Menu Psychology, Pricing, and Engineering

FBM 3196 / FBM P197
Food and Beverage Management
Objectives

Upon completion of this topic, you will be able to:

• Explain key features involving the psychology of menu items and their prices
• Identify ways of adding value for customers
• Discuss the relationship between menu prices, costs and profit
• Point out and explain control tools used in restaurants
• Explain and apply mechanics of menu pricing, using the methods of mark-up, prime costs and contribution margin
Key Features of Menu Psychology

• Focus is on value ≥ Expectation = Good deal
  – Value focuses on satisfying needs and wants

• Exercise: Metaplanning:
  1. What can be done to increase perceived value?
     – For example: Prima facie vs inclusive prices
  2. What is best way to increase perceived value?
Recommendations/Findings

Menu Psychology

• Customers like to have choices, even with a table d’hote (fixed price menu)
• Provide a range of prices within each menu category
• Customers tend to gravitate towards central prices unless you provide compelling alternatives
• Avoid pricing patterns for organizing your menu (ingredients, preparation methods or flavors are better alternatives)
• Revenue could be enhanced through house-made beverages
• House wine should not exceed the price of the lowest entrée (main dish)
• Highest price – entrée (main dish), try to establish a gap to other categories
• Carryout dishes are often lower priced
• Half-portions are not half priced
• Try to avoid price add-ons or surcharges (if it can be avoided then make it as a “choice” or a “supplement” – see next page)
Omelet Menu with Add-ons

**Fluffy Omelets**

All omelets are served with grilled 8-grain toast.

**Albuquerque**
- Red onions, cilantro, ripe tomatoes, pepper jack cheese and New Mexico green peppers. 9.75

**Western with Cheese**
- Finely diced sugar-cured ham with green & red bell peppers, onions and your Colby or Swiss cheese 9.50

**Greek Isles**
- Crumbled Feta cheese, fresh spinach, ripe tomatoes, grilled onions, oregano & sliced Kalamata olives 9.75

**Cheesy Vegetarian**
- Broccoli, red onions, ripe tomatoes and shiitake mushrooms with your choice of Wisconsin Cheddar or Gouda cheese 9.75

**Stockyard**
- Crumbles of pepper-cured bacon and country sausage with your choice of Swiss, Cheddar or pepper jack cheese 9.25

**Forest Mushroom**
- Sautéed assorted mushrooms and Swiss cheese with bubbling sherry-mushroom sauce on the side 8.95

**Spinach and Cheese**
- Fresh spinach, Brie and fondu tomato sauce 9.25

**Build Your Own Cheese Omelet**
- 3 eggs with your choice of Swiss, Colby, Wisconsin Cheddar, pepper jack, Feta, Brie or Gouda 7.95
- Egg white omelets 1.00 additional
- Homemade Salsa .50 additional
Group Exercise

• Distinguish between guiding customers, manipulating customers, and abusive pricing practices
• Give examples of each
• At what point does profit seeking compromise your clientele’s perceptions of your business?
Control Tools

- Standard recipe
- Standard portion size
- Standard portion cost
- Standard yield
- Standard purchase specification
Basic Structure of Budgets/
Income Statements

Sales (Price x No Sold)
- Variable Costs
= Contribution Margin (Gross Profit)
- Fixed Costs
= Net Income/Loss

Short: Sales – Total Costs = Net Income

Marginal Profit = Profit per food item
Standard Recipes

A Standard Recipe is a formula for producing a food or beverage item (see Exhibit 1, Chapter 7)

It includes: Ingredients, quantity of each ingredient, preparation procedures, standard portion size, equipment needs, garnishes and other information

Advantage: Consistency (the product will always look, cost, and taste the same).
Standard Portion Size

Needs to be part of the standard recipe

Standard Portion Size is important for consistency:

• No guest will receive a stronger or weaker drink

• No guest will receive a bigger or smaller plate (imagine: steak?)
Control Equipment

Use portion control tools such as:

• Weighing equipment
• Measuring equipment
• Ladles and scoops
• Jiggers and shot glasses
• Automated beverages-dispensing equipment
Standard Portion Cost

A standard portion cost is the cost of preparing and serving one portion of food or one drink item according to the standard recipe.

Formula:
Total Recipe Ingredient Cost / No. of Portions of Standard Recipe (do exercise)
Adjusting Standard Recipes

Reasons - Increases or Decreases of:

1. Portion numbers
2. Portion size
3. Combination

Adjustment:
1. Use an adjustment factor (when there is not a significant change in portions)
   (Desired Yield/Original Yield)

Does not work for everything (especially spices and herbs. Side dishes you might not like to reduce or increase!
Standard Purchase Specification

Is a description of quality factors desired for a particular item. (See Exhibit 2 – Chapter 8)

Why?

• Knowledge by all parties (consistency)

• You can easy get a quote from a supplier because the item is specified with the minimum expected quality (creates competition and saves money)
Standard Purchase Specification

Advantages:

• Lower purchasing costs
• Control over food cost
• Consistency
  (Customer retention)
Objective Pricing Methods

1. Mark-Up Method
2. Contribution Margin Method
3. Prime Cost Method
Mark-Up Pricing Method

From the budget you need to figure out the cost of food %.

Next determine the multiplier:

1 / Food Cost %

The food cost of producing one portion will be multiplied by the multiplier to calculate the base selling price.
Mark-Up Pricing Method

Example:

Budget:

Expected Food Sales $300’000
Expected Food Cost $100’000

Food Cost %: 33.3%

Price Multiplier:
\[
1 / 33.33\% = 3.003
\]

Food Cost of Chicken Cordon Bleu $4.--

Price of Chicken Cordon Bleu:
Multiplier (3) \times $4 = Price of Chicken Cordon Bleu $12.--
Contribution Margin Pricing Method

Contribution Margin =

Selling Price - Food Cost

or

Non-Food Costs + Profit

Steps for this method:

1. Find the “average contribution margin per guest”

2. “Average contribution margin per guest” + “standard portion cost”
   = CM base selling price
Contribution Margin Pricing Method

Revenue $130’000

Labor cost: 28%

Overheads: 24%

Net profit requirements: $11’700

Number of expected guests: 3000

Portion food cost “Special of the day”: $10.--

Calculate:  
- The average CM per guest
- Base Selling Price with CM Method of “Special of the day”
Simple Prime Costs Pricing Method

Prime Cost = Largest Costs
(food & beverage cost and labor)

Steps for this method:
1. Determine the required prime cost % from your budget.
2. Find average labor cost per guest (Labor cost/Expected No. of guests)
3. Determine the prime cost per guest (Portion food cost + average labor cost per guest)
4. Equation
   Price = 100%
   Prime Cost = Prime Cost %
Simple Prime Costs Pricing Method

Revenue: $250’000
Labor Cost: $75’000
Food Cost: $65’000
Expected guests: 25’000

Portion Cost “Special of the day”: $6

Calculate: Base selling price with Prime Cost Pricing Method!
Step 1: Labor cost % = 30%
   Food cost % = 26%
   Therefore: PC % = 56%

Step 2: $75’000/25’000 guests = $3

Step 3: $3 (LC per guest) + $6 (Portion cost) = $9

Step 4:
   x = 100%
   $9 = 56%
   x = $16.07
Subjective Pricing Methods

The Reasonable Price Method
Manager decides on a price which he/she thinks is a good value to the guest.

The Highest Price Method
Manager decides on a price which he/she thinks is the most a guest is willing to pay!

The Loss Leader Method
This is a plan to get the customer in your establishment!

The Intuitive Price Method
Manager takes a wild guess!

Many managers use only subjective pricing methods! Problem: Fails to relate the prices to profit requirements!
Elasticity of demand

Elasticity = How demand responds to price changes
Price sensitive = Price elastic (big changes in quantity)
Price insensitive = Price inelastic (small changes in quantity)

Managers need to find out how customers react to price changes of certain menu items in order to maximize the profit.
Elasticity of Demand

- If the price for a pint of beer increases and the demand for it proportionally higher decreases, then beer can be said to have an elastic demand.

- Conversely, some products have a relatively inelastic demand. For example: Coffee served at breakfast can be sold over a wide range of prices with little effect on demand (Family Mart vs. Starbucks).
Elasticity of Demand

• We need to find out what combination of menu price and sales volume will be most desirable to your customers and your business interests

• To start, you need to use the concept of marginal analysis (exercise: which item produces the most profitable price point on the menu?)
Menu Engineering

Objectives:

- Analyze the menu, and apply the right strategies to increase its performance

Kasavana & Smith (1982)
Menu Engineering

Evaluation of each menu item by

- Popularity
- Profitability

Requires to find Cutting Points:
- Popularity Index (Menu Mix Baseline)
- Average Contribution Margin
Menu Engineering

Average Contribution Margin

Av. CM = Gross Profit / Total no. of items sold

Popularity

1. Find expected popularity
   (Total no. of items sold / No. of items on the menu)

2. Multiply expected popularity * 70%

(Menu engineering assumes that an item is popular or efficient if its sales equal 70% or more of expected sales!)
Menu Engineering

• Control your Gross Profit
• Control No. of Sales
• Check your Revenue generated
• Try to increase the average price
• Try to increase the average CM
Success = combine menu psychology, control tools, pricing methods and menu strategies) – be creative and rational!