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Operators sold on new purchasing strategies

BY CATHERINE R. COBB

Faced with escalating costs for just about every food item that comes in the door, many operators are finding creative ways to slice their purchasing expenditures.

According to the U.S. Department of Agriculture, the prices of commercial vegetables, grains, milk, eggs, chicken and beef all have risen considerably in the past year, due in large part to the ripple effect caused by higher corn prices and unfavorable weather in some parts of the country. The All Farm Products Index, which reflects the prices received by farmers for their livestock and crops, jumped 23 percent during the 12 months from October 2005 to October 2006.

To offset higher costs, operators are reviewing the lengths and terms of their purchasing contracts, revamping their purchasing strategies to take advantage

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NEWS

Industry players sold on new purchasing tactics

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of greater economies of scale, seeking the advice of purchasing consultants and more carefully weighing the development of new menu items.

Matt Riddleberger, director of purchasing for the 295-unit Firehouse Subs chain, said that in his 25-year tenure in the foodservice industry he has never seen such a difficult market.

"Typically throughout history when some things have been up, others were down," he said. "But now, everything we buy is up and continuing to move up drastically."

Riddleberger said the Jacksonville, Fla.-based sub chain now negotiates all of its agreements and locks in prices for about six months, all the while taking downside protection so that if the market falls, Firehouse Subs' costs go down.

"Obviously, it is important to make sure that if the market does fall we are protected — otherwise we'll be paying a higher price," he said. "Can you imagine if all of a sudden the hedge funds get out of corn? So we have to protect ourselves."

Atlanta-based Focus Brands, operator and franchisor of 2,155 restaurants under such brands as Carvel, Cinnabon, Moe's Southwest Grill, Schlotzky's and Seattle's Best Coffee, stems its costs with a multipronged strategy.

"I've been in this business for 25 years, and I've never seen such tremendous cost pressures as the industry is facing right now," said Rich Kamph, the company's supply chain vice president. "We have to be vigilant. Every day we get another notice from another vendor on an upward price action."

First, Focus uses consultants for help in forecasting and deciding the appropriate time to hedge, Kamph said. In addition, while the company's portfolio of brands used to go to market separately, now they use a collaborative approach.

"We are often trying to buy common products that we can use in our different concepts," he said. "In the current environment, we actually see the benefit in not so much reducing costs but in maintaining and controlling them."

Focus also is asking vendors for longer-term contracts than it did before. This gives vendors the opportunity to do more capital investments, he said.

"While this is not really the time to enter into a long-term commitment, because of it we have gotten some vendors to lower margins sometimes," he said.

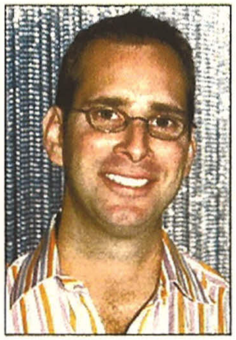
In addition, Focus has hedged some of its wheat, soy and butter fat purchasing to predict more accurately its menu inputs on a longer-term basis.

"This way we can tell what our mix is going to cost," Kamph said.

Cost consciousness also is playing a bigger role in menu development at Focus, with purchasing, marketing and product development teams working in tandem to design new menu items that are less susceptible to cost increases, Kamph said.

"For example, with the significant rise in dairy prices, we promoted a [nondairy-based] sorbet in June at the Carvel stores," he said. "That proved successful and offset the higher cost of dairy."

Maryville, Tenn.-based Ruby Tuesday has an in-house team of purchasing people that negotiates and secures long-term contracts on all of its major products, said Rick Johnson, a senior vice president of the 935-unit casual-dining chain. The team monitors commodities markets, stays in close touch with forecasts and trends, attends conferences, and talks and listens constantly to suppliers.



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— DAVID ABES
DIRECTOR OF OPERATIONS, HERE TO SERVE RESTAURANTS

"Over the past several years, and including this one, we have kept our overall cost of goods relatively flat by offsetting unavoidable price increases with savings on other products," Johnson said. "But it is an ongoing battle."

Lebanon, Tenn.-based Cracker Barrel Old Country Store says there has been a fundamental change in the way the chain views the purchasing process.

Ed Greene, senior vice president of strategic initiatives for the 566-unit family-dining chain, said in an environment where commodities are volatile and escalating, it makes sense to re-evaluate whether to have a fixed price for a period of time or to let it fluctuate based on variables that are determined in advance.

"This is a more complex method of purchasing, but appropriate and necessary in an environment such as the one in which the industry is operating these days," he said.

He said when working with fixed, versus variable, pricing structures, a company must be aware of any risk premiums that might be embedded within the costs.

"This is all about which suppliers we do business with and under what terms and conditions, and is in the context of doing business with the most competitive suppliers who can meet our specifications," he said. "We will not sacrifice our quality standards."

Consultants are helping to rein in costs at Tom Catherall's Here to Serve Restaurants and Fifth Group Restaurants, both in Atlanta. Officials at both companies said that given their sizes, nine restaurants for Here to Serve and five for Fifth Group, hiring a consultant was more economical than hiring a full-time purchasing professional.

David Abes, director of operations for Here to Serve Restaurants, which owns such eateries as Prime, Twist and Lola, said his company has been working with Dallas-based Lee Plotkin of LP Enterprises for about six months. Here to Serve is still in the preliminary stages of receiving bids through the consultant and comparing what's on paper to what Here to Serve is paying.

"We are going to save a ton of money, probably a couple hundred thousand dollars," he said. "It was definitely less expensive to hire him as it would have cost us double to hire someone."

Abes would not disclose the amount of the retainer-based fee the company pays to Plotkin.

Robby Kukler, co-founder and owner of Fifth Group Restaurants, said using an outside consultant was the best choice for the company with five restaurants and a catering company.

"We just didn't feel as if it was a full-time job, but we knew we had to leverage our economies of scale," he said.

Fifth Group, which owns Food Studio, two South City Kitchen restaurants, Ecco and La Tavola Trattoria, also used Plotkin.

"So many other costs are going up that we cannot control, like health insurance, utilities, liability insurance," he said. "We have one of the most price-sensitive industries out there, so we cannot constantly pass on price increases to guests. So we asked ourselves, 'Where can we manage our costs?'"

Kukler estimated that Plotkin has saved the company somewhere in the six-figure range. ■

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