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OUTLOOK

Some New Thoughts on Labor Costs

by **Dennis Monroe**

I've been reading everything I can to come to my own conclusions about proper approaches regarding impending increased labor costs for the restaurant industry. I also talk daily with multi-unit operators to get their take.

The threats for increased labor costs are from multiple sources, including minimum wage at the local, state and federal level; disparities in minimums between states; the movement to a livable wage; the Affordable Care Act and confusing wage and hour laws.

Given all of the above pressures, what are the fallacies regarding increased labor costs?

1. The current environment is bad. The fallacy is the increase in wages will have a dramatic effect on the restaurant industry. Restaurants already pay far above the minimum wage, so an increase usually does not have a significant adverse effect. It may help the servers, but there is a continuing movement in the country to implement tip credits or a two-tiered minimum-wage system. The recent Congressional Budget Office said an increase in the current federal minimum wage from $7.25 to $10 could result in 500,000 job losses, but would mean 16.5 million workers with more buying power.

2. The restaurant industry will not be able to raise prices. The restaurant sector has hurt itself as it relates to pricing because of couponing and dollar menu wars. Hopefully, with an increase in wages we'll see a decrease in couponing, prompting diners to seek quality rather than bargains.

3. Restaurants will go from profitability to losses. It's always been the case if your sales volume is close to break even, anything that causes the break even to go up may result in a loss. Many restaurants are profitable, and their profitability flow through is in the 40%-to-50% range. If restaurants are unable to raise prices, the effect on operating profits will be incremental, which most operators can deal with.

4. Little can be done if labor costs go up. This is totally false. It is about time the restaurant industry gets a handle on efficient labor vs. straight labor costs. There are a number of techniques that have been used which we will discuss below.

5. Obamacare is going to destroy the restaurant industry. The cost of Obamacare has turned out to be much ado about nothing. I have seen restaurants planning to go healthcare-lite and using more part-time workers in order to manage healthcare costs. But having healthcare may create a higher level of employee retention, which would then cut the overall labor costs and compensate for the extra healthcare costs.

Now let's look at some solutions:

1. Flexible Labor. Chain restaurants are developing market labor forces rather than an individual restaurant workforce. Employees can work in more than one restaurant, allowing for flexibility, and limiting labor costs and last-minute scheduling. This flexible labor force will reduce no-shows and overall labor costs, and it will keep employees happier because they will work more hours.

2. Natural increases in prices. There always has been a natural increase in prices, and it will continue. If there is any increase in labor costs, restaurants will need to find effective ways to raise prices. Some creative ways include increasing the price on key products, particularly signature products; cutting back on frequent dining cards and, as I said before, limiting couponing and Groupon.

3. Offering Better Service. With higher wages, employers should expect better performance from employees. This higher expectation starts with the front of the house and goes to the back. Operators must let their servers know how important they are and how successful they can be. Increasing their wages is a good start.

4. Cost Containment—Negotiating Leases. If labor costs go up, then one possible source of cost containment may be leases. Most restaurant leases have periodic increases in rents over the life of the lease. Limiting these increases may be a way to compensate for higher labor costs.

5. Use Less Labor. iPads and electronic ordering seem to be the way of the future. The unknown factor is: Will electronic ordering cut overall labor costs? It probably won't affect the back-of-the-house labor outlay. I do think technology will be a savior of labor costs across segments.

6. Effective Up-Selling. It's crucial every employee try to up-sell customers. It should be effective up-selling, however, not just up-selling to irritate the customer. This skill can be taught. For example, take an order for dessert from the start, or package menu items as combos and pairings.

7. Watching Tables. All employees should do consumer research by watching tables, noticing customer reactions and responding. Focus on customers. If that is maintained, the restaurant will have better-trained employees.

8. The Future. The restaurant industry is innovative. Thanks to the evolution of fast casual, the trend already is away from high labor costs and tips. Consumers are willing to pay more for food than they are sometimes for service, and that can be a guide to lower labor costs.

9. What Would the Answer Man Say? These questions would be better answered by the Answer Man, but he refused to return my call. So this liberal lawyer had to think outside the box. The restaurant industry thinks creatively. We challenged QSR, fast casual and casual dining to come up with innovative ideas. Those who break out like McDonald's in the 1950s or Chipotle in the 1990s will be the winners. There are huge opportunities to make money in the industry. Do not let labor concerns hold you back. The weakness has never been labor cost; the weakness has always been weak performance, bad products and lack of a compelling offer.

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