis.

Michelle Hook

Chief Financial Officer, Portillo's, Inc.

Great. Thanks, Dennis.

Dennis Geiger

Analyst, UBS Securities LLC

Thank you.