

THIRD QUARTER 2020 EARNINGS CONFERENCE CALL PREPARED REMARKS

OPERATOR SCRIPT

Good evening, and welcome to Shake Shack's **THIRD QUARTER 2020** Earnings Call. At this time, all participants have been placed in a listen-only mode and the floor will be open to questions following management's prepared remarks. It is now my pleasure to turn the floor over to Rik Powell, Senior Vice President of Finance. You may begin.

RIK POWELL - INTRO

Thank you, [operator name] and good evening, everyone. Joining me for Shake Shack's conference call is our CEO Randy Garutti and President and CFO, Tara Comonte.

During today's call, we will discuss non-GAAP financial measures, which we believe can be useful in evaluating our performance. The presentation of this additional information should not be considered in isolation or as a substitute for results prepared in accordance with GAAP. Reconciliations to comparable GAAP measures are available in our earnings release and the Appendix to our supplemental materials.

Some of today's statements may be forward-looking, and actual results may differ materially due to a number of risks and uncertainties, including those discussed in our Annual Report on Form 10-K, filed on February 24, 2020 and Form 10-Q filed on July 31, 2020. Any forward-looking statements represent our views only as of today, and we assume no obligation to update any forward-looking statements if our views change.

By now, you should have access to our Third Quarter 2020 earnings release, which can be found at INVESTOR.SHAKESHACK.COM in the NEWS section. Additionally, we have posted our Third Quarter 2020 supplemental earnings materials, which can be found in the Events & Presentations section on our site, or as an Exhibit to our 8-K for the quarter.

I will now turn the call over to Randy.

RANDY GARUTTI, CEO

Thanks, Rik, and good evening everyone. We hope you, your families and our entire Shake Shack community are staying healthy and safe through these challenging times.

Burger, by burger, Shake Shack continues to come back. Our business during this most recent quarter showed steady recovery, thanks to the hard work and dedication of our team, their agility in adapting new Shack protocols and models, and an increasingly strong suite of digital capabilities. As a result, guests have been able to enjoy their Shack the way they want it, with a choice of convenient and safe ordering and pick-up options, as we continue to expand and elevate the Shake Shack experience.

Since our last update at the end of July, forward momentum has continued and we're encouraged to see a strong recovery in both sales and profitability, with many Shacks returning to or even exceeding last year's results. Total year over year company-operated Shack sales declined (17%) in the third quarter, compared to a decline of (39%) during the second quarter, and further improved to a decline of just (5%) in fiscal October. Same-Shack sales have also improved sequentially in *every single one of* the last six months. This is an encouraging path to recovery, considering the drag that our high traffic urban locations continue to have on the business, while suburban Shacks are collectively, getting close to full recovery. Importantly, we're also almost back to a steady state development schedule and are ramping up the opening of *new* locations through the remainder of this year, and into 2021 and beyond. As of the end of fiscal October, we have opened 33 Shacks during this challenging year, including 15 domestic company-operated, of which 4 were opened in the Third Quarter.

The consistency with which our sales have continued to recover gives us added confidence in the gradual return to a more normal operating environment. As expected, with urban locations still acutely impacted by the pandemic, our suburban Shacks continue to recover more quickly, but both have shown strong improvement in recent months, particularly due to increases in in-Shack ordering and high levels of retention of our digital sales.

From a regional perspective we continue to experience a broad range of performance when it comes to speed and level of sales recovery. At times this is based on the extent to which dining rooms are open and also the relative concentration of urban shacks which are understandably more impacted by office, tourist and high traffic. New York City, particularly Manhattan, continues to lag other regions, and we expect this to be an ongoing headwind for the business until the city fully recovers. Throughout this pandemic, New York City has been hit especially hard, but despite that, we are pleased to see our hometown is beginning to make real progress, showing sequential improvements in same-Shack sales from down (64%) in the second quarter, to down (49%) in the third quarter, to down (40%) in fiscal October. Manhattan specifically, is also slowly improving, to a year-on-year decline of (60%) in same-Shack sales during the third quarter from (69%) in the second quarter, and showing further gradual improvement to down (51%) in October. It's particularly challenging for Manhattan with some of our historically highest volume locations, like Penn Station, the Theater District, Herald Square and others, remain deeply impacted at this time.

Following similar trends to our company-operated Shacks, our international licensed Shacks are also recovering. Total licensing sales sequentially increased throughout the third quarter, averaging \$5.3 million per week, nearly double the \$2.7 million in the second quarter. The speed and scale of our Licensing sales recovery has differed across the globe. Countries such as China and Korea which were faster to contain the COVID-19 outbreak, are recovering more quickly than those experiencing prolonged lockdowns or a resurgence of cases. Mainland China for example is showing a strong return in sales, now back to above pre-COVID levels. While just three of our international Shacks were closed as of the end of fiscal October due to COVID, the operating environment is changing on a regular basis. In August, we were excited to report the opening of our first Shack in Beijing, which has outperformed expectations, with sales in the opening month among the highest of any international Shack opening. Amazing when you consider the environment we're operating in, and testament to the continued strength of the Shake Shack brand across the globe.

The most deeply impacted part of our entire company remains our licensed airport and stadium business. With travel still severely depressed, and stadiums closed, only nine of our 22 domestic licensed Shacks are open as of the end of fiscal October, and we expect that to continue to be the case for the foreseeable future, which will hold back the recovery in this highly profitable piece of our business. However, we continue to take a long view here. In

normal times, these are some of the best Shack locations in the world, providing both high traffic and high brand visibility and we're excited for the day they will eventually re-open. In the meantime, we'll be working with our domestic licensed operating partners to support new openings as those opportunities arise, such as the Salt Lake City Airport for example, which opened in September. As we look to the future of licensed Shacks, we expect to open 12 to 14, net licensed Shacks for the full year 2020, with five to six new licensed Shacks expected to open in the fourth quarter, and 15-20 new licensed shacks for 2021.

Moving onto company-operated new development, despite the necessary pause earlier in the year, we're back to growth and have been regaining momentum in recent months. We opened 12 Shacks through the end of the third quarter and we're anticipating reaching a total of 18-20 new company-operated Shacks by the year end. Both recent and upcoming Shacks are in fantastic locations - such as Valley Fair in Santa Clara, University Village in Seattle, a free-standing Shack in Pasadena and locations that continue our penetration of key markets across Texas, Salt Lake City and Colorado. We're pleased with the operating results of those open so far with the 2020 class average, continuing to outperform the company average weekly sales during the third quarter. Make no mistake, before and after COVID, our strategy is to win, market by market, with a focus on top-tier real estate across the United States.

Our evolving multi-format Shack model positions us to take advantage of current real estate opportunities emerging across the country, particularly as we look at openings into next year and beyond. We're aggressively pursuing and developing sites where we can launch our new Drive-thru, our Shack Track drive-up and walk-up models, as well as the continuation of core Shack formats that have generated compelling returns for years.

I want to provide an update on the direction for each of these new Shack models:

- First on the recent launch of our Curbside Pickup - in place now at nearly 70 Shacks nationally. This model was created to solve the need for safe, contactless pickup and we executed on this in less than three months at the peak of COVID. Since launch, Shacks offering curbside have been experiencing about a third of all eligible app orders in that format, and that's been with limited marketing. Given this level of adoption we feel good that this is meeting a real guest need and we're excited to continue to evolve

and improve this as we learn more, and add this option to future Shacks wherever the layout allows for it.

- Second - on our roll out of other versions of Shack Track, with the objective of adding convenience in pre-ordering, combined with a fast and frictionless experience at pickup. As we look ahead, most Shacks in the pipeline will have some version of a Shack track, either through an enhanced interior pickup model, an exterior walk-up window; or a drive-up option, such as our upcoming retrofit in Vernon Hills, Illinois. Not only do these models aid in social distancing, but we believe they'll be a favored option for guests looking for speed and convenience on the go in a post-COVID environment. Through the end of this year, we'll complete seven to nine Shack Track retrofits in existing Shacks. Next year, most new Shacks will have some version of a Shack Track, and we expect roughly half the class to have either an exterior walk-up window or drive-up window as they open. It's too early to talk about results, but our goal is to drive convenience, frequency and long term sales growth through this model.
- Finally - we're getting really excited to launch our first-ever Drive Thru location late next year. The Shake Shack drive-thru will be a modern version of the traditional drive lane experience, supported by technology-enabled hospitality and innovative design – all while maintaining our core tradition of building community gathering places. We view this new model for us as an important step towards increasing our addressable market opportunity, and we're making a big commitment to this learning - targeting between five and eight drive thrus over the next 24 months.

As we look to 2021 we intend to return to the full development schedule that was in place before COVID, and are targeting between 35 and 40 new company-operated Shacks for next year. We'll be launching in new cities like Portland and Indianapolis, while going deeper in California, the Midwest and some of our other strong markets on the east coast. Our approach is to build a balanced set of formats across our portfolio, and to continue to diversify across markets as we look to ramp up Shack unit development in 2022 and beyond.

With this opportunity ahead, we're also investing in the future of the Shack digital experience. The influx of new and returning guests to our digital channels over the course of this year has given us a real opportunity to update and enhance our tools, enabling new ways to provide

hospitality at the core of the Shack experience. We are confident in our continued focus on our app and web channels, as these allow us to connect with our guests more frequently, and they continue to perform with a higher average check. As we mentioned in our last call, we're looking forward to offering delivery via our own channels, and are currently targeting limited testing of this functionality towards the end of this year, with broader testing and rollout over the first half of next year. This will be hugely positive for our digital strategy for a host of reasons - including the ability to create consistent and personal experiences with our guests across our own channels, combined with the additional data and insights that allow us to better understand our guests, and connect with them more directly as part of our broader digital strategy.

Turning to the menu – the return of Hot Chick'n has received a fiery welcome back by fans. New this year guests were able to order Hot Spicy Fries and Hot Chick'n bites, each with our new Ranch sauce. We've been offering three levels of spice: hot, extra hot, and fire, the latter only available through our digital channels. Since launching this hot menu offering in September, we saw a significant step up in overall chicken sales, with 40% more chicken items sold versus the previous two months. During the third quarter we also launched our Pumpkin Shake for the third year in a row. Made with the highest quality ingredients we use real pumpkin, cinnamon, nutmeg, and top it with delicious toasted pumpkin seeds.

As winter approaches, we're looking forward to the return of another fan favorite, our trio of holiday shakes, bringing back our Christmas Cookie, and two new flavors: Chocolate Spice and Candy Cane Marshmallow. In 2021, the team is excited to bring a regional favorite from our Korean shacks to the U.S: a Spicy Korean-Style Fried Chick'n sandwich featuring a Gochujang-glazed chicken breast topped with roasted sesame seeds, over white kimchi slaw. A version of this menu item is running as an LTO right now in our South Korean shacks, and is a good example of the way our international presence can enhance and elevate our brand as we share exciting and innovative menu items across the world. While COVID resulted in more of a focus on simplification in the short term, we're excited to be getting back to a more regular cadence in our limited time offerings in 2021, with a culinary calendar that raises the bar with bold new chicken flavors, the expanded testing of our exciting, new Veggie Shack, and innovation around our beverage and custard program.

Wrapping up, our progress in recent months is encouraging in nearly every corner of our business. We're certainly not out of the woods when it comes to the impact from the pandemic, but each day brings us new momentum and confidence we're on our way. With the innovation and work taking place across the entire company, we remain squarely focused on the safety of our operations, the ongoing enhancement and expansion of access across formats and channels, and the significant white space for growth *globally* that remains ahead of us. We're incredibly grateful to each and every member of our team, both in the shacks and in our home office who make this company the very special place that it is, each and every day.

And with that, Tara will take you through the financials.

TARA COMONTE, CFO

Thanks, Randy.

As you've just heard, we're pleased with the steady and consistent progress in our top and bottom line recovery, as well as the great work going on across the entire company. We're getting stronger every day and will continue to diligently execute against our key strategic initiatives while focusing on the significant growth that lies ahead.

In terms of third quarter results, **total revenue was \$130.4M, including \$4.1M in licensing revenue**. This represented a total Shack sales decline of 17% and a licensing revenue decline of 24% versus the same period last year. However, when compared to the second quarter, total Shack sales and licensing revenue increased 41% and 81% respectively.

As of the end of the third quarter, our trailing twelve-month average unit volume was \$3 million, as a significant portion of this trailing time period includes COVID impacted months. Average weekly sales, the key top line metric to monitor as we move through this recovery, were \$58,000 in the third quarter, and increased sequentially throughout that period, ending with fiscal September at \$61,000. We saw this improvement continue through our most recent fiscal period of October, with average weekly sales of \$62,000, and we've included this data in more detail on page six of our supplemental materials.

Same-Shack sales continue to show solid signs of recovery, declining (31.7%) during the third quarter compared the same period last year, improving from a decline of (49%) in Q2. Consistent with our total sales trends, comp base sales also improved in every fiscal month since April, with fiscal September same-Shack sales down (23%) and fiscal October further improving to down (21%) year over year.

Traffic declined 42% in the third quarter, offset partially by a positive price mix of 10.3%. This year-on-year price/mix growth was driven by a significant increase in average check, primarily from a higher digital sales mix, combined with an overall increase in that check as we've seen higher items per order since the start of the pandemic.

As Randy mentioned, we are encouraged by the improvement in performance of both our suburban and urban Shacks. As a reminder, our comp base today is comprised of roughly 50:50 urban:suburban shacks, although urban shacks had a higher revenue contribution pre-COVID at approximately 60% of comp base sales compared to approximately 50% in the third quarter. Same-Shack sales of our suburban comp base Shacks were down (16%) in the third quarter compared to the prior year, an improvement from the decline of (38%) during the second quarter, and they again improved in fiscal October to down just (4%). Urban markets are also showing steady improvement, however still impacted to a much greater degree by COVID. Urban comp base Shacks declined (43%) in the third quarter compared to last year, versus a decline of (57%) in the second quarter, and also showed continued improvement in fiscal October to a (33%) year-on-year decline.

Same-Shack sales improved across *all* regions on a sequential basis, with performance driven by increases in in-Shack dining in both urban and suburban Shacks combined with the continued strength of our digital channels. We do however continue to see levels of regional performance improvement differ based primarily upon the relative proportion of urban Shacks in the region. The comp base Shacks in our Southeast region for example, of which over 80% are suburban, were down (25%) year-over-year in the third quarter, a significant rebound from being down (41%) in the second quarter and subsequently improving further to down (13%) in fiscal October. Regions which are more significantly comprised of urban locations continue to be the hardest hit, with New York City being the most acute example of this and you heard some of those numbers from Randy a moment ago. All of our regional performance is clearly laid out on pages eight and nine of our supplemental deck and we're happy to answer additional questions about it after the call.

Digital channels remain the leading order method, representing 60% of total Shack sales during the third quarter, broadly in line with the 62% we last reported for fiscal July. As you can see on page 12 of our supplemental, this held relatively constant throughout the third quarter, *and* through our most recent fiscal month October where digital sales mix was 58%. As in-Shack sales improve, we've maintained a high level of digital retention, with more than 90% of digital sales retained in fiscal October compared to the high point in fiscal May. During the third quarter and similar to second quarter trends, our native web and app channels, when combined, continued to be the fastest growing channel on a year-on-year basis, with sales more than three times that of the prior year.

In our last call, we shared that we had added over 800,000 first time purchasers to our app and web channels between early March and the end of July. We're pleased that this trend has continued through October, increasing to over 1.4 million first-time purchasers on those channels since early March.

Looking forward, and now a month into the fourth quarter, we're pleased with our ongoing progress, but closely watching the performance of in-Shack sales particularly in light of evolving city and state dining regulations. As of the end of fiscal October, nearly all domestic company-operated Shacks were open, with approximately 80% of those with open dining rooms to varying capacity restrictions, and the majority of Shacks also utilizing outdoor patio space. While we're confident in a full, long term recovery, we know the timing of that return to pre-COVID levels is highly dependent upon the return of the high traffic areas that contributed to many of our strongest Shack sales, those most reliant on travel, schools, offices and major gatherings, as well as ultimately, fully open dining rooms. The timing of that recovery remains unknown today. With colder weather and the increasing number of reported COVID cases, we do expect Sales over the coming months to be pressured. We do have the benefit of a 53rd week in this fiscal year which will be accretive on an absolute dollar basis, but the underlying business continues to face a very challenging and volatile operating environment certainly through the end of this year. Taking all of this continued uncertainty into consideration, we will only be providing the earlier mentioned unit guidance at this time.

Moving to the strong recovery of Shack-level operating profit for the third quarter, we're pleased with the significant improvement here. As shared in our last earnings, we exited the second quarter with approximately 5% Shack-level operating profit in fiscal June and just above 2% for the quarter. Since that time, the combination of sales improvement, normalization of beef costs, and continued disciplined expense management across the business has led to a significant recovery, with Shack-level operating profit margin in the third quarter improving to 14.8%. Performance improved sequentially throughout the quarter, with fiscal July, August and a five-week fiscal September delivering Shack-level profitability of 12%, 14% and 17% respectively.

In addition to the benefit from recovering sales throughout the quarter, we also saw a number of improvements across various Shack-level expenses.

Food and paper costs in the quarter were 30% of Shack sales, higher than the same period last year by 100 basis points due to increased paper and packaging costs, with all orders packaged to-go. On a sequential quarterly basis, we saw an improvement of 350 bps compared to the second quarter, primarily due to the stabilization of beef costs. Although we don't anticipate any major food cost changes going into the fourth quarter, paper costs will remain elevated due to the continuation of those increased levels of packaging.

Labor and other related costs in the third quarter were 30% of Shack sales, an improvement of 460 basis points compared to the second quarter, and an increase of 270 basis points compared to the prior year, due primarily to the loss of sales leverage across fixed labor expenses. The sequential quarterly improvement was significant, and due to improved sales performance as well as somewhat lessened COVID specific headwinds on this line such as pay during closures. We're pleased with the improvement here but will continue to bear some level of labor inefficiency as we manage social distancing and safety protocols, together with open but limited capacity dining rooms.

We remain incredibly grateful for the resilience and commitment shown by our teams in the Shacks, and in recognition we extended premium pay for our hourly team members through to the end of fiscal August and also guaranteed manager bonuses in the third quarter. In September, we further extended this support for our Shack teams through the fourth quarter by introducing a year-end bonus for all our hourly team members, and we're pleased to be able to show our continued appreciation in this way. This investment in our teams had a \$2.1 million impact during the third quarter within the labor line, and was in addition to the \$2.4 million already paid in the second quarter.

Other Operating expenses in the quarter were 14.8%, an improvement of 120 basis points compared to the second quarter, and an increase of 240 basis points year over year due primarily to increased delivery commissions, combined with the loss of sales leverage on fixed expenses. Compared to the prior year, the increase in delivery commissions during the third quarter was partially offset by savings in reduced maintenance expenses within the Shacks which we do not expect to continue as we enter the fourth quarter.

As we look to the fourth quarter, and as I mentioned, our expectation is that Sales will face pressure due to the challenges of the ongoing Covid environment, as well as the onset of colder weather across a significant number of our regions. With the continued recovery of Shack-level operating profit highly correlated to Sales performance in terms of leverage on fixed costs, combined with the continuation of certain elevated costs in the P&L specific to the pandemic, we also expect any ongoing improvement in Shack-level operating margin in the fourth quarter to face pressure. Strong cost management will continue, with the safety of our teams and our guests however always being our first priority.

Moving onto **G&A**, which in the third quarter was \$15M, including \$1.7M related to non-cash items. With our continued recovery through the third quarter, and a strong balance sheet, we have gradually increased investment in key areas across the business, while slowly bringing back our team in preparation for the growth ahead. In particular, across our digital initiatives, but also in marketing, recruiting, and development as we focus on that significant long-term growth opportunity. We remain bullish on the size of the opportunity we have ahead, and are committed to investing in order to reap the benefits quickly and meaningfully. As we look out through the remainder of this year, we expect our fourth quarter total G&A spend to approach the same level of spend as the fourth quarter 2019.

Pre-opening expense for the third quarter was \$1.8M, with \$500K in non-cash deferred rent expense related to Shack locations we are in possession of, but are not yet opened. Now that development is back to a full opening schedule, this spend will increase meaningfully, and is expected to more than double sequentially through the fourth quarter as we complete this year's opening schedule and ramp back up to those 35-40 units we mentioned for 2021, a number of which should open in the first half of the year.

Finally, despite the challenges of operating within a global pandemic, work has continued to complete the successful final phase of Project Concrete which centered around our Shack-level supplier, inventory and invoice management systems with a focus on automation and time savings for our Shack teams. We're pleased to confirm that this is all now fully rolled out and I'd like to thank the entire Project Concrete team for their incredible achievement in such challenging conditions.

On an Adjusted Pro Forma Basis, we had a net loss of \$4.4 million or 11 cents per fully exchanged and diluted share. Excluding the tax impact of stock based compensation, our adjusted pro forma tax rate in the third quarter was 29.3%, slightly higher than guidance given earlier in the year, due primarily to a combination of state mix and lower tax credits. Year-to-date that rate is approximately 28%, and is in line with our full year expectations at this time. Similar to prior quarters, a full reconciliation of our tax rates is included in the appendix of our supplemental materials.

Our cash and marketable securities balance at the end of the quarter was \$191.8 million and we were pleased to have generated positive free cash flow for the quarter. We do expect an increase in cash use during the fourth quarter as our capital expenditure for new Shack construction ramps back up with a robust 2021 development schedule ahead of us.

We're very pleased with the significant improvements in performance across the company, from our recovering sales and profitability to the strong performance of our digital business. We do however remain in challenging and volatile times, but our foundation is strong, as is our balance sheet, and we're focused on that clear roadmap for growth ahead of us.

And with that, I'll turn you back to Randy.

RANDY GARUTTI, CEO (CONCLUSION)

Thanks Tara.

I want to end today's call noting a milestone that none of us could have ever dreamed back at the first Shack in Madison Square Park. We recently opened our 300th Shack in the world, in, Madison, Wisconsin! I could not be more proud of the hard work we've seen from our teams over the last 16 years to reach this occasion. Throughout this journey, we've had our share of triumphs and challenges, and it's the perseverance of this team that got us where we are today. I also want to thank our loyal Shack fans that have stuck with us and are coming back to enjoy their Shack in more ways than they ever could before. Above all, count on us always to lean into our purpose- to Stand for something good while creating uplifting experiences, caring first for our team members, and inspiring them to provide boundless hospitality to our guests, community, suppliers and investors.

To you and families, stay safe and stay healthy.

And with that, operator, please open up the call for questions.