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Capt. D's parent gets co-brand partner with Del Taco takeover

By Lisa Jennings

NASHVILLE, Tenn. (Feb. 13) - The new owners of the Del Taco brand are expected to speed the quick-service chain along in its goal to become a national brand and more than just its category's distant No. 2 player after Taco Bell.

Nashville-based Sagittarius Brands, parent of the 600-unit Captain D's Seafood chain, reached an agreement this month to purchase Del Taco, based in Lake Forest, Calif., whose chain of taco-burrito-burger units has 461 branches in 13 states. Terms of the transaction, which is expected to be completed by April, were not disclosed.

Del Taco chief executive Kevin Moriarty, who owns the chain along with three other executives, said he planned to step down after completion of the acquisition, though the rest of the management team will remain in place, and operations will continue out of Lake Forest.

Along with Sagittarius, backers of the transaction include private-equity investors Grotech Capital Group and Charlesbank Capital, which also are backers of Captain D's.

In addition, the financial firm Leonard Green and Partners of Los Angeles, which bought the Irvine, Calif.-based Claim Jumper casual-dining chain last year, is an equal shareholder in the Del Taco acquisition. Stockwell Capital LLC also joined as an investor, though with a smaller, yet "substantial" share, said Sid Feltenstein, chairman of Sagittarius Brands.

The goal of the Captain D's and Del Taco merger, Feltenstein said, is to grow both brands individually outside their respective regions — Del Taco is known primarily in the West but has begun growth into the Midwest, and Captain D's is focused on the Southeast. Both chains are about 40 percent franchised, and new growth will emphasize franchise development, Feltenstein said.

Sagittarius Brands also intends to test co-branded units, which, if successful, could speed up expansion of both concepts.

A foodservice veteran of Dunkin' Donuts and Burger King, Feltenstein is former chairman and chief executive of Yorkshire Global Restaurants, which sold the Long John Silver's and A&W Restaurants chains to Yum! Brands Inc. in 2002. Yum has since done numerous quick-service co-brandings of its own seafood and taco chains.

While Yum has had success with co-branding, the tactic tends to work for brands that target different dayparts, according to consultant Bob Sandelman, president of the Sandelman & Associates...
foodservice market research firm, based in San Clemente, Calif. Yum's Pizza Hut and Taco Bell concepts work together, for example, because pizza is more of a dinner and take-out item, whereas Mexican food is primarily a lunch and dine-in option, he said.

As of last June, Yum or its franchisees operated 95 co-branded Taco Bell and Long John Silver's units across the country. By comparison, the Taco Bell-Pizza Hut pairing had 588 locations, and Long John Silver's most numerous co-brand partner was A&W, with 296 locations.

Stuart Morris, president of QSR Consulting Group Inc. in Coronado, Calif., said the intended co-branding of Captain D's and Del Taco "will certainly raise eyebrows at the corporate headquarters of both Taco Bell and Long John Silver's."

Apart, neither Captain D's nor Del Taco poses a threat, he said. But together, "Captain D's immediately has lowered the risk of expansion into relatively expensive West Coast markets by piggy-backing off of Del Taco's existing locations," Morris said. And Del Taco will see similar benefits for expansion in the South, which is Captain's D's regional stronghold, he added.

The merger "moves both companies from being a regional quick-service restaurant organization to, perhaps, a nationwide co-branding juggernaut," Morris said.

The Grotech and Charlesbank investment firms last year bought the then-577-unit Captain D's chain from Lone Star Funds for $150 million.

At the time, Sagittarius was created as the parent company with the goal of operating "multiple brands that fit well strategically," Feltenstein said. Del Taco was an attractive concept because of its 15 consecutive years of positive same-store sales growth, average unit volume of $1.2 million, good margins and strong organization, he said.

Somewhat of a hybrid, Del Taco already enjoys some of the benefits others have derived from co-branding by being one of the few Mexican quick-service operators to offer burgers, fries and milkshakes alongside the chain's tacos, burritos and quesadillas.

Del Taco began in 1964 in Barstow, Calif., as Red-E-Foods Systems Inc. In the 1970s it became Del Taco Inc., and founders Ed Hackbarth and David Jameson later sold their stock to American Restaurant Group, which eventually merged with Naugles, another quick-service taco chain.

In 1989, Paul Hitzelberger took over Del Taco operations under GE Capital Corp. Moriarty, a former Burger King executive, arrived in 1990 and was given the mission of revamping the flagging brand.

After a planned 1993 bankruptcy to clean the balance sheet of liabilities, Moriarty and the three other executives bought the company for $85 million plus $12 million in warrants. Moriarty bought the warrants back from GE in 1997.

Franchising began a year later, and now Del Taco has 60 franchise development agreements in place that call for the opening of 338 restaurants over the next five years. Planned new markets include Michigan, Idaho and Oregon. Last year Del Taco opened 34 stores, 11 of them owned by the franchisor.
Del Taco's revenues for 2005 from sales at 264 company-owned units and royalties from another 197 franchised outlets topped $335 million.

Hitzelberger, who retired in 2001 and is now the largest Del Taco franchise operator in Utah, with 13 units and seven under development, said the acquisition is "a win-win for both companies."

"This is a very franchise-oriented team," said Hitzelberger of Feltenstein and Ron Powell, Sagittarius Brands' president and chief executive. "Sid and Ron have had tremendous success in the past. They know what they're doing. They're astute operators."

On the possibility of co-branding, Hitzelberger said: "I like the idea of two tastes in one place. It's a real-estate and convenience strategy, and it allows for substantial growth for both brands — and not just growth for growth's sake."

Ron Petty, Del Taco's president, said the chain once tested dual branding with the Mrs. Winner's chicken chain, which was then owned by Arby's franchisee RTM Restaurant Group. The test units were successful, he noted, though the units were closed about four years ago because of turmoil within Mrs. Winner's operations.

When the news broke about the acquisition, Petty said, he immediately began getting phone calls from Captain D's franchisees interested in opening Del Taco units.

"We see this as a great way to expand Del Taco quickly in the Southeast and, at the same time, grow in the Midwest," Petty said. "All of a sudden, in a short time, Del Taco could be a national brand."

E-mail the author at: ljenning@aol.com