WHITE PAPER

5 Steps to Mastering Restaurant COGS

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Introduction

If you're reading this, you already know how vital controlling COGS is to securing lasting success in the restaurant business. Over the course of a year, shaving just 1 or 2% off the 28–35% paid in food, beverage, and packaging leads to a surprisingly outsized bottom-line improvement. Likewise, when COGS begin their creep upward, profits grow more and more elusive.

Thankfully, COGS ***can*** be brought down in a short period of time. It requires diligent work in both the back office and the back-of-the-house, but meaningful improvements are very possible in as few as 60–90 days.

This white paper aims to comprehensively explain what goes into a restaurant's COGS, and will give actionable tips, strategies, and procedures to lower expenses and increase the bottom line.

Much of this information may already be known to the seasoned operator. But if this white paper gives you **one** takeaway that leads to a profit increase, then I'd consider reading it time well spent.

Andy Moore
Founder, RestaurantBoost

What Makes Up COGS?

Let's start with a recap of the basics...

In the context of the restaurant industry, COGS ("Cost of Goods Sold") are the expenses incurred in procuring and utilizing ingredients to prepare dishes served to guests.

The COGS number includes the total costs of the food, beverages, and any other items associated with preparing and delivering meals, like packaging and paper goods.

Calculating COGS is pretty straightforward. You take the following three variables for a given time period (which is typically a month):

- Beginning Inventory: The value of the inventory that's left over from the previous period
- Purchased Inventory: The value of the food, beverage and packaging purchases you make in the upcoming time period
- Ending Inventory: The value of the inventory that's left over at the end of the given time period

And then you run the following calculation:

COGS = (Beginning Inventory + Purchased Inventory) - Ending Inventory

So if a restaurant had $5,000 worth of goods on hand at the beginning of the month, it purchased $20,000 worth of goods during the month, and it ended the month with $3,500 in inventory, the restaurant's COGS would be:

($5,000 + $20,000) - $3,500 = $21,500

Let's say that the restaurant grossed $75,000 in sales for the month. That then means its COGS percentage was:

($21,500 / $75,000) * 100 = 28.6%

Which is pretty good.

#1 - Strategic Sourcing

Perhaps the most impactful place to reduce restaurant COGS is in the sourcing and procurement process. Here are some tips on how to leverage this often-overlooked area:

- **Develop relationships with suppliers and distributors.** Open communication establishes trust and lays the groundwork for mutually beneficial partnerships. Seek to understand how both parties can help each other.
- **Look for opportunities to consolidate SKUs.** Look for opportunities to cross-utilize ingredients and packaging products. Without sacrificing quality, consider sourcing pre-made products that can help reduce the burden of storing ingredients that spoil quickly.
- **Comparison shop to find better pricing**. This is the difficult work that really moves the needle — proactively sourcing more economical suppliers, while not sacrificing the quality of your products. It's critical to not burn bridges with current partners, but it's equally important to also stay informed of cost-effective alternatives.
- **Leverage market/demand forecasts and lock in contracts**. By accurately forecasting demand and negotiating longer-term deals, restaurants can take advantage of supplier discounts and preferential pricing. Long-term commitments demonstrate commitment to suppliers, which can lead to more advantageous pricing and terms. These deals also can be a good opportunity to secure consistent pricing if you're forecasting choppy market conditions in the future.
- **Don't neglect packaging.** While to-go orders have declined somewhat form their 2020-2021 peak, packaging and paper goods can still be a significant line items. They should also be monitored.

- **Audit invoices.** Mistakes happen, and it's imperative that any invoice overcharges are quickly caught and credited.
- **Maximize overall value.** Don't just negotiate to obtain the lowest price. Focus on maximizing value by considering customer satisfaction, product quality, and reliability.

#2 - Technology and Data-Driven Analysis

The POS ... and Other Technological Solutions

Building a technologically connected COGS management program requires fully utilizing the POS's **robust menu-mix reports**. This means creating a thoughtfully laid-out POS architecture that links every button that's tapped with its corresponding menu item. (These menu mix reports will really come in handy in both menu engineering and inventory management.)

Collect historical sales data and use the POS to identify any sales trends. Look for patterns related to the time of day, day of the week, or seasonality. This information can guide you in making pricing and promotional decisions.

The POS is also the key link to inventory and accounting software programs. And other, more futuristic tools also now exist to help lower COGS: For instance, a few tech startups can leverage **security cameras and AI** to tell when an employee is over-portioning a dish.

Leveraging Data to Improve Your Bottom Line

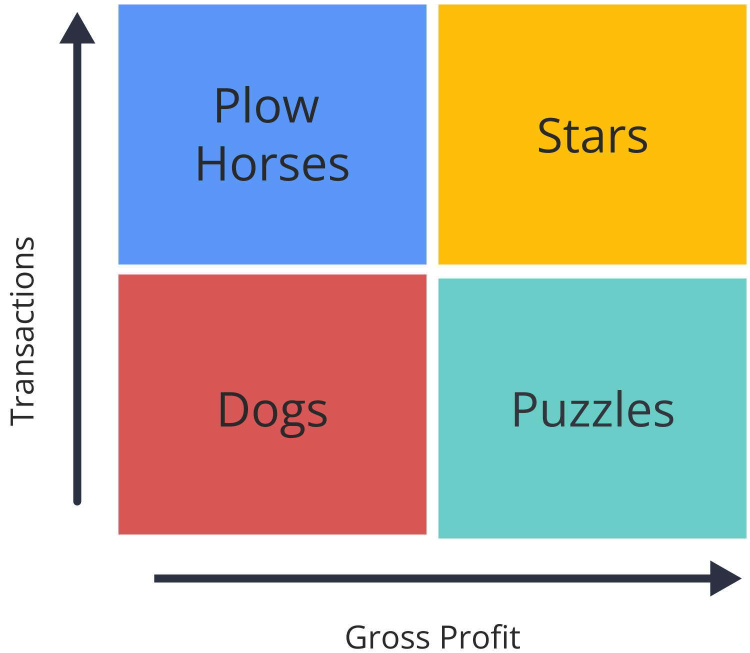
Routinely **calculate your ideal food cost** by utilizing recipe cards, recent invoice data, and the POS menu mix — while assuming perfect portioning, no waste, and no theft. Then match this "perfect" number with your actual food-cost number (calculated in the previous section).

The variance between the two numbers is due to any combination of the following: over-portioning, vendor overcharges, waste, or theft. If you do this calculation on a regular cadence, and break the information down item by item, you can **begin to test solutions to lower the variance**. For instance, if you calculate a high variance with French Fries, you can assume the variance is at least partly due to over-portioning and can begin to incorporate items like portion-control fry scoops into your system.

This exercise will nearly always lead to eye-opening, actionable data.

#3 - Menu Engineering

After running a POS analysis of your menu mix and calculating your theoretical food costs for each recipe, you can organize your menu into the following 4x4 matrix:



This data can lead you to a process of more systematically engineering your menu:

- **Plow Horses** are items customers love, but that aren't yet profitable. They could be good candidates for a price increase - or perhaps their portion size can be reduced, which would help their gross margins.
- **Dogs** aren't profitable or popular. The easy answer is to cut them from your menu — but sometimes a better solution is to first rework their ingredients or costs in an effort to move them up and to the right on the matrix.
- **Puzzles** are worth dedicated attention — they're profitable but not yet popular. Consider a name change or incorporating them in a marketing campaign.
- **Stars** are things of beauty — they're profitable and popular. Boost them at the top of your menu. (Consider even design element like boxes or icons to draw attention to your Stars.)

Finally, a note on the **size of your menu**:

During the pandemic, many brands were forced to make menu cuts due to supply-chain and labor shortages. What they found was that a concise menu not only simplifies the customer ordering journey, but it can also lead to a COGS reduction, as this greatly simplifies inventory management... which we'll discuss in detail on the next page.

#4 - Inventory Management

Never a particularly sexy part of running a restaurant, thoughtful inventory management and a **consistent** (key word) counting program are nevertheless imperative to controlling COGS. Inventory is, after all, made up of products that cost real money.

Here are some thoughts on setting up an inventory program that both gets used and increases your bottom line:

- Regardless of whether the restaurant is counting weekly or monthly, inventory should be **counted at the same time each period**. It's jarring how much effect flip-flopping between morning and evening counts can have on a COGS number.
- When creating an inventory count sheet, it's helpful to **place yourself in the operator's shoes**. How can the count sheet be organized to minimize the number of steps the operator takes? What units of measurement should be utilized to make the counting process straightforward, while still summing up to an accurate tally?
- Build in **flexibility for different pack sizes** on the inventory count sheet. While it would be wonderful if every item came in the exact same case and pack each month, we all know that's a tough target to hit. If you have multiple stores and you're ordering from multiple distribution centers, this area is where an inventory software can really earn back its investment.
- Consider implementing a **critical-item report**. This is a super-simple report where an operator counts 10-15 key items every shift - while the report won't be used in calculating the monthly COGS number, it does act as a helpful theft deterrence.
- While a restaurant should never run out of an item during service, aiming towards a **just-in-time inventory strategy** is a worthy goal. Cash is better in a bank rather than on a shelf, and this strategy reduces the indirect costs of carrying too much inventory. Use historical sales data and market forecasts to order the right amount of inventory to meet customer demand without overstocking. Stock the inventory by the **"First In, First Out" (FIFO)** method and label all perishable items with the product's expiration date.
- That being said - while overstocking perishable items is always a bad idea (tossing expired inventory hurts!), in our recent experience, the savings found from buying non-perishable items (like packaging and paper goods) **in bulk** may now exceed the cost of tying up cash in big purchases. It may seem silly to buy that case of 12,000 straws, but if you expect to use them in a reasonable period of time, then that is increasingly looking like a good investment.

#5 - Employee Engagement

It's great if you and your accountants are dialed in on COGS, but none of it matters if the frontline is not also engaged. Here are some actionable ideas for boosting their involvement:

- **Implement checklists.** As Atul Gawande wrote in *The Checklist Manifesto*, "Good checklists are precise. They are efficient, to the point, and easy to use even in the most difficult situations. They do not try to spell out everything--a checklist cannot fly a plane. Instead, they provide reminders of the most critical and important steps." With that in mind, here are two vital checklists to incorporate into your system :
  - **Temperature checklist**: Not only is a temperature checklist critical for ensuring food safety, it can help you save thousands of dollars in lost product. Never be surprised by a dead walk-in cooler - develop a consistent routine for checking refrigeration temperatures multiple times a day.
  - **Line checklist:** This checklist in hand, the operator walks down the line, making sure par levels are correct, portion controls are in the correct places, and, of course, temperatures are at their correct levels.

- **Highlight the impact of kitchen waste.** An average of 4-10% of restaurant food is wasted before making it to a customer (source: Foodprint.org). Tracking waste can be relatively high-tech (several software programs include waste tracking capabilities) or low-tech, yet still effective: Simply keeping a waste-only trash can in the kitchen makes for a visible post-shift reminder of missed opportunities.
- One useful exercise to use in training staff on how costly waste can be:
  - **Collect a pile of 100 pennies**, representing all the restaurant's sales. Ask the staff how many "pennies" they believe the restaurant profits each month.
  - Then pull away each line item expense (i.e. remove 25 pennies to represent 25% in labor costs). Even for profitable restaurants, the amount that's left is nearly always less than the staff's best guess.

#5 - Employee Engagement

- **Portions, portions, portions.** Portion control starts at the recipe level. Developing consistent portion sizes for every element of the recipe - standardized across the menu as much as possible - increases training effectiveness and ensures that's what taught to the frontline really sticks.
  - Notice if you're regularly throwing away extra food. Reconsider your portion sizes if most customers can’t finish your dishes. They won’t know the difference, and you’ll reduce your COGS.
  - Create clear instructions for each recipe, laying out the specific portions to include in the menu item build. Include in the instructions the ideal food cost of the item (which helps increase employee awareness of the value of what they're selling).
  - Make use of scoops, ladles, and other tools to portion out ingredients.
  - Film the proper way to make each item. A robust learning-management platform can be used, but even just a series of iPhone videos (with subtitles) will work. Drill the proper movements in crafting the dish so no ingredient is wasted.
  - A side benefit: in the process of dialing in each menu item, you'll be crafting ever more consistent experiences for your guests.
- Make an operator's job easier by **eliminating some of the guesswork involved in placing the food order**. Utilize forecasted sales, a targeted food cost, daily sales tracking, and recent purchases to give managers a budget to spend on each truck.
- **Incorporate a clear employee discount policy**. This has been shown to help cut down on theft.

Conclusion

Controlling COGS is never something that's permanently "solved." Measurable improvements **can** be achieved in a short period of time, but restaurants that succeed over the long-term embrace the concept of continuous improvement. Keep refining your processes - pulling in more actionable data, implementing new innovative training procedures, sourcing more cost-effective products. You've got this.

To find out more about RestaurantBoost can help increase your business's bottom line, request a FREE review of your most recent invoices by emailing andy@restaurantboost.co, with the subject line "Invoice Review."

Thank you for reading!