Journal of Hospitality and Tourism Management 29 (2016) 99–111

Contents lists available at ScienceDirect

Journal of Hospitality and Tourism Management

journal homepage: http://www.journals.elsevier.com/journal-of-hospitality-and-tourism-management

Drivers of success in independent restaurants: A study of the Australian restaurant sector

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ARTICLE INFO

Article history:
Received 1 February 2016
Accepted 12 June 2016

Keywords:
Restaurant performance
Innovation
Entrepreneurial self-efficacy
Human capital
Cluster analysis

ABSTRACT

This study used an inductive approach exploring the characteristics of high-performing, independent restaurants to determine the factors contributing to success in Australia's restaurant sector. Hierarchical and K-means cluster analyses were conducted to segment and profile 198 businesses based on their performance level. Performance was captured through owners' self-assessments of: 1) profitability, 2) volume of sales, 3) growth, 4) enterprise performance, 5) achieving expectations, and 6) overall success. Restaurants from this study fell into three clusters: High Performing Restaurants (HPRs), Average Performing Restaurants (APRs), and Low Performing Restaurants (LPRs). ANOVA, Kruskall-Wallis, Mann-Whitney U, and cross-tabulation tests were used to differentiate the clusters on a number of key business and entrepreneurial characteristics. The results found that business owners' level of entrepreneurial self-efficacy and the firms' innovation activities (service, process, and management innovation) were discriminating characteristics of HPRs. Human capital factors such as the owner's education, experience, and age were not significant in differentiating between the three clusters. The findings present new insights identifying the factors that distinguish successful restaurants from their less successful counterparts, enabling restaurant owners to prioritise the entrepreneurial skills and innovations they should develop to achieve business success.

1. Introduction

Independently owned, small and medium sized enterprises (SMEs) represent 99% of all restaurants in Australia. The sector contributes $22.1 billion in annual earnings to the national economy and employs the most people engaged in the tourism industry (ABS, 2014; Restaurant and Catering Australia, 2014; Tourism Research Australia, 2011). The recent 'Restaurant Australia' marketing campaign launched by Tourism Australia, the Government agency responsible for attracting international visitors (Tourism Australia, 2014) is indicative of the critical role played by the restaurant sector for Australian tourism. This campaign aims to brand Australia as the 'world's greatest restaurant', promoting the unique food and wine experiences being offered. However, the restaurant sector faces many challenges, with businesses struggling to succeed in the midst of intense competition, low barriers to entry, price conscious consumers, rising food prices, government regulation, and high labour costs (Assaf, Deery, & Jago, 2011; Restaurant and Catering Australia, 2014). Recent evidence suggests that 63% of restaurants earn less than 2% net profit after tax (Restaurant and Catering Australia, 2013). Business failure is also a critical issue as less than half of all restaurants operating in 2009 remained trading in 2013 (ABS, 2014). A successful restaurant sector is critical for the tourism and hospitality industry and for the livelihood of the entrepreneurs and employees.

A growing body of research focusing on restaurant business practices and performance has emerged over the past decade. Studies have examined employee turnover (Brandmeir & Baloglu, 2005), organisational strategy (Chathoth & Olsen, 2007), service quality (DiPietro, Parsa, & Gregory, 2011), menu engineering (Fang, Peng, & Pan, 2013), marketing strategies (Ghouri, Khan, Malik, & Razzaq, 2011; Ham & Lee, 2011), CEO duality (Guillet, Seo, Kucukusta, & Lee, 2013), customer satisfaction (Gupta, McLaughlin, & Gomez, 2007), and corporate social responsibility (Lee, Singal, & Kang, 2013). Previous studies measuring restaurant performance have focused on stock market valuations of public companies and chain/franchise restaurants in the US (see

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http://dx.doi.org/10.1016/j.jhtm.2016.06.003
1447-6770/

Choi, Kang, Lee, & Lee, 2011; Ham & Lee, 2011). However, in a sector where 99% of all businesses are privately owned SMEs (ABS, 2014), examining broader measures of performance are needed.

There remains a significant gap in our understanding of how SMEs in the restaurant sector operate and the factors that drive firm performance (Jogaratnam, 2002; Lee, 2015). Specifically, research needs to be conducted within an entrepreneurship framework where the business and the owner are intertwined; the capabilities, motivations, and objectives of the owner are often the driving force behind the business' strategies (Hallak, Brown, & Lindsay, 2012; Lumpkin & Dess, 1996). This study addresses these limitations and focuses on exploring the characteristics of small, independent restaurants with varying performance levels. We capture both firm and owner characteristics and use these variables to profile and distinguish among businesses based on their performance. To understand the characteristics of these businesses, information is collected on firms' innovation activities, including product, service, process, managerial, and marketing innovations, the owners' entrepreneurial self-efficacy (an owner's beliefs in his/her capabilities to successfully accomplish entrepreneurial tasks), as well as human capital variables including business experience and education.

This study adopts an inductive approach where no *a priori* judgements about the restaurant groups are made; rather, segments within the sample are determined from the analysis of data to explore a new phenomenon where theory is limited (Ostroff & Schulte, 2014; Spector, Rogelber, Ryan, Schmitt, & Zedeck, 2014). Through this approach, this research expands on existing knowledge by identifying the factors driving performance in small, independent restaurants. Segmenting restaurants based on their levels of performance and subsequently profiling them based on firm and owner characteristics delineates the variables that discriminate high performing businesses from their counterparts. This presents new theoretical insights into the drivers of business performance, constituting to inductive theory building concerning the performance of small, independent restaurants (Locke, 2007). Consequently, the findings also enable practitioners and industry bodies to implement strategies that support the success of the restaurant sector.

2. Literature review

2.1. Restaurant performance

Operationalizing performance in small business research often involves subjective (i.e. owner reported) measures (Hallak, Lindsay, & Brown, 2011). This is attributed to the difficulty in obtaining the actual financial records of SMEs. Capturing the performance of small hospitality businesses includes sales growth, volume of sales, profitability, return on investment, cash flow, net profit, market share, achieving expectations, and overall success (see Jogaratnam, 2002; Jogaratnam, Tse, & Olsen, 1999; Hallak et al., 2012; Lee & Lim, 2009). Research examining the performance of restaurants has adopted an entrepreneurship framework (Jogaratnam, 2002; Jogaratnam et al., 1999; Lee & Lim, 2009). Specifically, research has focused on Entrepreneurial Orientation (EO) which refers to the degree to which firms are inclined to compete aggressively, to take business-related risks, and to support change and innovation in the pursuit of a competitive advantage (Jogaratnam, 2002). Firms which pursue strategies such as low-cost leadership and aggressive marketing are found to perform better than those that do not (Lee & Lim, 2009). High performing restaurants are usually first to market with new products and services and seek continuous improvement in their product and service quality (Jogaratnam et al., 1999). Restaurants that are proactive in pursuing new opportunities, possibilities to expand, and anticipating future trends are able to achieve better performance than reactive firms (Jogaratnam et al., 1999).

Despite the contributions of previous studies, there remains a critical need to explore multiple predictors of restaurant performance to provide a more comprehensive picture of the factors that contribute to restaurant success (Jogaratnam et al., 1999). For example, Jogaratnam et al.'s (1999) regression model found EO to explain only a minimal amount of variance in restaurant performance ($R^2 = 0.19$), indicating the presence of other predictors of restaurant performance that are as yet undiscovered. Therefore, research is needed that examines both firm level characteristics (e.g. levels of innovation) and owner/entrepreneur characteristics (e.g. their entrepreneurial capabilities and knowledge) as predictors of performance. Examining both owner and firm characteristics simultaneously as predictors of performance is needed as the firm is an extension of the owner; and the capabilities, motivations, and objectives of the entrepreneur are often the driving force behind the business' strategies (Hallak et al., 2012; Lumpkin & Dess, 1996). Specifically, models on restaurant performance using an entrepreneurship framework need to include factors related to innovation activities, entrepreneurial capabilities, as well as the owners' knowledge and experience (conceptualised as human capital) (see Hallak et al., 2012; Hébert & Link, 2006).

2.2. Innovation in the restaurant sector

Innovation is considered central to entrepreneurship (Hébert & Link, 2006) and is defined as 'the process of bringing any new problem-solving idea into use…it is the generation, acceptance, and implementation of new ideas, processes, products, or services' (Kanter, 1983, p. 20). The Entrepreneurship Theory of Innovation stipulates that, in a capitalist system, entrepreneurs disturb or destroy existing economic structures and create new ones by putting untried methods into practice – a process labelled by Schumpeter (1952) as 'creative destruction'. In tourism and hospitality, entrepreneurs use new concepts, products, and ideas to set new standards and create radical shifts in the taste and preferences of their consumers, becoming a crucial factor in the evolutionary redirection of tourism and hospitality products (Hjalager, 2010). A continuous innovation process helps restaurants heighten barriers to imitation, keeping their portfolio ahead of the competition which establishes a long-term competitive advantage (Ottenbacher & Harrington, 2007). However, previous studies on innovation in the restaurant sector are limited, often presenting a descriptive overview of the new product development process (Ottenbacher & Harrington, 2007, 2009a, 2009b; Stierand, Dörfler, & Macbryde, 2014). Business innovation is a complex and multifaceted phenomenon, however, studies in hospitality are yet to examine a broader range of innovations including new services, processes, management structures, and marketing innovations (Hjalager, 2010). Resource constraints, including access to capital and expertise in human resources, pose challenges for the creation and implementation of innovations in the restaurant sector (Ottenbacher & Harrington, 2009a, 2009b). Unlike large firms with specialised R&D departments, small restaurants innovate by adopting and adapting innovations from outside sources.

In this study, we examine a broader operationalization of innovation to include product, service, process, management, and marketing innovations – based on the Schumpeterian approach and studies conducted under the Organisation for Economic Co-operation and Development's (OECD) guidelines (see Hall, 2009; Hjalager, 2010). *Product and service innovations* refer to new or significantly improved products and services such as the introduction of new materials, intermediate products, new components,