STABILITY RETURNS TO PUB TRADE

With nearly 7,200 licensed pubs operating throughout the country, the Irish licenced trade is a crucial component of Ireland’s important hospitality sector which employs 230,000, spends more than €2.9bn annually in wages and delivered €6.5bn in tourism revenues in 2017.*

While Irish pubs are renowned the world over for their unique blend of hospitality and sense of tradition, in recent years the domestic Irish pub sector has been changing to meet the demands of a more sophisticated marketplace as well as changing consumer behaviours and preferences.

Having emerged from a difficult period during Ireland’s recent economic downturn, the pub sector—particularly in the key urban areas of Dublin, Cork, Galway and Limerick—has once again achieved a degree of stability and demand for pubs in these key areas is significant.

“I think we are nearly back to a period of stability in the marketplace and there has been a lot more activity over the past two years as new operators entered the market, finance is once again available and there are less insolvency-related sales taking place,” says Tony Morrissey, Managing Director of Morrissey’s, the Dublin-based auctioneering and consultancy firm that specialises in the pub and hotel sectors.

“Over the last five years, as much as 60% of all transactions in the Dublin market, for example, were insolvency-related and while there are still a few cases in the pipeline, the market is now approaching a pre-recession level of normality with around 4-5% of stock changing hands every year. That’s around 35 pubs a year which is what it used to be before the downturn,” he adds.

As the capital city with the largest population in the country, the Dublin market has been the quickest to recover from the downturn, says Tony. He points out that there is pent-up demand in the market for premises in well-developed urban, suburban and mid-town areas that have a solid footfall throughout the day, offer food and maybe benefit from being near offices, good public transportation and population centres.

“Outside of Dublin, Galway is performing very well,” he says, particularly Galway city and again there are two or three pockets in the city that are stronger than Dublin in terms of prices. Cork and Limerick are pretty much the same. Along the west coast, places like Westport and Killarney are also doing well.

“If a pub is not turning over €8,000–€9,000 a week in rural areas, then it’s going to be very difficult for them to survive. The same is true of Dublin and if a pub is not turning over between €12,000–€13,000 a week, it’s in trouble,” he says. Valuations within the trade have also become a lot more sophisticated and the capitalising ratios arrived at after considering the multi profit nature of premises, including wet sales, food and off-license sales and

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TYPICAL MARGINS FOR THE PUB SECTOR IN IRELAND

* Source: Irish Tourism Industry Confederation

Source: Morrissey’s

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any entertainment or function revenue, can vary from 0.5 times net turnover up to 2.5 times or even higher for established “trophy pubs” in prime urban locations.

“These ratios are influenced by many factors like location, the make-up of the trade, volume of business, margins and profitability, competition and of course demand. Capitalising ratios below these, however, reflect licensed premises that have poor economies of scale relative to the volume of trade enjoyed and in turn the profitability - if there is a profit,” says Tony. Because of the decline in insolvency-related sales, the market has seen a corresponding increase in traditional private transactions – often in the form of off-market sales - with relatively new entrants to the marketplace seeking additional opportunities as some publicans contemplated their retirement options while many of the existing pub groups remained absent from the market, preferring instead to consolidate their existing stock and drive their business forward, says Tony.

“I think we will see more off-market transactions in 2018 as demand for pubs in key locations outstrips the supply. With the increased availability of finance for the right stock in the right location and the decline in insolvency-related sales, investors and operators are not waiting around for an ad in a newspaper before they make an offer,” says Tony.

“They know what kind of stock they want, and they will try and buy it if they can. But back in the 1980s and 1990s, over 50% of transactions were off-market and I think we are heading back in that direction again.”

In many cases, the newer operators that have entered the market over the last five years are opting for leasehold premises over freehold.

“Many of the newer operators who have grown their businesses over the past few years have done so by acquiring leasehold interests and they are more or less indifferent about whether it’s leasehold or freehold. The main thing is that they know it meets their requirements, it has potential and they know they can develop a good business with a minimum amount of capital expenditure.”

At an operational level, Tony says that the overall market has changed considerably over the last 10 years and many publicans have responded and adapted to the changes in consumer habits and behaviours.

Some of the more notable changes, he says, include a growing demand for craft-beers and premium spirits like whiskey and gin, more sophisticated wine and cocktail offerings and the opening of design-led concept units that target key demographical cohorts.

know the market they are targeting and they do it very well,” he says. “Food is an increasingly important component of the overall offering, particularly in pubs in city or town centres and suburban locations. In many cases the food offering has developed to such an extent that it positions operators against traditional restaurants and cafés which of course allows them to protect their turnover and margins,” says Tony.

“The downturn forced many publicans to become a lot more focused on their margins and become a lot more business-like than perhaps they were in the past,” he says. Typically, pubs in the Dublin area that have a viable and sustainable business should be working to net margins or EBITDA (earnings before interest, tax, depreciation and amortisation) of between 15-25% while for provincial pubs the margin should be between 10-15%, according to Tony.

When it comes to drink-only sales, pubs in the Dublin area should be operating off a gross profit margin of 57-72% on drink sales, he says. For food sales, the gross profit margin is typically between 60-70% while for off-licence sales it varies between 18% and 25%.

The typical gross profit margins for provincial pubs in good locations, meanwhile, are not far behind their Dublin counterparts, says Tony. “For drink sales, the margin should be between 50-55% while for food sales it’s anywhere between 55-65% with off-license sales typically operating off 15-20%,” he says.

For many publicans, rising wage costs are an issue and can have a significant impact on the bottom line, says Tony. He says that for Dublin pubs, wage costs as a percentage of turnover can vary between 19-24% for drink-only pubs while for those with a food offering it can rise to between 25-32%. While wages might be lower in provincial pubs, for drink-only pubs they can account for anywhere from 16-20% while for those selling food, they can rise to between 25-30% of turnover.

“Overall, the outlook for 2018 will be similar to the last six months of 2017 with confidence returning to the pub sector and, as a result, we believe that there will be more off-market sales and a reversion to auction as the preferred mode of disposal for quality licensed houses. But the demand will still be for well-located properties that enjoy solid population base, offer a good blend of product offering and are well-managed and have quality staff,” Tony concludes.
SUPPORTING IRISH PUBLICANS

On the back of strong economic growth, buoyant consumer sentiment, falling unemployment and a record year for tourism numbers, the Irish pub sector is performing strongly and there is a sense of optimism within the sector not seen for many years.

“A macro level, 85% of the turnover in Irish pubs is derived from the domestic markets; 5% comes from UK visitors, 5% from visitors from the USA and 5% from the rest of the world. All these markets grew in 2017 with total growth of 6%. When we look closer at these divisions we see growth in pub sales from domestic markets of 6%, 6% from UK and 9% from US with the rest of the world up by around 5.5%,” says David McCarthy, AIB’s Head of Hospitality & Tourism.

He points out that most of the legacy debt issues which were overhanging the sector for the past 10 years have been addressed and this has led to greater stability and clarity in the market.

“According to the CSO, new lending to the pub sector has increased by 65% to €86m in the 12 months to the end of October 2017,” he says.

“The majority of pubs that had debt levels that were too high have now been restructured or refinanced. In addition, the pub sales market has stabilised and retreated to more normalised levels of asset and trade sales. The CSO shows us that debt levels in the pub sector have decreased by around €1.4bn, or 61%, since September 2011,” says David.

“In some parts of the country there is a much higher reliance on tourism trade rather than domestic trade. Where these locations exist, there is a positive outlook for the coming years as Irish tourism is projected to continue to perform well.”

“When we review card usage data in pubs from AIB Merchant Services, we can see a 6% increase in spending by UK visitors in pubs in the 12 months to the end of October 2017. The UK accounts for 5% of all pub revenues in the Republic of Ireland. Whilst some pubs in major cities such as Dublin, Cork, Galway and Limerick derive more than 5% of their turnover from UK customers, we can see that the overall risk of Brexit on the pub sector is not excessive and the market actually grew over the past 12 months despite a decline in UK visitor numbers.

“There is also an opportunity for publicans to diversify their target markets as all other visitor markets are seeing continued growth into Ireland. Pub revenues from US visitors, for example, have increased by 9.1% over the past 12 months and by 5.6% from all other markets. In addition, there was a 5.8% increase in revenues derived from the domestic market,” David adds.

“Some pubs do have a higher level of exposure to UK visitors and they need to be mindful of the implications of further Sterling devaluations and any potential future travel restrictions post-Brexit.”

“Card usage is seeing continued growth in all three sectors. Total card spending has increased in pubs by 6%, however the number of transactions has increased by 17%. There is a trend of people using their card multiple times in a pub and this has been facilitated by convenience options such as contactless payments,” says David.

“IRISH PUBLICANS is performing strongly and there is a sense of optimism within the sector not seen for many years.

Source: Bord Bia

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“The Irish food service market for hotels, pubs and restaurants is worth €2.64bn, according to Bord Bia, and overall food service in the hospitality sector has increased by 5.6% over the past 12 months.”

With a decline in the day-time sales of alcohol, many publicans have broadened their product offering over the last number of years to include food, according to David. “While food sales can return good margins, it is a more complicated revenue stream to manage,” he says.

“The Irish food service market for hotels, pubs and restaurants is worth €2.64bn, according to Bord Bia, and overall food service in the hospitality sector has increased by 5.6% over the past 12 months. The biggest share of this growth was from hotels which saw their share of the food service market increase by over 8%. Pubs, however, have also grown their food sales by 3% and in 2017 food sold in pubs accounted for 37% of the total food service market in Ireland,” says David.

With the availability of finance to the pub sector no longer an issue in the marketplace, David points out that publican’s looking to borrow need to be mindful of the importance of developing a sustainable business that is underpinned by strong cashflows. “As the leading provider of finance to Ireland’s pub sector, AIB is a cashflow-focused lender. For all finance requests from the pub sector our credit assessment starts with the experience and track record of the proposed borrower and an assessment of the cash generating abilities of the business. All applications are stress-tested to account for potential future shocks like another domestic economic recession or the potential future risks of Brexit on the operation,” he says.

“Wet sales businesses are straight-forward in terms of credit assessment, however most large pubs these days have other income streams like food offerings and off-sales. It is important for pubs to stay on top of the key movements in trends not only relating to food and beverages but also consumer behaviours and preferences. Visitors to pubs don’t just come for the drink any more, but for the experience, whether its live music, watching sporting events or for an overall unique atmosphere. Successful pubs differentiate themselves and know which markets they are specifically targeting,” David says.

“From speaking to its publican clients, AIB understands there are still many challenges facing the industry. Similar to the hotel and restaurant sectors, and especially where there is a food offering in the business, attraction and retention of experienced staff continues to require ongoing management and innovation. Publicans also need to continually invest in their offering to ensure it moves with the trends in the industry and attracts the available markets. Other risks we hear our customers talk about are rising insurance costs as well as the risk that the 9% VAT rate will not continue in the medium term,” he adds.

“Overall AIB has a positive view of the pub sector and remains committed to supporting it. We have a team of dedicated Business Advisors across the country who have a strong desire to develop relationships with existing and prospective publicans. Through a combination of their local knowledge, coupled with a central sectoral expertise, AIB has positioned itself to be truly able to understand the performance and management capabilities of pubs in all areas of the country and to be able to match this with suitable bank products or services to assist with business growth or with risk mitigation within the business,” concludes David.
Havign been involved in the running of eight different pubs in Cork over the last 20 years, Liam Barry is passionate about the pub trade but warns that publicans need to focus relentlessly on their operating margins if they want to develop a viable business.

Best known for running the busy An Bodhrán on Oliver Plunkett Street in Cork city centre, more recently his interests have expanded to include the popular Goldberg’s Bar on Victoria Road and The Island Tavern on Military Road on the northside of the city.

Like other urban areas in Ireland, the pub trade in Cork city and county, however, has undergone considerable change.

“The industry has changed considerably over the last 20 years. Publicans made a decent living back then but it’s a different now,” says Liam.

“So much has changed: things like the cost of compliance for fire and safety, the cost of music licenses, much higher insurance costs and wages, amongst other things, mean that publicans have to be a lot more careful and focus on their margins if they want to develop a viable business.”

Having witnessed several pubs in Cork go out of business over the last 10 years, he says that some of them could have staved off their demise if they were more focused on the bottom line.

“There are publicans out there who will blame everyone but themselves and it doesn’t matter whether you are running a pub or a shoe-shop, it’s a business and it has to be run as a business first and foremost. And to run a business, you need to know what you’re doing. In the past, plenty of people bought pubs but many had no real business experience and a year or two later, when they couldn’t pay the Revenue Commissioners or their suppliers, they pulled the shutters down,” he says.

With all three of his pubs operated on a leasehold basis, he says that he has been lucky to have good landlords, but he is not too adverse to acquiring a freehold premises should a suitable one come on the market.

“The lease versus freehold argument is the same as the mortgage versus renting argument when it comes to a house. It all depends on what a business owner wants out of it whether or not they have a good landlord and the length of the lease that’s on offer. But they need to be careful that it’s not a big burden and that it leaves them with enough to run the business on a day-to-day basis. I’ve seen people paying way over the odds for a lease, which is fine if they are turning over €16,000 a week. But they weren’t and soon they realised that it wasn’t sustainable and they went out of business,” he says.

As a customer of AIB, Liam says the bank has played a key role in supporting the growth of his business.

“We’ve always had a great relationship with AIB and our local manager, Paul O’Callaghan, who has a great understanding of our business and what we are trying to achieve. He’s always there for us to talk about any issues. I also think that if a lot more businesses kept in touch with their bank and talked to them about their business and flag any issues that might be coming down the line, and be open with them, businesses would stand a much better chance of success. Unfortunately, too often some people bury their heads in the sand until it’s too late,” he concludes.

“Generating customers a reason to cross the threshold of one of its pubs is an important part of the business strategy that has underpinned the success of the Murray Pub Group, according to Ross Murray its managing director.

“You need to provide an experience for people to come out and enjoy themselves. If people want to watch a match on TV and have a beer, why would they want to come to us and spend €5 for a bottle of beer when they can stay at home and watch it with a bottle of beer that costs €1 in a supermarket? Pubs need to provide something that people can’t get elsewhere,” says Ross.

The Dublin-based group includes a number of high-profile pub brands like the popular Murrays Bar & Grill on O’Connell St., The Living Room, Fibbers Rock Bar and The Gate Hotel, all of which adjoin each other in a busy part of the city centre. Further south, in Dublin’s so-called Camden Quarter, the group also owns Jimmy Rabbitte’s Speakeasy and is in the process of developing the adjacent landmark Camden de Luxe complex into a bar and night-club venue following its high-profile acquisition in 2017.

According to Ross, the success of the business has revolved around knowing and understanding each pub’s target market. The flagship Murray’s Bar and Grill on O’Connell, for example, is a popular destination for tourists while The Living Room has built a reputation amongst sports fans as the top sports bar in the city centre. Fibber Magee’s, meanwhile, is a popular venue for fans of live rock music.

“Every property has its own unique selling point,” says Ross. “In the old days pubs just sold beer and spirits and barmen chopped a few lemons. People are not as brand loyal as they were. In the past there wasn’t the same choice, now they have so much choice and it’s totally different. Customers, particularly younger customers, expect and want a lot more and we have to cater for them. If we don’t, then somebody else will,” he says.

While Ross believes that the existing licensing laws should be changed to allow publicans more flexibility around opening hours, he is critical of the cost of insurance and the impact it can have on operating margins.

“But insurance is a big problem, particularly when it comes to bogus claims. Even though a case may never go anywhere, it still costs us anything up to €3,000 just to deal with it. That’s a big cost and can eat away at the margin,” he adds.

As a customer of AIB, Ross has developed a strong working relationship with the bank. “We have a great relationship with AIB and the bank has been a great support to us when it came to expanding and growing our business,” he concludes.