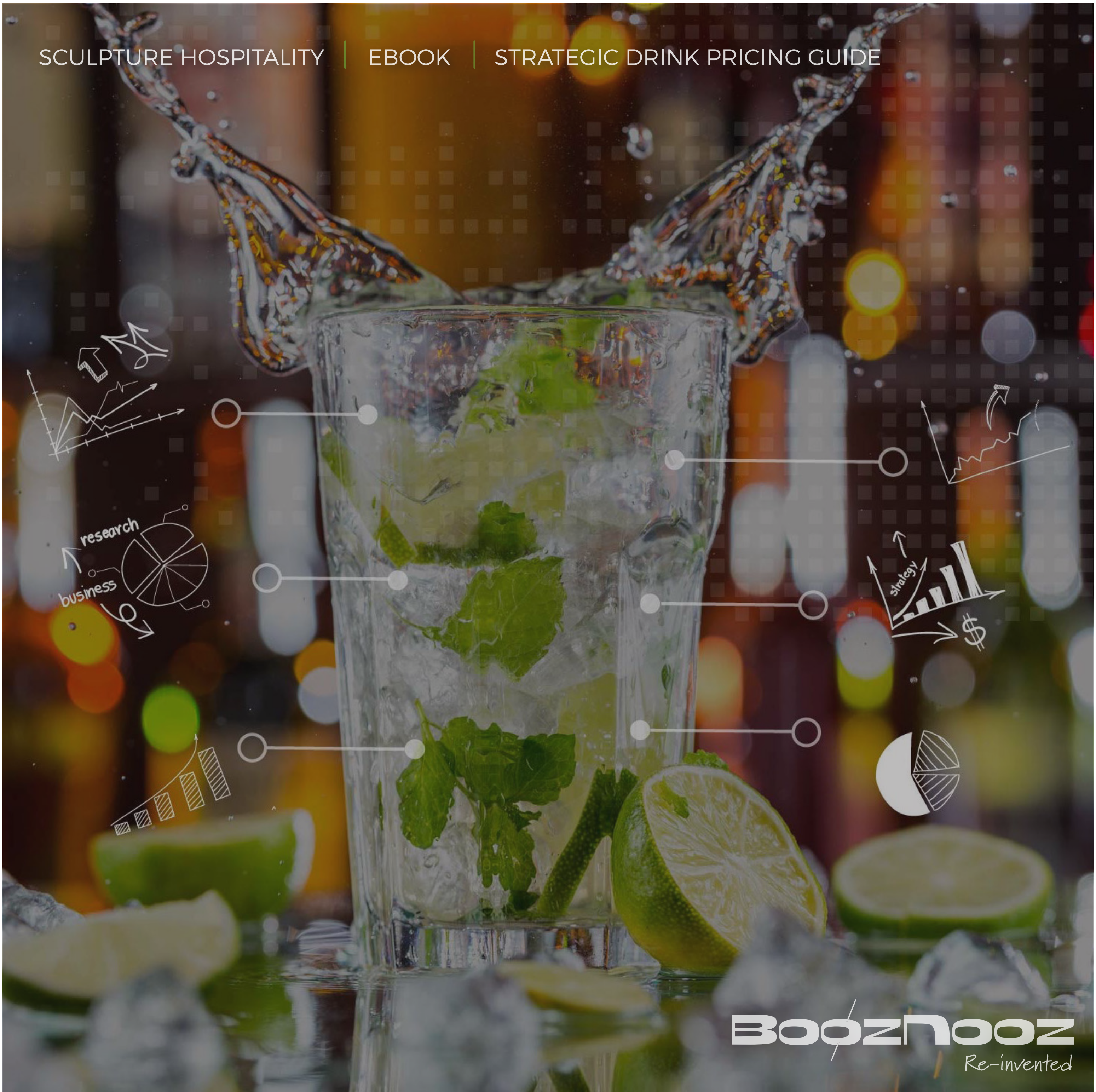


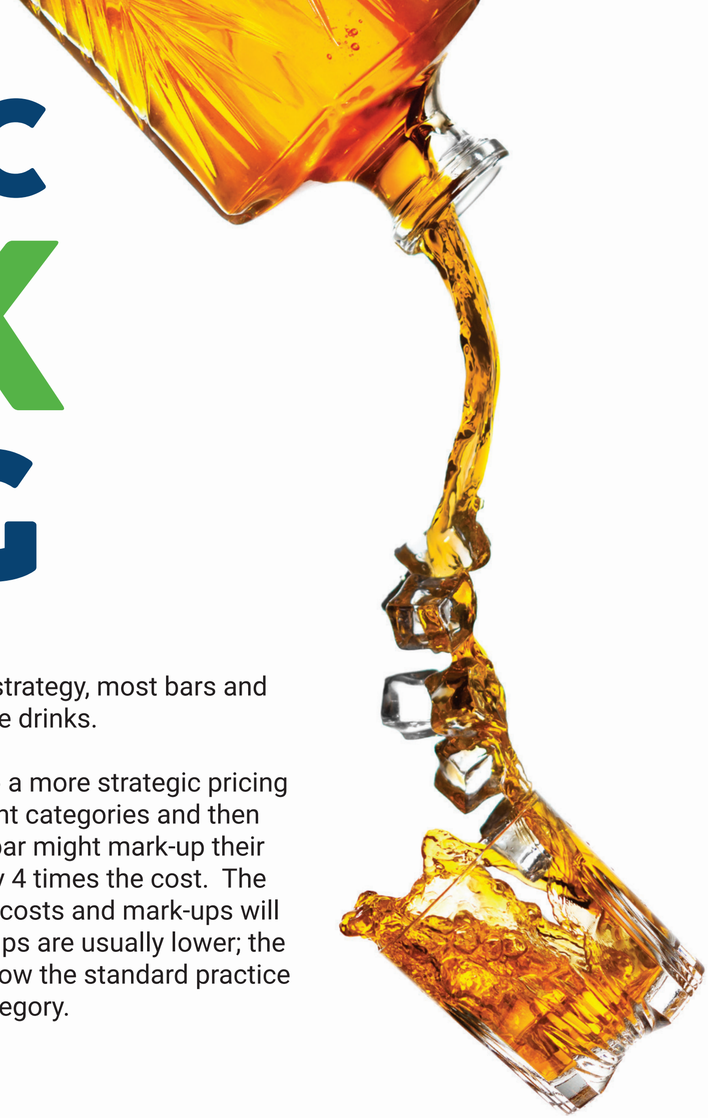
STRATEGIC DRINK PRICING GUIDE

(learn how much you should really be charging)

Written by: Ian Foster, Sculpture Hospitality – Regional Director West Coast

sculpture hospitality

STRATEGIC DRINK PRICING



With a few pricing adjustments, and a slight shift in pricing strategy, most bars and restaurants could add significant profits without selling more drinks.

The key is moving from an overly simplistic pricing model to a more strategic pricing model. The industry standard is to group brands into different categories and then apply a standard mark-up in each category. For example, a bar might mark-up their well liquor brands by 9 times the cost and their premiums by 4 times the cost. The table below is a common matrix in Southern California. The costs and mark-ups will vary from place-to-place; in Canada, for example, the mark-ups are usually lower; the same is true in a rural market. But operators everywhere follow the standard practice of setting drink prices based on a rigid mark-up for each category.

CATEGORY	BOTTLE COST	DRINK COST	MARK-UP	DRINK PRICE	POUR COST
Well Liquor	$10	$0.45	9x	$4.00	11%
Call Liquor	$19	$0.84	6.5x	$5.50	16%
Premium Liquor	$35	$1.55	5x	$7.75	20%
Wine - Glass	$11	$2.75	3x	$8.00	33%
Wine - Reserve Btl	$30	$30.00	2.5x	$75.00	40%
Draft	$150	$1.13	4x	$4.50	25%

Overly simplified mathematical approach:
Cost x Category Markup= Price

This approach was necessary years ago when most bars used a simple cash register with keys limited to "well", "call", "premium", "domestic beer", etc. But with today's Point-of-Sales (POS) technology, you can, and should, set the optimal price for each and every drink to maximize profits.

sculpture hospitality

888.238.4626 | info@sculpturehospitality.com | sculpturehospitality.com

HOW MUCH ARE YOU CHARGING FOR TITO'S VODKA?

Before we get into an analytical look at the important variables to consider, let's start by asking a simple question: how much are you charging for Tito's Vodka?

In Southern California, Tito's costs $21.50, roughly the same cost as Absolut vodka. So most of our clients apply the same mark-up and charge the same price as Absolut – let's say $6.25.

Sounds reasonable but that thinking is too simplistic: the fact is that most of your guests regard Tito's as a premium brand. They regard Tito's as a "better" brand than Absolut but perhaps not quite as "premium" as Grey Goose – more or less at the same level as Ciroc vodka which is priced at $7.25 at many establishments. Because your guest believes Tito's is as good as Ciroc, you should charge $7 or $7.25 for Tito's.

One of my clients sells 150 Tito's every week. If they adjusted their pricing to that of Ciroc, they would make an extra $7,800 in pure profit per year.

That's just one example of how a strategic pricing approach can be more profitable.

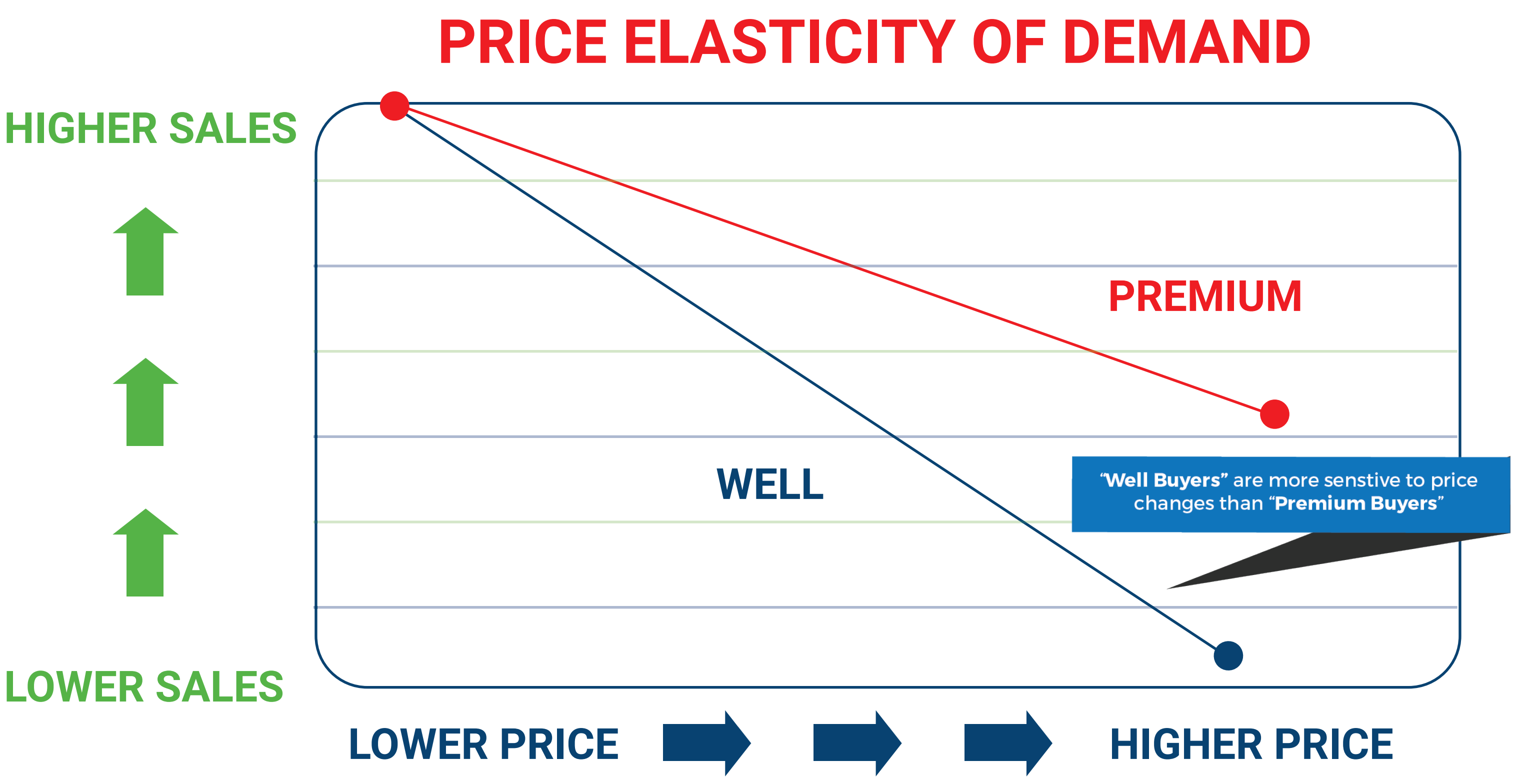
YOU SHOULD BE CHARGING MORE FOR PREMIUM BRANDS

Economists talk about a concept called the “price elasticity of demand” which translated into English means “how sensitive are your customers to price changes?” When you think about someone who might buy an $80 Wagu steak, for example, you can imagine that sales wouldn’t drop much if the price was increased to $95, nor would sales increase all that much if they lowered the price to $65. That reflects low price elasticity: the customer ordering a Wagu steak just isn’t that worried about the price.

Many premium alcohol brands are also like this. A Grey Goose drinker, or the single-malt scotch drinker, is not going to worry too much about whether the drink costs $8.50 or $9 or $10.

On the other hand, our guests who drink well vodka, or Budweiser, or other inexpensive brands do care about the price. If we raise the price from, say, $3.50 to $5.00, that guest will likely find another bar to patronize. These guests have high price elasticity: they pay attention to pricing and will buy less if the price increases.

We can see that reflected in the chart below. The blue line shows that sales on wells drop dramatically as the price rises. The red line shows that sales on premium products don’t drop as much when the price rises.



What can we learn from this? First, that it is critical that pricing on well liquor and domestic (non-craft) beer is about the same as your competitors. Guests ordering those products often decide which bar to patronize based on pricing.

You need to match your relevant competitors when pricing wells, house wines, Budweiser, Coors, Miller, and other mainline beers.

It's important that you identify relevant competitors when pricing your wells. If you run an upscale restaurant, your relevant competitor is not the dive bar around the corner because your guests are unlikely to leave you to drink at a bar that is so radically different. Your relevant competitor is other upscale restaurants within a reasonable driving distance. If you run a dive bar, your relevant competitor is likely to be other dive bars, sports bars, and taverns within a few blocks.

With that said, there is no reason to discount your premium brands. When customers call for premium brands they are stating their preference for quality (or, more often, status) over price – in other words, they are not particularly sensitive to the price. Cutting your premium brand pricing is unnecessary: nobody is going to switch to well if Grey Goose is an extra dollar or two. Similarly, the guest who orders Pliny the Elder is not going to switch to a cheaper IPA for a couple of bucks.

It is usually a good idea to be at the higher end of your competitors pricing range for premium brands.

Grey Goose is actually a perfect example. By definition, vodka is an odorless, colorless, neutral flavored spirit (Bureau of Alcohol, Tobacco, Firearms, and Explosives (ATF) definition). Obviously, that isn't quite true when you are drinking vodka straight up. But most guests are consuming vodka in a mixed drink. And it is impossible to tell the difference between Grey Goose and Absolut in a Screwdriver or mixed with Red Bull. And yet a Grey Goose drinker will still specify Goose in those mixed drinks. They just like ordering Grey Goose; price is not particularly relevant.

BAR OWNERS SHOULD LOVE "VEBLEN GOODS"

There is actually a subset of goods that have negative price elasticity. In other words, the more you charge for them, the more you sell. That sounds crazy but it's pretty easy to think of real-life examples of so-called "Veblen Goods": many consumers will insist on buying an expensive Chanel handbag even if they cannot tell the difference between the Chanel and a well-made, but way cheaper, knockoff copy.

Most bars have several Veblen brands. Guests who buy Cristal champagne, for example, are choosing Cristal because it is expensive, not in spite of the price. They buy Cristal to make a statement: that they are rich; or they want to impress their companions; or that they're a hip-hop star.

Remy Martin's Louis XIII cognac is another great example. We usually display it on the very top shelf, or in a special glass case, or lit up, all of which is intended to make an impression when a guest spends $175 on a drink: the bartender has to climb a ladder or unlock a case, or ostentatiously remove the bottle from the lighted display. If the music would stop, the lights would brighten and a siren would go off, it would be an even more effective way to let everyone in the bar know that a guest is dropping serious money on a shot of liquor – and, even though they might not admit it, that is exactly what the guest really wants when they buy a Veblen Good: for everyone to notice.

PREMIUM WELLS ARE A BAD IDEA

The price-elasticity theory also tells us that having a "premium well" is a bad idea because your price sensitive guests just don't care that much about a premium well. So if you charge more for a premium well, many will just choose a different bar where wells are cheaper. And if you don't charge more for a premium well, you are throwing money away.

A POS SYSTEM ENABLES YOU TO PRICE BASED ON PERCEIVED VALUE

Having a POS system means that you can have unlimited keys and hundreds of different prices (unlike an old-fashioned cash register where someone has to remember which price to charge for each brand). And that enables you to price based on perceived value. If your guest believes that Tito's is superior to Absolut, you should price them differently. You don't need to price both based on the fact that since they cost the same, you need to use the mark-up for a "Call."

POUR SIZE

We service thousands of bar in the U.S. No two bars have the same pour sizes for every drink. But it might be helpful to understand the statistics we see in regard to standard pour sizes. For a single-ingredient drink such as a highball:

- **40% of our clients have a 1.25 ounce standard pour size**
- **45% of our clients have a 1.5 ounce pour size**
- **5% of our clients have a 2 ounce pour size**
- **5% other pour size**

Which pour size is best? A lot depends on whether or not your guests will notice the difference. Or, perhaps more importantly, even if they do notice the larger pour, will they be willing to pay a higher price for the extra alcohol?

If you want to have a “heavy pour” you will need to charge more. If you are pouring an extra ½ ounce and that equates to 25% more than your competitors, obviously you will need to charge 25% higher prices to make the same profit margin. So the question is whether the majority of guests will recognize that your bar is pouring a slightly larger drink and, if so, will they be ok paying a higher price?

Furthermore, heavy pours mean fewer drinks will be sold. Guests drink until they reach a certain comfort level. Sometimes that might be because they intend to drive home and so they will drink only until they feel a little buzz from the alcohol. Sometimes it might be a big night out and they will drink until they can’t drink anymore. But either way, they will reach a level where they don’t order any more drinks. If your bartenders over-pour, or your pour size is heavier than your competitors, your guests will reach that limit sooner and you will sell fewer drinks.

One could argue that pouring a larger portion for the same price should result in a busier establishment but that rarely seems to happen – and even when it does, it usually means that the average guest buys fewer drinks.

OVER-POURING KILLS YOU IN TWO WAYS

There’s actually a much more important lesson that derives from the fact that heavier pours lead to lower sales. The lesson is that over-pouring will kill profitability. It does that by lowering your profit margin on each drink sold and, even worse, it leads to your guests ordering fewer drinks:

Lower profits + fewer drinks = profit problems

NOW IT GETS COMPLICATED

There are a number of other issues that should be considered when setting prices.

Martinis/Manhattans and other "boozy" drinks

Boozy drinks such as martinis and manhattans and drinks made with higher alcohol content must also be a consideration. If a given customer will be ready to leave after consuming six ounces of alcohol, that could mean you sell them 2 x 3oz martinis or it could mean you sell 4 x 1.5oz cocktails. If you sell the martinis for $8 and the cocktails for $5, you are either going to collect $16 selling martinis or $20 selling cocktails. So selling $8 cocktails would mean 25% lower sales dollars. This should be factored into your decisions on portion size and pricing.

Don't under-price high alcohol drinks like martinis and manhattans. Make sure that your martini glass size is appropriate. A 7, 8 or 10 ounce martini glass is a terrible idea.

Doubles

We see three different strategies for doubles whereby doubles are:

1. Double the size and double the price
2. Double the size but a discounted price
3. Slightly less than double the size at a discounted price

We think the sweet spot is #2 above: offering a true double but at a discounted price. It is particularly helpful to be able to suggest a discount on a double when dealing with guests who pressure your bartenders for a stronger drink ("why don't you order doubles – that way get a strong drink and a discount?").

For many guests the idea of ordering a "double" seems greedy or overindulgent, like ordering "supersize" fries. In the 1970s in Vancouver, Canada the Keg Restaurant chain promoted "Keg-sized" drinks, which were just discounted doubles. By calling them "Keg-sized" instead of doubles, their guests perceived the offer as a really good deal. As a result, the Keg sold a much, much higher percentage of doubles than other restaurants – boosting revenues and check averages.

If you are going to offer a true double at a discounted price, it's important that you give some thought into how to ring it up. Too many operators just add a $5 or $6 upcharge for the extra alcohol. As a result, they are charging too much for a well drink and nowhere near enough for a top shelf drink. If I see that ordering a double 18-year Highland Park (my favorite scotch) only costs an extra $5, I jump on it knowing that I'm getting the extra portion at cost. The best approach is to have a unique double key setup in the POS system for all brands, programmed with the appropriate price.

Shots and Rocks Drinks

Our clients are pretty evenly split between those who pour the same size portion for a drink prepared "on-the-rocks" versus those bars who pour a larger portion with a corresponding upcharge.

Almost all bars pour shots that are the same size as their standard highball pour. A few, though, pour a 1-ounce shot at a discounted price, believing that their guests are happier with a lower price for a slightly smaller shot and that this policy helps control drunkenness.

Cost of Mixer

Some mixers have a significant cost that warrants use of a modifier to build a higher priced drink. Here are the costs of a few popular mixers:

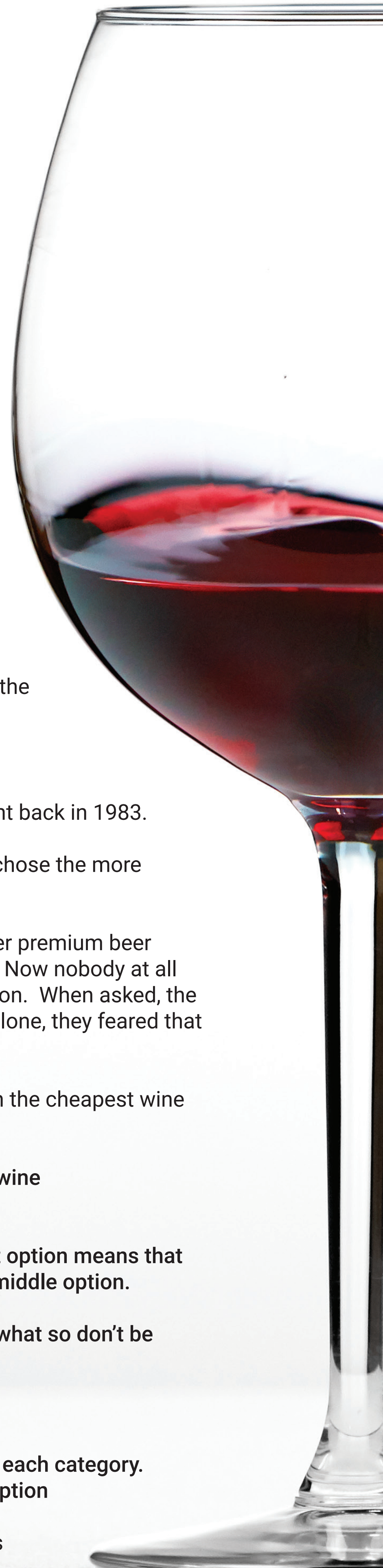
- **Highball 7¢**
- **Pina Colada 42¢**
- **Mule 60¢ (1/3 bottle)**
- **Bloody Mary 60¢**
- **Margarita 65¢ (cost of ½ oz triple sec + sweet'n'sour)**
- **With Red Bull 78¢ (1/2 can)**

Labor Cost

Some drinks take a significant amount of time to prepare. Mojitos have to be muddled, then shaken. Blended margaritas take extra time. Pricing on the ingredients doesn't factor in the labor cost. But sometimes that can be significant. Preparing 10 Rum & Cokes certainly takes less than 10 minutes. At a price of $3.50 each, that would add up to a 26% prime cost (liquor cost + labor cost) whereas preparing 10 blended margs or mojitos takes double the time. So at $4.50 each the prime cost is around 40%.

Pre-batching high volume cocktails is a great solution. It eliminates the labor cost issues and dramatically speeds up service at peak periods.

WINE PRICING IS BOTH ART AND SCIENCE



It makes sense to discuss wine in this separate section because wine drinkers have been notoriously outspoken about restaurant wine pricing. Here are some of the best ideas we've learned from our clients.

Offer two pour sizes for wines-by-the-glass

Several clients offer a 6-ounce and a 9-ounce option for wines-by-the-glass. They offer a very small discount on the 9-ounce size (for example if the 6-ounce is $8, the 9-ounce might be priced at $11.75 instead of $12). One server described it to me this way "6-ounces is what you get at most restaurants, 9-ounces is what you pour yourself at home!"

Guests like the option because sometimes (especially at lunch) 6-ounces is not quite enough whereas two glasses could be too much. 9-ounces is just right. Often a guest will start with a 9-ounce pour but half-way through dinner they realize that they want a little more so they add a 6-ounce glass. Without the 9-ounce option, the guest would likely have just ordered 2 x 6-ounce glasses.

At one particular client, incremental sales and profit rose significantly after they introduced the 9-ounce option – adding $500/week in extra profit from this one idea alone.

Offer three options: low, medium and high

The Journal of Consumer Research published what is now a famous beer pricing experiment back in 1983.

In the first experiment only two kinds of beer were offered. Priced at $1.80 and $2.50, 80% chose the more expensive beer.

When a third beer was offered, consumers always preferred the middle option. When a super premium beer was offered at $3.40 (you can tell this must have been 1983!). The impact was astonishing. Now nobody at all wanted the cheapest beer. 10% ordered the super premium. And 90% chose the middle option. When asked, the study participants said that the middle option seemed like a "safe" choice. Based on price alone, they feared that the cheapest option was low quality – and they didn't want to be perceived as "cheap."

What can we learn from this? Offer three options per category, taking the lowest mark-up on the cheapest wine and the highest mark-up on the most expensive wine. This works for a few reasons:

- **All your guests will judge the fairness of your pricing based on the lowest priced wine (economists call this "price anchoring").**

- **Your most price-sensitive guest will be reassured that the pricing of the cheapest option means that you are pricing fairly, but even those price-sensitive guests will end up buying the middle option.**

- **A significant number of guests will choose the most expensive option no matter what so don't be afraid to add a high priced option to your by-the-glass menu**

- **Most of your guests will choose the middle option**

- **If you have an extensive wine or beer list, it's a good idea to offer three options in each category. For example, list three chardonnays by the glass: a low, middle and higher priced option**

We would recommend using kegged wines for your low-price value selection. Kegged wines are well accepted these days. They offer a lower cost, easier storage, and fresher tasting wine - that won't spoil!

YOUR WINES ARE MORE EXPENSIVE THAN COSTCO

Guests use retail wine prices as their anchor in order to determine if they are being ripped off. If your guest sees Kendall Jackson Chardonnay on your menu for $30 and they have bought it at Costco for $11, they may conclude your prices are high. That isn't a fair conclusion: after all, running a restaurant is expensive and the guest is not factoring in rent, labor, overhead, advertising, maintenance and all the other costs of doing business. But fair or not, that is how many are going to evaluate your pricing.

If you are going to offer the same old (tired?) brands that your guest can buy in the supermarket, it would be a good idea to take your lowest margin, knowing that this will be an anchor price.

There are tens of thousands of excellent wines that are not routinely available in grocery stores and, therefore, don't offer that easy (and unfair) price comparison. The key is to offer familiar varietals (ie: cab, chardonnay, Malbec) but unfamiliar brands.

Trophy wines are the exception. Your prices can be higher than retail and your guest won't be overly concerned because trophy wines are Veblen Goods: your guest is buying them partly because they are expensive.

My pet peeve

There is nothing worse than a stale wine list that hasn't changed in five years. Actually, there is something worse: serving red wine at room temperature. In the summer that often means the wine is 73° or worse. I've stopped drinking wine at some really good restaurants because the red wine is way too warm. Inexcusable.

THE "DECISION CORRIDOR" IN YOUR BAR

Research by Diageo, the world's largest liquor company, has found that more than 60% of guests haven't decided what they will drink until seconds before they place their orders. Diageo describes the line-up at the bar as the "Decision Corridor".

Think about that for a minute. What an astounding opportunity for you to sell your customers something different from their usual "rum and coke" or "Bud Light" – something that they will enjoy; something that differentiates you from all the other bars in your neighborhood; something that is very profitable.

But most bars blow this opportunity because they don't have a strategic plan for the Decision Corridor. Our best clients do a few things to take advantage of this:

- **They have a signature drink that their guests cannot get anywhere else**
- **They have an interesting, unique drink menu that is prominently displayed**
- **They train their staff to make suggestions that their guests will enjoy**

A WORD ON UP-SELLING

It is also a good idea to train your staff on basic upselling techniques but perhaps even more important is to get your team to understand why up-selling is good for the bar and good for them.

Of course, up-selling to a premium brand is pretty stupid if you don't actually make more money by doing so. It is surprising, however, how often we find that our clients actually lose money by up-selling to some brands. For example, it is no good charging an extra $1 for a Grey Goose vodka if Grey Goose costs $1.10 more than your well vodka.

Every bar should calculate the ideal pour cost from each drink (and food item, for that matter) at least once a year.

As part of this analysis, we recommend figuring out the additional profit contribution from up-selling to a premium brand. In this example that we put together for one of our clients, we discovered that they actually lost money whenever a customer ordered a J&B scotch instead of a well scotch, and that the Glenfiddich pricing was too low compared to other single-malts:

BRAND	DRINK COST	REGULAR PRICE	POUR COST	PROFIT PER DRINK	UPSELLING PROFIT
Well Scotch	$0.51	$4.00	12.8%	$3.49	
J & B	$1.10	$4.50	24.4%	$3.40	-$0.09
Johnny Walker Red	$1.10	$5.00	22.0%	$3.90	$0.41
Chivas Regal	$1.19	$6.00	19.9%	$4.81	$1.32
Glenlivet 12yr	$1.63	$8.00	20.4%	$6.36	$2.87
Glenfiddich 12yr	$1.64	$6.00	27.3%	$4.36	$0.87
Laphroig 10 yr	$2.01	$9.00	22.3%	$6.99	$3.50
Macallan 10yr	$2.35	$10.00	23.5%	$7.65	$4.16
Glenmorangie 12yr	$2.56	$11.00	23.3%	$8.44	$4.95
Macallan 25yr	$7.11	$35.00	20.3%	$27.90	$24.41

This column shows profit from **upselling.** This type of analysis uncovers missed profit opportunities when **premiums are priced too low.**

Our company, Sculpture Hospitality, has been helping bar and restaurant owners make more money for thirty years. Our first priority is to help eliminate losses from over-pouring and lost sales because that offers an immediate and substantial increase in bottom-line profit. Once that has been accomplished (after a month or two) we often turn our attention to drink pricing issues.

If you'd like more information on Sculpture Hospitality's service, or some advice on drink pricing, please contact us at http://www.sculpturehospitality.com/