12 May 2015

# ENTERPRISE INNS (ETI): 132.4p
## First Half Results – 6mths to 31 Mar 2015:

*Group says will be 'maximising the returns from each of our assets to drive sustainable shareholder value…'*

| Year to end-Sep | PBT (£m) | EPS (p) | PER (x) | DPS (p) | Yield (%) |
|---|---|---|---|---|---|
| 2014 (A) | 121.0 | 19.0 | 7.0 | Nil | Nil |
| 2015 (E) | 123.5 | 18.7 | 7.1 | Nil | Nil |
| 2016 (E) | 127.2 | 19.2 | 6.9 | 0.5 | 0.4 |

Source: *Company & Broker Estimates*

## H1 Results: 6mths to 31 Mar 2015:

Enterprise has today produced a trading update for the 6mths to 31 March 2015 and our comments are set out below:

- The group has achieved LfL income growth of 0.6% in the 6mths under review. This represents an acceleration from the 0.3% seen in the first 18wks of the period
- Revenue was £302m v £308m last year. Pre-exceptional EBITDA was £144m (2014: £147m) and pre-exceptional PBT was £57m against £55m last year
- The group says its 'operational focus aimed at supporting our publicans has helped to deliver a 21% reduction in the number of business failures'
- EPS is up 4.7% at 9.0p (2014: 8.6p) and there is no dividend. LfL sales trends are shown below:

**Tab.1. Enterprise Inns LfL Income Trends:**

| Period | Ave.income per pub (%) | LfL income per pub (%) | LfL income, substantive estate (%) |
|---|---|---|---|
| H1 – 2008/09 | -8.0 | | |
| FY – 2008/09 | -8.0 | | |
| H1 – 2009/10 | -3.1 | | |
| FY – 2009/10 | -2.0 | | |
| H1 – 2010/11 | 0.0 | -5.0 | -1.5 |
| FY – 2010/11 | +1.0 | | |
| H1 – 2011/12 | +3.2 | -1.6 | +1.5 |

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Market Cap: £670m
12m range 98p - 146p

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| | | | |
|---|---|---|---|
| FY – 2011/12 | +2.6 | -1.2 | +2.2 |
| H1 – 2012/13 | | -4.2 | |
| Est. 'real' decline | | -2.0 | |
| Q3 – 2012/13 | | -2.7 | |
| Q4 – 2012/13 | | +0.6 | |
| FY – 2012/13 | | -2.9 | |
| H1 – 2013/14 | | +1.1 | |
| Q3 – 2013/14 | | +2.1 | |
| Q4 – 2013/14 | | +0.5 | |
| FY – 2013/14 | | +1.4 | |
| First 18w 2014/15 | | +0.3 | |
| H1 – 2014/15 | | +0.6 | |

Source: Company Reports

## Strategic Review:

- Enterprise has this morning updated on its review following the passage of the Market Rent Only (MRO) clauses within the Small Business Bill

- The group says it aims to 'optimise the returns from every asset within our property portfolio.'

- In order to achieve this, the group is to increase its operational flexibility which means it will 'continue to reinvigorate our tied tenancy business; expand our managed business; build a high quality commercial property portfolio; and make disposals where appropriate to optimise returns'

- This is in line with our (and the market's) earlier expectation that the group would introduce managed units, some franchises, leased and tenanted units. There will in addition be a more actively managed 'property business'

- Enterprise says that 'whilst recognising that this will be a dynamic process we are planning that by September 2020 our managed pub business should be operating in the region of 750-850 pubs and we expect to have a commercial property business with around 900-1,000 property assets.'

## Balance sheet, capex & other:

- In view of the uncertainty caused by the proposed measures, Enterprise has delayed and may cancel some capital projects

- It has invested £33m in the period (2014: £41m) and has sold £34m worth of pubs (2014: £42m)

- The group had net debt at period-end of £2.4bn and ETI says 'we have been advised by our external valuers that there is no market evidence to suggest that these property valuations would be materially different' from their last valuation

- Enterprise maintains 'we have a long-term, secure, flexible and tax efficient financing structure comprising bank borrowings, securitised notes and corporate bonds.'

## Conclusion:

- CEO Simon Townsend says 'we are pleased to report like-for-like net income growth for the first half of the financial year.'

- He adds 'we are now implementing our new strategy which provides a clear path to maximise returns from each of our assets. We are building upon our core capability of operating leased

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and tenanted pubs by extending our operational flexibility into the direct management of pubs and increasing the scale of our commercial property business.'

- Mr Townsend concludes re the group's evolution that 'this is a sustainable strategy for our business which embraces different operating models to best serve our publicans and their communities whilst delivering greater value to our shareholders.'
- Elsewhere in the statement, the group adds that the finer details of legislation are yet to be worked out and that the changes will happen over a 5yr (lease review) period
- It adds that the 'unintended consequences of the SBEE Act will only become clear over time' but reassures that 'we are prepared for the implementation of the legislation and its potential impact on our business.'
- We would expect similar comments to be forthcoming from Punch Taverns post the arrival of its CEO elect, Duncan Garood, in June

**Langton Comment:** Enterprise has reported numbers broadly in line with forecasts and has reassured that trading remains in line with expectations.

Trading would look to have improved somewhat at H1 progressed and, in the light of what we are hearing from the industry as a whole (MARS & MAB to come on Thursday), a mildly positive LfL performance is broadly to be expected / hoped for.

As regards the strategic review, Enterprise has concluded that it needs to managed its estate much more actively.

This cannot be achieved via a spreadsheet and the group intends to grow a managed business. This was to be expected but, at around 800 units, it could be a little larger than had been previously thought.

This response seems correct but it will not be without execution risk. Where will the staff come from, for example? The structure will need to be created and the demand for managers (if ETI and PUB are to look for c2k GMs, 4k to 6k AGMs etc.) will increase markedly.

Salaries could rise as a result and this will impact the industry as a whole but, as they say, unintended consequences are, well, unintended.

But that doesn't make them any less real and, as ETI begins its progression from a company with the middle-hundreds of staff to one with perhaps 15,000, it will need to execute its plan flawlessly in order to avoid hiccups.

We believe that this, rather than being a negative, should help to focus the market on the true worth of the company – and on that of Punch Taverns.

In terms of valuation, the group should earn around 18.7p in the current year putting its shares on a still-undemanding 7.1x EPS with a little growth to come in FY16.

Unfortunately, the MRO option, for which the secondary legislation will only be prepared in the autumn, has injected a note of uncertainty into proceedings but the response OF Enterprise under the circumstances appears to be measured and correct – and inevitable.

We are not entirely pessimistic with regards to the outcome and believe that there is some upside risk developing in the share prices of ETI and other impacted pub companies.

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