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CORPORATE FINANCE

Food, Beverage & Hospitality

Adapting to the new normal

July 2020

Adapting to the new normal

Consumer sentiment

- As lockdown measures begin to ease and UK food, beverage and hospitality operators enter the ‘new normal’, businesses which plan ahead to adapt and refine operational models to meet changes in consumer preferences and demand will be best placed to rebound.
- A successful return to ‘normality’ will largely depend on the degree of consumer confidence. Uncertainty caused by COVID-19 has led to an increase in the propensity to save amongst UK consumers, with mixed opinions of financial security.
- Some 9 million UK employees have been placed on furlough since the scheme was introduced. This proportion of the economy is much more likely cook from home, seek cheaper options in grocery stores and reduce spending on takeaways and non-essentials in order to save money. Food and beverage brands should look to support this group in the post-COVID economy, offering products which are perceived as better value for money by consumers.
- Without the usual opportunities to dine out and socialise in pubs and bars, food and beverage brands have taken the opportunity to grow their audience and establish increased consumption within the home. The shift in consumer demand from food service and retail to at-home consumption will result in some consumer packaged goods manufacturers seeing a corresponding increase in volume, revenue and profit.
- The consumer’s relationship with online delivery is likely to have changed for good. 55% of Brits have signed up to at least one new food or drink delivery service during lockdown. Of this 55%, around a quarter are likely to continue using the service once lockdown restrictions are lifted. Online supermarket delivery has experienced a significant increase in first-time customers, with 26.5% of the UK signing up during the initial weeks of lockdown.
- Since the COVID-19 outbreak, consumers have become increasingly mindful of how food and beverage products are sourced, produced and delivered. Consumers are purchasing from trusted local suppliers where possible.
- The majority of consumers plan to adopt healthier lifestyles as a result of the pandemic, shifting consumption towards nutritious food and beverages and reducing their intake of sugar and alcohol. Consumers are willing to pay a premium for goods which are both locally sourced and perceived as healthier.
- There is pent-up demand for both eateries and pubs to reopen nationwide, with many consumers willing to visit establishments within the first week of reopening. 30% of UK consumers intended to dine out or visit pubs and bars in the week lockdown rules are lifted, rising to 50% in London.
- Consumers’ expectations of health and safety will be heightened and businesses will need to provide reassurance that operations, premises and products are hygienic and safe. Consumers will expect best practice social distancing measures to be in place, staff to receive adequate training, and personal protective equipment to be worn where appropriate. Around two thirds of consumers remain cautious of visiting eateries immediately following the relaxation of lockdown rules.

43% of Brits are spending more time cooking at home

Pent-up demand for eateries and pubs to reopen

Increased use of online delivery platforms

Consumer preference for locally sourced and healthier products

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Practicalities of reopening

- Restaurants and pubs have been allowed to reopen from 4th July in England. Indoor hospitality operations are limited to table service, with businesses encouraged to minimise staff numbers and customer interaction where possible. The two metre distancing rule has also been relaxed to a 'one metre plus' rule.
- Certain establishments will be better placed to rebound from the effects of COVID-19, such as fast food outlets and coffee shops. Quick Service Restaurants (QSRs) allow for minimal consumer dwell time, lower property costs, greater integration with home delivery platforms and a younger target demographic (perceived as having a lower health risk).
- Experience-led establishments such as fine dining and casual dining will continue to face challenges in the near term. These establishments face higher rent and labour costs than QSRs and attract a higher proportion of 'at-risk' customers. Pubs are likely to suffer considerably as many in the UK operate with very fine profit margins and any material reduction in customer footfall is likely to have a severe impact on the ability of businesses to survive.
- In the short term, there will be a staged phasing of openings in favour of larger sites initially (which can accommodate social distancing more easily) and the opening of smaller sites may be deferred until more evidence of consumer trends and growth are seen. Many hospitality businesses will simply not survive in 2020 because they operate with too fine margins or are too highly geared to be viable in the post COVID-19 market place.
- Despite the encouraging news of establishments beginning to reopen and social distancing measures beginning to ease, the sector will continue to face difficulties in the near term. Most UK restaurants are small physical spaces and rely on maximum utilisation to survive, let alone generate material profits.
- The 'one metre plus' rule will support establishments in reopening, increasing the maximum capacity of venues from c.30% if two metre distancing was in place, to c.70%. However, reopening at any level of reduced capacity will still not be a viable option for many establishments. Kitchens are also typically small spaces relative to the number of staff and many restaurant kitchens will not be able to function at the required capacity whilst accommodating for social distancing.
- The Chancellor has announced further support for the hospitality sector as part of his Summer Statement. Diners will receive 50% off their restaurant bills during August in an effort to boost footfall and spending within eateries. Each week in August, businesses can then claim the money back, with the funds in their bank account within five working days. Establishments will be able to register for the scheme on Monday 13th July. The Chancellor also announced that a cut in VAT, from 20% to 5%, would apply to eat-in or hot takeaway food from restaurants, cafes and pubs. The lower tax rate will be implemented on 15th July, and will remain in place until 12th January 2021.
- Manufacturers will seek to minimise levels of human capital within production lines, in an effort to improve accuracy, efficiency and safety of processes. The use of automated storage and retrieval systems is likely to increase in popularity in future.
- Food and beverage manufacturers should leverage the benefits of the immediate community rather than global supply chains where possible. Severe disruption to global supply chains caused by COVID-19 may result in food and drink supply chains of the future shifting back towards seasonal produce, with local growth and supply where practical.

QSRs will be better placed to rebound from the effects of COVID-19

Manufacturers may consider storing additional stock in the event of future supply chain disruptions

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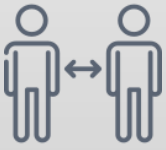
Rethinking venue design and operating procedures

- Current physical layouts will need to be adapted to cater for social distancing measures and changes in consumer purchasing behaviour.
- As establishments begin to reopen, customers' expectations of hygiene and safety standards will be heightened.
- New hygiene and safety measures should be clearly visible throughout venues to provide reassurance to customers.
- Establishments have been encouraged to minimise customer interaction where possible. Businesses should consider integrating technological processes such as digital ordering to help facilitate this.
- Many businesses are developing hygiene models whereby staff will be regularly temperature checked, with sanitisation operating models that will become the norm in future.
- An increased focus on retention and recruitment of local staff will feature in the 'new normal' economy, in order to reduce the hygiene risks associated with commuting.
- The preference for off-premise dining is likely to continue. Streamlined processes should be in place to facilitate contactless services, with an area of the premises dedicated to customer order collections.

Reactivating customer engagement

- Consumer behaviours have transformed as a result of restaurant closures. The consumer's relationship with home cooking, home delivery and takeaway is likely to have materially changed for good.
- Many have learned to cook or cook more experimentally during lockdown and the increased ease and variety of home delivery and takeaway is likely to result in less frequent retail eat-in experiences per customer per month in future. 20% of Brits are now cooking every meal from scratch.
- Loyal customers should be encouraged to return to on-premise dining via personalised messages and discounts, including critical information such as when establishments will be open and the measures taken to ensure maximum hygiene and safety standards.
- Retaining customers who became first-time buyers during the lockdown and those who have placed online orders during the period is essential. Loyalty programmes should be promoted to these customers.
- Many brand owners and business leaders agree that the lockdown period has given them the opportunity to completely revisit their brand positioning and business models, to ensure they are better aligned with the consumer of the 'new normal'.
- The pandemic will result in a cleansing of the UK hospitality sector whereby there will be fewer, leaner and better manged businesses, offering a more sophisticated quality of product and service offering; for what will be a far more demanding customer.

18% of consumers
agree that digital ordering should be an option at hospitality venues



Over 40% of consumers
are prepared to pay a premium in venues with enhanced social distancing measures

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Optimising the delivery model

- The shift in the consumer's preference towards off-premises dining will continue in the near term as customers seek to minimise dwell time in public areas.
- Many brands have discovered that online platforms and third-party aggregators have become the primary pillar of customer ordering and engagement during the pandemic.
- Optimising the digital consumer experience will be critical to retain these customers. Establishments should engage with customers via personalised offers and messages across multiple digital channels.
- Establishments should implement a strategy to manage and enhance online delivery capabilities and relationships with third-party aggregators, ensuring menus are aligned across all platforms.
- Incorporating digital platforms will streamline ordering processes, enhance the brand image and provide access to valuable end-user data to create more informed merchandising and promotion decisions.

Reassessing store footprint

- Throughout the UK economy, many companies have realised the efficiencies and cost savings that can be achieved by employees working from home; specifically, a reduced requirement for office space.
- As a result, there will be a permanent shift within multiple sectors of the economy towards employees continuing to work from home post-lockdown.
- It is anticipated that there will be a drop in natural footfall following the lockdown, with consumers avoiding crowded locations and favouring working from home where possible.
- This will have a subsequent impact on the average trading performance of central city hospitality providers, specifically on Mondays and Fridays as consumers often choose these days to work from home.
- It may not be viable to reopen venues in areas where footfall has been significantly affected. Establishments should evaluate the strategic benefits of shifting to delivery or collection-only operating models in specific regions.

55% of Brits

signed up to a new food or drink delivery service during lockdown

77% of employees

want to continue to work from home at least once a week

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Optimising supply chain models

- Food and beverage manufacturers have experienced severe supply chain issues as a result of the virus, driven by a shortage of goods, travel restrictions and increased shipping and freight costs.
- The industry has also experienced shortages of personal protective equipment and difficulties in adhering to social distancing measures within production facilities.
- Previously, manufacturers were reluctant to store extra capacity in warehouses or on production lines. However, given the supply chain disruptions caused by COVID-19, this model may change and drive additional capacity to be considered in future.
- Food and drink manufacturers will need to redesign current facilities and operating models in order to create leaner and more flexible production lines, whilst adhering to employee safety best practices.
- Manufacturers should give consideration to new product development, both from a supply chain perspective and to meet new and evolving consumer trends and purchasing patterns.
- Manufacturers should leverage the benefits of the immediate community rather than global supply chains where possible. Food and drink supply chains of the future may shift back to seasonal produce with local growth and supply where practical.
- Manufacturers will seek to minimise levels of human capital within production lines, in an effort to improve accuracy, efficiency and safety of processes. The use of automated storage and retrieval systems is likely to increase in popularity in future.

Monitoring consumer preferences

- Since the COVID-19 outbreak, consumers have become increasingly mindful of how products are sourced, produced and delivered.
- Consumers' expectations of health, safety and quality of produce will remain heightened after the virus subsides.
- Similarly to previous pandemics, demand for organic produce has spiked as consumers seek products which are perceived as healthier and more nutritious.
- The majority of consumers plan to adopt healthier lifestyles as a result of the pandemic, shifting consumption towards nutritious food and beverage products and reducing their intake of sugar and alcohol.
- Consumers are also purchasing from local suppliers where possible, not only to support smaller local businesses during the crisis, but for greater transparency and comfort of where products are sourced.
- Consumers are willing to pay a premium for goods which are both locally sourced and perceived as healthier.
- Before the pandemic, the world was already beginning to transition from industrial animal production for consumption to more sustainable, animal-welfare forms of agriculture, as well as a reduction in animals raised for food.
- Consumption of vegan products was one of the prominent health trends of 2019. As consumers switch from animal based diets to plant-based, there will be further demand for 'mock meat' products and meat alternatives in the future.

61% of manufacturers

plan to reduce supply chain dependence on dominant source countries in response to COVID-19

59% of consumers

have become more cautious of their overall health as a result of the pandemic

Sources: BBPA, Caterer.com, The Independent, FMCG Gurus, Attest, Work From Home Experience Survey

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Gambit Corporate Finance

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