Langton Capital Limited

27 May 2014

PUNCH TAVERNS (PUB): 14.25p
Update – Debt for Equity swap likely

Group reports latest proposed Proposals, debt for equity swap now seems to be on the agenda…

Year to end-Aug	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2013 (A)	17.0	5.7	2.5	Nil	Nil
2014 (E)	44.0	4.9	2.9	Nil	Nil
2015 (E)	40.0	4.6	3.0	Nil	Nil

Source: *Company & Broker Estimates*

Restructuring Update, Covenant Waiver:

Punch Taverns has this morning updated on the talks currently being held with its stakeholders regarding a restructuring of its debt and our comments are set out below:

Updated Proposals - Introduction:

- Punch Taverns has released details of 'restructuring terms proposed by a group of stakeholders in the Punch A and Punch B securitisations'
- It says the Proposals 'are supported in principle by a group of creditors…who together own or control c.34% of the notes across Punch A and Punch B and over 50% of junior notes in both securitisations and the equity share capital of Punch'
- It cautions that 'whilst the ABI Special Noteholder Committee is not currently signed up to the Proposals, substantial progress has been made in addressing their issues'
- The consent of other parties outside of the Stakeholder Group would be necessary and 'there can be no certainty that the Proposals will proceed'

Updated Proposals - Details:

- Whilst further details are given in the 30 page RNS, the new proposals include a potential debt for equity swap and issue of new shares
- Punch says 'a group of junior creditors would subscribe for ordinary shares in the Company at a significant discount to the current market price to raise additional funds to be applied to repay junior notes in the Punch A securitisation'

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Market Cap: £93m
12m range 9.25p 16.5p

Mark.brumby@langtoncapital.co.uk
Suite 415, No1 Alie Street, London, E1 8DE
020 7702 3389

- The Proposals would result in a reduction in total net debt (including the mark-to-market on interest rate swaps) of £0.6 billion.
- Significant equity dilution for existing shareholders would occur and the group says 'the Company's currently issued share capital would represent 15% of its total enlarged issued share capital following the restructuring'
- If the Proposals are implemented, pro-forma net debt to EBITDA of the group would fall to c7.7x at August 2014' and gross securitisation debt of £1,582 million would have an effective interest rate of c.7.9% including PIK interest

Updated Proposals - Conclusion:

- The Group is not yet recommending that shareholders approve the proposals. It says 'any decision by the Board to recommend a proposal involving dilution of existing shareholders would need to be carefully considered in terms of the value which it represents for existing shareholders'
- The Group adds that it would not be possible to launch any such restructuring before the end of June and says it 'will require an extension to the covenant waivers to provide sufficient time to implement a consensual restructuring'

Langton Comment: The new news here is that it is being proposed (or it is being proposed that it be proposed) that equity take significant dilution in order to stay in the game.

The junior bondholders are proposing issuing shares to themselves it order to redeem their own debt and the level at which that should be redeemed will be a matter for debate. This may be what the senior bondholders would like to see happen – i.e. that everyone below them in terms of covenants fight it out amongst themselves – but it may or may not be acceptable to Equity, depending on the terms.

If there were a Rights element, at or below the price at which the junior bonds are suggesting they subscribe (and depending upon the price of the junior bonds themselves), then it may be agreeable. But otherwise it could be best for Equity to vote down or at least to attempt to vote down the proposed proposals and take their chances with an Administrator.

This does not seem to be a very welcome turn. Agreement without dilution may or may not now be achievable. But, if agreement cannot be reached and a default occurs, then the securitisations are still 'owned' by equity, there are still assets held at PLC (cash, half of Matthew Clark, tax losses etc.), inflation will work to the advantage of the group's shareholders and a failure to agree and administration would not be the end of the world. The group's shares are likely to fall on this news but there remains very material upside, albeit at considerable and increasing risk.

Contact – Mark Brumby - +44(0)20 7702 3389

mark.brumby@langtoncapital.co.uk