Inventory Control Basics

A Systematic Guide for Controlling Inventory In Your Restaurant

Inventory management is as critical for restaurants as any business in terms of cost control. Unlike common retailers and manufacturers, however, your challenges include daily turnover of supplies and materials that are highly perishable.

By Joe Erickson

If you were just a common retailer, inventory control would be a relatively simple matter. Retailers purchase clothing, jewelry, hardware and other do-dads at wholesale prices, mark them up and sell them for a profit.

For these businesses, monitoring inventory is a matter of recording when the product is received and when it is subsequently sold, something any POS (point-of-sale) or accounting system can manage. If the store purchases 10 baseball caps and three are sold, then the system should show that seven remain in inventory. The seven caps might never sell at their original markup, but they will not "go bad" and can probably be liquidated at cost at some point.

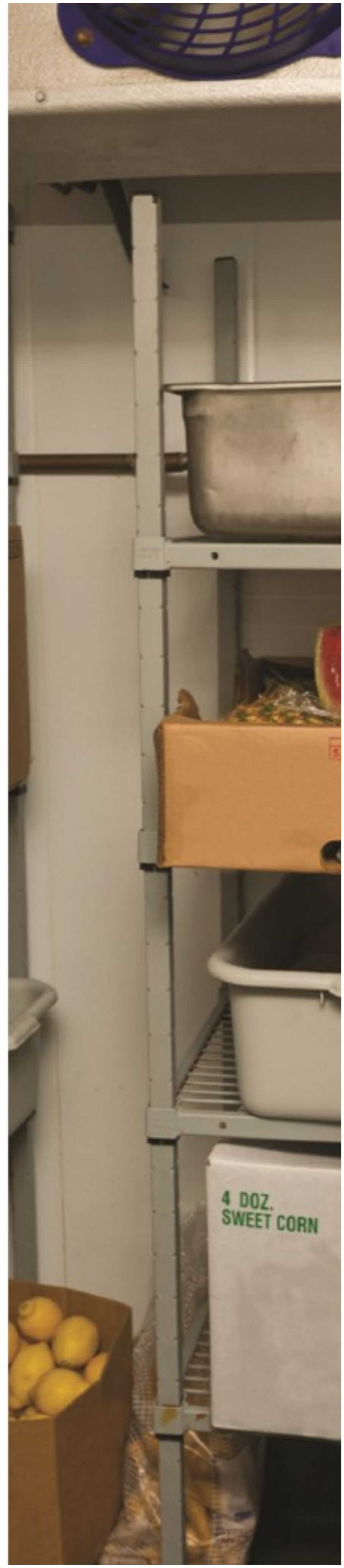
One of the reasons the restaurant business is difficult is due to its approach to inventory control. Restaurants are both retailers and manufacturers, yet many of the principles for controlling inventory in retailing and manufacturing simply don't apply to restaurants.

Sure, restaurants often buy and sell products, such as bottled drinks or chewing gum, in the manner of the common retailer; however, the bulk of what they sell most often requires "value-added processing" of ingredients to produce a menu item. And this is manufacturing by definition; however, manufacturers track both use of raw materials and their inventory of finished products, which may be stockpiled. Unlike most manufacturers, however, restaurants manufacture and sell items at the same time; they do not have the luxury of stockpiling their menu items for obvious reasons. It becomes inedible and cannot be sold at any price.

Besides the fact that most of a restaurant's raw materials are highly perishable, restaurant raw materials often require trimming and preparation before it can be used in a recipe. The "yields" — the amount available for use in a menu item — vary based on quality of product, freshness and the skill level of workers doing the preparation. The process is further complicated by the creation of "daily specials" for which exact recipes may not be recorded, making inventory control of the ingredients even more difficult.

You are not a common retailer. As a restaurateur, you are a different kind of independent businessperson. In your world you face unique challenges, and one of your weekly battles is keeping track of inventory. Losing this battle can be the difference between business survival and defeat.

In this article, I summarize the systems and procedures you will want to adopt and master to gain increasing control over your inventory. With this in mind, I categorize these inventory control measures into "basic," "advanced" and "expert."



Basic Inventory Control Measures

As you start your journey, you must consider your tools and your attitude. If either is suboptimal, it will hinder your progress.

Inventory control features in standard accounting software are fine for common retailers, but they simply will not work in restaurants. This has not been lost on software developers, and operators looking for an inventory control application need simply to search for "restaurant inventory control software" on the Web, where they will find scores of companies promoting inventory software for restaurants.

And while restaurant-specific software, if used properly, can certainly help in controlling inventory, other options are available that can be just as effective. In fact, the vast majority of restaurant operators use alternative systems for controlling inventory, depending upon their unique objectives. The decision each operator must make is to weigh the effort expended vs. the benefit received when it comes to adopting inventory control measures.

Using restaurant-specific inventory software requires an operator to train and allocate personnel to keep it up to date. For some operators, they simply can't afford to dedicate the manpower needed. The cost of tracking items sometimes is more than the cost savings gained.

Before deciding on which inventory systems you should use, it's important to first understand the purpose and objectives of inventory control. Here are some of the most important reasons for tracking inventory:

- Maintaining proper stock levels.
- Upholding quality and freshness.
- Vendor price comparison.
- Accurate cost-of-sales calculation.
- Spotting theft.
- Maintaining up-to-date menu cost.

You must be patient. Putting in place any inventory control system is a progressive endeavor. You cannot be proficient in this area overnight, so relax and begin at the beginning.

The basic inventory control stage is the most important level, as it marks the beginning of the journey to proficiency and the place from which you can gauge your progress. If you are serious about getting a handle on food and beverage costs, you must first gain control over your inventory. You do not need to add staff to use these systems; however, you will need to train your managers and key people to use them properly. To get started, here is a list of systems and procedures you need to adopt immediately.

Use a running inventory order guide. An order guide is a set of forms that contains a listing of all the products a restaurant uses. It is usually divided into separate sections, such as meat, produce, cleaning supplies and paper. The order guide is used as a tool for counting and tracking all the products that your restaurant uses and must reorder. When using an order guide, all products are counted at least once a week, and some, such as produce or seafood, may be counted as many as five to six times if you receive fresh product daily. The unique layout of the guide allows you to keep running inventory counts on all your products, thus simplifying inventory counts without too much additional effort.

Additional Resources From RestaurantOwner.com

How to Avoid Running Out of Product With an Effective Order Guide
www.restaurantowner.com/members/650.cfm.

Take monthly inventory counts. Most restaurants are either on a monthly accounting cycle or a cycle of 13 four-week periods. Regardless of which you use, it is virtually impossible to gain control over your inventory unless you take periodic physical counts after the close of business on the last day of the period, and then calculate its value based on current pricing.

For restaurants, inventory value is based on the last price you paid. The sample inventory form below provides a means for maintaining the most current price for each inventory item. The count column is used to record the number of units on hand at the end of the accounting period. The number counted is then multiplied by the price to get the total value recorded in the extension column. The totals for each inventory item within a category are then summarized to get the inventory value for the category.

Your restaurant name here
ENDING FOOD INVENTORY
For the Period Ending 12/29/2012
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ITEM DESCRIPTIONS	ORDER UNIT		ORDER TO INV	INVENTORY UNIT		COUNT	EXTENSION	TOTALS
	UNIT	PRICE		UNIT	PRICE			
MEAT								
Bacon slices	lb	$ 2.29	1.0	lb	$ 2.29	5.0	$ 11.45	
Ribeye steaks - 8 oz	lb	$ 7.77	2.0	ea	$ 3.89	15.0	$ 58.28	
Pork chops - 6 oz	lb	$ 1.79	2.7	ea	$ 0.67	20.0	$ 13.43	
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Inventories should be categorized as follows:

- Food groups.
- Food.
- Soft beverage.
- Beverage groups.
- Liquor.
- Draft beer.
- Bottled or canned beer.
- Wine.

For more detailed cost control, food can be further categorized by breaking into smaller categories; i.e., bakery, dairy, grocery, meat, poultry, produce and seafood.

Calculate monthly cost of sales. The only method for computing accurate cost of sales is to take physical inventories and then calculate the value of inventory on hand. Many operators erroneously believe that what they spend on food and beverage purchases is their cost of sales. While this may be true in the long run, for period analysis it is inaccurate. The correct formula for calculating cost of sales for each category is this:

Beginning Inventory + Purchases - Ending Inventory = Cost of Sales

Calculate inventory turnover. Maintaining tight control on inventory levels ensures that your cash is in the bank and not on the shelf in the form of excess inventory or, even worse, susceptible to spoilage and waste. To calculate monthly inventory turnover, you divide the cost of sales for the month by the average value of inventory on hand. For instance, if you use $10,000 per month in food product, and the average value of food inventory on hand is $2,500, then you are turning over your food inventory four times per month (10,000 ÷ 2,500 = 4). Optimum inventory turnover for most restaurants is:

- Food: four to six times per month (five to seven days of product on hand).
- Liquor: about once per month (varies among concept/sales mix).
- Bottle beer: two to three times per month.
- Draft beer: one to two times per month (varies with number on tap/concept).
- Wine: about once per month (varies with size of wine list/sales mix).

Advanced Inventory Control Measures

Now that you've successfully put in place monthly inventory control methods, you are ready to begin taking on weekly and daily controls. You have the basic skills to be successful, so go forward with confidence.

Calculate weekly cost of sales. Operators who take inventories and calculate their cost of sales every week are far more profitable than those who don't, putting anywhere from 2 percent to 10 percent more profit to the bottom line. The reasons are twofold:

1. Calculating the cost of sales weekly, operators can quickly identify problems, giving them the opportunity to react immediately rather than wait an entire month — and lose even more profit.

2. Maintaining tight control on inventory levels ensures that your cash is in the bank and not on the shelf in the form of excess inventory or, even worse, susceptible to spoilage and waste.

Many operators complain they just don't have enough time to take weekly inventories. Let's say you have a restaurant that generates $1 million in sales. And let's say, by taking weekly inventories, you are able to increase annual profits $20,000 to $50,000.

Daily key item inventory tracking. This is one of the most effective cost-saving measures any restaurant can carry out. The objective of this practice is to identify 10-15 high-cost, high-use items that you use every day, then to track the purchases and sales of that item daily.

For example, if your restaurant has several items that use 8-ounce chicken breasts, the manager begins the day by counting the number of breasts on hand and records it to the key item tracking sheet. She then enters the number of breasts received from the vendor that day. The number sold for the day is taken from the item sales mix report (includes all items that have an 8-ounce breast). Finally, she counts the number of breasts left at the end of the day. Ideally, the actual use should match the calculated usage.

The running inventory order guide mentioned earlier is an excellent tool for tracking your key inventory items. It also serves as an inventory count form for your weekly inventories. This system is the most effective in combating theft because it allows you to reconcile actual counts against calculated.

Expert Inventory Control Measures

By adopting the inventory systems described in the basic and advanced levels, you should immediately begin to see bottom line improvement. Once you are comfortable you have mastered these, you can now weigh the effort expended vs. the benefit received when adopting more stringent inventory control measures listed here.

Calculate the ideal food cost. Ideal food cost (also called "theoretical cost") is the cost expected for a given sales mix over a period of time, assuming proper portioning and normal waste and yields. It is impossible to know the ideal food cost unless you first know the portion cost for each ingredient of every menu item. Even then, as the cost for ingredients change, so will ideal cost.

Sales mix (the number of each menu item sold for a specified period) affects the ideal cost too. If one period you sell a greater percentage of high-cost menu items and the next period you sell more low-cost items, then the ideal cost for each period will differ; for that reason, ideal cost is an ever-changing target.

Your cash register or POS (point-of-sale) system should be programmed to track individual sales for each of your menu items. The sales (product) mix report is a basic feature found in most cash registers; if your register doesn't have this capability then you need to seriously consider upgrading. This report should tell you the quantity sold and total sales for each menu item for a given period. Most all registers will give you this report for daily sales. Some can be programmed to maintain cumulative totals for the week or month.

One of the most effective measures for controlling food cost is to periodically compare your actual food cost with the ideal cost. Ideal vs. actual comparisons can be made for overall food cost, departmental food cost (e.g., meat, seafood, produce) or by individual ingredients. Keep in mind: Comparing ideal vs. actual cost is equally important for liquor, beer, wine and paper cost.

Put in place inventory control software. Used properly, restaurant-specific inventory control software can eliminate the need for the multiple spreadsheets and systems. Earlier I stated that the vast majority of restaurants use alternative inventory control measures. This assessment is based on the fact that most inventory control software requires an "all-in" approach to be effective.

For instance, in the inventory systems listed earlier, cost of sales is calculated by tracking the total usage of each cost category. Purchases are recorded at the category level rather than the item level. Yet for most inventory control programs, the operator is required to record each item received, a task that takes much longer than cost category tracking. Some operators simply cannot justify allocating the man-hours needed to maintain the system on a daily basis.

Furthermore, many do not have staff proficient enough to use it. That being said, there are many restaurants that use these systems with great success. Some multiunit operators have dedicated staff for this specific purpose. The setup for these systems can sometimes be a time-consuming and complex endeavor. Though maybe not true for all systems, here is an overview of what it takes to get the system properly configured.

Inventory master. The inventory master is a list of all the ingredients you purchase. You will need to input information on each one that includes the description, pack and size of item, the purchase unit and price, the count unit and number per purchase unit and the build-to par level for the amount of inventory to be kept on hand. When purchases are recorded, the quantity on hand for each inventory item is updated.

Batch recipes. Batch recipes will need to be created for all prepared items. Each batch recipe will use a specific quantity of raw ingredients from the inventory master, or portions of other batch recipes. This particular phase of setup can become laborious, as you must also calculate yields for ingredients used as well as the batch yield itself.

Menu item recipes. Menu items, like batch recipes, are also composed of a combination of raw ingredients and batch recipes. Menu items should match the menu items programmed on your POS system so that when an item is sold the correct quantity of inventory ingredients is reduced from inventory.

Inventory locations. Most systems allow you to set up inventory locations to accommodate physical counts. Physical counts worksheets (or in some cases hand-held devices) list the products stored in that location and are then printed or displayed for recording counts.

Vendors. You will need to enter all vendors from which you purchase inventory. The system should allow for a separate vendor ID for each product purchased. Many systems can interface with vendor systems to get this information.

POS setup. Every menu item you sell needs to be entered into the POS system in a manner that accurately tracks the usage of the ingredients within a menu item. This includes any modifiers that change how a menu item is to be prepared, such as adding cheese or substituting a baked potato for fries. Programming the POS to accommodate ingredient tracking can present a problem for programmers.

The added programming might end up forcing the server to make a lot of extra keystrokes or touches just to ring an order. Any changes to the menu will need to be programmed into the POS. This includes daily specials. If you run specials often, or have a fresh feature of the day, the POS program will need to be reprogrammed to accommodate it. Every time you add a new menu item to the POS you'll need to add a recipe as well.

Lead the Way

Whether you are a beginner or an expert, each inventory control system you put in place will help to create a culture of cost awareness in your restaurants. Not only do you want to develop an aggressive mindset in tracking inventory, but you want this attitude to become a part of the culture of your business. The more emphasis you and your management team put on controlling costs, the more likely your staff will react in kind. RS&G