RESTAURANTS AND BARS REPORT 2022

REVIVE & THRIVE

AN OUTLOOK FOR RECOVERY

IDEAS | PEOPLE | TRUST

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THE RESTAURANTS AND BARS REPORT 2022

As in 2020, COVID-19 proved to be the dominating force on Restaurants and Bars in 2021.

However, as with last year, we prefer to use this report as an opportunity: to look at how owners and operators can best adjust to regulatory changes and shifting consumer sentiment; to minimise the negative impact of the pandemic on businesses; and to embrace all that we have learnt during the last two years.

In this year's report, we are delighted to share an interview with Des Gunerwardena, CEO of D&D London. Des explains how he has weathered the storm of the pandemic, and the trends impacting D&D.

Our resident BDO experts will also be providing insights on crucial issues and resolutions affecting the Restaurants and Bars sector currently. Namely, checking that you filed your CJRS claim correctly, restructuring options for hospitality firms, and reducing the blow of oncoming headwinds.

A WORD FROM MARK EDWARDS

PARTNER AND HEAD OF RESTAURANTS AND BARS

Welcome to the 2022 edition of our annual Restaurants and Bars report: your guide to changing consumer behaviour and trends in the sector.

The hospitality sector faced several months of complete closure at the start of 2021. Once trading was allowed to recommence, bars and restaurants were met with a barrage of challenges, such as social distancing restrictions, increasing inflation, and a labour shortage.

Yet despite this, as ever, the industry and its people have shown their resilience for another year. Businesses adapted to the fluctuating market and regulations, adopting Government-led support schemes, adjusting business models and even changing product-line to suit the rising demand for delivery.

As England embarks on its 'Living with COVID' plan, and restrictions ease across the rest of the UK, the hospitality sector can take its agile learnings of the past two years to revive and thrive in 2022. While we are well-aware of the many challenges the sector is currently facing and that many operators are bitterly disappointed by the limited support received from the Chancellor's Spring Statement, there are signs that the sector is ready to grow. Capacity in the sector has been reduced by over 15% and for businesses with operational excellence as well as a clearly defined customer proposition offering value for money at their heart, the prospect of profitable expansion is very real.

As such, our BDO experts are here to support you as you make the most of all the opportunities 2022 has to offer. I hope you enjoy reading the report. If you would like to discuss any of the issues highlighted, or to express your ideas on topics you wish to see in future editions, please do get in touch.

MARK EDWARDS
Partner
Head of Restaurants and Bars

ECONOMIC OVERVIEW

LUCY COLE
HOSPITALITY AND LEISURE MANAGEMENT CONSULTING
+44(0)20 3860 6525
lucy.cole@bdo.co.uk

DESPITE BUSINESSES STRUGGLING TO FILL VACANCIES, HOSPITALITY SALES PEAK AT 98% OF PRE-PANDEMIC LEVELS

Annual figures from the Office for National Statistics (ONS) estimate GDP to have increased by 7.5% in 2021, after a fall of 9.4% in 2020. Having closed 2020 with the largest annual contraction on record (-9.9%), the first quarter of 2021 saw the economy decrease by a further 1.5%. With a full lockdown in place for most of the quarter, the closure of schools and retail services brought down GDP output. Further declines occurred in production output, household consumption, and business investment.

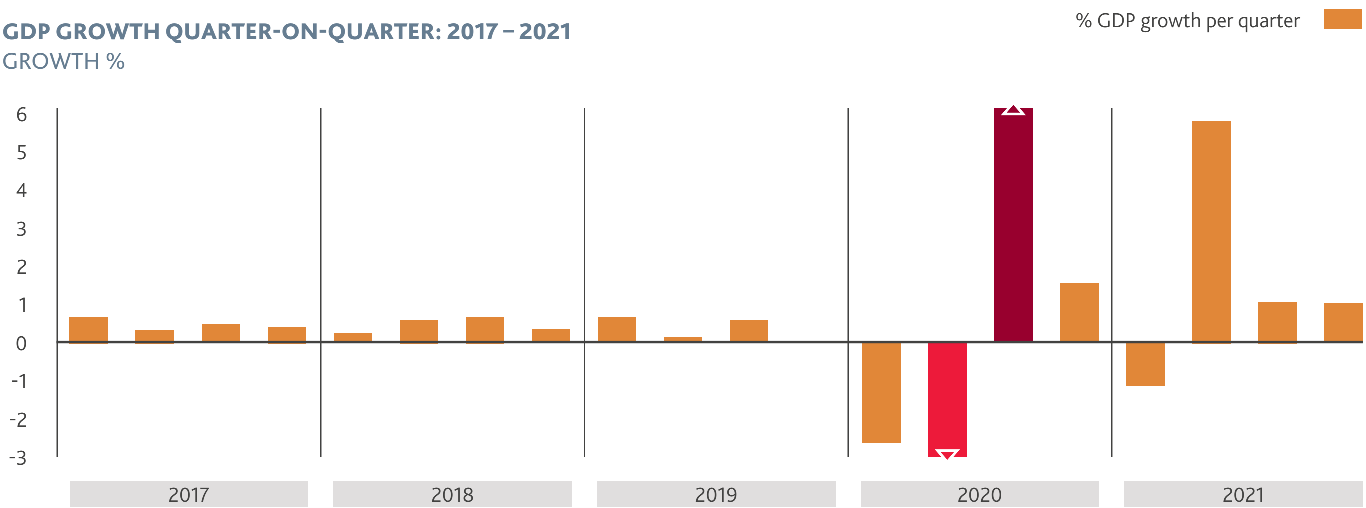
At the start of the second quarter, non-essential retail opened. Outdoor dining in hospitality venues also returned in conjunction with the 'Rule of Six'. In May, indoor hospitality was allowed to resume, in addition to smaller events, and international travel conditioned on a 'traffic light' system. As a result of these lifted restrictions, GDP increased by 4.8% in Quarter 2. The largest advances came from greater output in wholesale, retail, food services, accommodation, and education. Expenditure rose by 4.8%, of which 4.1% came from household consumption.

During Quarter 3, the lifting of all limits on social contact led GDP to increase by 1.0%. In output, hospitality, arts, recreation, and health contributed the most to this boost. As in Quarter 2, household consumption made up most of this rise in expenditure.

Quarter 4 saw GDP increase by another 1.0%. The start of the quarter was driven by increased GP visits and the extended roll-out of the COVID-19 vaccination programme. Again, household consumption contributed very positively to growth.

GDP fell by 0.2% in December as the Omicron variant was discovered in the UK. Isolation rules were reintroduced, Christmas sales in retail and hospitality dropped radically, and face coverings became mandatory once more. However, this drop of 0.2% left GDP at the same level as in February 2020, pre-pandemic.

GDP GROWTH QUARTER-ON-QUARTER: 2017 – 2021
GROWTH %



N.B. The extremity of certain results means they are unable to be presented on this graph. Unseen results are: 2020 Q2 **-19.4%**; 2020 Q3 **17.6%**.

Source: Office for National Statistics (ONS)

HOSPITALITY SPENDING

According to an ONS report published in May 2021, UK consumer spending on hospitality remained at circa 70% of pre-pandemic levels. Hospitality turnover in May was measured at 25% of pre-pandemic levels.

While hospitality sales were at 98% of pre-pandemic levels in the run-up to Christmas, according to UK Hospitality and CGA, Christmas Day sales fell by 60% and Boxing Day by a third. Instead, consumers chose to remain home amidst the rise of the Omicron variant.

HOSPITALITY EMPLOYMENT

The UK labour market showed some recovery in 2021 according to ONS data, with an increase in employment and a decrease in unemployment.

Overall, the employment rate moved from an average of 75.0% in Quarter 4 2020 to 75.5% in Quarter 4 2021; this is still lower than the pre-pandemic rate (December 2019 to February 2020) of 76.6%.

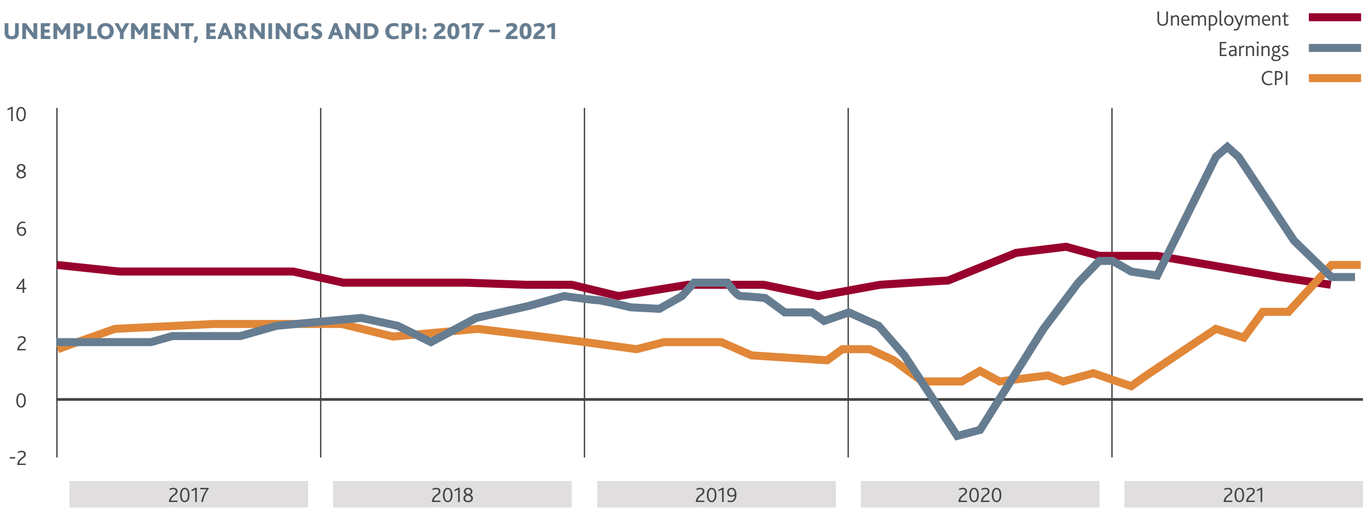
Unemployment decreased consistently in each quarter of 2021, moving from 5.1% in Quarter 4 2020 to 4.1% in Quarter 4 2021, compared to 4.0% pre-pandemic.

A further study in September by ONS stated that hospitality firms were twice as likely as other sectors to have difficulty filling vacancies, when compared to other industries' respective normal levels.

While 30% of hospitality firms stated that openings were harder to fill than usual, only 13% said the same across all industries on average. Hospitality had a record number of vacancies in June to August 2021: up by 59.1% compared to pre-pandemic.

Across all sectors with recruitment challenges, 25% quoted the reduced number of EU applicants as a factor: the number of EU nationals employed in the UK fell by 8.7% from pre-pandemic to June 2021.

UNEMPLOYMENT, EARNINGS AND CPI: 2017 – 2021



Source: Office for National Statistics (ONS)

ECONOMIC OVERVIEW

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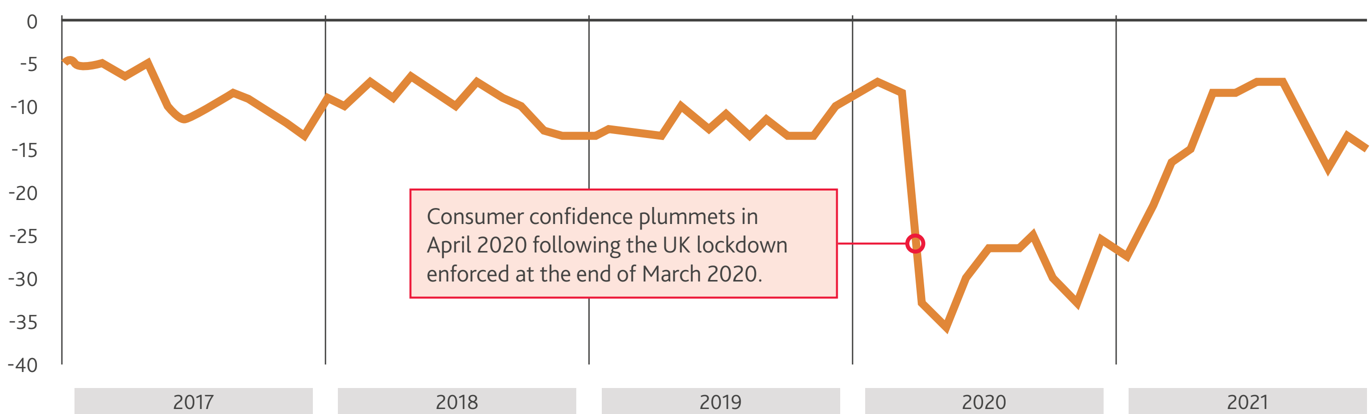
CONSUMER CONFIDENCE

At the beginning of 2021, consumer confidence sat at a very weak -28 points, according to the GfK Consumer Confidence Barometer. This was 19 points lower than January 2020, due to increasing job losses.

Consumer confidence rose steadily from February 2021 and peaked at -7 in July, on a par with February 2020, pre-pandemic. With easing restrictions and the re-opening of non-essential shops in summer, the retail industry enjoyed pent-up demand, with consumers stating they were prepared to make large purchases.

However, consumer sentiment began to drop again in August. In October, levels fell to all the way -17 amidst fuel and food shortages and a rise in inflation. After a brief relief in November, confidence dropped again in December, finishing the year at -15. New concerns over the Omicron variant and the rising cost of living meant that consumers felt less likely to make major purchases during the leadup to Christmas.

CONSUMER CONFIDENCE: 2017 - 2021
GROWTH %



Source: GfK Consumer Confidence Barometer

TRADING CONDITIONS

A lockdown from the start of the year meant that restaurants and bars were legally mandated to close until mid-April. However, when trading was able to resume in the second quarter, businesses remained hampered by social distancing requirements. With only outdoor dining allowed, some venues created exterior seating, but this took time. As a result, according to CGA, only two in five venues reopened immediately, with just over half open by the end of April.

Total sales in April 2021 were down 60.2% from April 2019, according to the Coffer CGA Business Tracker. Restaurants out-performed pubs and bars in this category, owing to the delivery option that many offered, pushing up revenue. On the other hand, in like-for-like sales, it was drinks venues who came out on top; pubs finished the month at -21.%, profiting from beer-gardens and sunny weather while consumers were permitted to gather outdoors only.

Indoor dining recommenced on the 17th May. With social distancing regulations still in place, venues with lower capacity remained closed.

However, for those restaurants able to trade, indoor consumers brought up sales to -13.0% compared to May 2019. This was higher than the average of all CGA's tracked restaurants, bars, and pubs, which came to -25.8% for the month.

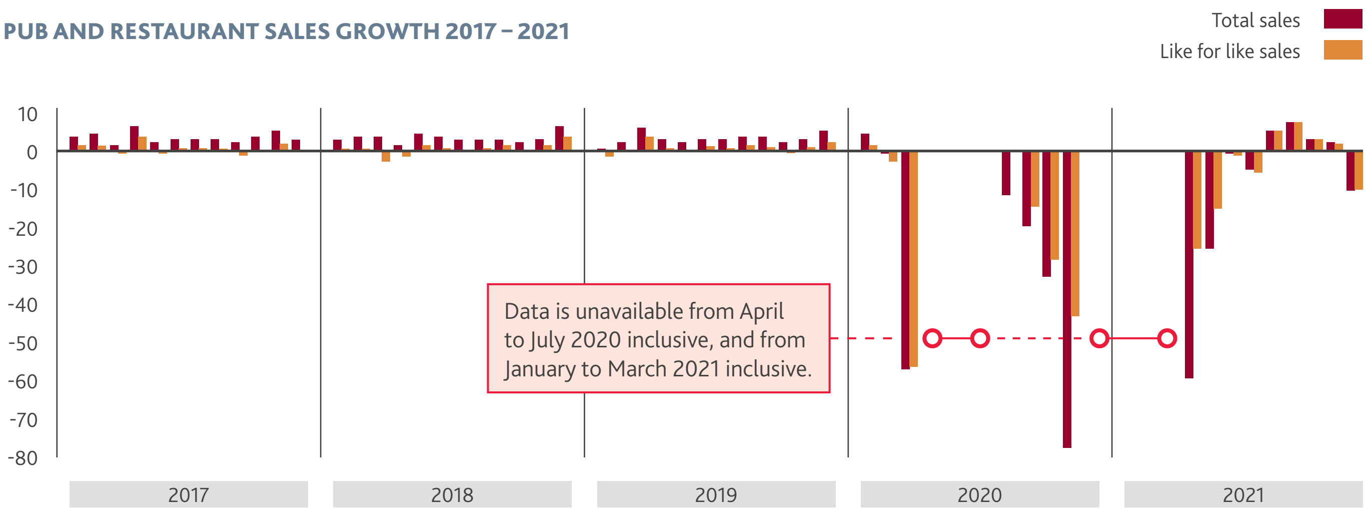
Social distancing restrictions lifted on the 21st June. Accordingly, total sales were roughly in line with 2019 levels at -0.6%. In restaurants in particular, performance was even higher than in June 2019 at 2.9%.

From August to November inclusive, total sales figures were all above 2019 levels owing to pent-up demand, peaking in September at 8.2%. Regional parts of the UK had the strongest results and benefitted from staycations, while London lacked both tourists and business visitors to fill hospitality venues.

However, as the year progressed and social distancing rules ended, restaurants and bar became plagued by another whole host of operational issues. The 'pingdemic' caused havoc: in the week to the 21st July, nearly 700,000 people were ordered to isolate by the NHS tracing app. Among them were hospitality staff, forcing some restaurants to close again temporarily. More broadly, a critical labour shortage in the hospitality industry, caused by both the pandemic and Brexit, has given rise to recruitment issues. All these factors have disrupted supply chains and created stock shortages. Finally, rising costs and low consumer confidence have continued to depress business. As a result, hospitality growth began to slow from October onwards, at 2-3% higher than 2019 figures in October and November.

The arrival of the Omicron variant dealt a final blow for hospitality firms at the end of 2021. While the industry was hopefully anticipating a boost to sales during what is usually the busiest time of year, consumers stayed at home, leading to another a decline. Total sales finished at -10.8% in December compared to 2019.

PUB AND RESTAURANT SALES GROWTH 2017 – 2021



N.B. 2021 data is year-on-year growth compared to 2019 rather than 2020, owing to the pandemic disruption.

Source: Coffer Peach Business Tracker

M&A MARKET OVERVIEW

HARRY STOAKES
PARTNER, M&A
+44(0)7785 576 325
harry.stoakes@bdo.co.uk

SAMUEL OTTERBURN
DIRECTOR, M&A
+44 (0)790 093 6420
samuel.otterburn@bdo.co.uk

The Restaurants and Bars (R&B) sector gained significant momentum in 2021 as restrictions were lifted, VAT and rates reliefs bolstered cash flows and the extended rent moratorium provided breathing space.

As operators started to re-open in April and vaccines were rolled out ever wider, consumer confidence returned and tables began to fill. It felt like the end was in sight, only for fresh challenges to emerge… the 'pingdemic', procurement issues (ingredients, equipment, concrete) and the need to continue interpreting the Government's flip-flopping.

Despite these challenges, like-for-like (LfL) recovery profiles became more predictable, forecasts more certain, and banks warmed to new lending opportunities. Most operators found a way to adapt and grow.

Brands resumed their growth strategies, looked for brands to acquire, and realised long overdue liquidity events through M&A or IPO. As 2021 progressed, M&A activity accelerated as shown in Fig. 1 on pages 8 and 9.

As predicted in last year's report, Quick Service Restaurant (QSR) brands and operators saw the greatest trading success in 2021, which fuelled M&A activity as a result.

Drive-Thru store formats, products designed to be consumed off-premises, highly-developed delivery propositions, and leading app/loyalty programmes have delivered an outstanding 18 months to QSR operators and Brand owners alike.

The sector's ability to continue trading, whilst other sectors were forced to close, resulted in QSR operators delivering impressive LfLs of >50% vs 2019. Operators with predominantly Drive-Thru estates have seen LfLs exceed >80%.

Highly predictable and resilient cash flows, coupled with VAT relief, saw significant de-gearing of balance sheets and the accumulation of substantial cash reserves. Operators, many of which were entrepreneurial and family led businesses, had the dry powder to accelerate their growth plans by expanding their multi-brand portfolio or performing buy-outs of system peers.

A number of franchisee-to-franchisee deals, launched last year, are currently in the depths of negotiations. We expect a string of completions over the coming months, and predict that portfolios with over index in drive-thru assets and with developed pipelines will command the highest multiples.

The QSR sector did see a number of completions in 2021, although these were led by institutionally backed operators:

- TDR Capital backed EuroGarages' transition to a food-on-the-go business, continued through the acquisition of 69-site health-conscious fast food chain Leon in April for £100m, Amsric's 52-site KFC estate in September, and 220-site bakery chain Cooplands. These built on previous 2020 deals, which included Ireland's largest KFC franchisee Herbert Group, and the £6.8bn acquisition of ASDA.
- In July, rumours started to circulate that Bridgepoint-backed Burger King UK was considering an IPO that could see the business valued at £600m. We understand that the float is planned to complete in H1-22.
- Neat Burger, the plant-based burger brand led by Zack Bishti and backed by F1 driver Lewis Hamilton, announced the closer of a £5m funding round in October, valuing the company at c.£50m. The investment is to be used to open 30 sites across London and fund international expansion. The round was led by SoftBank's Rajeev Misra.
- November saw Five Guys's UK CEO John Eckbert moot an IPO as being one possible option for the Charles Dunstone backed business to realise a return for the Company's shareholders.
- Finally, EuroGarages' 13-month pursuit of 1,025 stores Caffè Nero came to a head in Jan-22 as the Gerry Ford led company announced it had successfully refinanced £330m of the Group's debt.

M&A MARKET OVERVIEW

CONTINUED

FIG 1: M&A AND IPO DURING 2021

M&A activity IPO activity

Q1 2021

4 0 0 4

Jan 2021: **Soho Coffee Co**, reported a 63% fall in revenue for the y/e 31-Jan-21.

Feb 2021: **Creams** announced renewed expansion efforts via franchising across North England & Scotland.

Mar 2021: **Pret** announced:

- Food partnership with Moto and Tesco – the latter being to provide food across 700 sites; and
- Their intention to take on franchise partners to accelerate regional growth.

Mar 2021: **The Restaurant Group** announced a £500m re-financing package and updated the market that their four week cash burn rate remained at £5.5m during closures.

Q2 2021

2 2 2 6

Apr 2021: 700 site community pub company **Hawthorn** announced it's intention to IPO.

Apr 2021: **EuroGarages** acquired 70 site fast food chain Leon for c.£100m.

Apr 2021: **EuroGarages** announced the purchase of c.£140m of mezzanine loans in Caffe Nero from Swiss PE firm Partners Group.

May 2021: **Pret** announced its plans to open 100 franchised and 100 equity owned shops across regional towns.

May 2021: Gail's announced:

- Both revenue and profits for y/e Feb-22 were expected to exceed pre-pandemic levels
- Their intention to expand to 100 sites within 3 years; being 32 new store openings.

Jun 2021: Following a successful expansion into the US, **Snowfox Group** (previously Yo! Sushi) was understood to be considering a Q4-21 IPO on LSE.

Q3 2021

July 2021: **Tortilla** rumoured to be exploring a possible IPO and expansion to 45 sites.

July 2021: Starbucks franchisee **Cobra Coffee** acquired Amsric's portfolio of 12 Starbucks sites which were located across the South and South West.

July 2021: **Hawthorn Leisure**, which was previously exploring an IPO, confirmed it had been acquired by Admiral Taverns for £222m.

July 2021: **BKUK**, the Bridgepoint-backed Burger King Franchisor in the UK was rumoured to be exploring an IPO in late 2021/22.

July 2021: **SK Group** continues to lead expansion of **Tim Hortons** stores and plans to take the brand to every major UK town and city by 2022.

Aug 2021: **Grind** announced it had secured £22m of investment to further develop its D2C proposition and fund international expansion.

Aug 2021: **RedCat Pub Company** acquires 18 site pub operator The Coaching Inn Group.

Aug 2021: Vietnamese street food operator **Pho** received investment from private equity fund **Trispan**.

Sep 2021: **Hawksmoor** co-founder Will Beckett confirmed plan to IPO had been dropped.

Sep 2021: AmRest concept **Sushi Shop** announced plans to accelerate expansion across the UK via 'regional master franchise arrangements'.

Sep 2021: **Tortilla** strengthens partnership with **SSP**, opens first airport site.

Sep 2021: **The Restaurant Group** re-states long term growth plans including doubling its pub estate, add new delivery kitchens and up to 60 Wagamama sites across the UK.

Sep 2021: **Gail's Bakery** secured investment from Bain Capital Credit at to accelerate growth. Ebitda Investments (backed by entrepreneurs Henry McGovern and Steven K. Winegar) co-invested alongside Bain valuing the company at >£200m.

Sep 2021: **Coffee#1**, the Caffe Nero-owned brand, announced its intention to open 50 sites over the next 5 years under the new Coffi Lab concept.

M&A activity IPO activity

Q4 2021

6 12 4 22

Sep 2021: US coffee chain **Dutch Bros** announced it was seeking a $3.3bn IPO.

Sep 2021: **Black Sheep Coffee** announced plans to add 30 sites to their estate through both equity and franchisee led expansion.

Sep 2021: Founder of **Giggling Squid**, Andy Laurillard, confirmed the company was exploring an IPO.

Sep 2021: Three site, multi-brand dining hall **Boxpark** secured investment from LDC, in a deal that valued the company at c.£40m.

Sept 2021: **Pret** signed up **The Chesterford Group** as its first regional UK franchisee and secured a further £100m investment.

Sep 2021: **EuroGarages** acquired 52 site KFC operator Amsric, making EuroGarages the largest KFC franchisee in Europe.

Oct 2021: 40 site operator **D&D** reportedly exploring a sale to Montecito Equity Partners, valuing D&D at an EV of £100m.

Oct 2021: **EuroGarages** announced the acquisition of Coopland – one of the largest bakery chains in the UK.

Oct 2021: **Tortilla** enters AIM at a valuation of c. £70m.

Oct 2021: **Burger King UK** expected to float at £600m valuation in spring of 2022.

Oct 2021: Caring-backed businesses (**Caprice Holdings, Birley Group, Ivy Collection**) secure £168m credit facility from HSBC for site expansion plans.

Oct 2021: **CrepeAffaire** plans to triple portfolio over next 3 years with up to 50 new franchised stores, including 20 UK sites.

Oct 2021: Raymond Blanc's restaurant group (**Brasserie Blanc & White** Brasserie pub group) set for £50m takeout by **Alchemy Partners**.

Oct 2021: Pret A Manger agrees Canadian expansion deal with **A&W Food Services of Canada**.

Oct 2021: **Urban Pubs & Bars** acquires 13 sites from **Barworks**.

Nov 2021: **Hostmore** (TGI Fridays) begins trading on LSE. Share price opened at 153p, with a high of 156p shortly after placing. Price is at 118p as of 08/11/21.

Nov 2021: **Franco Manca** signs franchise deal for Greece, with at least 6 sites planned over next 3 years.

Nov 2021: **Portobello Starboard** acquires 12 freehold pubs as part of plans to build 80 strong business.

Nov 2021: **Valiant Pub Company** (Hawthorn founders & ex Ei Group director) agrees to buy 17 pubs from Welsh brewer & retailer **SA Brain**.

Nov 2021: **Mollie's Motel & Diner** (Soho House developed concept) secured £10m facility to expansion plans.

Nov 2021: **Yo! Sushi** owner puts £750m stock market float on ice.

Nov 2021: CEO of **Five Guys UK** says banks have said the 126 strong brand would be a good candidate for an IPO.

Nov 2021: **Wendy's** secures 1st UK drive thru site in UK. It currently has 3 sites in the UK, with at least 4 others in the pipeline.

Nov 2021: **Escape Hunt** to acquire **Boom Battle Bars** for £17.38m.

12 7 6 25

Nov 2021: **Inflexion** to launch auction of **Goals Soccer Centre** for c. £200m.

Nov 2021: **Nightcap** (AIM: NGHT) acquires **Barrio Familia Ltd** , the co. behind the 5 strong Barrio Bar Group for £4.9m.

Nov 2021: **Bru Coffee** and **Gelato** reveals plans for 20 new franchise sites by 2023.

Nov 2021: **Pret** sets out vision to double in size over the next 5 years, with opening of 200 new UK stores, incl. franchises. 2 new franchise partners, **Dallas Holdings** and **K&Z Holdings** signed.

Dec 2021: **Fulham Shore** reveals it has 21 sites in legals.

Dec 2021: **Boxpark** planning to quadruple in size over next 5 years.

Dec 2021: **Fortress** acquires 1300 sites strong **Punch Pubs** for a rumoured £1bn.

Jan 2022: **Sessions Market**, the food hall concept backed by Imbiba has raised £7.4m to fuel its expansion plans.

Jan 2022: **Brewdog** hires **Freshfields** ahead of IPO, with float expected to be in excess of £2bn.

M&A MARKET OVERVIEW

CONTINUED

Activity on an international level also stepped up a gear, with high profile transactions including Lagardère's acquisition of 145 Costa Coffee sites across Poland and Latvia, Abu Dhabi's Mubadala acquiring 300-site US Taco Bell operator K-Mac and listed Australian operator Collins Food Group acquiring additional KFC outlets in Europe.

Franchising has gained publicity as a way for Brand owners to accelerate domestic and international growth. Pret, Franco Manca, Black Sheep Coffee, Sushi Shop, Creams and Chopstix (to name a few) all announced successful franchise partnerships in 2021.

Best-in-class operators are in high demand and will only sign for those opportunities which promise the most compelling ROCE and growth opportunities. Jockeying between brand owners will only intensify in 2022.

For the branded R&B sector, 2021 provided a much-welcomed respite after a year of distressed activity. 'IPO' became the buzz-word of the sector with operators experiencing mixed success.

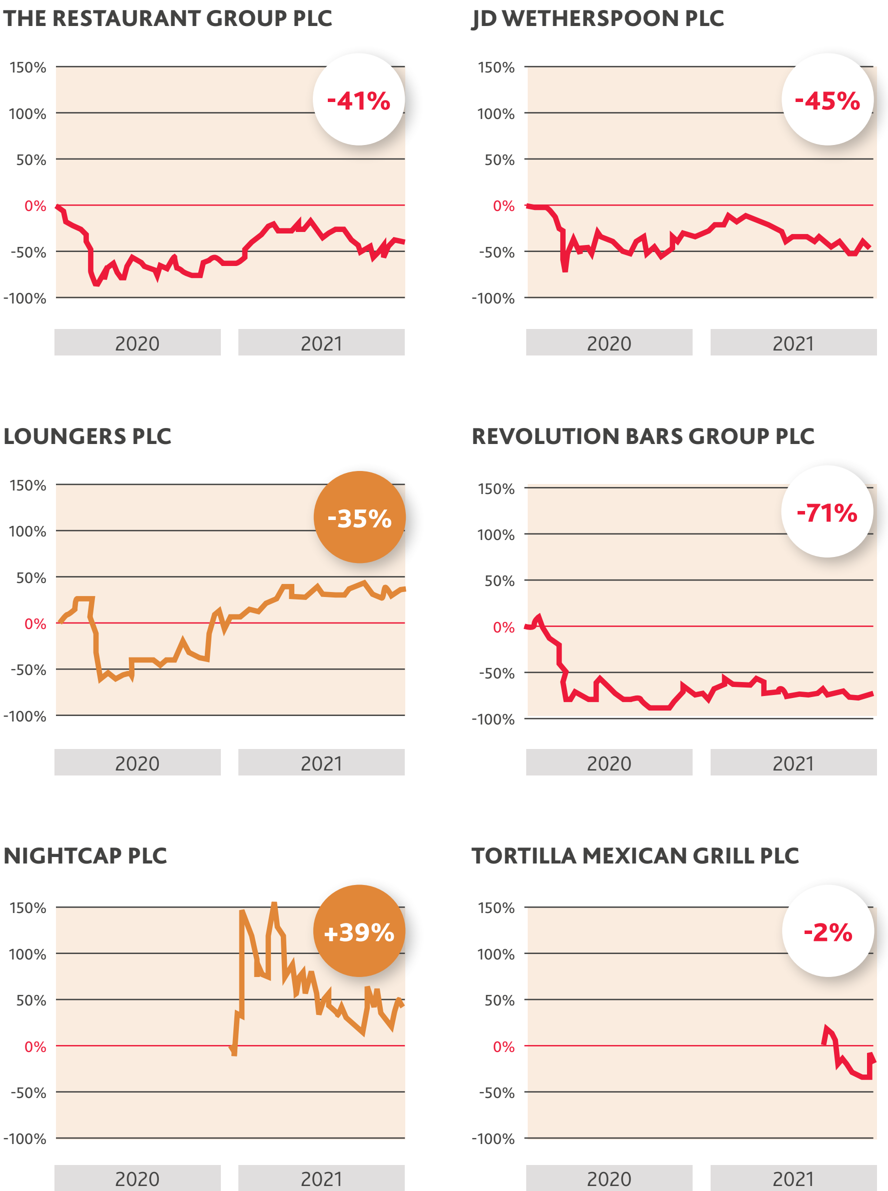
As trading restrictions began to lift in April, a broad spectrum of operators announced their interest in a public placement.

Players included Hostmore (TGI), Hawksmoor, Yo!, Giggling Squid, Tortilla and Nightcap. Three made it across the line:

- Nightcap was first out of the blocks with its placement completed in January, with £4m raised and a market cap of £13.5m, and the simultaneous acquisition of 10-site bar chain London Cocktail Club for £5.7m.
- The next placement didn't complete until October, when Tortilla raised £28m - £23m of which was paid to shareholders - at a £70m market cap.
- Finally, November saw 87-site TGI Fridays (now Hostmore) demerge from Electra and place with a market cap of £168m. The company did not raise any money in connection with its listing.

shown mixed performances since January 2020. Loungers, with its out-of-town footprint, and Nightcap have performed best. Other operators still have some way to recover to reach their pre-pandemic share prices:

FIG 2: PERFORMANCE OF UK LEISURE BUSINESSES' SHARE PRICE, JAN-20 TO JAN-22



In last year's Report, we looked at the wave of restructurings of branded restaurant and bar operators throughout 2020 which saw a third of locations close and landlords fall into disarray. Carluccio's, The Big Table (then The Casual Dining Group), Azzuri, Chilango and Côte exchanged hands for 1-3x pre Covid Company EBITDA multiples.

In Jan-21, Scandinavian night club operator Rekom expanded this list through its £10m acquisition of 42 bars and clubs from Deltic; representing a pre-Covid Company EBITDA multiple of 1.1x. The sites acquired include nightlife brands Eden, Pryzm and Atik.

2020 investment strategies had focused on rationalising stretched estates, de-gearing balance sheets and plugging working capital shortfalls during the re-opening period. If executed (and timed!) correctly, investors could hope to make 3x money multiples in less than three years once sector multiples recovered to pre-pandemic levels.

While M&A activity in 2021 appeared subdued compared to 2020, Brands with low levels of gearing, based in neighbourhood locations, or with strong delivery propositions faired best and took market share from their peers. These operators naturally caught the attention of investors who recognised the opportunity to turbocharge rollouts and acquire A* locations that wouldn't normally come onto the market.

Specialist sector investors showed their continued support to the sector:

- US-based Tao Group Hospitality acquired Hakkasan in April, taking the combined estate to 61 sites across 22 countries.
- In August, Trispan took a majority stake in Vietnamese street food restaurant Pho at a reported valuation of £37m.
- London 74 site, neighbourhood bakery chain Gail's was acquired by Bain Capital in partnership with EBITDA Investment (the Henry McGovern and Steven K. Winegar backed investment vehicle) and Capdesia in September for >£200m. This represents a pre-pandemic Company EBITDA multiple of >13x.
- The year closed with reports that Alchemy's acquisition of French restaurant chain Brasserie Bar Co was imminent.

Alongside this M&A activity, and with such a significant number of sites coming onto the market in 2020, organic growth opportunities were significant - provided you had the right brand to unlock the site.

In September Andy Hornby confirmed that, having successfully refinanced and re-opened the business, The Restaurant Group would resume growth, with targets to double the pubs estate, expand dark kitchens, and add a up to 60 Wagamama restaurants through new sites or conversions of the wider estate.

Hornby also hinted that for the right opportunity, M&A could also feature for the Group.

Similarly, The Big Table's growth ambitions were also impressive, with the Alan Morgan led Group targeting 50 new openings and 70 refurbs over a three-year period. The star of the show will be Las Iguanas which is expected to contribute 35 of the 50 openings – predominantly in major towns and city centre locations.

M&A MARKET OVERVIEW
CONTINUED

Finally, last but by no means least, the UK's much beloved pub sector was a hive of activity in 2021. M&A activity has been bold, material and decisive as PubCos vied to maximise the 'once in a lifetime' market dynamics and growth opportunities.

Oaktree's £200m investment vehicle RedCat, led by Rooney Anand, was particularly active in 2021 - acquiring 93 pubs across 13 transactions. The most notable of these were:

- The acquisition of 42 (predominantly freehold) pubs from Stonegate for £20m with 33 (30 FH, 3 LH) of the 42 pubs transferring in May for £16m. The sale was a condition set by the CMA to approve Stonegate's takeover of Ei Group in 2019.
- Acquired the Kevin Charity led freehold pub group The Coaching Inn Group in August for >£60m which saw BGF make a full exit. At the time of the deal, TCIG owned 15 freehold and three leasehold historic inns across the Cotswolds, the Peak District and Cambridgeshire. Earlier in the year, TCIG had been rumoured to be in talks with Greene King.

RedCat has not been alone in driving M&A activity across the sector. Many operators (particularly those with rooms and best position to benefit on the 2021 'staycation' boom) saw an opportunity to grow:

- In March, Northumberland freehold operator The Inn Collection secured £23m of follow-on investment from Alchemy Partners. Deployment was rapid with seven new freeholds being acquired and the Lindum Hotel expanded by acquiring an adjacent property. As the year closed, MD Sean Donkin announced he intended to maintain this momentum and open a further eight sites in 2022, taking the estate to 34 sites.
- In mid-July, Punch announced it would acquire the majority of Young's tenanted division – Ram Pub Company. 56 out of 63 sites transferred for £53m with proceeds being used to shore up Young's balance sheet, upgrade the wider estate and unlock longer term savings through a reduced head office infrastructure. Investors signalled their approval with Young's share price rising by 1.5%.
- Two weeks later, 674 community pub operator Hawthorn scrapped plans to IPO and instead accept an offer from Admiral Taverns for £222m. If reports are correct, the deal represents an 8.2x multiple.
- In September, leasehold operator Urban Pubs & Bars announced an unlikely partnership with international real estate investors Davidson Kempner and Global Mutual. Shortly thereafter UPB announced the acquisition of 13 London pubs from Barworks, taking the group to 34 sites.

The year closed with a bang as the Softbank-backed Fortress Investment Group announced the takeover of 1,300-site Punch Pubs for £1bn. The reasons for the deal are clear: Punch's estate was 93% freehold, located in suburban areas and had traded well through the pandemic, particularly compared to city-centric peers.

Less than a month later, in January 2022 reports began to circulate that SA Brain was on the brink of completing another sale, with 100 freehold pubs expected to be sold to Song Capital and Cerberus for c.£100m. This is the latest sale in a string of disposals by Brains having previously sold eight pubs to Marston's in Mar-21 and 156 pubs in Dec-20. Once this latest disposal completes, Brains will principally be a brewer with a modest pub estate division.

As for 2022, all eyes are locked on Covid-resilient Brands with differentiated propositions, large outdoor areas and loyal customers who rush back to dine at the earliest opportunity.

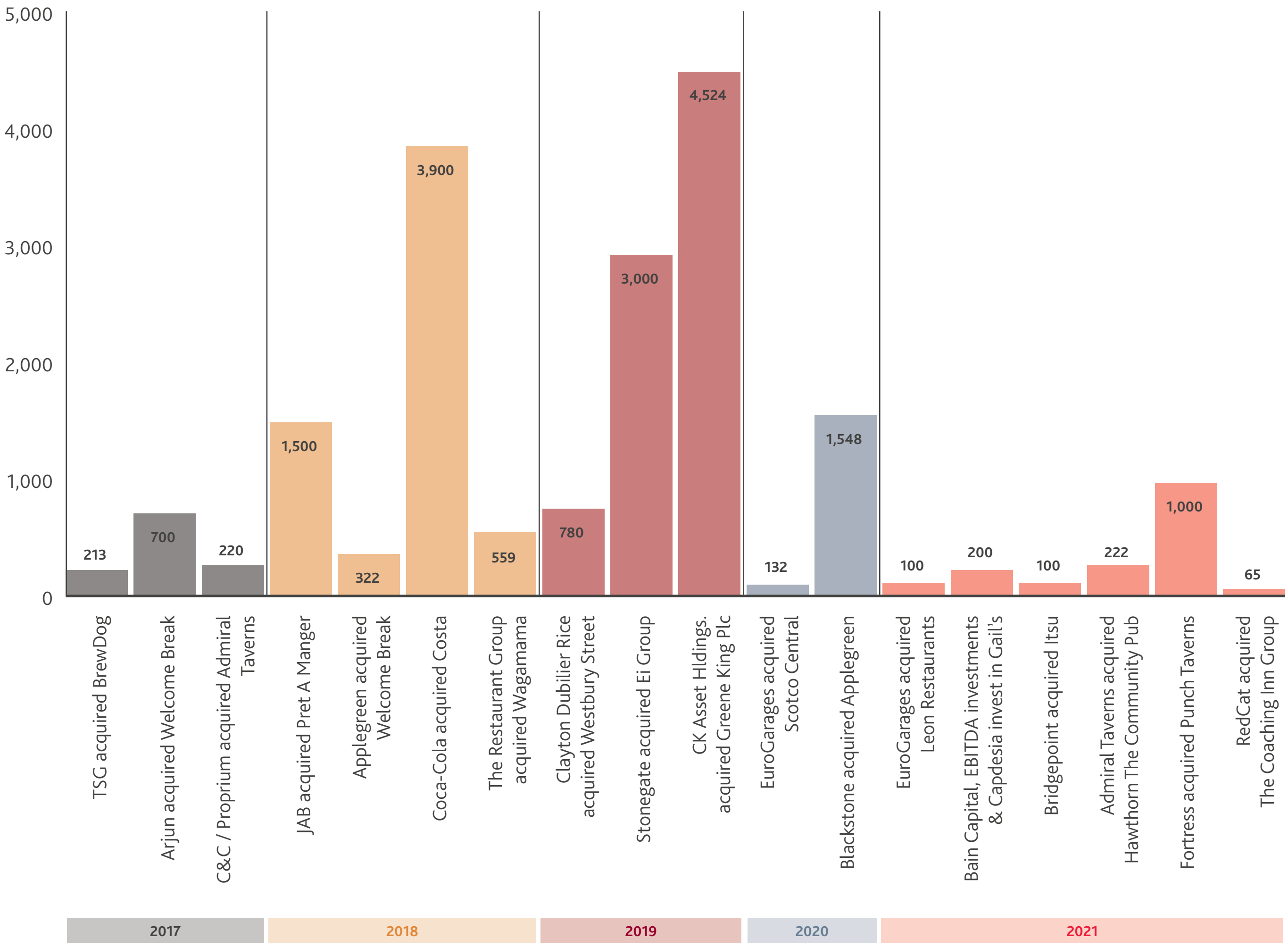
Although deal volume from 2020-2021 has certainly been lower than in previous years, both years have had their own behemoth transactions, and activity has notably ramped up over the last 12 months.

Outside the hard-hit R&B sector, 2021 was a record year for M&A activity across Europe; Baird reports that 760 mid-market transactions, worth €277bn, completed in 2021. The average EBITDA multiple for 2021 increased 11% vs 2019 – evidence that the wall of private capital competing over high-quality assets is driving premiums.

M&A and IPO activity across the UK's R&B, Pub and QSR sectors has been far from subdued. Investors are rushing back to the sector and looking to move early on high growth, segment leading brands and portfolios.

We're confident 2022 will be a knockout year for operators, investors and M&A activity.

FIG 3: THE UK'S LARGEST R&B, PUB AND QSR DEALS, 2017 - 2021



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IN CONVERSATION WITH DES GUNEWARDENA

CHAIRMAN AND CEO OF D&D LONDON

D&D London is a collection of 45 diverse restaurants, bars and one hotel based principally in London, but also with locations in Manchester, Leeds, Bristol, Paris and New York.

It was founded by Des Gunewardena and David Loewi (the eponymous D and D) in 2006. Since then the company has become a vital player in London's restaurant scene. Mark Edwards, BDO's Head of Restaurants and Bars catches up with Des to hear about trends and opportunities for D&D and the hospitality sector.

DES GUNEWARDENA

WHAT DOES D&D STAND FOR AND HOW WOULD YOU LIKE TO BE PERCEIVED?

I think it's fair to say that people think of us most for creating and operating big, bold, glamorous venues like Bluebird, Quaglinos and more recently German Gymnasium, 14 Hills, Haugen and 20 Stories in Manchester. We've won a number of global design awards for our restaurants. But I'd like us also to be better known for our foodier restaurants… like Angler, Launceston Place, Orrery and Issho in Leeds.

Angler retained its Michelin star this year and I'm sure Ben Murphy is on the cusp of earning a star at Launceston Place. Of course, we have always been and will continue to be very design focused but I think we also have some of the best chefs, sommeliers and managers in the business.

HOW DO YOU SEE CURRENT TRENDS EVOLVING AND HOW WILL THAT IMPACT D&D?

The pandemic has had a massive impact on the demographics of eating out and shopping. This in turn will have a far reaching, and I think permanent, impact on the future shape of our cities… particularly large cities like London and New York.

Hybrid office working is here to stay. However, it's not all doom and gloom for restaurants in large cities. When office workers travel to their workplace they are coming to meet each other and their clients... not to sit in front of their screens as they do at home.

And much of this socialising is going on in restaurants and bars. We have also seen our customers spending more on corporate lunches and dinners. So overall, though central London office occupancy is still reportedly at not much more than half pre COVID-19 levels, our restaurants are now back up to pre COVID-19 levels of trading.

And of course, central London should get a boost when international travel and tourism recover.

Our restaurants in regional cities and suburbs have benefited from the post pandemic growth in spends and increase in socialising, without suffering as much as central London from drops in office occupancy. Their revenues have therefore been consistently ahead of pre COVID-19 since reopening in April last year, and were hardly affected by Omicron which slashed revenues in London from mid December through January.

Long term I think regional cities and suburbs will continue to trade well above pre COVID-19 levels. So we as a company are keen on expanding further in the UK outside London. Central London will evolve… less retail, fewer offices… but more residential, more visitor attractions, more leisure and yes in due course more restaurants. So long term we remain positive about London too.

WHAT OPPORTUNITIES DO YOU SEE FOR THE SECTOR AND D&D?

For high quality operators, there are significantly more opportunities to expand post COVID-19. Customers and therefore property owners are hungry for new concepts and to create a future that is different and better than the past. There is also a recognition that there is a greater supply of properties seeking restaurant concepts than well capitalised restaurateurs able to fund and open them. Both in the UK and overseas we have therefore been inundated with approaches from landlords who will not only offer their properties at realistic rents but will also put up a significant proportion of the capital needed to open a new D&D restaurant.

This is in return for increased returns if the venue performs well. Even though the market is becoming more balanced as operators become more confident and start chasing properties… in London many overseas backed… more of a partnership model in terms of landlords and tenants sharing financial risks and rewards is I believe the long-term future for our industry.

We have a big pipeline of projects to follow after Colmore Row in Birmingham. In the UK we hope to announce shortly new venues to open in London, Manchester and Bristol including a second hotel in London. Overseas we have new ventures planned in New York, Boston and other US cities. And in mainland Europe we are in advanced discussions on two projects in Germany. We have opened 3 new restaurants since COVID-19 - Haugen, Klosterhaus and the relocated Paternoster Chophouse in the City. Post COVID-19 we are now planning quite a significant acceleration in growth provided that the economy recovers as we expect it to. We will however carefully monitor the pace of expansion in line with the challenges of staffing and inflation which are big issues for us and the industry generally.

WHAT DOES ESG MEAN TO D&D?

Without doubt the pandemic made us focus even more on sustainability. We all appreciated the clean air and walks in forests and on commons during lockdown. When we reopened we as people and as a company decided very explicitly to make sustainability central to how we operate and have implemented monitoring of key metrics to make sure we are making progress. We are not in a bad place. We commissioned an audit from the Sustainable Restaurants Association. They gave us their top 3 star rating. But there is much more we can do.

Apart from the basics of making sure we source our food sustainably, minimise waste and operate our restaurants to minimise energy usage, we have a programme of significant capital investment planned in LED lighting, building management systems and replacing inefficient mechanical and electrical plant. Our latest restaurant opening Haugen was rated Breeam "outstanding" which is very difficult to achieve. Less than 1% of new buildings achieve the 85% rating needed to be deemed "outstanding". Our Haugen building scored 92%. The credit for that has of course to go to our landlord Lendlease, not us. But Haugen has helped inject more ambition into our own environmental aspirations.

We have always supported charities that we thought were most relevant to us as a company and to our people. Action Against Hunger, Streetsmart and the Felix Project have been the three that we have supported most prominently over the last few years. Since reopening after COVID-19 we have asked our staff their views on other charities they believe we should support.

This month we are raising funds for Women's Aid alongside a big campaign to raise cash for Ukraine through a "3 million steps to Kiev" initiative which we hope every employee in D&D takes part in next weekend. Raising funds for and getting involved on a practical level with charities is very rewarding for our staff, and is an important part of our culture of trying to give something back to the communities in which we do business.

REVIVE AND THRIVE

Not sure we are yet in "thrive" mode but we have certainly managed to survive and revive D&D post pandemic closures. Survival in 2020 was due to the prompt and firm support of our shareholders, lenders, landlords and of course the government. We did however, reopen in the UK having had to take on significant bank and shareholder debt to finance lockdown and, despite substantial rent concessions, an overhang of rent arrears.

Much of this COVID-19 debt has now been settled through strong trading since reopening, despite the weakness of central London holding us back. To thrive in the future we have adopted a look forward and build back stronger culture in the context of major challenges on staffing and inflation. That has meant workstreams on food, wine, service, people, sustainability to improve every facet of our business. COVID-19 has changed our world and we also need to change…to survive let alone thrive.

HEADWINDS AND HOW TO FLOURISH

SARAH RAYMENT
PARTNER, BUSINESS RESTRUCTURING
+44 (0)207 893 3241
sarah.rayment@bdo.co.uk

PHILIP JORDAN
MANAGER, BUSINESS RESTRUCTURING
+44(0)161 833 8269
philip.jordan@bdo.co.uk

WHAT ARE THE MAIN HEADWINDS?

The hospitality sector has been one of the hardest hit during the COVID-19 pandemic.

While the relaxation of COVID-19 restrictions in 2021 saw revenues start to return, the sector still faces a number of operational and environmental headwinds created by the pandemic.

Many businesses have a build-up of debt comprising government-backed loans, HMRC and rent arrears. Management teams should consider opportunities, efficiencies and cash managements to improve trading performance and ensure serviceability of additional debt.

Evidence suggests that P&Ls continue to strain against the consequences of labour shortages and increased supply chain costs. Staff leaving the industry during the pandemic and/or as a result of Brexit have left businesses struggling to recruit, leading to insufficient employees to cope with growing demand. This, coupled with current inflationary pressures and a 1.25% National Insurance rise in April 2022, has led to increases in rates of pay, which is likely to affect margins.

The mounting supply chain disruptions, wet and dry stock prices, energy costs, and VAT of 20% from April 2022, will also impact margins and increase cost pressures on businesses. Businesses therefore need to consider whether to pass these costs on to customers.

In addition, from March 2022, Landlords were able to commence the recovery of rent arrears following the end of the moratorium, which offered protection from legal action the end of the moratorium, which offered protection from legal action.

Notwithstanding the above pressures, operators who were quick to make the necessary investments and adapt their offering in 2021 have seen success. The introduction of delivery services to profit from the thriving take-away sector is likely to continue in 2022 as consumers return to normal behaviours.

Whilst there is always a risk of further operating restrictions in the future, there remain strong growth opportunities for businesses who are able to capitalise swiftly on changing customer demands and the void left by pandemic causalities.

WHAT SHOULD MANAGEMENT BE DOING?

Strong management teams have shown resilience, making it through the hardest period the sector has ever seen. However, mindsets should now be shifting from survival-mode to business-as-usual, while recognising the new challenges and changing behaviours.

Operators need to fully understand their cash and balance sheet position to help them understand future working capital and CAPEX requirements. They should also be seeking to identify operational efficiencies and opportunities. Protecting against potential future trade restrictions and further inflationary costs should form part of normal forecasting procedures as we move forward.

Operational reviews, short-term cash flow forecasts, and robust longer-term financial projections should be prepared to identify potential funding issues and ensure appropriate and adequate funding structures are in place.

The people proposition for the business should be revisited to ensure it reflects the current market, ensuring that it can attract staff in the current competitive market. Adopting a strong ESG policy is becoming ever-more essential to both investors, customers and employees.

Major towns and city centre locations are likely to see an increase in footfall, presenting opportunities for investors who may be looking for growth opportunities at key vacant sites. Businesses should also recognise that the move to working from home has created more opportunities to increase the number of regional locations.

For businesses with rent arrears, the government has introduced an arbitration process; this provides a six-month window for landlord and tenant to reach an agreement on the rent arrears or apply for arbitration. Rent debts that have accrued during a period where trading was restricted or prevented completely as a result of COVID-19 have so far been protected from legal action.

WHAT OPTIONS ARE AVAILABLE FOR HOSPITALITY FIRMS?

With a high number of headwinds and an overhang of pandemic debt, businesses may need to restructure this debt to flourish moving forward.

The Government introduced various new restructuring tools under the Corporate Insolvency and Governance Act 2020 (CIGA) which came into effect on 26th June 2020. These tools aim to support viable businesses in light of the pandemic and to improve the likelihood of distressed companies surviving:

- The standalone moratorium can provide much needed protection for businesses while they undergo a restructure. This looks to deal with historic debts, under the supervision of a qualified monitor.
- A restructuring plan, which is modelled on a scheme of arrangement procedure but allows scope for greater flexibility, allows companies in difficulty to agree a formal arrangement with stakeholders.

Traditional restructuring tools such as a Company Voluntary Arrangement (CVA) continue to be available and were a popular tool prior to the pandemic for a business with leasehold estates. This process enables a company to make proposals to its unsecured creditors to compromise claims.

We expect that the use of these tools will increase as the government withdraws funding support measures.

Management should seek advice where necessary. BDO can assist with any of the above matters.

BDO'S INTERACTIVE TIMELINE CAN HELP BUSINESSES TO STAY INFORMED OF KEY UPCOMING EVENTS AND ASSIST IN DECISION-MAKING

FURTHER DETAILS OF THE GOVERNMENT'S RESTRUCTURING TOOLS CAN BE FOUND HERE

REVIEW AND REVIVE YOUR CJRS CLAIM

JACQUI ROBERTS
ASSOCIATE DIRECTOR, GLOBAL EMPLOYER SERVICES (EMPLOYMENT TAX)
+44 (0)203 219 4062
jacqui.roberts@bdo.co.uk

As life starts to get back to near-normal and business looks more like it was pre-pandemic, you might be forgiven for thinking that the end of the furlough scheme represents an opportunity to relax.

Unfortunately, HMRC's attention is now shifting more to the detail of the claims made, with many businesses being challenged and expected to repay large sums.

Given the speed of introduction and the complex nature of the CJRS claim calculations, it is unsurprising that errors, both over- and under-payments, have occurred. We have seen evidence that even large restaurant and bars chains with substantial HR resources have made errors due, in no small part, to the many changes to the rules.

WHAT WERE THE PROBLEMATIC AREAS OF CJRS?

There were 4 different versions of the scheme, which was first implemented in March 2020. Problems were caused by changes to the contribution percentages and elements of the pay subsidised, the difficulties of weekly verses monthly pay periods, and pay periods overlapping different calendar months, to name a few. The main errors fall under three headings:

1 The reference pay used to calculate the CJRS claim;

2 The calculation of hours worked by staff before furlough (used as the reference for calculating time on furlough);

3 The calculation of hours worked/on furlough while on flexi-furlough.

While regular salary forms part of the reference pay, discretionary pay (such as tips or commission) does not. Furthermore, the use of zero-hours contracts increased the complexity of calculating reference pay, requiring a comparison with equivalent pay before furlough or the average pay since April 2019.

The number of hours worked for the purpose of calculating the claim also presented an issue, and whether the employee worked during the furlough period added further complexity.

Also, in the first version of the CJRS, furloughed employees were not able to work although there were some exemptions - for example, in relation to training or directors performing statutory duties. Collecting post or handling deliveries were not exempt.

Businesses with a younger workforce demographic needed to be careful in making claims up to and including July 2020.

Whilst an employer's NIC could be claimed under CJRS, this was only the case if the employer's NIC was due for the particular employees – for example, where there are exemptions from paying employer NIC for employees aged under 21 or apprentices aged under 25. Similarly, claims could be made for employer pension contributions, but only where the employee had not opted out of the pension scheme.

There were also complexities around which employees could be furloughed as this changed over the course of CJRS's 18-month lifespan. For example, the third version of CJRS was restricted to employees who had been on the payroll on or before 30th October 2020 and could not be serving their notice period.

The final version had further restrictions as furloughed employees needed to be on the payroll between 20th March 2020 and 2nd March 2021 and required claims to cover at least a seven-day period and (ordinarily) could only cover days within the same calendar month.

As a result of the above, our experience shows that the majority of businesses made mistakes with their claims.

REVIEW AND REVIVE YOUR CJRS CLAIM

CONTINUED

WHAT IF YOUR CJRS CLAIM IS INCORRECT?

Any over-claims must be notified to HMRC directly, and arrangements made to make direct repayment to HMRC. Failure to notify errors could lead to significant penalties.

It is important to remember that the last CJRS claim is far from the end of the matter and at the very least, businesses must ensure that the CJRS payments received and any amount over-claimed are declared accurately on the organisation's corporate tax return.

Therefore, any CJRS errors that remain uncorrected by the time a business comes to submit its tax returns means that it may end up submitting an incorrect return. Valid CJRS receipts are taxable business income and excess claims are liable at 100% clawback; but errors in your return can lead to interest and penalty charges on top of any penalties directly attributable to the CJRS error itself.

In addition to ensuring any errors are corrected, hospitality businesses must also remember that if they have underpaid a member of staff, the employee has a legal entitlement to be paid their full cash entitlement for the furlough period, irrespective of the fact that they can no longer claim this amount from HMRC.

WHAT ARE YOUR NEXT STEPS?

It is more important now than ever to review your own calculations, so that if an error is identified, any amounts can be made good with HMRC on a voluntary basis – usually the cheapest and least time-consuming option. Penalties for over-claims can range from 30%, where disclosure is entirely voluntary and unprompted, right up to 100%, where HMRC has identified the non-disclosure and has treated it as "deliberate and concealed".

Voluntary disclosures should be handled more sympathetically by HMRC than if they discover the error themselves; therefore, it makes sense to take the pro-active steps of reviewing your claims.

CHANGES TO TIPS

Changes to the Employment Bill announced in October 2021 may impact businesses next year and are expected to include:

- Employers will not be able to make deductions from tips for anything other than tax and NIC, if applicable.
- Distribution of tips must be fair and transparent for employees.
- A Statutory Code of Practice will be issued by the Government and each employer that has employees who receive tips will need to put in place a written policy.
- Employers will need to retain a record of how tips have been dealt with and this can be requested by employees where they believe a failure to operate within the legislation has occurred.
- Enforcement will be through the Employment Tribunal.
- Tronc schemes/systems can remain where they comply with the legislation.

Notwithstanding the potential changes, now is the time to make sure that current arrangements for gratuities are robust. As we know, cash tips distributed to employees must be processed via the payroll; however, where Tronc schemes are used, NIC is not accounted for. Tronc schemes usually set their basis of distribution by reference to the role the employee performs (front of house, back of house etc) and/or the length of their shift(s) as well as the collection period for those tips.

It may be possible to also use the tronc scheme to set parameters including incentivising certain behaviours; for example, promoting particular products or services to drive revenue growth, or aligning with the company's ESG agenda.

The company cannot impose these conditions or set these parameters as there needs to be suitable separation from the running of the tronc scheme and the company's owners and directors.

Equally, however, the Troncmaster running the scheme will usually be someone with sufficient standing within the business to understand and support the company's values and, therefore, will be able to implement something that supports the company's plans.

If you would like to discuss any of the points raised above, please reach out to our Employment Tax team to discuss how we can help.

BDO SECTOR EXPERTISE

RESTAURANTS, BARS AND PUBS

BDO's national Restaurants and Bars team comprises industry specialists across audit, tax, and advisory. They offers clients expertise tailored to each business, and resolve unique challenges that may arise within the sector.

BDO is recognised as the leading adviser to the Restaurants and Bars sector, blending sector knowledge and experience with practical advice which is aimed at making a real difference to our clients' success.

With a focus on the economic engine (mid-market) and private equity, we frequently advise entrepreneurial businesses as they grow and offer commercial insight that is founded on sector expertise.

We know who is doing what in the market, we offer information of current trends and issues, and we are able to benchmark our clients' businesses, over and above our competitors.

With our dedicated transactional team, bolstering our audit and tax services, we are able to advise restaurants and bars throughout their full life cycle.

As thought-leaders across the sector, we offer specialised commercial and technical updates, including this Restaurants and Bars report, which we publish annually.

We also have a well-established network in the industry that spans finance directors, suppliers, and advisers, and we are always willing to use this to our clients' advantage.

LEISURE AND HOSPITALITY

As well as restaurants and bars, BDO has expertise across the hospitality and leisure sectors, with industry-focussed teams in retail, hotels, travel and tourism, betting and gaming, and professional sports.

BDO has a breadth and depth of expertise across each of these industry segments, and we provide business and risk assurance, tax planning, corporate finance assistance, performance improvement advice, and personal wealth management to our clients.

CONTACTS

We hope that you enjoyed this report.

For more information on our sector credentials, or to receive our thought-leadership reports in any of our other Leisure and Hospitality sectors, please get in touch.

MARK EDWARDS
PARTNER & HEAD OF RESTAURANTS AND BARS
+44 (0)207 893 3742
mark.edwards@bdo.co.uk

PETER HEMINGTON
PARTNER & HEAD OF MERGERS AND ACQUISITIONS
+44 (0)207 893 2344
peter.hemington@bdo.co.uk

CHRIS GROVE
PARTNER, TRANSACTION SERVICES
+44 (0)207 893 2163
chris.grove@bdo.co.uk

JONATHAN HICKMAN
PARTNER, TAX
+44 (0)207 893 2496
jonathan.hickman@bdo.co.uk

SARAH RAYMENT
PARTNER, BUSINESS RESTRUCTURING
+44 (0)207 893 3241
sarah.rayment@bdo.co.uk

CONOR LAMBERT
PARTNER, TRANSACTION SERVICES
+44 (0)207 893 2191
conor.lambert@bdo.co.uk

DAVID CAMPBELL
PARTNER, AUDIT
+44 (0)777 161 3951
david.campbell@bdo.co.uk

ED GREEN-WILKINSON
DIRECTOR, AUDIT
+44 (0)207 893 374
ed.green-wilkinson@bdo.co.uk

FOR MORE INFORMATION:

MARK EDWARDS
+44 (0)207 893 3742
mark.edwards@bdo.co.uk

www.bdo.co.uk

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