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Bars and restaurants: Trends in property market values

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Abstract
Hardly a day goes by without press commentary on the restaurant and bar market delivering a confusing message on this sector of the market. So what are the current underlying trends which are dictating values? In order to consider this question we need to look at who are the major players in the market, what types of concept they are rolling out and the types of property they are looking for. These factors combine to dictate trends in rents, premium and capital values.

WHO ARE THE MAJOR PLAYERS AND WHY?

Historically, pub retailers and corporate occupiers dominated the market, as can be seen from the statistics shown in Table 1.

These pub retailers, and corporate occupiers, have become more selective when it comes to site acquisitions. This has arisen from an appreciation that they are operating in a mature market with strong competition so their site requirements are more exacting. This in turn restricts the number of opportunities open to them and therefore there is a tendency towards rebranding existing sites as an alternative to acquiring new premises. Some are finding that these major restaurant brands are not delivering acceptable profit margins and are turning their attentions to other sectors of the leisure market, such as health and fitness and hotels. Companies such as Bass have considered a name change to reflect their commitment to these sectors of the market.

This cautious approach has created more opportunities for independent and private operators. They have fewer people involved in the decision-making process and can often respond more promptly than their counterparts. Matthews & Goodman

Table 1: Market composition 2000

Scottish & Newcastle		Whitbread		Bass	
Brand	**Unit Numbers**	**Brand**	**Unit Numbers**	**Brand**	**Unit Numbers**
Bar 38	10	Hogshead	155	Edwards	32
Rat & Parrot	61	Casa	15	O'Neills	35
Old Orleans	43	Beefeater	258	It's a Scream	75
Quincys	8	Brewers Fayre	380	All Bar One	52
		RSVP	10	Harvester	130

Unit numbers collated by Matthews & Goodman as at September 2000 have recently concluded independent research which shows that most private operators aspire to operating between two to eight units each offering between 2,500 and 3,500 ft^2. Having reached this target they would then look to sell on their business as small established groups, sold on a going-concern basis, are in demand.

WHAT TYPE OF CONCEPTS ARE THEY ROLLING OUT?

Corporates and pub retailers gradually roll out new brands so as not to dilute the branded integrity of their existing concepts. Scottish & Newcastle have their new concept Grape, Whitbread have Casa, Bass have opened Loaf in Manchester and others, such as the Noble Group, are expanding their Jim Thompson and Gunga Din concepts. The intention is to concentrate on quality to ensure repeat custom. Separate dance/music areas, no smoking sections and additional offers such as coffee are all being trialled to ensure customer satisfaction in the face of an ageing population. Over the next ten years, we will see a 17 per cent decline in the number of 'thirty somethings' and a 20 per cent increase in the 'forty somethings'.

WHAT TYPES OF PROPERTY ARE IN DEMAND?

The pub and restaurant market is so diverse that it is almost impossible to give an overview of the criteria applied by most operators. However, there is a tendency to prefer sites which are on established drinking circuits (an area with six or more pubs and bars) or failing this in good secondary locations such as side streets within walking distance of the main circuits. Most operators are risk adverse so they require good pedestrian and/or vehicular flow and to be within close proximity of business and residential areas to ensure both lunchtime and evening trade.

Unusual buildings are in demand

Unusual and character buildings are in demand, as are buildings which are offered in shell condition providing the incoming tenant with maximum flexibility when it comes to deciding how best to fit out the premises. Other than for a select few, such as signature restaurants operated by the likes of Marco Pierre White and Belgos, isolated locations are generally avoided, as are prime retail and pedestrian areas. Buildings offering multi-level accommodation and/or narrow irregular floor plates often lead to increased operating costs and are only favoured by a few operators. Generally speaking, the minimum trading area required for restaurants is around 1,500 ft^2 with 750 ft^2 of ancillary accommodation. Bars and pubs normally require around 2,500 ft^2 or trading area with 1,000 ft^2 of ancillary space. There is currently a shortage of good quality accommodation which satisfies the general requirements outlined above. This in turn impacts on capital, rental and premium values.

RESTAURANT TRENDS IN RENT, PREMIUM AND CAPITAL VALUES

Rental values

Rents are generally on the increase. However, we are experiencing extended rent-free periods and tenants requesting that further works be undertaken to properties to reduce their own initial investment.

From Table 2 it can be seen that rents have increased over the last two years with the exception of first generation leisure parks where rents have remained static.

Premium values

Premium values, the price paid for going-concern businesses, fell away in the late 1990s but are now re-emerging. The planning and licensing restrictions being imposed by the likes of Westminster City Council are creating an imbalance in favour of demand over supply. It is generally accepted that in Westminster it will be virtually impossible to obtain A3 (restaurant/bar) consent on units in excess of 800 m^2, and licensing will be equally as difficult to secure. Consequently properties with A3 planning consents and licences are likely to become valuable. There are now examples of failed restaurants in the West End attracting premiums in excess of £400,000. We will see more premium deals and group acquisitions throughout 2001.

Capital/investment values

Uncertainty in acquisitions and disposals

The leisure sector is generally out of favour with investors. This is primarily due to the uncertainty being caused by the number of acquisitions and disposals predicted over the next 12 months, as some operators decide to expand their business by securing brands, while others concentrate on other leisure sectors through a failure to generate sufficient profit margins. The withdrawal of the likes of Whitbread from the restaurant and city bar sector is a good example of a strategic change in direction. In order to guard against the risk of failed businesses in a volatile market, there is a greater emphasis on the part of investors to look at covenant status and minimum uplifts at review. However, opportunities do still exist, particularly for non-performing secondary retail and other commercial uses, which can be converted to restaurant or bar use and often attract a higher rent and a better investment yield. Average investment yields for pubs are currently in the order of around 7.5 per cent.

Table 2: Schedule of average rental values 1998 compared with 2000

	1998	2000
Central London W/E	£35 - £40	£40 - £45
Central London City	£20 - £25	£30 - £35
City Centres	£15 - £20	£20 - £25
Leisure Parks	£15 - £20	£15 - £20

NB: Matthews & Goodman research produced for guidance purposes only

SO THEN WHAT OF THE FUTURE?

The restaurant and bar market is a smaller and leaner market now than it was in 2000, but with continued activity and growth. In the future, rents will increase but tenants will want more for their money. The impact of the planning and licensing restrictions proposed for central London should not be underestimated. If implemented, many existing restaurants and bars will attract higher rents and premium values. The restriction on future restaurant licences will create a two-tier market, those with and those without favourable licences. We will see increased consolidation. Group purchases often lead to economies of scale which result in higher unit values. Traditional pubs are seeing some rental growth but failures will continue at the bottom end of the market leading to an increased number of pubs being converted to alternative uses, in particular residential. Lateral thinking will come to the fore. We are currently advising companies like Yo! Sushi on the possible acquisition of sites within existing retail premises, major transport termini and hotels. Investment yields are likely to improve from their general level of circa 7.5 per cent as investors really get to understand the leisure market relevant to other sectors. Like any market as it gets smaller, it becomes more complex with fewer traditional operators coming to the fore. Exciting times are ahead for those involved in this sector of the market.