

Restaurant Brands International, Inc., 2015

www.rbi.com, QSR

On December 4, 2014, Burger King Worldwide (BKW) officially acquired Tim Hortons, Inc., a Canadian coffee-and-doughnut retailer, for \$11.4 billion. With that deal, BKW created Restaurant Brands International (RBI), which overnight became the second-largest global quick-service restaurant in the world. The combined company, RBI, is headquartered in Oakville, outside of Toronto, Canada, although BKW was headquartered in Miami, Florida. A primary rationale for this acquisition was for BKW to save potentially millions of dollars through what is called *tax inversion*—a process where a company reduces its U.S. tax liability by relocating its headquarters to a country with lower corporate tax rates. Canada's corporate tax rate is 15 percent versus the USA's 39 percent, yielding in a potential huge annual savings in corporate taxes for BKW. As part of the deal, BKW agreed to (1) maintain employment levels at Tim Hortons' Canadian restaurants, (2) expand Tim Hortons' global presence, (3) maintain Tim Hortons' franchisee rent and royalty structure at current levels for a 5-year period, and (4) operate Tim Hortons and Burger King as separate brands, with no plans to create one unified brand.

Burger King Worldwide is the second largest global fast-food hamburger restaurant (FFHR) chain, behind McDonald's, in the quick-service restaurant (QSR) industry. Best known for the Whopper, BKW sells beef and chicken-based sandwiches along with other fast foods. Recently, BKW launched lower-calorie french fries, a gay-pride Whopper in San Francisco called "Proud Whoppers," and even brought back the YUMBO® sandwich.

Known internationally as "Tim Hortons Cafe and Bake Shop," Tim Hortons is Canada's largest quick-service, casual restaurant (McDonald's is #2). As of June 30, 2013, Tim Hortons has 4,304 restaurants, including 3,468 in Canada, 807 in the United States, and 29 in the Middle East. However, as of September 2014, there were fewer (3,665) Tim Hortons restaurants in Canada, but more (869) in the United States, and nearly double (56) in the Middle East (mainly on American and Canadian military bases). Tim Hortons has about 75 percent of the Canadian market for baked goods (based on the number of customers served) and about 65 percent of the Canadian coffee market (compared to Starbucks at #2 with 7 percent).

For the second quarter of 2015, Restaurant Brands International reported revenue of \$1.04 billion, beating analysts' expectations of \$1.01 billion. In the Burger King division, comparable store sales rose 6.7 percent in Q2, driven by product launches such as the A.I. Hearty Mozzarella Bacon Cheeseburger, Extra Long Pulled Pork Sandwich, and Chicken Fries. In the Tim Hortons division, comparable store sales increased 5.5 percent in Q2, boosted by strength in dark roast coffee and its Creamy Chocolate Chill beverage. In comparison, rival McDonald's (MCD) reported a 0.7 percent decrease in global comparable store sales during the Q2 that ended on June 30, 2015. Also during Q2, Tim Hortons added 52 net new restaurants, ending the period with 4,776 locations, while Burger King added 141 net new restaurants, ending the period with 14,528 locations. Last year, Burger King purchased Tim Hortons for \$11 billion. Restaurant Brands now has over \$23 billion in systemwide sales and over 19,000 restaurants in approximately 100 countries and U.S. territories.

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History

Tim Hortons was founded in 1964 in Hamilton, Ontario, by Canadian hockey player Tim Horton and Jim Charade, after an initial venture in hamburger restaurants. In 1967, Horton partnered with investor Ron Joyce, who assumed control over operations after Horton died in 1974. Joyce expanded the chain into a multimillion business. In November 2010, Tim Hortons announced it was closing 36 stores in the northeastern United States, due to high competition with New England-based Dunkin' Brands, owner of Dunkin' Donuts. In May 2014, Tim Hortons

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launched a new frozen drink, Frozen Green Tea, and a few months later launched a dark roast coffee blend.

Burger King Worldwide was founded in 1954 by James McLamore and David Edgerton, who opened the first location in Miami, Florida, after purchasing the trademark rights for “Insta-Burger King”—a franchise hamburger restaurant that used an insta-broiler to quickly and cheaply grill hamburgers. As franchisees of the Insta-Burger King chain, they purchased the Jacksonville, Florida-based franchise, renamed it Burger King, and successfully grew the company for the following 8 years. BKW introduced the Whopper in 1957.

In 1967, Pillsbury Company purchased Burger King and subsequently instituted several attempts to restructure the restaurant chain. After years of declining profits and poor performance, Burger King was purchased by its current parent company, 3G Capital, in 2006 for \$4 billion. 3G Capital made Burger King a private company, but relisted it as a public company in 2012, while retaining approximately 70 percent ownership. 3G Capital is currently the largest shareholder of Restaurant Brands International.

Dunkin’ Brands, Krispy Kreme Doughnuts, and Starbucks are rivals to Tim Hortons. McDonald’s, Wendy’s, Hardees, and hundreds of other hamburger chains are rivals to Burger King. Prior to the purchase, BKW had a presence in 97 countries with approximately 14,000 locations. The United States and Canada markets account for about 50 percent of these locations. Burger King Worldwide recently increased its locations in China substantially. With the creation of RBI, the international footprint of these two iconic brands now account for more than 18,000 restaurants located in 100 different countries.

Restaurant Brands International was founded on December 4, 2014.

Internal Issues

Vision/Mission/Values/Ethics

Burger King Worldwide’s vision is as follows: “Our commitment to premium ingredients, signature recipes, and family-friendly dining experiences is what has defined our brand for more than 50 successful years.” The company has an extensive Code of Ethics referred to as the *BKC Code* published on the website. As found in the *BKC Code*, BKW states, “Our vision is to be the most profitable QSR business, through a strong franchise system and great people, serving the best burgers in the world.” The *BKC Code* further lists the following corporate values: Bold, Accountable, Empowered, Meritocratic, and Fun. The company does not have a written mission statement. The *BKC Code* is published for all franchisees, employees, and executives to follow. It specifically addresses employee culture, key business strategies, guests, and how employees can adhere to the code in all of these areas. For example, the section on employee culture addresses diversity and inclusion as well as data privacy. Safety and restaurant quality are addressed under the Guest section.

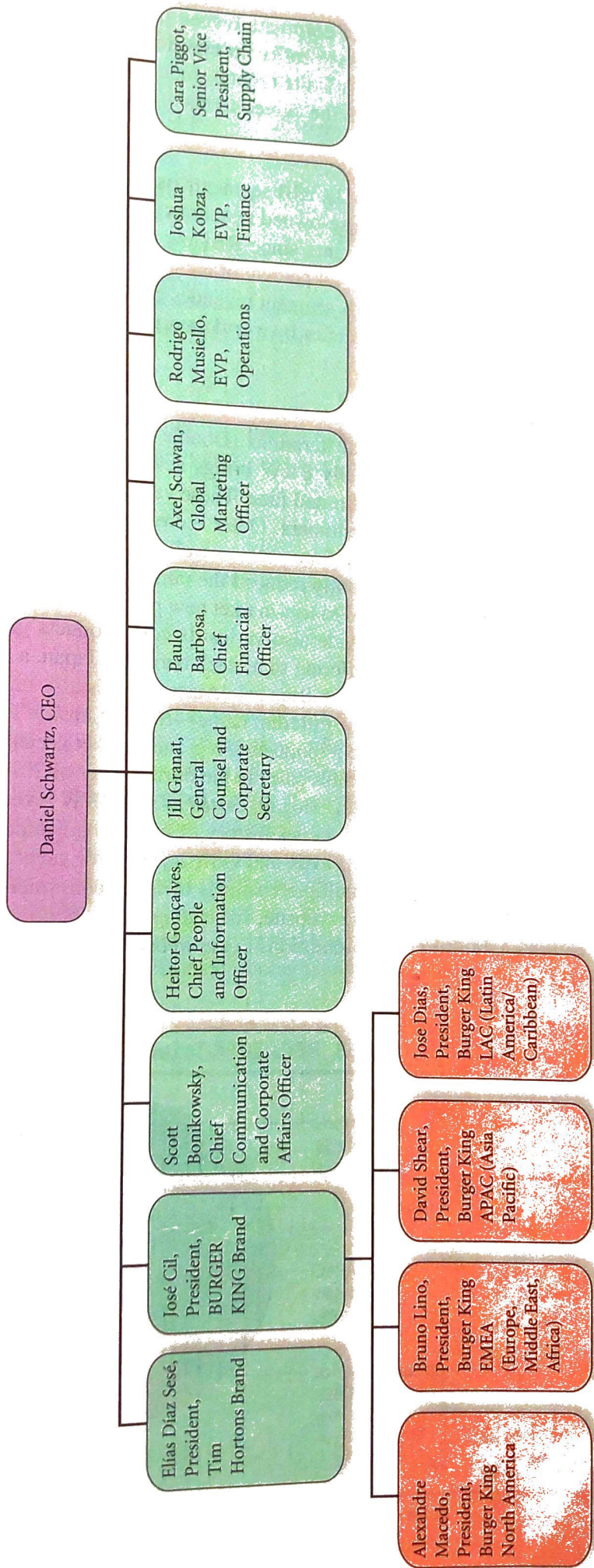
Organizational Structure

As illustrated in Exhibit 1, RBI operates using a strategic business unit type design, with there being two strategic business units (SBU): Burger King Worldwide and Tim Hortons. There are divisions by region below the two SBUs. Soon after the merger was consummated in December 2014, Daniel Schwartz was appointed CEO of Restaurant Brands International. Schwartz is leading the company’s day-to-day business and is responsible for the overall business strategy. Exhibit 1 reveals other executives appointed to the RBI’s leadership team.

Strategy

Restaurant Brands International is committed to fulfilling its agreed-on strategy dimensions for operating Tim Hortons. However, regarding its BKW brand, RBI is focused on (1) driving sales in the United States and Canada, (2) accelerating international development, (3) aggressively pursuing refranchising opportunities, and (4) maintaining strong focus on corporate-level cost structure. Burger King Worldwide is focused on increasing its global footprint through joint ventures and strategic partnerships. Typically, BKW provides franchisees with exclusive rights within specific regions. In return, franchisees receive minority stakes in the joint venture.

EXHIBIT 1 RBI's Organizational Structure



Source: Based on information provided at all three companies' websites.

Currently, BKW is focused on high growth or emerging markets. Simply stated, BKW is focused on reducing the number of corporate-owned franchises. Through these means, BKW intends to decrease costs and increase profits. In addition, BKW is focused on expanding Tim Hortons, likely first in the Northeast United States, then nationally, then globally—not necessarily in that order—but consistent with the agreed terms of the acquisition.

Segments

Reporting into its two SBUs, RBI segments its operations into five regions. Exhibit 2 details the locations of RBI's franchise-owned restaurants. Franchise-owned restaurants account for nearly 100 percent of all restaurants since RBI owned only 65 total restaurants out of over 19,000 worldwide. Note that only 24 percent of all stores are Tim Hortons.

Exhibit 3 shows RBI's segment revenues and EBITDA. Note that Tim Hortons has the poorest ratio of EBITDA/Revenues by a wide margin overall compared to the Burger King regional segments.

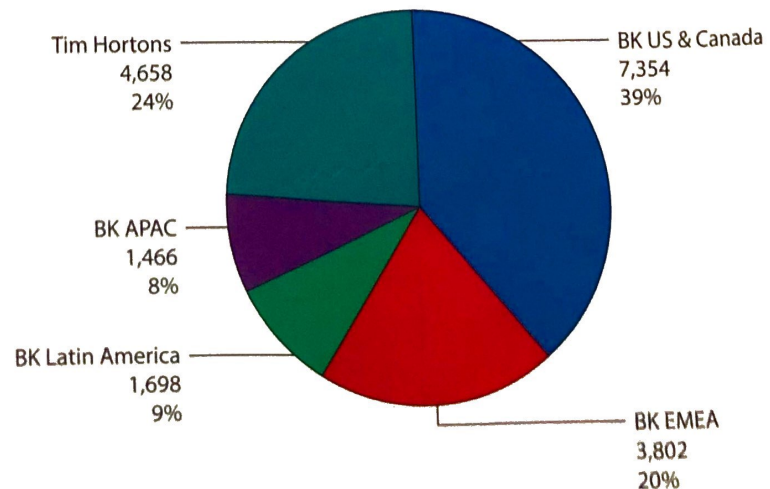
Marketing

The Whopper and several iterations (Double Whopper, Four Cheese Whopper, etc.) are core BKW products. Periodically BKW brings new iterations, such as the Angry Whopper and the Chipotle Whopper, for a limited time. These variations help drive new customers to BKW, while reinvigorating current customers. Other more experimental offerings have included the Pride Whopper, exclusive to San Francisco, as well as Satisfries, a healthier alternative to french fries. While BKW has significantly reduced the number of corporate-owned locations, the remaining 52 are intended to be used to test-market new products prior to wider release.

Burger King Worldwide also varies its core products globally to meet local tastes. Some examples would be the offering of a black burger in Japan, a Cheese Fondue Whopper in South Korea, and a Bacon Outback Burger in Australia. It is also only in Australia where Burger King restaurants operate under a different name—*Hungry Jack's*. This different brand further demonstrates BKW's commitment to meeting regional market needs, and helped lead to the 2.4 percent increase in global comparable sales in the third quarter of 2014.

With the new marketing slogan, *Taste is King*, BKW is focusing its marketing to put its food first. BKW has had a tumultuous history of marketing campaigns, but it has been known to be a front-runner within the FFHR and QSR markets for successful campaigns. The communication strategy integrates multiple channels to reach consumers, including social media, the BK app, and the website. The website, for example, is simple yet bold with its emphasis on food offerings. It also places promotions in the website navigation bar, again reinforcing the strategic

EXHIBIT 2 RBI's 2014 Total Franchise Stores



Source: Based on information in RBI's 2014 Annual Report, p. 6.

EXHIBIT 3 RBI's Revenues by Company-Owned versus Franchisee Restaurants
 (in millions of USD)

	2014		2013	
	Revenues	EBITDA	Revenues	EBITDA
BK US & Canada	640	446	655	437
BK EMEA	274	220	336	189
BK Latin America	77	69	86	67
BK APAC	64	56	58	49
Tim Hortons	142	35	—	—

Source: Based on information in RBI's 2014 Annual Report, pp. 120 and 121.

goal of communicating both core products and value. The Burger King app mirrors this as well, providing consumers the opportunity to find locations and receive coupons. The ability to pay by phone is also integrated into the app.

Finance

Restaurant Brands International's recent income statement and balance sheet are provided in Exhibits 4 and Exhibit 5, respectively.

Competitors

Every year, U.S. consumers spend about \$75 billion in the Fast-Food Hamburger Restaurant (FFHR) category. Companies in this segment compete based on price and convenience, leading to fierce competition. For example, it is common practice within this segment to quickly expand and open new locations to leave little space for other competition. Not only is there constant price pressure, but constant marketing of deals through coupons, a common tactic to drive traffic. Yet, the products (i.e., hamburgers) may be seen as undifferentiated by consumers. Both factors necessitate competitors to manage operating expenses, while spending marketing dollars to drive foot-traffic, and while striving to create brand differentiation and loyalty. Of the \$75 billion spent annually in FFHR, consumers spend about \$10 billion at Burger King Worldwide. Yet, BKW is only number two in this market segment, with McDonald's being number one and Wendy's close behind as number three in the market.

In addition to the real big companies such as McDonald's and Starbucks, Five Guys Enterprises, Elevation Burger, BurgerFi, and What-A-Burger compete aggressively with

EXHIBIT 4 RBI Income Statement (in millions of USD)

Report Date	December 31, 2014	December 31, 2013
Revenues	\$1,197	\$1,146
Operating expenses	1,015	624
EBIT	182	522
Interest and other	435	200
EBT	(253)	322
Tax expense	(24)	88
Partnership adjustments	(560)	—
Net income	(837)	234

Source: Based on RBI's 2014 Annual Report, p. 68.

EXHIBIT 5 RBI's Balance Sheet (in millions of USD)

Report Date	December 31, 2014	December 31, 2013
Assets		
Cash and equivalents	\$1,803	\$787
Accounts receivable	440	178
Inventories	194	70
Other current assets	223	39
Total current assets	2,660	1,074
Property, plant & equipment	2,540	802
Goodwill	5,851	630
Intangibles	9,441	2,796
Other assets	672	526
Total assets	21,164	5,828
Liabilities		
Accounts payable	223	31
Tim Hortons notes	1,045	—
Other current liabilities	657	315
Total current liabilities	1,925	346
Long-term debt	8,937	2,880
Other liabilities	2,681	1,086
Total liabilities	13,543	4,312
Preferred Partnership Units	3,297	—
Total stock	4,579	—
Retained earnings	—	226
Treasury stock	—	(7)
Paid in capital	—	1,240
Other	(255)	57
Total equity	4,324	1,516
Total liabilities, Preferred Partnership Units & equity	21,164	5,828

Source: Based on RBI's 2014 Annual Report, p. 69.

RBI. Five Guys, for example, proudly proclaims its strategy of offering healthy beef, not investing heavily in marketing and advertising, and serving all-you-can-eat peanuts and veggie burgers. Elevation Burger and BurgerFi focus on high-quality food and drinks. Elevation Burger markets its hamburgers as grass-fed, free-range, and organic—overall healthier food that is better for the environment. BurgerFi touts angus-beef burgers with craft beer and wine available for purchase. Also, there are more than a million mom-and-pop hamburger restaurants globally.

Competition for consumers is not limited to hamburger restaurants, as restaurants that sell pizza and other fast foods can compete indirectly. Yum! Brands—consisting of Kentucky Fried Chicken, Taco Bell, and Pizza Hut—represents significant indirect competition to BKW domestically and abroad. For example, there are about 4,600 KFCs and 1,000 Pizza Huts in China alone. Yum! Brands further views the Pizza Hut Casual Dining experience in China as containing untapped potential, given that two-thirds of sales are non-pizza. Yum! Brands recently began offering breakfast items, and serving breakfast even at its Taco Bell locations.

Exhibit 6 compares RBI, McDonald's (MCD), Wendy's (WEN), Starbucks Corporation (SBUX), and Dunkin' Brands (DNKN) on various metrics. Be mindful that franchised restaurants

EXHIBIT 6 Comparative Metrics for RBI and its Rival Firms

	RBI	MCD	WEN	SBUX	DNKN
\$ Revenue	1.2 B	27 B	2.1 B	17 B	750 M
\$ Net Income	(837) M	4.8 B	121 M	2.5 B	177 M
# Employees	4,600	420,000	32,000	191,000	1,600
\$ Revenue per Employee	261 K	64,000	65,000	89,000	469,000
\$ Market Capitalization	18.2 B	92 B	4 B	70 B	4.7 B
\$ EPS	(2.34)	4.80	0.32	3.30	1.65

Source: Based on company documents and Yahoo! Finance.

report revenues and income on the franchisee financial statements, not the big parent company. The parent reports royalty income from franchisees (i.e., on their income statements), but the property, plant, and equipment and everything for a franchised restaurant is on the franchisee's financial statements rather than the parent company. Note that Restaurant Brands International is much smaller than McDonald's or Starbucks.

McDonald's Corporation (MCD)

Headquartered in Oakbrook, Illinois, McDonald's has about 36,000 locations in 119 countries with about 6,700 locations corporate owned. McDonald's strategy includes operating a large number of corporate-owned locations, as it is viewed integral to lead-by-example for franchisees—a very different approach from BKW's current franchise strategy. McDonald's has been struggling of late due to intense price competition in the industry.

The Wendy's Company (WEN)

Headquartered in Dublin, Ohio, Wendy's has about 6,500 restaurants, primarily in the United States and Canada. Of those 6,500 locations, about 1,100 are corporate owned. Wendy's has about 400 franchised locations outside North America, in 25 other countries.

Starbucks Corporation (SBUX)

Headquartered in Seattle, Washington, Starbucks has about 22,000 restaurants in 65 countries. Historically primarily a breakfast restaurant, Starbucks now offers dinners and alcoholic beverages, and is open longer hours per day than ever before.

Dunkin' Brands (DNKN)

Headquartered in Canton, Massachusetts, Dunkin Brands' owns, operates, and franchises quick-service restaurants under the Dunkin' Donuts and Baskin-Robbins brands worldwide. The company operates 11,500 Dunkin' Donuts restaurants and 7,600 Baskin-Robbins restaurants globally. Dunkin has avoided Canada (having only 4 locations), just as Tim Hortons has avoided the United States, obviously to avoid crossing paths very much. There are approximately 2,200 Dunkin' Donuts in the Asia Pacific region alone, with plans to dramatically increase the presence in China, with over 1,400 new locations in the next 20 years. Currently, there are 8,000 Dunkin' Brands restaurants in the United States. Like BKW, Dunkin' Donuts caters to local tastes. For example, in Korea there is the Grapefruit Coolatta, the Choco Nut Donut in Thailand, and mochi-based donuts in China.

External Issues**The Public's Concern for Health**

There is an ever-growing concern regarding childhood and adult obesity. It is estimated that about one third of Americans are obese, and these figures are expected to increase. Obesity may lead to significant health issues, including diabetes and heart disease. To stave off these concerns, a number of regulations have been implemented at the local, state, and federal levels—all

of which could impact RBI's operations and revenues. For example, the U.S. Food and Drug Administration (FDA) will soon be mandating all caloric values be disclosed on menus. While RBI currently provides this information on its website, it is possible that as the public's understanding of calories grows, so may the negative impact on RBI's business. Simply stated, according to the company website, the Whopper has approximately 650 calories. Since the current daily allowance recommended is 2,000 calories, the public may eventually put pressure on BKW and other restaurants to provide healthier, lower-calorie alternatives. The Satisfries is a good example of BKW attempting to meet these demands. McDonald's is trying to raise consumers' perception of the quality of its food by adding kale to the menu. McKale chips may soon be available, alongside hamburgers and fries.

Class action lawsuits have been filed against various quick-service restaurants for not appropriately notifying the public of the health risks from such foods. Various lawsuits have claimed that marketing practices have unfairly targeted children—echoing the lawsuits against tobacco in prior decades. Even if RBI is not directly affected by such lawsuits, the publicity and attention they draw can negatively impact the company. A related dietary trend is the growing number of people following specialty diets. These may range from gluten-free to vegetarian. Restaurant Brands International does offer information concerning gluten on its website, but does not necessarily offer food for those who desire these options. Yum! Brands' Pizza Hut and Domino's Pizza, however, offer gluten-free pizza as a dining option. White Castle, a fast-food hamburger restaurant famous for its beef sliders, offers veggie burgers that are prepared separately from meat-containing foods to cater to vegetarians. If more competitors begin to offer these options, it may put more pressure on BKW to deviate from its core products.

Technology and Security

As of late, retailers have been the subject of cyberattacks and breaches of security, leading to the theft of customer and employee information. One such attack against Target led to the theft of 40 million credit card numbers. Neiman Marcus also experienced an attack, where the personal information of 70 million customers was stolen. Restaurant Brands International seems exposed to such an attack since the company looks to meet the needs of the consumer through technology. For example, the BKW app allows for payment through mobile phones. Any and all information BKW is storing and transmitting through this software could be stolen. One simply can ask what happens if RBI runs a controversial marketing campaign that offends a specific individual or group? Even the company's Whopper targeted toward gays in San Francisco could make the firm vulnerable in social media. All of these threats lead to the need to invest in risk assessment and mitigation measures.

Employment Law

New minimum wage and health-care laws impact RBI. Both at the state- and federal-level minimum wage levels are being challenged. There have been open protests against the hourly wages of fast-food workers. Viewed as low-wage workers, many of these people are protesting to increase the minimum wage to \$15 an hour. McDonald's as well as Burger King have been primary targets of these protests. To respond to these protests, many states have increased minimum wage. Cities have considered taking further steps, such as Seattle, where the minimum wage was increased to \$15 an hour. Wal-Mart, Target, and other retailers have recently increased their minimum wage rates paid to employees.

The Patient Protection and Affordable Care Act (ACA) represents another area of increased costs for franchisees, requiring that businesses offer health care to employees meeting the hourly threshold. This is another area where franchisee costs may increase. Other changes in employment law can cause disruptions and increases in costs, such as laws related to immigration, overtime, working conditions, and family leave. These potential changes are exacerbated by BKW's global presence, as it must monitor and support franchisees across the globe.

Future

Burger King Worldwide is actively transitioning from being a USA-based, global hamburger chain, to a Canada-based diverse restaurant chain. BKW's recent Tim Hortons acquisition and the creation of Restaurant Brands International has both BKW and Tim Hortons poised to grow

much faster globally—but where, when, why, and how? Some analysts assert that RBI's financial fundamentals are excellent. Same-store sales at Burger King and Tim Hortons rose 2 percent and 3 percent, respectively, in 2014, which is excellent. However, RBI operates from a desired 100 percent franchised-model, so future earnings largely rely on fixed-cost reductions and post-merger synergies. RBI shareholders are not pleased with the decline in 2014 net income, and are anxious to see growth of 5 percent-plus going forward. The new CEO of RBI, Daniel Schwartz, needs a clear strategic plan for the company. Help him develop an effective 3-year strategic plan for RBI.