Langton Capital Limited

14 May 2015

MARSTONS (MARS): 163p
H1 Results: 26w to 4 Apr 2015

Group reports 'returns-focused strategy continuing to drive long-term shareholder value…'

Year to end-Sep	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2014 (A)	83.0	11.70	13.9	6.70	4.1
2015 (A)	91.8	12.65	12.9	7.05	4.3
2016 (E)	100.0	13.90	11.7	7.35	4.5

Source: Company & Broker Estimates

H1 Results: Analysts' Meeting:

Following the announcement of its H1 numbers to 4 April 2015, Marston's hosted a meeting for analysts and our comments are set out below:

Overall Trading Environment:

- MARS believes that there is 'more clarity' on the MRO and it believes the changes will have a 'minimal impact'
- The group has been on a 'journey' to take control of its assets (via the move to managed and franchised units). The aim was to have 85% of pubs in these categories, the group is currently at 76%
- MARS will move to around 1540 units in FY16. At that point, the churn of assets will essentially be complete
- The mix change is evident in the fact that average profits per pub rose by 17% in the last year. They are up 27% over the last 3yrs
- The cost outlook is relatively benign. Food, drink, utility costs should rise by between 2% and 3%. Wages will increase by 3%.
- Recent trading is ahead of that seen in H1

Destination & Premium:

- The group has got visibility on new builds out to FY18. But it cautions that more capacity is being put on in the market
- New build costs are rising. There is more competition per site and regulatory costs have increased
- The group will build more lodges. It will open 3 this year and perhaps 5 p.a. going forward.

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Market Cap: £968m
12m range 137p 169p

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- It will also open a number of Revere units & new Pitcher & Piano sites. These will largely be leasehold

Taverns:

- MARS will consider new-build taverns. It has one in mind at present. These will be less capital-intensive than Destination units. They will be c40% food rather than 60% plus at new-build Destination outlets
- Within Taverns, franchised LfLs are around 1pp ahead of managed LfLs

Leased:

- All indicators here are now positive
- Only 'two to three' lessees have taken advantage of the group's free-of-tie offer over the last 5yrs or so
- Units moving to FoT have seen EBITDA for MARS rise slightly – but these units may not be comparable over the whole estate

Brewing:

- The opportunity for premium ale in the off-trade is interesting. This market is £0.5bn & could go to £1bn by 2020.
- MARS is number one in both premium bottled & premium cask ale

Assets, Debt, Balance Sheet:

- Debt is not a problem. It is serviceable at 6.4x EBITDA – but the group is still targeting 5x over time.
- No new builds have 'gone wrong'
- Units are still being sold 'at high single-digit' PERs – they are mostly now land plays

Summary, Conclusion, Beer Tie & Other:

- Marston's has confirmed that the macro-outlook is better than it has been for some time – but the group cautions that more capacity is being put on
- Overall, it has reassured that the churn of its assets is coming to a close and that earnings will feed through going forward

Langton Comment: Marston's has confirmed that trading continues to be in line with expectations. In the first few weeks of H2 the group faced tougher comps but these are now flat for the remainder of the period.

Clearly Whit Week (featuring a Bank Holiday, Half Term and pay week) will be important in determining whether the consumer is capable of putting his/her hand in his/her pocket.

Thereafter, comps are manageable and, should the weather be average, Marston's should be able to make further progress.

During FY16 and beyond, new-builds will continue to kick in and the dilutive impact of disposals will have worked its way through the system.

Hence growth should pick up and, with the group's shares trading on an undemanding 12.9x this year's earnings falling to 11.7x in FY16, there is material upside.

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