Langton Capital Limited

4 Dec 2014

GREENE KING (GNK): 761p
H1 2014: Analysts' Meeting

Group reports 'margin decline to slow, Xmas looking good & Spirit purchase to create UK's largest managed operator…'

Year to end-Apr	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2014 (A)	173.1	61.4	12.4	28.4	3.7
2015 (E)	176.6	63.5	12.0	30.1	4.0
2016 (E)	192.6	69.6	10.9	32.6	4.3

Source: Company & Broker Estimates

H1 Results, Analysts' Meeting:

Following the release of its H1 numbers earlier this morning, Greene King hosted a meeting for analysts and our comments are set out below:

Overall Trading:

- Whilst an accepted part of its business strategy, Greene King's recent disposals of bottom-end tenancies will dilute earnings going forward
- Trading ex-disposals is better with the retained estate generating PBT +3% and EPS +5.3%

Greene King Retail:

- Greene King reports that the sales growth for the year, at 0.8%, whilst acceptable, was 'lower than expected'
- This has led to EBITDA per managed house falling by 1.1% over the period under review
- Margin is down 80bps. It will be down in H2, but by a lesser amount
- New sites continue to deliver returns ahead of their WACC and opening plans are unchanged
- Spirit plans are unchanged. The purchase will make GNK the 31 licensed retailer in the country with around 3,000 pubs
- The acquisition 'augments & accelerates' plans already in place
- Trading remains 'subdued' though macro-economic lead indicators (wages, employment, costs etc.) are positive

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Market Cap: £1.67bn
12m range 740p – 925p

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- GNK is focussing on 'intergenerational offers' & has brought its digital strategy in-house
- It continues to invest in its people, its properties & its product. Value remains key
- Cost inflation is abating

Pub Partners:

- Pub Partners' EBITDA will be down by around £12m on the year on the back of disposals
- The number of units will shortly have halved since 2010. GNK has a target of c750 units
- It was surprised at the MRO option but has a menu of responses from competing on price, through to taking units into managed or disposing of them
- Group does not see the MRO as a major financial issue
- GNK believes its licensees 'are in better health'

Brewing & Brands:

- Brewing has increased its market share with take home (lower margin) taking a larger share of sales. It has maintained investment in its brands.

Balance Sheet, Debt, Cash Flow & Other:

- Some £41m has been invested in H1 at a return of 27%
- Cash flow is described as 'strong'. Net debt is 4.2x EBITDA (prior year 4.6x) but this will edge higher as the full-year EBITDA loss on disposals feeds through

Langton Comment: Greene King has reassured that its strategy remains on track and suggests that the Spirit purchase will accelerate this process.

That said, margins are slipping a little (as they are at MAB & JDW – but not at MARS) and the consumer remains extremely value conscious.

Overall, we believe that, though GNK shares offer good value at current levels, it is perhaps not necessary to own every pub stock out there. However, as we have preferred SPRT, MARS & JDW for the bulk of 2014, we may find ourselves holders of GNK by default and would be relatively comfortable with that outturn.

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