Langton Capital Limited

28 Nov 2013

MARSTONS (MARS): 144p
Preliminary Results, Year to 5 Oct 2013

Group reports that it is in 'revenue, profit and dividend growth…'

Year to end-Sep	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2012 (A)	87.8	12.3	11.7	6.1	4.2
2013 (A)	88.4	12.3	11.7	6.4	4.4
2014 (E)	93.0	12.5	11.5	6.6	4.6

Source: *Company & Broker Estimates*

FY Results: Analysts' Meeting:

Following that announcement of its preliminary results for the 53 weeks to 5 October, Marston's hosted a meeting for analysts and our comments are set out below:

Trading:

- The group confirmed that the year was one of two halves. The weather was unhelpful in H1 but much better in H2. More importantly, the group saw 'strong underlying trading'
- Destination and Premium were particularly good; this is where the group will be investing surplus capital – capex next year (not only new-build) will be around £140m; costs are under control. There is little change to H1 trends
- Taverns were mixed with franchised units good and tenancies under some pressure; the former will be migrated to franchised and the latter will be sold in increasing numbers
- Brewing was strong in the off trade, but this did weigh on margins; the group's five breweries are running at around 85% of capacity

Cash Flow, Capital Spending & Debt:

- The group's financing is 'flexible', bank debt has been pushed out for five years and the interest paid in the securitisation peaked in FY13

The Disposal & Further Sales:

- Marston's is securing £450k per acre out of London. New River believes that it has upside but MARS chose the pubs that it took; New River was not allowed to cherry pick

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Market Cap: £930m
12m range 120p 166p

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- The sold pubs are all in the securitisation; outside the securitisation, MARS has around 30% of its pubs with debt to EBITDA of around 2x

- Some £60m worth of fourth quartile pubs will be sold this FY and next (at say £250k each) suggesting perhaps 600+ pubs will be sold in 24 months

Current Trading & Trading Outlook:

- CEO Ralph Findlay suggests that any recovery is currently hard to spot and the consumer is still counting his pennies. Value remains key

- Competition remains intense and ill-prepared operators and smaller, wet-led units are under pressure (hence the disposal & concentration on new builds)

- The group will add 60, large pubs in the next two years, built at an EBITDA multiple of only six times

- Christmas deposits are ahead of last year by as much as 30% to 50% in some Destination units and upcoming comps for H1 are soft

Conclusion:

- The group is innovative (fast cask, franchising, its sale & leaseback and now its sale to New River and it knows where it wants to be

- It has more control over its units, more will be either franchised or managed and Marston's units will be much larger in scale over time

Langton Comment: Marston's should generate funds that will be channelled back into around 90 managed, food-led units over the next three years and, as these kick in during FY15 and FY16, EPS growth should exceed 10%.

The market has to value the group's shares during this period of transition but Marston's has given a clear indication that it will maintain dividend progression and that it expects a higher quality of faster-growing earnings to once again cover the group's dividend more than twice by FY16.

Overall, we believe that Marston's has done the right thing in taking decisive steps to refocus its estate. The group's shareholders are to be paid (a rising) 4.4% whilst the transition takes place and the quality of the group's earnings is improved.

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