



HUNGER FOR GROWTH

**UNLOCKING  
OPPORTUNITIES IN  
HONG KONG  
FOOD & BEVERAGE RETAIL**



# INTRODUCTION

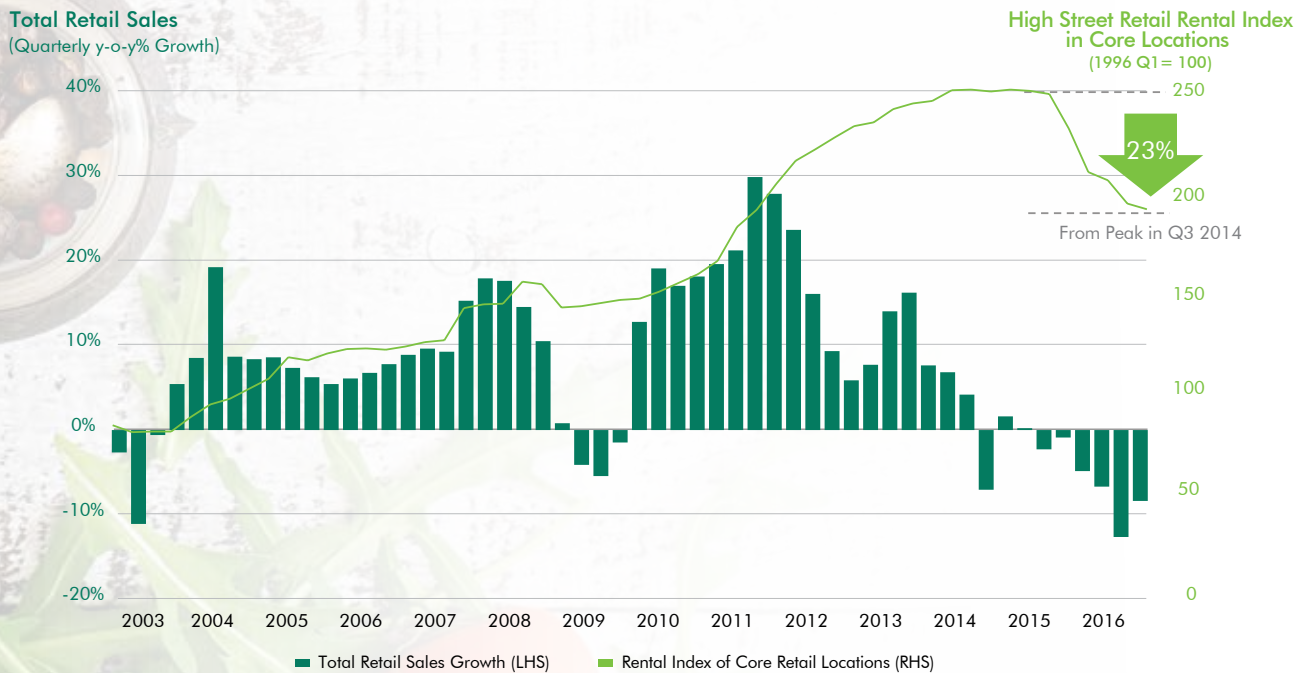
In September 2015, a CBRE Research Major Report entitled The Changing Retail Landscape – How to Survive the Slowdown in Hong Kong explained how the Hong Kong retail sector is undergoing a structural transformation that will result in a more balanced and sustainable market.

Total retail sales in Hong Kong have registered a y-o-y decline in almost every month since late-2014, with sales of big-ticket items such as watch and jewellery recording a double-digit fall for 22 out of the past 30 months. Luxury brands and tourist-oriented retail trades have scaled back their operations, but mid-market retailers and non-consumption goods-driven retail trades have

continued to expand. Shop landlords have become increasingly flexible, with prime street shop rents falling by an average of 23% since the market peaked in Q3 2014.

In contrast to other retail trades, the food and beverage (F&B) segment has weathered the slowdown well, and retailers in this segment retain a positive outlook towards expansion. This major report explains why the F&B sector has been so resilient; how the real estate sector has responded to growing demand from F&B retailers; and provides advice for retail landlords and F&B tenants on how to unlock opportunities in what will continue to be a very challenging market.

Figure 1: The "Retail Golden Decade" has gone



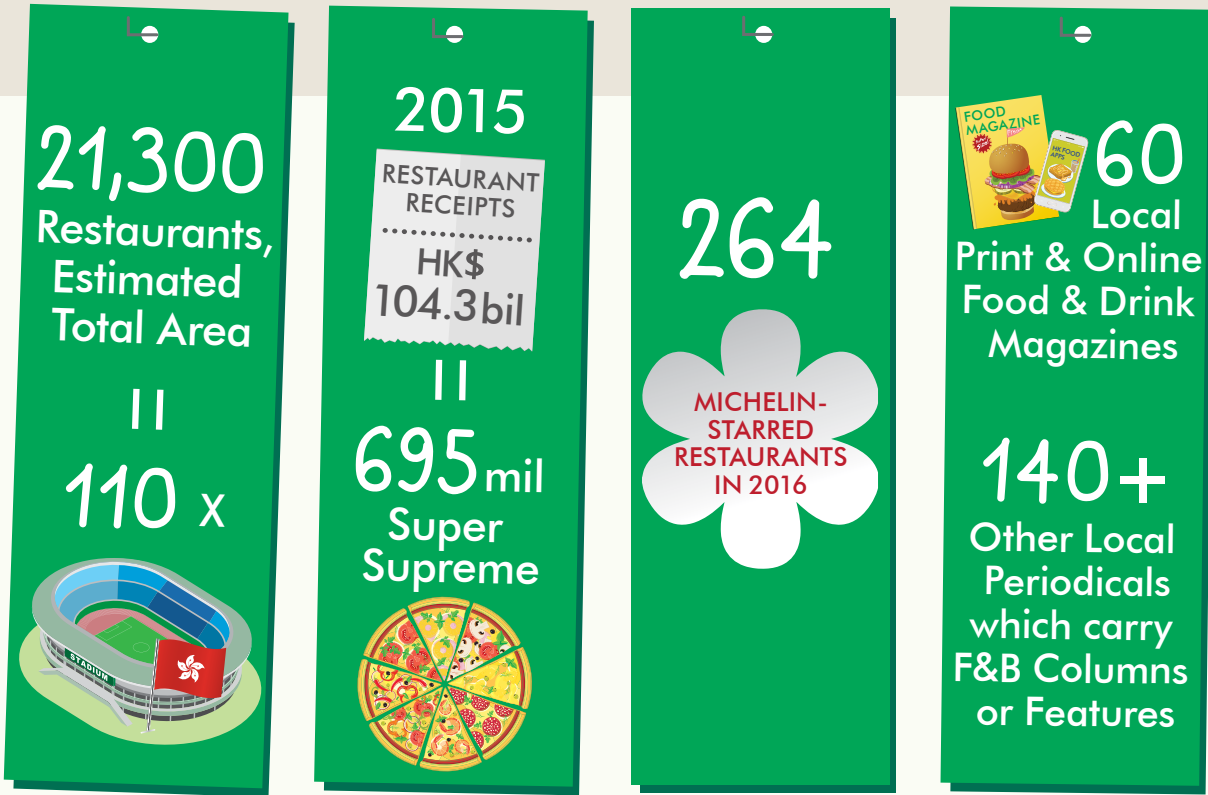
Source: Census and Statistics Department, HKSAR, CBRE Research, Q3 2016



# Hunger for Growth

## Unlocking Opportunities in Hong Kong F&B Retail

Hong Kong F&B Segment at a glance



### Why F&B is popular in HK?

- Long working hours
- Packed living environment
- Long opening hours of restaurants
- Market breadth and depth
- Eating out as a culture & lifestyle
- Media & technology

### How has the real estate sector responded?

- Ginza-style buildings & revitalized industrial buildings as alternative options
- Fine-dining in premium Grade A office buildings
- Emergence of eating and drinking hubs in neighbourhood areas
- Larger share of F&B space in malls

### Good outlook for the HK F&B sector

- Inelastic demand for food
- Eating out culture beyond a necessity
- Sustained packed living environment
- Demographic changes
- Better rental affordability of F&B operators
- Strong government support



CBRE RESEARCH  
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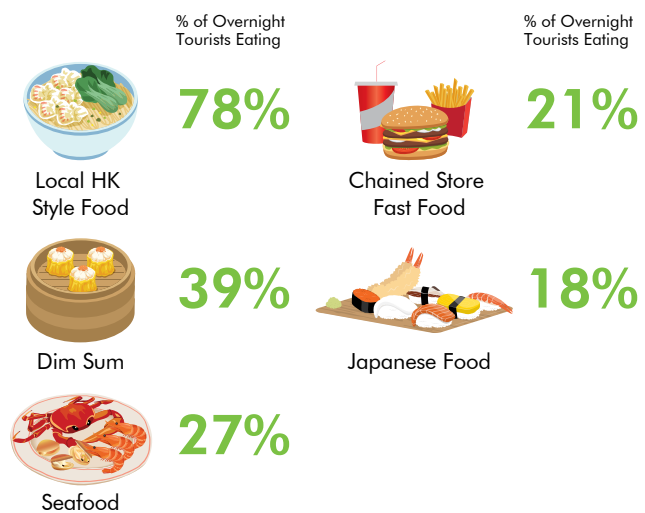
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## F&B – A MORE RESILIENT SECTOR THAN GENERAL RETAIL

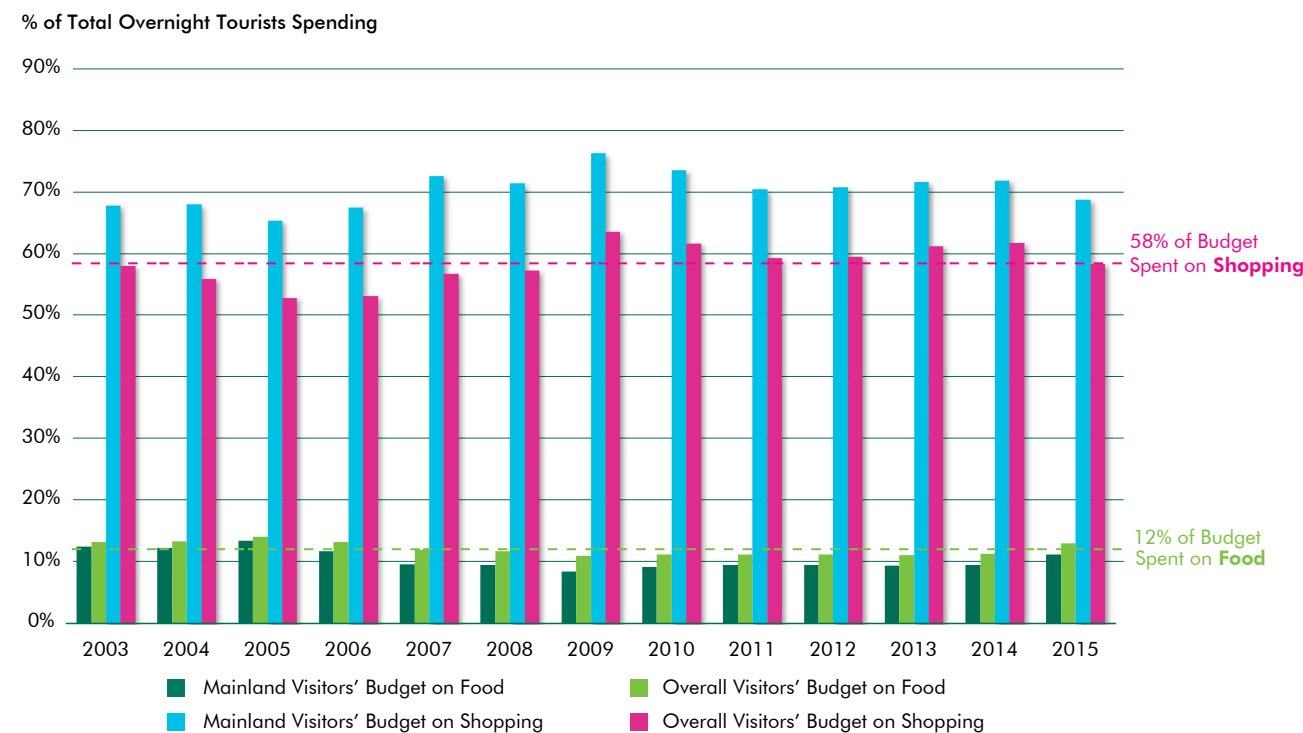
As food is a necessity, F&B sales are generally more resilient during economic downturns. In addition, unlike general retail trades, the F&B sector in Hong Kong is less dependent on tourists, with meals outside hotels consistently accounting for just 12% of total visitor spending. While tourists' spending on consumption goods registered a significant increase during the "Golden Decade" of Hong Kong retail between 2004 and 2014, mainly due to the boom in arrivals from Mainland China, spending on F&B during that period remained at around 10%-15% of their overall budget.

Figure 2: Top 5 most favourite food of tourists



Source: Hong Kong Tourism Board, CBRE Research, Q3 2016

Figure 3: Tourists allocate more \$ on shopping than food

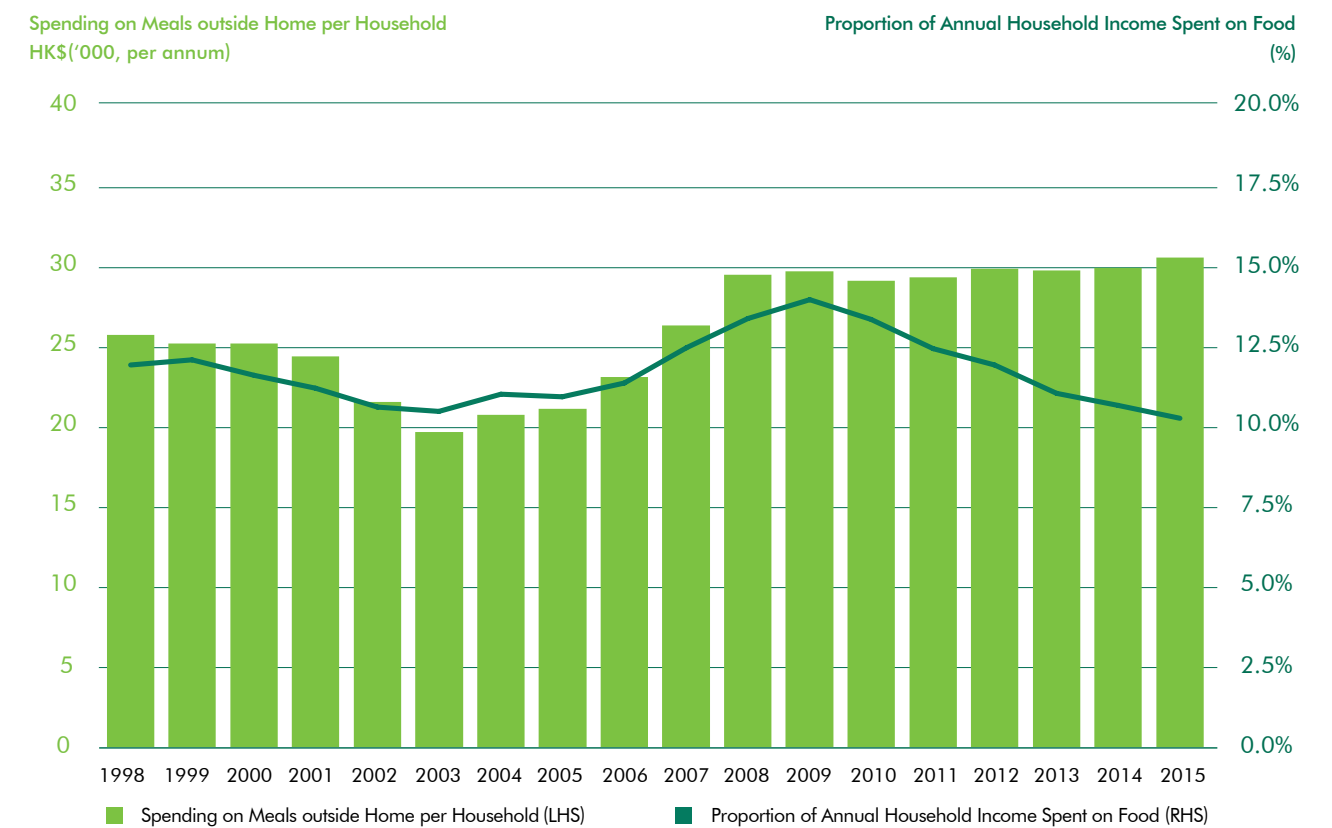


Source: Hong Kong Tourism Board, HKSAR, CBRE Research, Q3 2016

Unlike other retail trades, spending on F&B by local consumers has remained stable over the past decade. Median households allocate around 10%-15% of their incomes on eating out, irrespective of the economic cycle. A 2014 MasterCard survey on Consumer Purchasing Priorities found that people in Hong Kong spent the most among all Asia Pacific cities on eating out.

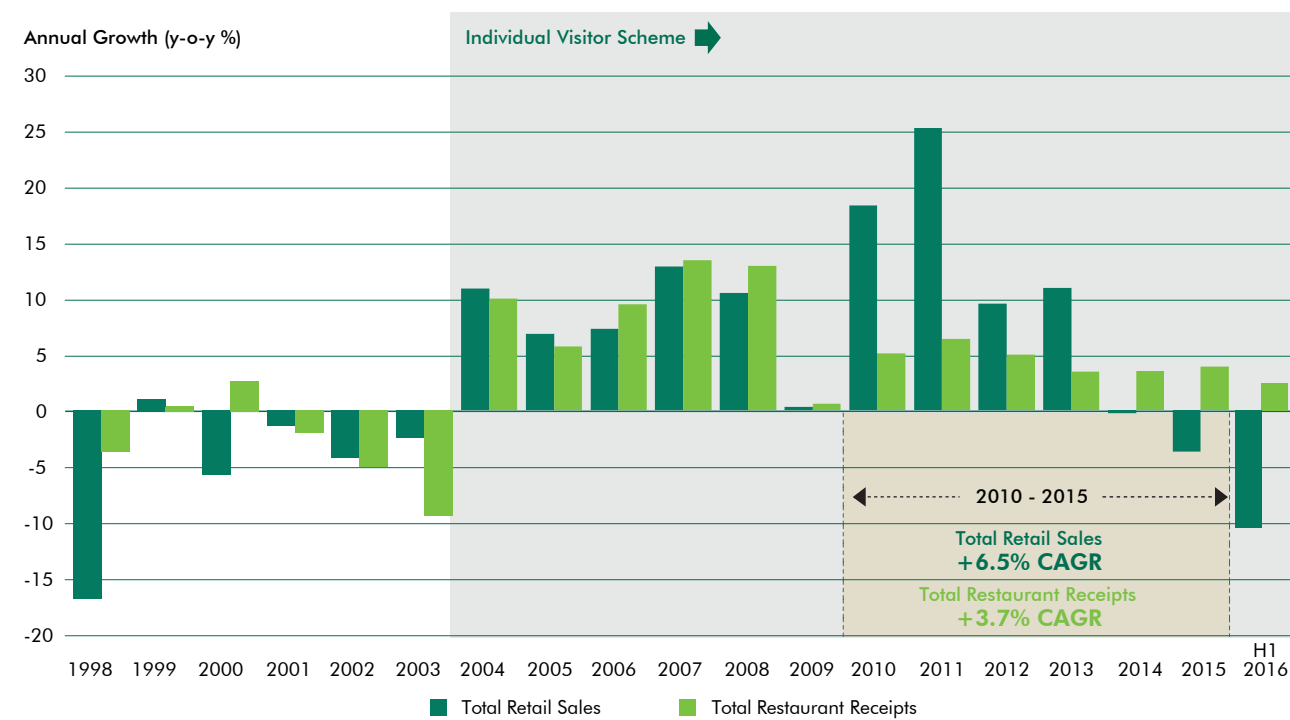
These trends have helped the F&B sector weather the retail slowdown remarkably well. Over the past six years, total restaurant receipts have increased by a Compound Average Growth Rate (CAGR) of 3.7% p.a., behind the 6.5% p.a. CAGR registered for total retail sales. However, while total retail sales fell by 3.7% y-o-y in 2015, restaurant receipts grew by a further 3.9% y-o-y. In H1 2016, total restaurant receipts rose by a further 2.5% y-o-y. While this was below the 4.3% y-o-y growth registered for H1 2015, it was well in excess of the 10.5% fall in total retail sales recorded over the same period.

Figure 4: F&B spending is relatively inelastic



Source: Hong Kong Tourism Board, Census and Statistics Department, HKSAR, CBRE Research estimates, Q3 2016

Figure 5: F&amp;B as a more resilient retail sector



Source: Census & Statistics Department, HKSAR, CBRE Research, Q3 2016

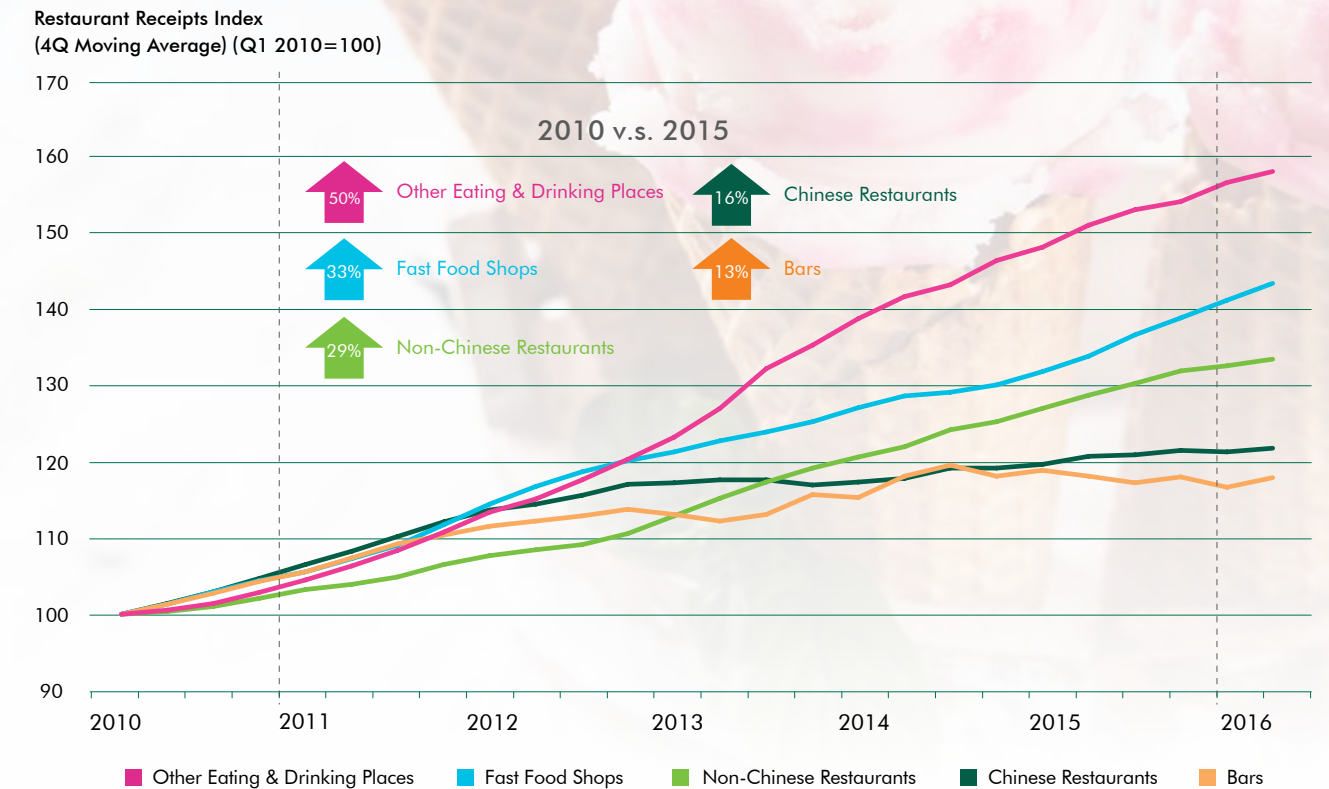
F&B categories with a high turnover rate have recorded the strongest growth. In the six years to 2015, revenues of fast-food shops increased by a CAGR of 4.9% p.a., while other eating and drinking retailers such as coffee lounges and ice-cream shops, rose by a CAGR of 7.0% p.a.. Conventional restaurants, on the other hand, experienced slower growth over the same period. Receipts of Chinese and non-Chinese restaurants increased by a CAGR of 2.5% and 4.4% p.a. between 2010 and 2015 respectively. The same trends have continued in H1 2016, with fast food shops and other eating and drinking retailers (up 6.6% y-o-y and 5.1% y-o-y, respectively) eclipsing the performance of Chinese and Non-Chinese restaurants (up 0.6% y-o-y and 2.4% y-o-y, respectively).

*“We like Hong Kong! Although running our business here is not cheap, the city has offered us great opportunities, supportive networks and a sophisticated quality driven consumer market. All of which have led to an excellent platform for growth.”*

Sanjay Ponnappa – CEO and Founder of Fuel Espresso

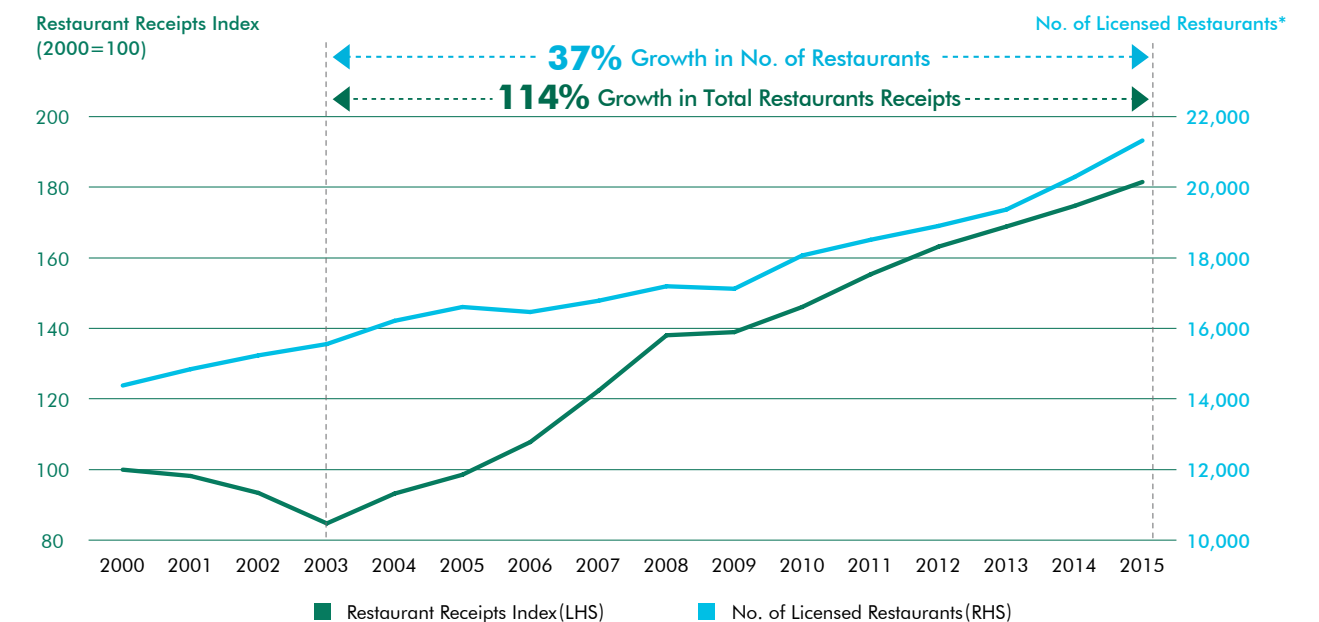
While the value of total restaurant receipts climbed 114% between 2003 and 2015, representing a CAGR of 6% p.a., the corresponding growth in volume has risen by 49% (3% p.a. CAGR). The same period saw the number of licensed eateries increase by 37%, highlighting the growth in consumer spending in restaurants, despite food costs outside home growing by 45% (2.9% p.a. CAGR).

Figure 6: Turnover driven restaurants enjoy stronger growth



Source: Census & Statistics Department, HKSAR, CBRE Research, Q3 2016

Figure 7: Supply-driven growth of restaurant receipts



\*Only restaurants/bars/clubs licensed by Food & Environmental Hygiene Department are counted  
Source: Food & Environmental Hygiene Department, Census & Statistics Department, HKSAR, CBRE Research, Q3 2016



# A RAPIDLY EXPANDING RESTAURANT INDUSTRY

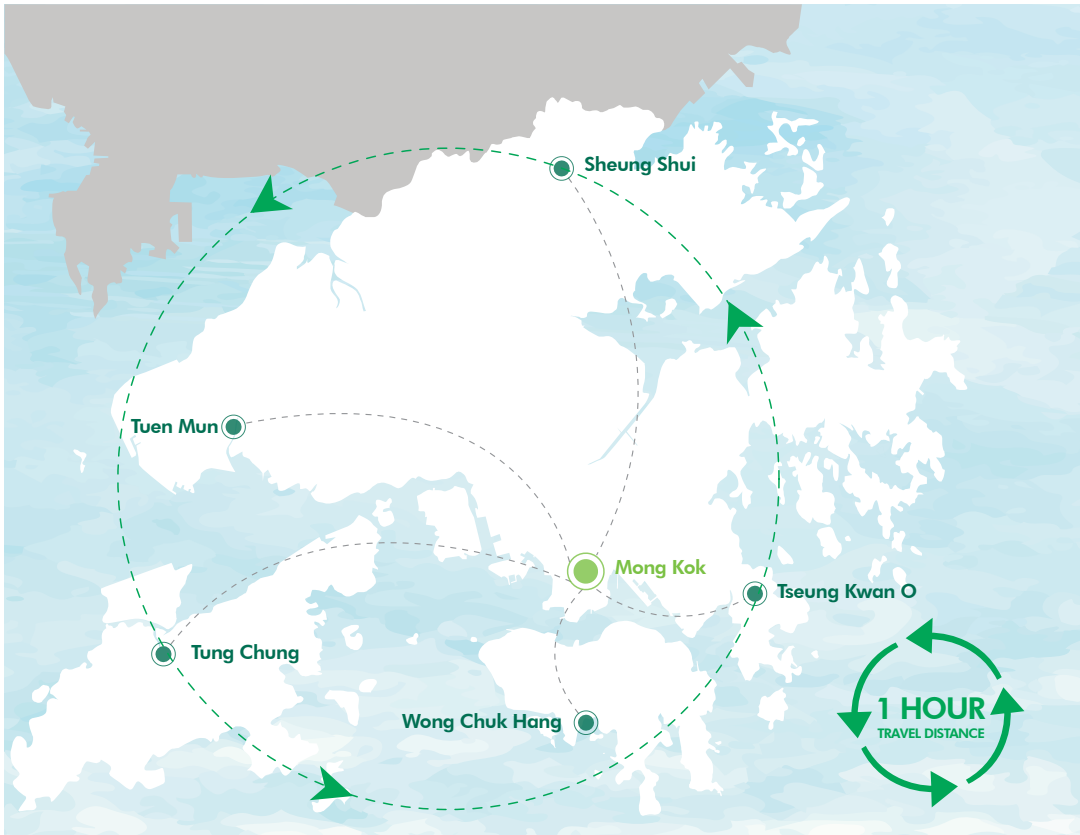
Reasons why dining out is so popular in Hong Kong:

## THE LIVING ENVIRONMENT

Typical office hours in Hong Kong run from 9 a.m. to 6 p.m. but working overtime is common. A UBS report entitled Price & Earnings 2015 published in May 2016 found that Hong Kong had the longest working week globally, at over 50 hours per week (2,606 hours annually). Long working hours discourage households, particularly those without a domestic helper, from spending time and effort on preparing dinner at home. In addition, the relatively short distance between

most office employees’ home, place of work and entertainment spots allows them to access restaurants conveniently. Furthermore, transport networks in Hong Kong operate very late, which means people can stay out late and do not need to rush home. For example, the last MTR trains depart at around 01:00am and there are more than 40 overnight bus routes, thereby making it possible for restaurants to stretch their business hours and maximise revenues.

Figure 8: Short travelling distance allows restaurants to have long business hours



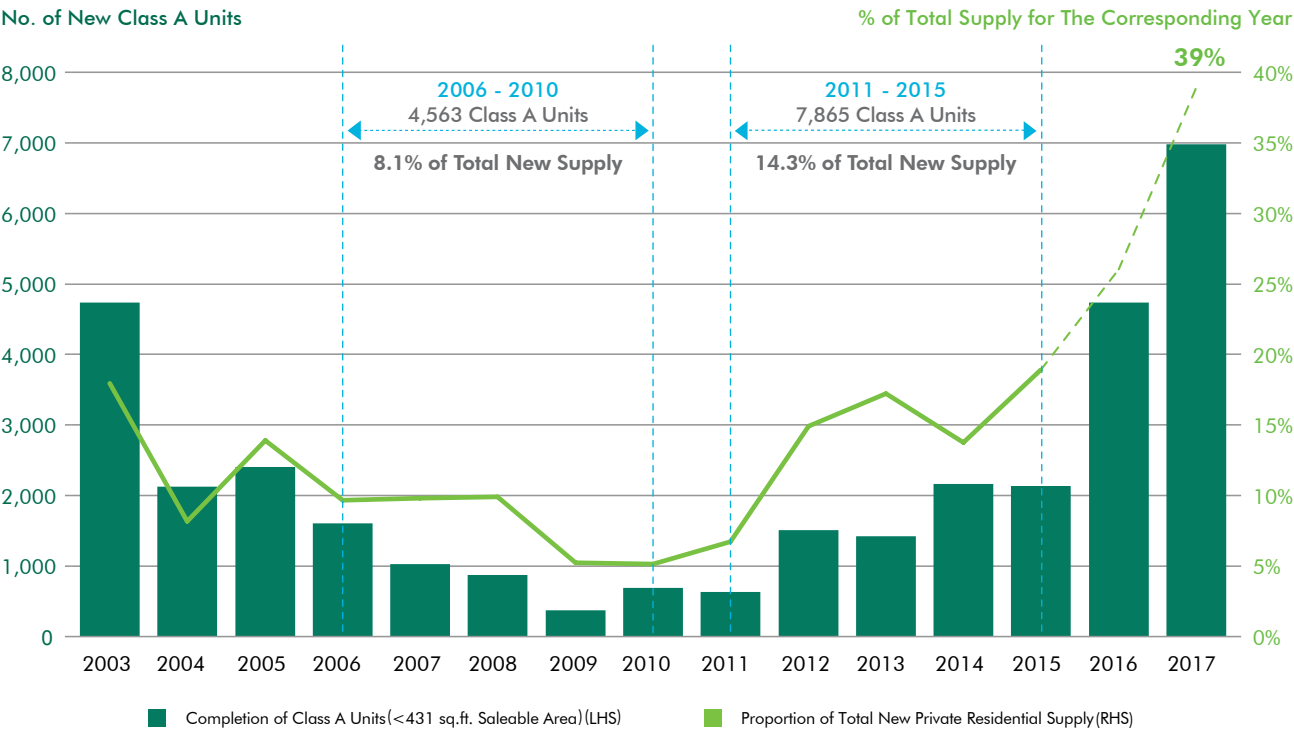
Source: CBRE Research, Q3 2016



Secondly, due to high property prices and the government’s focus on constructing more affordable flats for the mass market, apartment sizes in Hong Kong have shrunk in recent years. In the five years to 2015, a total of 7,865 Class A (saleable area smaller than 431 sq. ft.) flats were built, boosting the share of this smallest dwelling class amongst newly constructed apartments from 8% to 14% compared with the previous five-year period to 2010. These small flats typically feature open kitchens with limited storage space for cooking utensils, and thus do not facilitate cooking at home.

The crowded living environment in Hong Kong makes it more suitable for people to organise social gatherings outside. Large dinners with family members and friends in restaurants are particularly popular. This stands in contrast to overseas markets where it is more practical for people to hold celebrations or other social events at home.

Figure 9: Fast growing number of small apartment units in Hong Kong

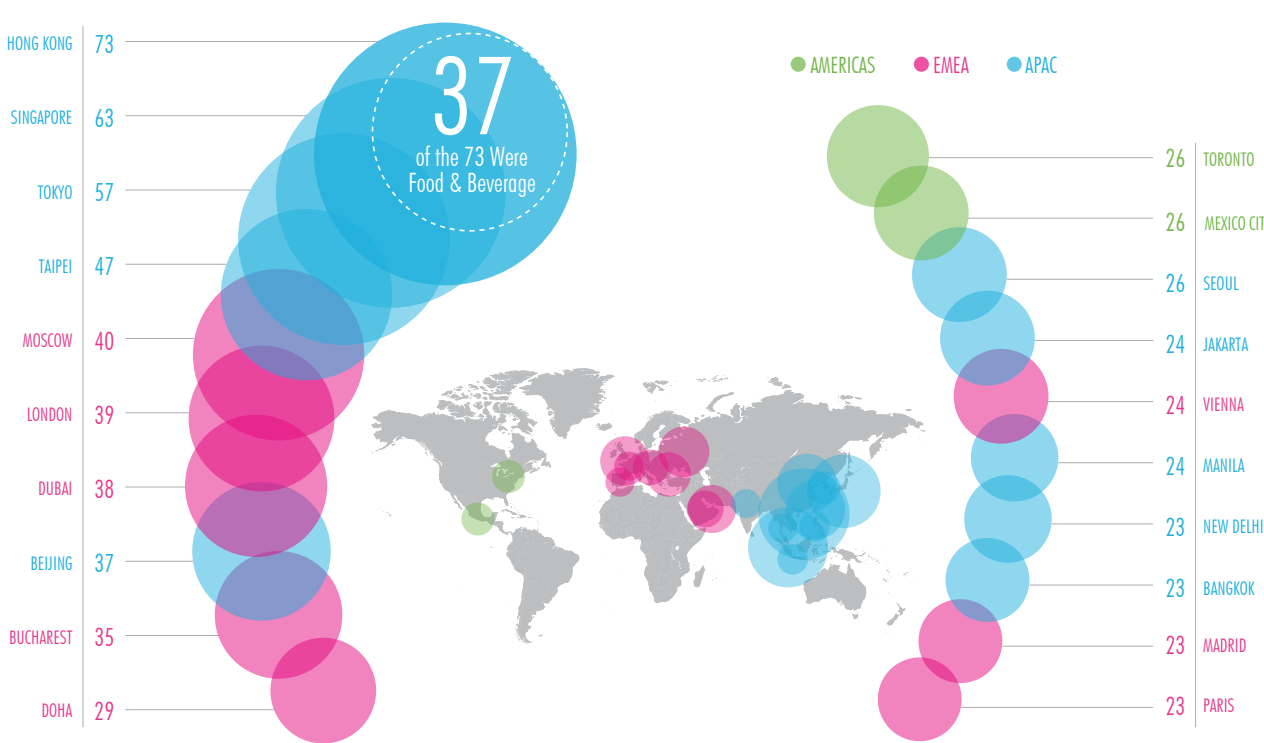


Source: Rating & Valuation Department, HKSAR, CBRE Research, Q3 2016

A CBRE Research major report entitled How Global is the Business of Retail 2015 found that Hong Kong attracted the highest number of new retailer entrants globally in 2015. Among the 73 new entrants, over half (37 retailers) were F&B operators. The findings reflect Hong Kong’s continued status as a leading global retail market and a hotspot for the F&B trade. In recent years, dining out has emerged as a leisure pursuit as people have turned more willing to explore new restaurants and sample different types of cuisine.



Figure 10: Hong Kong being a popular destination for global F&B operators



Source: CBRE Research, Q3 2016

THE MARKET BREADTH AND DEPTH

Established restaurant operators in Hong Kong have been active in launching new restaurants in recent years. Many groups are expanding the range of cuisines they offer and launching new brands to capture different segments of the market. This strategy is motivating people to explore new eateries and promoting food culture and dining out.

Leading Hong Kong chains such as Cafe de Coral, Tai Hing, Fairwood and Maxim’s have all expanded from their original fast-food and Chinese restaurant businesses and branched out into casual dining eateries. Other F&B groups such as JIA, Gaia and Castelo Concepts offer a wide variety of Western and Asian cuisines in Hong Kong at different price points and formats.

Retailers from other sectors are gradually entering the F&B industry. Lifestyle and luxury fashion labels such as Agnès b., Alfred Dunhill, Armani and Vivienne Westwood now all operate bars, coffee shops or restaurants under their brand labels. They see this as a way to market and advertise their brand and diversify their source of income.

In recent years, international celebrity chefs such as Jamie Oliver and Gordon Ramsay have opened restaurants in Hong Kong, capitalising on their high profile brand names.



MEDIA AND TECHNOLOGY

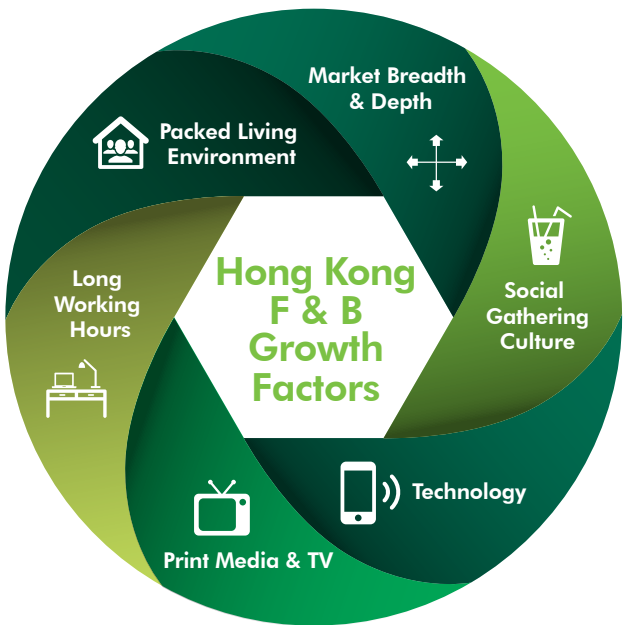
Media has played a key role in promoting gourmet culture in Hong Kong. In addition to the numerous local food and cooking programmes on television, recent years have seen the proliferation of dining guides and gourmet magazines. There are now over 60 local print and online food and drink magazines published in Hong Kong and an additional 140-plus other local periodicals which carry F&B columns or features.

Technology is changing the landscape of the F&B industry. In a city where mobile phone penetration ranks second highest in the world<sup>1</sup>, gourmet focused websites and smartphone apps such as OpenRice and U Food enable users to search and review restaurants and are facilitating the creation of a food and drink culture.

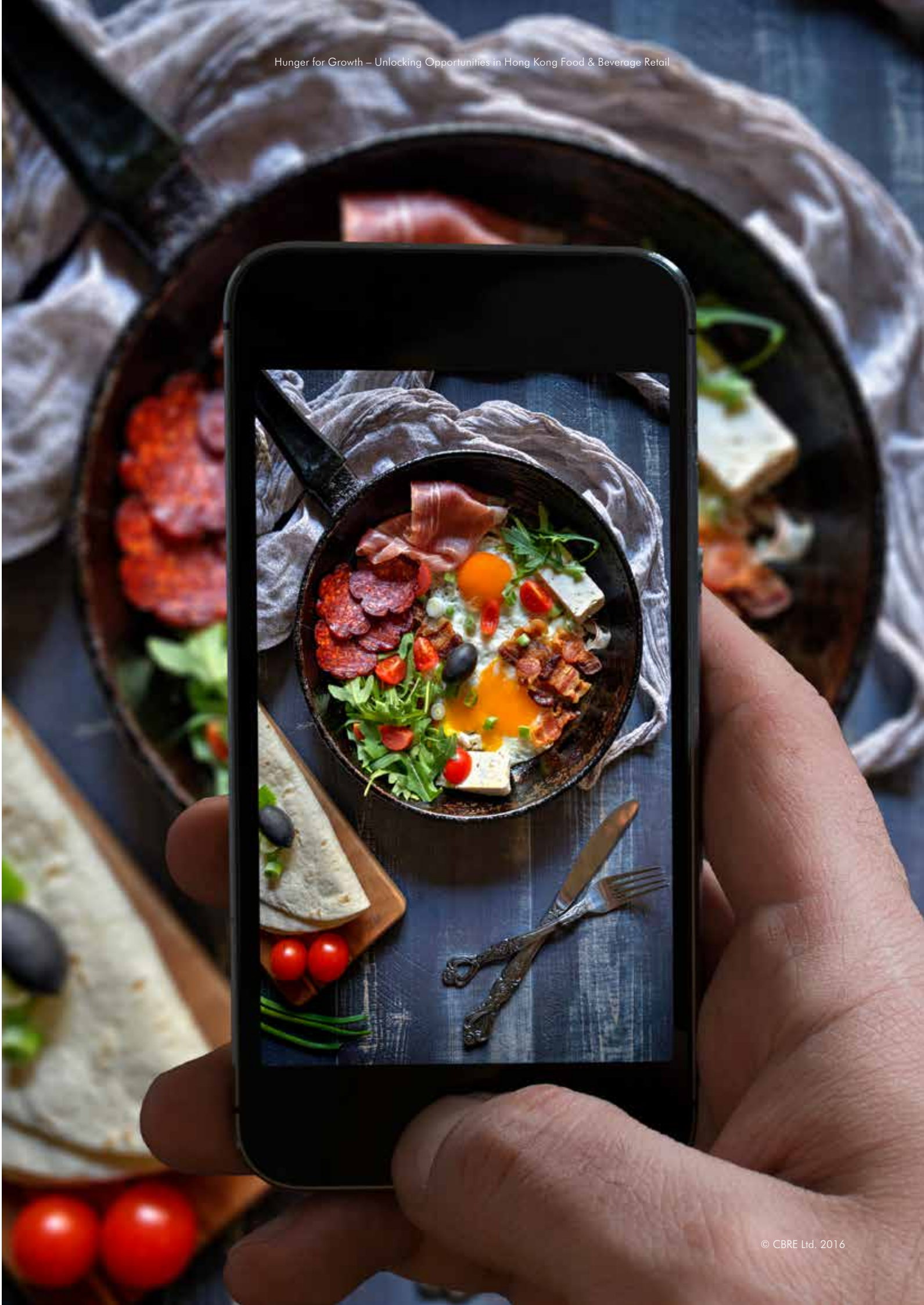
OpenRice was ranked one of top five “must have” apps for living in Hong Kong by the South China Morning Post in 2015. Social media provides a free platform for patrons to review and discuss their experience at restaurants. There are over 100,000 #hkfoodie or related hashtags on Instagram alone and close to 1 million dining reviews on OpenRice.com.

<sup>1</sup>Source: The World Bank

Figure 11: Factors to support F&B sector growth in Hong Kong



Source: CBRE Research, Q3 2016





## HOW HAS THE REAL ESTATE SECTOR RESPONDED?

Commercial property landlords have supported the growth of the F&B sector by allocating them more space in appropriate locations. For example, fast food chains and coffee shops that serve homogenous food and drinks and depend highly on turnover prefer to be located where foot traffic is the highest, typically on high streets or at key bearing points in shopping malls. In contrast, conventional restaurants typically require larger spaces, and are less sensitive to footfall as diners usually plan their visits beforehand. The business nature of conventional restaurants allows them to be situated not only in traditional hot spots, but also in locations that do not attract high footfall, such as on the upper floors of shopping malls or in high-rise commercial buildings.

Hong Kong is home to numerous pencil-type commercial buildings and revitalised industrial buildings equipped with floorplates and features suitable for F&B tenants. High profile examples include California Tower and the L. place in Central, Midtown in Causeway Bay and The One in Tsim Sha Tsui. These vertical retail or so-called Ginza-style buildings help cluster restaurants together and provide flexible layouts with unique features such as private lift lobbies, ample daylight and open city views. Depending on their location

and specifications, many offer space at more attractive rents compared to street shops in prime commercial districts. Drawbacks of these options include crowded elevators at peak times, poor visibility and a lack of shop frontage and inadequate car parking spaces. Nevertheless, this type of retail format is now firmly established in Hong Kong. Among the four core retail submarkets, circa 30% of the licensed F&B are located upstairs. CBRE Research's How Global is the Business of Retail 2015 report also found that of the 37 international F&B operators which made their debut in Hong Kong in 2015, eight opted to open their first restaurant in a vertical-retail building.

***"We enjoy being on upstairs! The panoramic view, the terrace, the privacy, you can never imagine how much our customers like the atmosphere up here. This is something shopping malls and street shops can never offer."***

Barbara Kukhno – Hong Kong Representative of Bulldozer Group

Figure 12: Upstairs retail as a mature operating format for F&B in Hong Kong

### Retail Format of Licensed F&B in Central, Causeway Bay, Tsim Sha Tsui and Mong Kok



Source: Food & Environmental Hygiene Department, HKSAR, CBRE Research, Q3 2016

Another noteworthy trend has seen landlords incorporate fine-dining restaurants into premium office buildings to raise the profile of their properties while providing office tenants with best-in-class restaurants under the same roof. These floors usually command premium rents over conventional retail space because of their unobstructed views, open spaces, balconies and sky gardens. Some are served by exclusive passenger lifts. Of the 230 Grade A office buildings in Hong Kong, nine have F&B floors. Iconic office buildings with signature restaurants as tenants include ICC in West Kowloon, One Peking in Tsim Sha Tsui and Prince's Building in Central.

Recent years have seen the emergence of mid- to high-end eating and drinking hubs in second-tier high streets and in some neighbourhood areas. Examples include Star Street in Wan Chai, High Street in Sai Ying Pun, Davis Street in Kennedy Town and Tang Lung Street in Causeway Bay. The transformation of a neighbourhood area into an F&B cluster is usually driven by demographic changes, often stimulated by new residential and commercial developments which attract a higher-income population. These emerging clusters are providing consumers and restaurant operators with more options outside traditional retail districts.





Figure 13: Latest emerging F&B clusters

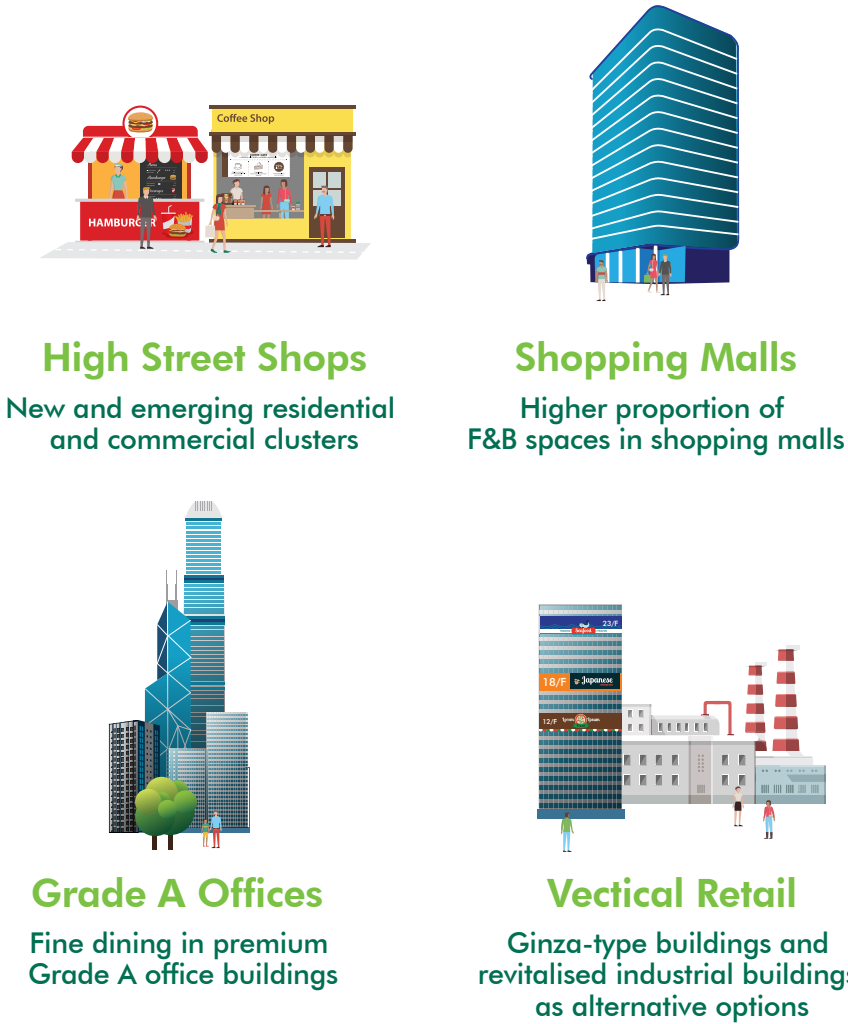


Source: CBRE Research, Q3 2016

In a market where general consumption demand is softening, and partly to align with a global trend, shopping mall landlords in Hong Kong are allocating more space to F&B tenants. They see this as a means by which to maintain footfall and enhance turnover, and also as an opportunity to improve the positioning of their malls. For example, Swire

Properties previously allocated 16% of the space in Pacific Place to F&B tenants, but reportedly plans to increase it to around 20%. Elsewhere, Harbour City expects to complete its Ocean Terminal extension in 2017 which will include a fine-dining zone with commanding views of Victoria Harbour.

Figure 14: Changing real estate landscape to facilitate growth of the Hong Kong F&B sector



Source: CBRE Research, Q3 2016



# OUTLOOK AND OPPORTUNITIES

The outlook for the Hong Kong F&B sector remains upbeat for the following reasons:

- Demand for food is relatively stable compared with other discretionary consumption items
- There is a growing gourmet culture in Hong Kong which is pushing dining beyond a mere necessity
- The crowded living environment will continue to encourage eating out
- Demographic changes resulting from the development of new commercial areas is boosting demand for dining hubs around these locations
- Rents are falling while the range of spaces for F&B operators is increasing
- The government has pledged to maintain and promote Hong Kong’s status as a gourmet hotspot

Substantial commercial development in several districts over the next few years will provide opportunities for F&B sector expansion. CBRE Research forecasts that close to 4.7 million sq. ft. of Grade A office space will be built in Kowloon East in the five years to 2020, bringing an additional 44,000 white collar workers to the district. Another 10.6 million sq. ft. of Grade A office space is expected to become available in the district upon the development of greenfield sites currently with the government. This will translate into a further 98,000 workers who will spend their days and nights in this commercial hub comprising Kai Tak, Kowloon Bay

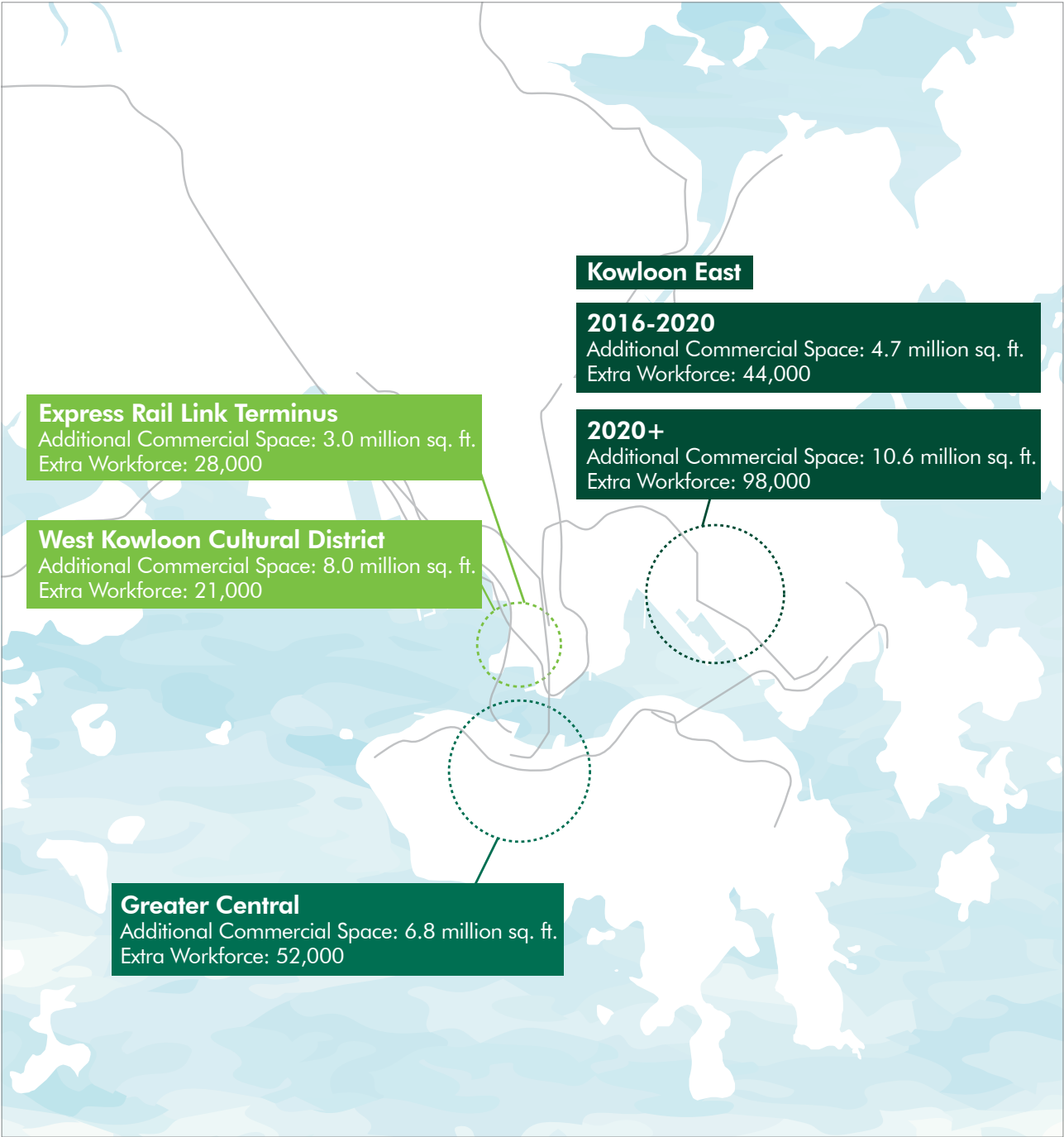
and Kwun Tong. Kai Tak, already home to a new cruise terminal, will see an increase of close to 90,000 residents, along with the construction of a sports stadium and more than 3,000 hotel rooms. These new developments will drive strong demand for both casual and business-grade F&B facilities.

While new commercial development in core business districts remains limited, several sites in New Central Harbourfront have been earmarked for commercial development in the medium-term. Once completed, these sites will have an estimated floor area of over 2.8 million sq. ft., sufficient to expand the working population in and around the CBD by more than 15,000 people.

The emergence of West Kowloon into an art, cultural, commercial and transportation hub will provide significant opportunities for F&B operators. The West Kowloon Cultural District (WKCD), which is scheduled to open in phases from 2016, will form one of the world’s largest cultural clusters and is set to become a major tourist destination. The Express Rail Link Terminus next to the WKCD will serve high-speed trains connecting Hong Kong with Shenzhen and Guangzhou and have circa 3 million sq. ft. of commercial floor space.

New residential developments continue to be constructed in emerging locations. The new towns of Shatin, Tseung Kwan O and Tuen Mun will see the strongest population growth by number in the five years to 2021, driving strong demand for neighbourhood F&B dining.

Figure15: Underlying demand for restaurants in upcoming commercial clusters



\*Commercial space includes office, retail & hotel, in GFA  
Source: CBRE Research estimates, Q3 2016



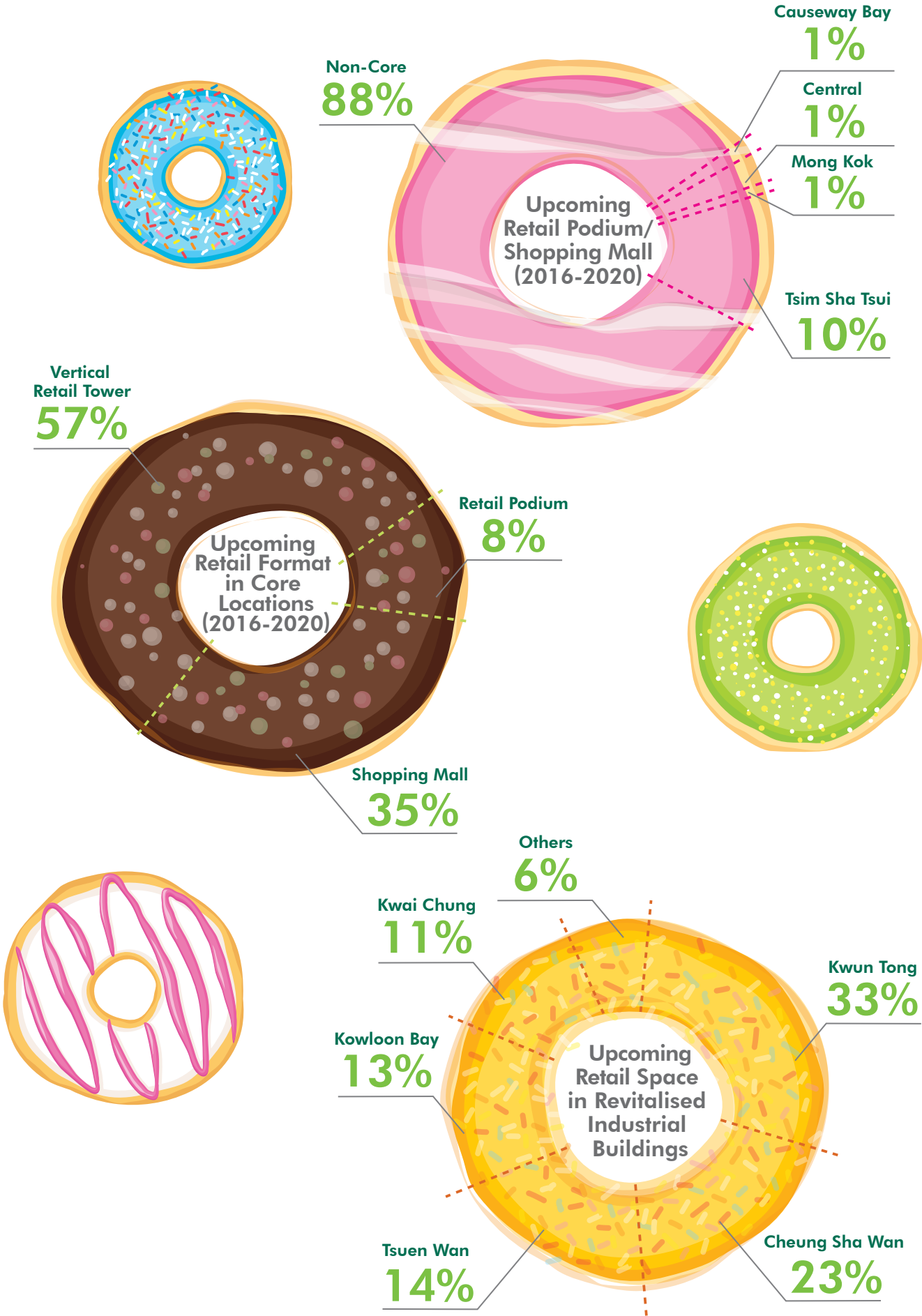


While almost 88% of the shopping arcades and malls scheduled to be completed between 2016 and 2020 are located in non-core areas, over half of the new retail supply (1.6 million sq. ft.) in the four core districts of Central, Causeway Bay, Tsim Sha Tsui and Mong Kok over the same period will be in the format of vertical retail towers. In addition, a total of 23 industrial revitalisation projects have been approved for conversion to

retail facilities, providing 1.9 million sq. ft. GFA of space. The majority of these conversion schemes are in emerging commercial districts such as Kwun Tong (33%), Cheung Sha Wan (23%), and Tsuen Wan (14%). Such schemes will continue to provide F&B operators with alternative space options to traditional commercial areas where space in conventional retail formats will remain limited.



Figure 16: Distribution of future retail supply (by GFA)





# RECOMMENDATIONS FOR F&B OPERATORS

CBRE Research advises F&B operators to consider the following strategies to capitalise on current market conditions and help differentiate their restaurants from the competition:

- 1 The current market downcycle is providing F&B operators with an opportunity to negotiate better lease terms and is hence the ideal time for them to expand their footprint. Taking up space in emerging districts can be a cost effective strategy.
- 2 For larger operators, basic food preparation such as food cutting and washing can be done outside restaurants. Establishing a centralised kitchen in industrial premises can reduce food processing and storage space in restaurants which are typically in more expensive locations, while ensuring better control over food quality.
- 3 Installing open kitchens can enable chefs to interact with their customers directly. Consumers like to observe the cooking process and share the experience on social media.
- 4 Restaurants can differentiate themselves by offering customers an interactive dining experience such as by enabling them to select raw food, participate in the cooking process and provide customised or seasonal menus.

*“The retail sector in Hong Kong is going through a tough time. I have been told by many that it will be last man standing, and those that come through this will be in a fantastic position to capitalize on future opportunities. For F&B businesses in Hong Kong this means ensuring one continues to maintain enduring relationships, and none is more important than with your landlord.”*

William Lyon – CEO of Big Cat Group & Jamie's Italian





# RECOMMENDATIONS FOR RETAIL LANDLORDS

The transformation of the Hong Kong retail market has prompted retail shop landlords to become more flexible towards rental levels and tenant selection. This change is structural and is likely to continue for the foreseeable future. CBRE Research advises landlords to continue to be open-minded and consider signing F&B operators as tenants. F&B tenants can provide retail landlords with better lease security as they prefer longer leases to amortise the higher fit-out and equipment costs. In addition, bars and restaurants guarantee footfall and benefit other retailers, particularly in the case of shopping malls.

CBRE Research advises retail landlords to consider the following strategies to capitalise on the growth of F&B retail and increase the appeal of their properties to such tenants:

- 1 Landlords should keep informed of the latest gourmet trends. Categories such as burgers, ice-cream, yogurt and waffles have seen tremendous growth in the number of operators in recent years. However, inexperienced operators often fail to survive in what is a very competitive environment. Landlords are therefore advised to carry out sufficient due diligence on potential tenants' track record to minimise risks.
- 2 In densely populated locations where the rental income from leasing smaller commercial buildings to office tenants may not be substantial, landlords can consider converting their premises to Ginza-retail buildings to maximise rental returns. F&B floors in less prominent commercial buildings in Wan Chai, Causeway Bay, Tsim Sha Tsui and Mong Kok can typically achieve a 20+% rental premium over office floors.
- 3 For properties which can be converted to Ginza-retail buildings, landlords are advised to equip them with the necessary technical features relating to floor loading, ceiling height, utilities provision, water and exhausted gas supply and disposal, and evacuation compliance to suit the requirements of F&B tenants. Particular attention should be paid to elevators so as to ensure sufficient and timely access for patrons and other tenants in the property. Buildings with balconies and rooftops will be particularly sought after by F&B operators. Landlords of Ginza-retail buildings can also consider providing facades or signage to help promote tenants' visibility.



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