Is It Crazy to Open A Restaurant in Hong Kong Today?

Hong Kong has always been a very challenging market for the restaurant industry. The territory has one of the highest restaurant densities in the world with over 16,000 locations or 20.4 restaurants per 10,000 population. Landlords are notorious for their selfish behavior and lack of interest in the success of their tenants. These "sharks," as they are known in the industry, have always assumed that the allure of tourism and the China market would keep rents steadily increasing and a steady flow of new tenants. While this may have been true historically for the fashion industry, it never really translated well for food & beverage. Most Mainland tourists were happy to eat a quick bowl of noodles in between their luxury shopping rounds in the city.

During the past 18 months, the situation has become dire for most retailers and the commercial property sector overall. A combination of street protests over the proposed Extradition Treaty and more recently COVID-19, have sent retail sales plummeting. In the most recent months, total retail sales have declined between 25-40%. The hospitality industry has been particularly hit hard with periodic restaurant closures, limited operating hours and a ban on immigration/tourism.

What is the future of restaurants in Hong Kong? Does it make any sense to invest in this sector in the future?

First, operating restaurants in Hong Kong has always been tough and will likely get tougher. There are just too many obstacles to cross to get to sustained profitability for most concepts, but there are always exceptions.

While landlords may become a bit more flexible in the short term, they always revert back to old habits as soon as the crisis passes, and raise rents again. Five key families, all billionaires, virtually monopolize the property sector, and will generally wait out a crisis rather than lower rents. They are content to see empty store fronts because they know that the minute they start to issue rent deals all tenants will follow with their demands. However, two property giants, Wharf & Hang Lung, posted almost $1 Billion in combined losses in their first half of 2020, and are starting to offer some short-term rent concessions. Some tenants have banded together and gone on strike for lower rents during COVID to try and curtail their losses.

International tourism and large-scale visits from Mainland China are not likely to resume until sometime in 2021, with all depending on a reliable and safe virus vaccine. The USA-China disputes are also not going to go away even with a vaccine, as increased sanctions may impact the overall mood of the city. Retail sales will continue to be anemic at least for the next 12 months.

Labor is another big challenge. Hong Kong parents simply do not want their children working in the restaurant sector. Like most Asian families, they care most about their kid's education and view the restaurant sector as a low-class vocation they wish their children can avoid except as a second chance career move. Loyalty to an employer is also very low and it is very common for staff to seek higher paying jobs as soon as opportunities present themselves. While labor laws are generally very employer friendly, workers in the restaurant industries have some bargaining power given the limited supply. Many Western restaurant groups try to supplement local labor with Nepalese and Filipinos to some extent but importing such labor may be more difficult going forward.

Moreover, menu pricing tends to be low especially in the mass market. For example, McDonald's Big Mac meal pricing is one of the lowest in the world when one considers the level of overall wealth in Hong Kong. Naturally with a cap on menu prices and high labor and tenancy costs, food costs tend to be very low resulting in smaller portions with poor nutritional properties – lots of carbs and very little protein.

For local operators with nowhere else to go, they must stay and wage the war to eke out a profit in this environment. They simply have no other options other than change their careers. However, we all know that people in this industry all over the world generally love what they do and will continue to fight on for another day in the hopes their business improves.

The situation is different for international groups. Recently, many global fashion brands have had enough and are pulling out at least for now. The successful international chains that have been in Hong Kong for many years such as McDonald's, Pizza Express and Outback Steakhouse are likely to carry on with perhaps fewer locations. The newer entrants like Five Guys Burgers and Cheesecake Factory will probably keep what they have and expand only when they see a great long-term rental deal. There will also always be room for local entrepreneurs catering to Westerners & upscale Chinese like The Black Sheep Group, among others.

New brands considering entry should be cautious and generally avoid the market all together in my opinion. Why do they want to consider entering Hong Kong in the first place? Is this just a "plant the flag" exercise or is there some strategic reason? It does make sense for successful Mainland brands to enter the city, since they probably have good brand awareness and have a menu most Hong Konger's enjoy such as rice and noodles. There is also almost no appetite in the local F&B community to franchise any international restaurant concepts except under very unusual conditions.

Hong Kong was a tough market before the protests and COVID, but it is far more challenging today. I think you would have to be a bit crazy to seriously consider starting a restaurant business there today, but there are many crazy people in this world…