

Opinions

Navigating third-party delivery in restaurants

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Delivery is the fastest-growing segment in the foodservice industry. Many restaurateurs are unable to provide delivery without using third-party services, which have high fees. How do you take advantage of this market segment profitably?



By Jeff Dover

Delivery is the fastest growing segment in the restaurant industry, led by third-party delivery.

Management consulting company Technomic estimates the top ten U.S. chains generated about \$8 billion in delivery sales in 2018. It further indicates that restaurant sales increased 3.6% in 2018; however, delivery sales increased 10% with third-party delivery accounting for 55% of delivery orders.

Service Management Group indicates awareness of third-party delivery increased 24% in 2018 over 2017 and usage increased 14% in this same period. The same survey found that 85% of respondents will use third-party delivery in the future. Third-party delivery users average 10.5% more restaurant visits than typical consumers. Clearly, this is a distribution channel that restaurateurs should seriously consider and could be at a competitive disadvantage if they don't.

Most restaurants do not generate enough business or can't find the drivers to do their own delivery. Third-party delivery, for many is a necessary evil. The commissions are significant, however—up to 30% for some and even the large chains' commissions exceed 20%. When you consider the average restaurant profit in the U.S. is 6.1% of gross sales for full-service restaurants and 6.6% for quick service restaurants, this is a key challenge.

Other challenges, such as the third-party "owning" the customer (and not sharing this with the restaurant) and the lack of integration between third-party delivering ordering platforms and the restaurant's point of sale (commonly referred to as "tablet hell") post logistical challenges. Third-party delivery customers are likely to blame the restaurant (as opposed to the third-party delivery company) for mistakes in the order, which is likely the restaurant's fault keying the order in the POS, and for longer delivery times than promised, which is likely not. Problem occurrence, according to Technomic, is three times greater with third-party delivery than it is for dine-in or takeout orders.

However, for most restaurants, delivery is becoming a key success factor. Consider:

Incremental business—A survey by TDn2K found that 89% of restaurateurs believe delivery to be incremental business. A Service Management Group survey supported this finding: if customers had not ordered food for delivery, only 10% would have visited a restaurant for that meal occasion. Third-party delivery generates incremental business, it is not cannibalizing in-store or takeout sales.

Greater average check—The TDn2K survey found 89% of limited-service restaurants and 51% of full-service restaurants generate greater check averages through third-party delivery over other to-go orders. This is not surprising as "anonymous" ordering provides more comfort to customers when upsizing their orders (i.e., no stigma to order the large fries) and, unlike human order takers, technology never forgets to upsell.

Demand is greatest when in-restaurant demand is lowest—Research by IPSOS in Canada shows that delivery demand is 185% greater during snow and 236% greater during heavy rain, times when on-premise demand is low.

3PD is key for the demographic that generates the most restaurant visits—Third-party delivery appeals to younger consumers who have taken over the baby boomers as the demographic generating the greatest amount of restaurant sales and visits. Netflix and Amazon Prime have resulted in the younger generation cocooning earlier; however, they want to eat what they want when they want it and delivery appeals to such needs. According to a survey by Services Management Group, among the primary reasons delivery is used, 18% are unable to travel, 17% prefer not to cook, 17% enjoy the ease of ordering and 12% see time savings.

So, the question becomes, how can restaurants be successful with third-party delivery and the high commission rates? One key way is to integrate their POS

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with the delivery company (i.e., no entering the orders). Some third-party delivery can integrate with major POSes, and I believe this will eventually come. For now, restaurants can use companies such as Chowley for integration.

Restaurants are adjusting menus and improving packaging for third-party delivery. Menu innovation can include modifying products to keep their quality from preparation to delivery. Many restaurants are including only its most profitable menu items on the delivery platforms. Some restaurants limit modifiers online; however, I believe this should not be done—integrate the third-party delivery platform with your POS instead. The ability to select ingredients and modify menu items is key for millennial and Generation Z consumers.

Another opportunity to offset commission costs is through pricing strategies. Charge more for menu items offered through third-party delivery. Consumers are willing to pay for convenience, in some cases accepting the delivery fee is greater than the total order. Experiment with the price elasticity of your menu items.

As restaurants grow their delivery business, they are typically able to reduce other costs. Some restaurants try to do their own delivery and only use third-party delivery for orders that they can't handle in house for a reduced commission. Front-of-house labor can be decreased. As more and more restaurant meals are being consumed off-premises (according to Technomic, \$198 billion or 38% of restaurant sales in 2018), restaurants are able to reduce their footprints and save on rent. Some restaurant chains are using “ghost” kitchens in low-rent areas for third-party delivery, though this can be an issue for franchise organizations cannibalizing delivery business from their franchisees.

In some markets, restaurateurs are combating high third-party delivery commissions by grouping together to provide their own delivery services. In North Collins, Colorado, restaurateurs have started NOCO Nosh while restaurants in Iowa City have banded together to start Chomp. Look for more “local” third-party delivery in the future.

In conclusion, be sure that your restaurant is taking advantage of the growth opportunity provided by 3PD.

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