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Level 3 Cambridge Technical in Business

05834/05835/05836/05837/05878 Unit 3: Business decisions

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Jasmine Gardens of Thailand Ltd

The business

Jasmine Gardens of Thailand Ltd (JGT) owns a chain of takeaway outlets serving food inspired by the country of Thailand. The business operates twelve food takeaway outlets in the London area, all called ‘Jasmine Gardens of Thailand’.

The business was started in 2008 by friends, Kai and Ling. Kai had identified a gap in the market for a takeaway business that served high-quality food and catered for a range of special dietary needs. JGT’s first takeaway outlet was in North London. JGT then opened other outlets in areas of London where commuters with above-average disposable incomes tend to live. The business does not currently own any properties. All of its takeaway outlets, and its Head Office, are secured on leases ranging from three to ten years.

As the founder with the original idea for the business, Kai owns 55% of the shares in JGT. Ling owns the remaining 45%. Whilst legally this gives Kai complete control over strategic business decisions, the two owners have an informal agreement that they will aim to reach agreement before any major decisions are taken.

The market

The food takeaway market is very competitive. The cost of setting up a takeaway business is relatively low and there are a large number of rival providers. Kai and Ling decided from the outset that they would market their business on quality rather than price. Their customer offer is based on using high-quality, fresh ingredients to produce dishes that present an authentic taste of Thailand. To maintain JGT’s marketing profile, the owners do not use the services of takeaway delivery companies; instead they employ their own delivery drivers at each of their outlets. The business was ahead of the market when it built its menu around the needs of people with special dietary needs. Most items on its menu are suitable for vegans, as well as being gluten-free.
In recent years, however, many food outlets have extended their menu offer in this way. As a result the market has become even more competitive. This has reduced JGT’s ability to sell its products at high prices. Despite this, the business is currently very profitable, with typical net profit margins of 10-12%. The business has built up healthy cash reserves of approximately £100 000.

The future

Kai and Ling have been thinking about the long-term future of the business. Both owners agree that the main aim of the business should be to expand without compromising on current rates of profitability. Kai thinks that it is now time to expand aggressively into new areas and would like to use the cash reserves to help finance this. Ling is happy to see the business continue to grow but would prefer the financial and other risks of expansion be kept to a minimum.

Kai and Ling agreed that they would each come up with proposals to support the business through the next few years. Between them, they have chosen three options to consider in more detail.

Option 1: Increase its chain of London takeaway outlets

Ling has identified two locations in the London area where JGT could open new takeaway outlets. Both are in places with similar customer profiles to the business' existing outlets. Both locations have premises available on 5-year leases. Each property would require renovation to make them suitable for JGT's needs. In addition, a new full-time manager and part-time staff would need to be employed for each location.

Ling has estimated that the capital expenditure for this option would be £60 000 per property. Ling would like to finance the capital expenditure using a 5-year, variable rate, business loan of £80 000 with an initial interest rate of 10%; with the balance being taken from the cash reserves. Additionally, there would be ongoing revenue expenditure of £100 000 per year.

Ling estimates that the average rate of return (ARR) for this option calculated over five years would be 7.5%, with a payback period of 45 months.

Option 2: Open a dine-in restaurant in central London

Kai has always wanted to open a dine-in restaurant. Kai has heard about a central London location (currently an upmarket Italian restaurant) that would shortly become available on a 10-year lease. The restaurant would be able to accommodate fifty diners at a time. JGT would need to employ a full-time manager and several chefs as well as part-time kitchen and waiting staff.

The restaurant would require capital expenditure of £80 000. The capital costs would be entirely funded by a 5-year, variable rate, bank loan with an initial interest rate of 10%. There would also be additional, ongoing, revenue expenditure of £350 000 per year. Kai hopes that JGT's cash reserves would be sufficient to fund the first three months' revenue expenditure, whilst the restaurant generates its own revenue.

Kai estimates that the average rate of return (ARR) for this option calculated over five years would be 5%, with a payback period of 48 months.

Option 3: Purchase a takeaway business in the Northeast of England

Ken's Wok Delights is a small chain of three food takeaway outlets in the Northeast of England. All three outlets are in a large seaside town which has recently suffered from several business closures. Kai has heard that some major new business developments have started in the town and he thinks that these will help to lower unemployment in the area. Ken's Wok Delights aims to compete by offering a low-priced menu and does not currently cater for vegans or those who prefer a gluten-free diet.

The three outlets would be rebranded as 'Jasmine Gardens of Thailand' and offer the same menu as the existing outlets in London. Capital expenditure for this option would total £300 000. This would be funded using all of the existing reserves plus a 7-year, variable rate, bank loan with an initial interest rate of 8%. There would also be additional, ongoing, revenue expenditure of £280 000 per year. Kai hopes that the first three months' revenue expenditure could be financed by a bank overdraft of £70 000 with an APR of 15%.

Kai estimates that the average rate of return (ARR) for this option calculated over seven years would be 5.71%, with a payback period of 60 months.

Turn over

Appendix 1: Restaurant profit margins

Some industries, like clothing and jewellery, operate on high profit margins.

The restaurant industry does not have the luxury of running on high profit margins like this. A sandwich is a sandwich, after all, so diners will not be happy to spend extravagantly on their afternoon lunch.

Average profit margins across different types of restaurants:

- Catering and Events: 7-8%
- Food Trucks: 6-9%
- Fast food and takeaway: 6-9%
- Dine-in: 3-5%

Why are they so low?

Restaurants have a lot of expenses. No matter how expensive a meal is, a significant portion of the revenue will go towards ingredient costs and overheads. The restaurant industry is highly competitive: diners can easily go to a competitor if they think that prices are too high.

Appendix 2: UK base rates

The UK base rate is the rate the Bank of England charges banks when they borrow money. The base rate influences the interest rates that banks charge businesses for commercial loans, overdrafts and other types of credit.

UK Official base (interest) rate 2013-2022