gamBIT
CORPORATE FINANCE

# Hospitality

## UK Market Review

March 2020

# Contents


**Executive Summary** 2

**UK Hospitality**

*At a Glance* 3

*Market Dynamics* 4

*Operator Insight* 5

*UK Investor Appetite* 6

**Gambit Corporate Finance**

*Sector Credentials* 7

**Contact Details** 8


**Gambit Corporate Finance**

Established in 1992, Gambit is an independent corporate finance advisory firm specialising in advising private and public companies on mid-market transactions in the UK and overseas. With offices in London and Cardiff, Gambit is widely recognised as a market leader in M&A advice in the hospitality sector having built up detailed industry knowledge and an enviable track record in deal origination and execution.

**www.gambitcf.co.uk**

**Corporate Finance International**

Gambit is the exclusive UK shareholder of CFI, a global partnership of middle-market investment banks and corporate finance advisory firms. With over 250 professionals located in 18 offices throughout the world. CFI members specialise in cross-border acquisitions, disposals, capital raising, and related services.

**www.thecfigroup.com**

# Executive Summary

**Jamie Kennell**

**Partner - Food, Beverage & Hospitality**

Jamie Kennell is the partner that leads Gambit's food, beverage and hospitality team. Prior to joining Gambit, Jamie was previously a partner at Beringea LLP, a specialist mid-market private equity firm with $500m under management.

After graduating in geography & economics and subsequently an MBA at Cardiff Business School, Jamie began his career with NatWest Markets in 1991, specialising in structured finance. During his career, Jamie has held positions as a director at KPMG and 3i PLC as well as Beringea LLP. Jamie has sat on more than 20 private company boards as a non-executive director. He has been an owner-manager on several occasions and is currently the co-owner and non-executive director of a restaurant group with 8 locations in the UK.

## In Summary

- Despite the industry experiencing ongoing headwinds in the form of Brexit, coronavirus and mounting cost pressures the sector remains resilient. Underlying trends are still spurring growth, with consumers dining out more and using restaurants as a place to socialise.
- Over recent years, the industry has seen the rise of quick service restaurants (QSR) which have been less vulnerable to the supply side pressures as opposed to the casual dining sub-sector. This is derived from the lower operating costs of these establishments and favourable consumer trends.
- Despite the perception of the casual dining sector being under pressure, the industry has experienced consistent growth between 2014-2019. Casual dining has experienced an oversupply of traditional chain restaurants which has led to a number of high-profile closures. Nevertheless, operators that are able to distinguish themselves in the market are still an attractive option for investment.
- Millennials and Generation Z have emerged as the largest consumer base, which has led to many restaurant establishments adapting their existing business models to cater for these generations. This includes utilising social media as a marketing tool and adopting technological innovations to improve the customer experience for the tech native generations.
- Food delivery services have surged in popularity as consumers have less time to cook and delivery options have expanded outside the traditional offerings.
- Meat consumption among UK consumers has fallen considerably as the public adopts new dietary trends such as veganism and vegetarianism. This has led to operators expanding their food offering to cater for these new consumers. First mover advantage has been seen in Greggs Plc which experienced a "record year" which it attributes to the popularity of its vegan food options.

# UK Hospitality – At a Glance

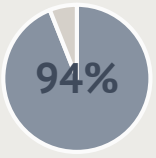
## 1. Cosmopolitan Palate

**30%** of adults rate British food as their favourite cuisine.

**22%** of adults prefer Italian cuisine.

**14%** of adults prefer Indian cuisine.

**12%** of adults prefer Chinese cuisine.




of the UK population include an international cuisine as their top five favourite meals.

## 2. Domestic Market

- The casual dining sector remains resilient, despite ongoing cost pressures.
- The QSR market has doubled in value over the past three years.
- High rents, evolving employment laws and the depreciation of the pound are the major issues facing industry operators.
- The recent outbreak of COVID-19 is likely to cause short to mid-term disruption to the sector, due to heightened anxiety across the investment community and lower consumer footfall.

**40%** Industry turnover since 2008.

**78%** Number of businesses since 2008.

**43%** Industry total employment since 2008.

## 3. The Rise of QSR

**40%** Of Millennials eat out weekly.

**½** of Millennials want a new experience when dining out.

**55%** of Millennials say convenience is a key issue when ordering food.

QSR will experience a **CAGR of 4.5%** between 2019 and 2024.

## 4. Utilising Technology

**80%** of restaurants are embracing technology to improve operational efficiency.

**1** in **3** operators use online apps.

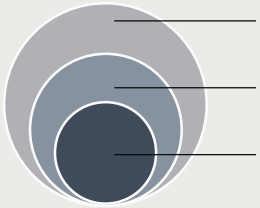
**77%** of customers claim restaurant technology improves the dining experience.

There is an increased focus on creating **'instagramable'** food and venues for online marketing.

**93%** of potential customers view a company's website before they decide where to eat.

Online customer reviews are still the most trusted source of marketing in the restaurant industry.

## 5. A New Audience



Vegetarian and vegans **3,432,000**

Vegans **1,100,000**

Lifestyle vegans **419,000**

Meat-free retail sales are expected to increase to £658m by 2021.

## 6. Future Developments

- **Technology** will be key to alleviate cost pressures in casual dining and QSR.
- **Data analytics** are set to improve the operational efficiency of restaurants and QSR.
- **Healthy eating** and individualised dietary requirements will mean industry operators will have to expand their service offering.
- **Delivery** demand will continue to rise which could have the potential to hurt the instore experience.

Source: Office for National Statistics, Companies House

# Market Dynamics

## 1. Quick Service Restaurant

- Quick service restaurants are currently the largest sub-sector within the hospitality industry.
- The QSR industry is expected to achieve a 7.61% CAGR over the next 5 years.
- Driving this growth are a combination of factors; limited exposure to cost pressures, low capex requirements and changing consumer preferences.
- QSR business models are better equipped to cope with the current market conditions due to their low human capital requirements, smaller operational facilities and reduced raw material need.
- Changing consumer preferences have also benefited QSR, as Millennials favour quick service, food on the go as opposed to a dining experience.
- QSR has traditionally been a sector that promotes unhealthy eating; however the sub-sector has been the quickest to respond to the rise of veganism among the public.

More **vegetarian** than **meat-led** restaurant openings.

- Greggs, an early adopter of vegan food has seen sales dramatically increase. However, more importantly the perceived brand identity has changed that caters for a Millennial audience.
- Nevertheless, the tightening of regulation surrounding animal farming and food standards has changed the public's perception of what QSR represents.
- Despite the recent trends, chicken outlets remain the largest subsector of the QSR market.
- From 2018-2019, there was a 40% increase in the number of consumers visiting chicken outlets with poultry being the most consumed meat from takeaways.

## 2. Casual Dining

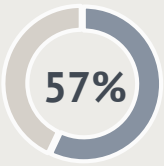
- The casual dining sector has remained robust despite economic challenges.
- When compared to the whole of the UK, London remains the region with the highest per capita spend on eating out.
- Within the sector quality standards have risen to differentiate themselves against QSR.
- Casual dining chains have often favoured fast roll out which came at the cost of food quality which has seen the collapse of brands such as Jamie's Italian.
- Challenging traditional dining concepts are proving popular with Millennials and Generation Z.
- Social media marketing in the casual dining sector is proving successful as younger generations are willing to pay a premium if the restaurant and the food is 'instagramable'.
- The vegan and vegetarian casual dining sub-sector remains in its infancy and fragmented.
- The current economic climate continues to support meat dish concepts due to chef training costs and higher margins associated with chicken, steak and pork meals.

### Millennial Dining Characteristics

- Quick service
- Unique concept
- Low calorie
- Lower income
- Online marketing
- Endorses food trends

### Baby Boomer Dining Characteristics

- Customer service
- Traditional dining
- Gourmet food
- Higher income
- Televised marketing
- Comfortable food




of Millennials currently subscribe to a special diet.

## 3. Adapting to a Dynamic Market

Casual dining and QSR are adapting to the current market conditions, however the way they are tackling this dynamic market vary:

- **Catering to a New Generation –** Millennials and Generation Z naturally favour QSR establishments, quick service and low-cost healthy food options. However, this generation can be easily accessed if you cater to their diets, habits and style. You can engage with this new consumer through social media and cater for them with a menu that has sustainability sourced food along with various dietary options. It is also important to make dishes and the restaurant interior unique with the intention of the customer promoting the restaurant on social media platforms.
- **Hospitality Innovation** – Across QSR, anytime anywhere ordering through apps and self-service kiosks have become widely adopted, improving the spend and personalisation of service across the sector. Casual dining has utilised technology by increasing customer awareness, automating table reservations, enabling pre-ordering of food and improving in-restaurant engagement.
- **Online Delivery/ Logistics** – Home delivery has grown 300% faster than dine-in traffic since 2014 with mobile orders making up 11% of QSR sales by 2020. It has also boosted casual dining sales with more restaurants joining Deliveroo and Uber Eats. However, with online delivery continuing to rise in the future, restaurant operators must not let the new revenue source cannibalise their in-store dining experience.

Source: Office for National Statistics, Companies House Sources, Gambit Analysis

# Operator Insight

## 1. Evolving Delivery Methods

- The growth of online food ordering services has enabled consumers access to restaurant products from home.
- A rise in the average weekly hours of work has reduced consumers leisure time and increased the need for quick alternatives to in-store dining or home cooking.
- Online delivery apps enable operators to build a relationship with consumers without ever entering the physical restaurant.
- Operators are also turning towards the development of grocery ranges as a method of enhancing brand loyalty and reaching customers.
- Diversified revenue streams allow operators to secure additional revenue outside of their primary operations.
- Notable examples of this are Nando's, whose peri-peri sauce is now the UK's best-selling chilli sauce, which generated £14.4 million in revenue last year, and Pizza Express which now sells more pizzas in supermarkets than in its restaurants.

**39%** of restaurants using apps increased orders outside of meal times.

## 2. Data Analytics

- Digitisation continues to reshape the functional and operational outlook of the restaurant industry.
- New metrics are now readily available providing owners with insight that has the ability to improve revenue streams and reduce operational costs.
- The data streams can improve menu decisions making, the guest experience and labour costs.
- As more data is collected, owners can begin to predict consumer behaviour improving order accuracy, forecast trends and minimise food waste.
- Once businesses are able to predict their service requirements, they then possess the foresight necessary to better manage their day-to-day operations. Maximising revenue streams and more effectively controlling costs.

## 3. Key Performance Indicators (KPIs)

Accompanying the data revolution are a new wave of KPIs that provide key insight into the running of a restaurant.

- **Sales Per Labour Hour** – Labour hours are one of the most perishable resources, as it cannot be utilised in the future therefore, the productivity of staff whether that is in the kitchen or on the restaurant floor has a significant impact on the operational costs of the business.

## 3. Key Performance Indicators (continued)

- **Sales Per Head** – Restaurants calculate their sales per head to establish how much customers are spending during various times throughout the day, month and year.
- **Revenue Per Available Seat Hour (RevPASH) –** A relatively new KPI, to understand how efficiently and effectively each seat in a restaurant generates revenue.
- **Seat Efficiency -** Seating the right party at the right table is important in maximising revenue generated by each table and improves the dining experience for customers.
- **Table Turn Time -** The time it takes for a guest to dine, from the time they sit down to the time they leave. For a casual dining restaurant, the faster the table turn, the more revenue is generated.

## 4. Overcoming Cost Pressures

- Operators are expected to face further cost pressures.
- The fall in the value of the pound has meant casual dining restaurants have reduced their menu offering, focusing on high quality dishes with larger margins.
- 25% of chefs and up to 75% of waiters in the UK are from EU nations.
- The availability of cheap labour will be reduced, therefore technology and data analytics will become more valuable, to improving in-house efficiency by streamlining the workforce.
- Tightening of regulation surrounding self-employment laws and zero hour contracts will put further pressure on restaurant chains and delivery services to innovate to reduce their human capital requirements.

**25%** of chefs and **75%** of waiters are from EU nations.

- Wage costs have risen as a proportion of revenue over the past five years, most notably following the introduction of the National Living Wage, which increased by 4.9% in 2019. Wage costs now account for 35% of industry expenditure.
- A restaurant's location is imperative to its success. Rising rent and rates costs have resulted in narrowing margins in recent years and are expected to account for c.20% of industry revenues in 2020. Rents paid in London are rising at rates far beyond inflation, with rent in some postcodes more than doubling.

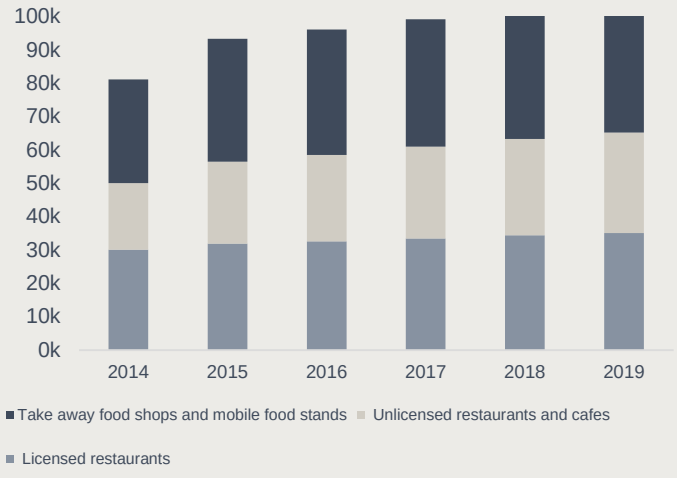
**x2**

Rent costs in some areas of London have more than doubled in recent years.

Source: UK Gov, Office for National Statistics, UK Survey of Restaurant Owners

# UK Investor Appetite

## Number of Net UK Restaurant Units by Sub-Sector




## 1. Market Summary

- The hospitality industry has reported consistent growth over the 5-year period.
- Despite rising operational costs, the sector remains buoyant.
- Takeaway shops and mobile food stands represent the largest segment within the hospitality sector.
- Substantial growth has occurred within both the 'takeaway' and the 'unlicensed restaurant and café' sub-sectors.
- Unlicensed restaurant and café sub-sector has been experiencing over 4% growth year on year.
- Café culture has proved popular with Millennial audiences and continues to be imported from the European continent.
- Casual dining has grown year on year dismissing the notion that the sub-sector is in retreat.
- Each sub-sector continues to grow, making the hospitality sector appealing to investors as well as operators. Innovation will be key to a business's success utilising new technology and catering to a new generation of consumers.

## 2. Factors Influencing Investor Appetite

### Industry Overview

Hospitality remains an attractive sector for investors.

In spite of Brexit, many firms have sought to invest in the sector, spurred on by the falling value of the pound, which has caused UK businesses to be at a discounted price to foreign investors.

### Sector Confidence

Despite the industry headwinds, the appetite of investors to support both new entrants and experienced operators has persisted.

The underlying trends that attracted financiers to the sector still exist, with consumers dining out more frequently and using restaurants as a place to socialise.

### Unique Concept

Businesses that define themselves in the industry, saturated by traditional concepts, continue to generate significant profits. Investors understand this opportunity and are willing to make funds available to operators with well managed sites or a strong business plan.

### Fast-Growing Sectors

Vegan QSR is receiving high transaction multiples as private equity firms such as Encore Capital make acquisitions in the sector.

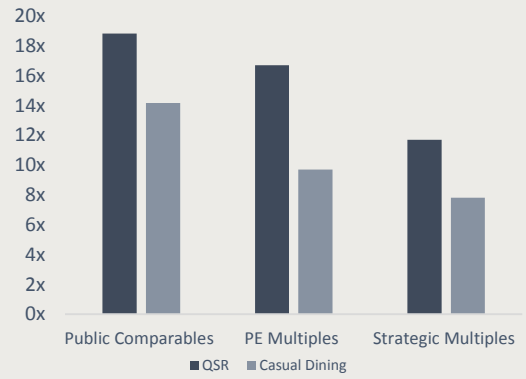
Food hall concepts are surging in popularity. Both Edition Capital and Bridgepoint have invested in businesses that have begun to capture the market.

### Food-Tech

Food-tech can enable restaurants to generate revenue and reduce operational costs using data analytics to identify opportunities.

From the data, KPIs can be derived which can ultimately help instil confidence in the management team when trying to obtain investment.

## QSR & Casual Dining Industry Multiples




## 3. Hospitality M&A Market

- Deal volumes, throughout 2019 remained robust, despite Brexit uncertainty having a real impact on the sector.
- In 2019, investors and investors became increasingly cautious around the sector.
- This caution was derived from large high-street brands falling into administration due to mounting debt obligations.
- A combination of Brexit uncertainty and the perception of high indebtedness across the sector resulted in a reduced number of mega-deals occurring.
- Mounting levels of dry powder have emerged in the sector, due to lower levels of M&A in 2019.
- Investors are under pressure to put this capital to work as Brexit uncertainty subsides.
- Businesses with strong financials and a clear runway for growth will attract investment interest in 2020.

Source: Office for National Statistics, Companies House Sources, Gambit Analysis

# Gambit Corporate Finance

## Sector Credentials

Gambit Corporate Finance has extensive credentials in the food, beverage and hospitality sector across acquisitions, disposals and raising of development capital. With a dedicated team and a credible track record in deal origination and execution, Gambit is well positioned to add value to its clients on a range of corporate finance activities.

Gambit is a member of an international partnership, Corporate Finance International (CFI), which has a dedicated food, beverage and hospitality team. The relationship with CFI provides Gambit with access to integrated group of food, beverage and hospitality experts across the globe, engaging in cross-border M&A activity, sharing insight and ultimately, providing a seamless service for clients. Jamie Kennell is a key part of the CFI food, beverage and hospitality team equipping him with direct access to its global network of food, beverage and hospitality expertise.

## Selected Sector Experience:

| | | | | |
|---|---|---|---|---|
| Jamie Kennell acted as an advisor to the board of **GORDON RAMSAY GROUP** on its sale of Muranto Angela Hartneet | Jamie Kennell acted as investor advisor to the board of COAL KITCHEN on its fundraising and sale | Jamie Kennell acted as an advisor to the board of **GORDON RAMSAY GROUP** on its fundraising | Jamie Kennell acted as investor advisor to the board of LOCH FYNE SEAFOOD & GRILL on its fundraising and sale | Jamie Kennell has acted as lead board advisor to **Donatantonio** on its fundraise and sale |
| Gambit Corporate Finance acted as lead advisor to the management of bluestone national park resort on its secondary buy-out with funding from BARCLAYS | Gambit Corporate Finance acted as lead advisor to the shareholders of CeltiC Inns Ltd on its sale to W&DB | Gambit Corporate Finance acted as lead advisor to the management of LION QUAYS WATERSIDE RESORT, MoretonPark on its management buy-out with funding from Rcapital | Gambit Corporate Finance acted as lead advisor to bluestone national park resort on its fundraising from MANSFORD, RBS, FINANCE WALES CYLLID CYMRU | Gambit Corporate Finance acted as lead advisor to CeltiC Inns Ltd on its acquisition of the pub estate of TOMOS WATKIN |
| CFI acted as lead advisor to BURGER KING BK SPAIN on its acquisition of MEGA FOOD From dianacapital GED | CFI acted as lead advisor to Sportfood Alimentando Paixões on its capital raise from Redoma Capital | CFI acted as lead advisor to groupebertrand on its acquisition of Frères Blanc | CFI acted as lead advisor to ProA CAPITAL on its minority investment in GALLO | CFI acted as lead advisor to bento SUSHI on its sale to an investor group |

# Contact Details

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