



## **Strategies for SMEs in the restaurant industry to cope with inflation**

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Bachelor of Business Administration, International Business

Thesis

2025

## Abstract

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<b>Degree</b> Bachelor of Business Administration
<b>Report/Thesis Title</b> Strategies for SMEs in the restaurant industry to cope with inflation
<b>Number of pages and appendix pages</b> 45 + 1
<p>Inflation has been a significant issue that has had an impact on many sectors, the restaurant industry included. In this thesis, we will examine SMEs from the industry and their strategies to survive inflation. The research in this thesis focuses on the operational costs, consumer behaviour, and pricing strategies among restaurateurs. The theoretical framework includes the history and main causes of inflation, its impact on the restaurant industry, and different pricing and cost management strategies.</p> <p>The research uses qualitative analysis, which is based on interviews with professionals from the restaurant industry and secondary research. These provided the study with extensive information about effective strategies to manage inflationary pressures. The key findings highlighted procurement accuracy, effective cost management, and strategic pricing of menu items. The research also highlighted the impact of consumer behaviour on pricing strategies and the need for innovative solutions to remain profitable during these problematic times.</p> <p>Internally, inflation has led to several operational inefficiencies, such as rising raw material and labour costs. These have led to changes in procurement practices and energy consumption. Externally, consumer purchasing power has decreased, and VAT changes have had an impact on the financial standing of restaurants. The research uncovers that even when some restaurants have been able to remain financially stable through improved internal processes, many still struggle with the challenging environment among restaurants. The rising costs and reduced profits have especially had an extensive impact on the operations of casual restaurants.</p> <p>The study identifies several cost management strategies, the most prominent ones being investing in staff training, procurement management through purchasing pools, and resource optimisation techniques such as waste reduction and inventory management. Additionally, the research emphasises the importance of benchmarking and measuring operational metrics for effective cost control.</p> <p>The results provide restaurateurs with recommendations which can be applied to combat the negative impact of inflation on their operations and to ensure financial stability. These recommendations include the adoption of balanced pricing strategies, focusing on high-margin menu items, and the use of innovative solutions to enhance operational efficiency. The results illustrate an extensive understanding of the factors contributing to the resilience of SMEs from the restaurant industry to inflationary pressures. The results also provide practical insights for maintaining financial stability in a volatile economic environment.</p>
<b>Key words</b> Inflation, Restaurant Industry, Cost Management, Pricing Strategies, SME

## Table of Contents

1	Introduction .....	1
1.1	Background.....	1
1.2	Research Questions and Methodology.....	2
1.3	Delimitation or Project Scope .....	4
2	Inflation and its effects.....	5
2.1	History of inflation.....	5
2.2	Causes of inflation and theory .....	7
2.3	Impact of inflation on businesses.....	11
3	Pricing and cost structure in restaurant industry .....	14
3.1	Pricing Strategies .....	14
3.2	Cost Structure .....	19
4	Methodology.....	25
4.1	Research Approach.....	25
4.2	Data Collection Methods .....	26
4.3	Data Analysis Methods.....	27
4.4	Research Process and Schedule .....	27
5	Results .....	29
5.1	Impact of Inflation.....	29
5.1.1	Internal Impacts .....	29
5.1.2	External Impacts .....	31
5.2	Pricing Strategies .....	32
5.3	Cost Management Strategies .....	33
6	Discussion.....	36
	Sources .....	41
	Appendices .....	46

# 1 Introduction

Inflation has been a prominent topic for many years, and it continues to be one for the foreseeable future. After the pandemic the economy started to recover for the first time in a while. However, due to the economic turmoil resulting from the Russia Ukraine war, new challenges have emerged for consumers and entrepreneurs. The war has caused several supply chain disruptions which has directly affected the prices of everyday goods such as wheat, corn, gas, oils, and metals to rise greatly. The imbalances of supply-demand and different policy supports that were already a concurring problem risen from pandemic times have created a problematic atmosphere which has a significant impact on our lives. In this thesis I will dig deeper into the subject from restaurateurs' perspective and how they can manage the impacts of inflation in the correct manner. (Attinasi, Balatti, Mancini & Metelli 2022), (Cascaldi-Garcia, Orak & Saijid 2023)

In this thesis I will explore into the subject from restaurateurs' perspective and how they can manage the impacts of inflation in the correct manner. In the theoretical framework I will go through inflation and its effects and pricing and cost structure in the restaurant industry. After reading the theoretical framework reader will be able to understand the basic concepts about inflation, including history, why and how inflation works and how it impacts restaurants. It also includes pricing and cost structures for the restaurants and guidance on how to implement and identify correct instruments to focus on.

In this thesis, I will use qualitative analysis by interviewing individuals in managerial positions from the restaurant industry to deepen my understanding of the situations and pressures that affect restaurants due to inflation. I will also do desktop research to find information regarding different phenomena and strategies. This knowledge will help to understand inflation and how to control the effects of it.

## 1.1 Background

The topic of this thesis is "Strategies for SMEs in the restaurant industry to cope with inflation". It is a research-based thesis for the degree of Bachelor of Business Administration, International Business. My major is financial management thus this thesis is done from a financial standpoint. The objective of this thesis is to give restaurateurs suggestions on how to handle the difficult situation regarding the costs, keeping the business financially stable and how to stay resilient to inflationary pressure. I aim to create a clear and helpful summary that has insight from various perspectives. I will highlight the procedures that restaurants that have succeeded in this difficult situation have used to survive and stay afloat. From consumer standpoint, I have recently noticed the impacts of

inflation on the restaurant industry and how it is operating. After the pandemic I have been working on the field parallel to university studies and I consider myself as a “foodie” and there has either been notable rise in the prices, or the quality of food has gone significantly worse. These methods might not be the most ideal ways of cutting the costs as the customer experience suffers from it.

As Finland has had a significant surge in business bankruptcies many entrepreneurs have been struggling to keep their business profitable. In 2023, over 2700 companies filed for bankruptcy with a 26% increase from the previous year. This is the highest amount since the 2009 financial crisis when 2200 companies filed for bankruptcy. The bankruptcies have hit several sectors severely and according to Jaakko Nors, a product owner specialising in bankruptcies at Asiakastieto, the trend of delaying the need for restructuring until it is too late has been a prominent problem as of late. With correct preparation by monitoring financial health of customers and supply chain partners and dialogue between debtors and creditors, some of the issues would be solvable. The restaurant industry is no different and the importance of planning and preparation is ever present. (Nors 2024)

Restaurant Industry in Helsinki has been in a recession for some time. Bankruptcies have risen by 70% from the year 2022 to 2023. As of March 2024, 16 restaurants and cafes in Helsinki have filed for bankruptcy. Customer behaviour has also changed overtime as the amount spending and restaurant visits have decreased. Customers' preference to order drinks or multi-courses menus is not as common as it used to be and on occasions of celebration, many prefer to celebrate at home instead of in restaurants. For many restaurants lunch is a big source of revenue. Customer behaviour regarding it has also changed due to pandemic, economic factors, and rising popularity of remote work. All these difficulties culminate and according to Nors, 17% of the food industry faces significant or severe challenges financially. (Bäckgren, Nissinen 2024)

## **1.2 Research Questions and Methodology**

The aim of this thesis is to help SMEs from the restaurant industry to find suitable strategies to cope with inflation and its impact on profitability, financial stability, and pricing models. The outcome of this thesis will be able to provide the reader a comprehensive understanding of factors contributing to restaurants' resilience towards inflationary pressure and how they can remain financially stable.

The international aspect required for all theses is fulfilled by the nature of the subject of inflation. Inflation is heavily influenced by global economic trends, trade and supply chain disruptions and policy reformations by central banks and governments.

Investigative questions:

IQ 1. What internal and external factors contribute to a restaurant industries SMEs resilience to inflationary pressure

IQ 2. What are the most effective measures that restaurants can implement to minimize the impact of inflation?

Table 1. represents the overlay matrix for this thesis. Table includes the investigative questions, which chapter discusses the theory of it. The table also includes the numbers of interview question sets and what results the set in question provides. The full list of interview questions can be found in the appendix.

Table 1. Overlay matrix

Investigative question	Theory	Results	Interview Questions
IQ 1. What internal and external factors contribute to a restaurant industries SMEs resilience to inflationary pressure	2.2 2.3 5.2	1. 2.	1. 2.
IQ 2. What are the most effective measures that restaurants can implement to minimize the impact of inflation?	3.1 3.2 5.3 5.4	1. 2. 3. 4.	1. 2. 3. 4.

### 1.3 Delimitation or Project Scope

The timeframe which I am focusing on will be 2020-2024, in this timeframe the COVID-19 and the aftermath of it has affected the supply chains and changes in consumer behaviour have affected the inflation. Also, many countries implemented fiscal and monetary stimulus measures to counter the effects of pandemic and support the economy. These measures increased the money supply and aggregate demand which created upwards pressure on prices. Energy and commodity prices have also increased due to geopolitical tensions, rising demand and environmental policies. On 2022 Finland's inflation rate was 7.1% higher than on the year 2021 rising from 0.3% to 7.1%. As the inflation rate in Finland has been between -0.2% and 4.1% from 2005-2021, the smaller restaurants have encountered some troubling times with the sudden rise of the price of goods. (Clausnitzer 2023)

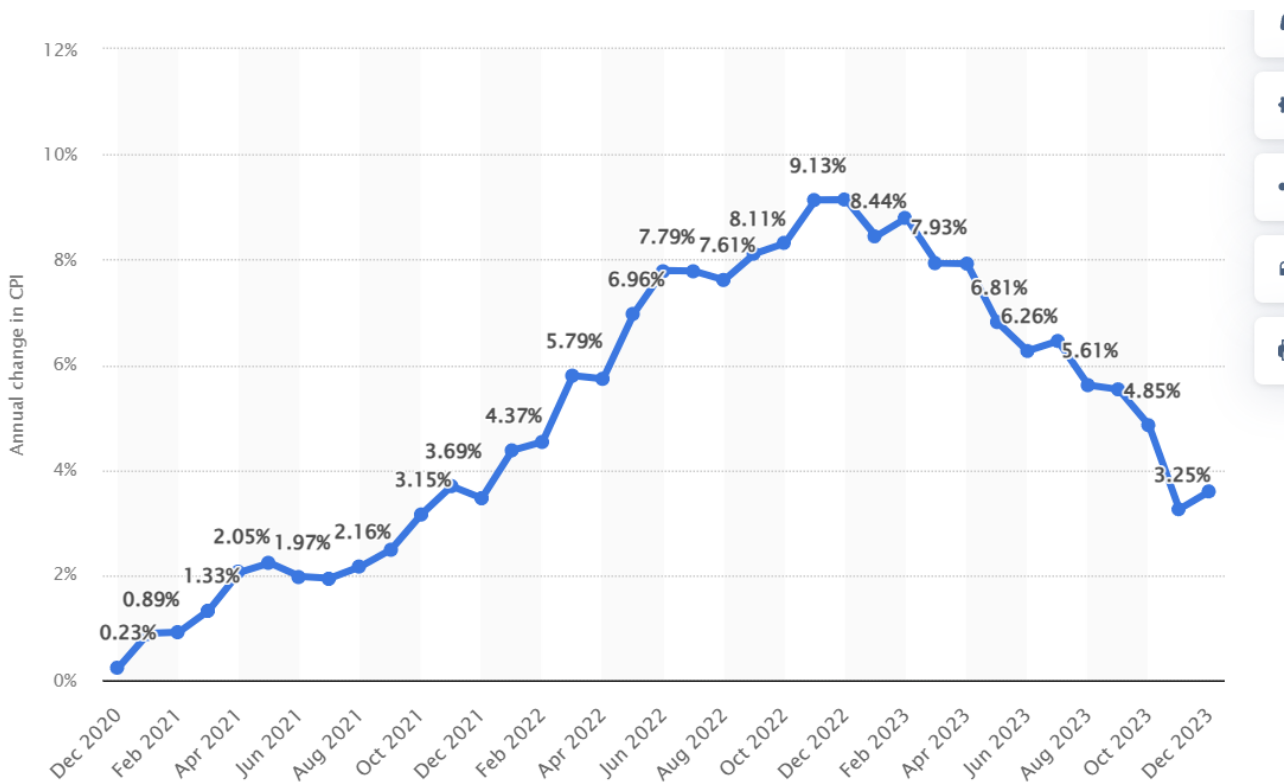


Figure 1: The evolution of Customer Price Index between December 2020 and December 2023 (Adapted online, Clausnitzer 2024)

As seen from the figure above, Customer Price Index has been on the rise since December 2020 which is not necessary a bad thing. However constant rise in CPI indicates rising costs and economic uncertainty. As wage adjustments are needed and interest rates rise, individuals are often left with struggle regarding their personal finances. (DeSilver 2022)

## 2 Inflation and its effects

This chapter includes the basic concepts and theory about inflation. I will start with the history and continue to the causes and theory and finish with the assessment of the effects on restaurants.

### 2.1 History of inflation

The word inflation originates from Latin, word “inflare” which means “inflate” or “to blow into”. It refers to a general trend of rising prices, rather than change in specific price. Inflation has been a recurring phenomenon since ancient times. In ancient Mesopotamia, Egypt, Greece and Rome, there have been occurrences of rulers reducing the valuable metal contents of coins or printing additional currency, usually to finance their wars, construction projects and so on. This has led to inflationary pressures. After the ancient times and the fall of Rome came the Middle Ages and later Renaissance, which had similar inflationary pressures. It mostly persisted due wars, changing trade patterns, political instability and the availability of precious metals used in currencies. (Elliot 2019)

The age of exploration and colonisation brought new wealth to Europe which increased the money supply which led to the rise of prices. In the 17th and early 18th century, central banks started to emerge. The Bank of England was founded in 1694, and it is considered as the first “modern” central bank by many. Other early central banks are Sveriges Riksbank (Sweden) founded in 1668, and Banque de France (France) founded in 1800. The rise of central banks brought more control in the currency management, financial system stabilisation and implementation of monetary stimulus. The industrial revolution also started in the late 18th century in the United Kingdom as it was the leading economy at the time. (Britannica 2024)

The introduction of central banks and the industrial revolution go hand in hand. The financial stability, support, and implementation of policies by central banks enhanced industrialisation. The invention of Spinning Jenny and other mechanisation and the use of steam power in manufacturing and transportation led to great changes in economic and social structures which are still present in modern society. The agrarian economies started to shift to industrialised ones, urbanization led people to migrate to urban areas from rural areas and the technological advancements and their implementation continued. The 19th century continued this trend, and inflationary pressures are present with economic expansion and rapid industrialisation. (Britannica 2024)

The 20th century was full of events that have had impact on the inflation. At the start of the 20th century there was several economic disturbances. The most notable one being the World War 1 which was triggered by the assassination of Archduke Franz Ferdinand. This resulted in war between the Central Powers (Germany, Austria-Hungary, Bulgaria, and the Ottoman Empire) faced

off against the Allied Powers (Great Britain, France, Russia, Italy, Romania, Canada, Japan, and the United States). The war had devastating effects on European nations and their economies, however U.S. economy had 44-month economic boom from recession as European nations purchased American goods for the war. After the war hyperinflation struck several nations. For example, Weimer Republic (Germany) experienced extreme inflation rates which resulted in German Marks value to become worthless. From 1929-1939 the world was struck by The Great Depression. In USA the economy collapsed in 1929, and many banks and businesses closed and at the peak of unemployment over 25% of the workforce was unemployed. Due to the instability in financial and political front, Europe was soon to be due the next big war in World War 2 which resulted in even more economic turmoil. (Medley 2013)

There are several factors contributing to the economic turmoil such as paper currency and deficit financing, which were results of increasing use and printing of paper money by governments. As war required significant number of resources, it led to vigorous expansion of monetary base and money supply. After second world war inflation was affected by elimination of wartime price controls, rising consumer demand and supply shortages. (Hamilton 1977) In 1970s Europe was hit by phenomenon called stagflation. Stagflation refers to economic situation with simultaneous high inflation stagnant economic growth. In 1979 Paul Volcker became the Chairman of the Federal Reserve. Volcker implemented drastic monetary policy measures to combat the high inflation. The measures that Volcker implemented included the significant raise of federal funds rate which is the rate which banks lend to each other. The rate went from 1979s 11% to its peak 20% in 1981. Volcker also enforced the tightening of monetary policy where The Federal Reserve changed its focus from targeting interest rates to the control of the growth of money supply. It especially targeted M1 Money supply which focuses more on the cash and checking deposits. Paul Volcker's practises were called Volcker shock, and this influenced global economy including Europe. (Medley 2013)

At the start of 21st century the global GDP growth rate averaged around 4-5% and inflation rates were generally low and stable. However, a lot of this changed when global financial crisis (GFC) happened. GFC originated from the United States and was caused by several factors with the most prominent ones being the large number of subprime mortgages issued and burst of housing bubble. As housing prices fell and interest rates rose, many of the borrowers defaulted their mortgage which led to the collapse in the value of mortgage-backed securities (MBS). As the MBS's had been sold to investors, the risk had been spread all around the financial sector. Everything led to significant losses to the financial institutions and liquidity crisis as banks became unwilling to lend to each other. (Duignan 2024)

After the GFC, the globe experienced a period of low inflation. Many central banks implemented unconventional monetary policies to combat deflationary pressures and stimulate economic growth. For example, quantitative easing (QE) was used in addition to standard policies such as lowering interest rates and adjusting reserve requirements. This Low Inflation Period lasted for about ten years, from 2009 to 2019. Following this period, the world was hit with pandemic-induced inflation. Supply chain disruptions led to higher prices and shortages of goods. Large scale fiscal stimulus packages were implemented by governments to support economies during these challenging times. The hospitality industry was particularly hard hit by the pandemic, as social gatherings and travel were heavily restricted. (Otrok, Strackman 2024)

In 2022, as the globe started to recover from the COVID-19 pandemic, Russia's invasion of Ukraine occurred. This event significantly impacted Europe. Energy prices fluctuated, sanctions were implemented, and commodities such as wheat and corn from Russia and Ukraine were disrupted. Many countries lost important trade partners, and trade routes had to be redrawn. (World Economic Forum 2024)

## **2.2 Causes of inflation and theory**

As inflation means the increase of price levels due to increase in quantity of money. As the growth of money supply increases faster than the level of productivity in economy from monetary standpoint. Term deflation is used to describe the phenomena of productivity increasing faster than the money supply. This would lead to decrease in prices and cost of living, which from economic standpoint is not desirable outcome. Numerous economists paradoxically interpret that deflation would be harmful for economy as it could lead to decline in consumer spending, increase in debt burden as value of debts remain constant whilst businesses and individuals' income decreases, monetary policy constraints and discouragements to invest as it reduces ROI (Return on investments). A lot of the arguments against deflation derived from English economist and philosopher John Maynard Keynes (1883-1946), concept of paradox of thrift. To put paradox of thrift briefly it means that when individuals increase their saving rates, there is a decrease in consumption expenditures overall. This might consequence to reduce of the economic growth. Due to this belief, many central banks seek for slightly inflationary monetary policy. Their aim is to keep economic growth and prices stable. (Probasco 2024)

Central banks primarily use inflation targeting to keep order of the steady economic growth. The most common inflation target is 2-3% and it is their primary metric for monetary policy. In case of faster rise in prices than expected, central banks will tighten their monetary policy with hawkish policies such as raise of interest rates. Central banks use other tools to manage broader economy

such as open market operations (OMOs), reserve requirements and discount rates. (Probasco 2024)

The common consensus is that  $\approx 2\%$  inflation rate is more beneficial than detrimental for companies. The  $\approx 2\%$  mark is the target inflation for the UK ( $2\% \pm 1$ ), The ECB  $\} 2\%$ , and US Federal Reserve  $\} 2\%$ . Central Banks wish to keep the inflation around 2% as higher inflation can indicate the overheating of the economy and as the prices of goods and services keep rising, it becomes less attractive to invest which might lead to less growth in the long-term. The reason why the target is 2% and not 0% is simple. Inflation of 0% is too close to the deflation which poses different disadvantages. The disadvantages include negative impact on businesses due to lower profit levels and bigger debt burden as the value of money has gone up, but the amount borrowed stays the same. However, there are economists who believe that Central Banks need to allow higher inflation up to 4%. For example, volatile commodities such as oil can spike up the inflation, thus leading Central Banks to be discouraged to cut from interest rates. This inflation is temporary and not from excess of demand in economy. Higher inflation rate also allows more room for manoeuvre. With higher inflation target more expansionary monetary policy would be achievable. Sticking to 2% could lead to trade-off of lower economic growth and elevated unemployment. As a result, higher unemployment leads to rising welfare costs, higher government borrowings and wasted resources. (Pettinger 2020)

The consensus is that  $\approx 2\%$  inflation rate is desired. However not all economists agree with this. Economists such as Oliver Blanchard and Kenneth Rogoff have mentioned that higher inflation rate could be viable. After 2008 financial crisis Olivier Blanchard suggested that a 4% inflation target could be ideal. The 4% inflation rate would provide central banks with greater flexibility to adjust monetary policy during economic downturns, particularly when interest rates are constrained by the zero lower bound. (Blanchard, Dell'Ariccia and Mauro 2010,11) Kenneth Rogoff, who is former Chief Economist of the International Monetary Fund, has been bit more cautious about adopting a permanent 4% inflation target. Rogoff sees it more as a tool and not as a permanent solution to manage economic shocks and the zero lower bound constraints on interest rates. He discussed this idea in his paper "Costs and Benefits to Phasing Out Paper Currency" in 2014. (Rogoff, 2014, 3)

There are several economic theories regarding inflation and its causes/behaviour. The root of inflation is driven by too great of a demand in relation to its supply. The former United States Chair of Federal Reserve Ben Bernanke and Andrew Abel wrote in their macroeconomics textbook: "Inflation occurs when the aggregate quantity of goods demanded at any particular price level is rising more quickly than the aggregate quantity of goods supplied at that price level." Inflation is usually

the result of many factors; however, supply shocks are often involved. Supply shocks are a result of major disruption in a crucial economic input, such as energy or fuel. If war or any other event stops the production of oil in a certain region, it will have a significant impact on the price of oil. This will lead to rise of the prices of other goods as well as energy is an important input into their supply. This phenomenon is usually referred to as “cost-push inflation.” The changes in money supply also influence inflation. Increase in money supply will build up the prices, especially when there are disturbances to supply of goods. More money to spend and less products to buy leads to the rise of prices. In a nutshell it is too much money chasing too few goods and it is referred to demand-pull inflation. (Frick, 2023)

There are different theories to assess the macroeconomic relationships concerning inflation with some notable ones being The Quantity Theory of Money, Fisher’s Equation, and the Phillips Curve. The Quantity Theory of Money focuses more on the relationship between price changes and the supply of money in an economy. This means that the prevalent price level of goods and services is directly proportional to the quantity of money in circulation. The Quantity Theory of Money is often expressed with equation of exchange:  $MV=PT$ . (Vipond 2023)

There has also been some criticism towards The Quantity Theory of Money. It has been labelled as simple truism as the total amount of money expenditures of buyers is equivalent to the full amount of money receipts for sellers. It does not state any additional information about the prices nor money. It just states simple form that is true, but it does not state the cause. There are also certain assumptions made, such as of full employment of resources and constant spending habits. It is assumed that  $V$ ,  $V'$ ,  $V''$  and  $T$  remain constant. In practice, change in  $M$  is destined to influence  $V$ ,  $M'$ ,  $V'$  and  $T$ . Evidence suggests that, rather than staying constant, the velocity of money tends to fluctuate in direct relation to the level of production ( $T$ ). (Marcuzzo 2017)

In the Keynesian criticism, especially the  $V$  is highly sensitive to interest rates in the short run, which in turn are functionally linked to switch in in the money supply. Keynes stated on the longer-term inflation: “So far, we have been primarily concerned with the way in which changes in the quantity of money affect prices in the short period. But in the long run is there not some simpler relationship? This is a question for historical generalisation rather than for pure theory...” [The General Theory of Employment, Interest, and Money (1936), p. 306.]

**M:** Money supply

**V:** Velocity of circulation (the average frequency with which unit of money is spent)

**P**: Average price level

**T**: Number of transactions involving money payments (real Gross Domestic Product)

**M'**: Bank Money Supply

**V'**: Velocity of Bank Money

Fisher's equation and The Quantity Theory of Money are both fundamental concepts in the field of monetary theory. As The QTM focuses more on the relationship of price changes and supply of money, Fisher's Equation on other hand links nominal interest rater, real interest rates, and expected inflation. The Fisher's Equations formula is:

$$(1+i)=(1+r)\times(1+\pi)$$

- **i= Nominal Interest Rate**
- **r=Real Interest Rate**
- **$\pi$ =Inflation Rate**

Fisher's Equation is often used on calculating the ROI or in the prediction of nominal and real interest rates behaviour. For example, if investor wants to determine the real interest rate earned on an investment after accounting for the effects of inflation. (CFI Team 2023)

While Fisher's equation is crucial part of understanding the correlation between nominal interest rates, real interest rates and inflation, it has faced some criticism. One of the major criticism it has faced is the assumption interest rate (i), real interest rate (r) and inflation rate ( $\pi$ ) remain constant. It has been deemed to be unrealistic due to economic turmoil and oversimplified as it does not capture the complexities of the impact on nominal interest rates and how expectations on inflations are formed. (Graham 1988, 961-968)

The last economic theory that I am going to discuss in this chapter is the Phillips Curve which was invented by New Zealand born economist Bill Phillips. It was published in the quarterly journal of *Economica*: "The Relation between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861–1957" in 1958. The Phillips Curve is a graphical representation of the short-term interrelation between inflation and unemployment within the economy. According to the Phillips Curve, relationship between unemployment rate and the inflation rate is negative/inverse. (Phillips 1958)

The Phillips curve illustrates the inverse relationship between unemployment and inflation and in short run it proposes that lower unemployment comes with high inflation and vice versa. This

phenomenon does not hold its validity in long run. The economy tends to return to its natural rate of unemployment despite the volume of inflation. In the 1970s stagflations characteristics went against Phillips curves model which led to questions regarding its validity. However, it is still considered as valuable tool for central banks to gain deeper understanding on inflation and the forecasting of it despite its limitations. (Engemann 2020)

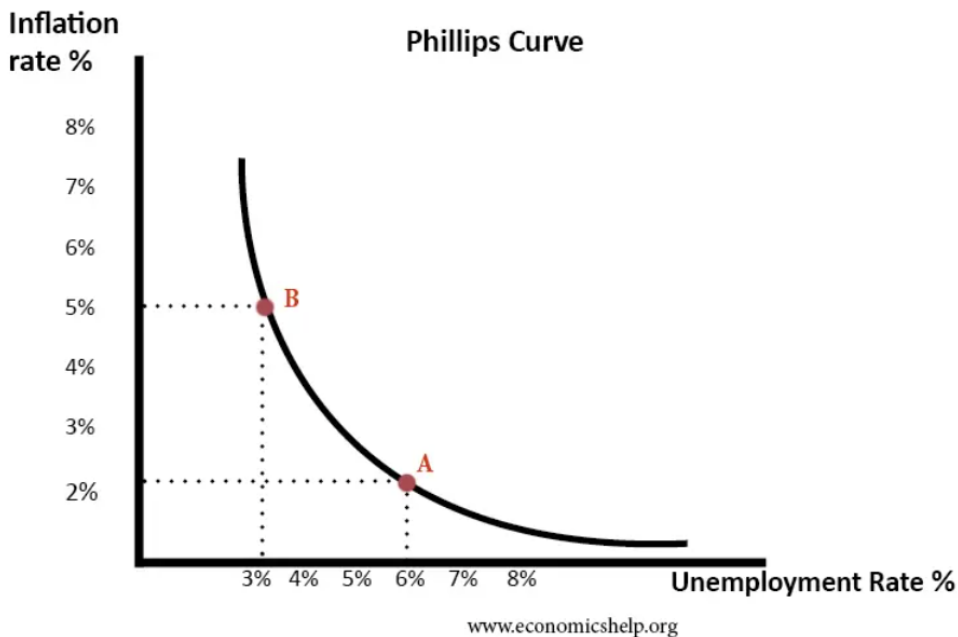


Figure 2: The Phillips Curve (Adapted online, Phillips, B .1958)

### 2.3 Impact of inflation on businesses

Inflation has had a major impact in most of the industries and the restaurant industry is no different. Both costs and consumer behaviour are directly linked to it. Cost of Goods Sold increases as ingredients, raw materials, and any other expenses linked to production of items from the menu. According to Tilastokeskus February 2023 wholesale prices were 22% higher than the year prior. (Sandqvist 2023)

Businesses across Finland have been affected by inflation. The price of raw materials and energy have taken a toll on the operations of businesses and increased their costs. The pricing strategies and cost structures had to be adjusted to fit the environment, thereby affecting the profitability. In 2023 over 2700 companies declared bankruptcy, which was a record number since the 2009 financial crisis. This trend continued in 2024 as over 2700 companies were already bankrupt by early November. The largest share of bankruptcies was in the industry of construction, which accounted for the largest share of 707 followed by wholesale and retail with 523 and hospitality with 334. The

rising costs and economic pressures have forced businesses to adapt quickly, often leading to difficult decisions and restructuring efforts. (Helsinki Times 2024)

The rising costs and decreasing profit margins have had an immense impact on the cost control and profitability, especially for the restaurants. Restaurants have already operated on tight profit margins and minimum wage increases and the rising cost of living have led to even more problems on the staffing department. As the labour costs and staffing challenges have been prevalent it is clear to see how the discomfort of the restaurateurs has affected the industry as whole. Labour costs have risen significantly and especially the smaller chains have had hard time to compete with larger departments, further decreasing the labour pool. Especially the high skilled employees are hard to find and maintain, and the turnover rates are high. Due the understaffing the quality of service has often suffered and having less of their budget left for expenses such as equipment and food. In many cases, these have led to problems with customer experience and overall efficiency for restaurants. The importance of innovative solutions has risen and solutions such as flexible scheduling has gained popularity. Other notable solutions are better employee benefits and improved wages. (White 2023)

The impact of inflation has influenced the purchasing power of the restaurants, mainly due the rising prices of ingredients and supplies. This has had an impact on the quality of food, portion sizes and influenced the increase in menu prices. These factors combined with the changes in customers purchasing power have made it extremely hard to remain competitive in restaurant industry. According to a survey conducted by the Consumers' Union of Finland, approximately 25% of respondents have been financially squeezed for years. The purchasing power of consumers has declined due to inflation ever since the price rate peaked in 2021. The average Finnish earner has lost the equivalent of two months' salary since the peak, which amounts to approximately 7,000 euros. (Yle News 2025)

The consumer demand refers to the willingness of consumers to make purchases. The other side of demand are the companies with ability to supply them. The ability to have proactive approach to customer behaviour is valuable. With higher inflation customer preferences shift more towards budget friendly options and value meals. However, impact on different segments vary. For example, high-income and low-income customers have different prisonisations. Customers with higher income tend to be less affected by inflationary pressure than their lower-income counterparts. With the right strategical choice's restaurants are able assess price sensitivity, value perception, restaurant type and promotional impact. (Chua, Karim, Lee & Han 2020)

The implementation of monetary policies aims to control economic growth and ensure stability. This affects the restaurant industry both directly and indirectly by shaping the economic environment. Restaurants often benefit from policies which are implemented to stimulate economic growth. For example, lowering interest rates and increase in the money supply can make loans more affordable. Boost on consumers disposable income often leads to increasing spending. This would enable restaurants to invest in growth and lead to increase in cash flow. On the other hand, policies aimed at controlling inflation usually have adverse effects. By raising interest rates and/or decreasing the money supply both restaurateurs and consumers behaviour is affected. If the borrowing cost are higher restaurants are more likely to avoid expanding or renovating due costly loans. Decreased money supply leads reduced access to credit as banks are less willing to lend. Monetary policies also indirectly affect restaurants' costs. Food prices and especially the imported goods, fluctuate due to inflation and currency exchange rate changes. (Sherman 2021)

### 3 Pricing and cost structure in restaurant industry

Pricing and cost structure are fundamental part of businesses profitability. There are several pricing strategies for different types of restaurants and target audiences. For example, high-end restaurant uses completely different pricing strategies compared to fast food chains. Different target audiences expect different things regarding food quality, service and setting. Cost structure is about the characterization of various types of expenses that a business incurs. (Schmidt 2024)

#### 3.1 Pricing Strategies

Pricing strategies play a crucial role in the success and sustainability aspects of restaurants. The culinary landscape evolves all the time, and the competition is fierce. The correct pricing of the products is extremely important from restaurants and customers perspective. The pricing strategies are not only about the face value of the dish, but also about the competition pricing, perceived value, and customer demand. (RPS 2024)

I will go through three of the most common pricing methods. The first one being the Cost-Based pricing with  $\approx 60\%$  out of the restaurants using it, second being value-based with  $\approx 40\%$  usage and third being value based  $\approx 35\%$  usage. (Demetriou 2022)

The type of cost-based pricing which is often used by restaurants is Cost-plus pricing. In cost-plus pricing COGS is used as the primary basis for the pricing of goods. Restaurants use a fixed percentage that represents the expected return of producing and selling a product. The formula for cost-plus pricing is:

$$P=(\text{Cost per unit})+(\text{Expected \% of return})$$

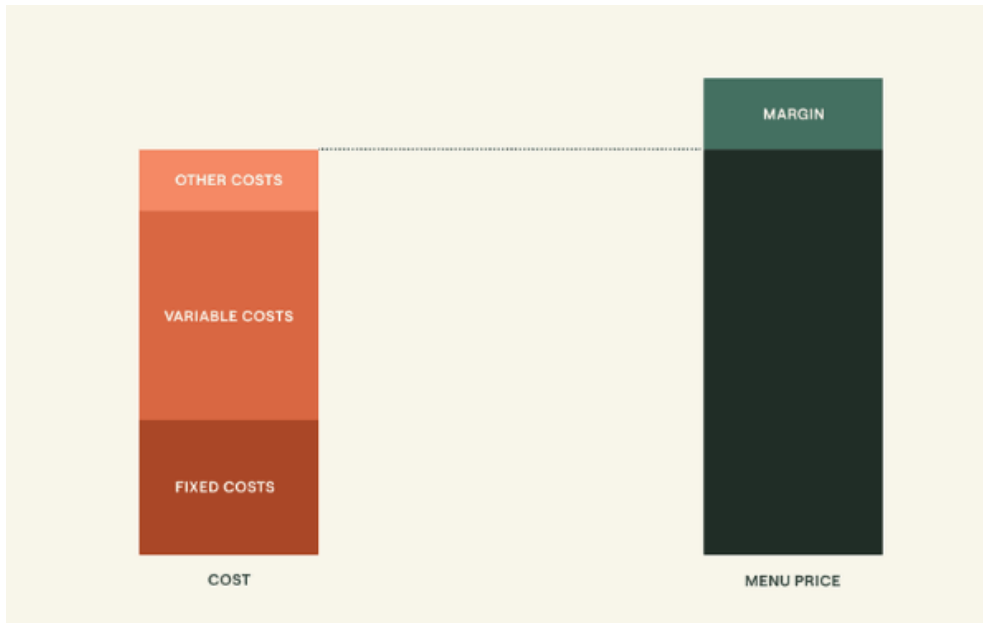


Figure 3. Visual interpretation of Cost-Based pricing, (adapted online, Pollak 2024)

Second strategy that I will discuss is Value-Based pricing. The value-based strategy does not rely on the calculation of costs and markup. This method of pricing focuses on the perceived value it provides to the customers, thus meaning that the price of the product is based on what customer is willing to pay for. The factors that need to be considered whilst setting value-based pricing are uniqueness, quality, convenience, and overall experience. The implementation of it also requires structured and deliberate approach, such as understanding of the market via market research and value assessment. (Delucci 2024)

Third strategy that I'll mention is Competition-Based Pricing. Competition-based pricing is like value-based pricing as both strategies are considering external market factors when setting prices. The key difference between the two is the perspective. In competition-based approach the prices are determined by the price which competitors have set. It requires the analysis of competitors, benchmarking of similar products prices, assessment of businesses positioning and constant monitoring. As seen from the key elements of competition-based pricing, the focus is more on the external market conditions, while value-based pricing is focused on internal value creation for customers. (Demetriou 2022)

Pricing strategies are ever-present on revenue management as pricing is key element of it. It involves reevaluating pricing strategy and developing disciplined tactics. Most of restaurants have constructed pricing strategy which is combination of different strategies to suit their needs and the aim being to maximise the capture of the value by implementing correct prices. When pricing strategy dictates the direction, pricing tactics take place. Tactics aim to create reforming pricing tools

that can react to changes in in the business environment. One of the key pricing tactics is the menu matrix. It offers guidance to the optimization of the menu offerings regarding balance pricing, profitability, and customer satisfaction. With categorization the menu items are divided into different categories via their characteristics such as popularity, profit margins and costs. It also considers placement, visual hierarchy, pairing and bundling, psychological pricing and seasonal adjustments. From customers perspective 9.99e is significantly more appealing than 10e and more profitable items are placed more prominently to attract as much attention as possible. (Pollak 2024)

Identifying suitable pricing strategies for the restaurant is not easy as there are several things to consider whilst making the decisions. It is important to identify revenue-enhancing opportunities for restaurant. In the case study implementing revenue management by J. Ho and S.E. Kimes, five-step revenue management process is used to identify what to do and why. The five steps include:

1. Setting up a standard for performances.

In the first step the assessment of current state of performance is required. It includes the gathering of data from various parts of revenue generating process. For example, customers acquisitions, data on sales, conversion rates and other metrics which provide valuable insight into the revenue generation process are used. The main objective of this step is to provide broad and clear understanding of the starting point.

2. Understanding the causes of performance.

When the standard for performance is created, it is important to recognize factors which are contributing to current form of revenue generation. The analysing of customer behaviour, market trends, customer behaviour, competitive landscape, internal operations, and other phenomenon affecting the revenue generation. The areas of improvement and opportunities are easier to uncover with a solid understanding of the causes.

3. Designing a strategy to maximize revenue.

The factors of performance are analysed to find the right approach to the current state. Examples of approaches are optimising pricing strategies, finding new customer segments, testing out new markets and improving market campaigns and boosting product offers. These approaches are evaluated to find solutions to the found causes with a potential to revenue growth.

4. Execution of strategies.

After the revenue-improving strategies are developed, they need to be implemented. In this step implementation of plans, resource management and the efficiency of putting new strategies into

practise is the key. Sales procedures, marketing campaigns and other divisions are modified to achieve the maximum success for the improvements.

#### 5. Evaluating of outcome.

The last step includes the checking and monitoring the key-metrics to see if the strategies have had the favoured outcome. Key Performance Indicators (KPIs) are tracked for deeper understanding of the effectiveness of the strategies implemented. Some KPIs to see the progress are, client retention rate, value of average transaction, growth of sales and profit margins. Tracking these KPIs will provide valuable information regarding if and where modifications are required.

The strategies used were categorised into three different categories: hot, cold, and all-purpose strategies. The strategies were determined by how busy the restaurant is. (Kimes & Ho 2019)

### Appropriate RRM tools

Tool	'Hot'	'Cold'
Menu Engineering	Yes	Yes
Menu Design	Yes	Yes
Server mentoring/ upselling	Yes	Yes
Table mix	Yes	No
Reservation management	Better manage	Maximize distribution channels
Promotions	Restrict	Yes
Suggestive selling	Only if doesn't extend duration	Yes
Pricing	Premium	Selected discounts

Table 2. Simple categorisation of Restaurant Revenue Management tools to hot and cold. (Kimes & Ho 2019, 9)

The Fairmont restaurants that implemented revenue management techniques generated five times more revenue growth within a Fiscal Year compared to the ones that did not implement the revenue management practises.

Hot and cold pricing strategies both have their ups and downs. Hot pricing strategies are linked to more aggressive market penetration and high flexibility. Cold pricing strategies are typically associated with a more stable approach, offering predictability. In Finland, fixed menu prices are standard in terms of menu engineering and approach. Additionally, all-purpose strategies can be introduced to adapt to market demands. They will offer flexibility and stability.

Table 3. Categorisation of Hot and Cold Pricing (adapted from article Types of Pricing Strategies TheStrategyStory 2024)

	Hot Pricing	Cold Pricing
Pricing Flexibility	Highly adaptable, continuous modifications	Consistent, occasional modifications
Revenue Maximization	Opportunity for increased revenue with dynamic pricing	Revenue is more stable but might not capture peak demand
Customer Experience	May be viewed as unfair without transparency	Reliable and consistent, enhancing customer trust
Operational Complexity	Does require advanced technology and monitoring	Less resources required and simpler manage
Required Technology	Requires advanced POS systems and dynamic pricing tools	Basic technology, dependent on regular price adjustments
Customer Perception	Fluctuating prices might cause dissatisfaction	Consistent and general accepted
Suitability for Market	For High-demand, competitive or fluctuating markets	For Steady markets

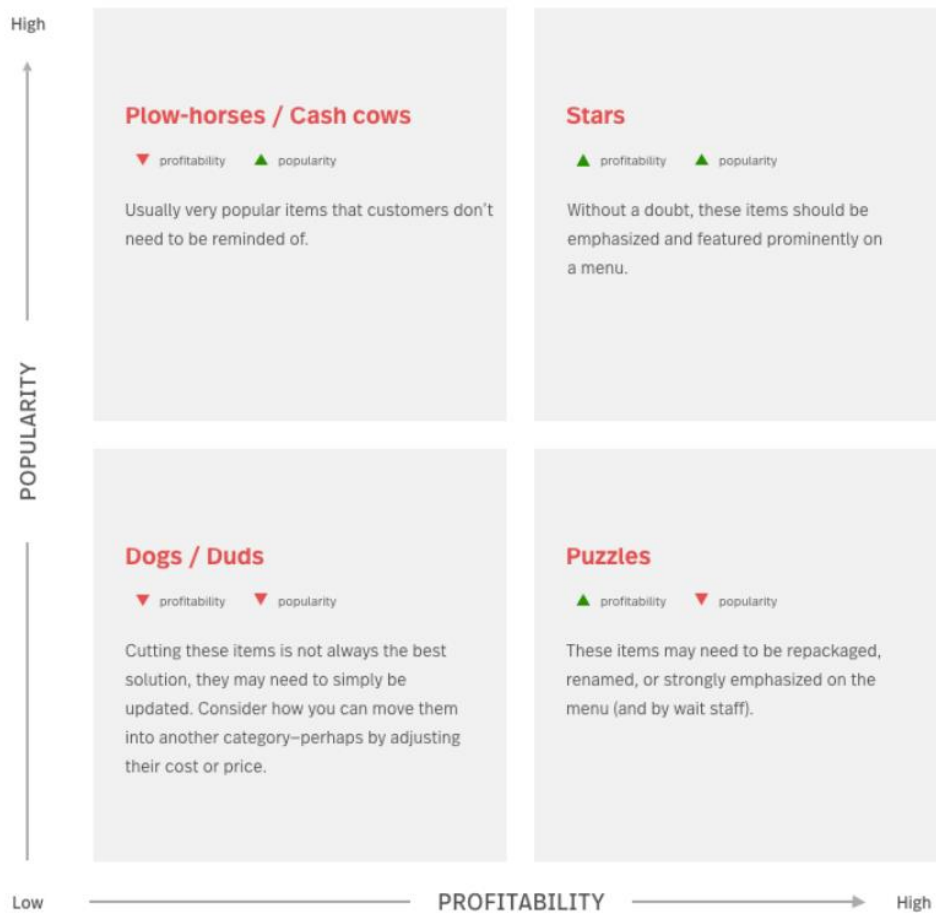


Figure 4. Example of Categorisation of restaurants dishes via Menu Engineering (adapted online, M.L Kasavana, D.I. Smith 1982)

### 3.2 Cost Structure

The key elements include the cost categories, different types of costs and couple key financial performance metrics. These subjects are significant for the financial wellbeing of restaurants and future planning. When the cost structure is clear it is easier to choose pricing strategies most suitable for the restaurants. Restaurant expenses and restaurant cost are often used interchangeably, but they are two different terms. A restaurant cost is one time expenditure, and a restaurant expense is recurring payment that creates revenue. However, for sake of clarity I won't focus too much on the difference and their use. (Darlington 2019)

The first metric that is discussed is break-even point. The break-even point indicates the level of sales at which the total revenue is equal to the total costs. This metric important for businesses as

it indicates the point where they start to make profit instead of loss. The formula for break-even point for restaurants is as follows: 
$$= \frac{\text{Fixed Costs}}{\text{Average Selling price per Meal} - \text{Variable cost Per meal}}$$
. Fixed and variable costs will be discussed in the following chapter. (Gallo 2014)

Two key types of costs are variable and fixed costs. Variable costs are expenses that change in direct proportion to the level of production or other business-related activity. The expenses fluctuate due to the volume of sales, use of ingredients and other usage-dependent expenses. For example, Cost of Goods Sold (COGS), utilities and facility management are often considered as variable costs. The fixed cost on other hand remains constant regardless of the volume of business activities. They are essential for maintenance of restaurants operations due to their predictable nature. It offers stability to the financial planning as they can be budgeted without a worry about sudden changes, and they offer key data to determine break-even analysis. Some examples of fixed costs for restaurants are rent/lease payments, fixed salaries of permanent staff who receive consistent pay regardless of business fluctuations, depreciation, and license fees. (Darlington 2019)

It is typical for restaurant to have high overhead costs and potential for waste. The largest expense categories are food, beverage, and labour. Food and beverage expenses are categorised as cost of sales and all other expenses are listed as operating expenses. Operation expenses can be divided into further subsidiaries. Labour costs is one of the two main expenses of any restaurants, and it includes wages, salaries, benefits, unemployment taxes and service commissions. Also uniforms and other equipment provided by restaurant are included. Many restaurants consider labour costs as variable costs as the shift- and parttime-workers hours vary by the business volumes. Second largest expense is COGS. COGS includes food and beverage costs and food preparation equipment. Kitchen equipment is not categorized as COGS in income statement as stoves, pans etc. are depreciated over time. Restaurants have often set themselves a goal percentage for their food costs, such as 33% of their sales. Other key categories for restaurants are marketing and advertising expenses, real estate occupancy expenses and maintenance, and daily administrative costs. (Redman 2019)

It is important for the restaurants to stay in control of their costs, and this requires cost management. Cost management involves various strategies to maintain profitability and sustainability. With cost control restaurant will be able to analyse their financial performance with achievable and realistic financial benchmarks. Good examples of vital benchmarks for restaurants are Prime Cost, Food/Labour Cost percentage and Profit margin. According to O'Neill understanding and monitoring Prime Cost regularly gives restaurants precise and accurate picture of profitability. Simply: "prime cost equals the sum of a restaurant's costs to sell its food, drinks, and products — its Cost of Goods Sold (COGS) – plus the various labour costs of its salaried and casual staff." (Luke

O'Neill 2020) For Prime Cost to have comparability for industry averages, it needs to be calculated as a percentage for a period such as a week or a month. Average prime cost percentage should be around 55% to 60% but if restaurant is a part of hotel or a sports club the number might go up to 65%. This is a result of them being loss leaders for core part of business as hotel has guests staying overnight and sports club has annual membership fees. (O'Neill 2020)

Save

## Prime Cost Formula

📷

**Cost of goods sold (CoGS) + Total labor costs**

## Prime Cost Formula (%)

$$\frac{\text{Prime cost}}{\text{Total sales}}$$

Figure 5 & 6, Prime Cost Formula and Prime Cost Formula Percentage, Adapted Online (O'Neill 2020)

The key metric for all businesses, including restaurants, is profit margin. Profit margin indicates how much profit a business makes relative to its revenue. It is usually expressed as a percentage to help understand the efficiency of converting sales into profit. There are different types of profit margins:

$$\text{Gross Profit Margin: } \frac{\text{Total Revenue} - \text{COGS}}{\text{Total revenue}} \times 100$$

$$\text{Operating Profit Margin: } \frac{\text{Total Revenue} - \text{COGS} - \text{Operating Expenses}}{\text{Total revenue}} \times 100$$

$$\text{Net Profit Margin: } \frac{\text{Total Revenue} - \text{COGS} - \text{Operating Expenses} - \text{Taxes}}{\text{Total revenue}} \times 100$$

These metrics reveal the core profitability of business. Gross Profit Margin gives the core production efficiency, Operating Profit margin includes operating expenses and Net Profit Margin counts all expenses, which provides the most complete picture of profitability of restaurant. (Davis 2024)

One of the key metrics related to food costs and ingredients is food cost margin. It indicates the percentage of revenue that the business spends on the cost of food ingredients. With low food cost margin, the business is effectively controlling its expenses while maintaining quality. On the other hand, if the margin is high, there might be pricing, waste or efficiency issues. The importance of menu engineering, reducing food waste and experimenting with lower-cost suppliers are all directly related to food cost. As mentioned before, menu engineering helps to identify high-margin items and underperforming dishes. This helps to make precise decisions about pricing, placement and promotion. The reduction of food waste is not only good for the planet, but it is also a good way lower costs. Portion control, inventory management systems and repurposing of leftovers offer more bang for the buck regarding cost control as the cost of ingredients used per dish decreases. Lastly, lower-cost food suppliers can greatly affect the cost of ingredients. Researching and negotiating with suppliers to ensure the best price without compromising quality will directly improve the food cost margin. (DeForest 2025)

Typically, businesses aim to keep food cost margin is between 25% and 35%. During inflationary pressures, restaurants might experience eroded margins due to rising ingredient costs.

$$1. \text{ Food Cost Percentage: } \left( \frac{\text{Cost of Ingredients}}{\text{Selling Price}} \right) \times 100$$

$$2. \text{ Food Cost Margin: } \left( \frac{\text{Selling Price} - \text{Cost of Ingredients}}{\text{Selling Price}} \right) \times 100$$

Labor cost and percentage are two very essential business metrics to track for a restaurant. Labor is one of the main expenses and it requires daily, weekly and quarterly tracking and reporting. The common misconception is that it only consists of wages. It includes several other components:

1. **Salaries & Hourly Wages-The primary cost for labor.**
2. **Overtime Pay-Additional pay for overtime hours at higher rate.**
3. **Payroll & Payroll Tax-Paid by both employer and employees.**
4. **Vacation & Sick Days-Compensation for vacations, sick days and other paid time of.**
5. **Healthcare-vision, dental or any other benefits provided to employees.**

The cost of labour formula is:

**Total Direct Labor Cost + Total Indirect Labor Cost=Cost of Labor**

The labour cost percentage formula is:

## **Cost of Labor / Total Sales \* 100= Labor Cost Percentage**

There are several factors that impact the labour costs. Location, staff size and efficiency all affect the costs. The type of restaurant concept requires different skillsets, and this will influence the labour cost percentage. For example, quick serve and casual restaurants have lower labour costs as the employees often work across multiple areas whilst more upscale restaurants require more specialized skillsets and require more training. This leads to higher labour costs. (Lozier 2024)

Pricing and cost structure are important to ensure the restaurant's profitability and sustainability. The choice of pricing strategies is affected by many factors. Fast food restaurants and fine-dining establishments are competing for different target audiences thus the choice of pricing strategies vary. Pricing doesn't only reflect the cost of production, but also value for customers, market demand and competition. Three main pricing strategies were:

- 1. Cost-Based Pricing**
- 2. Value-Based Pricing**
- 3. Competition-Based Pricing**

Pricing often involves tactical tools, such as menu engineering that optimizes menu offerings, psychological pricing and menu layout. All these play part in customers willingness to purchase the product. Revenue management is key factor in maximizing the income by aligning the pricing strategies with business conditions. With the five step-process restaurants can achieve substantial growth in revenue, especially when hot, cold and all-purpose strategies are implemented based on demand levels.

On the cost structure side, the understanding of restaurants financial situation is important. Expenses are crucial for choosing pricing methods and to ensure profitability. The two main cost types are:

- 1. Fixed Costs= Consistent expenses like salaries and rent.**
- 2. Variable Costs= Costs that vary by volumes like ingredients and utilities.**

The most prevalent categories are labour and COGS, followed by maintenance, marketing and administrative costs. There are metrics such as break-even point, prime cost and multiple profit margins which give guidance for the assessment of financial health of the restaurant. Other performance indicators to consider are food and labour cost percentages. In conclusion, restaurants must align with cost structures to remain profitable, competitive and responsive to market fluctuations.

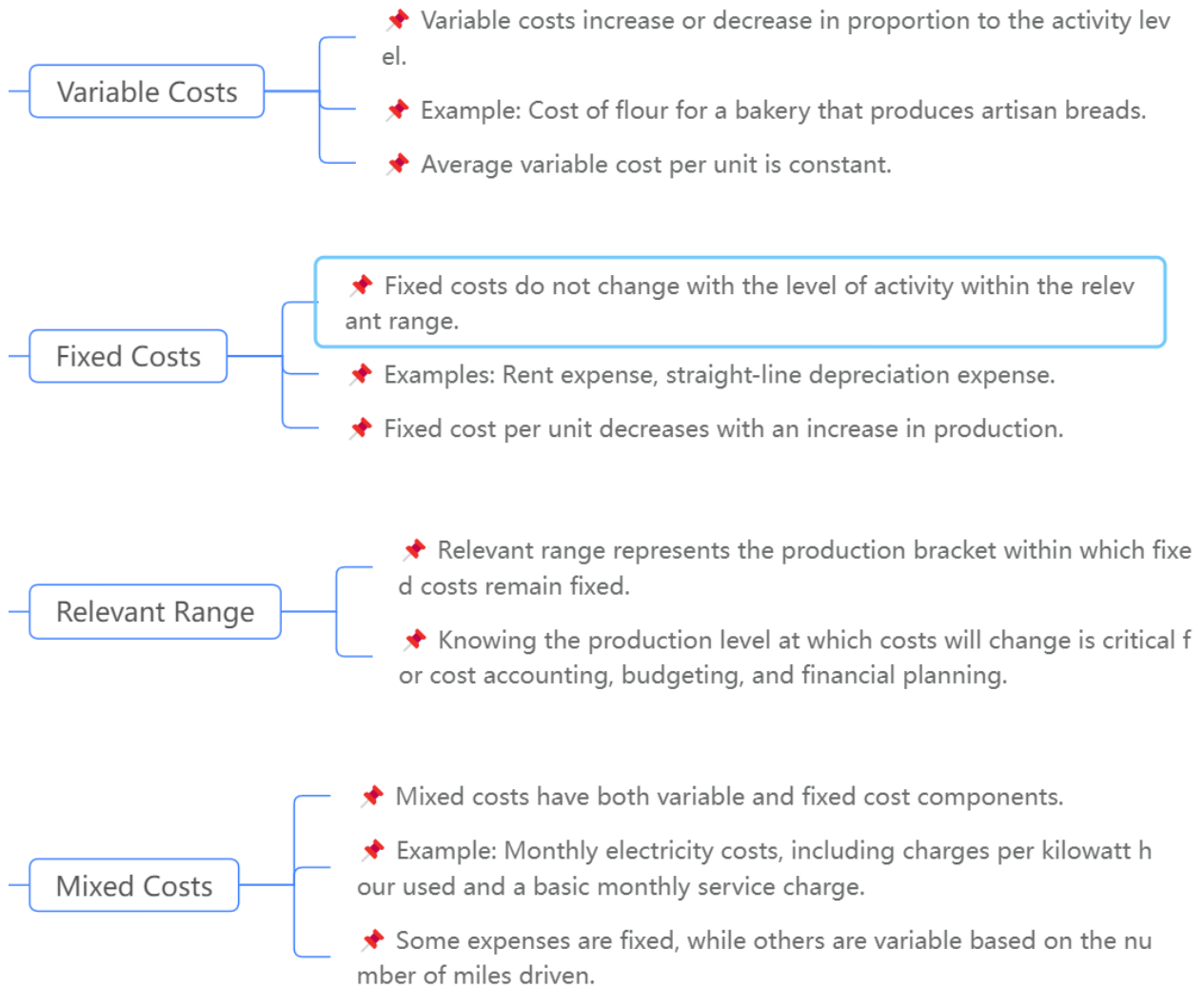


Table 4. Generated from: Cost Behavior: Analysis and Use, (Zweeni & Al Musawi 2019)

## 4 Methodology

This chapter outlines the methodology used for this thesis and how I am validating these choices. I conduct interviews with individuals from the restaurant industry and combining the findings with the literature research. I will conduct qualitative research via interviews which are done in a structured manner. The interviewees are holding various managerial positions, providing valuable insights into the impact of inflation, pricing strategies, and cost management strategies for restaurants.

### 4.1 Research Approach

The research problem of this thesis is how can SMEs from the restaurant industry cope with inflationary pressure and what strategies are vital for survival from this. I came to conclusion to choose the qualitative approach for this thesis as it was the most suitable to gain in-depth understanding of the nuanced ways inflation impacts SMEs. Quantitative data may miss the individual experiences and important decision-making processes which I aim to find. Due to the numerical nature quantitative data does not answer the questions of how and why behind the strategies and their usage. Qualitative research gives me the ability to have a more discovery-oriented approach whilst having flexibility in exploring the participants' insights. The information might uncover themes and characteristics that are not anticipated initially. (Streefkerk 2023)

My goal was to get a deeper understanding of the situation via phenomenology. Phenomenology is a qualitative approach which aims to explore the interviewees' experiences and feelings attached to those and how humans construct the connection of meaning to the social reality which they live inside. In phenomenology, humans are seen as the influencers of the social world and as the ones being influenced by it. When interacting with others, humans produce the meaning associated with events and objects. I am not only looking for the strategies that are used but also why they are used. This approach enables me to explore the subjective realities of restaurant owners to grasp the insights and concepts of their real-life challenges. (Huhtinen, Tuominen, 2020 chapter 19)

With qualitative approach the research works closely with the concepts and information from literature and desktop research. However, theory is not seen as the primary source of data but as an aid to explore and analyse the information received from the interviews. (Streefkerk 2023)

The interviews gave me detailed insights into the experiences and perspectives of the professionals from the field. My interview questions were divided into four categories "Background and experience", "Impact of Inflation", "Pricing Strategies" and "Cost Management Strategies" with these questions found on the appendix of this thesis. The ethicality of conducting data was taken into consideration. All participants were provided with detailed information about study and its purpose.

The purpose of their role was informed, and confidentiality and anonymity were guaranteed. All personal data was anonymized and is stored securely, with a sole purpose to be used for this research.

## 4.2 Data Collection Methods

To collect data for this thesis, I conducted semi-structured interviews. Semi-structured interviews are done systematically, with predetermined questions asked in specific order. With open-ended questions the participants were able to express their insights and perspectives freely whilst maintaining a framework which ensures that important topics are discussed. This method will provide consistent data which reduces the interviewer bias and provides uniformity to responses. With similar questions the identification of patterns and trends becomes more straightforward. This will help me to identify key information about the impact of inflation, pricing strategies and cost management strategies. However, as the interpretation of the questions is open-ended, allowing the interviewee the freedom to dive deeper into subjects they feel are relevant (George 2022)

The semi-structured interview is also known as thematic interview. As mentioned above, the main purpose of thematic interviews is how interviewee interprets the question and how they construct the meanings and answers. The degree of uniformity was aimed at being as uniform as possible, however during the interviews phrasing and order of questions was adapted to fit the interview dynamics. (Tuomi & Sarajärvi 2009, 72-74)

My sampling size consisted of six participants. My aim was to select participants with a role that has key decision-making regarding the operations on their organizations. These participants were chosen for their expertise and responsibility regarding financial planning, strategic planning and their understanding of the impact of inflation on their business. More specifically, they were owners or high-ranking individuals within their companies. Participants were recruited via two sampling methods: purposive sampling and snowball sampling. Four participants were selected through purposive sampling having met the criteria and two were identified via snowball sampling as they were recommended by initial contacts. Due to the overlapping of schedules, two of the interviews were conducted via text and four interviews were conducted on Microsoft Teams. Interviews conducted with Microsoft Teams were recorded with the consent of the interviewee. (Tuomi & Sarajärvi 2009, 85-87)

### 4.3 Data Analysis Methods

For data analysis, content analysis and theme analysis were used to analyse data collected from interviews. The combined approach gives a comprehensive insight as content analysis gives me patterns and frequencies and whilst theme analysis gives me a deeper meaning and contexts. I identified different topics from my sets of questions, Impact of Inflation, Pricing Strategies and Cost Management strategies. I categorized data into smaller units where specific responses to specific topics were bracketed. I used color-coding for the sake of clarity whilst segmenting. By counting the frequency of terms and topics I was able to build a comprehensive understanding of the key themes which occurred often.

I chose thematic analysis as a tool to organize and interpret data gained from the interviews. With a systematic process that allows me to identify different characteristics from the interviews, the thematic analysis works hand in hand with phenomenological approach as framework. I report patterns and distil core themes and commonalities from the interviewee's experiences. (Hecker, Kalpokas 2024)

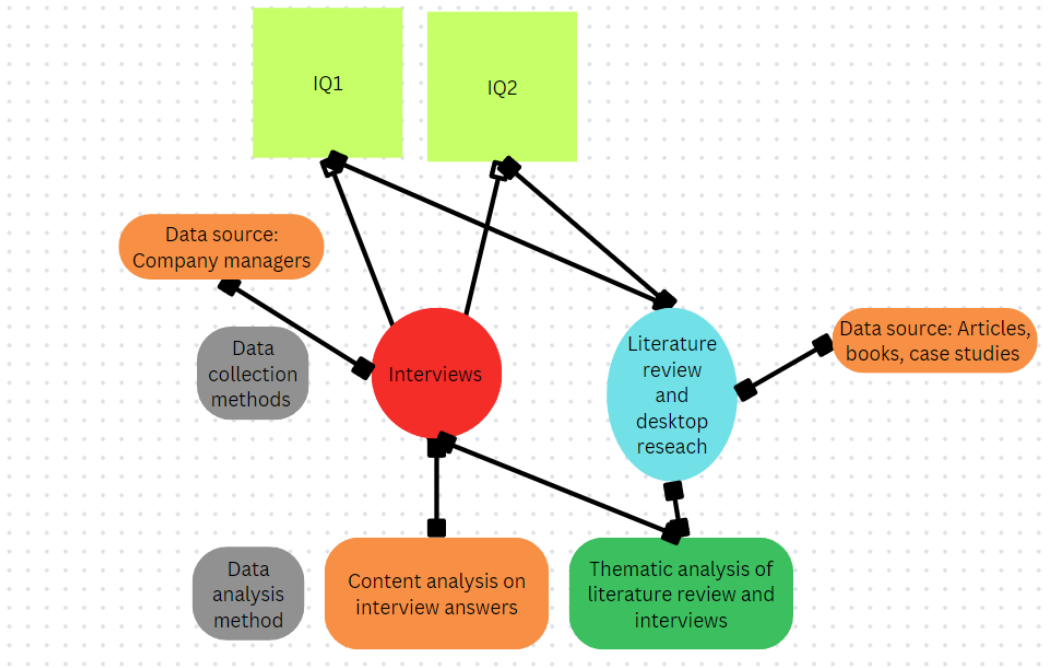
I am also using content analysis to understand the deeper meaning of the collected data. With content analysis I can uncover themes, patterns and meanings which might not be immediately apparent. The combination of content and thematic analysis provides me with a view that ensures that both the explicit and implicit characteristics are captured from the interviewees' experiences. (Super 2024)

### 4.4 Research Process and Schedule

My research journey for this thesis started in January 2024. First, I had an exploratory phase to assess the suitability of chosen topic; after identifying the research and investigative questions I progressed into literature review and desktop research, which can be seen in the figure 7. of research process illustration. The foundation of literature review and desktop research was conducted from February to June, after which paused for summer break.

The work continued in September with the focus on theoretical framework and transitioning to the methodological design phase in October. The data collection via semi-structured interviews was conducted between 19<sup>th</sup> of October and 22<sup>nd</sup> of December, with a focus on individuals from managerial positions. As seen from the figure 7. Data analysis methods of content and thematic analysis were used in January 2025 to obtain key findings. These findings were further examined and discussed from February to the start of May 2025, culminating in the finalisation of the thesis.

Figure 7. Illustration of thesis research process.



## 5 Results

This chapter discusses the results gathered from the interviews. The structure of the interview was divided into four parts: Experience and Background, Impact of Inflation, Pricing Strategies and Cost Management Strategies. Through content and thematic analysis, I gathered occurring themes and keywords and delved deeper into their meaning.

Table 5. representing Interviewees and their background on the industry

	Position	Experience	Type of Restaurant	Method of conducting & Date
1.	CEO & Entrepreneur	6+ years as restaurant entrepreneur	Seasonal Café & Bistro	Written, 19.10
2.	Restaurant Operations Manager	25+ years in the industry	Multiple Restaurants & Gastropub	Written, 24.10
3.	Chairman Of a Group, Co-owner	40+ years in the industry	Multiple Restaurants, Gastropubs, Catering	Teams, 4.11
4.	Owner	20+ years in the industry	Scandinavian Restaurant	Teams, 8.12
5.	Entrepreneur CEO	40+ years in the industry	Lunch and Cafeteria	Teams, 10.12
6.	CEO	15 years in the industry	Fast Casual restaurant Chain	Teams, 20.12

### 5.1 Impact of Inflation

The impact of inflation has had a massive impact on the restaurant operations. Internal and external factors were both mentioned and given emphasis on. Different restaurants had different factors contributing to vulnerability or resilience to inflationary pressure.

#### 5.1.1 Internal Impacts

Operational challenges have given more emphasis to cost management. It was stated that the cost structure of the restaurants has had massive changes after the pandemic. The traditional way of

running the restaurants has become much more challenging as inflation has hit the raw materials with a 20-30% rise which was mentioned by multiple interviewees. With rising energy and electricity costs, to ensure efficiency restaurants have been forced to upgrade equipment or adjust energy consumption patterns. Interviewee 5 stated: "Inflation has a direct impact on our contribution margin, which in turn affects our overall profitability. Last year was particularly challenging as raw material prices surged significantly, and we were unable to pass these costs onto our customers. As a result, we likely fell short of our target contribution margin by approximately 5-6%. This shortfall is substantial, as it directly reduces our profit." The contribution margin Management was seen as problematic. Many interviewees could not pass the increased cost onto customers without affecting the negatively customer flow.

Inflation has massively affected the raw material costs and labour expenses and operational efficiency. The increase in raw material costs has made it harder for restaurateurs to operate effectively whilst keeping high-quality ingredients. Many had to compromise on quality by switching to more affordable options. For example, switching to frozen ingredients was mentioned and the simplification of the menus was used to adapt to the situation. Especially the use of expensive key ingredients such as salmon was prevalent in many interviews. For example, the number of salmon used per dish must be monitored more strictly. Procurement accuracy was mentioned several times and as interviewee 3. stated, "Raw materials are still up by 20-30%, and procurement accuracy is important to prevent waste."

Economic uncertainty is affecting business performance across the sector. Several interviewees whose revenue had increased reported their profits decreasing due to higher costs. "Revenue has grown, but profits have decreased," was stated by interviewee 4. However, this was not the case for all interviewees. Interviewee 6 shared a more positive experience, as they were able to keep the profitability steady despite the challenges. "It has impacted the financial situation, but in our case, we could say that we have managed to control it over the past couple of years and maintained its profitability level." This success has been largely due to improvements in internal processes. "We've implemented more efficient and better procedures. So, while inflation has had an impact, it hasn't been as significant as it could have been."

The experiences shared by the interviewees highlight the different ways businesses are being affected by economic uncertainty. While some are struggling with higher costs eating into their profits, others are managing to stay profitable through effective processes and cost management.

### 5.1.2 External Impacts

Inflation has led to many external impacts. The most significant being the decrease in customers' purchasing power and rise in prices due to inflation. The general economic conditions have made it harder for SME: s to stay profitable. Especially the businesses whose target audience is everyday consumers, have seen the reprioritization of spending. As interviewee 1. noted, "Customers no longer buy as many specialty beers, because they are expensive. Similarly, there's been a decrease in customers upgrading their food portions." This indicates that customers are opting for cheaper alternatives. However, in more "High end" restaurants the rise in prices has not affecting the average purchasing power of customers, as they are already ready to spend more from the outset.

Other external pressures experienced by restaurants were the rise of VAT on September 1<sup>st</sup>, 2024. The Value Added Tax (VAT) in Finland is applied to most goods and services, it is divided into three rates: standard rate of 25.5%, reduced rate of 14% (restaurants and catering services) and reduced rate of 10% (books, newspapers, medicine, sports services and cultural events). Additionally, there is zero rate for exports and certain other items. (Tulli 2024)

The food that restaurants serve falls under 14% of the VAT bracket, but the alcoholic beverages are taxed at the standard 25.5% rate. This has influenced restaurants pricing regarding alcoholic beverages as the prices prior to September included 24% VAT rate instead of the current 25.5% rate. Interviewees 3 and 6 mentioned that the VAT rate changes had a major impact on their businesses.

Five out of six individuals who interviewed had one or more restaurants which offered lunch. One external pressure which was brought up multiple times was the fixed value of lunch coupons such ones provided by Edenred, ePassi and Smartum. These lunch benefits are extremely common for companies as they provide a subsidized way to enjoy meals during their workday. The costs of the lunch allowance are divided so that the employer pays 25% and the employee 75%. The fixed nature of these coupons presents challenges for restaurateurs as during periods of inflation the value of coupons does not adjust dynamically with inflation. Even though the maximum benefit has increased yearly from 10.50e of 2019 to 13.50e of 2024, the annual increase has not met the rising cost associated with inflation. While the nominal value of lunch coupons has increased, their real purchasing power has decreased. (Yle News 2024)

## 5.2 Pricing Strategies

Pricing strategies of the restaurants were mostly dictated by cost structure as well as what customers are willing to pay. The emphasis on what customers is willing to pay has increased. Most of the interviewees described the pricing strategy as being balanced between covering costs and maintaining competitiveness. Several strategies were mentioned, but cost-plus pricing was mentioned as a core strategy in all the interviews. However, the desired markup changed a lot depending on restaurant type. In many cases different products had different pricing strategies. Interviewee 1 stated that "Food products are mainly priced using cost-based pricing. Café products are priced using competitive pricing. Drinks and wines are more often priced using value-based pricing.". The strategic segmentation of pricing was used to balance profitability and market demand. Use several models gives restaurants freedom to address the unique cost and demand dynamics of different products. Gradual and periodic price increases were common theme amongst interviewees, but especially during lunch hours, the set price of lunch vouchers was seen as constraint which often had to be compensated with the quality of lunch offering and limitation of expensive ingredients.

The pricing adjustments were perceived as problematic. For many, the frequency of these adjustments has shifted from a more structured approach to a reactive model. The changes are minor, aiming to minimize any negative impact on customer. As Interviewee 3 stated, "If prices are raised too much, demand will weaken further." Interviewees 4 and 6 both stressed the option to modify the product instead of losing their competitive position in the market. "What will our price position be, where do we want to be, and will we remain relevant? This has forced us to adjust the product as needed, rather than pricing ourselves out of our current position." As expressed by interviewee 6. Interviewee 3 stated "The strategy involves monitoring competitors, determining the price point, and considering the cost structure to identify what cannot be done currently. Cost-based pricing cannot be raised as high as it should be.". While cost-based pricing is a strong indicator for setting prices, currently it cannot be the sole option due to constant market changes.

The observation of competitors prices and offerings emerged as a key factor in understanding and maintaining customers perception of value. The observation of competitors prices and products was mentioned by Interviewee 4: "You have to be the best in terms of price-quality on your own street, always keeping an eye on what the competitor offers and what you can offer.". This approach was especially common in competitive settings such as malls and shopping streets. In addition, the observation of general price level of the city was mentioned in the interviews. The importance of customers perception for value was seen in the menu engineering done by restaurants. As mentioned by interviewee 3 "In the development of the food and beverage menu, we are

designing combos and set menus to get better profit margins." This approach works well to increase perceived value. In the quiet times, interviewee 2 also mentioned discounts, such as 20% off from certain products, as a tool to gain customers' interest.

Restaurants with more value-based approach are not as volatile to inflationary changes compared to those working with more cost-based approach. For example, interviewee 6 mentioned their restaurants being in the same pricing position as before energy crisis. In addition, the VAT-raises will not be passed to customers via menu prices, but instead they will be deducted from the profit of the restaurant. Similarly, interviewee 4's restaurant was also less affected by price changes compared to others. Interviewee 4 mentioned that they have raised prices, but the increases have not been as significant as they could have been percentagewise. They emphasized communicating with customers and understanding their limits. Additionally, when customers visit a fine establishment, a small increase in the price of a glass of wine is not a major concern, especially if they are likely to purchase the whole bottle.

### **5.3 Cost Management Strategies**

Managing costs is a critical element for restaurants to remain competitive and profitable, especially during periods of inflationary pressure. Interviews conducted highlighted several key strategies used by restaurant owners and managers to combat the rising costs. Some themes that were brought up were efficiency, staff training, procurement decisions, partnerships and benchmarking.

Interviewees highlighted the importance of skilled staff frequently. Especially after COVID 19 pandemic the importance for knowledge regarding waste reduction, improved productivity and optimization of daily operations was seen as important. Interviewee 6 highlighted this; "Investing in staff training is a newer approach to cost management. The aim is for the staff to understand what is being done and why it is being done." For example, this approach helps staff to pay attention to portion control. Clear portion control helped reduce food waste and optimize costs more effectively. If everyone understands the value of ingredients, it makes a big difference in the long run. Labour cost management was also mentioned as a key element of cost management. The management of labour costs without compromising in service quality was valued. Using data to predict peak and off-peak hours helps managers optimize scheduling and staffing needs more effectively. When asked about the most important cost control strategy, Interviewee 6 summed it up: "It's quite difficult (Question), but I always advocate for efficiency in business. Gross margin and its planning and having the right number of people working. These two usually distinguish a functioning restaurant from a non-functioning one." The importance of skilled staff can't be underestimated.

Procurement management emerged as key cost control strategy among the interviewees. The selection of the right suppliers with quality ingredients and competitive prices was frequently highlighted. A juxtaposition between wholesale purchasing and purchasing pool was apparent, as 4 out of 6 interviewees were part of purchasing pool. Many interviewees were dissatisfied with the wholesale prices and saw purchasing pools as the only viable option to keep the procurement management costs manageable. Especially expensive volume products, such as salmon, were seen as problematic without purchasing pools. When asked about what cost management strategies used to combat rising prices, Interviewee 3 emphasised the role of procurement management: "Well, probably the competitive tendering of wholesale purchases, trying to increase the purchasing pool, which is a pricing strategy to optimize procurement by getting enough volume so that others will join our pool. That's quite an important part..." Collaboration was not only excluded for procurement, but some also used it in other areas, for example interviewee 4 stated having electricity contract with couple other companies to achieve better price. Interviewee 4, who was also part of purchasing pool, highlighted the importance of procurement, stating: "Profit is made through purchasing, and revenue is used to pay the rent. "

Benchmarking and measuring were mentioned by interviewees several times. Operational metrics such as food costs, labour costs, gross margin among others were seen as important tools to manage costs. Benchmarking also goes beyond the standard industry benchmarks as interviewee 6 stated: "And in the product itself, we believe that things that are not measured do not improve. So, we measure even quite small things. For example, we measured waste to find out where it originates." and "Some units we have had to dig really deep when sales margins have been slipping from month to month. For example, they have gone all the way to the shifts to find out what has happened here that has caused the situation to linger, and then it is usually found somewhere, for example, why a raw material has been used and in what way. E.g. 10% extra each time and then it accumulates." These examples show how benchmarking and measurement can provide valuable insight. Specific operational areas such as waste reduction and overall efficiency benefit significantly from this practice.

Resource optimisation was highlighted directly and indirectly several times. This paragraph focuses mostly on waste reduction, inventory management, and portion control. The importance of resource optimisation was critical to restaurants as the procurement costs are much higher than before. Every interviewee mentioned portion control and its importance due to rising costs. Interviewee 5 stated "Precise recipes and minimal waste, and the use of expensive ingredients such as smoked salmon, i.e., how much smoked salmon can be used per portion." This shows the common trend amongst the interviewees and presumably in the whole restaurant industry. As the profit margins are smaller than before, the importance of effective use of ingredients is essential. Interviewee

6 brought up resource optimisation as one of the umbrella terms for cost management on their operations. He highlighted the use of suitable ingredients to reduce unnecessary waste: "Are there ingredients that spoil easily? For example, the menu has certain raw ingredient elements that could be switched in a specific dish (for one that is not so prone to spoilage)." This also touches the subject of menu optimisation that supports efficient and sustainable inventory use.

In addition to more common cost management strategies there were a few methods that were less conventional or less frequently discussed. These methods were mentioned in interviews, but they weren't spotlighted as much as the ones mentioned earlier or they weren't present in multiple interviews. One of these methods was the upgrading of kitchen appliances to more ecofriendly ones. The modernisation of equipment and adopting energy-efficient solutions were viewed as long-term cost-saving strategies. Energy-saving measures were a theme in couple of interviews, but methods mentioned varied from restaurant to restaurant. For example, interviewee 4 collaborated with other businesses to secure better electricity contract. Optimization of menus was also a key theme. Streamlining menus to focus more on high-margin items while reducing complexity and waste was another strategy mentioned. Although these strategies were mentioned less frequently, they highlight the innovative approaches restaurants employ to combat the rising costs.

## 6 Discussion

The results conducted from my interviewees provided me with an extensive understanding of complex issues faced by restaurateurs during the inflationary pressures. With qualitative approach I was able to collect a broad set of data with great individuality for my research. The combination of thematic and content analysis helped me to find the key themes within the predetermined categories which supported my Investigative questions:

IQ 1. What internal and external factors contribute to a restaurant industry SMEs' resilience to inflationary pressure?

IQ 2. What are the most effective measures that restaurants can implement to minimize the impact of inflation?

The impact of inflation affected the operations of all the interviewees, as expected. Both external and internal factors were present in shaping their vulnerability and resilience. As the interviews revealed, the cost of raw materials and labour was a prominent and problematic topic, with one interviewee mentioning a raw material price surge of 20-30%. This had a significant impact on profit margins, aligning with the study by Sandqvist (2023), which reported a significant increase in the cost of goods sold. Similarly, White (2023) stated that rising costs and decreasing profit margins are common issues among restaurants. White also highlighted the importance of staffing and innovative solutions to address these problems. Many respondents acknowledged this and found their own ways to deal with it through improved effectiveness and training.

One major external impact was consumer behaviour. Many respondents felt that consumer demand had shifted towards more budget-friendly options. However, as stated in a study by Chua, Karim, Lee & Han (2020), restaurants with different customer segments are affected by consumer behaviour differently. For example, restaurants with budget-friendly menus tend to struggle less than their more expensive counterpart, which was supported by statements made by interviewees as well.

The operational challenges were also present in theory and in the interviews. The upgrade of equipment and adjustments to energy consumption patterns was mentioned as well as the importance of procurement accuracy for waste prevention. This finding is supported by the study published in the ECB Economic Bulletin by Attinas, Balatti, Mancini & Metelli (2022). This study emphasized the importance of efficient supply chain management and procurement strategies in mitigating the impact of inflation on businesses. Also, Cascaldi-Garcia, Orak & Saijid (2023) emphasized

the role of operational adjustments. This helps to maintain the stability of business during economic disruptions.

Pricing strategies were identified as crucial part to maintain the profitability in the restaurant industry. The primary pricing strategies in theory and in the interviews were cost-based, value-based and competitive pricing. As expected, most interviewees identified cost-based pricing as the core strategy. Particularly the cost-plus pricing was popular, but the mark up varied a lot. This supported the findings of Demetriou (2022) who estimated 60% of restaurants to use cost-based pricing. However, there was combination of many pricing strategies used, thus not every menu item follows the cost-based pricing as an absolute measure for price, even if it was mentioned as the core strategy.

Other pricing strategy which was mentioned was value-based pricing. Especially restaurants with premium-price point had set their prices with an intention of offering perceived value to customers instead of solely based on costs. This offered more flexibility regarding the pricing and for example one of interviewees was able to keep one product at the same price point even after small but significant rise in production cost. This approach is supported by Delucci (2024) who sees it as a valuable tool for the restaurants to adjust their prices with the perceived quality and experience. This strategy offers bit more immunity for economic pressures.

Third prevalent pricing strategy was competitive pricing. This was not mentioned as a primary pricing strategy for any of the interviewees, but it was identified as an indicator for pricing by some. This was supported by Demetriou (2022), who concluded that competitive pricing is popular especially in areas with multiple dining options. However, it requires constant monitoring of competitors.

Cost management strategies are essential for restaurants to remain competitive during inflationary periods. Key strategies which were identified were procurement management, labour cost management and resource optimisation. Procurement management and the use of purchasing pools were mentioned several times by the interviewees. Well maintained procurement management helps to obtain excellent ingredients at competitive prices. As Attinas Balatti, Mancini & Metelli (2022) mentioned in their study the role of efficient supply chain management is key factor in the mitigation of inflations negative effects. The use of purchasing pools emerged as a key strategy for restaurants, especially during inflationary periods. This was not initially covered in the theoretical framework of this thesis, but it is key part of procurement management, as it was mentioned by four out of six interviewees.

Labour cost management was an important aspect of maintaining the profitability of restaurants. The results gathered from the interviews highlighted optimisation of workforce scheduling and

cross-training of staff. Especially the optimization of staff scheduling during off-peak and peak hours was seen as necessary. As White (2023) states in her article regarding Rising Costs due the impact of inflation, rising labour costs and staffing challenges have been prevalent since the 2021. She states that effective scheduling which aligns the labour with customer demand is important and it also improves operational efficiency on top of labour cost control. Cross-training of staff was also mentioned by interviewee. This supports the perspective that increasing scheduling flexibility and developing a versatile workforce can help restaurants manage labour costs more effectively, while also enhancing employee engagement (White, 2023).

Resource optimisation is the last Cost Management strategy that I discuss. Resource optimisation was brought up in all my interviews with tools such as waste reduction, inventory management and menu engineering used. The use of ingredients has become a key factor in cost management and operational efficiency as it is a big part of the costs. The importance of waste reduction and portion control are not only beneficial from financial standpoint, but also sustainability wise, as DeForest mentions at her article. (DeForest 2025)

With the risen prices of goods inventory management emerged as a major focus among the interviewees. Many stressed how vital it was to track inventory closely to keep costs under control. Another recurring theme was menu engineering, which several restaurateurs described as a key strategy. By refining their menus to highlight higher-margin items, they were able to boost profitability. Interviewees explained that simplifying the menu not only made it easier to spotlight best-selling dishes but also helped them phase out less popular ones. This shift, they noted, led to a less complicated menu, lower food costs, and smoother operations in the kitchen. (Pollak, 2024)

For further studies, it could be beneficial to research the effectiveness of various financial strategies that restaurants could implement to cope with inflation. The research could dig deeper to effectiveness of different cost management strategies and techniques. These strategies could be dynamic pricing models, procurement strategies and financial health monitoring tools. Comparative study of many nations or areas could help to identify the best techniques restaurants could use anywhere. Furthermore, offering insightful analysis would be looking at the technological developments and their possible influence on financial management techniques. Finally looking at government financial support policies, financial consequences of consumer view of price and benefits of sustainability in cost reduction would provide thorough knowledge of general financial challenges and solutions regarding the resistance against inflation in the industry.

In terms of methodology, future studies could have mixed approach with the combination of qualitative and quantitative data collection methods. On top of the qualitative methods, such as the in-

depth interviews, quantitative method such as survey and financial data analysis could provide valuable information and broader perspective on the effectiveness of different strategies.

The benefit of this thesis is to give restaurant owners information about inflation's effects on their businesses. This thesis will provide a theoretical framework with valuable insight on inflation and its mechanics from an economic standpoint whilst also giving practical overview for the restaurants. Strategies and the practises will help coping with inflation and mitigating the negative effects of it whilst providing valuable information from multiple viewpoints. I am aiming to give suggestions which would align with specific needs of the restaurateur and provide information relevant to one's situation.

The benefits of this thesis for me are extensive. I hope that I can provide an informative and broad document with relevant information needed for this task. This was a huge challenge for me from a structuring standpoint, but I think it gives me a great foundation to work on future academic projects. Even though from a career standpoint I do not see myself working in a restaurant industry, I still see the topic relevant and fascinating. The information gained from this project won't go to waste as inflation will be a prominent topic for years to come and strategizing is present in every industry. However, as Charles Dickens famously said, "Never say never".



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## Appendices

### Appendix 1. Interview Structure

This interview is divided into four different topics and will begin as follows:

#### Question 1: Background and Experience

- **Could you briefly describe your experiences in the restaurant industry, how long you have been in it, and in what positions you have worked?**
- **How long have you worked at this restaurant and what is your current position?**

#### Question 2: Impact of Inflation

- **How has the rise in prices affected your business operations?**
- **Has it impacted the use of raw materials, labour, or other costs? If so, how?**
- **What is the current situation?**
- **Have these factors affected the financial situation of the business?**

#### Question 3: Pricing Strategies

- **How do you price your products?**
- **Have you had to change prices due to rising costs?**
- **What pricing strategies do you use?**

#### Question 4: Cost Management Strategies

- **What cost management strategies has your restaurant used to cope with rising prices?**
- **Which strategies have proven most effective in mitigating the negative effects of inflation?**
- **Have you implemented any new cost-saving measures in response to inflation? If so, could you share some examples?**
- **What do you think is the most important cost to manage and how do you focus on it?**
- **Do you have any additional thoughts or ideas on cost management that you would like to share?**