



# Food for thought

UAE 2018 Food & Beverage report



#FoodandBeverage

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# From the chef's table

**This is the fourth edition of our annual series which examines the Food & Beverage industry in the United Arab Emirates**

This is the fourth edition of our annual series which examines the current state of the United Arab Emirates (UAE) Food & Beverage (F&B) industry. Over the past few years, we have been overwhelmed by the interest and response we have received for our work. With each year's report, our endeavor is to listen to the voice of the industry, analyze upcoming trends and address some of the challenges faced by owners and operators. Analyzing financial and operational benchmarks for various segments within the sector—which we did for the first time in our 2017 report—is one such example. This year, we have broadened and deepened our coverage of these benchmarks, with an increased number of F&B operators sharing relevant information with us.

The key theme of this year's report is the challenging times facing the industry, which in a way is a continuation of what we saw last year. Operators are struggling to maintain topline numbers and achieve like-for-like growth in the face of increased competition and comparatively subdued consumer sentiment. Many have reacted by optimizing operations and costs to maintain margins, closely reviewing and adjusting their portfolios and opting to exit loss-making outlets and struggling brands.

The medium term outlook for the sector, however, remains cautiously optimistic. As we move into 2019, there is increased expectancy around Expo 2020 Dubai. The mega event will place the UAE center stage in the world, and will likely attract a greater number of international visitors. With this in mind, we have examined the expected impact of the event on the F&B industry and operators' projected plans.

In addition, we have probed deeper into the dynamics of the delivery business, which has witnessed year-on-year growth. This 'deliverution' (or delivery-led revolution) is a trend that is set to grow and operators are looking to capitalize on advances. Rental kitchens, for example, are one of the many ways in which business models are being influenced today.

Our 2018 report is focused on understanding the market and its developments from the operators' perspective as our past experience indicates that consumer behavior does not change dramatically in the short term.

We would like to extend our heartfelt thanks to all the operators who voluntarily shared insights and information with us – you help to make our report richer and more relevant every year.

I hope you find the publication useful and would be delighted to hear your feedback.



**Anurag Bajpai**  
Partner | Head of Retail  
KPMG Lower Gulf Limited

# Antipasti

## We examine the current state of the UAE's F&B market and understand the interplay of demand and supply dynamics

The UAE continues to lead the Food & Beverage market in the Middle East region, aided by an increasing number of tourists. According to a recent MasterCard study<sup>1</sup>, Dubai is ranked fourth in terms of international overnight visitors. According to the same study, Dubai placed first with respect to overnight visitor spend per day. The emirate also has the highest expected growth in overnight visitors.

Sector growth is also supported by the ongoing entry of new international and regional brands. The restaurant footprint<sup>2</sup> in Dubai remains high, second only to that of Paris. Based on an expected increase of retail gross leasable area (GLA) in the coming years, this is likely to increase.



### 2017 international overnight visitors and average spend for major global cities<sup>3</sup>

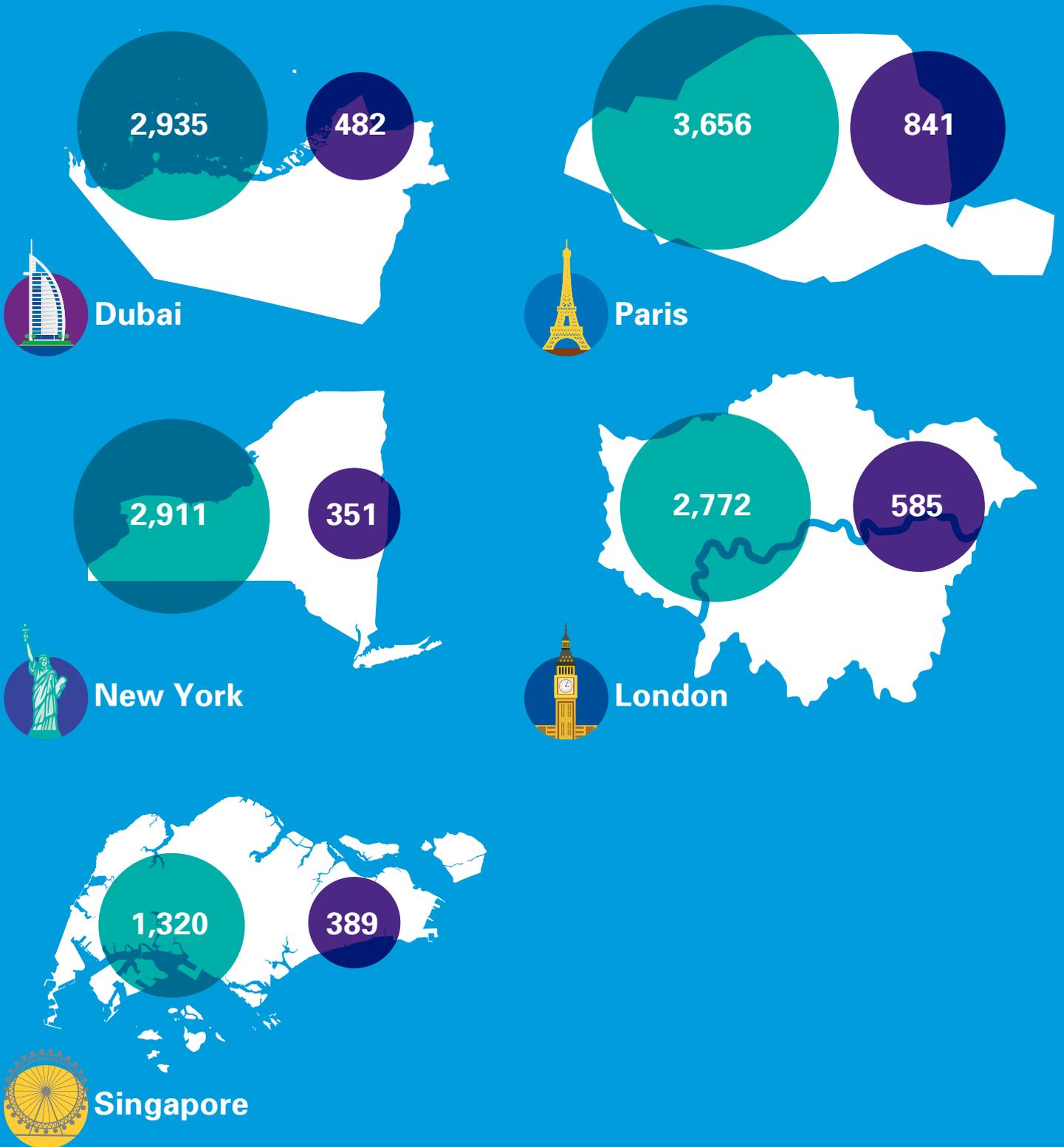
|   | 2017 international overnight visitors (millions) | Growth forecast for 2018 | Average length of stay | Average spend per day (USD) |
|---|--|--------------------------|------------------------|-----------------------------|
|  <b>London</b>    | 19.8   | 3.0%                     | 5.8 nights             | \$153                       |
|  <b>Paris</b>     | 17.4   | 2.9%                     | 2.5 nights             | \$301                       |
|  <b>Dubai</b>     | 15.8   | 5.5%                     | 3.5 nights             | \$537                       |
|  <b>Singapore</b> | 13.9   | 4.0%                     | 4.3 nights             | \$286                       |
|  <b>New York</b>  | 13.1   | 4.1%                     | 8.3 nights             | \$147                       |

1. Mastercard's Global Destination Cities Index (GDCI) 2018

2. Footprint is calculated according to the number of restaurants per million residents or per million residents and overnight visitors

3. According to MasterCard GDCI 2018, Bangkok is ranked first in terms of international overnight visitors. The other cities presented in our analysis are in the order of their rankings

Restaurants footprint – Dubai vs. major global cities<sup>4</sup>



Light blue circle: Restaurant footprint (residents)  
Dubai vs. major global destinations

Dark blue circle: Restaurant footprint (residents & overnight visitors)  
Dubai vs. major global destinations

4. United Nations, World Cities Culture Forum, Singapore Department of Statistic, City food authority websites

### A problem of plenty

Given subdued economic growth<sup>5</sup> in the GCC region, increased competition has affected the performance of many major F&B operators and businesses. Seven out of ten operators we spoke to noted declining like-for-like (LFL) sales, while nearly one in three operators witnessed double digit decline.

Margins are waning, the sector is experiencing unprecedented churn and those seeking to enter the market with new concepts are finding it increasingly difficult to sustain. Approximately 70% of operators we met do not see this changing in 2019. After an equally challenging 2016 and 2017, these are trying times for the F&B industry.



### How has your F&B business performed over the last 12 months?



29%

Substantial LFL decline  
(>10%)



42%

Minor LFL decline  
(<10%)



8%

Remained unchanged



21%

Minor LFL growth  
(<10%)



### What is your growth outlook for the next 12 months?



8%

Substantial LFL decline  
(>10%)



29%

Minor LFL decline  
(<10%)



34%

Remained unchanged



29%

Minor LFL growth  
(<10%)

### And plenty of challenges

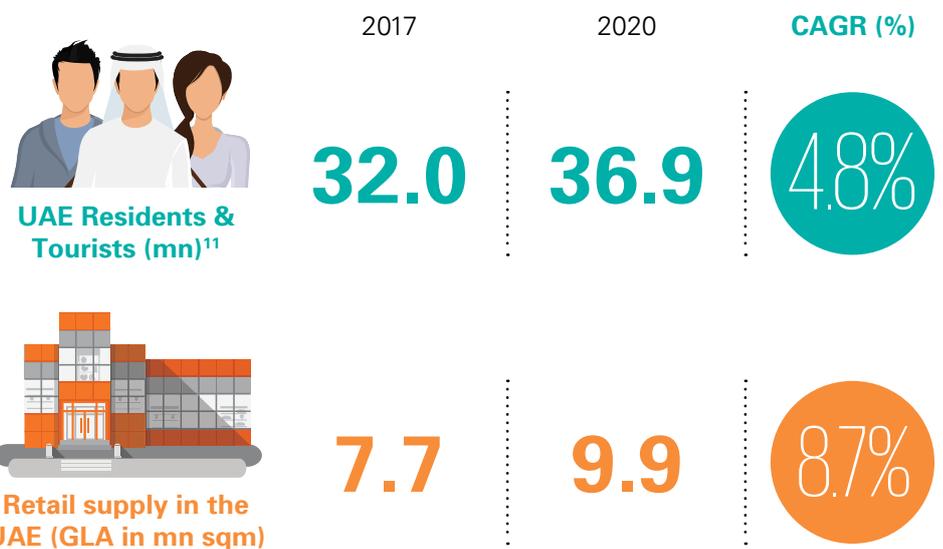
The UAE market is exemplified by a high supply of retail GLA. Retail space is expected to increase at an annual rate of 8.7%, growing from 7.7 million sqm in 2017 to 9.9 million sqm by 2020<sup>6</sup>. According to those in the industry whom we interviewed, F&B comprises a rising percentage of the retail mix for many recently launched and upcoming retail destinations. These two factors combined may result in increased competition—a potential concern for all operators.

F&B spending has also been impacted by changing demographics. While tourist arrivals to Dubai have increased at an annual rate of 6.7% between 2014 and 2017<sup>7</sup>, the increase has been primarily from Asian markets. These visitors tend to seek a budget-friendly experience and often gravitate towards more familiar cuisines. The increase in tourist numbers from other GCC markets and the West—visitors whose F&B spends are generally higher—has been relatively modest. While there are no official statistics available, industry stakeholders have indicated that there has been a similar shift in resident expatriate demographics.

Consumer spends have also been affected by various geopolitical and economic factors, for example comparatively low oil prices, a stronger dollar and modest GDP growth. In the short to medium term, these factors have resulted in subdued consumer confidence. While we have witnessed an uptick in confidence since Q1 2018<sup>8</sup>, our findings suggest that this has yet to trickle down to the local F&B sector.

### Tourist arrivals by top source markets (in '000s) – Dubai (2014 vs. 2017)<sup>9</sup>

|   | 2014  | 2017  | Change | Change % |
|---|-------|-------|--------|----------|
| <b>GCC</b>                                | 2,744 | 2,793 | 49     | 2%       |
| <b>Europe &amp; Americas<sup>10</sup></b> | 2,646 | 3,058 | 412    | 16%      |
| <b>India</b>                              | 1,272 | 2,073 | 801    | 63%      |
| <b>China</b>                              | 350   | 764   | 414    | 118%     |
| <b>Russia</b>                             | 420   | 530   | 110    | 26%      |



6. JLL Real Estate Market Overview- Dubai - Q1 2018, JLL's 2017 Year in Review report for UAE

7. Dubai Statistics Center

8. <https://tradingeconomics.com/united-arab-emirates/consumer-confidence/> Nielsen

9. Dubai Statistics Center

10. Includes only top source markets in Europe & Americas

11. Euromonitor, World Bank

### The times they are a-changin'

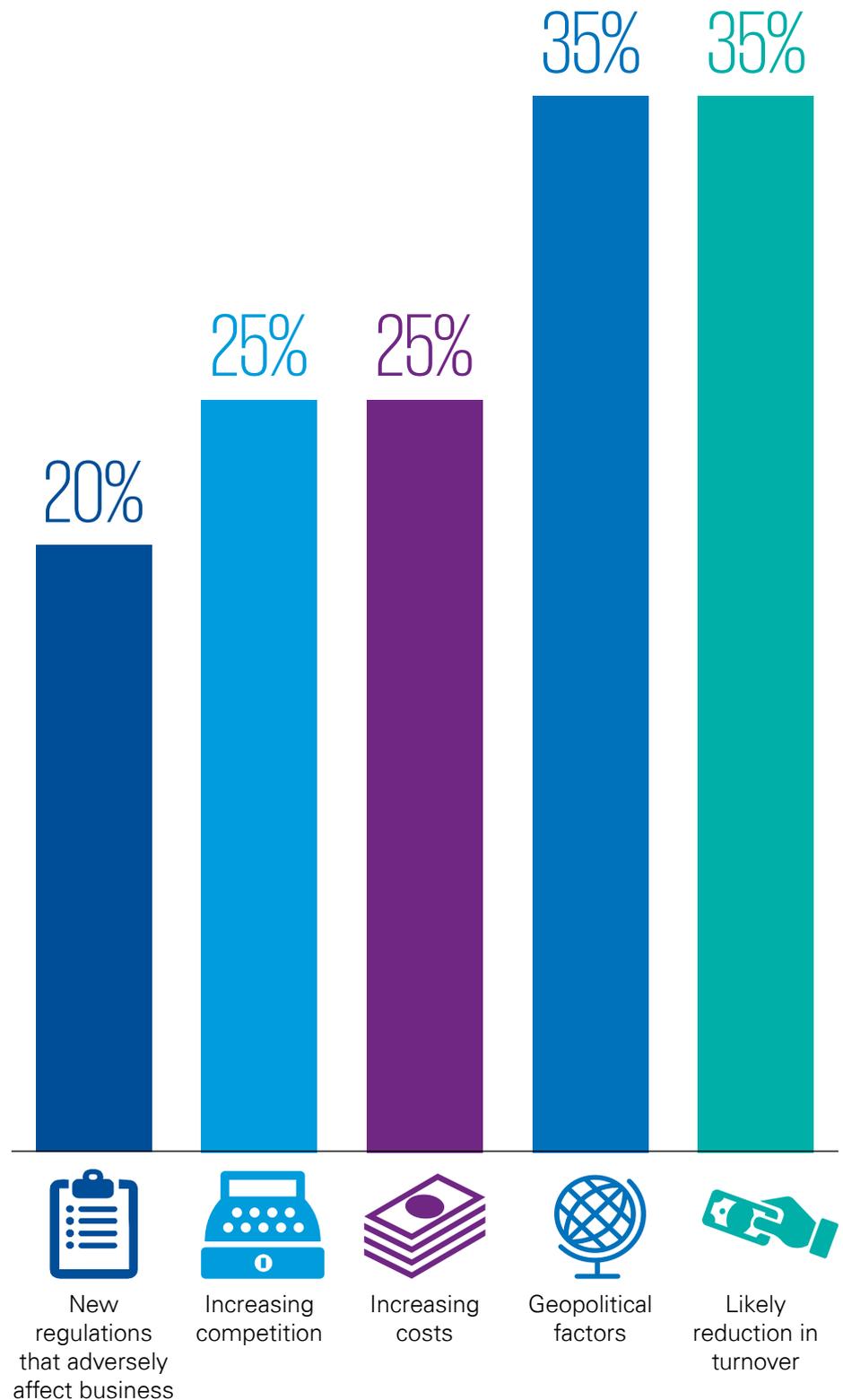
The F&B market is extremely dynamic, with increasingly discerning consumers. Some F&B businesses have been forced to make tough—though much-needed—decisions, for example to close poorer performing outlets, and some have exited brands which struggled in the local market. While restaurateurs have worked to improve certain aspects of their operations over the last several years, it seems this may be the time for them to take a 360-degree look at their business: from relevance of the concept in the market, to operational agility, to support function efficiency, and result-driven financial monitoring.

Many operators also expressed apprehension about other external factors. The cost of doing business in the UAE (as discussed on page 20) has been on the rise over the past few years and, in spite of ongoing cost optimization initiatives, F&B businesses have struggled to maintain margins. Compared with last year, geopolitics has become an area of increasing concern among operators.

While competition is generally considered good for the market, ensuring operators do not become complacent, the pace of F&B outlet openings and closures has been hectic recently. With a shorter average brand lifecycle and increasing operational costs, the economics of F&B businesses are being put to the test.



### What are your most pressing concerns over the next 12 months?



Multiple Choice Question

### VAT happened to my check

Value added tax (VAT) was introduced in the UAE on 1 January 2018. Most F&B operators, like other retail businesses, were generally well prepared for implementation, making changes to back-end billing, reporting systems and pricing strategies, as relevant.

In this context, creating a pricing strategy was—and continues to be—a key focus for operators.

The regulation requires all publicly displayed prices to be inclusive of VAT. While prices therefore required recalibration, operators had to manage this in a way that did not affect already pressurized sales.

Within the F&B industry, changes were primarily addressed through repricing and other strategies, such as combo offers and menu refreshes. While some revised prices in late 2017 and early 2018, others absorbed VAT costs during initial implementation.

For some operators, it seems repricing may have had a positive impact on their top line.

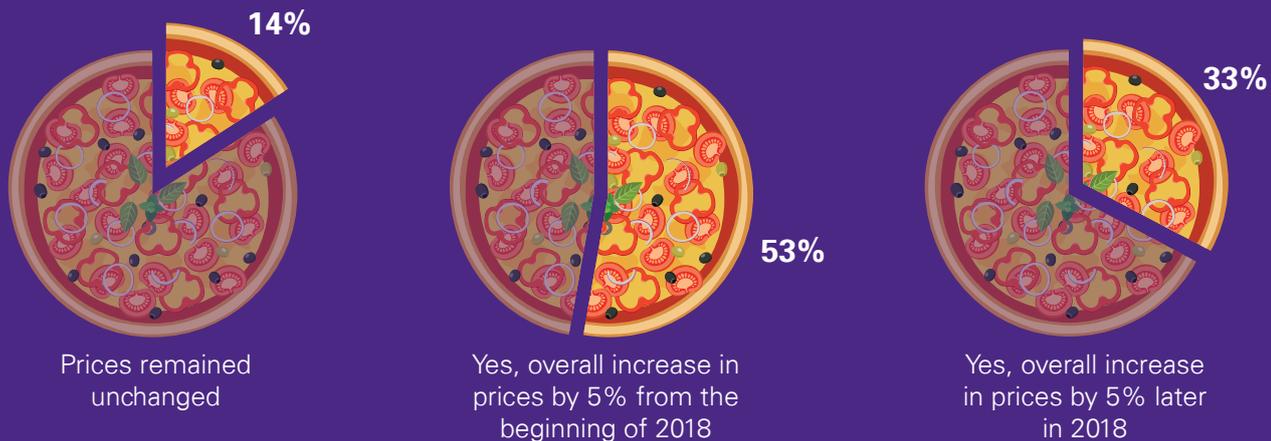
Per last year's report, the introduction of VAT (at a rate of 5%) was expected to have a limited, one-time impact among consumers in early 2018. After initial implementation,

consumers were anticipated to adjust to the new reality. In line with these expectations, half of the operators surveyed reported a decline in turnover in early 2018, mainly attributed to VAT. However, it is difficult to untangle the impact of VAT from other factors, such as subdued consumer sentiment and the earlier introduction of excise duty, which affected sales of certain beverages and tobacco products.

Despite an initial downturn, operators believe consumer sentiment is no longer noticeably influenced by VAT.



### Price changes in the last 12 months



### Impact of price changes on turnover



# Expo 2020 Dubai



The Expo 2020 Dubai site will feature more than 200 F&B outlets and 30,000 sqm of front-of-house space



AED 2 billion in F&B sales expected onsite during the event, with up to 85,000 meals served per hour at its peak



With a combination of franchises, new experiences and home-grown brands, Expo 2020 Dubai aims to allocate 20% of its F&B outlets to small- and medium-sized enterprises



Approximately 25% of F&B outlets at Expo 2020 Dubai will offer sit-down dining experiences (both premium and premium casual), while the remainder will provide faster services (snacks, impulse offerings, etc.)



Up to 20% of space within country pavilions may be allocated for commercial (retail and F&B) purposes



Per sqm trading volumes for F&B outlets at Expo 2020 Dubai are projected to be substantially higher than other locations in Dubai, due to increased footfall and dwell times



Between 10% and 15% of F&B outlets will remain after the Expo 2020 Dubai as part of District 2020, a mixed use residential and commercial community at the site

Source: Expo 2020 Dubai

## The big impact

Expo 2020 Dubai, the first World Expo to take place in the Middle East, Africa or South Asia region, opens on 20 October 2020. It will be a six month global event attracting countries, companies, decision-makers and tourists from around the world. Accordingly, local F&B businesses have been gearing up for this much-anticipated event.

Three out of four operators believe Expo 2020 Dubai will have a favorable impact and the event has the potential to provide a much-needed fillip to the industry.



## How is Expo 2020 Dubai expected to impact F&B industry?



15%

Highly favorable impact (>10% growth)



60%

Favorable impact (<10% growth)



25%

Not much impact

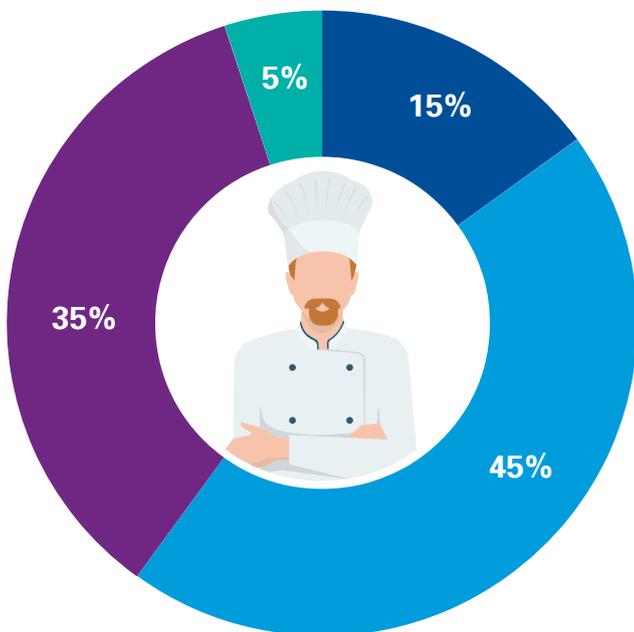
While 60% of operators expect a directly favorable impact to their businesses, some have a different view. Those who believed there would be little direct positive impact on Dubai's F&B sector mentioned that most of the activity will be in and around the event site. Some operators stated that the Expo 2020 Dubai may draw tourists away from existing F&B destinations in the UAE.

While Expo 2020 Dubai is just under two years away, more than one third of operators plan to directly participate, by establishing a presence at the site. An additional 20% are considering options for event-related campaigns to take advantage of the increased number of tourists in the city.

The remaining 45% of operators have not made event-specific plans as yet, but this may change in the interim. However, for most, the priority for 2019 is to set the house in order.



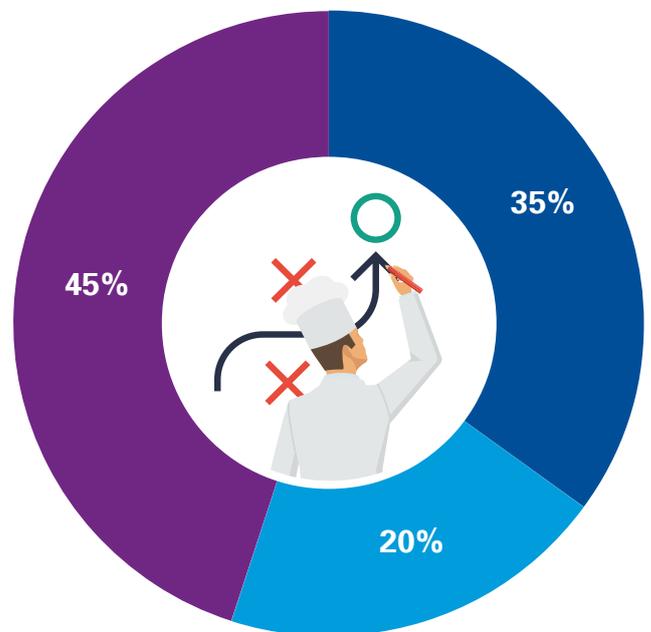
### How is Expo 2020 Dubai expected to impact your business?



- Highly favorable impact (>10% growth)
- Favorable impact (<10% growth)
- Not much impact from Expo
- Unfavorable impact



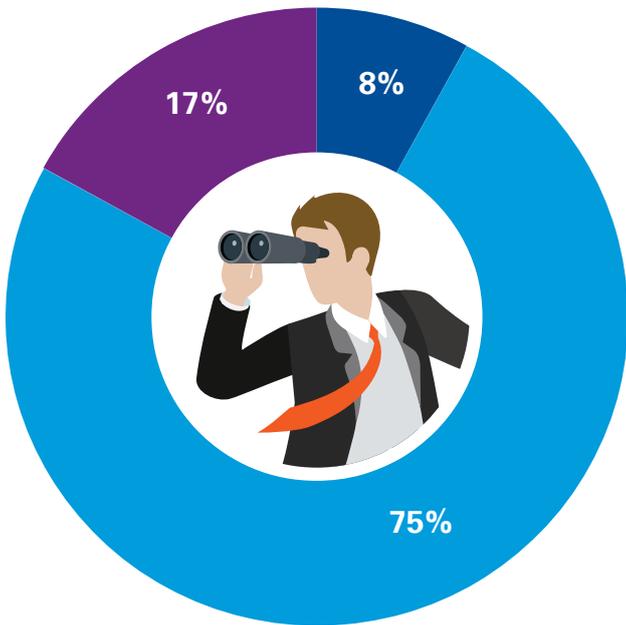
### What are your plans around Expo 2020 Dubai?



- Direct participation
- Expo-specific campaigns
- No specific plans as yet



### What is your medium term outlook for the F&B sector?



- High growth (>10% y-o-y)
- Low to moderate growth (<10% y-o-y)
- Low to moderate decline (<10% y-o-y)

### Creating the future

There seems to be a general consensus in the market that 2019 will continue to be challenging for the sector. Operators are, however, optimistic in the run up to Expo 2020 Dubai and are gearing up to revitalize sales. Although hopeful, some operators expressed concern that the positive impact may be limited to the duration of the event. But this does not deter F&B businesses from continuing to invest in future growth and the nature of investments seem to be changing. In 2017, attention was focused on expansion into new markets and geographies. Today, while the search for the next big opportunity—either in the form of a new market or a new brand—continues, many investments are aimed at operational improvements and local expansion of the winners in their existing portfolios. This is likely to continue in 2019 as well.

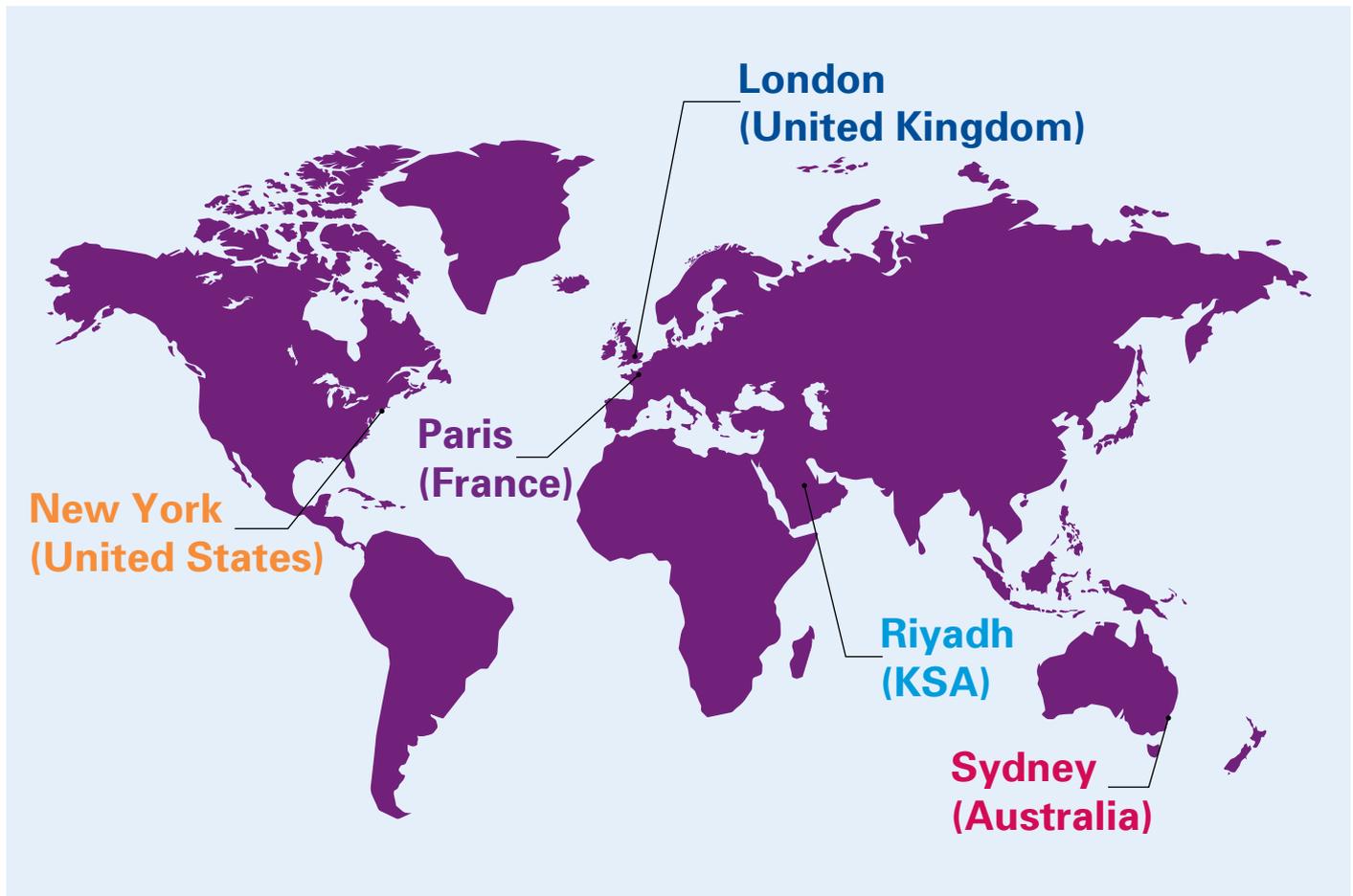


### Where are you looking to invest in the medium term?



Multiple Choice Question

## Preferred markets for international expansion



Given the market situation, many operators are taking a conservative approach to regional expansion and seem to be prioritizing stabilization within the UAE. Furthermore, some operators are now considering expansion into markets further afield. We may see this play out in the next few years, but for now the United Arab Emirates remains center stage for locally-based F&B businesses.



### KPMG view

Although the UAE market continues to gain prominence as a global F&B destination, increased competition and declining LFL sales are major concerns for operators. Given the cost of doing business in the UAE and the impact of the macro-economic environment on consumer confidence, the market may remain challenging in the coming year.

This is the time for operators to take a hard look at their portfolios and business models. While some have already begun this journey, there is no denying that it will require preparation to withstand the challenging times ahead. With the shifting market dynamics, this may be an ideal time for F&B businesses to undertake a more comprehensive, outside-in examination of what works and what does not.

Despite current market conditions, operators are optimistic about the impact of Expo 2020 Dubai on the F&B industry and some have already drawn their plans for the mega event. For now, Expo 2020 Dubai is one of the positives for the industry to cheer about.

# Specialties

## We look at what works in terms of formats and cuisines and how various formats have fared in the UAE in 2018

### Drive to value

Challenging market conditions and subdued sentiment have driven value-seeking behavior among consumers. As a result, quick-service restaurants (QSRs) have become more popular and appear to be faring better than other formats.

Furthermore, operators suggest that known brands and chains seem to be performing better than homegrown concepts—especially in the QSR and café segments.

We see both casual and premium casual offerings being more affected than other segments. Also noteworthy, premium outlets have witnessed a decline in diners and average ticket sizes. In a number of cases, this was attributed to a reduction in beverage spend.

Additionally, as fine dining and premium casual outlets seek to establish offerings which will attract and retain customers, the line between the two segments is beginning to blur.



| Formats  | What operators are saying   |
|--|---|
| <b>QSR/fast food</b><br>  | <ul style="list-style-type: none"> <li>– Doing well; it benefits from value-seeking consumer behavior</li> <li>– ‘Grab-n-go’ concepts suited for delivery are doing well</li> <li>– Health-conscious eating trends may prompt changes to QSR offerings in the future; currently they do not see a significant impact</li> </ul>   |
| <b>Café</b><br>           | <ul style="list-style-type: none"> <li>– Along with QSRs, cafés continue to be one of the most popular formats</li> <li>– While the segment is overcrowded, international chains and established brands seem to fare better than homegrown concepts</li> <li>– Innovation and differentiation will be key to cafés’ success</li> </ul>  |
| <b>Casual dining</b><br>  | <ul style="list-style-type: none"> <li>– Casual dining has been impacted by the downturn in the industry; footfall and ticket sizes have reduced</li> <li>– Well-executed concepts in the right location still do well, but growth has been a challenge</li> <li>– Increased variety in cuisine options has led to greater competition and a need for differentiation</li> </ul>  |
| <b>Premium dining</b><br> | <ul style="list-style-type: none"> <li>– Number of outlets have witnessed declining footfalls; however, relatively steady patronage for certain popular brands and concepts. Ticket sizes have dropped</li> <li>– Hotel-based, premium, licensed offerings face increased competition from licensed non-hotel outlets</li> <li>– Experiential and traditional ethnic offerings appear to be working better in the market</li> </ul> |

**What's recommended?**

Over the years, the UAE has become a melting pot of ethnicities, culminating in the globally-attuned F&B destination we see today.

Despite the wide variety of available cuisines, top preferences have remained largely consistent over the years and somewhat reflective of the UAE demographics. That said, interesting trends have emerged over the last year: veganism is on the rise and the popularity of East Asian food is expanding beyond Japanese and Chinese offerings. Last but not least, Emirati fare is also gaining popularity. Accordingly, many operators are aligning current and future offerings with these developing trends.



**Popular cuisines (according to operators)**

Arabic



Indian



Italian



Japanese



American





## Cuisines - what operators are saying



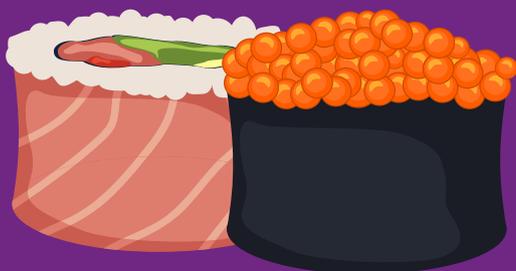
### Seemingly same top preferences

- Arabic and Indian flavors continue to be top choices. Italian is second choice to home-country cuisine for many UAE residents.
- In last year's report, we mentioned that consumers may be more adventurous, but their top choices seldom change. It is not surprising therefore to see some operators exploring gaps in their portfolio around these preferred cuisines.



### Healthy eating vs. guilty pleasure – a tale of two halves

- UAE consumers generally appear to love burgers, pizzas, fried chicken, as well as sugar- and chocolate-based offerings. However, increasing awareness about health has led some to reduce or give up meat, gluten and milk products. Multiple operators indicated a noticeable increase in vegetarian and vegan options.
- Despite a visible change in consumption patterns, the shift toward healthier food options is gradual and the market seemingly continues to be dominated by calorie-rich offerings.



### Asian continues to expand as consumers take notice of Emirati flavors

- Asian—primarily Japanese, Chinese and Thai—cuisines have been amongst the top choices in the UAE for several years. While these continue to be popular, operators see potential in expanding upon this and experimenting with other Asian flavors. Vietnamese and Korean food is expected to see greater acceptance in the future.
- Similarly, there has been a rise in the popularity of Emirati flavors, as expatriates and tourists look to experiment with local cuisine.



### Delivery-friendly food will grow

- With the rising importance of delivery in the F&B sector, many operators believe that foods which are more delivery-friendly will do better.
- In parallel, operators are exploring ways in which their offerings can be adapted to cater for delivery.

## Edible economics

Similar to last year, we examined the economics of various formats, including cafés, to see how each has fared across a range of relevant financial and operational metrics.

The success of any F&B outlet is determined by how well it is able to increase or maintain its topline and control costs. The wide ranges observed with respect to the number of transactions and average ticket size (among other metrics) provide a sense of fluctuating performance within each format—one characteristic of the market today.

While revenues have generally remained flat or reduced, some operators have managed to maintain or reduce costs, resulting in relatively stable margins.

Food costs are variable in nature. Any reduction has a direct bearing on outlet, or brand-level, margins. Rental and staff expenses, on the other hand, are largely fixed and movement in these outlays impact the operational leverage of the business (i.e. number of transactions needed to break-even at the outlet level). To date, operators have been able to manage their staffing numbers, and consequently staff costs. However, they are concerned about rentals—particularly in prime locations across the UAE.

Given the impact of rental cost on the economics and profitability of F&B businesses, it is the single most important line item for operators. Experience in managing this has varied: while some have succeeded in negotiating favorable terms with landlords, others have struggled to do so, and have sometimes ended with closures. That said, closing down an outlet is an expensive proposition, as well. As a result, business cases for new openings are carefully evaluated these days.



|                                  |                             |
|----------------------------------|-----------------------------|
| # of transactions                | <b>8k to 25k per month</b>  |
| Average ticket size (AED)        | <b>25-50</b>                |
| Beverage sales % of total sales  | <b>25-35%</b>               |
| Food cost % of revenue           | <b>20-35%</b>               |
| Rentals % of revenue             | <b>10-25%</b>               |
| Staff cost % of revenue          | <b>15-23%</b>               |
| Marketing cost % of revenue      | <b>1-5%</b>                 |
| Margins % of revenue             | <b>5-12%</b>                |
| <hr/>                            |                             |
| Average space per outlet sq. ft. | <b>800-1,800</b>            |
| Average number of staff          | <b>30-50</b>                |
| <hr/>                            |                             |
| Revenue/sq. ft. AED              | <b>200 to 450 per month</b> |
| Revenue/staff AED                | <b>12k to 25k per month</b> |



|                                  |                             |
|----------------------------------|-----------------------------|
| # of transactions                | <b>6k to 13k per month</b>  |
| Average ticket size (AED)        | <b>25-90</b>                |
| Beverage sales % of total sales  | <b>70-85%</b>               |
| Food cost % of revenue           | <b>17-26%</b>               |
| Rentals % of revenue             | <b>9-30%</b>                |
| Staff cost % of revenue          | <b>15-35%</b>               |
| Marketing cost % of revenue      | <b>1-4%</b>                 |
| Margins % of revenue             | <b>5-20%</b>                |
| <hr/>                            |                             |
| Average space per outlet sq. ft. | <b>1,000-6,000</b>          |
| Average number of staff          | <b>6-20</b>                 |
| <hr/>                            |                             |
| Revenue/sq. ft. AED              | <b>100 to 250 per month</b> |
| Revenue/staff AED                | <b>20k to 40k per month</b> |



## Casual

|                                 |                            |
|---------------------------------|----------------------------|
| # of transactions               | <b>4k to 15k per month</b> |
| Average ticket size (AED)       | <b>70-175</b>              |
| Beverage sales % of total sales | <b>5-20%</b>               |
| Food cost % of revenue          | <b>20-30%</b>              |
| Rentals % of revenue            | <b>7-30%</b>               |
| Staff cost % of revenue         | <b>17-30%</b>              |
| Marketing cost % of revenue     | <b>1-3%</b>                |
| Margins % of revenue            | <b>8-22%</b>               |

|                                  |                    |
|----------------------------------|--------------------|
| Average space per outlet sq. ft. | <b>2,500-7,000</b> |
| Average number of staff          | <b>15-35</b>       |

|                     |                             |
|---------------------|-----------------------------|
| Revenue/sq. ft. AED | <b>130 to 500 per month</b> |
| Revenue/staff AED   | <b>13k to 25k per month</b> |



## Premium dining (without license)

|                                 |                            |
|---------------------------------|----------------------------|
| # of transactions               | <b>3k to 11k per month</b> |
| Average ticket size (AED)       | <b>120-240</b>             |
| Beverage sales % of total sales | <b>15-40%</b>              |
| Food cost % of revenue          | <b>15-35%</b>              |
| Rentals % of revenue            | <b>10-25%</b>              |
| Staff cost % of revenue         | <b>20-35%</b>              |
| Marketing cost % of revenue     | <b>1-2%</b>                |
| Margins % of revenue            | <b>8-30%</b>               |

|                                  |                    |
|----------------------------------|--------------------|
| Average space per outlet sq. ft. | <b>3,000-9,000</b> |
| Average number of staff          | <b>40-100</b>      |

|                     |                             |
|---------------------|-----------------------------|
| Revenue/sq. ft. AED | <b>175 to 375 per month</b> |
| Revenue/staff AED   | <b>10k to 30k per month</b> |



## Premium dining (with license)

|                                 |                            |
|---------------------------------|----------------------------|
| # of transactions               | <b>3k to 10k per month</b> |
| Average ticket size (AED)       | <b>200-750</b>             |
| Beverage sales % of total sales | <b>30-60%</b>              |
| Food cost % of revenue          | <b>20-35%</b>              |
| Rentals % of revenue            | <b>0-20%*</b>              |
| Staff cost % of revenue         | <b>15-25%</b>              |
| Marketing cost % of revenue     | <b>1-3%</b>                |
| Margins % of revenue            | <b>10-30%</b>              |

|                                  |                     |
|----------------------------------|---------------------|
| Average space per outlet sq. ft. | <b>3,000-13,000</b> |
| Average number of staff          | <b>45-125</b>       |

|                     |                             |
|---------------------|-----------------------------|
| Revenue/sq. ft. AED | <b>200 to 500 per month</b> |
| Revenue/staff AED   | <b>12k to 45k per month</b> |

\* Premium dining with license includes hotel-based F&B, where rental cost is not allocated separately to the outlet

# A perspective on the costs in the retail sector

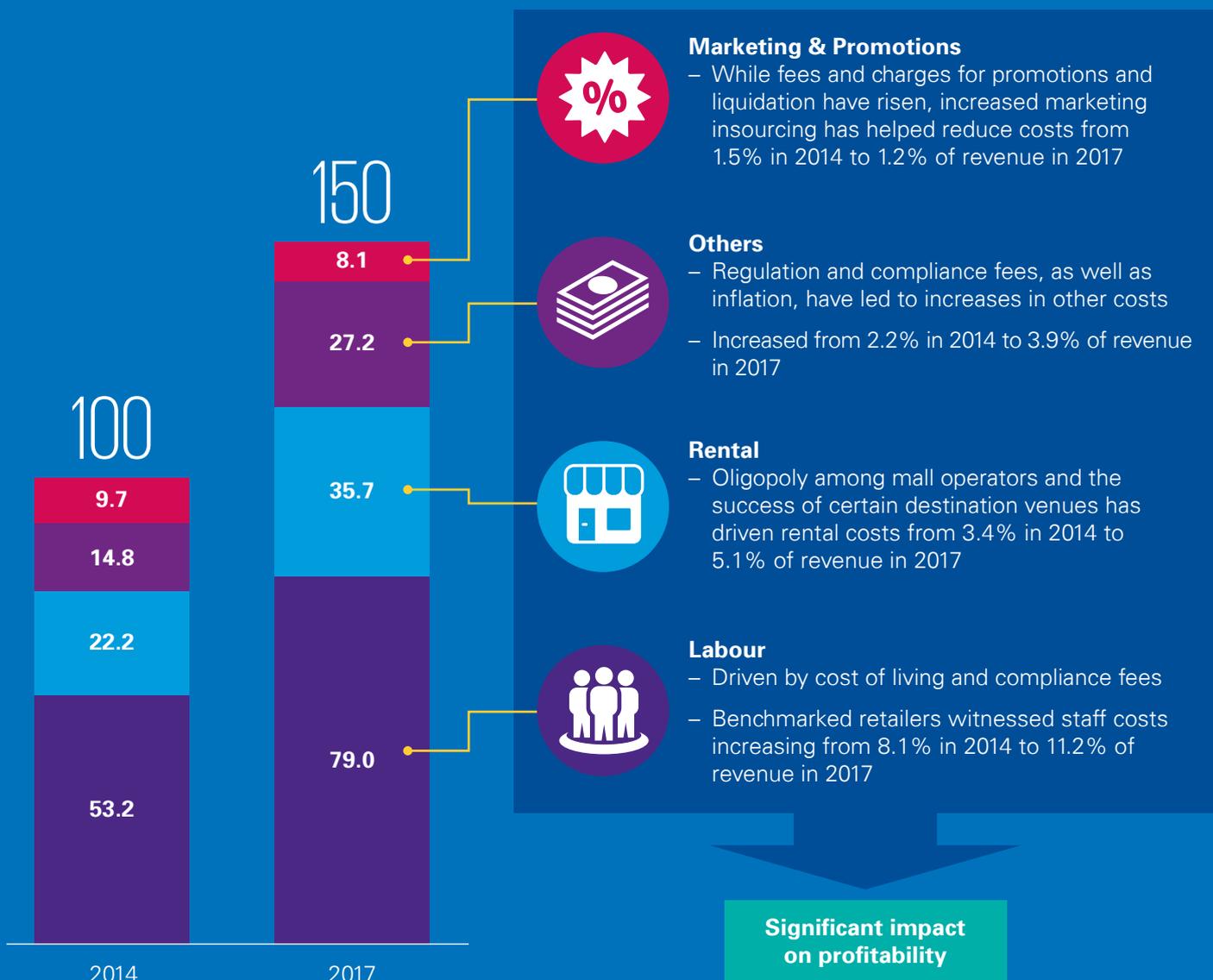
Increasing costs for F&B businesses were a key element of feedback from many operators. We looked at a cross-section of prominent retail businesses in the UAE (several operate in the F&B space) in order to assess trends in the major cost components over a four-year

period. The year 2014 was chosen as the base year for indexing and assessing changes in costs through to 2017.

Trends support operators' views around rising costs over this period: operational outlays in the UAE's retail

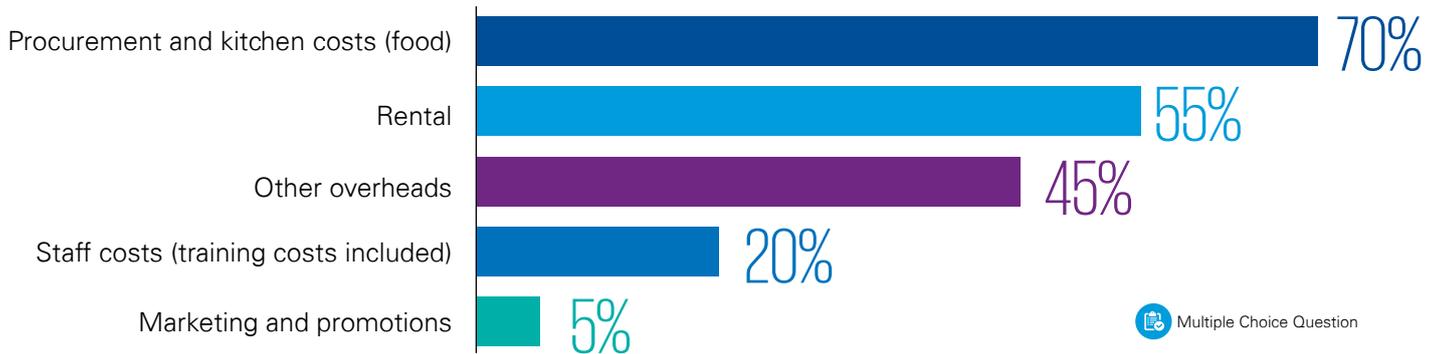
sector have increased by 50% with staff costs and rentals being the key drivers. Marketing and promotional costs have marginally declined, as retail businesses look to manage these activities in-house.

## Key operational cost index (base year 2014 = 100)





## What are the key areas of cost optimization for your business?



Multiple Choice Question

### Managing margins

Cost optimization and operational improvement continues to be top of mind for operators. In today's market, managing costs has become top priority. The true test is managing costs without affecting food quality or customer experience.

Operators are constantly on the lookout for better quality and lower cost products: the right procurement plan improves the bottom line. While there is a risk of focusing solely on cost reduction, many operators seem to be agile in navigating deals with vendors to manage costs.

Beverage sales are an important component of F&B revenue. It not only adds to overall returns but also tends to offer higher margins. Cafés and licensed outlets therefore benefit more than others from beverage sales.

Rentals have been a major focus and cause of concern. Due in part to increased competition and changing consumption patterns, many operators do not see the same outlet-level activity as they did in the past. Unfortunately, this is not reflected in rental costs—particularly in prime locations. Operators are also increasingly re-evaluating the size of their outlet(s) and revenue per sq. ft. is closely tracked—larger 'boxes' are only being considered if they add significantly to the concept and revenue potential. Furthermore, operators are hopeful that commercial rental regulations will be introduced in the coming

years to address concerns around rental transparency, escalations and other charges/fees.

Staffing is key, as a restaurant's success is largely dependent on service levels. While operators have optimized employment to some extent, they have been careful not to make drastic changes. The challenges around skill gaps and lack of staffing solutions on an hourly basis limit the opportunity to optimize through temporary staffing, unlike other global F&B destinations.

Overhead costs have been another key area for optimization. Marketing budgets have taken a hit, and businesses have sought to manage activities internally. Additionally, it is widely understood that the UAE has one of the highest credit and debit card transaction fees globally; several businesses expect the government to take steps to lessen the burden of such transaction fees.

Corporate overheads are also being revisited, leading to leaner operating structures, and overheads are being reviewed based on their revenue enhancement potential.



### KPMG view

While there are opportunities across all formats, casual and premium dining seem to have been most affected by recent market conditions. That said, well-executed concepts continue to do well.

The economics of the F&B industry are being put to the test—now more than ever, as the generally subdued topline growth has increased pressure to meet bottom-line expectations. It is important for all stakeholders in the eco-system to work together to bring the F&B sector back on the growth track.

Given current market dynamics, landlords could consider the impact of rentals on F&B businesses. In the long run, this could be a win-win proposition for operators and landlords. Regulations around commercial rentals would also help to bring transparency.

Considering the seasonality, higher adoption of temporary staffing solutions could help the F&B business model. This will require concerted efforts to create a support eco-system for skill development and shorter duration outsourcing contracts.

# Hot bites

## A look at how technology is redefining business models in the F&B industry

### Cash on wheels

In our 2017 report, we examined the impact of technology—both as a disruptor and an opportunity for operators. Food delivery, one aspect of the sector most prominently affected by technology, was catching the eye of operators. The UAE's 'deliverution,' or food delivery-led revolution, has remained strong in a challenging market in 2018. This is the only segment that witnessed

significant growth, both at the industry level and as a channel for operators.

Penetration of food and delivery apps was high among businesses we spoke to in 2017 (87%) and continues to be so in 2018 (86%). With topline challenges at the store level, operators are increasingly looking to boost performance through other channels, including a presence on

multiple delivery apps. However, some fine dining restaurants believe delivery is not aligned with their offerings and are therefore not listed.

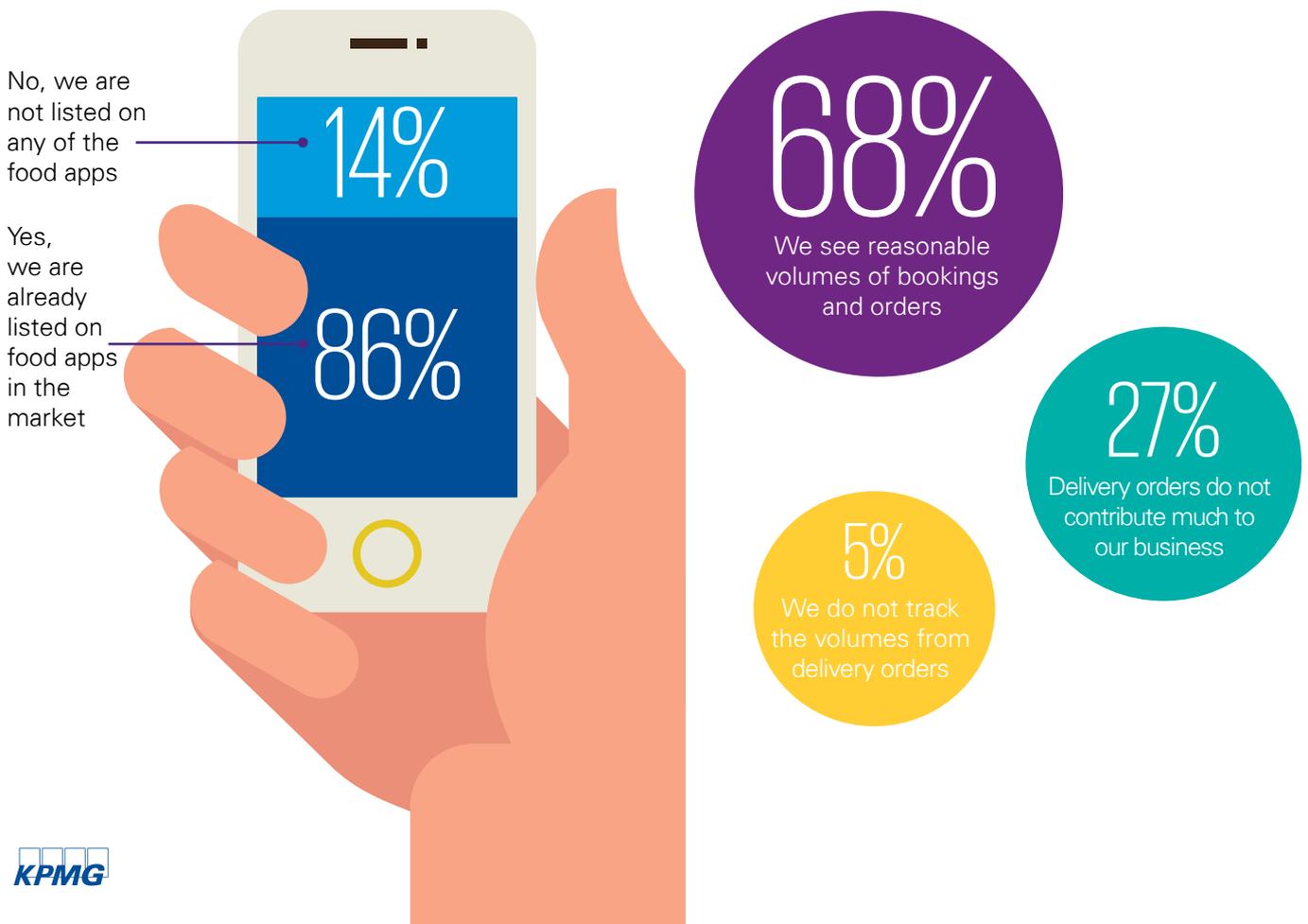
In line with 2017 findings, more than two thirds of operators see a reasonable volume of bookings and orders from delivery platforms in 2018.



Do you see value in food/delivery apps?



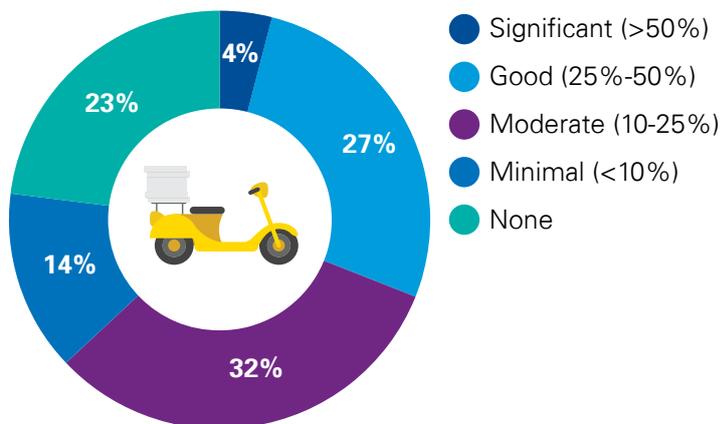
How are delivery apps affecting your business?



As a result of the growing popularity of delivery, as much as 32% of operators (versus 21% last year) attribute more than a quarter of their revenue to this channel. Furthermore, a number of operators have seen double-digit growth in their delivery business, year on year. This suggests that delivery is an increasingly vital component of the F&B business, as food-tech players and delivery platforms work to increase their presence and enhance customer experience.



### What share of your business comes from delivery?



### Experience the convergence

Technology has created a culture of convenience for today's customer—nearly everything is a few taps away. Racing for both a share of consumers' wallets and space on their mobile phones, technology players strive to improve the customer experience and battle it out to become their first choice among food apps. As a result, we are seeing a convergence of propositions that was unimaginable a few years ago.

Today, one can search and order food, ask for delivery, book seats at a restaurant and benefit from deals and promotions—all from the same app. Simultaneously, deal-based apps are offering food delivery services and pure delivery apps are enhancing the customer review process, as well as search and discovery functionality.

We believe that this trend is not only good for customers but will also position technology companies as increasingly strategic stakeholders in the F&B sector.



**Math on the go**

Even as the popularity and relevance of food delivery has increased, F&B businesses have been evaluating the economics. The channel’s impact on the topline is fairly evident—the challenge is to accurately assess implications on the bottom line.

There are two approaches to evaluating profitability. The first is a contribution-led approach. As most costs related to restaurant operations are fixed, delivery should only be assessed based on its net contribution, in other words based on revenue generated net of food costs and commission paid to the delivery partner. Hence, if the net contribution is positive—which is usually the case—the proposition is value-accretive to the restaurant.

The second approach is based on net profit generated by the food delivery business, considering its share of the costs proportional to revenue contribution. Some operators prefer to take this view, whereby the delivery side of the business will also bear its proportional share of the fixed costs: staff to prepare the food, kitchen resources and space used. While there is merit in the argument for allocation of staff costs, restaurant space is primarily created for the dine-in experience and delivery utilizes a small portion of the kitchen area.

The answer to assessing delivery economics may perhaps be a more granular approach. In this methodology, restaurants would carefully analyze and allocate individual costs to dine in and delivery segments based on appropriate metrics (for example, utilized store space, staff count), reviewing performance based on the merit of each proposition. With appropriate cost allocations and a proper evaluation of the economics, margins for delivery are likely to be in line with or better than that of outlet operations.

**Illustrative income statement for delivery for F&B operator**



|  | AED   | Share of revenue |
|--|-------|------------------|
| <b>Food cost</b><br>                          | 10    | 25%              |
| <b>Commission to delivery platform</b><br>    | 8-12  | 20-30%           |
| <b>Net contribution</b><br>                   | 18-22 | 45-55%           |
| <b>Fixed costs (staff, rentals, etc.)</b><br> | 12-16 | 30-40%           |
| <b>Net profit</b><br>                         | 2-8   | 5-20%            |

### New kitchen on the block

An extension of the value chain, delivery kitchens (also known as 'ghost kitchens' or 'rental kitchens') are a relatively new phenomenon in the UAE. They allow operators to tap into the opportunity while addressing a key pain-point: high rents in prime catchment areas.

Rental kitchens are the basic form of delivery kitchens, where a shell structure is provided to operators for delivery-only purposes. This is currently the most common model. An extension of this concept is a 'managed kitchen,' where a third-party provider manages end-to-end delivery operations.

In a short span of time, delivery kitchens have generated interest—85% of operators we spoke to believe they have potential. Twenty percent of operators currently utilize delivery kitchens, while an additional 30% are considering setting one up.

As the delivery channel continues to grow on the back of consumer demand and operator interest, increasingly efficient and cost-effective models, such as delivery kitchens, will likely find greater acceptance in the market.



### KPMG view

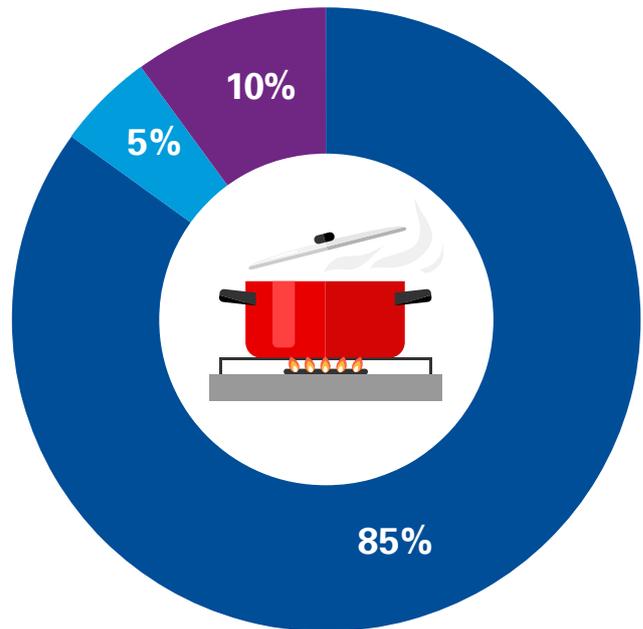
Food delivery is here to stay and seems to be an increasingly important driver of growth for F&B businesses, propelled by a variety of push and pull factors. Consumers' preference for convenience, coupled with businesses' needs for alternate channels and technological advancements, will continue to drive this shift in the F&B market.

As food delivery business grows and operators start analyzing segmental profitability, the economics of the delivery model will be assessed and tested more closely. Foodtech companies may do well to work with operators to achieve a win-win outcome. If delivery economics do not stack up, or delivery margins become tighter, it might not be long before operators start looking to other avenues for growth and profitability.

Delivery services and delivery kitchens both address a key pain-point for operators, while simultaneously providing an opportunity to get closer to customers on reasonable commercial terms. Along with food delivery platforms, delivery kitchens will contribute to the UAE F&B industry in the future.



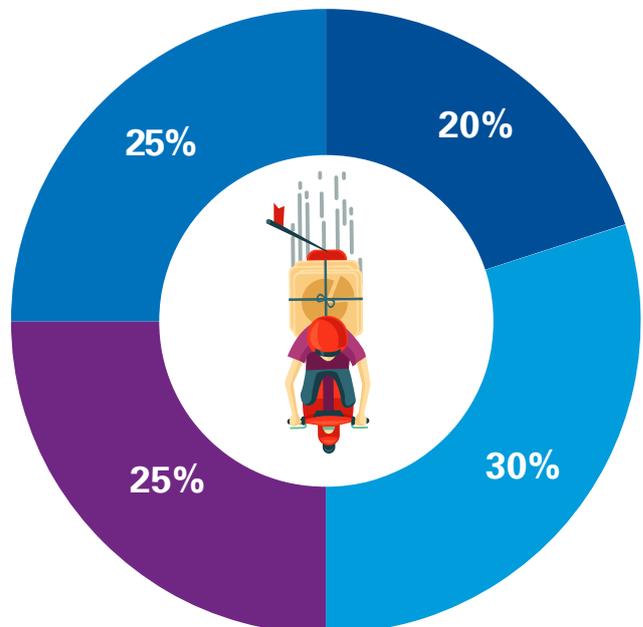
### Do you see potential in delivery kitchens?



- Yes, will become more prominent
- Yes, but will remain a niche
- The model is relatively untested



### Have you considered the delivery kitchen model?



- Present through delivery kitchens
- Currently considering this model
- Will be interested in the future
- Doesn't work for us

# Order summary

We summarize the key themes and conclusions for the F&B market in 2018



1.

## Challenging market

- Increased competition and subdued consumer spending have contributed to declining or flat same-store sales
- Rising costs are pushing operators to optimize their operations



2.

## Quick service restaurants (QSR) work

- Driven by market conditions, QSRs have outperformed other formats
- Casual and premium formats have suffered a decline in both footfall and average spends



3.

## Setting the house in order

- Operators are working on improving operational efficiency, revisiting their business strategy and, in a number of instances, rationalizing their F&B portfolio



4.

## Delivery makes further inroads

- The UAE's 'deliverution' has been one of the few areas of growth for operators
- The introduction of delivery kitchens in the UAE could further improve the delivery economics



5.

## Expo 2020

- Operators anticipate that the mega event will provide a boost to the UAE's F&B sector
- The bulk of operators have formulated plans around the event, with an intention to either participate directly and/or target visitors through campaigns

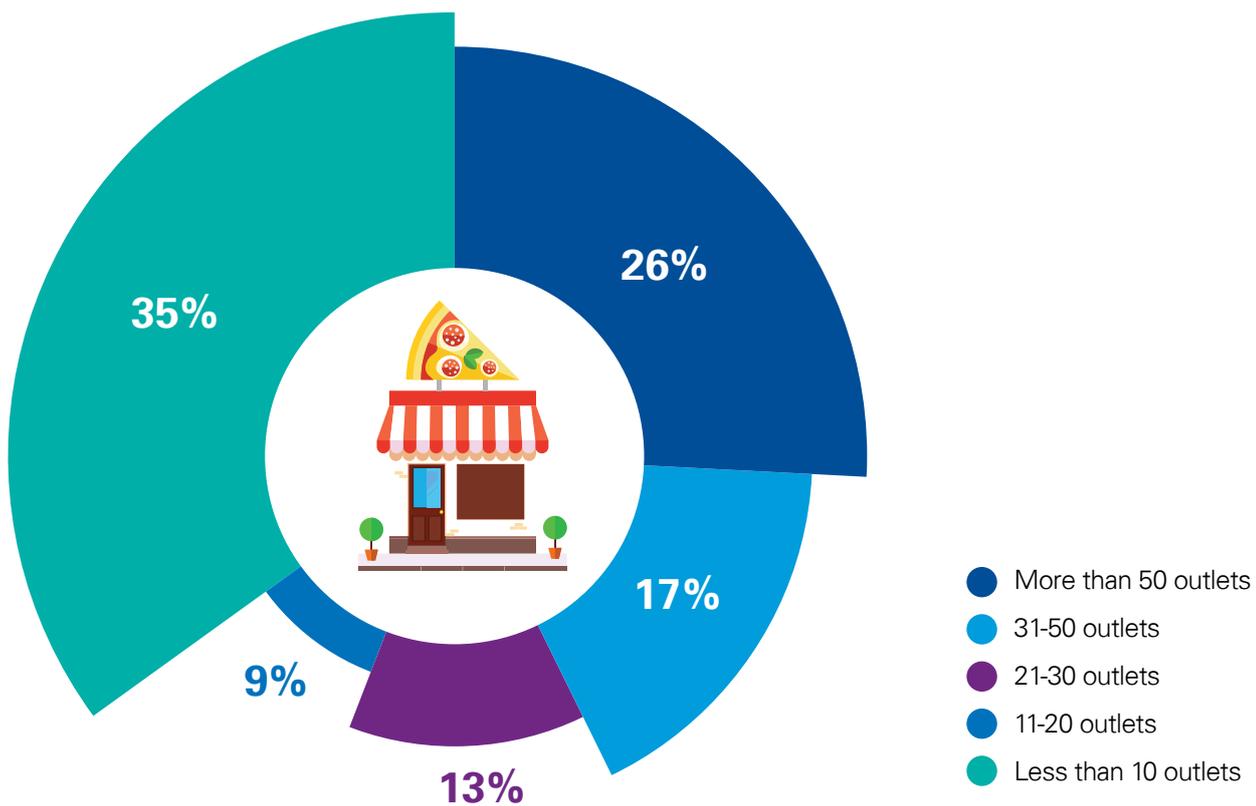
# Ingredients

## Methodology and demographics of those we interviewed

The 2018 UAE Food & Beverage report reflects the views of **25 industry stakeholders**, operating across the Emirates. These stakeholders included operators representing more than **120 brands** and approximately **1,700 outlets**.

Conversations with F&B stakeholders explored current developments in the market and future perspectives. Interviews were conducted during the third and fourth quarters of 2018, and included both qualitative and quantitative data collection.

### Operators split by size of their presence in the UAE



# KPMG services

## To assist Food & Beverage businesses



### Accounting and finance

- Audits and reviews of financial statements
- Agreed upon procedures
- Compilations of financial statements
- Outsourced payroll, bookkeeping and accounting services
- Attestation services



### Strategy

- Business planning
- New market entry
- Strategic transformation
- Consumer insight
- Go-to-market planning



### Deals

- Valuation services
- Financial due diligence
- Fund raising
- Financial restructuring
- Partner search
- Negotiations and closure
- Sell-side M&A



### Operations

- Internal audit
- Operational reviews
- Compliance reviews
- Store audits
- Development of SOPs
- Enterprise Risk Management
- Sustainability advisory



### Tax

- VAT advisory services
- VAT compliance
- VAT impact assessments and preparation
- Tax structuring
- International tax
- M&A tax solutions



### Data & Analytics

- Process mining
- Data quality & data governance
- Predicting demand for services & choosing the right location
- Product ranging & replenishment forecasting
- Executive reporting



### IT and cyber security

- Cyber security
- IT system reviews
- System selection and implementation
- Sourcing advisory



### Digital

- Digital strategy
- Customer experience transformation

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