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DC Discusses: Is private equity holding the check for Restaurant M&A?

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Overall, the Restaurant sector has exhibited remarkable resilience in light of economic pressures and consumer demand – diner preferences may vary, but they will continue to eat out. Despite being at the cross-section for wage, food, and energy inflation, restaurants continue to open, grow, and invest. However, the path has not been a smooth one for all, and concepts that have not been able to differentiate and move with the trends have struggled and lost market share.

In our latest article, DC Advisory's global Consumer team explores the themes and trends impacting the Restaurant sector and what they suggest for long term deal flow, including:

- The pressured consumer's ever-present need for value
- The importance of differentiating restaurant offerings in a saturated market
- The driving force of Japanese buyers
- The changing landscape as assets mature and the market stabilizes

The importance of value

In response to economic pressures tightening wallets, consumer spending patterns and habits have changed over the past few years. Despite the initial increase in restaurants' footfall following their reopening post-Covid – August 2020 restaurant reservations in the UK were up by more than half compared with pre-Covid August 2019¹ – subsequent Covid strains across Europe and the US caused this boom to be short lived. As consumers 'traded down' to maximise value, we have observed increased interest in the fast casual segment of the Restaurant industry, especially within Quick Service Restaurants (QSR), across Europe, the US and Asia. August financial reports demonstrate this: Burger King UK's total revenue for 2023 increased 30%²; Taco Bell's international sales grew 4% for Q2 2024³ and Tim Hortons Q2 2024 comparable sales rose 4.6%⁴. The size of this space is expected to reach \$192.4bn by 2030 in Europe⁵; \$454.3bn by 2030 in the US⁶; and \$236.3bn by 2030 in Japan⁷.

Across Europe and the US, we see casual dining and QSR activity dominate the Restaurant market -

- In January this year, CVC announced its acquisition of La Padieneria, a leading Italian QSR chain with more than 400 locations across the country, from Permira, the private equity firm which acquired it in 2018⁸

- Last December it was reported that HIG had appointed an advisor to handle the sale of its majority stake in Quick, France headquartered burger restaurant chain, after acquiring it in 2021 for €240m⁹
- Last January, McWin acquired a majority stake L'Osteria, Germany's Italian themed casual dining chain¹⁰. We have observed this private investment firm be a very active and focused restaurant investor in Europe, identifying strong growth concepts and turnaround opportunities. McWin's portfolio¹¹ includes QSR franchises such as Burger King and Popeyes, as well as chains with a strong retail presence, such as Big Mamma Group and Gail's. The Gail's financing was provided by Bain Capital Credit in 2021, advised by the DC Advisory team¹²
- In August this year, restaurant group Bill's announced the opening of multiple locations across the UK over the next two years, following record sales and a return to profitability¹³
- In June, Karali Group (former UK Burger King operator; sold the business in 2022 to Burger King) finalised two major acquisitions. First, by acquiring 46 restaurants from franchise owner Taco Bell Corp, Karali Group became the UK's largest Taco Bell operator.¹⁴ Additionally, Karali Group acquired Crosstown, the UK handcrafted artisan doughnuts multi-channel operator, and its 27 locations¹⁵
- In September 2023, US based Roark Capital

Group acquired Subway for \$9.55bn, marking the fourth largest deal in the region since 1995¹⁶, and demonstrating the ongoing opportunities for QSR chains as Subway boasted three consecutive years of global net growth following Covid¹⁷

In the pre-Covid landscape in Spain, private equity players were, in our view, driving consolidation in the industry, growing portfolios with restaurant chains in a bid to grow and increase efficiencies. Despite the landscape becoming more difficult in recent years, we are seeing this consolidation trend persist. Earlier this year, we advised Manolo Bakes on the sale of a minority stake to VGO, UK based private equity firm¹⁸. The sale intends to support Manolo Bakes, a Spain-based coffee bakery chain with 50 stores in cities across Spain, in its next growth phase since opening in 2018. This transaction also aims to consolidate Manolo Bakes' position in the Spanish market and aid international expansion. We foresee this trend continuing until they reach critical mass, at which point, strategic buyers should take notice.

We expect to see a continuation of activity from strategic buyers in the form of highly performing restaurant companies looking to build or rebalance their business. In December 2023, AmRest, a Madrid based restaurant operator of casual dining chains and QSR franchises in CEE, including Burger King and KFC, announced it was considering acquisitions to enhance and finetune its existing portfolio¹⁹. This announcement followed a year of record sales across AmRest's restaurant assets across all regions, with CEE representing the highest growth, making up 55.2% of revenue²⁰. As well as the recovery of dining-in at its 2,100 restaurants²¹, we believe stickiness and increased digital sales since Covid, have been growth drivers for the group.

In Japan, the casual dining format receives significant attention from consumers and investors alike. We have observed the dominance of major food chains in Japan remain relatively unchanged in recent years, and as a result, companies in the space may be hesitant to make dramatic moves. In May this year, we advised Carlyle Group, the US private equity group, on its take private of the largest Japan franchise of KFC²² for \$835m. The acquisition, once completed, will mark an exit for Japan trading house, Mitsubishi Corp, previously the parent company until 2015²³. For domestic players, Japan's unique 'shareholder benefit system'²⁴, has raised valuations and can lead to misaligned investor expectations and a small decline in investments for those publicly traded assets.

The importance of differentiating

When consumers dine out, they expect to be impressed and are increasingly demanding a differentiated experience. A recent survey found that 52% of UK consumers now have higher expectations of hospitality brands they regularly frequent²⁵. In a competitive and saturated market, those restaurants that are able to differentiate their offerings will have a competitive advantage. We are seeing this manifest in various ways –

- **Authenticity.** Across Europe, Asia and the US, SME restaurants with authentic cuisine offerings and/or social responsibility efforts are rising in popularity²⁶ with the consumer. Rockfish Group's successful equity financing earlier this year, a seafood restaurant group based in the UK, was awarded by the £200m British Business Bank's Southwest Investment Fund. The group boasts sustainability in its seafood procurement supply chain across its eight restaurants and two takeaway locations, and the funding is intended to support the group's expansion²⁷. The popularity of traditional Japanese cuisine in the US²⁸ and Europe also provides a good entry point for Japan-based corporations looking to expand internationally. Japanese fast food restaurant chain Yoshinoya announced its Europe expansion earlier this year, with plans to open its first restaurant in Edinburgh²⁹
- **Luxury.** In Spain, we are seeing Michelin starred restaurants rising in popularity with consumers and investors alike. For the consumer, it represents luxury and celebration; for the investor, it represents an opportunity to invest in the chef's popularity and skill. We saw this in April with the acquisition of a €44m stake in GDG (Grupo Dani García), restaurant group owned by internationally known Michelin-starred chef Daniel García, by Kharis Capital, Belgium based private equity fund³⁰
- **Social competitive.** In the UK, we are seeing social competitive offerings grow in popularity in recent years. Following the Covid and post-Covid time of limited interactions, consumers are responding well to the experiential side of socialization. State of Play Hospitality, operator of multiple social competitive concepts including Bounce and Flight Club, reported a 20% increase in pre-booked revenue compared with pre-Covid levels and is reportedly seeking a partner to aid expansion into Europe³¹
- **Robotics.** We are seeing a greater desire to bring robotics and automation technology into restaurant

spaces, both front and back of house. As a high initial cost, we believe that these advancements will be trialled in established chains or by innovative founders before smaller concepts take the risk. Big Table Group, restaurant operator of UK chains such as Las Iguanas and Bella Italia, announced a pilot partnership with Pudu Robotics, a China based robotics company manufacturing for the restaurants industry in 2022, marking the largest UK based restaurant group to introduce robot technology to date³². Coupled with rising labor costs across the US and Europe and the significant shrinkage of available workforce in mature economies, we believe this technology is likely to be explored in restaurant offerings increasingly, especially back of house, in a bid to increase efficiency and reduce the need for human labor

The importance of Japanese buyers

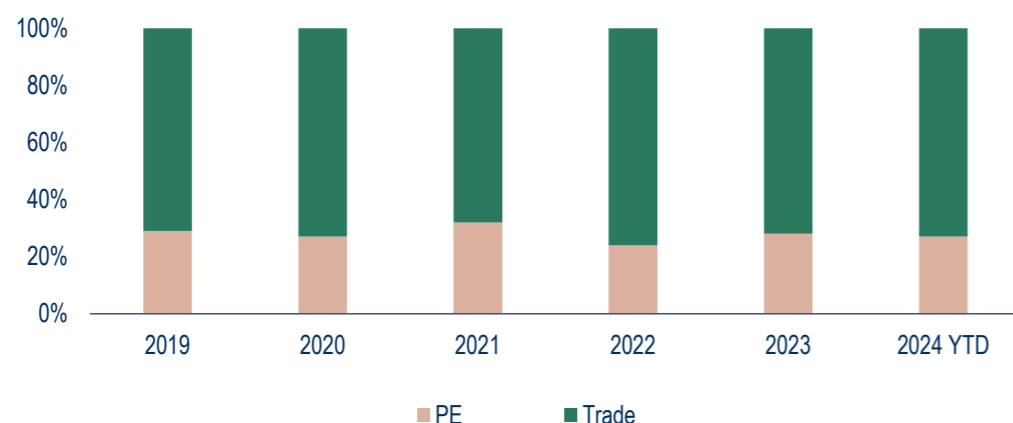
As a result of post-Covid market uncertainties, the current market landscape in Europe and the US is heavily populated by private equity owned restaurants assets nearing maturity. We have seen trade buyers dominate this sector's investor landscape in recent history, and this trend has continued into 2024 - this year so far, 73% of global transactions in the space were trade led³³. Once private equity buyers observe a stability in the sector and have their faith renewed, we believe they will become more active.

We have observed Japanese strategic and trade buyers driving activity in Europe and the US, providing exit

opportunities for private equity owners. Zensho Holdings, a Tokyo-based operator of fast-food restaurants, acquired SnowFox Topico, the sushi restaurant operator and manufacturer based in North America and the UK. The transaction, completed in September 2023, marked the largest Consumer exit in the UK for 2023³⁴. Zensho also acquired Sushi Circle last year, a leading sushi bar concept in Germany³⁵, marking its entry into the German market. Earlier in 2023, Toridoll, the Japanese operator of popular chains Wok to Walk and Marugame Udon, acquired Fulham Shore, UK-based operator of chains Franco Manca and The Real Greek, for £93.4m³⁶. Subsequent coverage stated that Toridoll was actively exploring further acquisition opportunities in the UK, identifying it as an area with long term opportunities³⁷.

In Japan, as many companies have returned to pre-Covid performance in FY23/24 and entered a growth phase, we are not seeing many large scale sell offs. We are however observing more SME restaurants (with a strong regional presence) considering M&A options with larger corporations to explore expansion and we believe this trend is likely to grow as external issues persist (labor shortages, rising costs of materials and utilities). As a result, we believe the gap between large corporations and SMEs may widen. In June this year, we advised³⁸ Ant Capital Partners on the sale of its shares in Amino, a Japanese sushi restaurant chain, to SRS Holdings, the largest Japanese family restaurant chain³⁹. Moreover, we have observed many Japanese restaurants struggle to develop laterally without a capital injection or M&A expansion. Essentially, we believe restaurants looking to accelerate growth, scale, and diversify, are seeking out M&A for the opportunity to do so.

Global transactions in the Restaurants space 2019-2024 YTD



Source: Mergermarket: Transactions announced in the Restaurant sector (75-500m GBP disclosed deal value, undisclosed value deals also included) between 01/01/19 and 30/08/24, with transactions categorized as led by private equity or trade

The importance of patience, stability, and optimism

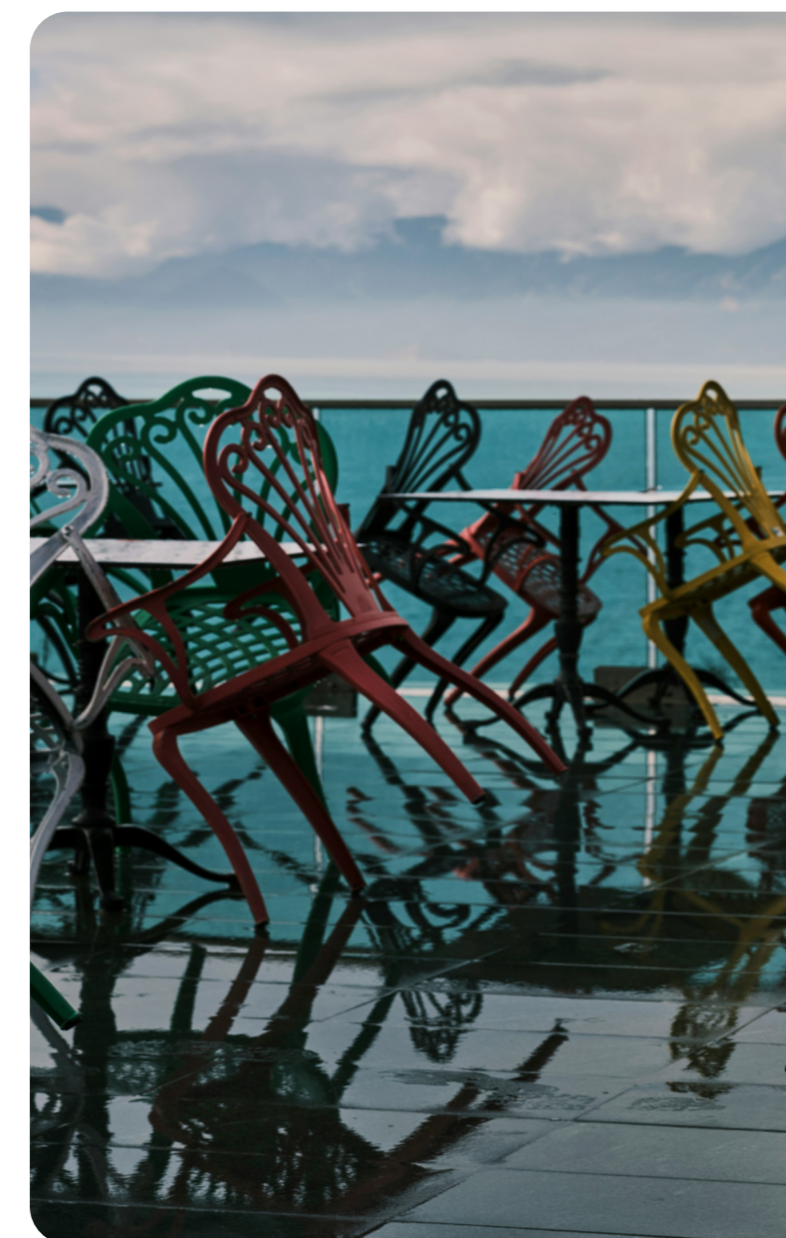
The restaurant market continues to fight against overwhelming macro-economic headwinds. Inflation across food⁴⁰, wages, and energy, are hitting all margins of the Restaurant industry. During Covid, major parts of the workforce left the sector for good, choosing other lines of work or moving elsewhere. Smaller players or players in locations outside of major population centers simply cannot find workforce anymore, but the drop in available workforce and in the quality of personnel is also affecting bigger players. Labor costs have continued their upward trend across Europe and the US over recent years, with the national living wage increasing by 9.8% in the UK this year⁴¹ and minimum wage in the US for hospitality workers increasing on average by 29% over the last four years in the majority of states⁴². Post Brexit legislative changes in the UK – such as introducing work visas and increasing the minimum salary threshold for entering European workers⁴³ – have also negatively impacted the hospitality industry workforce. In addition to these headwinds, there is a highly cautious attitude among investors following previous experience in the sector, urging new players to tread carefully and existing investors to wait for conditions to improve and the market to reopen. We believe those without patient capital are not currently interested in entering the market.

Despite these headwinds facing the industry, we believe there is reason for optimism for this sector over the next few years. Global economies seem to be stabilizing^{44 45} despite the inflationary pressures discussed, suggesting the peak of difficulty has seemingly passed. The German market has shown strong signs of recovery in sales, with hotels arriving at pre-Covid levels and Restaurants not far behind⁴⁶. Looking toward the end of the year, reducing rates should help on the valuation and financing front for some businesses in the industry.

Maturing restaurant assets must be released, and we can see that their 'unnatural' PE owners will be keen to release them when possible. Buyer scrutiny will likely remain high for assets with sustainable and further growth potential. There has been a shift in who the consolidators are and one of the challengers for targets of size is the limited number of truly international, multi-brand platforms. At some stage these companies may have to explore the public markets as a potential exit strategy.

So, who's holding the check?

We believe the worst is over in the Restaurant industry, and it is now a question of patience. Restaurants that have weathered the storm of the past few years have proven to be resilient, well-run, and well-differentiated. The sector can prove to be attractive, providing high growth, strong cash generative characteristics, but it's likely to be a sector for investors with an "acquired taste". We expect investment activity to continue to be good for smaller chains seeking investment and generally for QSR style formats. For the more sizeable portfolios, in the short to medium term, investment activity is likely to stem from strategic investors, including international or PE backed trade, or more opportunistic investors. What is certain is that there are a number of chains held by PE and lenders for some time that will want to transact as soon as circumstances allow them to do so.



To discuss any of the themes and trends explored in this article in more detail, please contact the authors below or our global Consumer, Leisure & Retail team [here](#) >

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