THE TREND REPORT

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NOT QUITE A FULL-SERVICE DINING EXPERIENCE, but a step above typical fast food, the quick service restaurant (QSR) has filled a critical niche for consumers who seek a reasonably priced meal out or to take home. The concept especially appealed to younger consumers and time-pressed families, who prize experiences over merchandise.

But just as retail real estate faced a crisis during the Covid-19 pandemic, so, too did the QSR industry. Minimizing face-to-face contact became critical, as did establishing outdoor eating locations and arranging spaces for pick-ups rather than dining in. The industry was forced to innovate — and now, four years later, many of the new technologies and strategies that resulted have become part of a new normal.

From in-store kiosks, apps, contactless deliveries and a growing reliance on drive-throughs, the look of QSR has changed, and real estate operators must accommodate them.

Yet even in this new normal, more challenges remain. Even more advanced technology will be utilized that will remake the facility, the restaurants' relationship with their customers and its real estate needs.

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DANIEL SPIEGEL
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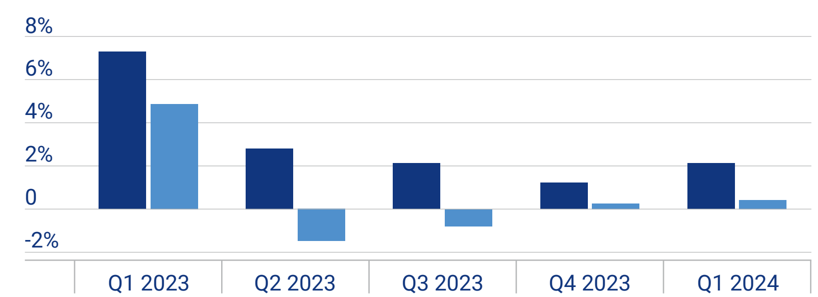
REINVENTING THE RESTAURANT

Amid Changing Consumer Trends

CLEARLY, PEOPLE STILL WANT TO EAT OUT, or eat takeout. In fact, in 2022, Americans spent more money at restaurants than in grocery stores[1]. That trend appears to be continuing. In addition, the faster and more affordable quick service sector is seeing more growth than full-service restaurants.

Fast-Casual & QSR Chains See Strong Visit Performance Compared to Full-Service Dining Chains

Year-over-Year Comparison



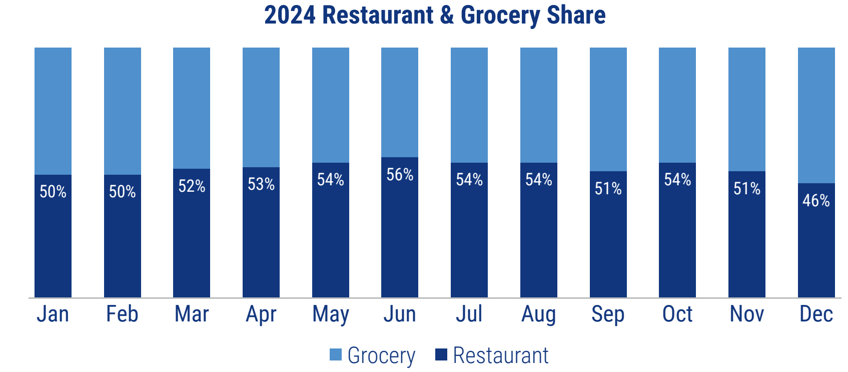
The United States Quick Service Restaurants Market size is estimated at $406.17 billion in 2024 and is expected to reach $662.53 billion by 2029, growing at a CAGR of 10.28% during the forecast period (2024-2029), according to Mordor Intelligence.

But the QSR experience is changing, both behind the scenes and in these eateries' customer relationships. The innovations introduced during the pandemic to minimize human contact have remained and even increased. These include apps to order in advance for pickup, dedicated areas to fulfill mobile orders and contactless delivery.

The industry also has continued to face challenges, including rising prices for materials and labor, albeit at a slower pace than in 2023. The latter, in particular, could face continued inflation if higher minimum wages continue to be mandated. It also must satisfy a younger and more demanding consumer, who wants experiences that are more personalized, more sustainable and more ethical.

To remain viable, restaurants will want to utilize technology, artificial intelligence and more to make their operations more efficient (which may even lead to the point of reducing or eliminating human employees, as is happening in test locations), possibly reduce or reconfigure their footprints and become more sophisticated in their dealings with the customer. This will have a profound impact on this sector's real estate needs and footprint.

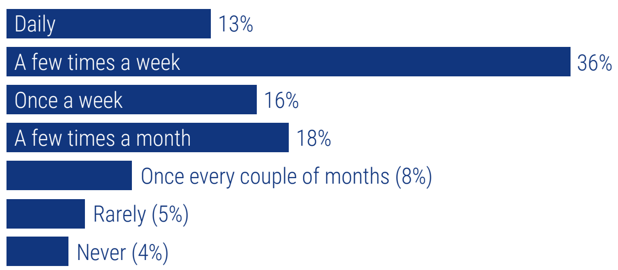
2024 Restaurant & Grocery Share



The CUSTOMERS

How Often People Eat Fast Food

2 in 3 people eat fast food at least once a week (65%)



THE TRUTH IS CLEAR: U.S. diners continue to eat out, especially if they can do so affordably. In a recent survey, two in three people (65%) reported they eat fast food at least once a week[2].

Last year, Deloitte reported that 55% of customers it surveyed said that their in-person dining was actually the same as or higher than before the pandemic, with 69% saying that they got takeout or delivery at the same rate or more frequently than pre-pandemic[3].

Why? For most, it's a matter of value. Grocery prices have risen, making restaurant visits affordable for some in comparison. For those on a budget, inflationary concerns are leading some to downscale from sit-down restaurants. And return-to-office mandates should lead to increased business during the day at urban locations.

But today's customer has very different requirements from even a few years ago. According to AlphaSense[4], they seek:

Authenticity: Guests today want to establish a relationship with the restaurant. It must have a strong brand identity, and really become more of a lifestyle rather than just a place to eat.

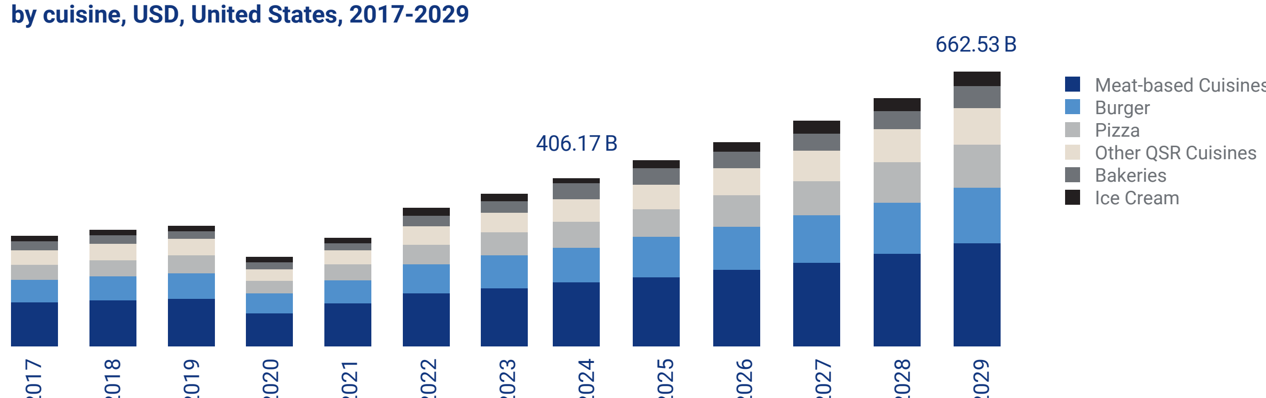
Sustainability: They want ingredients that are locally sourced and technology to be used to reduce waste and save energy, as well as recycling measures. More than half of diners (57%) say restaurant sustainability practices are "somewhat influencing" their choices when eating away from home[5].

A Focus on Wellness/Healthier Foods: Gen Z, in particular, is seeking healthier alternatives such as fresh foods prepared on site, utilizing ingredients that are more sustainable, more plant-based and with greater nutritional transparency. Beef is less important to this generation — Burger King introduced the plant-based Impossible Whopper and saw a huge foot traffic increase[6].

Customization and Customized Dishes: More than four in five (81%) of Gen Z shoppers are pleased when brands allow them to customize their products[7]. There also is a greater awareness of special diets and allergies.

Now, a new set of QSR restaurants that fulfill these needs are coming into the industry and looking for space.

Value of Quick Service Restaurants Food Service Market by cuisine, USD, United States, 2017-2029



Source: Mordor Intelligence

An Explosion of NEW CONCEPTS

RECENT YEARS have seen an explosion of new concepts for multiple reasons.

Customers are more aware of health post-pandemic and are seeking different new concepts; there has been a huge boost in Mediterranean eateries. Cava Grill is projecting 15% annual growth with a goal of 1,000 restaurants by 2032. Luna Grill Mediterranean Kitchen continues to expand in Texas and California, reports *QSR Magazine*.

Diners also are seeking new flavors and tastes, and are insisting that allergies and special diets be accommodated. Examples include The Halal Guys began as a food truck and is now expanding its Middle Eastern food into QSR eateries around the country. Jinya Ramen Bar offers ramen noodles and rice bowls and is expanding around the country. Vitality Bowls was founded by an entrepreneur looking to accommodate her daughter's allergies.

An interesting hybrid is Wonder Delivery, a restaurant delivery and takeout concept that works with well-known chefs including Bobby Flay and Jose Andres in New York City and its suburbs. Launched in 2021 in vans, Wonder Delivery now has multiple brick-and-mortar locations.

More traditional food categories continue to expand as well. Coffee chain Dutch Bros has quietly become one of the largest small store companies in the United States, reports CoStar, ranking fourth last year behind Wingstop, Starbucks and Yum! Brands among chains leasing spaces of 2,500 square feet or less[8].

Founded in 2017, Crumbl Cookies opened its 1,000th unit in February 2024, noted *QSR Magazine*. Papa John's is once again expanding, it announced in March[9]; Wendy's has hundreds of stores in development, *QSR* says; and Yum Brands' The Habit Burger Grill grew its store count from 349 units in 2022 to 378 locations in 2023[10].

All, however, face operational challenges that are forcing them to remake how they configure their stores.

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Recovery Brings NEW CHALLENGES

INFLATION MAY BE EASING and supply chains improving, but the aftereffects of the pandemic continue. The result is a more expensive operation in a highly competitive environment.

Some challenges are easing — staffing levels in the quick service and fast casual segments were 140,000 jobs (3%) above pre-pandemic levels as of February 2024[11].

But expenses are up. The National Restaurant Association reported that 88% of operators say their total food costs (as a percent of sales) are higher than they were in 2019, prior to the pandemic[12]. Labor wages are also increasing. On January 1, 22 states increased their minimum wages, resulting in pay increases for 9.9 million workers. In addition, 38 cities and counties increased their minimum wages above their state's minimums[13]. The results are higher costs for restaurant management — and a need to increase efficiency.

Restaurant Brands International saw multiple Burger King and Popeye's franchise operators file for bankruptcy in 2023. Smaller companies have shuttered units as well. As of April 2024, a search of Crexi revealed nearly 290,000 spaces are available for lease, with a median of 168 days on the market.

At the same time, there is a generational shift in ownership, as Baby Boomer franchise owners may be looking to retire and sell. Crexi reports nearly 2,800 QSR properties for sale with a median asking price of $1.88 million, again as of an early April 2024 search. Given the rise in construction costs, these also provide an opportunity to be converted into the newer formats that are currently expanding.

Transactions remain challenged due to higher interest rates and tighter capital requirements, reports advisory firm Kroll. During calendar year 2023, 271 deals were announced in the entire food and beverage space, 39 fewer than the year before[15].

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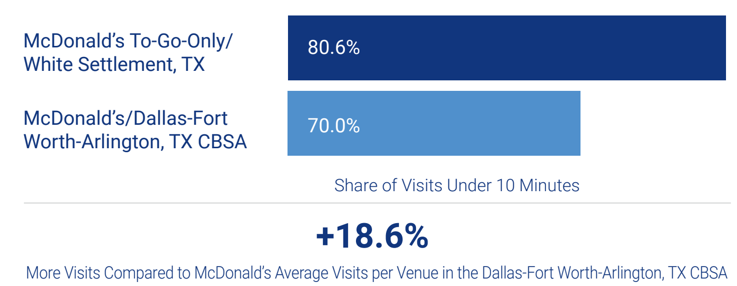
TECHNOLOGY: The Answer and the Challenge

TECHNOLOGY ALLOWED RESTAURANTS to get through pandemic lockdowns. Now it will help QSRs reinvent themselves at a time when the bottom line is challenged.

Automation: Replaces some human labor tasks, including order taking and delivery. The result is smaller stores with very small front of house, and much more space devoted to technology in the back. An example is the Fort Worth, Texas digital-only McDonald's, which has become its only takeout-only restaurant and sees shorter and more visits[16]. In addition, Sweetgreen has acquired a robotic food prep company.

McDonald's To-Go-Only Location Seeing Shorter Visits and More Visits
Q1 2024 Visits



AI: Used to create more seamless experiences with shoppers, beginning with ordering. In May 2023, Wendy's announced a partnership with Google Cloud to pilot Wendy's FreshAI, designed to reinvent the drive-thru food ordering experience with Google Cloud's generative AI and large language models (LLMs) technology. This will allow diners to customize orders just as they can inside the restaurant.

"Google Cloud's generative AI technology creates a huge opportunity for us to deliver a truly differentiated, faster and frictionless experience for our customers, and allows our employees to continue focusing on making great food and building relationships with fans that keep them coming back time and again," said Todd Penegor, president and CEO of Wendy's, in the announcement.

Panera Bread and Del Taco have also begun working with AI assistants in the drive-through.

AI has other uses, too. McDonald's and Google Cloud have partnered to apply generative AI solutions that are expected to help accelerate automation and assist managers in spotting equipment problems so solutions can be enacted quickly. It also can help chains learn more about shopper behavior, enabling the restaurant to offer personalized offers and promotions.

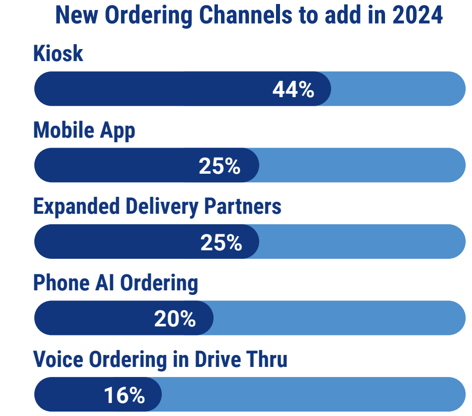
Integrated Technology: The mobile app can now be combined with loyalty programs and AI to offer guests customized offers based on previous behavior or discounts tied to holidays and special events. In 2022, Toast, which had already been operating in full-service restaurants, launched a version for QSRs that integrates countertop, payment and guest self-service terminals to allow greater customization, faster delivery and easier payment.

Gameification: Rewards programs can use games to offer discounts and prizes to loyalty club members. Shoppers often end up exploring and adding more to their cart.

Kiosks: Expanded during the pandemic and are growing even faster to reduce staff and guest wait times. Forty-four percent of brands plan to add kiosks as a new ordering channel in 2024[17].

Predictive Analytics: Integrated with POS data, solutions such as Mastercard's Test & Learn For Restaurants, Tango or Integrio can help restaurants predict peak and slow times, allowing managers to allocate staff and inventory accordingly. The result can reduce waste and maximize productivity. Analytics can also assess customer preferences and eating patterns to suggest menu changes and new items[18].

New Ordering Channels to add in 2024



The FOOTPRINT Effect

THE PANDEMIC AND THE POST-PANDEMIC ERA had a dramatic effect on QSR real estate in two ways: where they locate and where they locate within a property.

For decades, QSRs took advantage of urban density — they were the places for commuters to pick up a coffee or breakfast before work, and lunch or drinks after work in the heart of the city. Arguably, locations were overbuilt in central business districts (in many cities, a Starbucks on every corner wasn't a joke, it was reality), while suburbs were neglected.

The pandemic changed all that. Central business districts became ghost towns while former commuters worked from home.

"This has essentially caused the center of the QSR industry to officially move away from bustling business districts toward the places where people live," according to SafeGraph in The Big Wake-Up Call: Re-thinking the Entire Playbook for the Quick Service Restaurant Industry[19]. Even as workers are gradually returning to the office, at least some of the time, chains' focus on suburban growth remains. In 2023, Sweetgreen noted that most of its new stores would be located in suburbs[20].

Shopping center owner and managers must adapt to these changes. As the size of the buildings drops, their need for outdoor space may increase, whether to accommodate outdoor dining that was popularized during the pandemic or designated parking spaces for pickup orders.

"You can design a fast casual restaurant in less than 2,000 square feet, possibly with an outside seating component, and it's not a problem at all — especially in this day and age where people have become so keen to order off-premise," Juan Martinez, principal of industrial engineering company Profitality, told LoopNet in 2021[21].

That's not as easy as it looks, however, Martinez continued, as space must be left for people to park if they arrive before their order is ready. He suggested the building of an "escape lane" where customers can wait, yet another design element that must be planned by both tenant and landlord.

The good news is that these smaller stores can allow developers to place more on pads around their centers — as long as the property remains in compliance with parking ratios. Good relationships with municipalities will be critical[22].

But the greatest impact will be the return and the proliferation of the drive-through. Born during the suburbanization of America in the 1950s, the concept has returned during the resuburbanization of the early 2020s, when speed, convenience and more than a bit of isolation were required. Now, they provide operators the opportunity to save space, staff and money.

For example, in 2023, Chipotle opened 121 new restaurants — 110 of which included Chipotlanes, digital pick-up locations for orders placed online[23]. In Atlanta, Chick-fil-A, one of the fastest-growing QSRs in the U.S., will open a four-lane drive-through, with the kitchen located a level above. Meals are sent to a team member who delivers the order in a space covered by the upper floor[24].

"While drive-throughs minimize the physical size of the store, they require careful consideration of real estate for car queuing. Innovations like app-based drive-thru systems, such as Chipotle's Chipotlane, are optimizing this space," observes Jeff Rabbitt, Partner at design firm AO. "These systems leverage app ordering and real-time notifications to streamline the drive-thru experience, reducing the required length of queuing space. This innovation allows QSRs to operate in locations with restricted geometries that were previously considered unviable due to space constraints[25]."

Traffic patterns in parking lots may need to change to accommodate different entrances for those dining in and those picking up[26].

Inline locations are also possible, but the higher costs associated with these spaces need to be carefully assessed by both tenant and landlord. Look for smaller concepts such as cookie chains, tea sellers and local tenants to compete for these spaces.

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A Rebirth and an OPPORTUNITY

THE PANDEMIC and changing consumer needs could easily have destroyed the QSR sector. Instead, it found ways to innovate, survive and then thrive. Mobile apps, kiosks, contactless delivery and innovative new menus have remade the experience in the front of the house — and at shoppers' front doors.

But the back room, too, has changed. Technology and automation are now performing onerous restocking tasks, reducing the need for ever more expensive labor and preserving the bottom line.

And increasingly, each of these technologies can inform the others via artificial intelligence, allowing a unified experience for the guests — and insights into their behavior that companies can use to personalize menus and reward their loyalty.

The result may well be a smaller restaurant that will require a smaller building but more space for cars and drive-throughs. It will be up to real estate companies to work with, accommodate and learn from them.

For more information on these and other retail and restaurant trends, and how we can help you expand, feel free to contact a Coldwell Banker Commercial® affiliated professional at CBCWORLDWIDE.COM.

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