

Follow The Smart Money Investing In The Restaurant Industry

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About: [USCF Restaurant Leaders ETF \(MENU\)](#), Includes: [FXD](#), [VCR](#), [XLY](#)



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Summary

- Why is so much smart money invested in the restaurant industry?
- The importance of the group as a window into the consumer and GDP.
- Outlook for growth in the industry.

Why is so much smart money invested in the restaurant industry? The importance of the group as a window into the consumer and GDP Outlook for growth in the industry.

Follow the smart money invested in consumer spending

Investors looking to capitalize on important trends or growth in consumer spending should consider an investment in the USCF Restaurant Leaders ETF (NYSEARCA:[MENU](#)). MENU was designed to track the Quick Serve Restaurant ((NYSE:[QSR](#))) Category. An investment in MENU is appropriate as a small-mid cap growth allocation, and can make sense for tactical investors, core-satellite investors or simply people who like investing in strong brands.

U.S. Commodities LLC, as USCF Advisers, is the sponsor of the USCF Restaurant Leaders ETF . U.S. Commodities LLC, with nearly \$5 billion in assets under management (AUM), is best known for its United States Oil Fund (NYSEARCA:[USO](#)), which helped provide investors with the access they sought to the commodities space. U.S. Commodities is once again

addressing access to an important and growing category. The ETF structure of MENU, however, is very different than USO and it is expected that the tracking error in this ETF will be tight. MENU is benchmarked off of the restaurant Leaders INDXX Index, which is owned by Access ETF Solutions LLC, which in turn is owned by Dan Weiskopf, a prominent ETF Strategist.

The Quick Service Restaurant Category grew approximately 5% in 2016, and is expected to grow at about the same rate in 2017 according to Fitch. According to the National Restaurant Association, the industry has added \$200 billion in revenue since 2006 reaching \$780 billion today.

This is an interesting time for the industry because of both the secular trends of re-franchising, the adoption of technologies that are taking place, and the resulting outperformance that these stocks, especially in the Quick Service Restaurant Category, have been experiencing.

The chart below shows a ten-year history of the MENU index (in white). It is presented along with the S&P 500 (SPX) (in orange) and the Russell 2000 Growth (NYSEARCA:IWO) (in yellow) indices. Over the ten years, MENU has provided nearly double the annualized performance of its benchmarks.



More recently, as shown below in a one-year (January 4, 2016 through January 3, 2017) chart, MENU, after consolidating for two years, broke out with the Trump victory to new all time highs.



Over the past six years, various companies in the fragmented restaurant industry have moved away from the business of managing restaurants and into the business of brand building and franchising. The industry calls this "refranchising." Companies like Yum Brands ([YUM/YUMC](#)), Burger King ([QSR](#)), McDonalds ([NYSE:MCD](#)) and Jack in the Box ([NASDAQ:JACK](#)) have set out to be royalty driven companies with 80-90% of their stores franchised. As a result, these companies have recreated themselves as growth companies with predictable strong margins, high cash flow and low capital expenditures.

The trend towards refranchising has been driven by hedge funds, private equity and family offices. Arguably, the first major investment of note was 3G and Warren Buffett's investment in [Burger King](#). Activists have had great success in working with managements to upgrade the business model and create shareholder value. For example, Keith Meinster was active in Yum Brands [YUM/YUMC](#); Nelson Peltz in Wendy's ([NYSE:WEN](#)); and while it too early to say what will happen with Bill Ackman's position in Chipotle ([NYSE:CMG](#)) he has enjoyed a great run with Burger King as one of his largest positions. Other noteworthy firms that are playing activist roles

include Mick McGuire of [Marcato Capital in Buffalo Wild](#) (NASDAQ:BWLD), Jeffrey Smith of [Value Act in Darden](#) (NYSE:DRI), and Tom Sandell of [Sandell Asset Management](#) in Bob Evans (NASDAQ:BOBE).

[Roark Capital](#) is perhaps the private equity firm with the greatest focus on the sector, with an investment pool of about \$9 billion dedicated to consumer product companies. JAB Holdings, another aggressive PE firm dedicated to the space has stakes in Keurig Green Mountain (NASDAQ:GMCR), Peet's Coffee and Noah-Einstein Bagels. JAB Holdings has recently also acquired Krispy Kreme. [JAB's](#) describes itself as a "privately held group focused on long term investments in companies with premium brands, attractive growth and strong margin dynamics." Anyone interested in the space and MENU should take a look at the websites of Roark Capital and JAB Holdings as they further highlight the thesis that active investors have towards the group.

The Franchise Times recently reported on the industry's fragmentation and trend towards re-franchising, stating that in 2015, revenues for the largest top 10 operators increased by more than 14.2% or \$1 billion to \$8.6 billion, which is a very healthy 44% increase since 2012. The Franchise Times also reported that since 2009, unit locations by the top 200 firms has increased from 8,300 to more than 25,000. Both sets of figures demonstrate that the largest firms continue to grow quickly and gain market share. Franchisors are getting out of the operating side of the business, and strong operators led by PE firms have supported the trend as buyers. This trend is common in fragmented industries where rollups occur by strong operators who can benefit by scale.

The industry's growth has taken place even in the face of some difficult issues that have caused some indigestion. Specially, during the past 12-18 months, there have been concerns about a federally mandated minimum wage; excessive regulations; and excessive unit growth. This is what may have led both Roark and [Oak Hill](#) to decide to successfully cash out of

WingStop (NASDAQ:[WING](#)) and Dave and Busters (NASDAQ:[PLAY](#)). In addition, Whitney Tilson recently announced a large short on WING.

What's Ahead for the group?

The trend in dual income households will likely continue to drive restaurant growth. Quick Serve Restaurants provide a clear value proposition for those who need a convenient way to feed their family. The long-term trend of the dining out experience by the 80 million U.S. Millennials (those born between 1984 and 2000) is expected to continue until the group matures. And the Quick Serve Restaurant Category is best positioned to evolve and deliver added value to meet the needs of this target market. There will be winners and losers in this group and getting the offering right presents many challenges. Therefore, an index approach makes the most sense.

President elect Trump is supportive of small business, wants to simplify and lower taxes, reduce regulation, and provide other economic stimuli. This should help address some of the issues that are a concern to the industry. If one believes that U.S. growth in general, and consumer growth specifically, will accelerate, the companies within MENU should be strong beneficiaries.

The importance of the group as a window into the consumer

Investors looking to invest in broad U.S. consumer discretionary ETFs such as the Consumer Discretionary Select Sector SPDR ETF (XLY), Vanguard Consumer Discretionary ETF (VCR), and First Trust Consumer Discretionary AlphaDEX ETF (NYSEARCA:[FXD](#)) should look at MENU because broad ETFs only provide a 10% weighting towards restaurants, while holding an approximately 12% position in just Amazon (NASDAQ:[AMZN](#)).

As the chart below shows, over the past four years, MENU (IMENU = MENU) (in white) has meaningfully outperformed the Russell 2000 (RU20INTR = IWM) (in orange) and the Consumer Discretionary ETF (IXYTR = XLY) (in yellow) even with XLY's 12% weighting in Amazon, which has tripled during this time.



Moreover, in addition to being a potentially attractive investment, MENU is worth keeping on one's screen because it provides valuable insight on the U.S. consumer, particularly as to consumer confidence, employment and GDP growth.

MENU's focus on the Quick Service Restaurant Category represents 4% of GDP, and ancillary services and products make up an additional approximately 8% of GDP. Restaurants directly provide about 10% of the U.S. employment; and 50 million people visit a restaurant every day.

Consumer discretionary stocks can serve as a leading indicator as their performance is tied to consumer spending which tends to increase in expansionary period.

Summary

MENU, with its emphasis on QSR growth and ongoing catalysts by "smart money" investors, provides a play on the growth of many successful U.S. consumer brands. It also provides an attractive alternative allocation to the consumer discretionary ETFs (XLY, VCR and FDX) and can even serve as a broad allocation to small-mid cap ETFs (like the iShares Russell 2000 ETF (IWM) and iShares Russell 2000 Growth ETF (IWO)).

Furthermore, investors looking for insights into the consumer should pay attention to MENU.

Disclosure

I/we have no positions in any stocks mentioned, and no plans to initiate any positions within the next 72 hours.

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