Food apps provide slim pickings for investors

The online food delivery industry may be booming but just like anything new, there is a caveat for investors who wish to access it, according to Maria Toneva, global research analyst at Newton.

An influx of new mobile apps, which do everything from helping users with workout plans to providing hints and tips on how to survive an apocalypse, have created substantial changes to investment sectors just as the gig economy has formed ripples in the nature of employment. Together the two have made things more convenient for consumers. Case in point: the world of food.

One of the most globally favored ways to access food online, from millennials to Generation X, is through the use of instant food delivery apps. Many may recognize the names of popular services such as UberEats, Seamless and Grubhub, while one of the leading online food delivery marketplaces in the US is DoorDash.

These services are accessible via apps and enable consumers to order food from hundreds of restaurants in proximity of their location for a small fee—expanding meal deliveries beyond the traditional pizza and Chinese delivery services which gained popularity in the 1990s.

Such is the rising popularity of these services—online food delivery is set to become a US$200bn industry by 2025. However, Maria Toneva, global research analyst at Newton, says with new entrants constantly trying to enter this space and all the additional costs associated, it may make the industry convoluted in the eyes of an investor.

“There’s huge uncertainty as to how investors would make money. These companies can generate a lot of money from consumers but when you add in the other additional costs of pay-out to the deliverers and restaurants, their platform revenue becomes eroded,” she says.

“Another implication to consider is that there’s a lot of private equity money out there. This is a highly competitive market and a lot of the big players are subsidizing the delivery aspect of it,” she continues.

For example, one popular delivery app offers a subscription program to its customers. For a set amount each month customers get unlimited free delivery on orders, along with other discounts and offers. With perks like that, consumers win by getting to order as much as they want, whenever they want throughout the month. However, according to Toneva, the company may struggle with future profitability as they still need to pay the ‘deliverer’ hourly wages and pay out a portion of the sales to the restaurant.

“Reminiscent of the dot.com boom of the late 90s, the cash burn of such businesses is high and a winning or dominant business model has yet to emerge,” says Toneva. “Complicating matters is the fact that many such companies feature delivery staff that epitomize the downside of the gig economy,” she continues. This has resulted in criticism being leveled at such services over the lack of job security and benefits.

Foodora, a food app popular in Canada, Norway and The Philippines, was recently forced to implement a new contract for 600 Nordic employees after they went on strike. The new contract guarantees compensation for equipment used on the job, which include bikes, clothes and smartphones (which are usually supplied by the employee) as well as an annual pay increase for full time workers. It is considered one of the first successful collective bargaining agreements between a global food delivery platform and a trade union.
Despite the attractiveness to consumers of the food industry, the question remains, is the food app marketplace mature enough for investors to generate returns? According to Toneva, the only way profit would seem achievable at this stage would be through consolidation. “That’s the only way we’re going to see a change in this industry. Otherwise the delivery fee would need to increase significantly but even if that were to happen, it could make customers lose interest and order less,” says Toneva.

UK-based JustEat and its former rival Netherlands-based Takeaway.com recently agreed a £9bn ($11.6bn) merger, which would make them one the world’s largest online food companies, but the deal is yet to be finalized. With talks of the deal officially being in action by the end of the year, the merger would make the enlarged company UberEats’ biggest competitor.

“In our view the market needs to consolidate. It needs to become less competitive in order for investors to really make a profit, but at this stage globally, the big companies are still interested in competing with one another,” she concludes.
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