Cloud Kitchen: A Profitable Venture

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Abstract: This study examines the profitability of running a cloud kitchen over a traditional restaurant when it is pursued with the same level of efforts from the entrepreneur. Cloud kitchen with its many advantages over the traditional setup of a restaurant has shown to be a more profitable option in most of the cases. Cloud kitchens are not here to replace restaurants, it is just an additional food serving avenue for consumers. Only people who want to spend quality time with friends, colleagues, and family members will visit restaurants. For consumers who wish to enjoy and celebrate at home, cloud kitchens are available. These are two different venues altogether and none of them are here to replace each other. With direct competition with aggregators, new players are expanding the overall market. It fairly seems possible that in the future even lower-end traditional restaurants also will migrate to new norms and methods. Cloud kitchen hence seem a viable option for its enhanced efficiency in reach of customers, costs, time, ease, and regulated operations.

Keywords: Cloud kitchen, Dine-in, Entrepreneur, delivery only

INTRODUCTION

While number of new formats have emerged on the F&B scene in recent years, one format that has been making waves is Cloud Kitchen. With a model of minimum capital investment, low risk, high margins and endless opportunities, cloud kitchens are becoming one of the safest food business formats. Such has been the attraction of cloud kitchens, that many traditional kitchens have begun to shut their brick-and-mortar formats to make a move to the cloud kitchen format.

Cloud Kitchens, also referred as Ghost Kitchens is an outlet that gives no dine in facility in its premises it solely focuses on take-away and delivery for their business.

Most research and consulting reports on Indian cloud kitchens suggest that market size is expected to be about $1 billion by 2023 with a healthy double-digit growth rate every year, points out Narendra Singh Dahiya, Founder and Director, Homefoodi, a mobile application for home food made by home chefs.

According to Dahiya, earlier the contribution by cloud kitchens was estimated to be 20 percent of the food delivery market. However, this percentage is changing and will undergo drastic changes in the favour of cloud kitchens. The Indian F&B industry is witnessing a major drift from dine in to delivery business and the pandemic of Covid-19 has worked as a "catalyst" in the growth story.

The closure of restaurants due to the lockdown has pushed a majority of the population to opt for either home cooked meals or depend on food brought in through deliveries. (SOURCE: Gupta, P. (2020) "Growth of Cloud Kitchens in India" Retrieved from (https://ianslife.in/food-fitness/growth-cloud-kitchens-india))

According to RedSeer Management Consulting, the Cloud Kitchen industry in India is projected to become a $2 billion industry by 2024. It has been growing at 12% (2018-2023). The emergence of food aggregators and the changing food habits, especially in Metro cities, are critical in driving the industry's growth.

Cloud Kitchens accounted for 20% of the food delivery market, but that trend is about to change drastically in favour of Cloud Kitchens. (SOURCE: Redseer (2020) "Cloud Kitchens – The Secret Sauce to Survive in the Post-Covid Restaurant Market?" Retrieved from (https://redseer.com/product/cloud-kitchens-the-secret-sauce-to-survive-in-the-post-covid-restaurant-market /))

OBJECTIVE

1.   To examine the profitability of cloud kitchens over traditional dine-in restaurants.
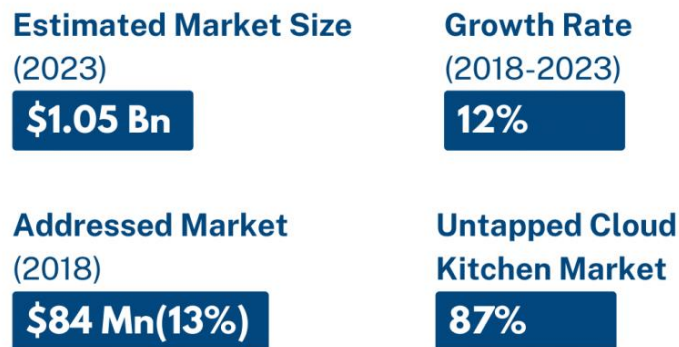
Figure 1 (Source: https://inc42.com/features/with-food-delivery-apps-backing-cloud-kitchens-do-restaurants-stand-a-chance/)

BENEFITS OF CLOUD KITCHENS FOR BUSINESSES

Now that it is established what Cloud Kitchens are, here are its benefits as compared to a traditional restaurant.

• **Cost of Entry:** One major obstacle for entrepreneurs to set their foot into the restaurant business is the cost to set it up, with Cloud Kitchens it is far lower, as they eliminate the need for high rents for prime locations, the need for any front house operations (such as valets, waiters, front desk employees, etc.), or any space for seating.

• **Lower Operating Cost:** Restaurants have a higher operating cost as they have to make sure to have better service staff & better décor to attract customers; on the other hand, a Cloud Kitchen does not have to deal with any of this as their only focus in on the quality of the food.

• **Flexibility:** Operating a Cloud Kitchen, owner can be flexible and easily adapt to a change in taste of consumers and therefore can change the menu, but with traditional restaurants is not an easy job to adapt to every trend in taste. Not being tied to a physical location means Cloud Kitchens can change the menu or even operating times to suit business needs without as much of an impact on customer satisfaction.

• **Access to User-Data:** As Cloud Kitchens and technology go hand in hand, the user data is easily accessible to them and with that they can easily optimize their processes, schedule of staff, user interface and even the margins based on the consumer behaviour

• **Covid Times:** With the recent pandemic of Covid-19, post-lockdown, it is seen that people have reduced their non-essential outdoor activities and prefer deliveries over the dine-in experience due to safety reasons, this is a great opportunity not only for the new entrants in the cloud kitchen business but also for the existing ones.

• **Lower CAC:** CAC refers to Customer Acquisition Cost, which means the cost incurred to acquire a new customer. Cloud Kitchen brands gain easy and quick exposure through their delivery partners, rather than having to market themselves. Even though they have to pay for their visibility on the delivery platforms it is overall cheaper than the amount a restaurant spends on traditional advertising.

• **Competing Prices:** One of the direct advantages of having low operating cost is that the cloud kitchens can use that to have a much more competitive pricing of their food; this helps them to make their menus more affordable and opens them up to new customer base.

• **Quality of Food:** In the traditional restaurant business there are a lot of overhead expenses, due to which they have a very little left to spend of the quality of food items in their dishes; On the other hand, Cloud Kitchens don't have large overhead costs which in turn helps them to focus on the quality of their ingredients and the final product.

POTENTIAL CHALLENGES FOR CLOUD KITCHENS

• **Dependence on Technology:** A Cloud Kitchen's business structure is totally dependent on technology. No matter how much advancements are done in technological sector, even a small difficulty can interrupt their entire operation.

• **Online Visibility Only:** The Cloud Kitchen business is strictly an online enterprise, it is a big challenge for them to cater to the older generation customer base, as most of them are less tech-savvy and majority of the base don't easily trust online businesses because of their beliefs.

• **Threat of New Players:** Since it is easy for new entrepreneurs to setup Cloud Kitchens, there is a constant threat of new businesses and brands arriving onto the scene and making it tough for the existing players in the market.

• **Food Quality and Safety:** The Cloud Kitchen Business model is all about take-away and deliveries, so it's reputation depends on the food getting to the customer in perfect condition, and with a huge surge in the deliveries many times the

delivery boys get sloppy and that ruins its reputation and in recent time of pandemic Covid-19, if the delivery boy is tested positive then it destroys the brand too.

• **Dependency on Delivery-Apps:** The major part of revenue of Cloud Kitchen is from the deliveries, and for that they are dependent on third-party delivery apps, who sometimes charge high fees which reduces the margins.

• **Lack of Human-Touch:** The Cloud Kitchen business model lacks human interaction between the vendor and the customer. The entire process, which begins from ordering the food to its delivery, has an absence of face-to-face interaction. Which sometimes leads to sub-standard food being delivered as the staff thinks there aren't any consequences because the customer isn't there to complain about it.

DATA COLLECTION

This research is totally based on Secondary Data. Secondary data included collecting information about various cloud kitchen and restaurants setup cost, the industry standards, etc from the various portals from the internet, journals, magazines etc.

Cloud Kitchen Vs. Restaurant

Factor	Cloud Kitchen	Restaurant
Rental Cost	As Cloud kitchen provide no dine-in facility, they don't need to think so much about the location of their premises, because they don't need any foot traffic, they can easily find a place for their setup at low rental cost.	Location influences the success or failure of a restaurant in a host of ways, from attracting enough initial customer interest to being convenient to visit. The location impacts its success nearly as much as the menu. If a restaurant is in the wrong place, it won't attract the number of customers needed in order to stay in business. So, the rental cost automatically increases vastly as nicer the location higher the rent.
Kitchen License	Licensing is an integral part of setting up a Cloud Kitchen. The major licenses required to start a cloud kitchen business are FSSAI, GST Registration, NOC from the fire department, etc. The cost of these licenses varies between 10,000-20,000.	To run a restaurant business in India licenses from the government are required. The major licenses required are Trade license from the municipal corporation, FSSAI, GST Registration, Professional Tax license, Business Registration, etc. The cost of obtaining these licenses varies between 50,000-1,00,000, depending on the size of the venture.
Equipment	The cost of setting up the kitchen will vary depending upon the cuisine and food offering. For example, the cost of setting up a cloud kitchen that wants to serve items like Burger, Pizza, Pasta, and Sandwiches will not cost more than Rs 2,00,000. Packaging plays a crucial role in creating a brand recall for the customers. The packaging must be sturdy to preserve the quality of the food during the delivery. Since Cloud kitchens don't provide a physical guest experience, packaging should leave a good impression on the minds of the customer. A good packaging machinery could cost around 30,000-40,000.	The cost of setting up the kitchen will vary depending upon the cuisine and food offering. For example, A kitchen for a 50-seater restaurant with multiple cuisines could easily 8 Lakhs – 15 Lakhs.
Alcohol	For a cloud kitchen to add alcohol, the cost of a liquor license is with 50,000 Rs.	If a restaurant wants to add alcohol in their menu, a liquor license would easily cost between 5 lakhs to 10 lakhs.

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Service & Management Staff	No service staff (such as waiters, valets) and no management staff (such as front desk manager, cashier) are required as cloud kitchens do not provide dine-in facility.	Well trained waiters, managers, cashiers, valets are a must for a successful restaurant, as they need to communicate with the customers and provide a fine dine-in experience, and experienced and well-educated employees do not come at a cheap price.
Décor and Aesthetic	As could kitchens do not provide dine-in facility the décor is not a factor for its success, they focus more on the quality of the food and the packaging as their only source of revenue is through deliveries.	Decor is important. First impressions count. Nowadays with the dawn of social media. Restaurants have lots of free advertising if people like the decor. People post in their Instagram or Twitter or even Facebook. People love posting beautiful pictures. If they tag the restaurant in their posting, its free publicity. The cost of setting up the décor and maintaining it varies according to the size of the restaurant and the theme on which the décor is based.
Profit Margins	Cloud kitchen usually enjoys an average profit margin between 10—12 percent, one of the main factors for this being low cost of operating.	Just as a restaurant's success is not wholly determined by the food or drinks it serves, the average profit margin for restaurant is impacted mainly by its cost of operations. The range for restaurant profit margins typically spans anywhere from 0 – 15 percent, but average profit margin for restaurants usually falls between 3 – 5 percent.
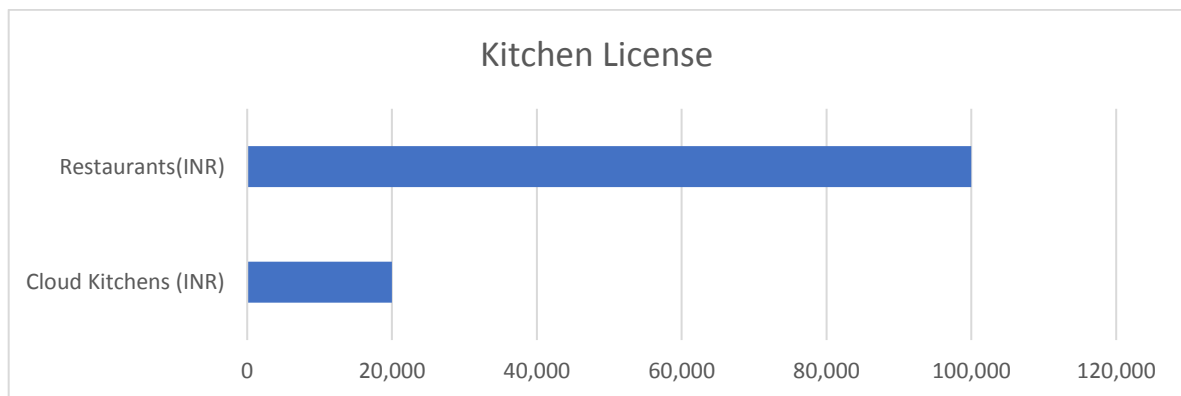
Figure 2 (Showing the Difference between the Avg. Kitchen License Cost of Restaurant and Cloud Kitchen)
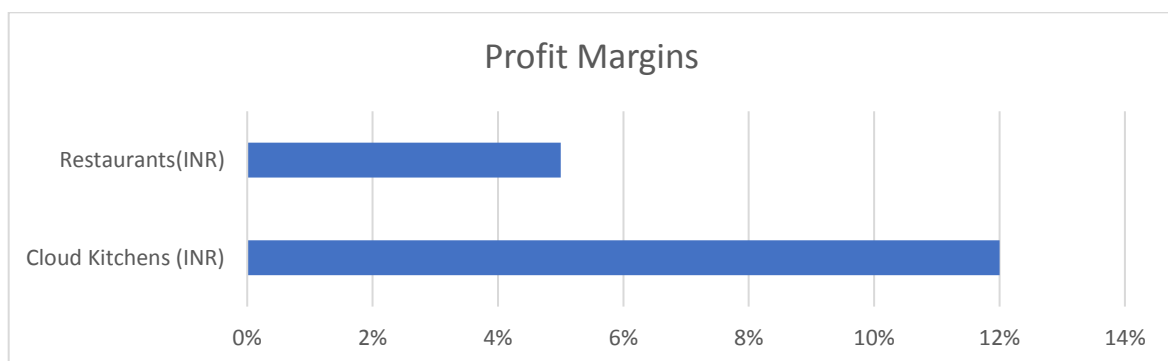

Figure 3 (Showing the Difference between the Avg. Profit Margins of Restaurant and Cloud Kitchen)

CONCLUSION

After reviewing the Secondary data collected via internet, journals and magazines, with the explanation of the basic factors responsible for the higher profitability of a cloud kitchen over a traditional dine-in restaurant in the table above, it is conclusive that, If an entrepreneur goes the cloud kitchen way over a regular dine-in with the same level of efforts, with its fair share of advantages such as low cost of entry, low overhead cost and low operating cost, The cloud kitchen without any doubt can turn out to be a more profitable venture. Even though there are certain limitations like late delivery, dependence on internet etc. Cloud kitchen is the ultimate need of time over traditional restaurants.

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