RESTAURANTS AND BARS REPORT

DECEMBER 2013

INTRODUCTION

Welcome to the latest edition of our review of the restaurant and bar sector.

It has been a year since our last report, and 2013 has definitely been the year when our predicted rise in deal volumes finally happened, which together with the return of IPOs to the sector bodes very well for the financial strength of Restaurant and Bar businesses in the UK.

A very strong year of trading from most in the sector, together with the long awaited return of consumer confidence have really kick started the market and the sector has finally regained the ground lost during the recession.

In this issue, alongside the regular Boardroom Agenda covering the 'state of the nation' and the economic environment, we take a closer look at that increase in deal activity, and what has attracted BGF to the sector in particular.

We also take a look at some advice on expanding your brand internationally, as well as considering the way in which the worlds of hoteliers and restaurateurs are overlapping more and more these days.

Finally we have gazed into our crystal ball and present our Top 10 predictions for 2014.

We hope you will find these articles both interesting and stimulating for your business. Happy reading!

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BOARDROOM AGENDA

The UK economy has obviously had a tough five years. Many cash-strapped consumers reined in their discretionary spending and whilst eating and drinking out have proved remarkably resilient, operators have clearly faced a very challenging environment. But after the recent strong quarter things may at last be looking up.

Fresh confidence in the economy

The monstrous hangover from the 2008 financial crisis may at last be fading, with 0.8% growth in GDP over the third quarter of 2013.

Not only was July-September the best quarterly performance since 2010, but it built on the 0.7% growth that we saw in Q2. This has prompted a U-turn from the IMF, which accused George Osborne of "playing with fire" with his austerity programme.

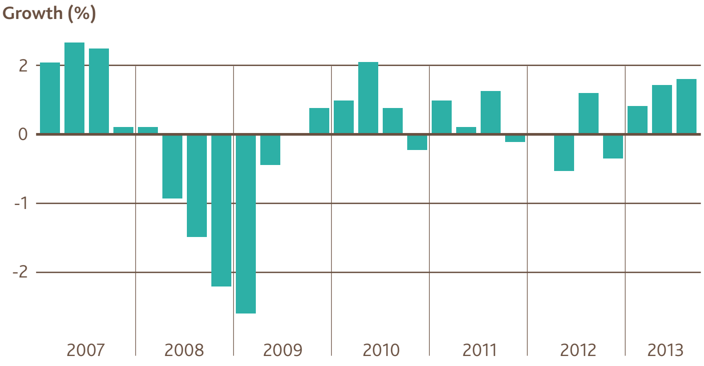
Now the IMF forecasts GDP growth of 1.4% for the year, double its prediction back in April. All the signs indicate a recovery that is gathering pace, and we should see growth accelerate through the final quarter of 2013.

However, even as it stabilises, the UK economy is still at risk from the global markets, and a shock from Europe or Asia may hinder the return to prosperity. Nevertheless these risks are slowly receding, with a rebound expected in Asia and emerging Europe. It is Western Europe that still poses the greatest threat, though the tide may have turned there too, with growth expected over the next two to three years.

The upturn is being felt across a variety of sectors. Retail sales, investment spending and net exports are all up, and the BDO business trends survey showed a steady recovery for manufacturing and services. What's more, consumer confidence is at its strongest since November 2007, and it is many years since business confidence was so high. Quite simply, the economy has got its spark back. Progress is a bit less upbeat for inflation. The consumer price index currently stands 0.7% above the 2% target set for 2013 by the Monetary Policy Committee, though the outlook has improved a little. Hikes in utility prices remain the largest inflationary pressure, with food and fuel prices also expected to rise. The labour market continues to post strong employment growth, albeit with few signs of an imminent reduction of unemployment (currently 7.7%). The strong figures come largely from falling levels of underemployment, as many employers squeeze more out of existing workers rather than hiring more.

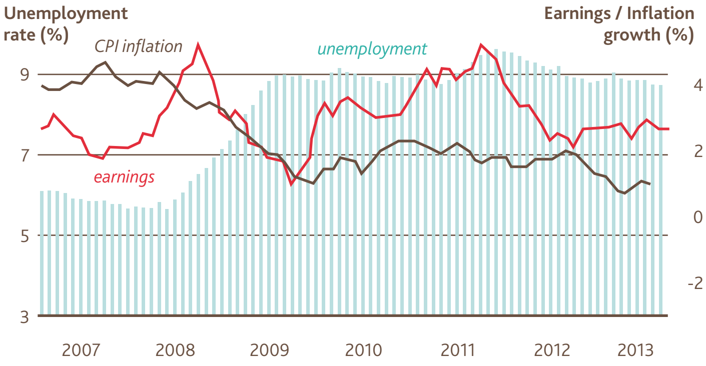
This lack of real wage inflation is though a drag on the consumer that may yet hold back a real resurgence in consumer spending – wage inflation still lags cost inflation and until this reverses consumers will have reduced spending power month on month, regardless of how confident they may be feeling about the future.

GDP Growth Quarter-On-Quarter 2007-2013



Source: ONS

Unemployment, Earnings, Inflation 2007-2013



Source: ONS

BDO OPINION

The UK appears firmly on the road to recovery, but real risks remain. Businesses should not assume they will simply be able to ride a new wave of consumer spending. The reality of the matter is that GDP is still 2% below pre-2008 levels, and with inflation still outstripping wage growth, consumers continue to have less money in their pockets than they did 12 months ago.

As for the much talked-about strength in the housing market, this should be treated with caution. The rise in house prices is by no means uniform across the country, with the North and Midlands seeing static prices at best, while they continue to fall in Wales and Northern Ireland. The apparent boom is entirely driven by growth in the South, particularly London, where international property demand has driven double digit growth. The government's Help to Buy scheme has given the market a shot in the arm, but at the risk of causing a housing market bubble if issues on the supply side are not addressed. There is also a real danger of a retrenchment in consumer spending when interest rates eventually rise and make mortgage payments more expensive, which may happen sooner than we would like.

Trading picks up

Trading conditions have undoubtedly improved in 2013, with both total sales and like-for-likes demonstrating relatively robust growth over the past six months. During the economic downturn many consumers chose either to cut spending on eating out completely or to trade down to cheaper alternatives such as takeaways. The improving consumer climate has helped people become less cost conscious, and they are going out more.

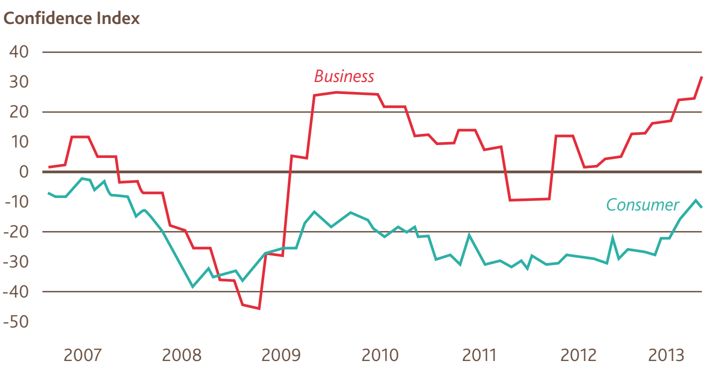
Even though in real terms consumers are no better off than they were 12 months ago, average spend per head and restaurant patronage are up.

The UK consumer has never put up with poor customer service, but in these uncertain times many operators have chosen to invest more in providing quality food at affordable prices. This value for money has been a key driver in bringing some of the volume back into the market – but it remains crucial to give excellent customer service.

Technology has really helped to invigorate this sector, with the likes of Square Meal and Top Table offering operators better access to consumers, albeit at the expense of increased competition and cost. The resurgent services sector should help to boost demand at the high-end of the restaurant market, with business lunches and client entertainment regaining popularity, particularly in London.

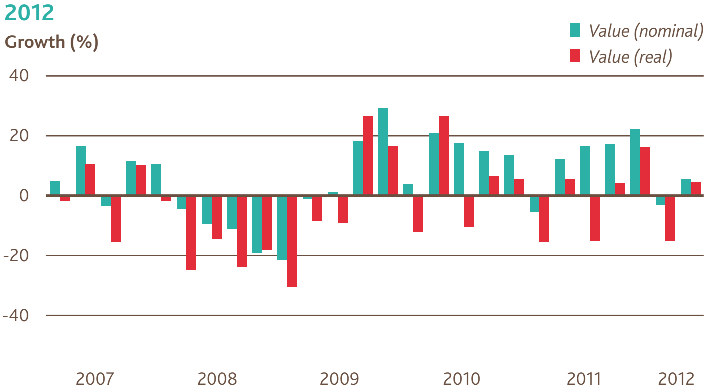
There is still however a strain on profit margins, with the cost of wages, rent, utilities and food costs going up, and with no signs of slowing in the future. But there is a drop of relief to be had in the fall of wine prices over the past five years, thanks to global over-supply and strong competition from New World producers.

Business and Consumer Confidence 2007-2012



Source: GfK, NOP, ICAEW

Household final consumption across restaurants, cafes etc 2007-2012



Source: ONS

BOARDROOM AGENDA

Legislation still a burden

The sector continues to wrestle with an ever-changing tax and legislative environment.

Despite the government supposedly championing SMEs, the number of alterations in policy mean that trading in this sector is not getting easier. Employment costs have also risen due to an increase in minimum wage and the introduction of auto enrolment pension schemes for staff, with take up on these schemes being higher than many anticipated.

At least a quarter of this sector's workforce is hired at the minimum wage, so any rise translates into a major hit for restaurants and bars to take.

Moving onto other legislation, the use of late-night levies and early morning restrictions continues to be hotly contested, with a number of local councils choosing to reject outright the possibility of future use. Some fear that local businesses could suffer from their use, which may lead to trade migrating to neighbouring areas.

Minimum wage brings mixed fortunes

From 1st October, the minimum wage for workers aged 21 and above rose 1.9% from £6.19 an hour to £6.31. For those aged between 18 and 20 the hourly rate is increasing by 5p to £5.03, while those aged 16 or 17 will see their minimum wage increase by 4p to £3.72.

Personal licences – should they stay or go?

In September the government launched a consultation into whether personal licences should be abolished. If this were to happen, licensing authorities would be able to apply relevant conditions to premises licences where appropriate. So far the response has been mixed, with opinions divided as to what effect this review may bring. A number of operators have suggested that, although the current system is flawed, a complete overhaul may not be the answer.

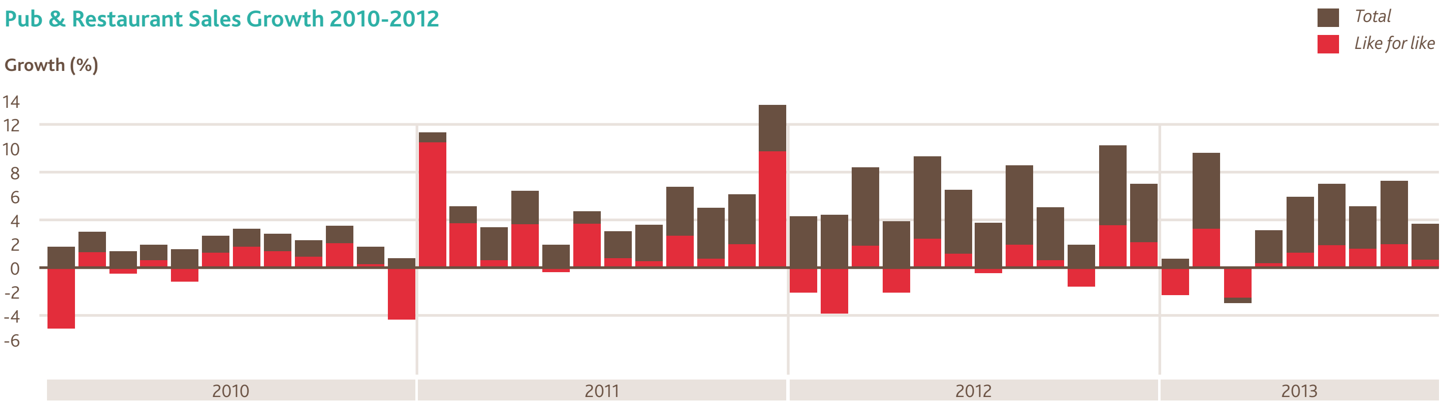
Conclusion

The worst of the recession is clearly behind us, and growth forecasts and expectations for consumer confidence and spending look positive. Whilst the limited rise in wage inflation may hold consumers back a little in 2014, we remain confident that the sector is well placed to enjoy its most buoyant year for some time.

BDO OPINION

Trading conditions in the restaurants and bars sector should improve further over the coming 12 months. Even though consumer leisure time is expected to be squeezed by a rise in average working hours, the demand for convenient, quality food and drink will grow more robust. Operators that successfully tap into prevailing social trends – with an emphasis on quality and value – are likely to benefit in 2014 as consumer confidence continues to rise.

Pub & Restaurant Sales Growth 2010-2012



Source: Coffer Peach Business Tracker

M&A UPDATE: OUR PREDICTION PROVED RIGHT

Last December we forecast that 2013 would see M&A activity pick up, and the year duly delivered. There is a real sense that the wheels of the M&A machine are starting to turn a little quicker, and a number of high profile transactions have caught the eye of consumers, operators and investors alike as BDO's Kieran Lawton explains.

The national press is also starting to sit up and take note, with a number of reports highlighting this resurgence in activity, whilst also drawing attention to private equity's continuing love affair with the sector.

The menu of big deals

Hutton Collins' £100m acquisition of Byron is just the latest in the string of high profile transactions that have taken place since our last report. There had been considerable interest in the burger chain and its potential sale for some time, and a price that achieved a reported multiple of 10x run-rate EBITDA will have delighted Gondola. The Byron deal came hot on the heels of another six-figure transaction, that of CBPE's £100m acquisition of Côte. It was widely acknowledged that the owners of the French brasserie chain were considering offers and, although the sum achieved was below original reported expectations of £125m, it still represented a healthy price for the 45-strong chain and secured another profitable exit for serial sector investor Richard Caring.

Another eye-catching sale was Risk Capital Partners' exit of Giraffe, which was sold to Tesco in a deal valued at nearly £50m, giving Risk a reported return of eight times their original valuation. It was no secret that Risk had been looking to exit but the buyer came somewhat from left field. The supermarket giant's investment in artisan coffee shop concept Harris + Hoole was perhaps a sign of things to come, but the Giraffe deal still surprised many who had expected a wider sale process to be run some time next year.

In a busy period for Luke Johnson's outfit, Risk also invested in multi-cuisine buffet concept Red Hot World Buffet. Other high profile deals that grabbed the press' attention included Bowmark Capital's backing of Drake & Morgan in a £30m deal, Graphite Capital's investment in premium steak concept Hawksmoor, and LDC's £50M buy-out of high end restaurant group D&D London.

D&D: *"D&D has a collection of unique central London sites such as Bluebird, Skylon and Coq d'Argent which have demonstrated tremendous resilience over many years. This provided comfort that these are sites which have an enduring relevance in the London fine dining market."*

BERTIE AYKROYD | LDC

In other deals, Beringea wrapped up an exit from Tossed by selling to the management team (backed by a private investor), while Calculus Capital's backing of Benito's Hat showed that funders are still keen on Mexican food.

Piper Private Equity followed its recent investments in Be at One and Loungers with £6m of funding to help roll out Caribbean concept Turtle Bay, while leisure specialists Kings Park Capital invested in juice and smoothie operator Fuel Juice Bars and more recently in pubs with rooms operator Inn Collection. Around the same time as the KPC's Fuel deal, The Business Growth Fund put money into another smoothie concept: Richard O'Sullivan's Boost Juice Bars. As noted later in this report, BGF demonstrated more fondness for the sector with its investment in Camino, which will sit alongside portfolio companies Barburrito, Peyton & Byrne and Wear Inns.

In the pub sector, Cerberus's £200m purchase of Admiral Taverns caught the attention and provided a welcome exit for Lloyds Bank. At the other end of the scale, a £2.7m investment in Tim Bacon and Jeremy Roberts's New World Pub Company (owner of the Oast House and Botanist brands) was of interest, not least because it was the first investment through Hub Capital's F&B Fund, the tie-up between Paul Campbell and LDC.

M&A UPDATE: OUR PREDICTION PROVED RIGHT

Why private equity loves wining and dining

A busy period for M&A in the restaurants and bars sector has been particularly sizzling for equity investors. Clearly, there are big attractions to restaurants and bars that go beyond them being nice places for financiers to socialise.

Bowmark partner Ron Pearson explains a bit more: "We and other private equity players like the restaurants and bars sector because the businesses are in what has proven to be a resilient part of the consumer market; they are highly scalable and differentiation is not a function of size. As a result you can find relatively young businesses that with a strong management team can deliver superior returns."

That is not to say that investments are straightforward. As Peter Kemp-Welch of consumer specialists Piper points out: "Investors still need to be wary. While there has been an uptick in deal activity and some healthy multiples being paid, there is perhaps a risk over over-exuberance. Barriers to entry are low, pubs are raising their game and there are an increasing number of concepts taking space in the market. Operators need to be mindful of this; only the best concepts and management teams will attract investment".

Drake and Morgan: *"The management team have developed a sustainable proposition that is highly appealing to customers and landlords alike. Together with the team, we believe we can build a really significant business over the next four to five years that has a lot of room for further growth beyond that."*

RON PEARSON | Bowmark Capital

Red Hot World Buffet: *"We believe the buffet dining space to be one of the fastest growing segments of the UK's restaurant market and that Red Hot offers great choice and great value for money to its customers in these challenging times. We are looking forward to working with the Founders and the wider management team to help them in their ambitious growth plans."*

LUKE JOHNSON | Risk Capital Partners

Investing in a management team

Successful concepts are cash generative and scalable, so they lend themselves to the private equity model. However, there is more to an investment than a differentiated concept and roll-out potential. As Pearson and Kemp-Welch point out, investors are backing the management team to deliver that potential.

Jamie Tillman of Kings Park Capital views it as follows: "We look to back management teams, and particularly those where our expertise and contacts can help them accelerate their growth plans.

As with our other investment in the QSR sector, Abokado, in Fuel we were attracted by an entrepreneur who has built a successful and consistent model with substantial rollout potential."

LDC's Bertie Aykroyd agrees that the management team is key. Referring to the D&D deal, he said: "We have partnered with two of the best restaurateurs in London, who have an enviable track-record of creating exciting new concepts."

Similarly, Omar Kayat of Graphite Capital emphasises the importance of a strong management team: "We are keen on the sector and have supported a number of restaurant and leisure businesses in the past, with a common theme being that we always look to back 'best in class' management teams".

Turtle Bay: *"We spent a lot of time talking to Turtle Bay's customers in advance of investing and were delighted to discover that our research supported our initial assessment; that Turtle Bay offers something different in a competitive marketplace. This, along with the management team's track record in the sector, gave us the confidence to invest and we're very excited about helping the team develop the concept further."*

PETER KEMP-WELCH | Piper Private Equity

Exit strategies

Another reason equity houses have a taste for this sector is the number of viable exit routes. Savvy investors put money into concepts where growth potential goes beyond a single investment period, meaning that it is very common for one private equity house to sell to another. However, while the secondary / tertiary (etc) buyout clearly remains an option, our recent experience suggests equity houses are becoming less reliant on it as the only viable exit route.

Looking at Tesco's foray into casual dining, it is too early to say whether other supermarket chains could follow suit. Nevertheless, the Giraffe deal is one transaction that has demonstrated that the buyer pool, and therefore exit routes for restaurant and bar group owners, is perhaps wider than one might think. This fact will not have been lost on private equity investors.

Furthermore, as the recent Eclectic IPO showed, there is a growing willingness to consider the use of capital markets to raise finance and/or provide an exit for investors. Risk Capital's Luke Johnson recently suggested there was scope for 6 to 10 restaurant companies to go public in the next 6 to 18 months. We expect more companies in the sector to follow Eclectic in the year ahead.

Fuel Juice Bars: *"With its shopping centre locations and freshly made smoothies and juices, Fuel is well positioned to benefit from the long-term consumer trend towards healthy eating and drinking, as well as the shift of consumers away from the high street to shopping malls."*

JAMIE TILLMAN | Kings Park Capital

Looking forward

Ben Redmond of Risk sees the sector continuing to be an attractive one for investors: "The long term trends of eating out remain clear, with the recession re-enforcing the importance of value for money to the consumer at the lower end, and the relative resilience of fine dining at the higher end."

Peter Kemp-Welch suggests the sector's resilience over the last few years highlights the fact it is a good one to invest in: "The industry has been thoroughly stress-tested through the recession and has met the challenge head on, giving investors comfort that, even in tough economic times, restaurant and bar businesses can be successful. There is a culture of creative innovation and a depth of skills in the sector that ensure that will remain the case, and also make it an interesting and exciting one for investors like us to be involved in."

Hawksmoor: *"In Hawksmoor we have invested in a premium restaurant concept that has done well during difficult economic times. We consider it to be the best in its field and it's run by an excellent team that generates very good returns on investment. We are looking forward to helping the business continue its roll-out in London and beyond."*

OMAR KAYAT | Graphite Capital Partners

The BDO view

We expect deal activity to continue, with private equity remaining at the heart of things. There are a significant number of pub and restaurant groups in the hands of private equity, some of which have been held in portfolio for a longer period of time than would have been envisaged when those houses originally invested.

As such, it is likely some will make moves to realise those assets; the deal activity (and the decent multiples being paid) over the last 12 months has given investors renewed confidence in the market, both as a seller and a buyer. This optimism should pave the way for further sector transactions, and we are confident that the capital markets will play an active part in that as more restaurant and bar businesses find that an IPO can give an attractive valuation from a readily available source of finance.

Ron Pearson of Bowmark agrees the sector will remain an attractive one for investors. "I believe there will be a good level of deal activity in the sector over the next 12 to 18 months. Recognition that the sector has proven more resilient than many had expected means bank debt is available for the best businesses. I expect a number of businesses that have grown over the last five years will now be seeking to go to the next stage of development."

The outlook for 2014 certainly whets the appetite. Exciting, differentiated concepts are emerging and looking to expand, PE portfolio companies are seeking new partners to fund the next stage of their growth and exit routes are opening up.

There is more capital available, greater appetite from buyers and improving consumer confidence. The table is set for another year of buoyant M&A activity in the sector.

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EXPANDING RESTAURANT BRANDS INTERNATIONALLY

Asia Brand Partners operate restaurants and retail businesses across Asia as a franchise or joint venture partner and makes it easy for great brands to set up in the growth markets of Asia. Here they give us a view of the key things to be considered for success.

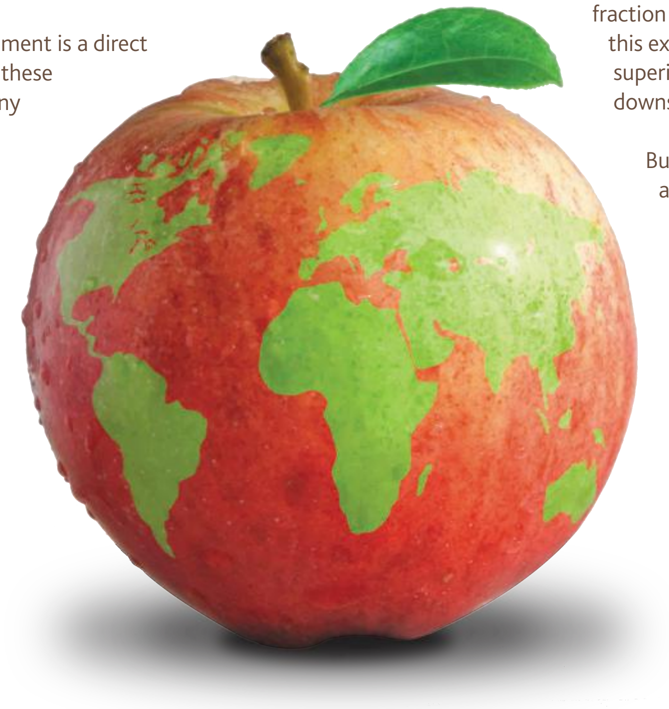
Incredible as it might have seemed in the 1970s, the UK now has one of the world's great concentrations of high calibre restaurant brands. The UK – and London in particular – has become a Mecca for food and beverage, particularly in the casual dining and fast casual sectors. The scene is vibrant and innovative, and remains attractive to customers and investors alike.

This of course gives brand owners the opportunity to explore international expansion. Notwithstanding hard economic times in the West, most of the world is experiencing an unparalleled consumer boom, and in many markets the demand for branded restaurants far exceeds supply. Setting up in these markets can be very tempting, particularly given the high equity multiples in BRICs and N11 countries, not to mention the potential to increase home market valuations.

However, the road to success is littered with broken dreams. The plain truth is that international development is highly attractive but also highly risky. Why? Because of the many variables. Which market? Partner or direct? Equity or franchise? Which partner? Where to start? How to execute? How to structure? How to exit?

Successful market-entry and development is a direct function of how well brands manage these variables. But it's staggering how many of the factors are ignored or poorly managed.

This happens for a range of reasons. Most importantly, serious international development takes time, is expensive and requires material management focus. When trading in the UK is tough and capital scarce, brands may look to cut corners through franchising, selecting apparently easy markets or simply by cutting corners on the process. In the short term it can be seemingly straightforward to study a market, find a partner, do a deal.



It can look as if you have succeeded. But the problems tend to set in further down the track.

There are however several operators who have shown that international development can be managed, so long as there is rigour and attention to detail. PizzaExpress, for example, has invested in a systematic approach to market-entry and has developed a number of successful international platforms, particularly in Hong Kong, India, and Shanghai, as well as in high potential markets such as Indonesia.

For India, PizzaExpress assembled a multi-disciplinary team of in-house experts and external advisers. Then over a 12 month period it developed a detailed business plan, met more than 50 potential partners and struck a joint venture with one of India's most respected business houses, Bharti (who also have partnerships with Walmart and Del Monte). The first site opened in December 2012 to rave reviews, and a pipeline of new sites is planned to create a scale business.

Why did they choose India? Well, Indians love pizza and other Italian food, and the Domino's licensee's equity trades at an extraordinary 30x EBITDA on the Mumbai stock exchange.

Consumers need great quality branded offers and financial returns (ROCE and IRR) are now comparable with the UK, and indeed often greater. Furthermore, the country is only a fraction of the way to being fully developed. To this extent, investors can see the means to gain superior returns and leave material upside for downstream acquirers.

But for every Pizza Express, Yum!, Din Tai Fung and Costa Coffee, there are five examples of sub-optimal international development.

How can brands maximise their chances of success? We have put together our guide to weapons-grade market entry:

GET CLEAR ON THE OVERALL RATIONALE

Why is the brand going overseas? For equity? For revenue contribution? To test the waters? Pret-a-Manger started with a fast expansion (revenue), then consolidated (cost management) and now takes a smart and deliberate approach to market-entry (test market and use equity).

GET THE RIGHT PEOPLE ON THE JOB

Most market development projects that fail tend to do so because the wrong people get involved. Who really knows what they're doing? (as opposed to who fancies a bit of flying around?). Do they have the time? Can they leverage the necessary contacts and network? – these are usually key to success. Do they command the ear of investors?

One of the issues with the topic is that many people are keen to "have a go" at international development, or consider themselves (perhaps mistakenly) as experts on given markets. It's a bit like the phenomenon of everyone claiming to be a restaurant expert, except the consequences in this case can be very, very costly.

PICK THE RIGHT MARKET(S)

This may seem obvious enough, but it can be tough to get right. What you need is a thorough system to analyse the pros and cons of target markets. Take your time, and talk to anyone and everyone. Every market choice is a trade-off so getting clear on the priority selection criteria (versus 'nice-to-haves') is critical. And make sure you use current data, not the online reports that are usually out of date.

GET ON THE GROUND

Obvious? We have lost count of the number of brands who visit for 48 hours here and there, then fly off home. And when on the ground, get close to the action. Grab menus, buttonhole customers, read the local reviews, try everything, walk the streets. Build your own picture of the market – don't rely on consultants and spreadsheets, for you will proceed at your peril.

DO IT YOURSELF

Frankly, partnerships are often the problem. If you can use your own capital, hire local management and keep control, then do so. Finding and managing partners can take just as long and ultimately cost you far more than going it alone. The list of great food and beverage brands in dispute with their partners is very long.

IF PARTNERING, BE A MAKER NOT A TAKER

To find the best partners, you need the best process. This starts with having your own clear business case and being able to sell the benefits of your brand. Other than McDonald's or Starbucks and a few lucky others, selling is a must. Don't assume confident businesses in growth markets will be easily impressed. The good ones usually have many partner approaches a month.

IT'S NOT PARTNER OR BUST

If you can't find the right partner, move on. Admittedly, this can be easier said than done, so someone in the organisation needs to have the permission to say "No" even at the most advanced stage of the process. Bad partners can destroy value and make it harder in other markets. Remember you are playing a long game.

FACE UP TO THE BIG OPERATIONAL ISSUES

At a consumer demand level, most emerging and growth markets are attractive. The big issues arise usually in relation to accessing affordable real-estate, the ability to price to market, and building the team. Get clear on the level of these barriers at an early stage. Everyone loves the idea of Hong Kong until they've done their first round of landlord meetings…

GET YOUR BEST PEOPLE ON THE CASE

If you're serious about going international, it needs your A Team. These people need to be dedicated to the task. Over time build the kind of expertise that Yum! or McDonald's have in-house – but do it your way, and don't copy models that may be better suited to large US listed companies.

LOCALISE THE BUSINESS NOT THE PRODUCT

Unless you have a Fortune 500 balance sheet, it's unlikely you'll target very early-stage and highly disorganised markets where product customisation is a must. Stick to your guns on the product but think and act as if you were a great local business. GE and Lever have cracked India because they figured this out early.

There have never been so many international opportunities for good brands. In fact there are too many. What's needed is good prep, local experience and persistence – in fact, the same skills and attributes you find in great chefs. Great F&B brands don't take shortcuts in the kitchen and they shouldn't take them internationally. By going about it in the right way, the UK can conquer the world in F&B and create exceptional value for shareholders – as well as some familiar destinations for us weary travellers.

Asia Brand Partners (ABP) is a joint venture between IMM Associates and Vermilion Partners, both emerging markets advisers and investors with operations across Greater China, India and Asia. ABP is expert in helping great brands succeed in new markets as their franchise, licence or JV partner. www.asiabp.com

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THE GROWTH DILEMMA

BGF was established in 2011 to help Britain's growing smaller and medium sized businesses. Their aim is to recognise businesses that have real potential and desire to succeed and provide a collaborative approach to financing growth. BGF have often provided capital to concepts before other investors and banks would be willing, and here they share some of their recent investments in the sector and why they considered these good opportunities.

Despite the talk of doom and gloom on the high street, the UK's passion for dining out has rarely been hotter. New concepts launch every month, successful brands are looking to grow at pace, and there is fierce competition for good sites, especially in London.

"The restaurant sector offers enormous potential for growth as tastes and trends are constantly changing. The profile of this market is such that word of mouth can increase popularity very quickly and drive growth. It is also a sector where there is very real opportunity to take regional successes onto a national stage, and in so doing create new jobs."

ANDY GREGORY | Regional Director, BGF

If you are a strong operator with a good concept, it is a great time to be in the business. More people are eating out more often, and in recent years UK diners have become ever more demanding. They expect quality, variety and good service wherever they eat, and they want brands that deliver on their promise at the right price point.

Yet expanding a restaurant business requires significant investment. And although the broader climate may feel conducive to new openings, the problem of just how to fund site rollout hasn't gone away.

It may be possible to finance some additional openings with cashflow generated at existing outlets, but this is likely to be a slow process and the resulting delay can mean missing out on prime sites, or seeing competitors steal a march. The current competition for prime sites demonstrates why it is so important to have the funds to move quickly.

Bank debt may be a solution, and the cheapest option, but it is likely to come with strict performance-related covenants and the amount may not be sufficient on its own. When unexpected difficulties are encountered during development, or a new site takes longer than expected to mature, such covenants can leave a burgeoning business vulnerable.

That is why equity finance can often be a better answer. It provides the capital that you need up front, without the expectation of repayments in the short term, and before any new investment has begun to deliver a profitable return.

A growth capital investor like BGF will also provide more than just money. The feedback that we get from business owners suggests that our partnership approach, providing counsel where required and sharing expertise, guidance and contacts, is just as valuable to them as the capital that we inject into their businesses.

BGF has already invested c.£30 million in six leisure and hospitality businesses based across the UK. These businesses are proving that despite the difficult economic climate, it is possible to prosper and grow with the right business plan and the support necessary to underpin that growth.

Common to all the businesses we have backed is a strong management team. We only ever take a minority stake in a business, so ultimately it is the management team above all that we are investing in, and it is that team that will run the business.

We are looking for teams with a track record, clarity of vision, passion and profound commercial sense. Successful scalable concepts exist at all price points and in all areas, but they share a robust strategy and a clear understanding of their customer. The breadth of opportunities is illustrated by the companies that we have already invested in.

In March 2012, BGF invested £3.25m in Barburrito, a Mexican restaurant chain with six outlets in the North of England. The investment kick-started a national rollout programme, with Barburrito planning to triple the number of restaurants that it operates within four years.

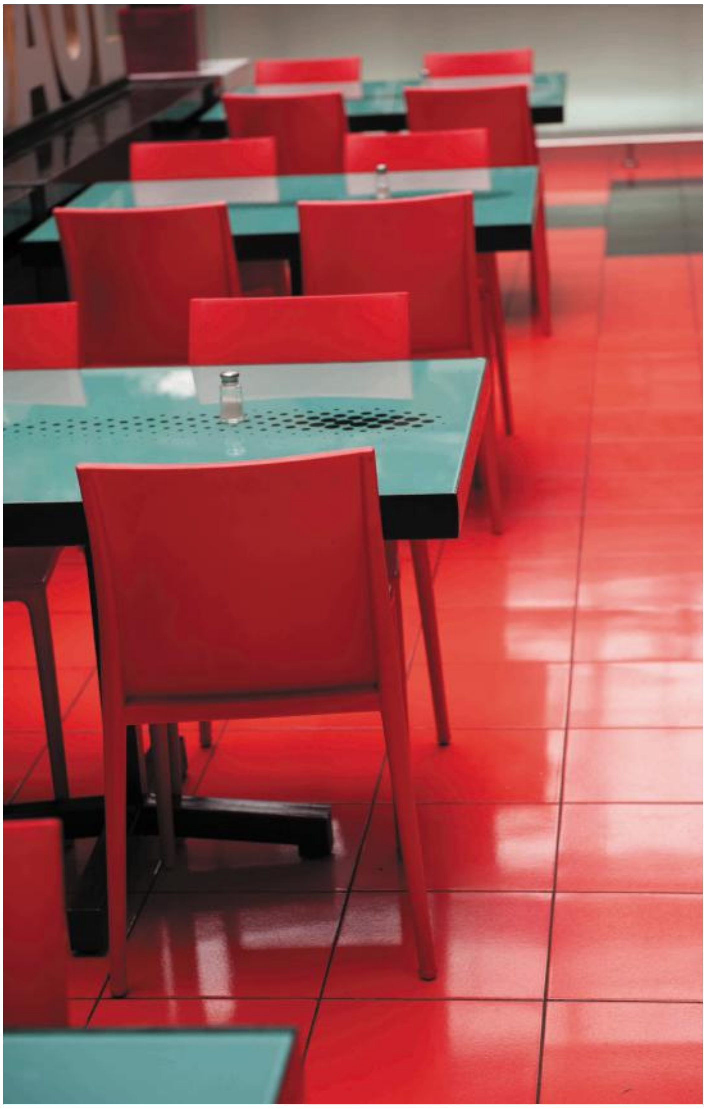
We made a similar investment in Camino, a group of London tapas bars. Our £3m is allowing the management team to build further brand awareness and expand the concept across a number of new locations.

"Instead of worrying about cashflow, we now worry about growth, which is a much happier problem to have. In the past we've definitely missed out on opportunities because we didn't have the funding to cope with more than one project at a time."

OLIVER PEYTON | Founder, Peyton and Byrne

"With BGF, we've been able to turn on the hosepipe, not least because the money has given us real credibility when we talk to landlords about securing leases. We've already got 4 new stores at the final stage of legal discussions and we expect to add 10 more in each of the next 3 years; we could never have contemplated that sort of growth prior to this funding."

RICHARD O'SULLIVAN | Founder, Boost Juice Bars



For Barburrito and Camino, as for most of our other investments, BGF's ability to provide follow-on capital is very important. Furthermore, because we invest from our own balance sheet we can also live up to our claim to be a long term investor. BGF can continue to provide capital to build on success. Boost Juice was launched in the UK by Richard O'Sullivan, a serial entrepreneur with a track record that includes the development of Millie's Cookies.

We have invested £2.5m to dramatically accelerate rollout of the chain, capitalising on consumer demand for healthy food and drink products. As a result 10 new sites are set to open in each of the next three years.

BGF has also backed Peyton and Byrne with an equity investment of £6.25m. Founder Oliver Peyton recognised that he needed external funding to realise his vision for high quality public catering and for a new chain of specialist British bakeries, in which both parts of the business would serve customers' increasing expectations for quality and service wherever and whenever they eat out.

However, Oliver was determined to continue trading as a family business rather than ceding control, and BGF's minority stake investment met that requirement.

Finally our £8m investment in Durham-based Wear Inns demonstrates that growth doesn't always come from an innovative concept or exotic cuisine. Wear Inns' strategy of turning round underperforming pubs is simple and highly effective, but it does require significant investment. With £8m from BGF and additional investment from an existing investor, the pub chain has already been able to add 11 new pubs to its 15-strong portfolio.

What should now be clear is that there is no typical BGF investment. Nevertheless, there are some common themes and traits. All of these businesses could demonstrate a proven concept across several sites and show a strong return on capital invested. Most crucially, every entrepreneur we have backed has ambitious plans for the future and a realistic roadmap for getting there.

With BGF's capital and wider support, we believe that they are each a little closer to realising their aspirations.

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HOTELS: A TASTE OF SOMETHING DIFFERENT

Something big is happening to food and drink in hotels, and it's happening worldwide. Hotels are looking at their restaurants and bars in a new light. The food and beverage department has of course always been an integral part of a hotel's operation – but now it looks increasingly pivotal to a hotel's success as BDO's Govinda Singh explains.

Food and beverage (F&B) has gone from being merely a "must have" space to being one that, if managed correctly, could be a major destination, attraction, and profit generator in its own right.

What is offered will of course depend on each hotel's market positioning and the facilities within the building. Some hotels have substantial meeting and function facilities which distort the picture as far as our review is concerned, so for the purposes of this article we have ignored the conference and banqueting side of hotel F&B operations.

Nevertheless, in broad terms the food and beverage concept in hotels is being reinvented, given the huge development of the eating out market as a whole, especially in mature markets where there is now a plethora of choice. What does this mean for hotels and indeed restaurateurs – most notably in the UK?

The UK is often the guinea pig for creativity in F&B, the key market in which new concepts are tested – even if those concepts started life elsewhere, such as in the USA or the Far East. Examples here include "super foods", the cupcake craze, American BBQ, cocktails and street food, as well as the gourmet hamburger joint (Five Guys, Shakeshack), the single and dual dish restaurant, Bubbledogs, Burger and Lobster, Tramshed (chicken and steak) and Dirty Burger. If it works in the UK, the signs are good.

Faced with a multitude of pressures – the need to maximise 'other' revenue and space, rising food costs and wages, and the increasing choice for the discerning palate in city centre locations – hotels have had to raise their game when it comes to food and drink.

Gone are the days when a hotelier could just focus on the rooms side of the business – now, with room occupancy and average rates at some of their highest levels yet (especially in London), there is little upside to manoeuvre. So owners must look at other ways to improve returns on their investment.

Food trends in hotels

There are some interesting trends out there now. A popular one – though of debatable impact for hotels so far – is the collaboration between a hotel and a renowned chef, such as Heston Blumenthal at the Mandarin Oriental, Marcus Wareing at the Renaissance St Pancras, or Gordon Ramsey at the Marriott Grosvenor Square.

Admittedly this may work for the upscale and luxury brand hotels, but what about the mid-scale and boutique sectors?

A possible answer here lies in the High Street coming into hotels, as we have seen in the proliferation of the big coffee shop brands, think Starbucks, Nespresso and Costa.

Hotel restaurants have also shown an aptitude for keeping up with food fads or the latest diets. Not so long ago fresh, local produce and high-quality products were a novelty – now most customers expect them.

And the ever-popular cocktail has recently hit new heights of fashion, particularly within hotels, with more ingredients, more exotic varieties of spirits, flavoured syrups and even ice cubes, and serving is becoming an art in itself: how about a touch of liquid nitrogen, with flavoured smoke, in an Alice in Wonderland glass?

They're even playing with time: the rise of the digestif cocktail on London menus means that cocktail hour can now be after dinner.

A recent suggestion from the hotel industry is that the term "food and beverage" could make way for "food and fitness". There is a growing trend and demand for hotels to have light and healthy options on menus for both adults and children.

Hotels will also need to think more about how to cater for the world's ageing population, with food and beverage offerings to reflect the health requirements of older people, a key target market that will only expand.

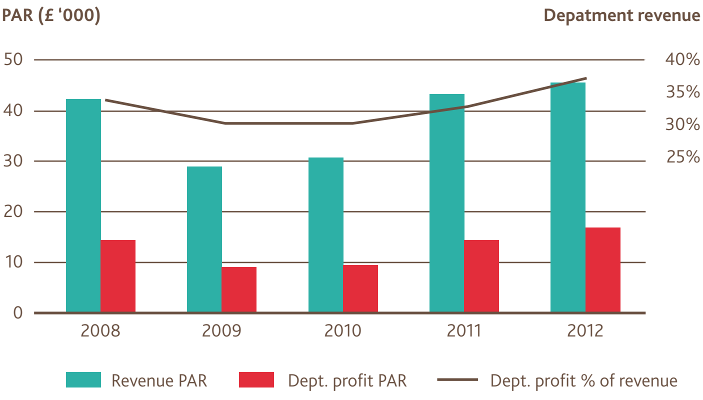
Finally, shifting trends in inbound travel are bringing new visitors to UK shores, such as from China and other emerging markets. Hotels are already responding with more diverse menu offerings aimed specifically at these new markets, and chefs too are no doubt honing new skills!

HOTELS: A TASTE OF SOMETHING DIFFERENT

Do hotels benefit from investing their own money in F&B?
History would seem to be against it. A full food and beverage service offering is hugely labour intensive and thus not so profitable as rooms. Indeed, many hotels have tended to run this department at a break-even, or even at a loss to attract guests (much like the swimming pool in a city centre hotel). So is it a bit of a radical idea to suggest that it should actually contribute more to the bottom line? Can it be done – and is it worth all the hurdles involved in getting it right?

What do hotel guests spend on F&B?
Our BDO database shows us the performance of upscale London hotels (excluding those properties with significant conference and banqueting facilities to allow a more balanced comparison) in terms of annual Food and Beverage Revenue per sleeper. We can see that this is varied, with an average of £39.35 per sleeper for the hotels sampled; however, if one excludes the seven top performers, this drops to £24.53. One interesting detail was that the best performers were either in the W1/Knightsbridge area, or near to major commuter stations. This is no surprise, giving the high footfall of such locations and the typically upmarket affluent clientele.

Upscale London hotels food and beverage PAR trends 2008-2012



Source: GfK, NOP, ICAEW

Within the upscale sample of hotels analysed, this translates to average revenue of £28,899 per week. Excluding the luxury properties, some of whom already have a well established fine-dining experience this reduces to circa £18,580 per week. For many restaurateurs these can be considered good 'base' numbers and we all know what the value of a good brand could potentially do to increase these numbers further still.

So what does this mean for restaurateurs?
In this author's opinion, there is clearly a symbiotic relationship that could be further explored between hoteliers and restaurateurs. Think Trader Vic's relationship with Hilton, Gordon Ramsay at the Savoy, and Nobu at the Metropolitan.

A full-service hotel needs to provide breakfast, lunch and dinner to guests, but this can be within the combination of one or more restaurants. A partnering or straight rental arrangement with a food brand is an opportunity for hotels to rent 'dead' or outlet space to a restaurateur.

This benefits both parties in a number of ways: the hotel is able to offer a recognised 'fine-dining' or alternative experience, thus enabling it to concentrate on its core activity, the business of selling rooms. A source of rental income provides the hotelier with less distortion in cash flows, and indeed if managed correctly, can become an attraction to the hotel itself.

For the restaurateur, it provides an opportunity to have an establishment in a good location, which can provide instant visibility, whilst having a 'base' source market of guests in the hotel. Having this base market in the first instance immediately allows the restaurateur the flexibility to concentrate on what it knows best, ie food and service and build on the strong F&B spending levels noted above. On the downside, access and branding issues can be a challenge for restaurateurs, as can the need to provide breakfast and occasionally room service, not part of their core business.

Clearly, the right concept must fit the right hotel, and issues such as revenue/profit sharing and access will need to be addressed from the outset, not in hindsight. But clearly this is an opportunity which should be explored by both sides further.

A glance into the crystal ball

So we cast our eyes towards the future, and some possible trends to look out for. We can expect to see more menu-pairing with cocktails and beer, not just wine. In the UK this is very much in its infancy but is gathering pace, thanks to growing enthusiasm such as the recent 'Let There Be Beer' campaign.

We should also see hotels further developing the existing "pop-up restaurant" concept, which has proved the most popular of the pop-up ideas (the others including art galleries, shops and salons). It can be a way for a hotel to earn revenue from otherwise dead space, particularly during periods of low demand. Recent examples include Nobu's presence in Claridges (2012) and the Crustacean Bar on the Terrace of The Churchill Hotel near Marble Arch (June 2013).

Expect greater customer customisation of food and drink, too. Although this is mainly being seen in the restaurant sector, there are examples of it creeping into hotels. The most recent example is the interactive sushi station at Jumeriah Carlton Towers, which forms part of their live canapé stations for meeting and events, and the smoothie bar at the Four Seasons for corporate and other guests.

A move towards more female-friendly environments comes not a moment too soon. Already being rolled out in hotels as part of their rooms offering, this (perhaps obvious) idea is also being tested in the restaurant and bar areas, which may historically have been intimidating for single female travellers.

Finally, there is a growing notion that restaurants and bars operators can translate their business or their brand into a successful hotel concept, with early examples being the Buddha Bar, Soho House and Hard Rock.

This looks like the flip-side of the trend we have been talking about: just as hotels are putting more effort into their restaurants and bars, successful restaurant and bar brands are aspiring to open hotels.

Both sectors are hankering for something that the other can offer – so perhaps it will be a natural synergy for the two to cohabit. As ever, time – and the bottom line – will tell.

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OUR TOP 10 PREDICTIONS FOR 2014

1. RETURN OF THE SECTOR IPO: 2014 could be the year when capital markets re-discover Restaurants and Bars - expect more flotations than for many years.

2. CONTINUED STRENGTH OF THE M&A MARKET: After struggling until recently, 2014 will see continued M&A activity.

3. MORE POP-UPS AND MOBILE UNITS: As the demand for 'street food' continues to go from strength to strength, operators will utilise extremely short term leases or mobile units in order to create an exclusivity surrounding their offerings.

4. MORE SINGLE ITEM MENUS: With the younger generation of diners regularly enamoured with the idea of trying the 'best' of a certain dish, expect to see more operators opening single item restaurants where they do one dish extremely well.

5. GOURMET FAST FOOD: 2013 was the year of the gourmet burger; 2014 will see demand for other forms of gourmet fast food hit the spot light - chicken wings, ribs etc still have room to grow.

6. RESTAURANTS IN RETAIL STORES: As retailers look for innovative ways to drive footfall, expect the more savvy retailers to start offering dining experiences in order to increase dwell time.

7. THE RISE OF THE PUB: Growth in consumer spend in pubs will rise by more than growth in spend in restaurants as they food-led pubs continue to improve their offer.

8. DISCOUNTING REDUCES: As operators look to improve margin, the focus on discounting will diminish. This will be in small stages, however, so don't expect them to disappear but they will become more focussed and less frequent.

9. DEMAND FOR QUALITY AND PROVENANCE WILL GROW: Dishes containing ingredients with protected designation of origin will be increasingly sought after.

10. HEALTH DRIVE CONTINUES: The UK's health drive won't be tempered this year as consumers will continue to try and watch their waist lines, particularly during lunch hours.

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