

Does each Subway \$5 Footlong cost the franchisee more than \$5?

Subway, the fast food restaurant franchise, recently announced it is bringing back the “\$5 Footlong” promotion. Hundreds of Subway franchise owners are protesting the promotion, saying that they cannot afford to sell the footlong sub sandwiches for \$5.

Assume that the costs related to a Subway footlong and a Subway franchisee include the following:

Cost item	Details	Cost per sandwich
Food ingredients	Per footlong	\$ 2.00
Labor cost per footlong	Labor \$14.00/hour wage rate, each worker can make 7 sandwiches per hour	2.00
Credit card transaction fee	1.0% + \$0.10 per transaction	0.15
Electricity	\$360 per month divided by 4,000 orders per month	0.09
Rent	Rent \$1,200 per month divided by 4,000 orders per month	0.30
Franchise fee amortization	Franchise and startup fees \$36,000 divided by 180 months (15 years) divided by 4,000 orders per month	0.05
Royalty fee	8.0% of sales	0.40
Advertising fee	4.5% of sales	0.23
Equipment leasing cost	\$600 per month divided by 4,000 orders	0.15
Cost per footlong sandwich		<u>\$ 5.37</u>

Assume that all transactions are paid for using a credit card.

Questions

1. Identify each of the listed costs of one footlong sub sandwich as either variable, fixed, or mixed.
2. What costs and factors do you think should be relevant to the footlong sub sandwich pricing decision? Explain.
3. What is the contribution margin of each \$5 footlong sub sandwich?
4. Do you agree that a Subway franchisee would lose money for each footlong sold for \$5? Why or why not?