**Case Study Report**

**Wendy’s Chili-A Costing Conundrum**

**Submitted to:**

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**Introduction**

Wendy’s Inc. is a quick-service restaurant that mostly serves hamburgers, located in Columbus, Ohio, and was founded by David Thomas in 1969. The restaurant’s continued success and growth is attributed to Thomas’ efforts who applied various strategies to make his restaurant unique from its competitors. Thomas aimed to offer affordable excellent quality hamburgers in a traditional way. They also had to expand the product line. This paper provides answers to the case study solution.

**Background:**

The restaurant’s management knew the only way they could effectively cater to the customers’ individual orders was to get their traditional hamburgers directly from the grill and serve them as quickly as possible. The cooks needed to have hamburgers ready to make in preparation for customer demand when they arrive at the restaurant (Brownlee, 2014). Wendy's initial sources of revenues were from interest earned on investments, sales made by the restaurants; royalties paid by franchisees, and technical assistance fees paid franchisees. However, the company saw a decline in profitability because itslimited menu items were popular (Brownlee, 2014). The restaurant had to critically consider shifting fromits old ways by cutting the production of chili.

**Strategic Analysis:**

Wendy’s success and rapid growth and expansion was attributed to its excellent strategic locations, excellent product differentiation, offering quality products, and timely delivery of products to its customers. Moreover, the quick and simple drive thru also improved the company’s competitiveness. The weaknesses lay in the few menu items that the company sold. There is a need to sell more than four commodities to improve customer choices. Wendy’s also failed to invest heavily in marketing, reducing customer awareness of their chili.

Regarding opportunities, Wendy’s can invest in social media sites and create sites for customer interaction. Moreover, it can expand its operations into foreign markets to increase the level of sales. The case also discovered the need for additional items on the menu to serve various kinds of customers. One of the influential threats is competition, where the company produces imitable commodities. The rivalry lowers the best associated with product differentiation.

Thus, the recommendations are:

* Invest in a wider market
* Expand the menu instead of the current four items
* Address product differentiation to avoid imitation
* Invest in social media platforms

**Financial calculations:**

1. **How was Wendy's able to achieve its initial success and growth?**

Many factors contributed to Wendy's success in the oversaturated fast-food industry, including the division of the hamburger market into young and old. This activity contrasted with the traditional method of fast-food chains. They made fresh beef burgers that were served hot off the grill to their customers. Customers could purchase freshly prepared hamburgers at reasonable prices. Wendy's used square patties on round burger buns, which gave them an edge. Customers could taste and see the patty as it extended beyond the round burger bun. This action aided Wendy's in differentiating its products from those of other fast-food restaurants. Wendy's also limited its menu options to four primary items. Customers, on the other hand, could order a total of 256 different combinations of these burgers. David Thomas had previously run similar networks and was well-versed in Wendy's operations. It was rapidly expanding, with 1407 restaurants open in the first ten years. He limited the menu items to become more competitive by serving high-quality products at reasonable prices. Hamburgers, Chili, French fries, and Wendy's frosty dairy dessert were the four main products. Wendy's signature square patties could also be used to distinguish it from competitors' products. One of the most crucial factors for customers was the delivery time. Wendy's tried to serve food as quickly as possible, using fresh and high-quality ingredients. It was known for providing faster service than other fast-food restaurants, which made customers happier. Wendy's made it easier to maintain a competitive edge by offering only four menu options. Wendy's could anticipate customer needs and provide timely service. As a result, they were able to more accurately and efficiently estimate and control costs.

1. **What benefits might have resulted from Wendy's "limited menu" concept?**

Reduced costs, such as low inventory, limited menu options, and shared resources, lower product cost, quick service, and better-quality items might have been key results for benefits. Wendy Chili's competitors were able to launch new menu items and earn higher profits in fragile situations in the States in the 1980s. Limiting the menu to four major products allowed Wendy’s to control its costs and better forecast the demand for their products. While the cost remained low, Wendy’s could gain price competitive while serving good quality food. Predicting demand for four products is far more accurate and accessible than estimating demand for a large variety of products. The increase in efficiency in providing quick service to the customers was another advantage of this limited four-item menu. The concept ‘limited menu’ was also a differentiating product factor for the restaurant. It made Wendy’s compete out amongst its competitors which was a successful marketing strategy and customers of the firm, that could easily remember the Wendy's menu. As of the new millennium, the quality, price, and variety of products sold would be crucial factors for customer satisfaction.

1. **What were the disadvantages of such a concept?**

Catered to Limited Customer Segment, and Limited Product Items were major drawbacks for Wendy’s. For instance, Wendy’s did not provide a variety of products for the customers when the competitors were offering a vast assortment of products. This gave their competitors a competitive edge over Wendy's in terms of product varieties (Negulescu, 2019). For instance, Wendy’s excluded vegetarian customers, and children, who preferred chicken to beef. This led to a loss in market share (Negulescu, 2019). The restaurant would not be the best place for holding family outings or dinners because the menu does not suit the needs of all the people in the family or group.

1. **Why was the concept eventually discontinued?**

The concept was finally discontinued because more fast-food restaurants were being established which made competition very stiff. This forced Wendy’s to expand its menu to align with the competition. They had to change customer demands and adapt to the new trending consumer market, like providing customers with the desired chicken and more salad options.

1. **Why was Wendy's drive through successful in compared to other quick service restaurants?**

Wendy's drive-thru window was successful due to its quick processing time and accurate order. Wendy's customers can receive their orders in less than 30 minutes, whereas all their competitors require at least 30 minutes. When there were a limited number of high-quality menu items, it was simple to manage all orders. As a result, fast speed and correct order are critical factors for customers who want to use a drive-thru service. Wendy's drive-thru also had a good design and was in a densely populated area. They created the pick-up window so that customers could be served quickly and easily. They were in densely populated urban or suburban areas with high customer traffic. Furthermore, Wendy's was the first in its industry to have a drive-thru window, so customers would recognize Wendy’s first and tend to purchase the drive-orders through's continuously before its competitors. The overall SWOT analysis will be shown below in annex.4.

5. **How much does a bowl of chili cost on a full-cost basis? An out-of-pocket basis?**

This calculation will proceed as follows. Firstly, the crew members oversee cooking the meats. Second, Wendy's Chili was made fresh every day by the assistant manager, who oversaw chopping the meats and adding the necessary ingredients. The average time to prepare the Chili menu is 21 minutes, which is derived from 1-minute: 5-minutes: Getting well-done ground beef from the walk-in cooler: 5 minutes for chopping the meat into small pieces: A crew member cooks patties in 10 minutes after mixing small pieces of meat with special ingredients. Third, each employee who works on the Chili menu must pay taxes equal to 10% of their hourly wage.

When preparing a pot of Chili, three types of costs should be considered for a full-cost basis calculation. Starting, raw materials, which include all the ingredients needed to cook a Chili batch, cost $56.5 for 57 servings, or $0.99 per 8-ounce serving. Direct labor costs, including the assistant manager and crew who prepare and cook patties daily, are $11.55 and $6.33, respectively. These two figures are derived from hourly rates of $10.50 and $5.75, respectively, plus 10% of payroll taxes and other employee-related costs. The total direct labor cost for preparing 57 servings is $3.56. The direct labor cost per serving is $0.22

1. **Assumptions for Scenario 1: Out-Of-Pocket-High Season**

Since Wendy's already had employees committed to making patties, this calculation will assume that direct labor costs, such as the assistant manager's salary, crew member's salary, and tax payment, have been removed. Wendy's needs to prepare and cook 10% more beef during peak season (October through March) due to increased sales (60 percent of total annual sales). Detail in annex.1.

1. **Assumption for Real cost-high season**

The calculation of the actual cost for high season will assume that it is necessary to cook 10% more beef due to a 60% increase in sales, so the cost of ground beef will be $4.20 (10% of the $42 cost of ground beef). (Detail in annex 2)

1. **Assumptions for real cost-low seasons**

The assumptions of the low season's actual cost did not include the crew member's labor cost. In this scenario, the assistant manager is still required to walk into the walk-in cooler to retrieve the patties. Our team uses the same standard as Chili to calculate raw material and packaging costs. So, in the low season, the total actual cost is $0.41 (detail in annex 3).

Regarding Chili, our team believes that it is a byproduct of hamburgers. By was cooking from leftover ground beef. Wendy's did not attempt to make this a stand-alone product line. Furthermore, Booth (2019) stated, "The meat of the Chili comes from leftover meat on the grill that dries out, and is then cut up, frozen, and bagged for later use in the Chili." This is like how the accounting tools website (2020) defines byproducts: “byproducts can be discerned by seeing which ones have a minor resale value in comparison to the value of the other products.”

**6. Would you recommend dropping chili from the menu? Why or why not?**

**Decision: Don't drop chili from the menu**

  It is suggested that Wendy's keep Chili on its menu because this menu strongly indicates product differentiation. Wendy's unique Chili enables the company to gain a competitive advantage over other quick service restaurants in the same industry. Furthermore, product differentiation usually fosters brand loyalty and adds value to customers because the unique Chili is worth paying for. Wendy's can still make a profit of 60-70 percent by selling 8-ounce Chili for $0.99. The leftover ground beef from hamburger is a sunk cost that has already been incurred and cannot be recovered.

**Annexes:**

**Annex 1. ASSUMPTIONS FOR SCENARIO 1: OUT-OF-POCKET-HIGH SEASON**

Since Wendy's already had employees committed to making beef patties, this calculation will assume that direct labor costs, such as: the assistant manager's salary, crew member's salary, and tax payment, have been removed. Wendy's needs to prepare and cook 10% more beef during peak season (October through March) due to increased sales when most people are buying burgers unlike other months (60 percent of total annual sales). As a result, the out-of-pocket cost of ground beef will be $4.20 (10% of the $42 ground beef cost), while the other out-of-pocket expenses include the cost of raw materials which is used in the production of Chili, and the cost of Chili's packaging. The out-of-pocket cost of the high season will be $0.40 per serving, consisting of $0.33 in raw materials and $0.07 in packaging costs. Table 3: Chili's out-of-pocket costs contain additional information (High season).

Table1:Full-cost basis of Chili

|  |  |  |  |
| --- | --- | --- | --- |
| **Description** | **Full-cost basis** | | |
| **Raw material** | **Cost per unit** | **Quantity** | **Total Cost** |
| Crush Tomatoes (can) | $2.75 | 1 | $2.75 |
| Tomato Juice (can) | $1.25 | 5 | $6.25 |
| Seasoning (packet) | $1.00 | 1 | $1.00 |
| Red Beans (can) | $2.25 | 2 | $4.50 |
| Ground Beef (lb.) | $3.50 | 12 | $42.00 |
| Total Raw material cost | | | $56.50 |
| Raw material cost per serving | | | $0.99 |

|  |  |  |  |
| --- | --- | --- | --- |
| **Direct labor** | | | |
| **Activity** | **working times(mins)** | **Cost per hrs.** | **Total cost** |
| **include 10% tax** | **(Time in hrs. \* Cost per hrs.)** |
| Get patties - Asst. Manager | $ 1.00 | $ 11.55 | $ 0.20 |
| Cook patties - Crew | $ 10.00 | $ 6.33 | $ 1.11 |
| Prepare patties | $ 2.00 | $ 6.33 | $ 0.22 |
| Chop meat - Asst. Manager | $ 5.00 | $ 11.55 | $ 1.01 |
| Add ingredients - Asst. Manager | $ 5.00 | $ 11.55 | $ 1.01 |
| Total Restaurant Labor cost /each/hr | | | $ 3.56 |
| total Restaurant Labor cost/each/minute | | | $0.06 |
| Direct labor cost per serving | Total direct labor cost/patty/minute | | $0.22 |

|  |  |  |  |
| --- | --- | --- | --- |
| **Other costs ($ per serving)** | | | |
| Serving Bowl |  |  | $0.035 |
| Bowl Lids |  |  | $0.025 |
| Spoons |  |  | $0.010 |
| **Total other costs ($ per serving)** | | | $0.07 |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Overhead cost** | **Cost in 2001** | **Cost in 2000** | **Average cost** | **5% Allocating** |
| **per year** |
| Depreciation of Property and Equipment | $118,280.00 | $108,297.00 | $113,288.50 | $5,664.43 |
| Operating cost | $91,701.00 | $86,272.00 | $88,986.50 | $4,449.33 |
| Total average Overhead cost per year | | | | $10,113.75 |
| Overhead cost per serving | | | | $0.49 |
| Total cost per serving | | | | $1.77 |

**So, the total cost per serving is the sum of Raw material cost per serving plus direct labor cost per serving and other costs per serving. Which is $0.99 + $0.22 + 0.07+$1.77 = $3.05**

**Table 2: Comparing the out-of-pocket basis of Chili at high season and low season.**

|  |  |  |
| --- | --- | --- |
|  | low season | high season |
| A bowl of Chili cost | Out of Pocket costs | |
| Direct Raw material costs | |  |
| Crushed tomatoes | $2.75 | $2.75 |
| Tomato Juice | $6.25 | $6.25 |
| Wendy's seasoning packet | $1.00 | $1.00 |
| Red beans | $4.50 | $4.50 |
| Ground beef patties | out | $4.20 |
| Total raw material cost | $14.50 | $18.70 |
| Total raw material cost per serving | $0.25 | $0.33 |
| Serving costs | | |
| Serving bowl per serving | $0.035 | $0.035 |
| lid | $0.025 | $0.025 |
| spoon | $0.010 | $0.010 |
| Total serving costs per serving | $0.070 | $0.070 |
| Total cost per serving | $0.32 | $0.40 |
| (Other direct cost + raw material costs) |

**Annex 3. ASSUMPTIONS FOR REAL COST - HIGH SEASON**

1. **ASSUMPTIONS FOR REAL COST - HIGH SEASON**

The calculation of the actual cost for high season will assume that it is necessary to cook 10% more beef due to a 60% increase in sales for that specific time period, so the cost of ground beef will be $4.20 (10% of the $42 cost of ground beef). As a result, Wendy's must pay the direct labor cost for the assistant manager and crew member, as both positions are required and very vital while preparing extra meat for serving the high demand of customers during peak season. Our team also considers the cost of obtaining patties, which equals $0.19 because the assistant manager will take one minute to walk in the cooler to obtain patties. The raw material and packaging costs are computed using the same standard method as Chili's total cost. As a result, the total actual cost during peak season is $0.62.

**Table 3: Comparing t**he actual cost of Chili at High season and low season.

|  |  |  |
| --- | --- | --- |
|  | low season | high season |
| **A bowl of Chili cost** | **Actual costs** | |
| **Direct Raw material costs** | | |
| Crushed tomatoes | $2.75 | $2.75 |
| Tomato Juice | $6.25 | $6.25 |
| Wendy's seasoning packet | $1.00 | $1.00 |
| Red beans | $4.50 | $4.50 |
| Ground beef patties | out | $4.20 |
| Total raw material cost | $14.50 | $18.70 |
| Total raw material cost per serving | $0.25 | $0.33 |
| **Direct Raw material costs** | |  |
| Get patties (Assistant manager) | $0.20 | $0.20 |
| Prepare patties (Crew) | - | $0.22 |
| Cook (Crew) | - | $1.11 |
| Chop meat (Assistant manager) | $1.01 | $1.01 |
| Add ingredient (Assistant manager) | $1.01 | $1.01 |
| Total direct labor (57 servings) | $2.23 | $3.56 |
| Total labor cost per serving | $0.04 | $0.06 |
| Total direct labor cost | $0.09 | $0.22 |
| **Serving costs per serving** |  |  |
| Serving bowl | $0.04 | $0.04 |
| lid | $0.03 | $0.03 |
| spoon | $0.01 | $0.01 |
| Total serving costs per serving | $0.07 | $0.07 |
| **Total cost per serving** | **$0.41** | **$0.62** |
| **(Other direct cost + raw material costs)** |

**Annex 3. ASSUMPTIONS FOR REAL COST - LOW SEASON**

Wendy's can use leftover patties for cooking at a cost of $0.19, so the assumptions of the low season's actual cost did not include the crew member's labor cost. In this scenario, the assistant manager is still required to walk into the walk-in cooler to retrieve the patties. Our team uses the same standard as Chili to calculate raw material and packaging costs. So, in the low season, the total actual cost is $0.41.

Following that, our team computes the operating profit for each season and weighs the profit throughout the year to determine true profitability. However, the profitability of Chili cannot be calculated using the full-cost method because Chili is a by-product material that is already produced from the core product (i.e., hamburger). Our team starts estimating Chili's actual cost by deducting the actual cost of raw materials, direct labor, and other packaging costs. The calculations for the high season (October-March) and the low season (April-September) are separated. Following that, we calculated the total actual cost per serving for the high and low seasons to be around $0.62 and $0.41, respectively. As a result, the high season profitability is 0.99-$0.62 = $0.37 and the low season profitability is 0.99-$0.41 = $0.58. As a result, we take the average profit of the high and low seasons to calculate the profit for the entire year, which is ($0.37+$0.58)/2 = $0.48 per serving.

Regarding Chili, our team believes that it is a byproduct of hamburgers. By was cooking from leftover ground beef. Wendy's did not attempt to make this a stand-alone product line. Furthermore, Booth (2019) stated, "The meat of the Chili comes from leftover meat on the grill that dries out, and is then cut up, frozen, and bagged for later use in the Chili." This is like how the accounting tools website (2020) defines byproducts: “byproducts can be discerned by seeing which ones have a minor resale value in comparison to the value of the other.

**Annex 4. SWOT   Analysis**

|  |  |
| --- | --- |
| **Strength**   * Previous Experience in Fast Food Industry * Quality Product – Unique Shape, Fresh and Cooked to Order * Quick Service and accurate order * Reasonable Price * Good Product Mix * Common Raw Materials * 256 Burger Combinations * Reduced Waste * Optimally Located restaurants (area) * Hight Brand image * Large franchise store   **Opportunities**   * Expand menu by creating variations of popular menu items they already have * Offer seasonal menu items | **Weakness**   * + Limited Segment   + Limited Menus   + Single-Unit Franchise Expansion   + Customization of Burgers   + Unhealthy food   + Limited international presence     **Threats**   * Limited menu = limited customer base * Competitors having similar items plus other menu items * Keeping up with changing markets (ex: being more health conscious) |

**Annex 5: Main notes from presentation**

**1. Using the data from the case, how do you think Wendy is performing now, especially during the pandemic?**

The question focuses on the preference of drive-thru window and quick-service restaurant chains during the pandemic. They are performing as well as expected, when the pandemic first began income in the company was very slim to none. As the pandemic has become less and people are able to move around in their daily lives, we have seen a rise in the marketing used to get money back as well as customers using the drive through most to receive their food.

**2. Given you were Wendy’s manager, which costing method would you prefer?**

Each accounting method has its merits and demerits. However, some methods are best suited for a given set of operations or businesses. The job costing method would be best suited for this company because each job has a price and certain job as well as each product. In that case, it is best to separate each giving the amount of money needed for each job.

**3. Should Wendy’s keep or remove their Chili?**

Wendy's can reduce beef waste and increase overall profit margins if they keep their Chili. Furthermore, by expanding into new and niche markets, Wendy's will be able to increase profits. However, removing Wendy's Chili will result in increased food waste and lower profit margins. In this situation, Wendy's must accurately forecast the beef used to make hamburgers to reduce food waste, which influences the overall profit decrease. The group that presented talked about the idea of Wendy’s keeping their Chili but offering other options as well like using a different type of meat for the chili. Also, they talked about having healthy versions of chili as well. Another idea that was brought up was having chili as a seasonal item instead of year-round. They discussed some complications that would arise from that like if Wendy’s would lose money if they only offered the chili for a limited time.

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