

PHOENIX BUSINESS JOURNAL

Economy shaping up

Experts say poor rankings
don't reflect the real picture

ERIC JAY TOLL, 10

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EXECUTIVE INC.

LEARNING A NEW HISTORY 27

REAL ESTATE

CEO opts for Dallas over Phoenix

Frank Busch sees greater expansion
possibilities in Texas. **MIKE SUNNUCKS, 9**

HEALTH CARE

Valley has right Rx for specialty pharmacies

Avella CEO Rebecca Shanahan talks
about why the Phoenix area has seen
new players come in and existing ones
expand. **ANGELA GONZALES, 18**

TECHNOLOGY

Allbound gets \$1.5M in funding

Seed round adds to money raised by
software startup. **HAYLEY RINGLE, 12**

RESTAURANTS

Pizza, taco eateries opening

Restaurant expansions continue as
Sauce and Chronic Tacos look to tap
into more diners' tastes.

STEVEN TOTTON, 24

OVER COOKED

Phoenix's restaurant scene is bigger
than ever, but it may be running out
of space for new concepts as rents
increase and competition grows.

STORIES BY MIKE SUNNUCKS 4-7

Not for commercial use



REAL ESTATE

HISTORIC CHURCH GETTING MAKEOVER 8

T H E
L I S T

VALLEY PR PROS TALK ABOUT BRANDING

Between social media and real
life, people create their own
brands, creating ramifications
in the business world.

CASSIDY TROWBRIDGE, 21



ENTREPRENEUR

BUILDING A BETTER BABY BIB 29

CELEBRATING

35
YEARS

1980 - 2015



BACK IN BUSINESS

STATE FAIR EVOLVES INTO ENTERTAINMENT

16

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COVER STORY

FOOD FOR THOUGHT

BY MIKE SUNNUCKS

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PHOTOS BY JIM POULIN | PHOENIX BUSINESS JOURNAL

Every Arizonan will spend a record \$1,700-plus this year dining out.

That will generate an estimated \$11.5 billion in total restaurant sales statewide – also a record, according to the National Restaurant Association.

This kind of spending has benefited Phoenix-area restaurants, especially homegrown ones, which have surged since the recession and are pulling in almost double the revenue they earned during 2005.

Dining out has become a popular pastime in the Valley, and restaurants now are driving infill and adaptive reuse real estate developments in central Phoenix, the Arcadia area and Tempe. They also are driving traffic to – and filling space in – shopping centers that lost many brick-and-mortar retailers to the world of Amazon and other online services.

Restaurants are a big reason the regional retail vacancy rate is at 9 percent, according to commercial real estate firm CBRE, while office vacancies languish above 20 percent.

But some question the continued ability of new, independent restaurants to drive the commercial real estate recovery, and others are seeing signs of a bubble ready to burst.

Longtime commercial developer and landlord Michael Pollack sees the writing on the wall that the surge may be ending. He owns 2 million square feet of commercial space in Arizona and 1 million square feet in California. About 70 percent of the restaurants he gets inquiries from are unable to meet his criteria for leasing space because of the lack of a solid business plan, adequate financing or business acumen to survive, let alone succeed, he said.

"I think the only recipe these people will be good at is a recipe for disaster," he said.

Pollack said he's more apt to lease to an existing restaurant concept or business that has had a track record. He said one prospective tenant asked him for three months free rent and then hoped to make it a month-to-month arrangement rather than a long-term lease.

A perfect storm

Arizona's rising restaurant tide is the result of a confluence of factors. The National Restaurant Association projects a 23.8 percent growth in restaurant jobs statewide during the next decade, which is tops in the U.S. There currently



"You can't get a dining experience through Amazon."

GERMAN OSIO, CEO, Osio Culinary Group

are 208,000 restaurant and bar workers across Arizona. That is up 7,000 jobs from last year and 23,200 from 2012, according to the Arizona Department of Administration.

New ventures are popping up, existing eateries are expanding, and chefs are getting out of the kitchen to open businesses. Investors and baby boomers are putting money into restaurants with aspirations of being the next Bobby Flay or Wolfgang Puck.

"We all kind of woke up at the same time," said chef Justin Beckett, owner of Beckett's Table and Southern Rail



"I think the only recipe these people will be good at is a recipe for disaster."

MICHAEL POLLACK, Michael A. Pollack Real Estate Investments Inc.

restaurants in Phoenix.

The growth stems from a perfect economic, demographic and real estate storm following the Great Recession that propelled local restaurants in a market historically dominated by chains.

The recession left in its wake distressed and empty properties. That lowered rents and opened landlords and developers to leasing to restaurants, as well as renovating existing space for food-centered concepts.

Jared Lively, a commercial real estate broker and vice president with Rein & Grossoehme Commercial Real Estate in Scottsdale, said restaurants were able to get space for \$16 to \$18 per square foot during and immediately after the recession. Now, that same space is going for \$25 to \$30 per square foot.

As a result of cheap rents, restaurants have driven adaptive-reuse and infill projects. The Yard redevelopment near Seventh Street and Bethany Home Road in Phoenix, home to Sam Fox's Culinary Dropout concept, led the way in that segment. It was followed by Upward Projects' restaurant hub on Central Avenue and others.

Now, infill developers such as Davis Enterprises, Wetta Ventures and Venue Projects have found a niche in adaptive-reuse projects focused on restaurants.





Justin Beckett yells into his bullhorn, a gift given to him a few birthdays ago, at his restaurant on Indian School Road near 36th Street.

Wetta is redeveloping a furniture store at Indian School Road and 28th Street in Phoenix into restaurant redevelopment. Davis is redoing a former college bookstore on Rural Road next to Arizona State University in Tempe into a new restaurant and retail project.

The resurgence of the Town & Country shopping center at Camelback Road and 20th Street has been driven, in part, by restaurants such as Pizzeria Bianco, Snooze and Grassroots Kitchen.

Lively, who currently is marketing the redevelopment of a 10,000-square-foot office building near 32nd Street and Indian School Road into a 4,000-square-foot restaurant and 6,000 square feet of retail space, said the renovation wave is expanding the boundaries of desirable submarkets such as the Arcadia neighborhood in Phoenix.

'The good deals are done'

The commercial real estate market is clawing its way back from the recession, but rising rents are making it harder on independent restaurants. Lively said there is some sticker shock for restaurateurs who might have gotten a sweet deal in 2010. There also are cases where landlords are dramatically raising rents on existing tenants.

Pollack said while he is loyal to tenants who leased during the recession, he's seen some other landlords try to raise rents 50 to 60 percent. Those increases can push restaurants with already tight margins out of a location or out of business.

Robin Trick, who owns House of Tricks in downtown Tempe with her husband Robert, said she believed all the cheap leases restaurants signed during and right after the downturn are a thing of the past.

"I think the good deals are done," said Trick.

The increase in restaurants also has many concepts chasing the same amount of consumers and the same money, Trick said.

The plus side to the expansion is it is helping Tempe move beyond bars and cheap eats for ASU students, Trick said.

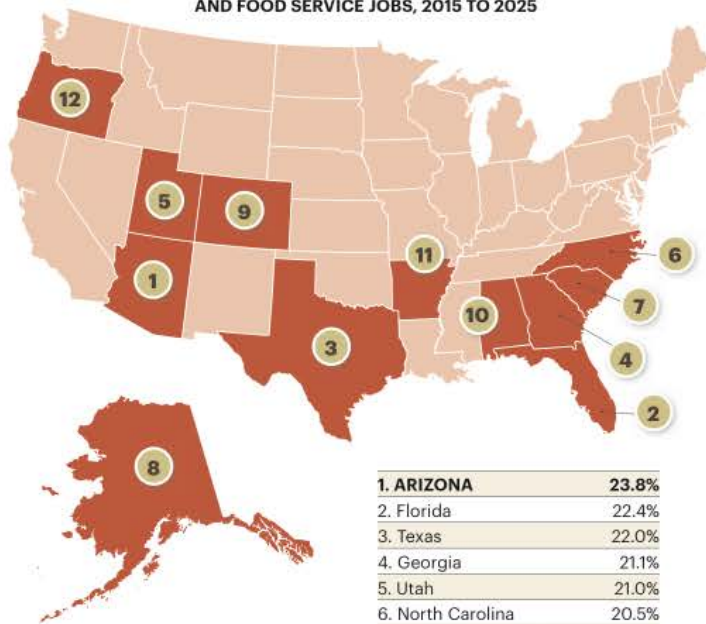
"It's making Tempe a little bit more of a destination," she said.

Still, Pollack and others interviewed for this story wonder when all the new restaurants and restaurant-oriented development will reach a saturation point.

"There comes a point where anything can be oversaturated," he said.

CONTINUED ON PAGE 6

PROJECTED GROWTH IN RESTAURANT AND FOOD SERVICE JOBS, 2015 TO 2025



1. ARIZONA	23.8%
2. Florida	22.4%
3. Texas	22.0%
4. Georgia	21.1%
5. Utah	21.0%
6. North Carolina	20.5%
7. South Carolina	18.6%
8. Alaska	16.1%
9. Colorado	15.7%
10. Alabama	15.3%
11. Arkansas	14.7%
12. Oregon	14.7%

SOURCE: NATIONAL RESTAURANT ASSOCIATION

2015 RESTAURANT SALES (PROJECTED)



SOURCE: NATIONAL RESTAURANT ASSOCIATION

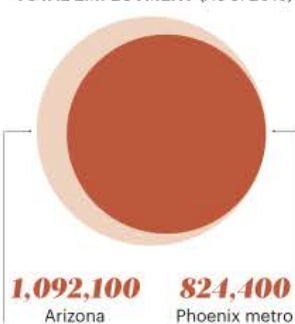
ARIZONA EMPLOYMENT (AUG. 2015)

Sector	Employees	Change from August 2014
Restaurants, bars	208,000	7,000
Health care	282,000	10,300
Retail	315,100	5,000
Manufacturing	156,700	-200
Construction	130,300	5,100

PHOENIX METRO EMPLOYMENT (AUG. 2015)

Sector	Employees	Change from August 2014
Restaurants, bars	147,100	5,400
Health care	233,700	9,600
Retail	223,000	3,500
Manufacturing	118,100	-600
Construction	102,500	7,000

TOTAL EMPLOYMENT (AUG. 2015)



SOURCE: ARIZONA DEPARTMENT OF ADMINISTRATION



German Osio, owner of Osio Culinary Group, thinks the Phoenix restaurant scene needs more ethnic and Mexican concepts.

Osio looks to take SumoMaya to Texas, California, other markets

A prominent local chef wants to take one of his successful concepts national.

Chef German Osio plans to bring his SumoMaya Mexican-Asian Kitchen concept to a handful of other major U.S. cities. The first SumoMaya opened in Scottsdale in 2014.

Osio said he hopes to open SumoMaya restaurants in Houston and Dallas. Those could open next year. He's also looking at locations in markets such as Austin, Denver and Pasadena, California.

SumoMaya is a fusion of Mexican and Asian cuisines. Its menu features sushi rolls with chipotle, pickled jalapeños and other Mexican flairs. Other dishes include Korean beef tacos, tamarind shrimp and a Mexican version of Vietnamese pho soup.

Osio was born in Mexico City and is CEO of Osio Culinary Group. He also owns Local Bistro, Central Bistro and Kale & Clover.

SumoMaya is at the Marketplace at Lincoln Scottsdale. The restaurant-heavy center is at Lincoln Drive and Scottsdale Road. The center sold earlier this year for \$14 million.

Jared Lively, a vice president at Scottsdale-based Rein & Grosseohme Commercial Real Estate who specializes in the restaurant sector, said concepts such as SumoMaya fit well in current consumers' wheelhouses of unique dining options and a unique atmosphere.

"It's a hybrid," Lively said. "It constructs its own agenda."

There is plenty of economic growth in Texas, especially Dallas. The Dallas-Fort Worth market had 8.5 percent regional GDP growth in 2014, according to the U.S. Commerce Department. Phoenix's GDP growth last year was 1.8 percent, 148th among U.S. metros.

Osio also plans to open a new restaurant at the Colony redevelopment project at Seventh Street and Missouri Avenue in Phoenix. He said that restaurant will be more of a modern Mexican coastal diner.

He believes Phoenix needs some new concepts in its ethnic and Mexican food scenes.

"I feel there is just a need for it," Osio said.

— Mike Sunnucks

COVER STORY

CONTINUED FROM PAGE 5

Retail down, restaurants up

Steve Chucuri, president and CEO of the Arizona Restaurant Association, counters there are major economic and demographic trends working in restaurants' favor of continued growth. He points to national and regional consumer data showing restaurant spending outpacing grocery store shopping.

Millennials, empty-nest baby boomers and households in which both partners are working all contribute to restaurant dining and take-out winning out over home cooking. Chucuri said even during the recession, restaurants were seeing plenty of sales.

"That means people making \$25,000 or \$30,000 a year were dining out a lot, too," said Chucuri, adding lower gas prices are putting more money in consumers' pockets and that is giving people the discretionary income to eat out.

The 'buying local' phenomenon also may be feeding the frenzy for successful concepts such as Upward Projects' Postino, and local chefs and restaurateurs such as Fox, Kevin Binkley, Beckett and German Osio are receiving regional and national acclaim.

"We've become a culinary destination in many ways," Chucuri said.

Osio, CEO of Osio Culinary Group and owner of SumoMaya and other restaurants in Phoenix and Scottsdale, said the decline of brick-and-mortar retail has made restaurants and coffee shops key traffic drivers for shopping centers.

"Retail is down," he said. "You can't get a dining experience through Amazon."

Osio said during the recession a number of Scottsdale restaurants were insulated because of then-favorable exchange rates with Canada, whose visitors continued to flock to the region.



Osio and Beckett said Phoenix still has a long way to go to have the kind of restaurant market seen in California. Osio said Phoenix needs to cultivate a stronger mix of ethnic restaurants to go along with its bevy of contemporary concepts.

"We're still missing a big part of it," said Osio, who is opening a new Mexican restaurant at the Colony restaurant redevelopment at Seventh Street and Missouri Avenue.

Natural selection

Chefs, developers and real estate brokers all expect to see some new and existing restaurants falter as more competition



Justin Beckett prepares all the ingredients in advance for his recipes so every dish on his menu is 90 percent complete. When a diner orders from the menu, he and his staff are able to plate the meals in a timely manner.



SumoMaya Executive Chef Matt Zdeb works to combine Mexican and Asian flavors for a unique culinary experience.

hits the market, rents rise and consumer tastes change.

"I definitely do think there will be some weeding out," Osio said.


There have been some notable casualties. Kincaid's in downtown Phoenix, a longtime business lunch spot, succumbed earlier this year to competition from restaurants at neighboring CityScape.

Startup costs can be another deterrent. Beckett said it can cost between \$200,000 and \$3 million to start up a restaurant. That often puts a new venture behind the financial eight-ball even before it opens for business.

It's often better to take over an existing restaurant space that has grease traps and fixtures in place. That can run as little as \$5,000 to get going, Pollack said.

Still, many aspiring chef-owners aren't prepared for the tight margins and attention to detail it takes to run a restaurant, Trick, Osio and Beckett all said.

While those are prone to fail, there is hope in the restaurant realm that a new concept or venture can work, even where previous attempts have failed.

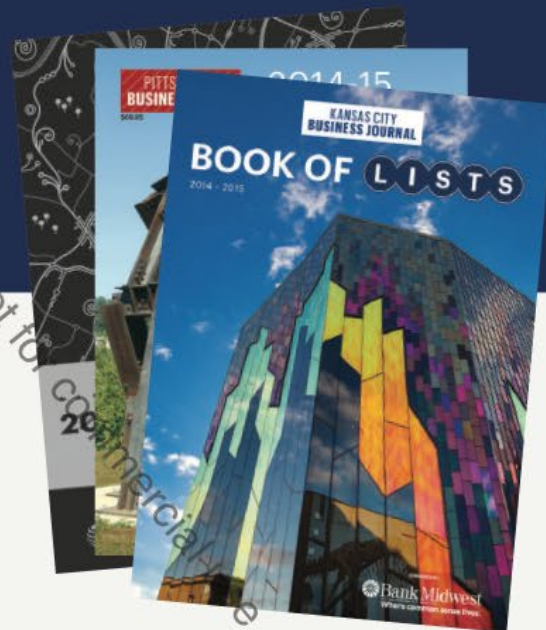
"There's a time and a place for everything," Beckett said. 



Jared Lively of Rein & Grossoehme stands inside one of his brokered deals called 32 Fairmount, a redevelopment aimed at restaurant and retail users.

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