Variance Analysis – How to Utilize it for your Restaurant Business

Do you find your restaurant's operating results unsatisfactory? Do the profits turn out to be diminished compared to what you had anticipated? It's time you took a closer look at the operations scenario and figure out what's making those numbers shrink. Variance analysis is one of the most powerful and practical tools at your disposal to investigate the deviations between the budgeted and actual results.

It goes without saying that restaurant owners prepare budgets from time to time for both the fixed costs and variable costs. The budgeted cost is then topped with a percentage markup to arrive at the selling price of the items on the menu. It is when the actual costs deviate from the budgeted that there is a variation between the budgeted and the actual profits. The variation could be either positive or negative. Let's take a look at the following example.

Let us consider that your restaurant had expected to serve 1400 meals this week with an average bill of £30. That makes your budgeted sales £42,000. However, you ended up serving 1450 meals with an average bill of £32. Hence, you made an actual sale of £46,400. The difference between the actual sales and budgeted sales is called the variance. In this case, there is a positive revenue variance of £4,400 because the actual sales exceed the budgeted, which is a good sign.

The sales variance of £4,400 can be split into two parts; £1500 and £2,900 based on the idea of volume variance and price variance. The positive sales variance of £1500 is the result of the rise in volume by 50 meals at the rate of £30. On the other hand, the £2 increment in the anticipated average bill of £30 for all the 1450 meals resulted in the positive sales variance of £2900.

Similarly, if the actual sales fall short, there would be a negative sales variance, which could be a cause for concern if there is a major and consistent decline or stagnancy over a longer period. This is when you would need to analyze the variance. By that we mean, finding out what went wrong and why?

There could be several reasons the actual outcomes diverge from the anticipated ones. Particularly in the restaurant industry, one or more of the following factors are commonly responsible for the sales variance.

- Unforeseen fluctuations in the occupancy rate
- Varying bill sizes
- Deviation in the actual cost of labour from the budgeted affects both the cost variance and profit variance.
- Deviation in the actual procurement cost of ingredients from that budgeted affects both the cost variance and profit variance etc.

Whenever there is a negative sales variance, any increased costs can take up a major proportion of the sales revenue, thereby eating into the profits.

When do you analyze the variances?

The one very intriguing characteristic of variances is that not all of them are subject to examination. It depends on how significant or abnormal a variance is. For example, you accounted for cost of a specific quantity of the ingredients for the week to be £12,000. However, there was a rise in the prices of certain ingredients and you had to pay £13,000. The additions £1,000 spent on ingredients might not be as significant and hence, you might give it a pass.

However, if you continue to pay increased prices over the long run, you might need to analyze the variance in the cost of procurement. Renegotiating the prices of the commodities in question with your supplier would be the most sensible thing to do. If that doesn’t work out well, you could try looking for another supplier. However, make sure you do not compromise the quality of the ingredients. Some restaurateurs would also consider raising the prices of the specific items on the menu using the dearer ingredients.

Let’s not ignore the fact that the variance in the occupancy rate and cost of labour can occur alongside. The percentage aggregate variance could have a major impact on the profits. Therefore, it could be detrimental to your business to disregard a variance for analysis if you think its percentage is negligible.

So let's face it, guesswork is risky. Conducting variance analysis on a regular basis is the practical and feasible method to prevent yourself from losing track of all the costs and deviations. We hope this write up helped you understand how vital the tool of variance analysis is when you want to establish the cause of discrepancies and implement corrective measures.

Previously we had shared an insightful write-up about efficient inventory management practices. In the upcoming article, we would discuss the winning strategies for pricing the items on your restaurant's menu. Stay tuned!

Best,

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