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## Business Reference Guide Online

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### Restaurants -- Full Service

**SIC:** 5812

**NAICS:** 722110

**Number of Businesses / Units:** 945,000

#### Rules of Thumb

30 to 35 percent of annual sales plus inventory

2 to 2.5 times SDE plus inventory

2 to 3 times EBIT

2.5 to 3 times EBITDA

Note: California restaurants seem to be receiving higher multiples than the rest of the country with the possible exception of New York City. For example: 35 to 40 percent of annual sales and 2 to 5 times SDE.

#### General Information

"Advertisements, good customer service, and consistency will help to survive in this business."

"Restaurants with liquor licenses and entertainment permits always remain the most desirable restaurants to operate."

"Very seldom is there a profitable restaurant that has an absentee owner."

"Keep the number of items on the menu average; don't attempt to be everything to every customer."

"'Second Generation' restaurants are the way to go. In lots of instances, original owners have difficulty in paying upfit costs and end up selling for a few cents on the dollar."

"Location, good management, and a good lease are the key elements."

"Most 'rules of thumb' regarding valuation of restaurants don't apply across the board. Each is very individual unless the restaurant is a franchise. Don't forget to include CAM in calculating occupancy cost."

"Very rare to find a restaurant that is absentee owned and profitable. Some can do it but must gross over \$1.5MM."

"It's all in the lease! It's Location, Location, Location. Books must be well kept and make sense."

"In a slow economy it is important for restaurateurs to sharpen their prices, service, cleanliness and don't stop advertising (just have to look for the best results)"

"Don't do it, unless you can commit to 7-day work weeks and long hours."

"When going into this business, in my opinion, you need to plan to be there a lot. There are 2 kinds of bartenders out there. The ones that steal from you and the ones that steal from you a lot. You need to keep that in mind and plan to work the operation a lot."

"Anyone considering purchasing a restaurant would be wise to have some experience in the industry. Experience is less important for some of the quick-serve concepts, but it is important to determine if the hours and work environment are a good fit. Those considering a franchise should thoroughly review the terms and conditions of the franchise agreement as some have become inflexible to the point of making it difficult to make a profit."

"80% of \$15 to \$25 check avg restaurants are independents....65% have sales over \$1 million... 55% have less than 200 seats."

"Requires BOTH knowledge of back AND front of house"

"Absentee owners don't work very often. They call me all the time and want out because they aren't making any money. You need to be on site as an owner a lot. Customers like it and your employees need to be watched."

"Interesting that it's one of the toughest businesses to run successfully but still attracts many potential buyers that have a 'better idea.' Having been the wine steward of my own restaurant many moons ago, the business can be fun if you enjoy playing host."

"It is a people business. It is better that the buyer of this type of business be experienced in the food industry But I have seen many owners that started in this industry without any experience and by treating customers like royalty (giving superb service) and buying quality products have been very successful."

"To succeed in this business, a buyer should have capital to easily carry him for the first two years. It takes a long time, 12-24 months, for a community to get used to, comfortable, and familiar with a new eating establishment."

"They are tough deals to put together. It is important that even if the concept is outdated that the space is workable, there is a sufficient kitchen."

"A good operation can be successful if it is unique and interesting. It must be a fun place to come. Fine dining is very difficult. Never start too big. Must have a good physical plant. Ease of operation. Good kitchen. Storage and buying ability a must. Good system. Good accounting. Theft is a major problem. Most employees do not understand the damage which can be done when food and drinks are given away."

#### Full-Service Restaurant Model

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Use this as a model for a full-service restaurant as to the various categories of sales. A fine-dining restaurant might have 10 to 15 percent wine sales, while an Irish pub might have 10 to 15 percent beer sales.

#### Expert Ratings

• Competition	2.5	(1=Lot of : 4= Not Much)
• Amount of Risk	2.6	(1=Very : 4= Not Much)
• Historical Profit Trend	2.4	(1=Down : 4= Up)
• Marketability	2.2	(1=Low : 4= High)
• Industry Trend	2.2	(1=Declining : 4= Growing)

- Ease of Replication 2.4 (1=Easy : 4= Difficult)

### Expert Comments

"During the economy boom, there was an enormous growth of new restaurant sites and restaurant re-sales. Investors had no problems in securing bank financing, and homeowners were refinancing their mortgages to buy restaurants. With the current situation, many in the industry feel they overpaid for their purchases and are currently paying lease rates that are not justifiable with the current decline in business."

"One has to understand the trends."

"Current sales and profits are weak due to the poor economy. Most full-service restaurants in my area [California] have seen a decrease of 20-30% of revenues over the past year, with quick-serve declining in the range of 10-20%. There is still room for industry growth after we recover from the current economic downturn. There are great opportunities for experienced buyers at this time."

"More and more emphasis must be placed on quality of food and service to survive these days."

"Tough, but a fun business if you like long hours. Need to really have it in your soul."

"Market volume is dropping. Cost of opening a new location is getting more expensive. There are a lot of unprofitable locations for sale."

"Although many restaurants are sold each year, marketability is difficult due to bad revenue reporting and third-party financing."

"Cost of start-up is high, location is extremely important unless there is a uniqueness about the product and operation. It is important to look at historic trends against industry standards because the historic trends could be the real cost of the operation."

"1. The restaurant industry is extremely competitive and difficult. 2. Because of its competitive nature the industry is also extremely risky, especially for the uninitiated. 3. Profits have been trending downward in the current economy as many restaurateurs have found it necessary to reduce prices while suppliers are raising prices. 4. Location and physical facility are imperative. Customers want convenience and ambiance along with quality and price. 5. Marketability is difficult at best if you are to deliver a truly qualified buyer in a financial situation where the seller is almost invariably going to be asked to carry some or all of the paper. 6. Mom-and-pops are falling by the wayside and being crushed by the chains. The chains can afford to lose money in a market while destroying the local competition. 7. The physical plant, equipment and decor are fairly easy to replicate. What is difficult to replicate is employee attitude and customer service as well as some KEY menu items and recipes."

"Given the right combinations, a restaurant can be highly profitable and thus attractive to sell."

"Food costs have escalated after gas crunch. Anti-smoking laws have hurt."

"Highly competitive industry—competitors like to be in the same area as others"

"The restaurant industry will have a very difficult time; the industry trend will decline. It is extremely important to have the right concept for the location."

"Competition is usually not a consideration if it is the only concept in the trade area, but independent restaurants have to compete with franchise restaurants. It's critical for an independent, full-service-restaurant owner to have experience in the industry plus have good management skills."

"Competition from national chains and their advertising clout means an operator must strive for total perfection."

"Food service is one of the most competitive industries out there. Be aware of trends and a location or concept's potential longevity."

"1. Competition is daunting. Big chains can & do kill independents. 2. Very risky business due in large part to competition but also changing customer attitudes and the media. 3. Profit trends are down due to increasing labor costs and competition. 4. Location, location, location! 5. Tough to sell due to all other factors. 6. The field is growing but is being diluted by grocery and big discount stores selling pre-packaged meals. 7. Most any concept can be fairly easily replicated in menu and design. The key is in quality, quantity and service."

"This industry has been hard hit by fuel costs. Average covers are down. Average check is down. Many forced to reduce portion size to keep pricing competitive. Liquor/bar/lounge sales continue stagnant."

"You never know why one concept works or doesn't, but location is key and you're only as good as your servers!"

"Competition is very heavy between different food concepts. As gas prices go up, restaurant sales continue to go down."

"Competition and risk are both high because it's rather easy to enter the industry(getting harder) and too many novices attempt owning a restaurant. The economy is definitely affecting the bottom line. Due to the high cost of recent construction, the rent factors have increased and are cutting into the restaurant's profitability and also hindering the opening of new restaurants in prime locations. In the high-rent areas of Metro Orlando the costs have risen from \$25.00/S.F. to as much as \$60.00/ S.F. My office sales still constitute approx 45% food-related businesses. The industry is still growing although more difficult to replicate than in past years. "

"The location and quality of the assets and facility add value, even if the current concept is not profitable. Historical profitability is a key factor for determining the actual price. The more simple concepts translate to lower risk and this also results in a higher price. A restaurant requiring a skilled chef, or one closely associated with an owner's name and reputation, can be difficult to sell and the price will reflect the higher risk of transfer."

"The hard truth is that most restaurants fail. It is often the 2nd or 3rd restaurateur that makes a location work. Part of the reason is that that party has a lower initial cost than the original party that did the build-out, purchased new equipment, etc. Buyers benefit tremendously from seller's losses."

"Competition is high, there is an attraction to the restaurant business by a lot of people. They think it's like entertaining friends and a lot of fun. Of course, they find out differently, usually too late. Risk is also high because of competition, inexperience, high employee turnover and national chains taking a bigger chunk of the pie. Historical profit trends are in most cases increasing, more & more people eat out. Location & facilities are also improving and are now more important. Marketability is very good; my office sales are about 35% to 40% food-related sales. Personally, over 50% of my sales are restaurants. Industry trend is on the upswing, as cooking at home habits are changing to eating out. Ease of replication is thought to be easy, therefore there are a lot of new 'wannabe' restaurateurs and their inexperience adds to the high mortality rate in this industry."

"Higher petroleum costs have negatively impacted total sales, cost of goods and bottom line for smaller independents."

"Large amount of competition and risk, especially in metropolitan and populated suburban areas."

"Franchises have continued to increase product lines, and in some case combine products. Many now sell their food products directly to consumers in the supermarkets. Franchises generally maintain the better locations."

"Location is critical in most restaurants and it helps to have other ones around you to give the customers a choice."

"Consolidation is occurring at the highest levels in the industry, however the restaurant business is still one where a good idea can still flourish for the one-man operator."

"It generally takes at least 2 years for a new restaurant to reach its initial potential."

"There is nothing proprietary about any restaurant concept in the country today. The chains have the financial wherewithal and technical expertise to replicate anything that exists."

"Restaurants are not as attractive as bars due to the food component. Food automatically can drive gross margins up 15-20%. Most restaurants purchased will require a full 'face-lift' for an opportunity to do well."

"Highly competitive industry, management experience is very important."

"Competition is heavy because of the easy entry into the business. Location is paramount, and good space is difficult and expensive to obtain."

"Location, parking and access are important. Cleanliness, appearance of restaurant, as well as quality and taste of food, are key to the success. Liquor license for a restaurant serving dinner will attract customers and increase sales."

"Many restaurants rely on profit pockets, i.e., appetizers, drinks and desserts, to increase margins. Lack of disposable income impacting industry. DUI laws have had impact on liquor sales."

### **Seller Financing**

It ranges from 3 to 7 years, with most industry experts reporting 5 years.

### **Questions**

"Will the owner offer financing, training, non-compete (for how many miles), is the lease assignable, is all equipment approved by the NSF (many states do not allow domestic appliances in a commercial location), are trade name, Web site, recipes and training manuals included in the deal?"

"Reason for sale. Be aware of promotional advertising discounts that may increase sales but not profit. Make sure to understand the labor and staffing as there are often family members working with no pay, or there may be employees that are key to the business (chef or bartenders even, as examples). Know if Health Dept. is going to expect modifications to bring the facility or equipment up to code."

"How many hours do they work?"

"What is the real reason (not given reason) you want to sell?"

"How long since menu/price change?"

"Can you provide me with your most recent health inspection reports? Both operation inspections and structural!"

"What are the real costs of doing business and are the reported costs real?"

"If the equipment is owned or leased/rented, make sure it is in good and working condition. If the chef/cook will stay. The reason for sale. "

"Ask about the lease."

"Where is the labor pool? Who are key suppliers? What is the demographic base? Who are major employers in the market? Who are the competition?"

"What is the gross annual revenue? Are all equipments paid or leased and NSF approved? Are there any governmental issues, including city and health departments?"

"It is useful to know if the owner has experimented with different hours (breakfast, lunch, dinner, weekend brunch, late night entertainment. Of course the reason for sale is good to know. Any expected modifications from health dept. or franchisor? Any liquor license violations or restrictions?"

"Is there any competition coming to the area?"

"Review the lease in advance. Sellers often perceive, knowingly or not, that they have a more favorable lease than they do."

"Real financial information"

"Why are you selling? Tell me about your lease. What type of books do you keep?"

"Bring a tire iron and a pry bar and dig as deeply as possible."

"Blend of sales food/liquor"

"Ask about cash payroll. May sellers pay all or part of their payroll in cash. Check if the POS computer is connected to the corporate headquarters or franchise. How long the seller has owned the business might be a good indication that after they bought it they decided that they made a mistake and want out."

"I really think you have to ask as many as it takes to understand the operation, the employees, the financials, the seller discretionary earnings and verify it. More importantly the buyer needs to determine if he/she can do a better job than the present owner or at least match it."

"Ask about the competition in the area, both current and future/pending. Know if the marketing includes coupons which deeply discount the pricing. Take a close look at the labor expenses to determine if this is properly reflected. Realize that cost of goods can be distorted if the business is on a cash basis and does not count inventory regularly. Make sure to understand the lease terms including options to renew."

"How long have the employees been working there?"

"Why are you selling? Ask questions about the hours and days of operation to determine if there may be room for increasing sales based on changing the hours. Find out about coupons, discounts and promotions, to be aware of whether these may be increasing the sales without increasing the profits."

"Work histories of staff? Staffing resources? What vendors should I NOT deal with and why? Suggestions for growth or expansion?"

"Who is chef and how long has he/she been in place? Does chef have total control of menu?"

"Do they have good and current tax returns, are the federal, state and payroll taxes current and does the family have non essential employees on the payroll? Are sales taxes and gratuities being included in the sales? Some accountants will permit the operator to do that, then remove them as an expense."

"Which equipment do you own that is leased? Do you have any gift-card programs?"

"Why did you get in the business and why are you getting out?"

"How much of your income is in cash? How much of your payroll is paid in cash?"

"Does a refurbishment need to occur? Why are you selling now?"

"How to explain the high food and liquor costs and what type of marketing has and has not worked for him."

"How many hours a week do you work? If they say anything less than 50, don't believe them."

"What is your strongest area in your business? What part of your business needs the most improvement?"

"Vendor relationships, tenure of key help, rumored new competition, how long current menu/prices, outstanding gift certificates, lease restrictions,"

"Are you participating in any credit card advance programs? What equipment leases do you have in place?"

"What is the condition of the equipment, and how old? What type of liquor license will transfer with this establishment? Check the history with the health department."

"How long in business? How many employees? PT/FT? Gross Sales? Cost of Goods? Personal expenses paid by the business? Complete Lease Information. A list of all other business expenses. Reason for sale. Non-compete miles and years. etc."

"Length of lease with options, how long have key employees been with you, age and condition of equipment , where do customers come from, any liquor violations"

## **Pricing Tips**

"Number of meals served, average meal ticket, location, age of equipment"

"You need to understand the value of the liquor license."

"Common sense applies. If the business is named after a chef or the menu requires special skills, then it will be a riskier transition and will sell at the low end of a multiple. In contrast, a simple operation such as a coffeehouse or deli may sell at a higher multiple given the same SDCF. The operating hours will also be a factor in how the multiple is applied."

"Gross sales multiples are most relevant. Everyone thinks they can run it better themselves."

"With the recent economic conditions and excess market supply, most non-profitable restaurants are rarely valued over \$100,000."

"While gross revenue and SDE is important, one factor that may be easily overlooked is the number of days and hours the establishment is operated to achieve those numbers."

"Including the real estate, the sale price should be about 1 x gross sales."

"Food cost, wages, management costs"

"Pay close attention to the location and competition. Also, occupancy cost has never been more important than now. Note that if occupancy cost is over 10%, adjust accordingly."

"Some closed restaurants represent excellent opportunities to buyers with 'better ideas.'"

"The terms of the lease—assignability, relationship to market rent, remaining term and solid renewal options are key to the value of the restaurant."

"Business averaging less than \$750K in sales normally can be sold for 2.5 times EBITDA, but anything above normally gets sold to a pro operator, and most of them are not willing to go higher than 2 times EBITDA."

"Make sure that it is making a profit."

"Only add back what you can prove."

"Location is very important in this current economy. Annual revenue should exceed \$300,000; otherwise it should be listed as an asset sale."

"There are 5 critical criteria for restaurants to meet. #1 is location: busy location, high traffic, booming business in the area and finally mid to high income population. #2 is rent: it should not exceed 10% of gross revenue. #3 is conversion potential: can the restaurant be converted into another concept that will not compete with other restaurants within same particular center? #4 is condition of equipment: are they NSF approved and in good condition? Since they are expensive, we shouldn't overlook that. #5 is asking price: the most important is percentage of gross revenue, which shouldn't exceed 30%–40%, that's what experienced restaurant owners/buyers look for; and the gross annual revenue shouldn't be less than \$500,000 for a full-service restaurant, otherwise it should sell as an asset sale. If you have all these 5 criteria, the business will sell for market value."

"Lease terms and liquor license are important factors that can affect the value. If the facility is relatively new and up to current codes, it can be sold as an asset sale even with negative cash flow."

"1. Occupancy cost should not exceed 10% of annual gross sales. 2. Watch accounts- payable aging. Restaurant operators tend to drag vendors out to 60–90 days. 3. If cost of sales exceeds 35%, there is probably some skimming going on."

"Currently a buyers' market: must be profitable or will sell for depreciated asset value only. Lease obligations are a large part of negotiations."

"2 times EBITDA plus value of FFE + Liquor License + Inventory"

"Be wary of comparing industry statistics against smaller mom & pops who do not have equal purchasing power. Fuel surcharges are pushing costs much higher."

"Most restaurants will sell for 30%–35% of gross sales, but the bigger the business the better. Over \$2 million in annual sales normally needed to make real money."

"Adjust for exceptionally low operating hours vs. extremely long hours."

"Restaurants with small profits are worth more as an asset sale than based on sales or net cash flow. The cost of opening a new restaurant makes over 50% of the restaurants for sale only worth what the buyer feels he would have to spend to open a new one. The cost of permits and fees has driven the cost of new restaurants through the roof, and buyers should always consider taking over an existing one even if not profitable."

"You must factor in the value of the liquor license and understand if it is transferable. Being a cash business it is often difficult to find out what actual sales are."

"Including real estate the sale price should be close to 1x gross sales. Always use discretionary cash as a final check to be sure it makes sense to a buyer as well."

"The increase in supply of restaurants in 2008 due to the declining economic conditions, primarily in Southern California, have dramatically reduced the value of restaurants. The owner of a failing restaurant may be lucky just to receive some consideration while at the same time being relieved from the facility lease, thus stopping the bleeding."

"Non-franchise restaurants are worth 30%–40% of annual sales. Franchise sit down have been selling for 50% of annual sales, if they make a profit big enough to justify the price. Johnny Rockets are now selling for around 1 year's gross income. Franchise food not making money; before debt service, they are worth the value of the assets in place."

"The last 100 full-service restaurants sold were sold for an average of 2.2x Seller's Discretionary Cash Flow (SDCF), or cash flow available to a full-time working owner. The range was 0.0x (simply taking over a lease for a non-profitable venture) to 5.0x SDCF (well-established community icon with unique and non-duplicatable concept). Lease rate and term, and competitive environment are the most critical. In certain geographies, availability of liquor licenses may be even more critical."

"If real estate is included the sale, the price should be about 1x gross sales depending on condition and quality of the building. Any of these rules of thumb should be confirmed by deducting the debt service on 80% of the sale price (20% down) from the seller's discretionary cash and determining then what is left over for owner's income. This also needs to make sense to a buyer."

"Due to the high cost of creating a restaurant, we are seeing more conversion sales or asset sales. For unprofitable newer restaurants (with recent build-outs and newer equipment) having long-term leases in place, we can often recoup 1/3 to 1/2 of the total cost of creation."

"Adjust cash flow for Cost of Goods against industry standards of 30%–40%. Adjust % of sales multiple for rent factor against industry standards of 6%–8% Selling pricing compared to competition."

"5-day breakfast, lunch, or alcohol-only bar: 40% of sales. Large full-service over 6000-sf and \$1 million in sales: 25% of sales. All others: between 30–35% of sales depending on profitability and condition of facility."

"F, F & E have a 'Fair Market Value' of approx. 20% of new 'in place,' 10% 'off site.' Perishable inventory and 'open' liquor have no value at all. The BIG ONE: LOCATION, LOCATION, LOCATION!!!"

"Will typically sell in the 32%–35% of sales range."

"You have to be able to reconstruct the financial statements and understand what type of restaurant is best suited for the space."

"I usually value the restaurant at 33% of gross sales but may actually end up selling for 30%. SDE multiple is anywhere from 1.87 to as much as 2.5. This is usually affected by # of hours open for business to ease of operation and favorable lease."

"May require reverse gross margin proofing. EBITDA formulas typically larger restaurants."

"Minimum length of lease: 10 years; consistent sales history over three years. Assumes no major renovations required. Pricing for going concern only with market rent."

"Worth 30%–35% of the gross sales. Rent must be below 10% of the gross sales for a restaurant to survive."

"Most sell for about 1.5 times SDE"

"30% of sales for a restaurant"

"75% food sales and 25% beverage sales—40% of sales for a sports bar"

"60% food sales and 40% beverage sales—50% of sales for a bar"

"Since it has become so costly to do a new build-out or startup restaurant, a large percentage of restaurants in our market area (California) are sold as conversions, with the value based on furniture and equipment, infrastructure (tenant improvements), ABC license, and lease rights. Applying the historical rules of thumb based on sales and cash flow is not always indicative of the fair market value."

"Since a buyer will probably introduce their own concept, the most important factors tend to be lease term and rate, equipment and condition, and type of liquor license."

"Full-service restaurants rarely sell above 40% of sales with 30% (or less) being common. Remember the lease must be at market or below. Restaurants with over-market leases rarely sell. Always remember to normalize wages as many operators over or under pay themselves. EBITDA is true EBITDA with management in place, not owner's cash flow. SDE is owner's cash flow. Big problem with overstated value due to misstating earnings. Also, for restaurants that are losing money, conversion method is best. Don't try to 'create' cash flow. Our company has used the conversion method for years and now I am teaching it. Simply, the conversion value of a restaurant is based on the value of the infrastructure and FF&E in place. It is common for a full-service restaurant operator to spend \$100–\$200 per square foot to build out (a leased space) and equip a restaurant. So based on our experience, we estimate the value another operator will recognize for the space. Another operator will utilize the plumbing, electrical, hood, grease trap and some of the FF&E. It is subjective but has been very accurate. We assign a dollar-per-square-foot value to a fully equipped restaurant that has a long-term market (or below) lease. Rarely is this number higher than \$40 per square foot. The conversion method will not work in depressed markets where many empty restaurant properties exist."

"Any liquor/food mix of 30/70 may demand slight premium. Watch for loss leaders that will increase COGS."

"35%–40% of gross sales if in leased space and up to 100% of gross sales if real estate is included. Always check your work to see if there is reasonable owner's salary left after debt service."

## Benchmarks

### Statistics

Number of Enterprises	190,931
Average Wages per Employee	\$13,160
Average Profit Margin	6.0%
Average Revenue of Enterprise	\$921,904

Source: IBISWorld, August 2009

Product/Services	Share
Casual Dining -- Full Service Restaurants	39.4%
Asian Foodstyle Restaurants	19.7%
Traditional American Foodstyle Restaurants	21.1%
Pizza Full Service Restaurants	10.2%
European Foodstyle Restaurants	9.7%
Latin American Foodstyle Restaurants	7.6%
Middle Eastern Foodstyle Restaurants	1.3%

Source: IBISWorld, August 2009

Item	Cost
Purchases	34.0%
Wages	32.9%
Rent	9.2%
Utilities	3.5%
Depreciation	3.2%
Other	11.2%
Profit	6.0%

Source: IBISWorld, August 2009

### Representative Cost of Sales Profile

Sales	
Food	28% to 32%
Liquor	18% to 20%
Beer (Bottle)	24% to 28%
Beer (Draft)	15% to 20%
Wine	23% to 35%
Combined Cost	28% to 32%

Source: Charles Perkins, The Boston Restaurant Group 2009

"Ideally prime costs (cogs & labor) should be 60% of sales. Seldom can a restaurant be profitable if prime costs are over 65% and never over 70%."

"Food cost should be at 33% & liquor at 25%."

"Although 6% occupancy cost is a benchmark, 8% is most common. This should include all net charges."

"Food costs can range from 20% to 40% for most concepts, so it is hard to generalize. The occupancy cost is the most important factor since it may be fixed, although there are opportunities to renegotiate leases at this time. In California it is still difficult to have occupancy cost in line with national averages."

"Some may argue that the most important factor to succeed in the restaurant business is the lease. If you can pay the rent with the gross sales of one strong day, you will definitely make it. Updated numbers for costs in a full-service restaurant: Food: 27% to 35% Liquor: 22% to 28% Beer: 28% to 35% Wine: 30% to 36%. Most restaurants are heavily discounting pricing through daily food and drink specials, coupons and special promotions to keep the sales volume at a higher cost of goods sold"

"Sales \$350 to \$400 per sq. ft. Food cost should be 28% to 35% of sales depending on the concept, except for seafood restaurants."

"Keep food and labor below 60% and occupancy in the 5-6% range."

"Since the square foot rent cost is all over the place it is hard to allocate a \$ amount per sq. ft., rather I apply what the % cost is per sq.ft. The ideal # is 6% however an operation may still be profitable even with a 9 to 10% rent factor."

"Labor 20%–25%, Food cost 28%–32%."

"Look for maximum utilization of space. \$300-400 per square foot for multi meal operations."

"Food costs under 33% are a plus."

"Sales \$350 per sq. ft."

"Rent should not be much more than 10% of monthly gross income."

"Food cost should be between 27% and 35% of sales depending on the concept. Rent all inclusive shall be less than 10%."

"The occupancy cost as a percentage of sales is 10%, since today's higher market rent, 6%, is really low; as long as it's under 10% it's acceptable."

"Food costs should be about 33% and liquor should be at 25%. Otherwise use these figures to determine how much cash is unreported or poorly managed."

"If a restaurant can keep the food costs in the low 30's%, retain staff, the rent below 6%"

"Prime costs (cogs & labor) should be 60% or less."

"Say a company with two units, each doing about \$3 million in volume, wants to add two more stores in the next year and add another \$6 million to the business,' Grace says. Usually overhead, or general and accounting costs, in restaurants should average between 5 percent and 7 percent of sales, he says.

"With a younger company, you have to make that percentage larger, say 10 [percent] to 12 percent,' he says. 'If you are adding \$6 million in volume, that means you can use 10 percent of sales, or \$600,000 for overhead.'"

Source: "Upstart Chains let system growth dictate HQ staff needs," Nation's Restaurant News, September 1, 2008

"In California, it is difficult to achieve gross profit margin greater than 40% for a full-service restaurant, due to high labor costs primarily, and more recently due to the increasing cost of food product. Also, occupancy cost tends to be higher, with 10% or less an acceptable range under the current conditions."

"A good full-service operator should drive 10% to the bottom line if the total occupancy costs are 8% (of sales) or less in major markets. 6% has always been the benchmark but this cannot be achieved in larger markets due to cost of real estate. The theory is simple; controllables (cogs & labor) must be within industry standards. If the occupancy cost is high (as a percentage of sales) the controllables must be lower to achieve the same earnings."

"Rents are approaching the 10% of gross monthly sales mark. Food costs must be kept < 30% and labor at around 25% to be profitable."

"Maintain payroll, cost of sales and occupancy costs under 70%."

"Combined food and labor costs should not exceed 55%–60%."

"Full service—food cost should be in the 30% to 35%. Fast food, sub shops, pizza & the like should be under 30% food cost."

"You've got to find a way to compete with the buying power of the chains and the big stores or you cannot compete on a COGS basis."

"If food costs exceed 30% you are in trouble. If rent is more than 10% it is hard to make a profit."

"Food cost should be about 33% and liquor cost should be about 25%. Often (like the IRS) you can figure out how much cash is missing from the recorded sales. This won't help at the bank but might influence a buyer as to how much sales are not being recorded."

"'No prudent restaurant operator allows his lease to get down to two to four years, because if he has been there a number of years before that and he is doing good business, he will be walking on egg shells,' says Richard Lackey, president of the Lackey Cos. and a founder of the CIRB. 'On the other side of the coin, if the market is declining, but you want to stay in that neighborhood and still upgrade your facility, I think you should approach your landlord like you are in it together. 'We've been in this marriage for 15 or 20 years, and I need a lower rent if I'm going to survive.' If the landlord is smart, he'll work with you."

#### Representative Restaurant Ratios

Owner Salary	\$ 40,000 to \$50,000 depends on location
Cash Flow	10%–15%
Rent —Full-Service Restaurant	5%–7%
Rent— Fast-Food Restaurant	9%–11%
Lease Length	5 + 5 + 5
Rent + Debt Service	Not more than 75% of Cash Flow

Advertising	1%–3%
Maintenance	1%–3%
Utilities	4% –5%
Rent Increases	12%–15% every 5 years
Refurbish	5 years
Renovate	10 years
Chain Requirements	Sewer/Parking/Demographics
Food Cost	Fast Food 25% to 30%, Full Service 28% to 32%
Payroll Costs	Fast Food 25% to 30% , Full Service 28% to 32%
Primary Costs Food & Payroll	60% to 65%

Source: Charles Perkins, Boston Restaurant Group, 2009

#### Expenses as a Percentage of Sales

• Cost of Goods	25% to 35%
• Payroll/Labor Costs	25% to 30%
• Occupancy Costs	6% to 10%
• Profit (pretax)	10% to 15%

#### Industry Trend

"As we turn the corner and see a recovery, the new owners should benefit from lower occupancy costs and a great pool of qualified employees."

"Smaller faster casual, more ethnic"

"More healthful food being served. Many restaurants will include nutritional information if not required to by regulation. I believe value will be the key for the next few years, as people will not spend as freely as they did before the recession."

"Cost of goods are increasing due customer demanding more value. costs continue to increase. Labor continues to be a problem due to local legislation."

"Small will struggle, especially with the evening meal. Gross sales need to be in excess of \$2.0m to make any real money."

"Restaurants will continue to struggle until market rates subside. The recent real estate boom in California has inflated rental market rates to the point where restaurants cannot survive until the rates are adjusted accordingly."

"Profits might go down as people drink less, and non-smoking will be hard on bars."

"The trends are always positive for good operations. Marginal businesses will fail in weak economies."

"The next few years will see many independents failing and major large players slowing expansion and revising demographic minimums for growth,"

"Franchise growth leveling off. Some growth in independents."

"The trend is down; however, restaurants with desirable locations will benefit the most."

"The slowed economy will likely result in a shakeout of weaker restaurants, including some national chain units."

"Some franchises and independents will do better, but over all, it will be a very challenging few years."

### **Who is Doing Well**

Fast Food -- was doing well until the summer. Customers were trading down; however the fast-food core customer—Joe Six Pack—doesn't have as much discretionary income and has cut back.

Fast Casual -- has really taken a hit. Many of them are located in markets where real estate values are off and there is high unemployment - Florida, California. Also many units -- Chili's, Applebees -- are located around shopping centers and customer traffic is way down.

Steakhouses -- have really suffered due to their high guest check average (\$85) and the cut back in business travel.

Celebrity Chefs -- are still holding their own; however same store sales are probably off 10%. The bottom line has held up as they are more creative using cheaper cuts of meat and doing prix fixe to create value.

Irish Pubs and bars are enjoying increases at the expense of the general marketplace. It is all about beer, burgers and big screen TVs. People want value and they want to socialize."

Source: Boston Restaurant Group

### **Advantages**

- "70% profit margins after overhead is covered"
- "Second generation restaurants have a lower entry cost."
- "Easy to find a place to buy."
- "Restaurants are always marketable due to the existing tenant improvements such as hoods, walk-in refrigeration, grease traps, plumbing, etc."
- "It is a lifestyle decision, and those who enjoy the social aspect and creativity of the hospitality industry and are willing to work long hours will find it an interesting, challenging, and profitable business. It is still about the numbers though, with food

and labor costs key, so the owner must possess a varied combination or realize that professionals must be employed to fill in the gaps of knowledge."

- "Everyone needs to eat. If you have affordable rent you can survive; if your investment is low, you will succeed."
- "There are always a base value and buyers for restaurants, whether or not they are successful."
- "Being in business for oneself. Opportunity for earning above-average profits."
- "Still attractive to ethnicities and people that see themselves at front or back of house."
- "The advantage of this business is the fact that eating is a part of life, so a quality establishment should endure difficult times even with declining sales. Consumers may reduce spending on certain luxuries, such as eating out, though they will never eliminate this luxury entirely."
- "People still tend to dine out on a regular basis so the market remains strong even though this year has seen decreases averaging about 20% of revenues. People that thrive in this business over a long period of time enjoy the customer interaction and the creative process in the kitchen."
- "People seem to be eating out more than ever so the business can be profitable if it captures a fair share of the market. Although the hours are long, most owners enjoy the work environment."
- "If you do enough advertising you will succeed. Easy to calculate the value of a business to buy or sell."
- "The advantage of a restaurant operation is that it is always marketable. Unless it is simply located in a bad location, a buyer can change the concept and the seller can recoup substantial value for build-out, equipment, liquor license, etc."
- "Most people are in this business because they love people and love food. It is a lifestyle choice for the independent operator. For single-unit franchises, it can be a good job replacement business, and for multiple-unit franchisees or chain restaurant owners, a good return on investment is possible."
- "Can be a lot of fun to operate if you are into it."
- "Cash business"
- "The restaurant industry tends to attract high-energy, self-disciplined and self-motivated individuals who enjoy working with and motivating others. A restaurant owner/operator needs the same skill sets and leadership capacity as a quarterback on a football team."
- "It will do business both in good times and slow times. People will always eat out. According to the economy and their own pocketbook they will adjust to which restaurants they will go to, expensive or less expensive but they will still go out to eat."
- "Restaurants can make a family realize their American Dream. It also provides an environment that thrives on having family members active in the operations."

### **Disadvantages**

- "High risk, long hours, labor intensive, bar theft"
- "There is a high cost of entry in terms of building-out a restaurant facility. Government regulation including Health Dept and ABC must be considered. Hours are often long and employees may be on the lower end of the experience and pay scale so turnover and training can be a challenge."
- "Too many hours, too much employee turnover and too much competition."

- "Profits and sales are dropping."
- "Competition is the major problem, in addition to higher occupancy cost, labor and food cost."
- "Most restaurants require owner presence to maintain quality and service. This also means that owners may spend up to 60 to 70 hours per week working the business."
- "Labor pool, food & beverage costs, increasing health & code regulations."
- "Most concepts fail and the investors lose large amounts of money. The landlords usually want very high rents for prime locations, and the investment to build out the location can be almost as much as buying the real estate."
- "People, location, economy. Meals, especially an evening meal, becomes an option for patrons. Landlords can kill you with rents that remain fixed when the economy goes south due to things like the cost of auto gas."
- "This is a lifestyle-oriented business that is highly volatile. Poor service, a new chef or a public incident could ruin a business's goodwill overnight."
- "High risk, low earnings, strong competition from national chains."
- "COG's, labor, regulations"
- "It is incredibly frustrating. Good help is almost impossible to find and retain. Restaurants tend to be a 'first' job for young people, so turnover often exceeds 300% per year. The hours are terrible. Plan on working holidays and weekends and having no life outside the restaurant."
- "The disadvantages right now of owning a restaurant are the inherent failure rates of restaurants, coupled with increasing food and delivery costs, and rent expenses nearing or exceeding 20% of gross sales."
- "Competition is the #2 problem. High rents are the biggest. Landlords are taking 15%–20% of gross sales. A business cannot survive paying these high percentages."
- "Long hours, dedication, and the historical high rate of failure."
- "This is one of the most highly competitive industries that exist, with significant copy-cat operators and relatively low barriers to entry."
- "Long hours and managing employees are the typical complaints. Many variables must be in place to become successful, marketing to achieve a profit volume, maintaining quality food and service to retain customers, and controlling the food and labor costs to achieve a profit."
- "Shrinking legal labor pool, pilferage, shrinkage, spoilage, fuel costs, municipal standards, i.e. sprinklers, grease traps, code requirements, etc. One seller (said with a smile) 'It ruined my marriage.'"
- "Depending on the hours of operation, the restaurant business can be hard on the family, as the hours often include evenings and weekends. Finding and retaining reliable employees can be a challenge."
- "Lots of hours and once you are tired of it, it takes a lot to go to work."
- "The profit margins are tight and the concept has to be right on the money. The investment required today is significant, given the cost to build and the need to conform to all the local, state and federal code requirements. Constant oversight of all aspects of the business. Training and employee turnover are constant issues."
- "Finding and keeping good employees, especially during the day, is difficult."
- "Competition abounds, lack of qualified help"
- "Long hours. Owner has to work evenings, weekends and holidays. Having to deal with the fact that some employees will not stay for a long period of time, i.e., wait staff, and in general dealing with the public and handling their needs and complaints."
- "Increasing governmental regulation and unstable commodity prices"

- "Competition, shrinkage, pilferage, spoilage, human resources, code requirements, etc."
- "Employee problems; long hours; growing competition; difficult in finding competent employees"
- "Your work hours may be different from the 9 to 5 office/business environment."
- "Long hours, and employees are always a big problem, especially in the fast food end of things."
- "Growing competition, difficulty in finding a competent work force, employee benefits are too costly, governmental oversight is too costly, can't afford quality help"
- "Continuous supervision is required. Employee turnover and finding employees, especially during the day shifts, continues to be a real problem."
- "The three main reasons for failure are undercapitalization, level of experience, and concept/location. Everything must be right."
- "Risk and employee nonsense"
- "Can be long hours, can be a lot of work. You should have strong operating experience before owning an establishment."
- "Amount of competition, food costs and health issues"
- "Many hours. Sustaining power. Difficulty of under-financing. Employee apathy. Not recognizing the tax consequences."
- "Very competitive. Easy to lose control."