

Carsten Hirschberg,
Alexander Rajko,
Thomas Schumacher,
and Martin Wrulich

The changing market for food delivery

Telecommunications November 2016

Online food-delivery platforms are expanding choice and convenience, allowing customers to order from a wide array of restaurants with a single tap of their mobile phone.

The business of delivering restaurant meals to the home is undergoing rapid change as new online platforms race to capture markets and customers across the Americas, Asia, Europe, and the Middle East. Although these new Internet platforms are attracting considerable investment and high valuations—already, five are valued at more than \$1 billion—little real knowledge about market dynamics, growth potential, or customer behavior exists. Research from McKinsey, based on a six-month study covering 16 countries around the globe, provides insight into this fast-changing market.

The shape of the market today

Worldwide, the market for food delivery stands at €83 billion, or 1 percent of the total food market and 4 percent of food sold through restaurants and fast-food chains. It has already matured in most countries, with an overall annual growth rate estimated at just 3.5 percent for the next five years.

By far, the most common form of delivery is the traditional model, in which the consumer places an order with the local pizza parlor or Chinese restaurant (although many other kinds of restaurants, particularly in urban areas, now offer delivery) and waits for the restaurant to bring the food to the door. This traditional category has a 90 percent market share, and most of those orders—almost three-quarters—are still placed by phone.

However, as in so many other sectors, the rise of digital technology is reshaping the market. Consumers accustomed to shopping online through apps or websites, with maximum convenience and transparency, increasingly expect the same experience when it comes to ordering dinner.

Two tiers for online food delivery

Two types of online platforms have risen to fill that void. The first type is the “aggregators,” which emerged roughly 15 years ago; the second is the “new delivery” players, which appeared in 2013. Both allow consumers to compare menus, scan and post reviews, and place orders from

a variety of restaurants with a single click. The aggregators, which are part of the traditional-delivery category, simply take orders from customers and route them to restaurants, which handle the delivery themselves. In contrast, the new-delivery players build their own logistics networks, providing delivery for restaurants that don't have their own drivers.

Aggregators

Aggregators build on the traditional model for food delivery, offering access to multiple restaurants through a single online portal. By logging in to the site or the app, consumers can quickly compare menus, prices, and reviews from peers. The aggregators collect a fixed margin of the order, which is paid by the restaurant, and the restaurant handles the actual delivery. There is no additional cost to the consumer. With their asset-light model, aggregators post earnings before interest, taxes, depreciation, and amortization (EBITDA) margins of 40 to 50 percent. Although investment continues to pour in (Delivery Hero and Foodpanda, for example, both attracted €100 million in new investment in 2015), most of the consolidation in this subcategory has already occurred. Four players—Delivery Hero, Foodpanda, GrubHub, and Just Eat—have achieved global scale. These four players tend to focus on different regions. On a national level, there are typically two or three competitors that dominate, mostly driven by their ability to build a large user base. Consolidation is advanced in most markets and will likely continue. McKinsey research shows that just 26 percent of traditional-delivery orders are made online today, but we expect this share to increase rapidly.

New delivery

Just like the aggregators, new-delivery players allow consumers to compare offerings and order meals from a group of restaurants through a single website or app. Crucially, the players in this category also provide the logistics for the restaurant. This allows them to open a new segment of the restaurant market to home delivery: higher-end restaurants that traditionally did not deliver. The new-delivery players are compensated by the restaurant with a fixed margin of the order, as well as with a small flat fee from the customer. Despite the higher costs of maintaining delivery vehicles and drivers, the new-delivery players achieve EBITDA margins of more than 30 percent. Players include brands that operate globally such as Deliveroo and Foodora, which are continuing to capture new regions. We believe the addressable market for new delivery will reach more than €20 billion by 2025.

Both aggregators and new-delivery players have attracted significant investment, allowing them to advertise widely and build recognition for their brands quickly. GrubHub and Just Eat, for example, each reported marketing budgets of about €70 million in 2015. Since there is no limit to the number of restaurants these platforms can sign up, once they enter a market, they can grow rapidly (see sidebar, “The new-delivery business model.”)

The new-delivery opportunity

The opportunity for new delivery is to extend food delivery to a new group of restaurants and customers. Rather than competing directly with the aggregators, new-delivery players

The new-delivery business model

As the newest online category, new delivery offers advantages (as well as some disadvantages) for restaurants, customers, and deliverers.

The restaurant

For restaurants, the new model offers an additional source of revenue and a higher utilization rate of existing kitchen facilities, as well as the chance to build relationships with a new pool of customers. The platforms offer free marketing and a logistics network for restaurants that previously were not able to deliver meals. While an estimated 1 percent of current on-premises customers will migrate to home delivery, total restaurant spending by high-income households will increase by an estimated 10 percent. However, there is potential for greater disruption if more high-end customers opt to consume restaurant meals at home. Another downside: the restaurant has little control over the customer experience.

The customer

Here, the advantages are convenience, greater choice, and more restaurants than previously were available for meal delivery. This is especially attractive to customers looking for healthier alternatives to pizza. The customer also benefits from the ability to track delivery in real time.

The deliverer

New-delivery operators can control the complete customer experience. In addition, with their wide portfolio of restaurants that previously served meals only on their premises, new-delivery players are able to tap into a new tier of consumers for home delivery of meals. By working with higher-end restaurants, new-delivery players achieve a higher average order size than the aggregators. The biggest disadvantage is the need to invest in a delivery fleet and drivers, which can quickly turn into a cash drain if the operators cannot achieve a high rate of utilization.

are expanding the overall market. However, it is possible that in the future even lower-end traditional-delivery restaurants will migrate to new delivery because they will find it more cost efficient to outsource logistics; thus, new delivery poses at least a potential threat of disruption to the aggregators.

The growth in new delivery is driven by two sources of consumer demand. This first is as a substitution for dining in a restaurant. With new delivery, consumers can dine at home with the same quality food they would enjoy at a fine restaurant. Some platforms even include Michelin-starred establishments in their offerings in selected cities. The second source of demand is as a substitution for meals prepared and consumed at home.

Customer behavior

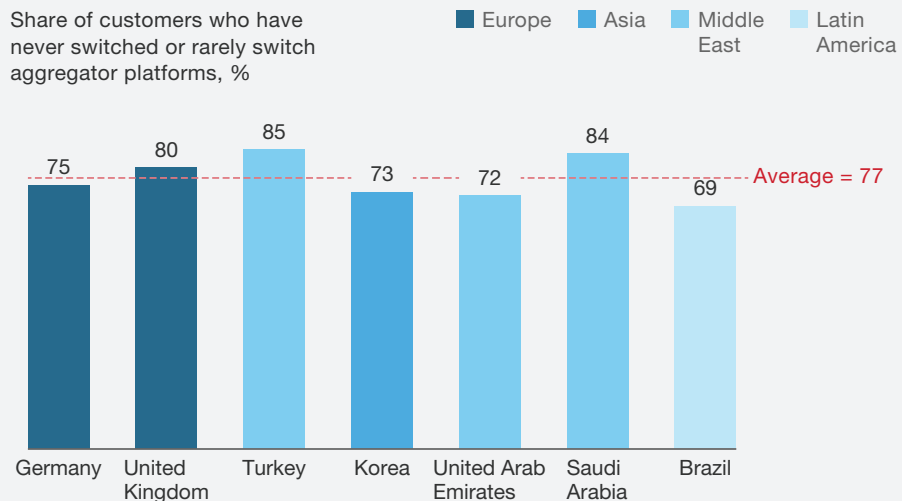
Customers drawn to the new online food-delivery platforms have a different set of needs and expectations from the traditional pizza customer. Our study uncovered the following important traits:

- **Platforms are sticky.** New-delivery platforms, which personalize the ordering experience by storing relevant customer data, are sticky (Exhibit 1). Once customers sign up, 80 percent never or rarely leave for another platform, creating a strong winner-take-all dynamic, in which the reward goes to the player who can sign up the most customers in the shortest amount of time.
- **Time is critical.** Speed of delivery is the biggest variable in customer satisfaction, with an average 60 percent of consumers across markets citing it as a key factor. The optimal wait time is no more than 60 minutes.
- **Meals are for home.** Most orders—82 percent—were placed from home, while only 16 percent were placed from the workplace.
- **Orders spike on weekends.** The highest-volume days for the online platforms were Friday, Saturday, and Sunday, when 74 percent of orders were placed.

Exhibit 1

New-delivery platforms have a proven track record of retaining customers.

Share of customers who have never switched or rarely switch aggregator platforms, %



McKinsey&Company | Source: McKinsey consumer research (n = 10,000), Sept 2015

Channel migration

With the new online platforms making inroads around the world, the food-delivery market is in the midst of a dramatic channel migration. We expect online delivery to grow by 25.0 percent per year from 2015 to 2018 in key markets, after which it will taper off to 14.9 percent per year until 2020 (Exhibit 2).

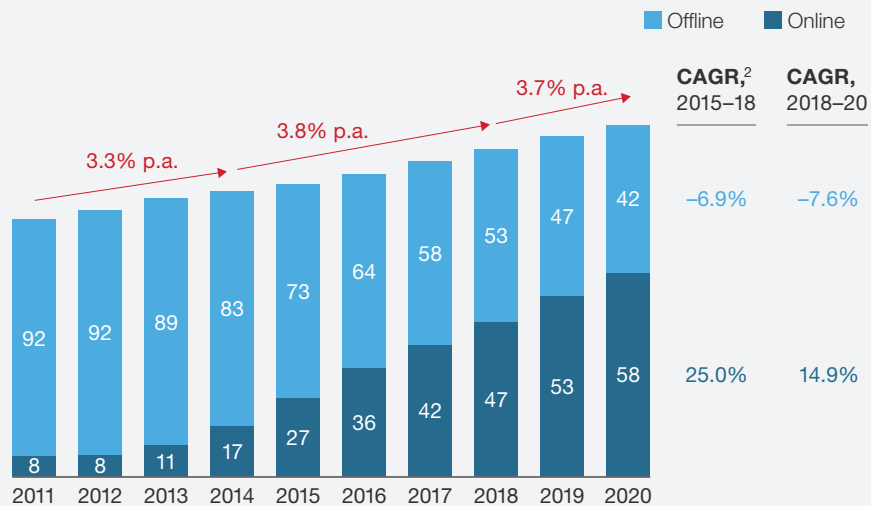
Our research indicates that online’s penetration of the total food-delivery market broke 30 percent in 2016. We believe penetration rates will grow further as the market matures, eventually reaching 65 percent per year. This is the pattern we’ve seen, for example, in the more mature flight-booking category, which has seen a dramatic channel migration over the past 10 to 15 years, as well as for selected food-delivery players, such as Domino’s Pizza in the United States. It is quite likely that the food category will follow these patterns.

We’ve already seen much of that growth pattern play out in Europe, where online penetration rates run from 56 percent in Sweden to 43 percent in Austria. At the other end of the spectrum, Asia, Latin America, and the Middle East are at the beginning of the growth cycle. The key

Exhibit 2

The food-delivery market has the potential for robust growth.

Total addressable classic food-delivery market,¹ %



¹For selected countries only.
²Compound annual growth rate.

Exhibit 3

Valuations for new-delivery companies are rising rapidly.

Key players	Market valuation, Aug 2016, € million	Foundation	Life-cycle stage	Business model	
				Classic delivery	New delivery
Just Eat	4,620	2001	IPO (2014)	●	
GrubHub	2,950	2004	IPO (2014)	●	
Delivery Hero	2,740	2011	Series I (2015)	●	●
Deliveroo	1,000	2013	Series E (2016)		●
Takeaway.com	1,000	2000	Series B (2014)	●	●
Foodpanda	500	2012	Series E (2015)	●	●

McKinsey&Company

catalysts for the adoption of online food delivery are the overall level of funding for the industry and the size of marketing budgets. Technology penetration—mainly smartphone and online penetration—has only been slightly relevant to the speed of adoption so far due to the geographic expansion of food players. We believe that the food category will grow in line with the smartphone category as new smartphone users adapt their behavior to take full advantage of the technology.

With the top five global players having reached a combined valuation of more than €10 billion, the key question is what a sustainable level of profitability will be for the online-food-delivery business models. The market has become more bullish on the sector, giving the players that are still private significantly higher valuations and higher levels of funding than earlier companies achieved at the same stage (Exhibit 3). Two of the top five online deliverers, GrubHub and Just Eat, made their IPOs in 2014. They raised moderate total funding, of less than €100 million, before their IPOs. In contrast, Delivery Hero and Deliveroo, which could see their own IPOs in the next year or two, already have high valuation-to-equity ratios: Delivery Hero has €2.7 billion valuation versus €1.2 billion funding (a ratio of 2.2:1) and Deliveroo has an estimated valuation of €1 billion versus total funding of €4 million (2.5:1). Clearly, the market believes there is still rapid growth ahead for these players. The challenge now is for them to deliver on that belief. □

Carsten Hirschberg is a senior partner in McKinsey's Berlin office, **Alexander Rajko** is a consultant in the Cologne office, **Thomas Schumacher** is a partner in the Düsseldorf office, and **Martin Wrulich** is a partner in the Vienna office.