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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Brinker International Q3 Earnings Call. (Operator Instructions)

It is now my pleasure to turn the floor over to your host, Mika Ware. Ma'am, the floor is yours.

Mika Ware

Thank you, Paul. Good morning, everyone. This is Mika Ware, Vice President of Finance and Investor Relations, and welcome to the earnings call for Brinker International's Third Quarter Fiscal Year 2018.

Results for the third quarter were released earlier this morning and are available on our website at Brinker.com. Wyman Roberts, Chief Executive Officer and President; and Joe Taylor, Chief Financial Officer, join me here this morning in Dallas.

During the comments portion of the call, Wyman and Joe will provide a more detailed overview of the third quarter and will update the progress of our strategic initiatives underway at the company.

Of course, before beginning our comments, please let me remind everyone of our safe harbor regarding forward-looking statements. During our call, management may discuss certain items, which are not based entirely on historical facts. Any such items should be considered forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All such statements are subject to risk and uncertainties, which could cause actual results to differ from those anticipated.

Such risk and uncertainties include factors more completely described in this morning's press release and the company's filings with the SEC.

Additionally, on the call, we may refer to certain non-GAAP financial measures that management uses in its review of the business and believes will provide insight into the company's ongoing operations.

With that, now I will turn the call over to Wyman.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Thanks, Mika. Good morning, everyone, and thanks for joining us to review third quarter results and our plans to build on our momentum in the quarters ahead. Brinker delivered improved performance in the third quarter with comp sales of minus 0.3% despite a challenging winter, which had a negative 60 basis point impact. So adjusting for weather, sales would have been positive. We showed sequential growth both quarter-to-quarter and throughout the quarter, and the trajectory of our business continues to hold strong.

And our third quarter sales were slightly below Black Box. Our traffic results significantly outperformed the category. We understand the importance of reversing traffic trends. And our plans are built on strategies designed to first close the gap, which we've done and then move to positive traffic.

First quarter was about putting the strategy in place, second quarter was about implementation, and the third quarter, we started to see momentum with significant changes in traffic. Now it's about building on our progress by maximizing our ability to connect with our guests and deliver on their needs.

I'll touch on our Maggiano's and global business first, and then we'll spend the remainder of our time on the Chili's brand.

Maggiano's delivered another positive comp sales quarter, with sales up 0.5%. And when you adjust for the significant weather they had, given their heavy presence on the East Coast, it was an impressive quarter, primarily driven by double-digit increases in take-out and delivery. And we see even more opportunity to expand our off-premise business moving forward, especially since Maggiano's food is so appealing to take-out. We're working to add individual delivery to our already strong catering business. We're also enhancing our banquet business, and we have new menu innovation around the corner, all to drive relevance and increase traffic.

Our global business partners in Latin America and the Pacific had a strong quarter with positive comps, while our Middle East partners are more challenged, given the dramatic economic factors impacting that region. The net was combined comps of negative 0.2%. We do continue to enjoy strong demand for the brand globally. Already, this year, our partners have opened more than 30 restaurants, and we're pleased to announce our first partner in China, whose territory will cover the Shanghai region. We're in negotiations with additional partners to cover more regions across China. We're excited about what fiscal 2019 will bring as we further expand Chile's footprint in Asia.

Here, in the U.S., Q3 marked the second quarter into our turnaround strategy, and it's clearly the investments we've made to increase quality, consistency and value are paying off. We're seeing sales and traffic improvements across both dayparts, and we believe this momentum is sustainable because of the foundational work we've done to strengthen Chili's overall value perception.

We've improved our menu, our atmosphere. And we're providing a faster, more consistent and convenient experience. All of this is having a positive impact on the value perception of Chili's, and a strong value perception is critical in this very competitive environment.

I mentioned during our last call that we would get more aggressive at lunch. During third quarter, we went on air to remind people about our lunch combo offering, and we drove several percentage points of improvement in lunch traffic. Then we followed that up with 3 -- our 3 for $10 promotion, which is driving traffic at lunch and dinner. We also added our $5 margarita platform with new innovation every month, which is growing alcohol sales and contributing to traffic growth as well.

We're seeing increased frequency both among heavy users and light users as they come back more often to see what's new at Chili's. And with online ordering rolled out across our company and franchise restaurants, we have a great opportunity to market our curbside program, one of the easiest take-out experiences in the industry.

Online ordering grew upwards of 30% during the quarter and continues to climb, creating a more efficient model for us and more compelling and consistent experience for the guests and has increased our overall to-go business to more than 11% of total sales.

Finally, during the quarter, we exited the Plenti program. We're excited about the opportunity to reignite My Chili's Rewards and to lean further into our ability to connect with guests in the digital space. Moving forward, we're well focused on growing our already large customer database by shifting some of our marketing resources from traditional to more digital mediums, so we can build relationships with our guests that drive incrementality. And we're making additional investments to further enhance the guest experience and drive top line.

First, consumers clearly plays a tremendous value on convenience. So we're devoting even more resources to work on Chili's off-premise experience. We've assembled a new team focused on improving the infrastructure, operational processes and technology solutions to make it easier for the operator and for the increasing number of guests, who want to enjoy hot, fast, Chili's food away from the restaurant.

Next, we're continuing to invest in food quality and menu innovation, target around what we do best: burgers, ribs, fajitas and margaritas. We have exciting new recipes coming soon, designed to increase frequency as well as preserve simplicity in operations, so we can maintain our improved speed and consistency. And with winter finally behind us, we'll get back to work investing in our atmosphere. We started up construction on our fleet with the goal of reimaging roughly 250 restaurants during fiscal '19.

What I'd like you to take away today is that our core strategy to improve our quality, consistency and value is working well for us across our entire business. We're confident we can sustain this momentum. We are energized by the work the teams are engaged in, and we're excited about the continued investments and opportunities ahead.

And now I'll call -- I'll turn the call over to Joe to give you more insight into third quarter results. Joe?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Thanks, Wyman, and good morning, everyone. Let me continue the overview of our third quarter performance by first providing some brief comments as to the numbers reported earlier today, and then we can get to your questions.

As Wyman indicated earlier, this quarter represented the opportunity to move more aggressively on building momentum per the strategy implemented in the second quarter. We saw that come to fruition as the weeks unfolded, as offerings we developed around our core equities drove traffic improvements that reached positive year-over-year levels as we ended the quarter.

Our third quarter revenues of $813 million represents a slight improvement over the third quarter last year, with growth in franchise and other revenues more than offsetting the small reduction in comp sales growth.

Brinker reported comp sales of minus 0.3% for the quarter, a meaningful sequential improvement. Its more aggressive value promotional activity drove comp sales with traffic as opposed to check.

For the quarter, price contributed only 1.2% to comp sales, a necessary drop from the 2% plus levels we'd been running for the last several quarters.

At the brand level, Maggiano's reported positive comp sales for the quarter of 0.5%, while Chili's reported quarterly comp sales of minus 0.4%.

While we took another step forward in our trajectory towards positive quarterly comp sales growth. The pace of our improvement will not reach the annual guidance of comp sales growth we provided earlier in the year.

We now believe our comp sales performance for fiscal year '18 will be in the range of minus 0.5% to minus 1%.

For the quarter, we reported restaurant operating margin of 16.1%. The year-over-year reduction in operating margin of approximately 90 basis points is a result of investments in our successful promotional activity for the quarter as well as increases in labor-related expenses. Let me provide a little more detail. Cost of sales for the quarter increased 70 basis points, as we invested into the abundance and quality of our burgers, ribs and fajitas, an experience successful traffic-driving results from our 3 for $10 promotion that started in early March.

Restaurant labor increased 50 basis points, as we experienced higher insurance claims during the quarter, but added to the ongoing market-driven wage rate pressures, which continued in the 3% to 4% range.

Restaurant expenses for third quarter were favorable by 30 basis points. Slight increases in property-related costs were more than offset by savings in tabletop device and Plenti program costs.

Planned performance through the above-restaurant components of our P&L, supported by a reduced effective tax rate, resulted in adjusted net income of $49.6 million or earnings per share of $1.08, a 14.9% improvement from prior year.

Cash flows from our operations remain in good stead. For the quarter, we generated $97 million of free cash flow after accounting for capital expenditures of $21 million. This allowed us to purchase $90 million worth of shares during the quarter as part of our ongoing capital allocation program.

As it relates to our existing capital structure, we will refinance the bond issuance that matures in mid-May under our revolving credit agreement.

Additionally, a lower effective tax rate, improving operations and the resulting benefits to cash flow allow us the opportunity to review various capital transactions, including the sale/leaseback of owned restaurant assets. Such capital transactions potentially would allow the use of proceeds to manage overall revolver borrowings to support strategic initiatives of the brands or to include in our ongoing capital return to shareholders.

In summary, we're pleased with the overall direction of our brands as they are again demonstrating the ability to grow the business in a positive sustainable manner. With momentum established as we continue into the final quarter of our current year, we believe our strategy of focused operations, improved food and enhanced guest experience will continue to grow traffic and capture share as we move forward.

And with that, Paul, let's open the lines up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And the first question is coming from Jeffrey Bernstein.

Jeffrey Andrew Bernstein - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Calling from Barclays. Two questions. One, just -- Joe, I guess, on the comments you just made about the potential capital transactions that you're reviewing, sounds like you're focusing on the real estate. I'm just wondering if you can give any granularity in terms of -- but I guess you mentioned sale/leaseback, so how many sites we're talking about, the potential proceeds, and maybe, the offset being the higher rent presumably that you would be paying? So any color that you can give initially in terms of the real estate potential transaction?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Jeff, there's not a lot of additional color in that regard since we are potentially looking at transactions and don't have anything specific to report at this time. We'll keep you obviously appraised as we go through the review. What we have said before is we have owned real estate assets of approximately 190 restaurants. Now obviously as you -- if you look at the transactions, I would not expect all of those to be included in a transaction if we would do one. So it would be somewhat lower than that. But we'll keep you updated as the review progresses.

Jeffrey Andrew Bernstein - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Got you. And then just on the comp trends. One, I'm not sure whether you're able to provide some thoughts on the broader industry or whether you want to talk specifically to Chili's, but it does seem like both yourselves and the industry have seen an uptick most recently. I'm just wondering if you could talk about what you think are your drivers of the industry or the specific things that you think Chili's is doing that seemingly has driven the narrowing of the gap versus that industry trend?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Jeff, yes, I think from an industry standpoint, we've seen some strengthening obviously through the; quarter. And that was encouraging especially, again, given it was a relatively tough winter, especially for the northeast. It does appear that there is greater strength in some of the bigger concepts. So relative to the averages, that's encouraging for a brand like Chili's that gets to leverage its scale and its size. And I think we're starting to see some of that play out and putting more pressure on some of the smaller independents, which, again, bodes well for big brands that have the scale to get their messaging out there. With regards to Chili's and trajectory of the sales, we've been very encouraged by -- after a pretty slow start out of the holidays, the momentum that we've been able to capture, both as we cleared some hurdles, making the menu changes is a process that takes a little bit of time to work through when you delete 40% of your items. And once we got past that, we got past some higher pricing from prior years and then the team really started to get their marketing momentum, both with lunch offerings, with their direct programs and then with their promotional strategies, and the trajectory has been good. As you can see, it's really a traffic-based strategy and (inaudible) traffic in the third quarter and the momentum is driving a wider gap as we move out. So we're -- our focus is getting people into the restaurant and giving them experience -- the improvements that have been made, and we're seeing that across pretty much all the markets.

Operator

And the next question is coming from Sara Senatore.

Sara Harkavy Senatore - *Sanford C. Bernstein & Co., LLC., Research Division - Senior Research Analyst*

Bernstein. I just wanted to clarify -- I wasn't sure if I caught that, but the full year guidance implies you're running kind of low single-digit positive comps this quarter. So that was question one. And then question two was, can you just talk about the value component of this? Because if I look at your food margins, there was more compression that I might have expected, certainly, given that you have a point a price on the menu. So to what extent should we anticipate that this kind of pressure on cost of goods should continue? If I kind of back into, it looks like a point of price, but you still had kind of net 300 -- I'm sorry, 3% kind of net inflation. So I'm just trying to -- try to understand what the trade-off between margin and top line will look like?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Sara, this is Joe. To the first part of our question, obviously, we don't do quarterly guidance, but I think the implications are fairly apparent and accurate with what you stated for this current quarter. And then as it relates to the margin question, yes, as we stated on prior calls, and I think you're starting to see come to fruition, we will invest in the business through margins and cost to sales is one place if you would see that. So -- and that's about the abundance move we've made in improving the quality of the food. And then when you look at promotional activity, such as the 3 for $10 that does have implications within that area. So I think the level you have seen will be relatively consistent as we kind of move through the rest of this year.

Operator

And the next question is coming from David Palmer.

David Sterling Palmer - *RBC Capital Markets, LLC, Research Division - MD of Food and Restaurants and Consumer Analysts*

RBC. Could you first touch on that gap between company stores and the franchise stores that we saw in comp store sales in the quarter? Do you see that narrowing in the future? And what were the factors that caused that to widen in that last quarter?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

David, Wyman. Yes, it was a combination of things, the biggest being just weather. Our franchise partners pretty much sit in the middle of the country, and there was quite a bit of weather that moved through the middle and then into the northeast, and again, relative to where a lot of our company restaurants are in California, Texas, Florida, the weather was significantly more challenging to them. They are also working a little bit -- they didn't all necessarily run the exact same marketing strategy. So there was a little bit of a difference there. But I think we're closing that gap. We're actually seeing that gap close now as we move through the quarter, and we're confident that it will be significantly closer as we move throughout the rest of the year.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

David, the one thing I would add, just to give you a little color to that too, is that the trajectory of their business performance throughout the quarter was very similar to ours, too, with the strengthening and kind of moving to positive territories that quarter wrapped up.

David Sterling Palmer - *RBC Capital Markets, LLC, Research Division - MD of Food and Restaurants and Consumer Analysts*

Awesome. And with regard to reimaging, that's something you've talked about perhaps getting back to at least a retouch-type reimaging. How meaningful could that be? I know we're not getting into fiscal '19, but any comments about that? And then also on loyalty, you've had some fits and starts with the type of loyalty you've done. How should we view loyalty programs now being a dragger boost or perhaps a net positive versus where you were?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Thanks, David. I will take the reimaging, and then Wyman will have some comments on your second question. But we do view it as a meaningful opportunity as we start moving into that reimage program. It will be kicking off very shortly with -- approximately in the mid-200s to 250 approximately restaurants targeted for reimage in 2019. As we have kind of updated you and have gone through the testing of that program, we have expectations for a decent mid-single-digit lift in -- from that kind of program. And our expectation is that we would see that kind of performance as we move throughout that program. And we'll keep you updated as it actually kicks into gear and provide you some more insights to '19 in future quarters.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

And then Dave, with regard to loyalty. So with the Plenti program going away, we have that opportunity to assess kind of where do we want to go next. We have the My Chili's Rewards Program and while it was a points-based program in the past, we've decided to not get into a points-based program. So we're just -- we're focusing on, first, just growing the database. We know that with the technological infrastructure we've built, with the skill of the marketers that we have and the partners that we work with to understand how to interact with our guests. Digitally, we can create a really good return and drive incrementally off of unique offers that really are compelling to the individual guest. So what we're doing right now is we're really focused on just increasing the already large size of our database or kind of in a recruitment mode, and there's a little bit of an investment involved in that. But we are absolutely convinced that the future of marketing is going to be led by digital, and we want to be on the forefront of that as well as other technology. And so that's kind of where we're headed, and we're excited about it. And I think we're posed to really leverage it in ways that others can't. When I talk about some of the differences we're seeing in the industry between large brands and maybe some of the smaller brands, I think this is one of those things that could also help drive that.

Operator

And the next question is coming from Robert Derrington.

Robert Marshall Derrington - *Telsey Advisory Group LLC - MD & Senior Research Analyst*

Telsey Advisory. Wyman, you all have invested heavily in technology over the last couple of years, whether it's propping up and improving your Curbside To Go program, with Olo refining your loyalty program, are some of the economies of the business really allowing you to kind of hold the store-level margins, I guess, stronger than otherwise would be the case, given some of the value that you're providing to consumers?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes, I mean, we've got pressure across different line items in the P&L. But I think independently, when you think about where technology can come to bear, we've definitely used it in the past, and we continue to see opportunities to use it to help us leverage labor, to be more efficient without losing that hospitality and that making people feel special culture that Chili's and Maggiano's have We also see it as a big advantage to kind of overcoming and offsetting the increased inflationary pressures on media and our marketing in traditional sense. So I think those investments help balance the P&L from that perspective, but then more importantly, they really help drive the top line. And that's what we saw this quarter with Olo kind of in our Curbside program rolled out now nationally and the marketer is able to really unleash some marketing around it to see the kind of growth that we saw 30% and more consistently in that segment. That's just -- that just is helping the top line, which then allows you to leverage the P&L, and that's the best way to do this, through traffic and top line growth. So that's the primary way we want to leverage technology, Bob.

Robert Marshall Derrington - *Telsey Advisory Group LLC - MD & Senior Research Analyst*

Quick question on Maggiano's. Basically, I think one of your local restaurants has started a program, and I'm trying to figure out if it's a (inaudible) or not, of offering an add-on or a "buy one, take one" program. I think it's an add-on price of $5 or $6 to get a second on trade similar to -- is that something -- is that one of the catalyst you see for the business as you move forward into the fourth quarter here?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

I mentioned in my remarks, Bob, that we are excited about taking our delivery program at Maggiano's to a more individual level. And so, assuming you're talking about Nashville, which is where we're testing one of those ideas and -- so we're right now about to test. But we're looking at ways to broaden the appeal of what's already a very popular program within Maggiano's to a much broader base of individual consumers.

Robert Marshall Derrington - *Telsey Advisory Group LLC - MD & Senior Research Analyst*

It's a great value. I hope you don't take it away from us.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

I would say, keep coming in, and we won't take it away.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

And I would say, Nashville is responding well to it.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes. So far so good.

Operator

The next question is coming from John Glass.

John Stephenson Glass - *Morgan Stanley, Research Division - MD*

It's Morgan Stanley. Wyman, can you talk a little bit more about the to-go business this quarter? I think you said it was 11% of sales. Remind us what it was a year ago? How much of the growth in that business is from delivery versus traditional to-go or the component pieces, whether it's online piece or traditional to-go? And how does that -- is that what is the contribution to comps? Some of your peers are talking about half of the growth in their comp is now coming from an aggregate to-go business. How is it relative to the Chili's business?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

John, so I'll give you some specifics. Obviously, we don't want to get too detailed on some things just from a competitive perspective. But obviously, to-go for both Chili's and Maggiano's is important piece of the business. So at 11%, wasn't that long ago, we were at 10%. So we're seeing that number move up quite a bit as we see close to double-digit growth across the category, across all to-go. But that's really being driven, as I stated, by the online and Curbside usage and the rollout of the new technology, which has been growing at more than 30%. So we're seeing that part of the business account for somewhere depending on the week and the month, it could be a third to half of the growth that we're seeing in the improvements in comps.

John Stephenson Glass - *Morgan Stanley, Research Division - MD*

That's very helpful.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

With regard to delivery -- sorry, John, with regard to delivery, I know that was in other part of it. As Chili's is still a very small piece of the business -- obviously, at Maggiano's, where we've invested in the delivery program for almost a decade now, it's a bigger piece -- and so we are looking to expand what we do at Maggiano's and leverage that as well as just get an understanding for the most appropriate and financially viable way to bring delivery to our Chili's guests. And so there are a lot of tests out there with a lot of third-party providers as well as a new group of really smart people within the organization kind of tasked with evaluating that. But as a percentage of Chili's business, our delivery is very, very small.

John Stephenson Glass - *Morgan Stanley, Research Division - MD*

Okay. That's very helpful. And then Joe, just on the sales leaseback, what got you over the hump to look at that? Historically, you said it wasn't as simple as tax reform that lowers capital gains or implied the friction, if you will? And is there any way to dimensionalize, for us, what the cost basis is on the properties? Or how much of a step up there would be for actualized cash versus sales price?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Can't give you any update as it pertains to the second part of your question. But to the first part, tax reform is really one of the bigger drivers there because obviously moving those statutory rates to a lower level does materially decrease the friction that would be involved in transaction. So again, we're still in the evaluation stages of that and nothing specific to announce. But that clearly changed some of the dynamics as how you would look at that kind of transaction.

Operator

And the next question is coming from Jeff Farmer.

Jeffrey Daniel Farmer - *Wells Fargo Securities, LLC, Research Division - MD and Senior Restaurant Analyst*

Wells Fargo. And just following up on John's question. So again why pursue sales leaseback as opposed to pushing that leverage level above, I think, it's 3.25% to 3.75% is your target level. It seems to me that even with an elevated level of debt that you guys would still get, potentially a better rate from your credit facility than you would from sale/leaseback. So just, again, why sale/leaseback?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

And again, I want to be clear in my comments, I said, potential capital transaction was an exclusive to sale/leaseback. You obviously have the opportunity -- Jeff, you are correct -- to look at a variety of options there. So that's the review process that we're undergoing right now.

Jeffrey Daniel Farmer - *Wells Fargo Securities, LLC, Research Division - MD and Senior Restaurant Analyst*

Okay. That's helpful. And then value has been on top of the conversation this morning. Can you share what's your value perception score trends have been with your customers over the last 3 quarters? It sounds like that's one of the things that's really driven some better traffic for you guys?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes, we have seen significantly -- a significant improvement in the value scores. They are reaching kind of the levels that were all-time for us, and we're encouraged by the composition as much of how we're getting those. And so again, base menus doing better. Obviously, the promotional offers are doing well. We're starting to see that lunch category start to move for us. And I think that's when you look at the category and you see some of the differences -- one of the -- I think your lunch presence and how much lunch kind of means to your overall business is also skewing some of that. It's a more pressured daypart, and I think that's one of the things that we're really focused on is how do we continue to drive the lunch business and be successful out and we're having some pretty good success right now, and we think we've got the right kind of momentum around that daypart. So the value proposition is kind of playing itself well, and we are seeing growth and strength in it really across the portfolio of guests.

Jeffrey Daniel Farmer - *Wells Fargo Securities, LLC, Research Division - MD and Senior Restaurant Analyst*

And then just final question. You touched on it, but how are you able to deliver on the EBITDA guidance range, the implied EBITDA guidance range, with the reduced same-store sales and restaurant level margin guidance? What sort of piece of the income statement is allowing you guys to do that? And I know we are dealing with rough ranges here.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Yes, I mean, again, I think, we are performing well within the G&A side of the equation. The rough ranges, obviously, it's trajected if the business improves. We would expect to see some of the improvement flow through to the cash flow side of the equation. But the target ranges that we anticipate to be in or close to as we go out through the rest of the year, Jeff.

Operator

And the next question is coming from Gregory Francfort.

Gregory Ryan Francfort - *BofA Merrill Lynch, Research Division - Associate*

Just going back to the value. I kind of think just the customer in casual dining comes a couple of times a year, and so there's probably some delay when you reduce prices and when that's theoretically impacts traffic. And so clearly, the lowest pricing you had in a couple of years now in this quarter. Do you think there's a lag effect? And how long do you think that normally is?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes, interesting, Greg, I cannot think of it the kind of on the opposite. We've taken price at Chili's, specifically more aggressively in the last fiscal year and kind of rolling into this fiscal year than we have in the past. And the impact of that pricing strategy or that the impact of a little more aggressive pricing had an impact on pressure on our traffic trends that we're kind of working our way through. And as we've kind of laughed that now in the late second quarter, really, third quarter, I think we've got that kind of out of way and -- with a more lower level of pricing, we're starting to see, I think, the momentum pick back up and we get pass some of those more aggressive pricing impacts to traffic. So I think we're kind of maybe talking about the same impact, but we feel it more when we aggressively price. When we put value offers out there, we're pretty specific about making sure people see them and understand what they are, so that we can get kind of some immediate impact because we obviously understand the impact of trading. It happens fairly immediate. And so it's really -- we're -- marketers are pretty good at making sure that when we put a value proposition out there, that has implications to margins and price, that we get that broadly communicated quickly. We see that visit frequency pick up right away.

Gregory Ryan Francfort - *BofA Merrill Lynch, Research Division - Associate*

Got it. Makes sense. And Joe, just one question for you. In terms of putting the debt for the refinancing on the revolver as opposed doing a longer-term bond deal, what was the thought process there? And any sort of help in terms of how you guys are thinking about that?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Yes. I think -- Greg, I think about it really more from a timing perspective. We developed the revolver to have that capacity, so that at the point of maturity, if we chose to, from a market condition standpoint, from a business evaluation, from looking at, again, the capital transaction possibilities, it's an easier move at the time of maturity, and then we can continue to evaluate the capital structure for other appropriate moves as we kind of go forward.

Operator

And the next question is coming from Karen Holthouse.

Karen Holthouse - *Goldman Sachs Group Inc., Research Division - VP*

It's Karen Holthouse from Goldman Sachs. Another question on the pricing side of things. So you've started to roll off the price increase from last year. Should we think of sort of on a go-forward basis, the strategy being to maintain sort of a gap to food away from home or full service food away from home? Or do you think that you're only -- you need sort of a 1 year or onetime pricing reset and then can kind of go back to pricing with the industry from there?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Karen, this is Wyman. I mean, I think our stated strategy is to really target somewhere in that 1.5% range, plus or minus a little bit, but to keep it in that range, which tends to be historically kind of manageable for the industry and from a guest perspective to absorb. I mean I just think historically when you look at brands that have been more aggressive without -- there are examples where in a -- the state category, where beef prices have shot up dramatically, where there may have been able to price accordingly. But in general, that seems to be the kind of pricing strategy that works best for maintaining your traffic trends and keeping your guests kind of in line with you.

Operator

And the next question is coming from Andrew Strelzik.

Andrew Strelzik - *BMO Capital Markets Equity Research - Restaurants Analyst*

BMO. So my question, if Chili's is going to sustain a positive momentum and gets back to positive traffic, hoping you can help me think through the flow-through of that better comp? You've already been asked about the (inaudible) side and the value equation. But when comps were negative and traffics been negative, you've also been matching labor to that lower sales volumes. So will you need to be adding back headcount from a labor perspective if the comps get better? Just trying to understand what the flow-through might look like.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Thanks, Andrew. I won't view it as needing to add back headcount per se. Again, as business continues to improve, volumes and traffic at restaurants continue to improves, you could see labor hours added back into the equation. We are very focused on providing good hospitality and guest experience. And that is a component of our labor model thinking. So you could see volumes kind of driving some increases in labor hours, and frankly, from our perspective, that's a good thing. But I don't envision changing it from a headcount situation per se in that regard. We're going to be very cognizant of the need to manage flow-through and improve flow-through as you kind of move through this process. We've been very focused on the traffic-driving aspects of the strategy, and we'll continue to do that. And then our operators are going to be working very diligently to manage flow-through because we're making investments back into the margin side of the business, but there are still opportunities to control expense and improve the flow-through to the bottom line.

Andrew Strelzik - *BMO Capital Markets Equity Research - Restaurants Analyst*

Okay. And then just my second question. I believe you've been fairly clear in the past on the remodels that it can still fit within kind of current CapEx thinking that there wouldn't be some outsized increase, but as you're talking about that you said mid-200s next year, does that still the thinking or might we see kind of an upward trajectory to that CapEx next year?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

I think the key comment and the keyword you just said is outsized increase. Again, we've been very consistent that you would expect to see CapEx float up somewhat, while we haven't provided a specific guidance. We will be making more capital investments through the reimage program, but I wouldn't expect it to be an outsized increase in CapEx.

Operator

And the next question is coming from Brian Vaccaro.

Brian Michael Vaccaro - *Raymond James & Associates, Inc., Research Division - VP*

Raymond James. Just a few questions, if I could. First of, back to the fiscal third quarter comp and that 60 bps of weather impact. Could you -- you mentioned Maggiano's had an outsized impact. Could you just parse that out between Chili's and Maggiano's, the weather impact, specifically?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes. I think the Maggiano's impact was kind of mid-1.5-ish kind of range, and the Chili's number was closer to the average just because of the waiting. But yes, over double the impact at Maggiano's just because of the presence and the impact of -- when weather hits Maggiano's restaurant and their banquets booked, they go away. And they don't really rebook usually because there's usually an event. And so when you lose a banquet Saturday night, that has a different kind of rebound effect than just having a soft Saturday in a typical restaurant. That kind of bounces back may be on Sunday or you pick it back up a little bit -- some of it back up a little later.

Brian Michael Vaccaro - *Raymond James & Associates, Inc., Research Division - VP*

Yes. Okay. That makes sense. And on the sale/leaseback, Joe, I just want to circle back on that. And I guess thinking about the potential use of proceeds in context of your lease-adjusted leverage ratio, what was that leverage ratio at the end of the quarter? And would you be comfortable taking that ratio above 4x or potentially even resetting your covenant, which I think is at 4.25x these days?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

We finished the quarter pretty similar to the prior quarter at 3.8x leverage. And Brian, I really don't have any further comment to make on the other -- again, that's -- we will keep you appraised if we make any changes to that or any of the other kind of financial philosophies we have.

Brian Michael Vaccaro - *Raymond James & Associates, Inc., Research Division - VP*

Okay. And then on the guidance. Joe, I'm trying to understand sort of the store margin dynamics that are implied by your updated guidance. You got comps guidance that implies returns of low single-digit positives, but it looks like the store margin guidance implies sort of a similar year-on-year decline as to what you just saw in the fiscal third quarter. Is that food cost primarily or are there some other puts and takes we should be aware of in the fiscal fourth quarter?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

I think as it relates to the fourth quarter, it should be a fairly consistent approach as we round out the year. I would -- all the combination of promotional activity, food investment, I think, will be in similar ranges for the fourth quarter.

Brian Michael Vaccaro - *Raymond James & Associates, Inc., Research Division - VP*

Okay. And then last one from me is just wanted to check in on the G&A and D&A lines. G&A dollar is flat through the first 3 quarters. Do you still expect that to be up $5 million or $6 million for the year?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

G&A is going to be impacted primarily from the final calculations on our incentive compensation programs for those individuals that run through the G&A side of the equation. I would not necessarily expect to get back to that quite increased level.

Brian Michael Vaccaro - *Raymond James & Associates, Inc., Research Division - VP*

Okay. And same question on D&A were down around $4 million though guidance was down $2 million to $3 million for the year. Is that also coming in a little bit ahead of what you were expecting or is...

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

I think -- Brian, I think you are right. That will come in a little bit head of that guidance range.

Operator

And the next question is coming from Stephen Anderson.

Stephen Anderson - *Maxim Group LLC, Research Division - Senior VP & Senior Equity Research Analyst*

I'm calling to actually parse out some of the energy markets. I know that -- going recent quarters that's been -- actually going back couple of years, I would say, drag on comps, but can you parse out like what kind of positive effect that has had on your comps? And I have a follow-up.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Yes, Steve, Wyman. So obviously, Texas and Oklahoma, after having to talk about energy markets for years, on the flip side, we are seeing them kind of lead the way out, and that's encouraging and exciting to see those markets kind of come back, especially as you know with our kind of overweighted presence in those markets. That said, we're seeing broad-based strength across the Chili's portfolio. So led by Texas and Oklahoma primarily in some of those oil markets, but really seeing some good performance in other markets. And I think if you were to look into the Black Box, you'll see, as a country, pretty good performance in California and Florida as well as Texas and Oklahoma and some of oil states. So it feels like maybe there's some of the broader economic straightening and job growth and household income growth is working its way across a pretty broad section of the country.

Stephen Anderson - *Maxim Group LLC, Research Division - Senior VP & Senior Equity Research Analyst*

I wanted to -- excuse me, a little bit -- talk about the Plenti program. I think if I remember correctly, when you first joined the program, the thrust there -- one of the key thrust was potential cost savings. Do you now not taking My Chili's Rewards back and how do you contemplate bringing some of those costs back? And on the flip side of that, I mean, do you see retaining -- regaining part of your customer data as a part of bringing back the My Chili's Rewards back in house?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Well, our first, Steve, on the -- the objective or the reason we went with the Plenti program was because of the quality of the players that were involved, right. We had American Express kind of running that program as well as Exxon Mobil and AT&T involved in it. And the objective, it wasn't really about saving cost, it was about combined leverage with really other strong brands to create a more powerful marketing model for us. The program, for a lot of reasons, just didn't never really catch on like all of us have thought. The folks at American Express, AT&T, Exxon and us all thought that we had more potential there and it just didn't resonate the way that we thought it would, and so it's been kind of put to the side. As we go forward, as I mentioned earlier, we're still committed to a direct customer relationship and leveraging digital in our marketing strategies in our team. And our investments and technology will allow us to do that. And we think we can do it as good as if not better than most. So it hasn't come without some learnings. But in that learning process, there has been some investment, but more importantly, there's been some really good knowledge to learn, and we've got a really strong team of digital marketers partnering with some really good agency partners that are helping us kind of move to that next generation of marketing.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

And Steve, as it relates to your cost piece of the equation, yes, there is reduced costs that will be seen in the restaurant expense line, offsetting with comp expenses that will be one of the components of the comp numbers we report going forward. But the critical piece is that, that database and the acceleration we're seeing in the sign-up of individuals into the loyalty program providing their e-mail addresses and becoming part of that program. So we've seen that acceleration, and that's one of the key components of being able to build that database. So...

Stephen Anderson - *Maxim Group LLC, Research Division - Senior VP & Senior Equity Research Analyst*

And are you seeing related jump in food cost when you sign-up for the program you get a free -- you get a free beverage every time you go or free sauce. I mean, can you quantify how much of a food cost hit you see from that?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

And again, it will really be a component of the comp number that we provide you going forward. And we're not seeing an impact on the food cost side of the equation.

Operator

And the next question is coming from John Ivankoe.

John William Ivankoe - *JP Morgan Chase & Co, Research Division - Senior Restaurant Analyst*

With JPMorgan. I was hoping that you identify, I guess, an average package for the 250 remodels or reimages that you're doing in fiscal '19, for us, at least focus on that part of the CapEx model?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

John, I really don't have an average package to give you. I think we're in a review process of that -- oh, with remodel, sorry, John. I thought we were going down the...

John William Ivankoe - *JP Morgan Chase & Co, Research Division - Senior Restaurant Analyst*

I would be curious to hear the answer whatever it was that you were going to answer. I don't want to take away from you.

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Sorry, getting out ahead of you, John. I think we're looking at an average package that's in the -- between the $200,000 and $250,000 per restaurant spend. There will be some components of the reimages -- some restaurants that will have a lesser spend based on number of different criteria, but most of them will be in that $200,000 to $250,000 range, John.

John William Ivankoe - *JP Morgan Chase & Co, Research Division - Senior Restaurant Analyst*

And could you remind us your customer-facing, I mean, what is going to accomplish? And I know you mentioned what you think the sales lift is going to be, but what is the customer going to see? And how, if any -- is the restaurant going to be more efficient for the employees to run it?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

John, it's -- there's 2 questions in there that you slipped out last one in. But from a consumer perspective, which is what we're really talking about, it just puts the brand in a more relevant light. It -- all the work we've done are really in the last -- almost 1.5 years. As we have worked with different versions of this reimage, it puts a bigger focus on the bar, but more importantly, opens up the restaurant to be the kind of space that is more relevant for today's consumers. I think it creates more energy. The materials that we're bringing to the work front are more contemporary for lack of a better word, not that it's a contemporary design but they are just more in today's style. And you've got a brand that's unbelievably strong, but it's 43 years old. So you got to continue to remind people that we're investing to keep it relevant for today's consumers. And today's consumer is a little different. They are looking for an experience that's got some vibrance to it, that kind of conveys the message that, "Hey, we understand what you're looking for." And then obviously, the piece that's got to sit on top of that is the hospitality and the service and the quality of the food that we provide, which this reimage doesn't do anything to hinder that. And there are some technology ideas that we are currently rolled out in restaurants, like handhelds, that we think, when coupled with this reimage or not, can also provide even better guest experience that we're continuing to work with and work through and very excited about the potential to get that laid into be more effective and more efficient, while providing a better guest experience. So the reimage itself is more customer-facing, but there are some things we're looking at that also worked to make the team members' jobs easier and actually more effective.

John William Ivankoe - *JP Morgan Chase & Co, Research Division - Senior Restaurant Analyst*

Okay, great. And then a completely separate question. Obviously, you're talking to industry trends that got better in March, they got better again in April. Certainly, in April, I mean, I think there's less of a weather, if any weather impact, and maybe consumers are finally feeling better about the excess cash that's in their paychecks at the end of every month. Whether it's through just their wages going up or whether it's through lower taxes. Sometimes, in the past, we've seen the restaurant industry benefit temporarily from these trends and then trends kind of eased again, and maybe there are other cycles where we can sustain the trends that we're seeing in April are even improved. Every economic cycle is different. There is obviously a ton of push and pulls regarding a consumers own income statement that dictates how they spend the money, including to grocery, including to independent restaurants. If it's fair for the call, what is your view of, I guess, the restaurant industry and branded casual dining as we move throughout the next 6, 12, 18 months? I mean, how are you guys feeling about just the overall macro as it relates to casual dining?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

John, we don't spend a whole lot of time trying to predict where the economy is going. It's just so far out of our control. We feel good about kind of where the economies are today for the reasons you mentioned. I think they're going to hold for the near term. So I don't know why anything that we have kind of line of sight to change that in the next 6, 8, 12 months. So that feels good. Low unemployment, more people in the workforce, higher household incomes and a consumer confidence level that's getting back to some historic levels, those are all good for the economy. They are good for the restaurant industry. What we're really more focused on is how do we gain share and grow in a very competitive environment, regardless of what the economy is doing and that's through a focus on quality, consistency and value and how are we bringing higher quality, more consistency and stronger value proposition to the consumer in a way that compels these really strong brands forward, and that's how we're going to win. If the economy gets a little softer, that's still going to be our focus. We think it doesn't really change our strategies kind of moving forward.

Operator

And the next question is coming from Greg Badishkanian.

Frederick Charles Wightman - *Citigroup Inc, Research Division - Senior Associate*

It's actually Fred Wightman on for Greg at Citi. Just a quick question on lunch. I know last quarter you'd mentioned that, that was a disappointing, but it also sounds like that for you 3 for $10 had been a bit of traffic benefit this quarter. So can you just talk about where that daypart is versus where you'd like it to be on a longer-term basis?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

It's getting there, Fred. I think the work that -- we kind of said it up last call that we're going to -- the team was going to really focus on driving some traffic back into the lunch daypart for us. It's an -- as an industry, it's the more challenged daypart out there, especially early week lunch for a lot of reasons. But just turning the marketing on and reminding people what a great offering Chili's has at lunch every day was impactful. We hadn't really gone out there with that message for a while. And then getting more specific in the promotional aspects as well as in some of the direct marketing aspects has helped move that business significantly and is a major reason why we're seeing the momentum we've talked about here from kind of where we were December/January to where we sit in March and April.

Operator

And the next question is coming from Will Slabaugh.

Hugh Gordon Gooding - *Stephens Inc., Research Division - Research Associate*

Stephens. This is Hugh on for Will this morning. Sorry for going back to digital piece, but I just wanted to quickly touch on mobile and see if we could get any updates around that business? It's contributions from really the overall to-go business. And may be any adoption metrics you could give us there?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

Yes, Hugh, it's very key component of driving the to-go business. You're seeing mobile ordering push north of 40%, so between 40%, 50% of to-go orders are being delivered consistently kind of in that range. And the year-over-year growth rates, again, I think as Wyman indicated, are exceeding 30% on a very consistent basis. So it is an increasing workhorse as it relates to the to-go business, and it is one we think is going to continue to increase and accelerate as we go forward.

Hugh Gordon Gooding - *Stephens Inc., Research Division - Research Associate*

That's great. And then just looking back at the comp, can we expect mixed run in this level for some time at Chili's. As Chili's works to kind of figure out its value footing and level of promotional activity and as we work through it, would you expect mix to tick higher from just the highlights of the new menu and more protein-driven items?

Joseph G. Taylor - *Brinker International, Inc. - Senior VP & CFO*

I think it will perform in that consistent level what you are seeing right now. There's opportunities at any given quarter based on our promotional sequencing, contest, things of that nature. But I think this is a pretty indicative range to possibly may be and slightly below this range tick.

Operator

The next question is coming from Joshua Long.

Joshua C. Long - *Piper Jaffray Companies, Research Division - Assistant VP & Research Analyst*

It's Piper Jaffray. My question was going back to the comp trends. It was encouraging to hear the geographic spread and how everything was more or less improving in step. I was curious if that was similar to on a weekday daypart basis while I know you mentioned kind of, obviously, early week lunch is a tough part of it. But just curious on kind of how the performance and improvement has been trending kind of on a week or a daypart basis?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Jeff, we have seen improvement across all the dayparts, early week as well as late week lunch and dinner. So again, I think from a relative perspective, it's been broad-based improvement in the business. From an absolute perspective, that early week lunch is still the more challenged daypart. I think it's the more challenged daypart. Again, I think I've said it a couple of times now in the industry that, especially in casual dining as you see some of the strength in the fast food guys as well and they continue to do a good job at growing their business. We know that, obviously, it's a heavier lunch crowd. So for those reasons as well as a few macroeconomic and demographic issues, we think the early week lunch is the bigger challenge.

Joshua C. Long - *Piper Jaffray Companies, Research Division - Assistant VP & Research Analyst*

That makes sense. I appreciate giving that color and clarification. And I wanted to go back to your earlier comments, Wyman, in terms of just that kind of split between some of the larger chains and smaller chains and how that performance is a little bit bifurcated in your favor? Was curious, if you had -- if we can dig in to or kind of seeing where some of that improved performance for your brand is coming from. If it -- are you getting that incremental visit on kind of guests that had more or less than your core guests and you're getting them in a little bit more often? Or if perhaps you're giving in -- cashing a wider net now and getting some people that -- some guests coming that maybe had been a little bit more lapsed or just not as in connected -- not as connected with Chili's? It might be a little early, but just curious on kind of how are you seeing that performance from a guest set?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

It's actually we do track that, Joshua, and we're seeing both -- we're seeing increases in usage frequency with our heavier users and with some -- with our lighter users, which is encouraging, right, to get some of those lighter users back into the restaurant to experience what we think are stronger menu offerings and some better execution and hospitality is what's got us excited about kind of the potential to continue to get them back in more frequently. So we're seeing in both our heavy and our light users.

Operator

And we have a follow-up coming from Robert Derrington.

Robert Marshall Derrington - *Telsey Advisory Group LLC - MD & Senior Research Analyst*

Wyman, I'm trying to understand some of your numbers here, and Joe, maybe, you can help me out. As we look at the franchise and other revenue, the royalties as far as the company had been trending lower on an annual basis -- as we look at the company's overall numbers, yet your unit counts are increasing fairly substantially. Are the new international and are franchise locations principally lower average unit sales stores or the franchise royalties lower on those? How do we think about that?

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

No. Bob, no, they're not. To take the second part, they're fairly consistent across the board. Remember that the franchise and other revenue is a large component of things. I mean, you have the royalty income in there, you have development fee income in there, you have banquet fee income. All the gift card related expenses and incomes flow through there, so there's a -- and our gaming revenues. There is a lot of different puts and takes within that category. So I want to construe any change up or down at any given period to just the royalty piece of the equation.

Operator

And there were no other questions from the lines.

Wyman T. Roberts - *Brinker International, Inc. - CEO, President & Non-Independent Director*

Well, great. We appreciate everybody's attendance this morning. And we look forward to talking to you again in August with our year-end conference call. And everybody, have a good day. Thanks.

Operator

Thank you, ladies and gentlemen. This does conclude today's conference call. You may disconnect your phone lines at this time, and have a wonderful day. Thank you for your participation.