Food & Beverage - Do You Know Your Break Even Point? - By Joe Dunbar

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In my MBA program at Rutgers University, they made sure every graduate could calculate break even points. We were given a myriad of scenarios with a variety of variables. Our tests included irrelevant information to make sure we could focus on the essential formula. Break even point analysis was taught in microeconomics, cost accounting, advanced cost accounting, finance and analytical techniques courses.

The basic formula for determining your break even point follows:

BE=FC/(1-VC%)

BE Break Even Point

FC Fixed Costs

VC Variable Costs

If your business had fixed costs of $500,000 and a 75% variable cost rate, your break even point is $2,000,000. If your fixed costs are $800,000 and your variable costs are only 60%, you'd have the same $2,000,000 break even point.

Which operation would you prefer to own in a growth market? How about a recession?

When a business experiences solid growth, it's possible to increase fixed costs and prosper. The operation with the low variable cost % would be the growth choice. However, you'd want the low fixed cost scenario during recessions.

Think of higher fixed costs as unit expansion. You invest in new FF&E, leasehold improvements, etc. and you expect a big increase in sales and profits. Restaurant expansion may slow this year. We may see units closing and corporate management positions decline in number. Companies are working hard to lower their fixed costs.

When you read about comparable unit sales in the financial press, get your calculators out. If our unit with the $500,000 fixed costs above experienced a 10% drop in sales, fixed costs would need to drop $50,000 to maintain the same break even point. With higher commodity costs, food manufacturers and suppliers are raising prices. Market prices have shot up in major grains and dairy markets. Delivery costs are up due to higher energy prices.

The government may eliminate food and energy from the core inflation rate but we can't ignore these increases. If your sales are in decline and your variable costs are increasing, it's probable last year's profit may not be possible. If you use the previous year's results in your budget calculations, management meetings will be more contentious this year.

The smart operators will look for unique menu solutions which reflect value to customers and help lower variable costs. Buying new equipment is a risky gamble in this climate. It's best to constrain your menu team with the existing equipment. Look carefully and evaluate the work needed to prepare and finish any new menu items. Labor cost is a key component of variable costs.

What items can you add to a dinner menu? A popular pasta dish is a good choice for these profitable meals. The sauce may be reused for several days without additional labor. The pasta is cooked to order and is shelf stable. You can offer profitable add on items like shrimp and chicken. Try to buy the same shrimp and chicken specifications already used in your base menu. We want to limit the number of protein items required overall.

Joe Dunbar

Dunbar Associates

P.O. Box 579

Fairfax, VA 22038-0579

800-949-3295

http://www.joedunbar.com

jdunbar401@aol.com