Chipotle Mexican Grill, Inc. (NYSE:CMG) Q2 2024 Earnings Conference Call July 24, 2024 4:30 PM ET

Company Participants

Cindy Olsen - Head, IR and Strategy
Brian Niccol - Chairman and CEO
Jack Hartung - CFO and CAO

Conference Call Participants

David Tarantino - Baird
Sara Senatore - Bank of America
Dennis Geiger - UBS
Peter Saleh - BTIG
Christine Cho - Goldman Sachs
Sharon Zackfia - William Blair
John Ivankoe - JPMorgan
Andrew Charles - TD Cowen
Lauren Silberman - Deutsche Bank
Jon Tower - Citi
Brian Harbour - Morgan Stanley
Danilo Gargiulo - Bernstein
Chris O'Cull - Stifel

Operator

Good afternoon, and welcome to the Chipotle Second Quarter Fiscal 2024 Earnings Call. All participants will be in listen-only mode. [Operator Instructions] After todayÂ's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being record.

I would now like to turn the conference over to Cindy Olsen, Head of Investor Relations and Strategy. Please go ahead.

Cindy Olsen

Hello, everyone, and welcome to our second quarter fiscal 2024 earnings call. By now, you should have access to our earnings press release. If not, it may be found on our Investor Relations website at ir.chipotle.com.

I will begin by reminding you that certain statements and projections made in this presentation about our future business and financial results constitute forward-looking statements.

These statements are based on management's current business and market expectations and our actual results could differ materially from those projected in the forward-looking statements.

Please see the risk factors contained in our annual report on Form 10-K and in our Form 10-Qs for a discussion of risks that may cause our actual results to vary from these forward-looking statements.

Our discussion today will include non-GAAP financial measures. A reconciliation to GAAP measures can be found via the link included on the presentation page within the Investor Relations section of our website.

We will start todayÂ's call with prepared remarks from Brian Niccol, Chairman and Chief Executive Officer; and Jack Hartung, Chief Financial and Administrative Officer, after which we will take your questions. Our entire executive leadership team is available during the Q&A session.

And with that, I will turn the call over to Brian.

Brian Niccol

Thanks Cindy and good afternoon everyone. Before I begin discussing our results, I need to recognize and congratulate Jack Hartung on his nearly 25 years with Chipotle and roughly 80 earnings calls with all of you.

I want to thank him for being a great friend, a terrific leader and a champion for our purpose and brand. I'll say a few more words about Jack and Adam before I hand it over to him.

Now, turning to our results. The second quarter was outstanding as successful brand marketing, including the return of Chicken Al Pastor as a limited time offer drove strong demand to our restaurants.

Additionally, our focus and training around throughput paid off as we were able to meet the stronger demand trends with terrific service and speed in -- driving in Â– driving over an 8% transaction comp in the quarter.

For the quarter, sales grew 18% to reach nearly $3 billion, driven by an 11.1% comp. In-store sale grew by 24% over last year. Digital sales represented 35% of sales. Restaurant level margin was 28.9%, an increase of 140 basis points year-over-year. Adjusted diluted EPS was $0.34, representing 36% growth over last year, and we opened 53 new restaurants, including 46 Chipotlanes.

Before I give an update on our five key strategies, I want to take a minute to address the portion concerns that have been brought up in social media. First, there was never a directive to provide less to our customers. Generous portion is a core brand equity of Chipotle. It always has been, and it always will be.

With that said, getting the feedback caused us to relook at our execution across our entire system with the intention to always serve our guests delicious, fresh, custom burritos, and bulls with generous portions.

To be more consistent across all 3,500 restaurants, we have focused in on those with outlier portion scores based on consumer surveys, and we are reemphasizing training and coaching around ensuring we are consistently making bowls and burritos correctly.

We have also leaned in and reemphasized generous portions across all of our restaurants as it is a core brand equity of Chipotle. Our guests expect this now more than ever, and we are committed to making this investment to reinforce that Chipotle stands for a generous amount of delicious, fresh food at fair prices for every customer, visit.

The good news is that we are already beginning to see our actions positively reflected in our consumer scores and our value proposition remains very strong. We believe our focus on operations, including throughput as well as terrific marketing and menu innovation, have strengthened the brand and our value proposition. And we will continue to listen to and treasure our guests to earn every transaction.

I will turn to our five key strategies that help us to win today while we grow our future. These strategies include running successful restaurants with a people accountable culture that provides great food with integrity while delivering an exceptional in-restaurant and digital experiences, sustaining world-class people leadership by developing and retaining diverse talent at every level, making the brand visible relevant and love to improve overall guest engagement, amplifying technology and innovation to drive growth productivity at our restaurants, support centers and in our supply chain and expanding access convenience by accelerating new restaurant openings in North America and internationally.

First, I will start with running successful restaurants. As I mentioned, the improvements we have seen in throughput positions us well to meet the strong demand we experienced in the second quarter, driven by what we call burrito season or our peak seasonality as well the success of Chicken al Pastor. We often are asked why throughput is such an important operational KPI for Chipotle. So I thought I would begin by expanding on this.

It is the outcome of a strong operational engine that delivers a great experience for our teams and our guests. In order to deliver exceptional throughput, restaurants need to be fully staffed and properly deployed.

Our crew needs to complete all food prep on time and they need to be well trained execute the four pillars. This results in a better overall experience for our crew, which leads to more stability and, therefore, more experienced teams that execute better every day. And for our guests, faster lines with hotter, fresher food. This type of guest experience strengthens our value proposition and drive incremental transactions.

Over the last year, we have improved our tools and training to deliver exceptional throughput. This included rightsizing the cadence of digital orders during peak periods and enabling our restaurants to see in real time at the point of sale, the number of entrees in each 15-minute interval. This has received tremendous feedback from our restaurant teams.

It has helped to accelerate momentum as it creates excitement and allows our teams to celebrate in a moment when they achieve their goal. And our GMs can coach in the moment when they fall short. In fact, one of our field leaders in New York have 5 five of his eight restaurants achieved their throughput goal in the second quarter, which compares to just one of his restaurants a year ago.

While we are seeing progress, we still have a lot of opportunity to increase the percentage of restaurants executing the four pillars. Expo is a great example as it is the most impactful pillar.

As a reminder, Expo is the crew member between Salsa and Kash, who helps expedite the bagging and payment process. restaurants within Expo in Expo in place are averaging five incremental entrees in their peak 15 minutes, yet we only see a little over half of our restaurants with place during peak periods. This is certainly better than where it was a couple of quarters ago, but it should be a lot higher.

The good news is that I strongly believe we have the right leaders in training in place to keep the momentum going as we continue to gather the data on the execution of the four pillars and provide feedback and coaching on a weekly basis, I am confident throughput can go much higher.

This brings me to world-class people leadership. As we mentioned last quarter, crew and GM turnover is at some of the best levels I've seen since I joined the company. And the stability is allowing us to develop and grow our people pipeline to achieve our goal of promoting over 90% from within. We have many inspiring stories at Chipotle of crew members who have grown with the company to become some of our top leaders.

In fact, our recently promoted regional Vice President started as a crew member 25 years ago. She moved to the United States at 14 years old without knowing English. At 19, she started working at Chipotle and has moved her way up, including spending time in a language development role, supporting other employees at Chipotle to learn English as a second language.

Her people-first mentality is what has made her so successful at hiring, developing and retaining many of our best leaders. And she has two sisters that have each been with Chipotle for over 15 years and our top-performing field leaders.

With the addition of her role, we now have three of our 10 regional vice presidents who started as crew members and have made their way up to leading a region and managing over a $1 billion business.

These stories really do inspire our entire organization, as the opportunity to develop and grow within Chipotle, along with our industry leading benefits and pay, enables us to attract and retain exceptional people. In fact, as we look to expand to 7,000 restaurants in North America, we will be adding an RVP nearly every year along with hundreds of restaurant leadership roles.

Finally, our 50-to-1 stock split: One of the largest in New York stock Exchange history enables our employees' and others to purchase whole shares, at more affordable prices and gives us more flexibility to compensate our top performers in stock, all with the goal to have more employees participate in the financial success of our company. It really is an exciting time to be part of Chipotle.

Now, turning to marketing, the Chipotle brand continues to gain momentum as we focus on exceptional operations and making the brand more visible, more relevant, and more loved.

Chicken Al Pastor is a great example as it once again surpassed our expectations, reaching over a 20% incidence rate and more importantly, driving incremental transactions and spend.

Similar to Carne Asada, we proved that when we bring back a limited time offer, we were able to make it more delicious with seamless execution. And while Chicken al Pastor will end later this summer, I am excited to share that we will be bringing back Smoke Brisket this fall for a limited time.

Brisket was among the most requested in many items, as our guests love the combination of Smoked Beef, Charred on the grill and finish with the Brisket sauce made with smoky chili peppers. It took a huge cross-functional effort across supply chain, culinary finance and marketing to bring back this delicious LTO.

Our marketing team also continues to find creative ways to generate excitement drive more engagement around our annual promotions. In the second quarter, we had a record-breaking National Burrito Day, where gamified

promotion resulted in Chipotle's best sales and digital sales day ever. It also drove an influx of new and lapsed customers and was the best enrollment day of the year for our rewards program.

I'm also thrilled to share that later this week, team Chipotle will be visible on the world stage as we leverage our real food for real athletes' platform for those competing in Paris. We highlighted the inspiring journeys of Anthony Edwards, Sophia Smith, Taylor Fritz, Sara Hughes and Jagger Eaton.

Their go to Chipotle meals and Howard Greens have been a key component of their training regimens. We will also bring back our gold foil for burritos for a limited time in both North America and France to celebrate all the athletes competing.

Shifting to technology and innovation, I want to provide an update on a few of our in-restaurant initiatives starting with the Dual-Sided grill. Over the last year, the Grill has been in 10 restaurants, and we have received consistent feedback that our teams and our guests love it.

The grill can cook the chicken and steak in, under half the time it takes on the Plancha with consistent execution and the same sear and char. It also maintains better moisture resulting in juicier chicken and steak with less waste. And for our teams, it takes one of the most complex positions in our restaurants and significantly improves the learning curve.

Finally, for high-volume restaurants, it opens up capacity and drives efficiency during morning prep, as chicken and steak can be closer to serving. We are in the process of rolling out the dual sided grill to an additional 74 high-volume restaurants this year, and we'll continue to evaluate the economics prior to rolling it out further across the organization. Additionally, our automated digital makeline in Autocado are making their way through final checks ahead of being pilot tested in their first restaurant.

Our food safety and operation teams have worked closely with our technology teams to assure that the design takes into account things like cleaning, speed and accuracy as well as maintaining our high culinary standards. The next step will be to get each device into a restaurant to continue to learn and iterate part of our stage gate process.

I'm excited about each of these initiatives, and I strongly believe we will see some impactful back-of-house changes in the years to come, that will help to improve consistency in our restaurants and drive a better overall experience for our teams and our guests.

IÂ’m also proud Chipotle continues to be a learning organization. Using the stage gate process is our way to drive discipline around what ultimately gets rolled out. I'm confident this process will further strengthen Chipotle as a leader in technology and innovation.

Now moving to our final strategy, which is to expand access and convenience. In North America, we remain on track to open 285 to 315 new restaurants this year, and our openings remain strong across all markets.

While our time lines remain consistent to last quarter, our development team continues to see groundbreaks meaningfully higher compared to last year, which should help smooth the cadence of openings as we get into the back half of the year.

I also wanted to share an update on our partnership with the Alshaya Group. Our first restaurant in Kuwait has been open for several months and continues to have strong performance.

The good news is that the feedback from guests is that the culinary experience is right on par with North America, which is fantastic to hear. It also tells me that when we execute our culinary and delivering an exceptional experience for our guests, Chipotle's brand resonates across geographies. We look forward to opening our second restaurant in Kuwait as well as expanding into Dubai with the Alshaya Group later this year.

To close, our crew members, GMs and field leadership delivered an excellent second quarter helped by our committed support centers that enable restaurants to better succeed. We are very fortunate to have a clear purpose and an organization that is full of talented people at all levels. It is exciting to see the progress we have made so far, and I am confident there is much more growth in front of us.

Finally, I want to spend a few minutes reflecting on my time with Jack and his extraordinary 25 years at Chipotle. Jack is just as passionate about our brand and our purpose as he is about protecting our economic model.

I know you all agree with me that he is one of the best CFOs in the business and has played an instrumental role in growing Chipotle from under 200 restaurants to over 3,500 restaurants, investing in our premium ingredients, and supply chain, protecting our exceptional value proposition and delivering industry-leading economics and returns.

As Jack always says, these three characteristics are incredibly difficult to replicate, premium ingredients, affordable prices and attractive margins. Beyond that, he has developed an exceptional finance team, including Adam Rymer, who will become our next Chief Financial Officer.

Over the last 15 years, Adam has reported directly or indirectly to and been mentored by Jack in preparation for this role. And importantly, he is just as passionate about our brand, our purpose and protecting our economic model.

I'm highly confident he is the right leader to become our next CFO, and that it will be a smooth transition. So again, thank you, Jack, for your friendship, leadership and so many contributions to Chipotle.

And with that, I'll turn it over to you.

Jack Hartung

Thank you, Brian, for those kind words. I'm extremely fortunate to have had the privilege and honor to serve Chipotle, our employees our shareholders for all these years. While retiring was one of the hardest decisions, it was also one of the easiest I've ever had to make.

It was hard because Chipotle is a special brand, a special company and it's full of special people. But it was also easy because I know Chipotle is in great hands with a family of smart, talented people who are committed to our purpose to cultivate a better world.

It's also easy because I have a large and growing extended family, and I treasure the time I get to spend with every one of them, and now we'll have the chance to enjoy even more special experiences with them.

I'm delighted that Adam Rymer will be our next CFO, and as Brian mentioned, Adam has worked with me for 15 years, and I can tell you he's a very talented leader who knows our brand and our business well, and I'm confident in his ability to help lead Chipotle to the next level.

In addition, Jamie McConnell will be elevated to our Chief Accounting and Administrative Officer. And since joining Chipotle six years ago, Jamie has provided great leadership, built strong teams and is well prepared to serve in our new role.

With that said, I'll turn now to our quarterly results. Sales in the second quarter grew 18.2% year-over-year to reach about $3 billion as comp sales grew 11.1%, driven by 8.7% transaction growth. Restaurant-level margin of 28.9% increased about 140 basis points compared to last year.

Earnings per share adjusted for unusual items was $0.34, representing 36% year-over-year growth. The second quarter had unusual expenses related to unrealized loss on investment and an increase in legal reserves, which negatively impacted our earnings per share by $0.01, leading to GAAP per share of $0.33.

Sales comps were highest in April, driven by the Easter shift, a strong reaction to the return of Chicken al Pastor and several successful activations, including National Burrito day. Comps settled back to around 6% in June, and continue to be driven by positive transactions.

July has been more difficult to read so far due to the fourth holiday, weather disruptions in Texas and the impact from a recent technology outage, but we believe the underlying trend remains similar to June.

We are maintaining our full year comp guidance of mid- to high single-digit. And as a reminder, we will roll off about 3 points of pricing in early Q4 as we lap our menu price increase from last year.

Before I go through the individual P&L line items, I want to give an overview of what to anticipate. We expect our margins will be under pressure for the next couple of quarters. Most, if not all of this pressure is seasonal, temporary, or it's an investment that we can offset through efficiencies, and we believe our industry-leading margin structure is still intact.

I'll now go through each of the key P&L line items, beginning with cost of sales. Cost of sales in the quarter were 29.4% in line with last year Benefit of last year's menu price increase was offset by inflation in avocados, increased oil usage and higher incidence of beef as a result of the continued success of Braised Beef Barbacoa marketing initiative.

For Q3, we expect our cost of sales to be just below 31%. About one-third of the step-up is due to the higher protein costs as we roll out Chicken al Pastor and then launched Smoke Brisket later in the quarter.

About one-third is due to an uptick in dairy and avocado prices and the final one-third are about 40 to 60 basis points is an investment we are making as we focus on outlier restaurants to ensure correct and generous portion. We expect this investment will ease from these levels somewhat. We also believe that we can offset the remaining investment with efficiencies and innovation over time.

While avocado prices are higher than the very favorable levels we have seen over the past several quarters, this is in line with our expectations from earlier this year. Additionally, we are less impacted by the recent volatility in the Mexican avocado market, as our supply chain team has done a fantastic job of diversifying our exposure, and in the third quarter, the majority of our avocados come from Peru.

Outside of avocados and the protein mix shift, we anticipate underlying cost of sales inflation will be in the low single-digits range for the remainder of the year.

Labor costs for the quarter were 24.1%, a decrease of about 20 basis points from last year, as the benefit from sales leverage more than offset wage inflation. For Q3, we expect our labor costs to be in the low 25% range due to seasonally lower sales, with wage inflation to remain at about 6%.

And as a reminder, about half of the wage inflation is due to the nearly 20% step-up in wages in California as a result of the increase in minimum wage for restaurant companies like ours that took effect in April.

Other operating costs for the quarter were 12.9%, a decrease of about 100 basis points from last year. The decrease was primarily driven by sales leverage. Marketing and promo costs were 2.1% of sales in Q2. And in Q3, we expect marketing costs to remain in the low 2% range with the full year to be in the high 2% range.

In Q3, other operating costs are expected to be in the high 13% range, due to seasonally lower sales and higher seasonal expenses like utilities and maintenance and repair. Based on these expectations provided, we anticipate restaurant level margin to be around 25% in Q3.

As I mentioned earlier, some of the pressure is seasonal, like the shift from Chicken al Pastor to Brisket. Some is temporary like the higher prices in avocados and dairy, which if they persist, we can address with menu prices overtime.

And finally, we're confident that the investment we're making to ensure we are delivering correct and generous portions can be offset by efficiencies and innovation overtime.

G&A for the quarter was $175 million on a GAAP basis or about $171 million on a non-GAAP basis, excluding $4 million increase in legal reserves. G&A also includes $122 million in underlying G&A, $43 million related to non-cash stock compensation and $6 million related to higher bonus accruals and payroll taxes and equity vesting and exercises.

We expect our underlying G&A to be around $128 million in Q3 and step-up each quarter as we make investments in people to support ongoing growth. Anticipated stock comp will be around $40 million in Q3, although this amount could move up or down based on our actual results.

We also expect to recognize around $6 million related to higher bonus accruals and employer taxes associated with shares that vest during the quarter, bringing our anticipated total DNA in Q3 to around $175 million.

Depreciation for the quarter was $84 million, or 2.8% of sales, and we expect depreciation to step up slightly each quarter, as we continue to open more restaurants.

Our effective tax rate for Q2 was 25% for GAAP as well as for non-GAAP. Our effective tax rate benefited from option exercises and equity vesting above the grant values. And for fiscal 2024, we estimate our underlying effective tax rate will be in the 25% to 27% range, though it may vary based on discrete items.

On June 26, we successfully completed our 50-to-1 stock split: One of the largest in New York Stock Exchange history. We believe this will make our stock more accessible to our employees as well as a broader range of investors.

Our balance sheet remains strong as we ended the quarter with $2.5 billion in cash, restricted cash and investments with no debt. During the quarter, we repurchased $151 million of our stock at an average price of $63.52.

At the end of the quarter, we had nearly $650 million remaining under our share authorization program. We opened 53 new restaurants in the second quarter, of which 46 at Chipotle.

We continue to anticipate opening between 285 to 315 new restaurants in 2024 with over 80% having at Chipotle, and we remain on track to move towards the high-end of the 8% to 10% range by 2025, assuming time line conditions do not worsen.

To close, I also want to thank our employees for all their hard work in driving our strong results and for continuing to build and grow Chipotle. I also want to reflect how our historic 50-for-1 stock split.

When Chipotle went public at $22 per share -- I was very optimistic that we have a special brand with a tremendous growth opportunity. I'm not sure I could have ever imagined then that we would split the shares at just over $3,200 per share, but I did envision that we would reach over 3,000 restaurants, as we have today in the U.S.

And today, I know we have a special brand with industry-leading economics and returns. I'm also just as optimistic about our growth opportunity to reach 7,000 restaurants in North America and to expand internationally.

And we further our purpose of cultivating a better world we'll continue to drive extraordinary value for our guests, our employees and our shareholders. It is truly and exciting time to be part of this purpose-driven company with seemingly limitless opportunity.

And with that IÂ’ll open lines for your questions.

Question-and-Answer Session

Operator

We will now begin the question-and-answer session. [Operator Instructions]

The first question comes from David Tarantino with Baird. Please go ahead.

David Tarantino

Hi. Good afternoon. First, Jack, congratulations on an amazing career at Chipotle. And you're going to be missed, and we look forward to working with Adam going forward.

Jack Hartung

Thanks David.

David Tarantino

So, my question is about the sales trends you called out, I think you said the comps moderated into the kind of 6% ballpark in June, and you think that underlying trend is carried over into July.

While that's very good relative to what we're seeing from a lot of brands, it is slower than what you were running previously. So, I just wanted to get your thoughts on why you think you saw that slowdown -- whether it's macro or something inside the business that may have caused that?

Brian Niccol

Why don't I start and then Jack can fill in. The -- look, first of all, David, I would tell you the quarter was really spectacular. And when we look at brand metrics, they've never been stronger. So, value, food scores all the key metrics to make sure that the brand is in a good spot really continue to improve throughout the quarter.

And then from an operating standpoint, I don't know if you've been to our restaurants recently, but I think the teams are doing a terrific job on continuing to deliver quick culinary grade throughput.

And then, obviously, we mentioned in our earlier comments, we've doubled down on making sure we're also providing great portions, which is, I think, a key equity for this business as well.

One of the things we've seen, which is consistent with what we saw last year, is this kind of seasonal move with kind of the summer change of behaviors. And so obviously, we're trying to understand what that looks like because it appears to be new trends since coming out of COVID. So, that's one piece of the puzzle.

And then obviously, we're trying to understand if there are any macro things going on as well. But the one thing we know for sure is the feedback on the business from our customers has been great value, great culinary and improving speed. And those are the things we can control, and those are the things we're going to forward. Jack, I don't know if you want to add anything.

Jack Hartung

No, I mean, just to add some more text to like seasonality things like July 4 used to be a weekend and now it looks like it's two weekends. So, it looks like the combination of there's a holiday and then work from home is more acceptable. Now it just seems like the holidays, it used to be three or four days or so. It seems like they're stretching out a little bit.

We even saw for the first time ever on Juneteenth, we saw a little softness there as well. So, we wonder if that's also kind of a work-from-home environment as well. So the last couple of summers have been very hard to predict. And so we think that's definitely a big part of what we're seeing.

David Tarantino

Great. Thank you very much.

Operator

The next question comes from Sara Senatore with Bank of America. Please go ahead.

Sara Senatore

Thank you. First of all, congratulations to both Jack and Adam. I've enjoyed working with both of you, but the question I have first is just a quick follow-up. If you could just maybe talk a little bit about the composition of the price mix and how you're thinking about that going forward, given some of the reinvestments that you are making?

And then also wanted to get a sense of store growth and how that is progressing. Just I know there have been endemic problems across the industry, but the goal was to get the growth rate higher and perhaps into that 10% range next year. So, any updates there? Thanks.

Jack Hartung

Yes, I'll start with the components of the comps, Sara. Transactions were up 8.7% during the quarter. We also had a menu price increase effectively was 3.3%. That was 3% that we took, effectively a 3% that we took last year, and then we had the 1% effective that we took for the FAST Act as well.

And we did have a negative mix, and the negative mix was based on group size. The negative mix was 1%. Group size was down about 2%, but that was offset by we did have some add-ons, mostly in chips, queso, and extra meat as well.

What we're seeing as we moved into June, we're still seeing transactions be the main driver. So, transactions were in the 3%, 3.5% during the month of June. And then on openings, I mean, we're still on track, Sara.

We're not seeing the timelines really change at all. We did see some modest improvements so far this year, but the pipeline is very robust, and we feel good about the openings for this year. If that continues, just based on the inventory building alone, and if timelines don't worsen, we think we can get close to, if not all the way to that 10% in the next year.

Sara Senatore

Got it. Thank you. And just pricing for the rest of the year?

Jack Hartung

So, we have the 3% from last year that runs out in the middle of October. We'll continue to have California. Right now, we have no plans for further pricing. I mean, we'll look at how the rest of the next few months unfold.

We'd love to get through the rest of the year based on what's going on, and again, we don't know how much is seasonality, whether there's something bigger going on. But it'd be great to not have to take any price for the rest of this year.

Sara Senatore

Thank you.

Operator

The next question comes from Dennis Geiger with UBS. Please go ahead.

Dennis Geiger

Great. Thanks very much, and Jack and Adam, congratulations to you both. Just wanted to ask Jack a little bit more on the margin commentary that you made, specifically as it relates to some of that pressure over the coming quarters. If you could dive in a little more to some of the moving pieces there, and maybe some of the efficiency offsets that you spoke to? Thank you.

Jack Hartung

Yes. So, there's three main buckets. We've got inflation. Inflation generally has been relatively benign. We have two items we called out, avocado and dairy. Both of those ingredients we do expect either near the end of the year or into early next year. We think those will normalize.

Avocados, as you guys know, has been really a benefit. We've had great avocado prices for the last several quarters. And so even the current avocado prices we're seeing right now are more in the normal range, but we think that those will ease through the end of the year or into next year, so both of those we feel good about. We do have pricing power, so we'll watch that very closely, and at some point in the future we'll be able to offset that.

The other item that we talked about, Brian mentioned, we decided that that this brand equity called Generous Portions is something we don't want to take for granted. We don't want to take something that's been a positive for all these years and then have it turned out to be a negative because of some of the social media comment.

So, we've made this investment, we'll continue to make the investment. We already have a number of initiatives underway. Some of them are operational. Some of those are supply chain efficiencies.

We won't go into details of what those are, but we do think over the next couple of quarters that we'll be able to see some of efficiencies and I think that's really in terms of where our margins are and what we think--

Dennis Geiger

Just to move from Chicken Al Pastor.

Jack Hartung

Yes. I mean, that's clearly temporary.

Dennis Geiger

Yes.

Jack Hartung

I mean, you have the mix shift. Clearly that's going to be in LTO, once we move from brisket into the next LTO, especially if it's a chicken. Not only will that reverse, but it'll turn into a positive for us.

Dennis Geiger

Make sense. Thanks and congratulations.

Operator

The next question comes from Peter Saleh with BTIG. Please go ahead.

Peter Saleh

Great. Thanks. I did want to ask about labor, if I could. I think, Brian, I think you mentioned a little over half of the units with an expeditor during peak hours. What's the holdup in terms of expanding the expeditor to more units, because it feels like that's a key driver of throughput? Is labor just really tight? Is there a lot of turnover? Just any thoughts around that would be helpful. Thank you.

Brian Niccol

Yes, sure. So, look, the good news is we've made progress to get the 50%. The other piece of good news is, we've got experienced in the past. We've been able to get to that number closer to 70%-plus.

So, I'm confident with our operational leadership that's going on in the field right now, and here's a key piece of us think that gives us the ability to improve from where we are. We have really great staffing levels right now with turnover at some of the best levels it's been to-date.

And so the fact that we're getting these teams to be, I would say, more cohesive, more centered on the culture of great throughput, combined with great culinary, I'm confident that these teams will continue to improve.

The other thing, too, you guys might have seen is we talked about this, giving our teams the visibility through reporting has really enabled them to enhance their performance. And I think just repetition using the tools that we have, and then just making sure that we don't have any real disruption to what the organization needs to be focused on.

I think we've done a nice job of keeping the teams focused. If you look at our leadership hierarchy, I think you talked to anybody in the operational leadership hierarchy. They all know we want great deployment. We want great culinary. We want great throughput. We want great culture.

And like you, I wish it would go faster. I'm sure the good news is that we're making progress. And that's what I continue to keep an eye on. And I continue to make that we're staying consistent with our message. And we're supporting the teams with tools to set them up for success.

Operator

The next question comes from Christine Cho with Goldman Sachs. Please go ahead.

Christine Cho

Thank you so much. Congratulations Jack and Adam and congrats on a great quarter. I just wanted to get -- to pick your brain on the overall industry trying to win traffic share with discounts and promotions.

And I think you mentioned that to pull a value proposition is still very strong. But do you see any shift within the consumers that you can highlight? And specifically, I think a question for Brian. I think the last instance when we had this pretty fierce price competition, you were kind of on the other side of the fence.

So, any key lessons you would take away from that experience back then? And how that applies to your plans going forward in navigating through this environment? Thank you.

Brian Niccol

Yes. So, look, there's a lot there. But I'll start with -- I think I've said this over and over again. The thing that we need to make sure we do really well is great culinary, great burritos and bulls and treasure every single guest that comes into our restaurants, whether it's in-line or online. And when we do that, we see our value scores our brand become more loved.

And one of the things that I keep an eye on closely is, are we gaining market share? And what's great to see is we're gaining market share every month, okay? So as we stay focused on executing Chipotle's core business, we see the results not only in the comp and transactions that we're delivering, but also the market share gains that we're making.

And I've said this before Chipotle is not built on this idea of promotional footballing prices, okay? Chipotle is built on this idea of great culinary, exactly how you want it and with great speed.

And look, weÂ’ve had a simple idea. Great food done fast. We keep executing against that simple idea. I think we'll continue to get market share. And I think our value scores will continue to go up and our team will continue to be successful. And -- obviously, we've got to let other people play how they want to play. We're going to play our offense throughout process.

Operator

The next question comes from Sharon Zackfia with William Blair. Please go ahead.

Sharon Zackfia

Hi. Good afternoon. Thanks for taking my question. I guess just following up on that. I think in the prior few quarters, you had talked about kind of outperforming amongst lower-income consumers.

And I apologize if you mentioned that, it's a really choppy connection on my end. But are you still seeing that kind of strength across income cohorts? And on the Brisket, is that something we should expect, Jack, to impact the fourth quarter as well? Thanks.

Brian Niccol

So, I'll answer your first question. The good news is we are seeing transaction growth from every income cohort, which I think speaks to the strength of our brand and value proposition. And then as we continue to march forward, our goal is to continue to give people the bowls and burritos that they want at the speed that really delights them.

So, hopefully, that continues to resonate with every income cohort. To-date, it has -- and from what we see in our consumer research, it will continue to delight every income cohort. On your Brisket question, I'll let Jack jump in on that.

Jack Hartung

Yes, Sharon, what I can tell you is there will be an impact, but there's other things going on as well. So, our food costs -- we expect our food cost to be similar in Q4 as Q3. So, not another up.

Sharon Zackfia

Thank you.

Operator

The next question comes from John Ivankoe with JPMorgan. Please go ahead.

John Ivankoe

Hi. Thank you. The question was on the automated digital make line. Just in terms of what you've seen in your cultivate center and your culinary center, how scalable is this machine?

In other words, if you do decide and like what you see in the stage-gate process, how fast could this potentially be nationally? Does your equipment supplier have the capacity to kind of get up and running for the entire system is kind of the first question?

And then secondly, related to that, if we are talking about consistency and speed as being two things that you want to do really well, it does seem like an automated make line would be perfect for that, not just on the digital make line, but even putting it into the front counter as well, whether kiosk ordering or app ordering or whatever that case may be. Would that be considered as part of an early stage gate process as well once you establish it on the back make line? Thank you.

Jack Hartung

Yes, and thanks for the question. Obviously, we're really excited about Python and the automated digital make line. We will have that in a restaurant probably here at the end of August, early September, somewhere around there, which will be really exciting to see.

Look, obviously we want to stay after consistency and speed. Those are two equities of the brand that are really important. The good news is we've got a bunch of different initiatives in the stage gate process.

So, look, I never like to have all my eggs in one basket, right? And what I'm really delighted about is we've got things that make us more efficient with prep, whether it's avocado, a veggie slicer, a dual sided grill, looking at modifications to our rice cooker, our fryer equipment.

So, there's a lot of things going on back at house to make us more effective culinary-wise, prep-wise, which then sets us up to be successful consistently on the front line and the digital make line. I've talked about these things also where we're also experimenting with AI and vision to ensure that our teams get the support.

I'm actually reading a great book right now, it's called Co-Intelligence, it talks about how you use AI as a partner. And that's really what, you've heard us talk about this, is co-biotics, right? I think now this is, I like this term co-intelligence, to help our teams be more effective with forecasting, executing every single bowl correctly, bringing things up exactly correctly.

So, look, I'm really excited about all the things we have in the pipeline. Obviously, we've spent a lot of time talking about hyping because it's probably the most visible, it looks pretty darn cool too.

But I just want to make sure it's important we talk about, we've got a lot of things from an innovation standpoint that really understand the operating model to make us more efficient, better culinary every single time, consistent every single time, and frankly, makes the job easier for our team members to be successful, which then results in, I think, great outcomes for our customers.

So, a bit more answer to your question, but I think it's important to just highlight hyping's a great tool, but there's a lot of tools we're working on that I think are going to make us better in the future.

John Ivankoe

That's great. Jack, congratulations.

Jack Hartung

Thanks John.

Operator

The next question comes from Andrew Charles with TD Cowen. Please go ahead.

Andrew Charles

Great. Thank you. And just like everyone else, congrats to both Jack and Adam. Jack, what a ride it's been. Jack, curious just with the guidance, why keep the mid-single-digit part just given the blowout from 2Q as well as the fact that it sounds like July spotty, but around that 6% trend.

That mid-single-digit piece suggests a pretty wide range of outcomes for the back half of the year and implies some deceleration potentially coming. So, can you just talk more about the guidance philosophy?

Jack Hartung

Yes, I mean, there's two things going on. One is, like we said, since the pandemic, the summer months have been more difficult to predict. Like the first year when you'd have the normal going back to school and, or leaving school and then going back to school, that was very, very different.

Last year, vacations really were pulled forward. This year, vacations were pulled forward again, and it looks like they've even stepped up again. So, there's difficulty in predicting the seasonality.

The other thing keep mind is we do have 300 basis points of pricing rolling off. So, now what we hope to do is hopefully in a couple of quarters, we're talking about how the guidance ended up being perhaps on the conservative side.

But right now, with everything that's going on, whether it's seasonality or something that's more of a bigger approach or a bigger impact on the consumer. We think this is the right guidance level.

And our intent is giving you a little bit more granularity in terms of what the months are looking like to give you kind of idea an idea of what we're seeing right now. And I think with Brisket coming up, we're very optimistic that was a big demand the first time. We actually just couldn't even keep it in stock it. We ran out of it so fast. We're optimistic, but we also want to be cautious in this environment.

Andrew Charles

That's helpful. And in past years, before the inflation issue, we saw that there was typically about a 2% price increase, 2.5% price increase taken in December. What's the likelihood we see that again for next year? I know you're seeing some temporary margin headwinds. But as we think about pricing levels for next year, I mean what's the likelihood we see something coming in December?

Jack Hartung

Well, that's a long time away. I assume you're thinking December 2025. That's a long ways away. In this environment, we love the idea of being able to get through the rest of this year without a price increase.

Where we would feel better in terms of the timing of a price increase, is in an environment where the economy is robust and healthy. The consumer is feeling very, very healthy, and they're spending and the restaurant industry in general is going well. And transactions are accelerating, not decelerating.

That's a great environment when you use inflation to take a modest increase our price increases have gone well, but we would not want to take that for granted. So I think it would be really data dependent like what's going on in inflation. But as importantly, what's going on with the consumer, what's going on with transaction trends.

Andrew Charles

ThatÂ’s helpful. Thank you.

Operator

The next question comes from Lauren Silberman with Deutsche Bank. Please go ahead.

Lauren Silberman

Thanks a lot. I wanted to ask on the LTO strategy. You have one in spring, one in fall. It just seems like you generally comped the LTO comp for lack of a better phrase pretty consistently.

What enables you to keep growing LTOs year-over-year incidence rates growing each year? And do you tend to see like during the periods of LTOs that comps actually accelerate even though it's off a higher base?

Brian Niccol

Yes. So, look, the good news is we have a nice mix with our menu news of items that we've done in the past as well as completely new menu items. And I think what we've demonstrated is when we go back to something like a Chicken al Pastor or Carne Asada, we seem to be able to talk about it in a much more exciting way maybe than we did the original time because we learned some things on it.

We execute better, because we know how to train on it. The teams are familiar with the execution. So, that's been really nice to see. The one thing I want to remind everybody on all these things, though, is one of the ways make all these initiatives much more effective, great operational execution.

If we have terrific throughput, terrific deployment, and we execute culinary really well, the menu innovation gets amplified, because we give our guests a great experience. So, it does a great job of bringing in incremental customers, incremental transactions. But if we have soft operations, these efforts won't be nearly as effective.

So, I really think it's a combination of stronger operations than maybe the last time when we executed this program combined with, I think, a more informed marketing program than we did at the prior time.

So, that's one of the things I love about this organization. We're committed to learning. We're committed to always figure out how we can be better. And I think that's what you see coming out of Chipotle time and time again.

Lauren Silberman

Great. Thanks. If I could just do a quick follow-up on the 3Q guide. I understand a lot of noise, but can we -- is it safe to assume that the 25% restaurant level margin guide implies about a 6% underlying comp for the quarter?

Jack Hartung

That's a fair assumption. Yes, you're in the ballpark.

Lauren Silberman

Thank you very much.

Operator

The next question comes from Jon Tower with Citi. Please go ahead.

Jon Tower

Great. Thanks for taking the questions and congrats, Jack and Adam. Maybe just a quick follow-up and then a question. First, you had mentioned earlier the generous portion stuff that you're going to be doing in the short-term. Are you doing anything to message that to the consumer maybe something beyond what Brian you've already done on social media?

And then I guess my question is more along the lines of -- there's obviously been a fairly significant price increase in California because of the wage rate hikes. Any sort or change in consumer behavior in that market that you're seeing at your stores or perhaps more broadly across the industry that you could speak to?

Brian Niccol

So, look, your first question, part of the reason why we went and looked across the system was when we got the feedback on the portion sizes. We've always felt the key equity of Chipotle is these generous portion sizes.

So, we wanted to make sure we're executing consistently across the system. And we've probably found about 10% or more of restaurants that we really view as outliers that needed to be retrained re-coached to be executing against what we believe are the right standards.

At the same time, we collectively said, look, we do not go back one inch on our -- that equity of generous portion sizes. So, we communicate to the entire system. And look, I'm already seeing it in social media, people commenting on the burritos, the bowls that they're getting. And I think that is the best source of marketing is the word of mouth as people have these experiences with Chipotle.

But the thing I want to emphasize is for 90% of our restaurants, they're doing business as usual. So, I don't want it to be lost on the fact that this really was something where we doubled down as a system, but we really needed to kind of train up roughly 10% of the system.

So, I think it's going to continue to be a key equity of ours. And as I mentioned in my prepared remarks, it's an equity we care about. So, we'll invest in it, and we'll figure out how to make sure we consistently do it every time.

Jack Hartung

Yes. And then -- and then on California, so I'll make a comment or two. So yes, what we've seen is really across the entire state, we've seen a step down in the industry we've seen individual data points within the individual restaurants. And we've seen reports that there really has been a pullback in spending we've seen it as well.

We've also seen that when we've seen individual restaurants. There's not a correlation between the step back in the spending versus the major price increase that was taken. And so it looks like there's just kind of a macro impact of less spending in the restaurant. We saw the same thing.

Unfortunately, we raised prices by 100 basis points. We normally don't see much resistance. We still resistant to the point where we didn't get the 100 basis points at all. So, saw a pullback that equal the effect of menu price increase that we took. And it looks like that's about equal to what the pullback in the industry is.

Jon Tower

Got it. Thanks for taking the questions.

Jack Hartung

Sure.

Operator

The next question comes from Brian Harbour with Morgan Stanley. Please go ahead.

Brian Harbour

Thanks. Yes. Good afternoon and Jack and Adam, congratulations as well. The Barbacoa kind of marketing initiative, could you just comment on that? Was it kind of a pretty material driver? Did people respond as you expected? Are there kind of other opportunities to do that sort of thing?

Brian Niccol

Yes. Look, that was really effective. I think the marketing team did a great job of informing people of a great product that we have on our menu all the time. And as a result, we saw incidents go up and I think it's going to be something we'll revisit in the future.

The good news is we got another hidden gem, I think, with Carnitas that we'll evaluate as well. But yes, you'll probably see us do that again because it worked really well for us.

Brian Harbour

Okay, great. And Brian, your comments on automation but also some of the other kind of initiatives that you mentioned. How fast do you think some of those can show up? Is this the sort of thing where we start to see it in a year or two? Or are some of these longer-term? Do we see it in the form of kind of continued margin upside? Or like how should we kind of assess some of those as outsiders?

Brian Niccol

Yes. Look, I think, like you would expect with any good portfolio of ideas, we have short-term, medium-term, and longer-term, right? And some of those things are much closer in versus something like a hyphen is a little bit further out.

And the thing that's great is we're validating all of it through the stage gate. This is one thing I love about the stage gate process is it doesn't slow things down. It just ensures we don't have any unintended consequences. So, that as we roll things out, we're informed with what we're executing.

But yes, some of those things can happen on much faster timelines and some of the other things take a little bit longer. So it's a real, it's a really nice blend of, I would say, near-term, mid-term, and long-term.

Operator

The next question comes from Danilo Gargiulo with Bernstein. Please go ahead.

Danilo Gargiulo

Thank you. Brian, last time we discussed, you were talking about throughput that was in the mid-20s. Where do you stand today? And can you maybe help us understand the major catalyst of throughput acceleration from here on?

Brian Niccol

Yes, sure. So, obviously, we saw our biggest improvement in throughput during the month of April, which was great to see. And we continue to see great throughput execution from folks.

The thing that's going to push the throughput forward even further is ultimately the deployment being done correctly, right? So if we get that expo number to a higher percentage, not surprisingly, that expo position is the biggest impact on throughput gains.

And so that's why you hear us talking about that position is kind of like the key metric of, are we deployed correctly to execute great throughput during peak? So, I'm optimistic that we're going to move that 50% number up, and I'm optimistic that we'll be able to move from the mid-20s to the high-20s in the not too distant future.

Danilo Gargiulo

Great. And can you please provide an update on the restaurant-level margins and demand that you're seeing in European markets? I mean, you're making some bold investments over there, changing leadership as well. So, when do you think it's going to be realistic to expect an acceleration in units in Europe as well?

Brian Niccol

Yes, look, I'm really excited about the progress that our team has made over in Europe, in really short order. They've taken a lot of the tools in the U.S. We put them into place in Europe. I think we're managing food better.

We're managing the supply chain better, managing deployment better. The culinary, I think, has really improved. So not surprising, you're seeing -- we're seeing nice improvements both in top line and bottom-line.

So, I'm optimistic that we're going to be proving those as investable markets to kind of go even faster down the road, similar to what happened in Canada. So, the team has made nice progress. I'm sure they'll be busy in Paris with Olympics coming up, but I'm really, really delighted with Brian have done in kind of short order.

Operator

And our last question will come from Chris O'Cull with Stifel. Please go ahead.

Chris O'Cull

Thanks and congratulations Jack and Adam. I just wanted to ask, Brian, do you see any signs that the increases in value promotions by the QSR chains have had any impact on the company's results?

Brian Niccol

We really haven't. And I kind of point to the fact that we're gaining market share according to the data we get back. And the brand metrics continue to strengthen, and one of those key strength components is our value proposition.

So, when I kind of connect all the dots of market share gains, strength in the brands, strengthen our operational execution, it appears some of these promotions are not having an impact on our business as of this moment.

So, again, the thing we have to do is play our offense. And our offense, as I mentioned earlier, is great culinary, great teams, great throughput and that results in great Burritos and Bowls for our customers. So we're going to stay after it.

And if the environment gets tougher, the good news for us is if the prior macro issues or recessions that we face, Chipotle is one of the one of the last ones impacted. And we were of the first ones out slowdown. So, it gives me confidence that we've got the right focus, the right operating model. And I think it's going to continue to resonate with customers.

Chris O'Cull

That's helpful. And just as a follow-up. You talked a lot about product innovation, obviously, that has been very successful. And one of the factors, I think, Jack, you mentioned benefiting April sales was the marketing activation event.

And I'm just wondering, can you help us understand how impactful these events can be and whether this is something the company could consider using more frequently if the consumer spending environment were to become more challenging?

Brian Niccol

Yes. Look, it's a great question. And this is really, I think, the power of our combination of our digital marketing/consumer database, combined with what I think are some really clever marketing moments, right, like National Burrito Day, National Avocado Day.

Obviously, we have the ability to turn on block mode. We have the ability to do other things that I think are very insight-based that we know resonate with the Chipotle customer.

And I think that's one thing that's great about having such a big Canada base on our customers and then doing, I think, a really effective job using digital marketing or traditional marketing tools to communicate these unique opportunities with our customers.

So, you'll continue to see us use it. And I think it's a huge advantage that we have, the strength of this loyalty program combined with a really talented marketing team.

Chris O'Cull

Great. Thanks, and congratulations guys.

Brian Niccol

Thank you.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Brian Niccol for any closing remarks.

Brian Niccol

All right. Thank you. And thanks, everybody, for all the questions. Again, I do want to recognize Mr. Jack Hartung on having the privilege to work with Jack as well as, I think Chipotle and everybody involved with Chipotle has a huge thank you from Mr. Hartung. So thank you again, Jack.

Jack Hartung

Thank you.

Brian Niccol

And obviously, we're excited for Adam to step into the CFO role and then obviously, Jamie McConnell stepping up into her Chief Accounting role. So terrific leaders under, again, Jack's leadership that are going to get the opportunity to make even bigger contributions to this great brand. So congratulations, everybody.

And then on the business, obviously, it was an outstanding quarter. I couldn't be prouder of the results the organization and what we accomplished. We get 8% transaction growth in any environment is pretty special.

And I think it's a testament, great operations, great marketing, great digital. I mean we just -- we've got a lot of things going the right way. And as a result, the brand metrics have never been better. The value proposition is super strong. And whatever is in store for us. I'm sure we'll have our ups and downs.

I always go back to having a strong brand with a strong organization sets you up for success. And I'm confident that we are building from a position of strength. And I look forward to finishing the year strong.

Obviously, we've got a couple of more quarters to go. But I just want to reemphasize what a great quarter. What a great team and really proud of where we are and where we're headed. So thank you, everybody.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.