Surviving the 2012 Drought's Food Cost Impact

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The old saying "when it rains, it pours" apparently has nothing to do with water falling from the sky. Perhaps a more accurate metaphor might be "when it doesn't rain, food profits go down the drain". The massive drought this year covers approximately 60% of the continental U.S., the largest area since the dustbowl droughts of the 1930's. According to USDA economist Richard Volpe, "In 2013 as a result of this drought we are looking at above-normal food price inflation. Consumers can expect to pay 3 percent to 4 percent more for groceries next year."

Of course, this is an election year, so we can expect the government to estimate on the optimistic side. As a reality check, the markets seem to be saying otherwise. Karsten Berlage, managing director and head of weather solutions at Allianz Risk Transfer in New York, noted that corn prices had already gone up nearly 50 percent since the beginning of April. And the price of wheat and soybeans has also seen significant price increases. "Clearly, a lack of supply by a lot of farmers giving up on their crop could impact the prices [even more] dramatically," he said. "It's a disaster," said Rick Tolman, CEO of the National Corn Growers Association, who noted the drought is expected to cut production 20% or more – roughly 3 billion bushels less than normal.

Survival Options

Assuming we see price increases to food service operators of between 3 and 5% for most purchased items, with the potential to be much higher than that, the options would be to raise menu prices to compensate, reduce portion sizes, reduce overuse or find lower pricing for purchased goods. Perhaps the answer is to do all of these things to some extent. Regardless of the approach, maintaining the status quo is not an option. Action must be taken now, since prices are already rising.

Of all the options, the one with the least impact on the guest is getting suppliers to reduce their prices – or in this case – to keep them from rising. The best way to accomplish this is through an aggressive bidding process. Bidding all food items purchased to all qualified vendors has been shown to consistently result in prices 3-5% lower than pre-bid pricing. This process alone could offset the majority of the coming price increases, but requires constant data collection and comparison of thousands of items from dozens of vendors.

The next best option is to reduce overuse. Theft, waste, spoilage and over-portioning are the key components of this loss, and can easily add up to another 3-5% of food costs. This type of control requires tight security, vigilance in the kitchen and constant comparison of actual usage to ideal usage on an ingredient level.

Coming in third, but only because it affects the guests, is portion size reduction. Small reductions in portion sizes can have huge impacts on profits, and may not even be noticed by the guests. If we need to save 3-4% to offset price increases, we could simply reduce portions 3-4%. Who would notice the difference in reductions that small?

Of course, this represents across the board reductions, which are generally not advised. But selecting key, high value or high sales menu components and making unnoticeable cuts in the right places, the results can be even more dramatic. Reducing portions correctly requires a strong knowledge of plate costs, margins and product sales. Menu engineering approaches work well in this regard because they identify products that would benefit most from this approach.

Any or all of these options can help reverse the effects of the coming price increases, but they come at a cost. The labor required to collect and compare bids, track item usage and perform menu engineering is significant and may outweigh the benefits. On the other hand, this is exactly what F&B management systems are built to do, along with much more. And with cloud-based solutions, the up-front costs can be minimized and implementation can be rapid.

So the question we should all be asking is how will we prepare for and survive the coming onslaught of price increases. If we can find a way to do it without adversely affecting our guests, we may find a pot of gold at the end of the rainbow – assuming it ever rains again!

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