# *This is Not the Restaurant Business I Grew up in*

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Like many other American teenagers, my first paycheck job was at a hamburger stand. That was just two years after Ray Kroc had purchased the development rights from Mac & Dick McDonald. Burgers were 15 cents, a shake 20 cents and just 12 cents for great fries. All in all, a great lunch for 47 cents. All transactions were cash. I used to get tips when I worked at the window.

I cut my teeth working for Carroll's Hamburgers. It was a 1,168 SF building with a basement. That's where I had to go to get the 50 pound bags of potatoes. I carried them upstairs, peeled them, cut out the eyes, sliced them into a sink filled with water. Then I got up to my elbows stirring them up to rinse off excess starch. Cooking them was a two-step process. First, they were par cooked for about three minutes. Those par cooked potatoes needed about another two minutes to finish them off to a golden brown. Our competition wasn't McDonalds since there weren't any in New York. Instead, it was Wetsons, Burger Chef and the newly opened All American Burger.

I went to college and majored in Civil Engineering. I got to work on everything from solidifying the soils under Subways in Brooklyn, up to working on building the first nuclear power plant in the Carolinas. But I wasn't having fun!

An opportunity opened up. I visited a recruiter. He asked, "What do you think about real estate?"

"I know they're not making any more of it." And off I was in Commercial Real Estate.

About 3 years later, a requirement came in for Restaurant Real Estate. And I was off to the races. I read that Marriott purchased Big Boy. I loved their strawberry pies. I wrote to Marriott to suggest I could find sites on Long Island for Big Boys. A Tennessee gentleman, Bill Killpatrick, from Marriott, wrote back to me.

"We're not interested in bringing Big Boys to Long Island. But we just bought a chain, Roy Rogers. We would be interested in growing that chain." It was my start in restaurant site selection.

After spending two years finding locations for Roy Rogers, and even having dinner with Roy Rogers himself, Bill Kilpatrick threw me a curve. The mayor of Alexandria, VA had called Bill Marriott. They had built a new City Hall. He wanted Marriott to build a restaurant in the old city hall. I was invited to the opening of their first dinner house restaurant. The Joshua Tree. I loved it. I told Mr. Marriott that the concept would work very well in Long Island.

"If you can find a good location, we will definitely consider that."

And so began my time in dinner house real estate site selection. Doing deals for a 7-10,000 SF restaurant paid four times better than finding a location for a 2,200 SF Roy Rogers.

Dinner houses were FUN! And the comp meals were a lot better than just a Roy Rogers Roast beef sandwich … even with fries.

So, from the Marriott Dinner houses, I went on to Rustler Steakhouses, Moonraker, Plankhouse, Coco's, Steak & Ale, Chi Chi's, and then came Rusty Scupper. I learned from their real estate departments. They then asked me to find location in other markets: Connecticut, New Jersey, Massachusetts, Pennsylvania and down to Washington DC.

In the 1970's dinner houses were king. Footprints typically were 10,000 – 14,000 SF. Other than Marriott operations, they served Lunch and Dinner seven days. A visit to one of them was … an experience. You might be in a Victorian townhouse, a Mexican Hacienda or a beautifully skylit Oak environment with porpoises jumping over each other in a surfboard inspired bar top.

The 1980's brought us ferns. "Fern Bars" ranged from TGI Fridays and Houlihan's to their copies, Ruby Tuesdays and Applebee's. They broke down the mode of having one room for the bar and another room for dining. As women emerged in the workplace, they now could meet a friend for drinks, be seated at a table, and not be hassled. At the same time, a businessperson on the road could sit at the bar and order from the full menu.

The footprints shrank. Instead of 10-14,000 SF, their footprints decreased to 8,300 down to 5,500 SF. Clearly there was less distinction between Dining and Drinking areas. Socially, this was the place to meet and greet.

The 1980's became the decade of chain emergence. California Pizza Kitchen, Boston Chicken later to morph to Boston Market, and Cheesecake Factory were three of the early leaders. Who remembers Il Giornale? It was owned by Howard Schultz who then purchased a coffee bean merchant in Pike's Place Market and Starbucks was launched selling hot beverages.

The 1990's saw a number of shifts. The first McDonalds opened in Moscow, and the last Horn & Hardart closed in New York City. Steve Ells, a Culinary Institute of America graduate, and a former line cook at Stars in San Francisco concluded that Americans wanted better food fast. His response was to open Chipotle. Others followed and Fast casual was born.

Meanwhile, Pepsico's restaurant brands, Kentucky Fried Chicken, Pizza Hut and Taco Bell all grew faster than ever, domestically and internationally. The restaurant industry found there were more stomachs outside the United States than there in the US. International growth started to exceed domestic growth. Our brands were exported.

Restaurant sales continued to absorb more and more of the food dollar. Total restaurant industry sales rose to $295,000,000 from a mere $42,000,000 in 1970, a sevenfold increase.

At the turn of the century, a new word came into vogue: "VALUE". It preceded the word "menu". Burger King had 11 items on its $1 value menu. McDonalds and others followed.

Darden Restaurants initiated Seasons 52. That followed the trend of having fresher menu items in the hopes of better nutrition. The consumer clearly was embracing the concept of more sophisticated dining and better fare. Seasons 52 had a decent wine list; a first for a chain restaurant.

Ruth's Chris emerged from the deep south and led the growth of high end dining as a chain. In Providence, RI, Ned Grace answered with Capital Grill.

Nutrition became the buzz word. President George Bush called for Nutrition Labeling. Three out of four consumers said they were trying to eat more healthfully in restaurants. Restaurant sales continued to grow and increased to $500,000,000.

New York City passed legislation that any restaurant with 12 or more units had to display calorie counts on their menu. To avoid compliance, Houston's Restaurant changed the name of their Manhattan Restaurants to Hillstone.

The top three soft drink companies agreed to stop selling sweetened sodas to schools. Mayor Michael Bloomberg started his attack on sweetened sodas. At the same time, more and more restaurants started buying local produce. "Farm to Table" became prominent in that never ending search for a healthy image.

Meanwhile, restaurants began to shrink. Not in numbers, not in sales, but in footprint. TGI Fridays shrank their footprint from 8,300 SF to 6,700 SF. At a construction cost of $350/ SF, the reduced footprint could be built for a savings of $500,000 per unit at a cost of only losing 15 seats. However, the loss of seats wasn't a problem. Due to shifts in consumer habits, lunch time wasn't just 12:00 – 2:00. More people were having lunch later in the day. Later evening dining was a result of people working later.

At the same time, white tablecloth restaurant saw shrinking customer counts during the week. We saw a distinction between "Eating" and "Formal Dining". A full service dining experience would take an hour and a half to two hours typically. With more women in the workforce not cooking home meals, and folks working later and, on their computers, available time for dining shrank. The demand now was for Casual Dining. Consumers wanted to be in and out under an hour. Chili's, Cheddars Scratch Kitchen, Red Robin, California Pizza Kitchen and he like, were just what the doctor ordered.

Restaurant developer, Norm Brinker took up the fight against mandatory insurance. He found that only 26% of his employees were the primary wage earner in their families. All the others were covered by the insurance of the primary earner in their household.

He also fought against minimum wage increases. Half of his employees earned far more in tips than they did in wages. So in the full service restaurant industry, things were just fine as they were.

Conversely, if a politician or a legislator raises minimum wage, they fully expect to get the full backing – and vote – of all those who would benefit.

Seattle led the charge by imposing a $15 minimum wage. Like flipping a switch, the substantially higher minimum wage was implemented. As quickly as they could, employers substituted technology for staff.

If you walked into a McDonalds, rather than finding a counter backed by smiling faces, you were confronted with self-service touchscreen terminals; not by staff giddy about their higher compensation.

Effectively, the increased minimum wage served to eliminate jobs. Back in 2014, a front of the house employee in New York received a minimum of $5 an hour as payroll. In the decade since we're looking at an almost tripling of wages to the front of the house. Funny thing. I haven't seen anyone working three times as hard or performing their duties three times as fast.

While the front of the house wages rose, the back of the house demanded more as well. The $10/hour line cook who used to work 60 hours a week, now was raised to $15, but became unaffordable at the $22.50 overtime rate.

Along came Covid. It was both a catalyst and an accelerator. Patrons wanted to eat outdoors. That is, those who were willing to venture out at all. Rather, third party delivery services thrived. I'm trying to figure out how an industry with a 10% bottom line can afford to pay 30% to a third party to deliver their goods. Some New York City operators formed ghost kitchens that existed only online. Their prices were suspiciously 20% - 30% higher than their normal menu pricing to absorb the fees from third parties.

More people than ever are working remotely. If someone is working from home Mondays and Fridays, the downtown restaurateur has lost 40% of their market. Unfortunately, they are still required to pay 100% of their rent.

The viable numbers in the restaurant industry have changed drastically. Diners used to be open 24 hours a day. Operators couldn't afford these elevated rates. They have significantly cut back their 168 hour work weeks, and 50% of diners are closing altogether.

Let's review some of the basic restaurant metrics. Are you buying whole chickens and butchering them? That saves food cost but raises labor cost. I don't care what is your food cost. I don't care what is your labor cost. But I care very much what is your food plus labor cost your Prime Cost. Ideally, that was about 30% food and 30% labor for a prime cost of 60%.

Anyone who has been to a supermarket has seen significant increases in the cost of commodities. The sale prices are higher than the pre-covid prices on just about everything. The price of eggs doubled. Rack of lamb used to sell for $8.99 per pound. Currently $16.99. Before Covid, you could buy a steak for substantially less than today.

There is a limit on just how much of the costs can be passed through to the consumer. There is a strong pushback as fast food meal prices approached the promotional prices being offered by casual dining.

The Cost of Living increase from 2010 – 2020 was a mere 1.6% per year compounded. However, restaurant pricing has increased by over 60% in the past decade. Starbucks prices (on selling hot water) have increased by 39%; Taco Bell by 81%; Pizza Hut by 86% and McDonald's prices have doubled.

A decade ago, you had to pay a server \$5/hour. Today it's \$15/hour minimum.

I used to say to restaurateurs "I don't care what your food cost is. I don't care what your labor cost is. But I care very much what is your food plus labor costs."

With food costs and labor costs increased as they have, today it is extremely difficult to hit a prime cost (food + labor) under 65%. And half of operations are closer to 70%. So where do these additional percentage points come from?

Profits! For example, diners that used to enjoy about 12% profits, are struggling to make half of that as pre-tax profit.

So how can an operator deal with these tectonic shifts? One way is to close for lunch Monday – Friday. Among other benefits, that will limit overtime labor costs. Diners that used to be open 24 hours, now close by 9 or 10 PM.

One of our clients ran a 60 seat cantina. With staffing challenges during Covid, they did away with the floor staff. Now you have to come to the take-out counter to pick up your food. Tips decreased therefore lowering the cost to the consumer. Tables turns increased and net profits increased.

However, new operations are tending to be moving towards much smaller footprints. Today, most requests for new restaurant are in the 2,000 SF range. Historically, I have leased dozens of restaurants in the 10,000 SF range. Therefore, I have to do five deals in order to earn the same commissions I got from a single deal.

Did I mention credit cards? Think about this. Today the typical full service restaurant with liquor has their credit card charges being greater than their sales.

Another sad note. In the New York Metro area, sales tax plus real estate taxes exceed profits. So why should someone invest hundreds of thousands or millions of dollars to build a restaurant, just so they can give most of it to the government.

Norman Brinker who was founder of Steak & Ale, Bennigans and developer of Chili's and Maggianos and other brands, said it best.

**"Your competition isn't the guy down the block. It's the Government. They can put you out of business faster than anything else."**

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