Jun 8th, 12:00 AM - Jun 10th, 12:00 AM

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Repository Citation
Green, Yvette and Williams, John, "An Examination of operating costs within a state's restaurant industry" (2010). Caesars Hospitality Research Summit. 11.
https://digitalscholarship.unlv.edu/hhrc/2010/june2010/11

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An Examination of Operating Costs within a State’s Restaurant Industry

ABSTRACT

An examination of operating costs within a state’s restaurant industry. The study provided benchmark data that restaurants can use to make sound strategic business decisions. The results provided vital information that can be used in conducting future research.

INTRODUCTION

The Louisiana restaurant industry is a major driver of the state’s economy. Restaurants in Louisiana have an annual economic impact of $5.9 billion. For every $1 spent in restaurants in Louisiana, an additional $1.05 in sales is generated for other industries in the state. State sales tax revenue generated by the Louisiana restaurant industry is more than $134 million annually and there are approximately 10,700 eating-and-drinking places in Louisiana. It is estimated by 2017 that employment in the restaurant industry in Louisiana is expected to increase 20.4% (Louisiana Restaurant Association, 2009).

There is no denying the impact that the restaurant industry has on the state of Louisiana. However, the success of the restaurant industry relies heavily on the creativity of restaurateurs to control operating costs while increasing sales revenue. The purpose of the study was to examine operating costs within a state’s restaurant industry, a phenomenon which had not been done in the past. This gap in information provided the impetus for the study. Ultimately, the study reported comprehensive data on the state’s restaurant industry in the critical business area of operating costs and provided benchmark data that restaurants can use to make sound strategic business decisions.

LITERATURE REVIEW

For the past few years, the wholesale cost of food has steadily increased. In 2007, the US Department of Agriculture reported sizable increases in food staples. For example, the cost of eggs increased by 29%, while whole milk increased 13.1% and citrus fruits by 10.1%. The cost of bread increased by 7.4%, while coffee went up by 6.3%. The costs of chicken and beef increased 5.8% and 4.4%, respectively (USDA, 2007). Other increases which impacted restaurants included an increase in energy costs, fuel surcharges for food delivery, and increases in wages (Lockyer, 2008; Schwartz, 2008).

To combat the increases in food, utilities and labor, restaurants have tightened cost cutting measures as well as become creative such as entering into food co-ops (Lockyer, 2008). Independent operators benefit from food co-ops by pulling purchasing power from several independents. Chain operators already benefit from purchasing power based on the size of the restaurant chain (Lockyer, 2008). Another measure to combat the increase is to off-set it with menu price increases (Gale, 2007; Killian, 2008). In a 2006 study by Restaurants and Institutions, surveyed restaurants increased their menu prices by 2.5%, however, were not sure as to what represented an optimal menu price increase. (Gales, 2007).
With each passing year, the cost of doing business is steadily rising and restaurants need a means of benchmarking and monitoring the trend on a local level as well as national level.

**METHODOLOGY**

*Survey Instrument*

The survey instrument was developed through a literature review and input from restaurateurs across the state of Louisiana. The survey included questions on general restaurant demographics, sales and expenditures, operating costs, salaries, wages and benefits, and business expansion. The survey was posted and collected using SurveyMonkey.com.

*Data Collection and Analysis*

Using a database of approximately 3800 restaurant operations, the state restaurant association provided a link to the survey that was sent to all users in the database. After removing undeliverable emails, surveys representing 344 properties were received. The survey data was downloaded from the host site, SurveyMonkey.com after the survey was closed. The data was edited for accuracy and logical consistency. SPSS 15.0 was used to analyze the restaurant surveys. Statistics for the year 2005 were not compiled for all survey questions because of the incompleteness of data due to Hurricanes Katrina and Rita.

**RESULTS**

*Restaurant Demographics*

Restaurants responding to the survey represented organizations in business less than one year and up to 98 years. 10.2% were in business for one year or less, while 49.2% were in business 5 years or less. 32.3% of the restaurants were in business 25 years or more. 82.4%, an overwhelming number of restaurants in the survey, were independent operators. The other 17.6% of properties represented in the sample were corporate restaurants. Of respondents, 65.5% were single unit operations and 34.5% were multi-unit operators. Multi-unit operators had an average of 15.2 operations and 27.3% of the multi-unit operators were franchises. The mean number of seats for restaurants was 142 seats. The range of seats in restaurants was 18 seats to 500 seats.

*Costs*

Average food costs have risen over the past years. Food cost in 2004 was 31.6% and in 2006 it was 32.2%. In 2007, food cost was 32.7 % then in 2008 it jumped to 36.5%. Beverage costs have remained relatively consistent over the past years. Beverage cost in 2004 was 19.9% and in 2006 it was 22.1%. In 2007, beverage cost was 21.8% and in 2008 it was 22.2%. Labor costs have risen over the past several years. In 2004, labor cost was at 24.9%. Following Hurricanes Katrina and Rita, it jumped to 27.0% in 2006. In 2007, labor cost was 28.0% and it jumped again in 2008 to 29.7%. Table 1 depicts this cost figures for 2004, 2006, 2007 and 2008.

| Table 1: Food, Beverage and Labor Cost with Mean Percentage Increase by Year |

<table>
<thead>
<tr>
<th>Year</th>
<th>Food Cost Increase</th>
<th>Beverage Cost Increase</th>
<th>Labor Cost Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>31.6%</td>
<td>19.9%</td>
<td>24.9%</td>
</tr>
<tr>
<td>2006</td>
<td>32.2%</td>
<td>22.1%</td>
<td>27.0%</td>
</tr>
<tr>
<td>2007</td>
<td>32.7%</td>
<td>21.8%</td>
<td>28.0%</td>
</tr>
<tr>
<td>2008</td>
<td>36.5%</td>
<td>22.2%</td>
<td>29.7%</td>
</tr>
</tbody>
</table>
Since August 2005 (Hurricane Katrina), food cost was reported as increasing by 11.5%. Beverage cost has increased 5.4% since Katrina. Insurance has increased 38.9% while labor cost has increased 12.0% and liability/property/workman’s compensation has increased 13.3%. Since Katrina, restaurants are paying 9.2% more for water, 12.1% more for gas, 19.8% more electric, 6% more for payroll tax, and 11.9% more for marketing. Restaurants have raised their menu prices by 10.1% since August 2005 and have raised their beverage prices 9.0%. Table 2 shows the mean percentage increase in operating costs for restaurants since August 2005.

**Average Check, Menu Prices, Customer Counts**

Food sales were reported as 76.5% of total sales for restaurants. Beverage sales were 19.0% of total sales as reported by restaurateurs. The average check for breakfast was reported as $11.82. Average lunch check was $14.54 while dinner was $24.26. The average number of turns for restaurants was .54 for breakfast, 2.41 turns for lunch and 3.65 turns for dinner. Restaurateurs reported increasing menu prices by 10.13% and increasing alcoholic beverage prices by 8.95% since August 2005.

Since August 2005, 48.3% of restaurants increased their customer count at breakfast by 18.7%. 34.5% of the restaurants saw a decrease in breakfast customers by 9.6% and 17.2% of restaurants maintained the same customer counts for breakfast. Lunch customer counts for restaurants were reported with 34.8% of restaurants having a 22.7% increase in customers, while 54.3% of restaurants had a decrease of 18.6%. 10.9% of restaurants reported their lunch customer counts remained the same. Dinner customer counts for restaurants were reported with 28.6% of restaurants having a 20.2% increase and 61.2% of restaurants had a decrease of 17.6%. 10.2% of restaurants reported that their dinner customer counts remained the same.

**Table 2:**

<table>
<thead>
<tr>
<th>Cost</th>
<th>Mean % Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Food</strong></td>
<td>11.57</td>
</tr>
<tr>
<td><strong>Alcoholic beverage</strong></td>
<td>5.4</td>
</tr>
<tr>
<td><strong>Insurance</strong></td>
<td>38.9</td>
</tr>
<tr>
<td><strong>Labor before Payroll Taxes and Benefits</strong></td>
<td>12.0</td>
</tr>
<tr>
<td><strong>Liability/Property/Workers Comp</strong></td>
<td>13.3</td>
</tr>
<tr>
<td><strong>Water</strong></td>
<td>9.2</td>
</tr>
<tr>
<td><strong>Gas</strong></td>
<td>12.1</td>
</tr>
<tr>
<td><strong>Electric</strong></td>
<td>19.8</td>
</tr>
<tr>
<td><strong>Payroll Taxes and Benefits</strong></td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Marketing</strong></td>
<td>11.97</td>
</tr>
</tbody>
</table>
DISCUSSION

The results showed a steady increase in food cost and labor cost, while beverage costs remained steady for 2004 through 2008. Restaurant operators faced additional challenges with the percentage increase of other costs, the greatest being insurance, followed by utilities and marketing. The cost of doing business is becoming increasingly more expensive for operators. Restaurateurs are looking for ways to cut costs without having to pass the expense onto the customer (Lockyer, 2009; Tanyeri, 2009). An interesting trend was the increase in breakfast customer counts as oppose to lunch and dinner counts. This was supported by a slightly higher average guest check for breakfast. Perhaps restaurateurs are capturing breakfast guests because the average guest check is lower than lunch or dinner and guests appear to spend a little more at breakfast accounting for the increase in this guest check. The restaurants reported menu price increases that were higher than average on a national basis.

Restaurateurs have a unique challenge in balancing the increases in operating costs with maintaining a steady profit margin. Increased sales would off-set this trend, however, a decline in consumer discretionary spending impacts this solution. Other alternatives may include reduction in portion size or reduction in quality purchase standards. Both may have a positive impact on controlling costs for the restaurant operators, but may have a negative impact on the guest. Restaurant operators can control costs through other measures such as inventory management, reduction in theft, waste and spoilage. These production control measures will not have guest impact and will go along way in reducing costs for the operator.

CONCLUSIONS

In conclusion, the study yielded interesting results on the state restaurants. The benefits and significance of such a study to restaurateurs and academics are great. Results of the study will help restaurants with strategic planning and allow restaurateurs to do comparatives for their organization in comparison to other organizations as well as analyze trends. The survey provided crucial information for the restaurateurs on the impacts of increases in food and beverage commodities as well as overhead costs.

On the academic side, this study is the first of its kind in the nation collecting such comprehensive restaurant operations data on a state level. The study provides the framework for longitudinal data collection, which in turn will allow trending research to benefit the state restaurant industry.

As with all research, this study was not without limitations. The results of the study represent the state of Louisiana restaurant industry. The results cannot be generalized to the US restaurant industry.

FUTURE RESEARCH

This study provided an important first step in assessing the current state of the restaurant industry in the state of Louisiana. The results provide vital information that can be used in conducting research. It also serves as an example for other states interested in gaining a more comprehensive overview of the restaurants in their states.
REFERENCES


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United States Department of Agriculture Food Staples Statistics (2007).