

CBRL GROUP INC  
Form 10-K  
October 02, 2007

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act  
of 1934

For the fiscal year ended August 3, 2007

OR

Transition report pursuant to Section 13 or 15(d) of the  
Securities Exchange Act  
of 1934

For the transition period from \_\_\_ to \_\_\_\_\_

Commission file number  
000-25225

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CBRL GROUP, INC.  
(Exact name of registrant as specified in its charter)

Tennessee  
(State or other jurisdiction of  
incorporation or organization)

62-1749513  
(I.R.S. Employer  
Identification Number)

305 Hartmann Drive, P.O. Box 787  
Lebanon, Tennessee  
(Address of principal executive offices)

37088-0787  
(Zip code)

Registrant's telephone number, including area code: (615) 444-5533

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Securities registered pursuant to Section 12(b) of the Act:

Common Stock  
(Par Value \$.01)

Common Stock Purchase Rights  
(No Par Value)

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Exchange Act Rule 12b-2. (Check one)

Large accelerated filer  Accelerated  
filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The aggregate market value of voting stock held by nonaffiliates of the registrant, by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter which ended January 26, 2007, was \$1,194,552,449. For purposes of this computation, all directors, executive officers and 10% beneficial owners of the registrant are assumed to be affiliates. This assumption is not a conclusive determination for purposes other than this calculation.

As of September 25, 2007, there were 23,726,030 shares of common stock outstanding.

Documents Incorporated by Reference

<u>Document from which Portions are Incorporated by Reference</u>	<u>Part of Form 10-K into which incorporated</u>
1. Annual Report to Shareholders for the fiscal year ended August 3, 2007 (the “2007 Annual Report”)	Part II
2. Proxy Statement for Annual Meeting of Shareholders to be held November 29, 2007 (the “2007 Proxy Statement”)	Part III

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INTRODUCTION

General

This report contains references to years 2007, 2006, 2005, 2004, and 2003, which represent fiscal years ending or ended August 3, 2007, July 28, 2006, July 29, 2005, July 30, 2004, and August 1, 2003, respectively. All of the discussion and analysis in this report should be read with, and is qualified in its entirety by, the Consolidated Financial Statements and the notes thereto. All amounts other than share and certain statistical information (e.g., number of stores) are in thousands unless the context clearly indicates otherwise.

Forward Looking Statements/Risk Factors

Except for specific historical information, many of the matters discussed in this Annual Report on Form 10-K, as well as other documents incorporated herein by reference may express or imply projections of revenues or expenditures, plans and objectives for future operations, growth or initiatives, expected future economic performance, or the expected outcome or impact of pending or threatened litigation. These and similar statements regarding events or results that CBRL Group, Inc. (the "Company") expects will or may occur in the future, are forward-looking statements that involve risks, uncertainties and other factors which may cause our actual results and performance to differ materially from those expressed or implied by those statements. All forward-looking information is provided pursuant to the safe harbor established under the Private Securities Litigation Reform Act of 1995 and should be evaluated in the context of these risks, uncertainties and other factors. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "trends," "assumptions," "target," "guidance," "outlook," "opportunity," "future," "plans," "goals," "objectives," "expectations," "near-term," "long-term," "projection," "may," "will," "expect," "intend," "estimate," "anticipate," "believe," "potential," "regular" or "continue" (or the negative or other derivative of these terms) or similar terminology. We believe the assumptions underlying these forward-looking statements are reasonable; however, any of the assumptions could be inaccurate, and therefore, actual results may differ materially from those projected in or implied by the forward-looking statements. Factors and risks that may result in actual results differing from this forward-looking information include, but are not limited to, those listed in Part I, Item 1A below, all of which are incorporated herein by reference, as well as other factors discussed throughout this document, including, without limitation, the factors described under "Critical Accounting Estimates" in that portion of the 2007 Annual Report that is incorporated by reference into Part II, Item 7 below or, from time to time, in our filings with the SEC, press releases and other communications.

*Readers are cautioned not to place undue reliance on forward-looking statements made in this document, since the statements speak only as of the document's date. We have no obligation, and do not intend, to publicly update or revise any of these forward-looking statements to reflect events or circumstances occurring after the date of this document or to reflect the occurrence of unanticipated events. Readers are advised, however, to consult any future public disclosures that we may make on subjects related to those discussed in this document.*

## PART I

### ITEM 1. BUSINESS

#### OVERVIEW

CBRL Group, Inc. (“we,” “us,” “our” or the “Company”) is a holding company that, through subsidiaries, is principally engaged in the operation and development of the Cracker Barrel Old Country Store® restaurant and retail concept. Prior to December 6, 2006, we also operated Logan’s Roadhouse® (“Logan’s”) restaurants. On that date, we completed the sale of Logan’s. We were organized under the laws of the state of Tennessee in August 1998 and maintain an Internet website at cbrlgroup.com. We make available free of charge on or through our Internet website our periodic and other reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act of 1934 (the “Exchange Act”) as soon as reasonably practicable after we file such material with, or furnish it to, the SEC.

#### 2006 – 2007 Strategic Initiatives

During 2007, we completed the strategic initiatives that we began in 2006, which included the divestiture of Logan’s, substantial share repurchases financed by an increase in total debt, and the redemption of our convertible debt.

#### Divestiture of Logan’s

On December 6, 2006, we completed the sale of Logan’s, for total consideration of approximately \$485,000 after post-closing adjustments for working capital and capital expenditures as provided in the sale agreement. The net cash proceeds of the sale of Logan’s were used to fund \$350,000 of share repurchases and, along with cash on hand, to pay down \$75,000 of debt and to pay taxes.

#### Share Repurchases

During 2007, we repurchased 8,774,430 shares of our common stock in a series of transactions. These repurchases required a cash outlay of approximately \$405,000. Our principal criteria for share repurchases are that they be accretive to expected net income per share and are within the limits imposed by our debt covenants under our credit facility.

#### Redemption of Convertible Debt

During 2007, we redeemed our then outstanding \$422,030 (face value at maturity) zero coupon convertible notes. The redemption took place after we exchanged notes having a net share settlement feature for \$375,931 (face value at maturity) of the previously existing notes. The net share settlement feature allowed us, upon conversion of a note, to settle the accreted principal amount of the debt for cash and issue shares of our common stock for the conversion value in excess of the accreted value.

In connection with our redemption of the convertible notes, holders of approximately \$401,000 principal amount at maturity outstanding elected to convert their notes into common stock rather than have them redeemed. Each \$1 (face value at maturity) of notes was convertible into 10.8584 shares (or equivalent value) of our common stock. We issued 395,775 shares (which subsequently were repurchased and were a part of the repurchases described above) of our common stock upon conversion and paid approximately \$189,000 in cash to redeem the notes. We obtained funds for the redemption by drawing on our delayed-draw term loan facility and using cash on hand.



OPERATIONS

Cracker Barrel Old Country Store, Inc. (“Cracker Barrel”), headquartered in Lebanon, Tennessee, through its various affiliates, as of September 28, 2007, operated 565 full-service "country store" restaurants and gift shops in 41 states. Cracker Barrel stores are intended to appeal to both the traveler and the local customer and consistently have been a consumer favorite. During 2007, for the 17<sup>th</sup> consecutive year, Cracker Barrel was named the “Best Family Dining Restaurant” in the Restaurants & Institutions magazine “Choice in Chains” annual consumer survey. For the<sup>th</sup>14 consecutive year, Cracker Barrel was ranked as the “Best Restaurant Chain” by Destinations magazine poll. For the<sup>th</sup>6 consecutive year, Cracker Barrel was named “The Most RV Friendly Sit-Down Restaurant in America” by The Good Sam Club. In 2007, Cracker Barrel was ranked as the number one

restaurant in the casual dining category in the Kanbay Research Institute Competitive Advantage Report. In addition, Cracker Barrel was the top-ranked family dining restaurant in the service and facilities categories and ranked second overall in the Zagat Full Service Survey 2007.

**Store Format:** The format of Cracker Barrel stores consists of a trademarked rustic, old country-store design with a separate retail area offering a wide variety of decorative and functional items featuring rocking chairs, holiday and seasonal gifts and toys, apparel, cookware and foods, including various old fashioned candies and jellies among other things. All stores are freestanding buildings. Store interiors are subdivided into a dining room consisting of approximately 27% of the total interior store space, and a retail shop consisting of approximately 22% of such space, with the balance primarily consisting of kitchen, storage and training areas. All stores have stone fireplaces, which burn wood except where not permitted. All are decorated with antique-style furnishings and other authentic and nostalgic items, reminiscent of and similar to those found and sold in the past in traditional old country stores. The front porch of each store features rows of the signature Cracker Barrel rocking chairs that can be used by guests waiting for a table and are sold by the retail shop. The kitchens contain modern food preparation and storage equipment allowing for flexibility in menu variety and development.

**Products:** Cracker Barrel's restaurant operations, which generated approximately 78% of Cracker Barrel's total revenue in 2007, offer home-style country cooking featuring Cracker Barrel's own recipes that emphasize authenticity and quality. Except for Christmas day, when they are closed, and Christmas Eve when they close at 2:00 p.m., Cracker Barrel restaurants serve breakfast, lunch and dinner daily between the hours of 6:00 a.m. and 10:00 p.m. (closing at 11:00 p.m. on Fridays and Saturdays). Menu items are moderately priced. The restaurants do not serve alcoholic beverages. Breakfast items can be ordered at any time throughout the day and include juices, eggs, pancakes, bacon, country ham, sausage, grits, and a variety of biscuit specialties, such as gravy and biscuits and country ham and biscuits. Prices for a breakfast meal range from \$2.29 to \$8.49, and the breakfast day-part (until 11:00 a.m.) accounted for approximately 23% of restaurant sales in 2007, while lunch (11:00 a.m. to 4:00 p.m.) and dinner (4:00 p.m. to close) day-parts reflected approximately 37% and 40% of restaurant sales, respectively, in 2007. Lunch and dinner items include country ham, chicken and dumplings, chicken fried chicken, meatloaf, country fried steak, pork chops, fish, steak, roast beef, vegetable plates, salads, sandwiches, soups and specialty items such as pinto beans and turnip greens. Cracker Barrel may from time to time feature new items as off-menu specials or in test menus at certain locations to evaluate possible ways to enhance customer interest and identify potential future additions to the menu. Lunches and dinners range in price from \$3.69 to \$12.99. Cracker Barrel's menu has daily dinner features that showcase a popular dinner entrée for each day of the week. There is some variation in menu pricing and content in different regions of the country for both breakfast and lunch/dinner. The average check per guest for 2007 was \$8.31, which represents a 1.4% increase over the prior year.

Cracker Barrel also offers items for sale in the retail store that are also featured on, or related to, the restaurant menu, such as pies or cornbread and pancake mixes. The retail operations, which generated approximately 22% of Cracker Barrel's total revenue in 2007, offer a wide variety of decorative and functional items such as rocking chairs, seasonal gifts, apparel, toys, music CDs, cookware, old-fashioned-looking ceramics, figurines, a book-on-audio sale-and-exchange program and various other gift items, as well as various candies, preserves, syrups and other food items. The typical Cracker Barrel retail shop features approximately 3,400 SKU's. Many of the food items are sold under the "Cracker Barrel Old Country Store" brand name. We believe that Cracker Barrel achieves high retail sales per square foot as compared to mall stores (over \$429 per square foot of retail selling space in 2007 on a 53-week basis) both by offering appealing merchandise and by having a significant source of retail customers from the high volume of restaurant customers - an average of approximately 7,600 per week in a typical store in 2007. The substantial majority of sales in the retail area are estimated to be to customers who also are guests in the restaurant.

**Product Development and Merchandising:** Cracker Barrel maintains a product development department, which develops new and improved menu items in response either to shifts in customer preferences or to create customer interest. Coordinated seasonal promotions are used regularly in the restaurants and retail shops. The Cracker Barrel merchandising department attempts to select merchandise for the retail shop that reinforces the nostalgic theme of the

restaurant. In 2007, Cracker Barrel continued to honor the authentic connection between country music's past and present by releasing exclusive music projects with Josh Turner, Merle Haggard and the *Songs Of The Year* CD. These recordings feature new music from Josh Turner, Merle Haggard, Trace Adkins, Trisha Yearwood and George Jones among other notable country and western recording artists. Another Cracker Barrel exclusive, The Grand Ole Opry® *Live Classics* CD series, showcases 60 previously unreleased live recordings by some of the Opry's biggest stars including Patsy Cline, Loretta Lynn, Johnny Cash, George Jones, Dolly Parton and Waylon Jennings.

**Store Management and Quality Controls:** Cracker Barrel store management, typically consisting of one general manager, four associate managers and one retail manager, is responsible for an average of 105 employees on two shifts. The relative complexity of operating a Cracker Barrel store requires an effective management team at the individual store level. As a motivation to store managers to improve sales and operational performance, Cracker Barrel maintains a bonus plan designed to provide store managers with an opportunity to share in the profits of their store. The bonus plan also rewards managers who achieve specific operational targets. To assure that individual stores are operated at a high level of quality, Cracker Barrel emphasizes the selection and training of store managers. It also employs district managers to support individual store managers and regional vice presidents to support individual district managers. A district manager's individual span of control typically is seven to eight individual restaurants, and regional vice presidents support seven to nine district managers. Each store is assigned to both a restaurant and a retail district manager and each district is assigned to both a restaurant and a retail regional vice president. The various levels of restaurant and retail management work closely together.

The store management recruiting and training program begins with an evaluation and screening process. In addition to multiple interviews and verification of background and experience, Cracker Barrel conducts testing designed to identify those applicants most likely to be best suited to manage store operations. Those candidates who successfully pass this screening process are then required to complete an 11-week training program consisting of seven weeks of in-store training and four weeks of training at Cracker Barrel's corporate facilities. This program allows new managers the opportunity to become familiar with Cracker Barrel operations, culture, management objectives, controls and evaluation criteria before assuming management responsibility. Cracker Barrel provides its managers and hourly employees with ongoing training through its various development courses taught through a blended learning approach, including hands-on, classroom, written and Internet-based training. Each store is equipped with training computers for the Internet-based computer-assisted instruction programs. Additionally, each store typically has an employee training coordinator who oversees training of the store's hourly employees.

**Purchasing and Distribution:** Cracker Barrel negotiates directly with food vendors as to specification, price and other material terms of most food purchases. Cracker Barrel is a party to a prime vendor contract with an unaffiliated distributor with custom distribution centers in Lebanon, Tennessee; McKinney, Texas; Gainesville, Florida; Elkton, Maryland; Kendallville, Indiana; and Ft. Mill, South Carolina. This vendor's contract currently runs through July 2013 with scheduled annual fee increases. The contract requires Cracker Barrel to pay for market fuel prices that exceed certain designated prices. Conversely, Cracker Barrel is required to be reimbursed for market fuel pricing that is below a designated price. The contract will remain in effect until both parties mutually modify it in writing or until terminated by a material breach of any obligations by either Cracker Barrel or the distributor. Cracker Barrel purchases the majority of its food products and restaurant supplies on a cost-plus basis through this unaffiliated distributor. The distributor is responsible for placing food orders, warehousing and delivering food products to Cracker Barrel's stores. Deliveries generally are made once per week to the individual stores. Certain perishable food items are purchased locally by Cracker Barrel stores.

Four food categories (dairy (including eggs), beef, pork and poultry) accounted for the largest shares of Cracker Barrel's food purchasing expense at approximately 14%, 13%, 11% and 9%, respectively, in 2007, but each category does include several individual items. The single food item within these categories, accounting for the largest share of Cracker Barrel's food purchasing expense, was chicken tenderloin at approximately 6% of food purchases in 2007. Cracker Barrel purchases its chicken tenderloin through two vendors. Cracker Barrel purchases its beef through nine vendors, pork through nine vendors, and poultry through seven vendors. Eggs are purchased through two vendors. Dairy is purchased through numerous vendors including local vendors. Should any food items from a particular vendor become unavailable, management believes that these food items could be obtained, or alternative products substituted, in sufficient quantities from other sources at competitive prices.

The majority of retail items (approximately 77% in 2007) are centrally purchased directly by Cracker Barrel from domestic and international vendors and warehoused at Cracker Barrel's Lebanon distribution center. The distribution center is a 367,200 square foot warehouse facility with 36 foot ceilings and 170 bays, and includes an additional

13,800 square feet of office and maintenance space. The distribution center fulfills retail item orders generated by Cracker Barrel's automated replenishment system and generally ships the retail orders once a week to the individual stores by a third-party dedicated freight line. The freight line contract, which currently runs through 2010, requires Cracker Barrel to pay for market fuel prices that exceed certain designated prices. Certain retail items, not centrally purchased and warehoused at the distribution center, are drop-shipped directly from Cracker Barrel's vendors to its stores. Approximately 30% of Cracker Barrel's retail purchases in 2007 were directly from vendors in the People's Republic of China. Cracker Barrel has a relationship with a foreign buying agency to source purchased product, monitor quality control and supplement product development.

**Cost and Inventory Controls:** Cracker Barrel's computer systems and various analytical tools are used to evaluate store operating information and provide management with reports to support detection of unusual variances in food costs, labor costs or operating expenses. Management also monitors individual store restaurant and retail sales on a daily basis and closely monitors sales mix, sales trends, operational costs and inventory levels. The information generated by the computer systems, analysis tools and monitoring processes are used to manage the operations of each store, replenish retail inventory levels and to facilitate retail purchasing decisions. These systems and processes also are used in the development of forecasts, budget analyses, and planning.

**Guest Satisfaction:** Cracker Barrel is committed to providing its guests a home-style, country-cooked meal, and a variety of retail merchandise served and sold with genuine hospitality in a comfortable environment, in a way that evokes memories of the past. Cracker Barrel's commitment to offering guests a quality experience begins with its employees. Its mission statement, "Pleasing People," embraces guests and employees alike, and Cracker Barrel's employees are trained on the importance of that mission in a culture of mutual respect. Cracker Barrel also is committed to staffing each store with an experienced management team to ensure attentive guest service and consistent food quality. Through the regular use of guest surveys and store visits by its district managers and regional vice presidents, management receives valuable feedback, which it uses in its ongoing efforts to improve the stores and to demonstrate Cracker Barrel's continuing commitment to pleasing its guests. Cracker Barrel also has for many years had a guest-relations call center that takes comments and suggestions from guests and forwards them to operations or other management for information and follow up. Cracker Barrel has public notices in its menus, on its website and posted in its restaurants informing customers and employees about how to contact Cracker Barrel by Internet or toll-free telephone number with questions, complaints or concerns regarding services or products. Cracker Barrel conducts training in how to gather information and investigate and resolve customer concerns. This is accompanied by comprehensive training for all store employees on Cracker Barrel's public accommodations policy and its commitment to "pleasing people." In 2005, Cracker Barrel implemented an anonymous, unannounced, third-party store testing program to ensure compliance with its guest satisfaction policies and commitments. In 2006, Cracker Barrel introduced an improved interactive voice response ("IVR") system to monitor operational performance and guest satisfaction at all stores on an ongoing basis. Cracker Barrel has used an IVR system in the past to monitor the performance of new restaurants and to provide insight into the performance of under-performing stores.

**Marketing:** Outdoor advertising (i.e., billboards and state department of transportation signs) is the primary advertising medium utilized to reach consumers in the primary trade area for each Cracker Barrel store and also to reach interstate travelers and tourists. Outdoor advertising accounted for approximately 64% of advertising expenditures in 2007, with approximately 1,500 billboards at year-end. In recent years Cracker Barrel has utilized other types of media, such as radio and print, in its core markets to maintain customer awareness, and outside of its core markets to increase brand awareness and to build guest loyalty. Cracker Barrel defines its core markets based on average weekly sales, geographic location, and longevity and brand awareness in the market. Cracker Barrel plans to spend approximately 1.8% of Cracker Barrel's revenues on advertising in 2008. Outdoor advertising is expected to represent approximately 60% of advertising expenditures in 2008. Cracker Barrel plans to increase broadcast advertising as a percentage of the overall budget as it plans to implement a test of TV and radio advertising during 2008.

## UNIT DEVELOPMENT

We opened 19 new Cracker Barrel stores in 2007. We plan to open 20 new stores during 2008, four of which already were open as of September 28, 2007.

Stores are located primarily along interstate highways; however, as of September 28, 2007, 71 of our stores are located near "tourist destinations" or are considered "off-interstate" stores. In 2008, Cracker Barrel intends to open approximately 45% of its new stores along interstate highways as compared to 68% in 2007. We believe we should pursue development of both interstate locations and off-interstate locations to capitalize on the strength of our brand associated with travelers on the interstate highway system and to increase sales through TV and/or radio

advertising by having more units in media markets where satisfactory interstate locations may not be available. We also seek to develop new markets through both interstate and off-interstate locations. We have identified approximately 650 trade areas for potential future development with characteristics that appear to be consistent with those believed to be necessary to support successful Cracker Barrel units.

Of the 565 Cracker Barrel stores open as of September 28, 2007, 404 are owned, while the other 161 properties are either ground leases or ground and building leases. The current Cracker Barrel store prototype is approximately 10,000 square feet including approximately 2,100 square feet in the retail selling space. The prototype has approximately 200 seats in the restaurant.

## EMPLOYEES

As of August 3, 2007, we employed approximately 64,000 people, of whom 531 were in advisory and supervisory capacities, 3,445 were in store management positions and 41 were officers. Many restaurant personnel are employed on a part-time basis. None of our employees are represented by any union, and management considers its employee relations to be good.

## COMPETITION

The restaurant industry is intensely competitive with respect to the type and quality of food, price, service, location, personnel, concept, attractiveness of facilities, and effectiveness of advertising and marketing. We compete with a number of national and regional restaurant chains as well as locally owned restaurants. The restaurant business is often affected by changes in consumer taste; national, regional, or local economic conditions; demographic trends; traffic patterns; the type, number, and location of competing restaurants; and consumers' discretionary purchasing power. In addition, factors such as inflation, increased food, labor and benefits costs and the lack of experienced management and hourly employees may adversely affect the restaurant industry in general and our restaurants in particular.

## RAW MATERIALS SOURCES AND AVAILABILITY

Essential restaurant supplies and raw materials are generally available from several sources. However, in the restaurants, certain branded items are single source products or product lines. Generally, we are not dependent upon single sources of supplies or raw materials. Our ability to maintain consistent quality throughout our restaurant system depends in part upon our ability to acquire food products and related items from reliable sources. When the supply of certain products is uncertain or prices are expected to rise significantly, we may enter into purchase contracts or purchase bulk quantities for future use.

Adequate alternative sources of supply, as well as the ability to adjust menus if needed, are believed to exist for substantially all restaurant products. Our retail supply chain generally involves longer lead-times and, often, more remote sources of product, including the People's Republic of China, and most of our retail product is distributed to our stores through a single distribution center. Although disruption of our retail supply chain could be difficult to overcome, we continuously evaluate the potential for disruptions and ways to mitigate them should they occur.

## ENVIRONMENTAL MATTERS

Federal, state and local environmental laws and regulations have not historically had a significant impact on our operations; however, we cannot predict the effect of possible future environmental legislation or regulations on our operations.

## TRADEMARKS

We deem the various Cracker Barrel trademarks and service marks that we own to be of substantial value. Our policy is to obtain federal registration of trademarks and other intellectual property whenever possible and to pursue vigorously any infringement of trademarks.



## RESEARCH AND DEVELOPMENT

While research and development are important to us, these expenditures have not been material due to the nature of the restaurant and retail industry.

## SEASONAL ASPECTS

Historically, our profits have been lower in the first three fiscal quarters and highest in the fourth fiscal quarter, which includes much of the summer vacation and travel season. We attribute these variations primarily to the increase in interstate tourist traffic and propensity to dine out during the summer months, whereas after the

school year begins and as the winter months approach, there is a decrease in interstate tourist traffic and less of a tendency to dine out due to inclement weather. Our retail sales historically have been highest in our second fiscal quarter, which includes the Christmas holiday shopping season.

#### WORKING CAPITAL

In the restaurant industry, substantially all sales transactions occur either in cash or by third-party credit card. Like most other restaurant companies, we are able to, and may often, operate with a working capital deficit. Restaurant inventories purchased through our principal food distributor are on terms of net zero days, while restaurant inventories purchased locally generally are financed through normal trade credit. Because of our retail operations, which have a lower product turnover than the restaurant business, we carry larger inventories than many other companies in the restaurant industry. Retail inventories purchased domestically generally are financed from normal trade credit, while imported retail inventories generally are purchased through wire transfers. These various trade terms are aided by rapid product turnover of the restaurant inventory. Employee compensation and benefits payable generally may be related to weekly, bi-weekly or semi-monthly pay cycles, and many other operating expenses have normal trade terms.

## ITEM 1A. RISK FACTORS

*Investing in our securities involves a degree of risk. Persons buying our securities should carefully consider the risks described below and the other information contained in this Annual Report on Form 10-K and other filings that we make from time to time with the Securities and Exchange Commission, including our consolidated financial statements and accompanying notes. If any of the following risks actually occurs, our business, financial condition, results of operation or cash flows could be materially adversely affected. In any such case, the trading price of our securities could decline and you could lose all or part of your investment. The risks described below are not the only ones facing our company and is not intended to be a complete discussion of all potential risks or uncertainties. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations.*

***We face intense competition, and if we are unable to continue to compete effectively, our business, financial condition and results of operations would be adversely affected.***

The casual dining sector of the restaurant industry is intensely competitive, and we face many well-established competitors. We compete within each market with national and regional restaurant chains and locally-owned restaurants. Competition from other regional or national restaurant chains typically represents the more important competitive influence, principally because of their significant marketing and financial resources. However, we also face growing competition as a result of the trend toward convergence in grocery, deli and restaurant services, particularly in the supermarket industry. Moreover, our competitors can harm our business even if they are not successful in their own operations by taking away some customers or employees or by aggressive and costly advertising, promotional or hiring practices. We compete primarily on the quality, variety and value perception of menu and retail items, the number and location of restaurants, type of concept, quality and efficiency of service, attractiveness of facilities and effectiveness of advertising and marketing programs. We anticipate that intense competition will continue with respect to all of these factors. We also compete with other restaurant chains and other retail businesses for quality site locations and management and hourly employees, and competitive pressures could affect both the availability and cost of those important resources. If we are unable to continue to compete effectively, our business, financial condition and results of operations would be adversely affected.

***Our business is affected by changes in consumer preferences and discretionary spending.***

Our success depends, in part, upon the popularity of our food and retail products. Shifts in consumer preferences away from our restaurants or food or retail items would harm our business. It is difficult to predict what merchandise consumers will demand, particularly merchandise that is trend driven. Failure to accurately predict constantly changing consumer tastes, preferences, spending patterns and other lifestyle decisions, or to address consumer concerns effectively, could adversely affect short-term and long-term results because a substantial part of our business is dependent on our ability to make trend-right decisions for a wide variety of food items and merchandise. Also, our success depends to a significant extent on discretionary consumer spending, which is influenced by general economic conditions and the availability of discretionary income. Accordingly, we may experience declines in sales during economic downturns or during periods of uncertainty like those that followed the terrorist attacks on the United States on September 11, 2001 and Hurricanes Katrina and Rita in September 2005. In addition, recent increases in fuel and other energy prices as well as consumer uncertainty that has accompanied the recent home mortgage and credit “crisis” and general weakness in housing markets could result in decreases in discretionary consumer spending. Any material decline in consumer confidence or the amount of discretionary spending could have a material adverse effect on our sales, results of operations, business and financial condition.

***The price and availability of food, ingredients and utilities used by our restaurants or merchandise sold in our retail shop could adversely affect our revenues and results of operations.***

We are subject to the general risks of inflation; however, our results of operations depend significantly on our ability to anticipate and react to changes in the price and availability of food, ingredients, utilities, retail merchandise, and other related costs over which we may have little control. Fluctuations in economic conditions, weather and demand can adversely affect the availability, quality and cost of the ingredients and products that we buy. We require fresh produce, dairy products and meat, and therefore are subject to the risk that shortages or interruptions in supply of these food products could develop. Our operating margins are subject to changes in the price and availability of food commodities. For example, the recent focus on ethanol as a fuel, as well as the emergence of China as a major consumer of food products, has placed tremendous demands (with attendant supply and price pressures) for corn and dairy products, which in turn increase feed

costs for poultry and livestock. The effect of, introduction of, or changes to tariffs or exchange rates on imported retail products or food products could increase our costs and possibly affect the supply of those products. Our operating margins are also affected by fluctuations in the price of utilities such as natural gas, whether as a result of inflation or otherwise, on which the locations depend for much of their energy supply. Our inability to anticipate and respond effectively to an adverse change in any of these factors could have a significant adverse effect on our results of operations. In addition, because we provide a moderately-priced product, we may not seek to or be able to pass along price increases to our guests sufficient to offset cost increases.

*We are dependent on attracting and retaining qualified employees while also controlling labor cos*