LOOK BEFORE YOU LEAP

By Jay Goldstein

An old adage in this business is that every restaurant owner with one unit wants a second, and every owner with two operations wants a third, and so on and so on. Particularly if you are in your third or fourth year of operation as a startup owner, and think that you have a good handle on your present enterprise, you may be considering launching another. You're not unique in this desire.

The good news is that you've survived a crucial phase in the startup process and that your successful track record can open financing opportunities not available when you were starting out. Institutional investors will take you more seriously. Friends, family members, and business associates will want to jump on your bandwagon. Additionally, you have developed systems and procedures that can be carried over to another restaurant and you may have developed competent trusted management staff to assist you with the process.

The not-so-good news is that the restaurant business can become geometrically more complex with each unit you add, particularly if you decide to operate multiple concepts with different menus. Running both a fine dining steakhouse and a family pizzeria could require the agility of a juggler.

But even if the thought of a new challenge gets your adrenaline pumping and — torpedoes be damned — you decide that you want to expand to a new location, just respect that you are now playing a new game. You will want to know the do's and don'ts of the game, as well as proven strategies for success, and how to win before you even start to play. You will need additional information and knowledge to avoid any serious missteps so that you succeed and excel.

The ranges of decisions you will face and the complexity of starting a new unit could fill a book. Here, we examine the kinds of questions you will want to consider before adding properties.

Throughout my career I have been involved with growth scenarios, including company store growth and franchised growth, and both domestic and international growth covering 57 countries. In the

Illustration by Keith Ibsen

mid-'90s, I led the operations department of a small but growing concept that was positioning itself for an initial public offering (IPO) and we were able to realize that goal within less than two years. Although each of these situations was quite different, I learned that there are several key principles required for successful growth. This article will explore the core issues and what you need to know to grow, how you gain that knowledge, and who can help.

What is the best location? The best place to start here is with the concept definition. This definition tells what you are, what you provide, your value proposition, and identifies your target customers. It should describe what the customers see and experience when they walk in the door, and what they say about the experience as they leave the building.

Explore All Avenues of Growth

I have found that growth in your business can occur in several ways, without taking out a second lease or breaking ground across town. Before any operator or owner embarks on the path to open additional restaurants they should examine their current business to uncover opportunities that already exist. Consider Edd Hendee and his restaurant, "The Taste of Texas." Hendee had multiple chances to expand to other locations and each time he discovered he could do more business by looking aggressively at his existing operations. Over time he has added banquet sales, wine tasting parties, catering, new menu items, and improved training for his staff. Without fail, Hendee has increased sales with every initiative. On the other hand, there is "Becks Prime" concept, which has experienced steady growth over the past two decades by staying true to its concept, keeping the menu fresh and alive, and by constantly building the brand in the Houston area. It has sites in the most dynamic suburbs, the downtown tunnel system, at the city-owned golf course in Memorial Park, and an established catering business. In both cases, the owners of these concepts developed the systems and procedures to support their growth, and guaranteed quality experiences for both their staff and their customers. Developing your growth strategy will be an important step, and it will provide a filter through which decisions will be made. This is the step in the process when you frame your plan of attack.

It Always Starts With a Business Plan

To begin this process you need to think "first things first." At the top of your list is writing, rewriting, or updating your business plan. (For more information, see "Mapping Your New Restaurant's Journey," *RS&G*, May 2005.)

The process of writing your plan is as much an exercise in soul-searching as it is an effort to create a business blueprint. The process will cause you to honestly assess your assets, resources, operations, and position in the marketplace. It deals with people, management systems and practices, investment and financials, cash flow, information technology, marketing/branding, the marketplace and competition, and the business model.

Beginning with the end in mind will give you a picture of where it is that you want to go as a company or concept. You will want to answer questions like:

What will growth accomplish? Is your answer to increase sales or profit margins (good reasons) or to satisfy your ego (not-so-good reason)? What will growth get you that you really want or value? Don't lose sight of the things in life that really matter, such as more time with your family.

What are all the pros and cons to growth? Here is where talking to other restaurateurs can help you. Find out the benefits and pitfalls they encountered in the process. What happens if you don't grow? Will you be able to meet your financial goals? Will you get bored with your present operation? Will you not be sufficiently diversified geographically or market-wise to weather an eventual leveling off or downturn in your sales as your existing concept(s) mature? Sometimes expansion is necessary just to maintain your present position.

As you answer these questions you will gain a better understanding of why you are doing this and what it will mean to you. This is a step that several owners have skipped and then wondered what the heck they had done.

A Natural Progression

Understand that the best reasons to grow one's business occur naturally. If you feel in your gut that you are forcing the issue, it may be a sign that you or your business is not ready to expand. Natural reasons for growth include:

Readiness to make more money and create additional financial security. This sounds like a "no-brainer" at first blush. If you can replicate the profit potential of a single unit two or more times, you can multiply your wealth. This is simple math, if the other numbers, including your time, add up. No matter how much capital you raise, you only get 24 hours in a day, and you only have so much time to personally devote to each unit. It is easier to correct problems and address opportunities in a single business, when that is your sole focus. For more than one unit, you need to develop operational and financial systems and procedures, and have trusted managers in place to carry them out. With one restaurant you can improve your business by

STAND COUNTER-TOP WALL-MOUNT

Cascades' ServRite™ dispenser – Three-fold savings!

Cascades' new ServRite™ one-at-a-time napkin dispenser serves up savings in a big way. Its convenient concept lets you save three ways: cut costs, reduce waste and save time. This low-cost unit dishes out napkins one at a time, thereby reducing needlessly dispensed napkins by up to 50%. Not only does this dispenser reduce waste, but it also contributes to environmental preservation by using Cascades' recycled napkins available in white, Moka™ or custom printed. Moreover, its 600 napkin capacity means less frequent refills… because every second counts in the foodservice industry.

ServRite™ – Serving up savings every day

Servrite™ Cascades

Cascades Tissue Group
TOLL-FREE NUMBERS:
(US) 1-800-246-0711 • (CAN) 1-800-361-4070
www.cascades.com

Cascades

working on, not in your business. (See "How to Turn a Good Restaurant Into a Great Business," *RS&G*, June 2005.) With more than one restaurant, this strategy might be a matter of survival.

Build the brand and dominate the market. If you can leverage the visibility of each unit to build business for the other units, you have bolstered your marketing program without spending an extra dime on advertising and public relations. Consider ways to cross-promote each unit in your business plan. If you have a hot name in the restaurant market, consider that intellectual property, which as one attorney said, "is the gold standard in this economy." For example, a successful franchise is based on the value of the name and reputation of the concept. Its most valuable asset is intangible: its trademark.

Build a larger business to create opportunities for family members or others. Always consider how to leverage your resources. If you have eager and smart family members and business associates chomping at the bit to help you be more successful, growing the business can leverage this talent. If you have a young family who has an interest in the restaurant business, growing your enterprise can create "intergenerational" equity (value passed to the next generation). Some of the most successful businesses in the United States have remained in single families for years.

Beat the competition to the punch. If a great new location is becoming available in your community, you might want to exploit it before your competitor does. You might be better off competing against yourself than another restaurant.

Create other business opportunities. Consider the steakhouse that had a brisk banquet business, but lacked the capacity (available days and seating) to tap the full potential of the market. It opened another full-service restaurant, and used its existing location as a dedicated banquet facility.

Increase purchasing economies. Particularly, if you are expanding your concept into a chain or franchise, you will be able to purchase inventory in greater quantities and drive down food and other costs.

A pregnancy can be natural, whether planned or unplanned. Likewise, you can't control every aspect of the future in your business life. Natural growth can be rigorously planned or "accidental." Planned growth is knowing where you are going and why, how and when you are doing it, how much it will cost and what you will gain. Accidental growth is somewhat opportunistic. It occurs when someone offers you a unique site that targets your customer profile, or a venue such as an airport or university business opportunity. You may be pressed for an immediate answer or the opportunity will be lost. In either case you will still want to go through the same basic steps to ensure a greater chance of success.

Site Selection

What is the best location? The best place to start here is with the concept definition. This definition tells what you are, what you provide, your value proposition, and identifies your target customers. It should describe what the customers see and experience when they walk in the door, and what they say about the experience as they leave the building. This captures what you are as a concept. Knowing your target customer will allow you to find out where they work, live and play. As you decide where to locate the new restaurant you will look for a target-rich environment, thereby enhancing your chances for success. The right location for your restaurant will be a mix of being in the right market with the right site dynamics to attract your target customer. (For more information, see "On the Money — How to Find the Right Location for Your Next Restaurant," *RS&G*, October 2005.)

Another decision you will need to make is whether you will grow locally, regionally, nationally or internationally. This should be determined by assessing your current business and its capabilities. The international market for U.S. franchises, particularly in countries with emerging middle class populations (e.g., Mexico and China) is booming. In most cases it is wise to stay local until you have established your brand, and then to begin regional growth to reinforce the brand. Moving to national growth requires an entirely different organization with more sophisticated skills. In this case you will deal with markets in which you have very little knowledge or expertise. A great deal of

Structuring Growth

There are several ways to finance and structure growth. Here are the most common arrangements in the restaurant industry.

Company-owned. You or your company owns the business. In this scenario, you operate all the new units, typically under an umbrella organization that provides centralized administrative and management support. Managing shareholders and partners remain the same, although you might offer silent investment opportunity for passive shareholders/partners. This scenario works best when there is no need for business oversight talent, the restaurant can afford to employ whatever talent it needs (e.g., general managers) and the concept is neither interested in nor conducive to franchising.

Partnerships. You take on managing shareholder partners with money, or experience, or business expertise. There are ways to structure these deals so that you retain control of operations and are the day-to-day decision-maker for the organization. It is advantageous to partner with people who bring things to the table that you don't have. There is very little reason to bring on partners with the same skills, abilities, and resources you already possess. This is an opportunity to balance your "team" and have the sum greater than the total parts.

Franchising. You grow your concept through a franchising system. This is a tremendously complex strategy, and there are many responsibilities and legal requirements with which you will have to deal. You will also need to support the franchisees in operations, marketing, research and development, and purchasing to help ensure their success and the integrity of the brand. It is also necessary for you to "police" the system to ensure that the value of the brand is upheld and that the customers know what to expect. The concept has to be right for franchising and operating systems need to be thorough and replicable. In other words, it must be a highly distinctive concept that can be readily branded in the marketplace, have a somewhat predictable return on investment, and be replicable in a number of markets through systems, procedures and training.

Acquisitions. This is one of the most common ways for restaurant businesses to expand. You, your company, or new partners/shareholders find an existing eatery for sale and you purchase the entity or the assets. (For more information, see "Know the Score When Buying an Existing Restaurant," *RS&G*, June 2005.) The ideal "target" businesses include successful enterprises that are on the market because the owners want to cash-out or retire or a restaurant that has the location or market to be successful but is faltering due to poor management. In the latter case, this can be an excellent deal if the owners want to get out from under debt. There are reputable restaurant brokers who can help you find businesses for sale.

Conversions. As markets change some restaurants move or go out of business. This presents opportunities for operators to move into buildings that require very little infrastructure investment as most of the mechanical, electrical, and plumbing have been done. The site is already zoned and approved for a commercial restaurant and it will be easier to get permits. There is usually equipment left behind that can be purchased for pennies on the dollar. A great example of a concept that took advantage of conversions is Darden Restaurants' Smokey Bones Barbeque & Grill. Its initial growth was through acquisitions with lower investment levels and high returns.

due diligence is required before taking the concept across the nation. The landscape is littered with extremely successful regional concepts that expanded nationally and failed. International growth is absolutely the most complicated and you must work with people who have a positive track record of successes in the international arena. If you are considering franchising, you need to work with an experienced franchise consultant. The operational and legal issues are mind-numbing. While franchising is a hot growth strategy in this economy, it can be disastrous to attempt it without expert guidance. (We will address this aspect of growth in future issues.)

Staffing

In building the organization to support your growth you have some decisions to make. You will first determine the needs of the organization with the addition of a new restaurant and then you will assess what you already have and what it is that you will need. This process is called a "gap analysis." It will be necessary to write job descriptions for the new positions so that you know what you are looking for in candidates, and so that anyone filling the positions will know what is expected and how they will be measured. You will find that you have some definite areas of strength and some areas of weakness. Your purpose is to eliminate those weaknesses.

You might need to bring on additional marketing or accounting talent. Depending on the results of the gap analysis, your financial resources and your preferences, you can fill the gaps in three basic ways. The first is to create new in-house positions, hiring existing staff members in your company who have the ability to fill the roles or hiring additional full-time employees. Either way, this can be an expensive strategy for a small company since it creates long-term commitments to financing these positions. You will want to be sure that this is a position that you feel is absolutely necessary to have as an in-house function.

As a second strategy, you might consider consultants and contractors. There are hospitality industry-specific consultants that specialize in disciplines of the business, and to whom you can outsource functions until you develop in-house talent.

The third approach, of course, is a hybrid strategy. Many operators in growth mode mix their professional staff with hires and contractors. You may feel comfortable about making a commitment to hire a marketing person, but you want to outsource parts of operations and accounting. In any case you will be able to find competent, industry-specific consultants to support your organization if that is the path you choose.

The results of your gap analysis will tell you the strengths and weaknesses of your people. You will need to hire consultants and staff for a number of positions, but you will need to count on tried-and-true teammates to some degree; after all, they are the ones that helped you get to a place where you can expand.

As long as this analysis was done honestly and objectively it will give you the information you need to help you determine your ability to grow. If you have determined that your people are well-qualified and able to competently complete key job duties and responsibilities with minimal supervision, you are well on your way. It is also important for them to be experienced and know what to do and when to do it. Ensuring that they have received thorough training will not only lay the foundation for their success, it will also help you retain them. Turnover is one of the greatest enemies of positive growth. You need to project for turnover and then include that rate in your manpower planning. You know how difficult it is to operate a successful Friday night shift when you are a dishwasher and a server short. Imagine how much trouble it will be if you are short-staffed in two or more restaurants.

As you bring on new hires for the anticipated growth it is imperative that you allow for a full training period and some experience in operations. One final important point to consider is the preservation of the "culture" you have spent so much time building and maintaining. You will look for people who are a strong "cultural fit" for your organization, and who will feel comfortable with your methods of operating. You want people on your team who become a part of your system rather than change the system to suit them. To do the best job at screening applicants you will need to have the key features of your culture documented so that you can easily explain what is important to you. You will develop a list of questions that will be asked of each candidate during the interviewing process. This will help you understand whether they are a fit.

Financing

With the lessons learned from the opening of your first operation, you are well-prepared to anticipate what you can expect for the next one. The preparation of your capital budget is a critical step in the budgeting process. This is money that once spent can never be altered. You are saddled with the expenses for the life of the restaurant, and there is absolutely no good reason to spend more than you need to get the restaurant opened. It is wise to include all associated expenses in this capital budget so that there are no surprises as you go along. Some of the things that may typically be forgotten include some permits, professional fees for consultants, attorneys, accountants and others, preopening training expenses for management, and the contin-

The financial projections should include three scenarios: a conservative, a moderate and an optimistic case. The conservative case will serve as your worst case, the moderate case will be your best estimate of what will really happen, and the optimistic case is the best case and will show what can happen if all things in the marketplace work to your favor.

gency working capital. Once the budget has been set it is important to guard against "change orders," as these will creep up on you and drive the cost of the project outside the parameters of your financial models. As the cost of your initial investment increases so does the sales required to meet your break-even and return projections.

It is easy to get caught up in the excitement of your new restaurant and to expect nothing but outstanding results. This is the time for a serious "gut check" so that you don't make the mistake of counting on the best-case scenario. A number of operators will plan for the highest sales estimates, lowest investment costs, and the lowest operating costs. This spells potential disaster, as these results rarely occur. The financial projections should include three scenarios: a conservative, a moderate and an optimistic case. The conservative case will serve as your worst case, the moderate case will be your best estimate of what will really happen, and the optimistic case is the best case and will show what can happen if all things in the marketplace work to your favor.

With careful planning you can ensure that you spend the appropriate amount of money and get the most out of each dollar you spend. Also, you will not necessarily retain every dollar you save in this process, as you will invest some of it back into areas for improvement in your operations.

One of the biggest reasons for failed restaurants is that they are underfunded. With well-done budgeting and planning you will know how much money is required to finance the opening of the restaurant and to continue operations the first six months. It would be foolish to attempt to take on the new restaurant without the proper level of funding. It puts enormous pressure on the restaurant to perform, leaves no room for error, and creates tension and friction with vendors, landlords, and others who will not be paid on time. It may even cause you to strip funds from your current operations to fund the new project, putting those same kinds of pressures on existing operations. There is no reason to ruin your existing business for the sake of growth. Don't strangle the first unit to shore up the second. This is a losing proposition. Consider the following financial issues carefully as you size up your opportunities for expansion:

Cash flow. You will need to know how much money you have and at what time you will have it. This allows you to plan for the ongoing operations of the business. By having a cash flow analysis done you can plan the use of funds at the right times to conduct business and build the business. Insufficient cash flow kills more enterprises than anything else. You need to have sufficient reserves to carry you through the first couple of years until you master your business cycle.

Financing base. Know the source of your funds. A number of operators have gone well down the path to opening only to find out that the funding they were counting on dried up. Before embarking on the new project, have the funding not only lined up, but also in hand and available. As noted, one of the upsides of starting a new operation is realizing that you have access to financing that you didn't have when you started out in the business. Just don't count on a penny until the check is written. This is especially true when looking to family and friends for money. Folks' enthusiasm can wane when it comes time to open the checkbook.

Affordability of your ideal location. Your first site was an obvious success or you would not be looking to grow. Occasionally the first site is a one-of-a-kind and may not be repeatable. Again, be sure that you are realistic in your financial projections for any sites you consider. Since you opened your first restaurant, real estate likely has become more expensive and the market significantly more crowded. As you evaluate the marketplace for new sites there are a few things to keep in mind. First, there are A, B and C sites in the market. Focus your search on B+ and above. Although these sites will be a bit more expensive upfront, the returns should be better as a result of higher sales. Next, look into the future and know how many units the market will hold for you. With this knowledge you can do a market plan that maximizes your potential market penetration. It is also important for you not to pick a site that is between two potential sites, because you will miss the opportunity to build two units by locating there.

Sufficient resources to go head to head with new competition. By understanding the competitive set in your new location you can better define your points of difference and reinforce those points. It will also help you with pricing your food and beverage so that you are not too cheap or too expensive for the market. It may also tell you where you have to boost advertising and promotion efforts. One last point is that you will need to be aware of what they are doing for marketing and promotions, as you build your marketing strategy for the location.

Finally, Don't Be Afraid to Ask for Help

No restaurateur is an island. Where can you turn to find help? Do you have a trusted restaurant consultant to call when you are in a jam? Is there another restaurateur in town who can serve as a mentor as you ply unchartered waters in your business? This is more critical than most people think. When business problems erupt, you can feel very alone in this world. A trusted adviser who understands the business can help you develop focus and gain an objective perspective. If nothing else, get on the RestaurantOwner.com online forum and post a few questions. You'll be delighted how many operators will provide candid and insightful comments.

If you are relatively new to the business, you might be pleasantly surprised that the restaurant industry has no shortage of folks who want to help others, even potential competitors. The information you need is pretty much there for the asking. As you talk with these people, be sure to find out the following:

- ✓ What worked and what didn't?
- ✓ Did things go according to plan?
- ✓ What resources did you find that you needed that you had not planned for? How did you react to recover?
- ✓ What would you do differently next time?
- ✓ What would you change?
- ✓ If you had it to do all over again would you do it, and why or why not?

Also learn from the mistakes of others who have expanded, failed and then expanded again. This is a more common scenario than you might think. Some of the best operators in your town have learned from the school of hard knocks, which in this business is the best education you can find. Find out why they failed, and the lessons learned along the way. This is probably one of the greatest resources available to you. **RS&G**