22 Apr 2015

PUNCH TAVERNS (PUB): 103.25p
H1 Results; 28w to 7 March 2015

Group reports performance 'in line with expectations' & is in line to hit full year guidance…'

Year to end-Aug	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2014 (A)	50.8	n/a	n/a	Nil	Nil
2015 Est	57.2	21.1	4.9	Nil	Nil
2016 Est	59.6	21.4	4.8	Nil	Nil

Source: *Company & Broker Estimates*

H1 Results:

Punch Taverns has this morning reported H1 results for the 28w to 7 March 2015 and our comments are set out below:

Headline numbers:

- Punch Taverns has this morning reported H1 numbers for the 28w to 7 March saying that its 'performance [was] in line with expectations'
- EBITDA was £105m million (2014: £108m) and Punch has reiterated full year underlying EBITDA guidance of between £193m to £200m
- Core LfL net income grew by 0.5% (the core estate accounted for 90% of outlet EBITDA) and recent trading details are set out below:
- **Tab.1. Punch Taverns LfL EBITDA Per Pub Trends:**

Period	LfL EBITDA/pub (tot. estate) (%)	LfL EBITDA/pub (core estate) %	LfL EBITDA/pub (non-core) %
FY 07/08	-3.4		
H1 08/09	-11.3		
FY 08/09	-11.0		
H1 09/10	-11.0		
FY 09/10	-11.0		
H1 10/11	-7.0		
FY 10/11	-5.2	-2.1	-13.0
H1 11/12		-2.1	
FY 11/12		-3.7	
Q1 12/13		-5.2	
Q2 12/13		-3.5	

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Market Cap: £228m
12m range 87p 290p

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Q4 12/13	+0.4	
FY 12/13	-2.4	
Q1 13/14	+1.4	
H1 13/14	+1.4	+0.4
Q3 13/14	+1.4	
FY 13/14	+1.3	
10w 14/15	+0.8	
H1 14/15	+0.5	

Source: Company Reports

Trading:

- The group says revenues in its H1 were £221.7m (2014: £233.5m). EBITDA was £105m v £108m, PBT came in at £30.4m (2014: £49.7m) and EPS was 14.op

Strategy, development, restructuring etc.:

- The group says its 'disposal programme [is] ahead of target with £57m of proceeds; full year guidance revised up to £80m'
- It points to its successful capital restructuring & reminds observers that it has cut debt by £0.6bn (debt now 7.3x EBITDA v 9.5x in August 2014)
- The group has reduced debt by £53m since the 8 October capital restructuring and says it is 'on track to meet £200m deleveraging target over next three years'

Conclusion:

- Punch remains the only company to our knowledge to have unpicked a complicated securitisation in the aftermath of the 2008-09 credit crunch
- Unfortunately, having just done so last autumn, the group, along with the industry in which it operates, was hit by the (as yet uncertain) MRO legislation
- Punch says 'actions have already begun to provide a more flexible business model in light of the anticipated introduction of the Market Rent Only option (MRO) in 2016'
- These actions, which it would be impolite to outline ahead of the arrival of new CEO Duncan Garood in June, are likely to include managing units, potentially franchising some and generally taking more active control over some assets
- Interestingly Enterprise Inns will outline its strategy with its H1 numbers on 12 May
- Stephen Billingham, Executive Chairman of Punch says 'we have delivered profits for the half year in line with our expectations and are on track to meet full year underlying EBITDA guidance of between £193 million and £200 million.'
- He adds 'group debt has materially reduced following the completion of the capital restructuring on 8 October 2014 and we have delivered strong cash flow generation during the first half. All of our debt is long-term securitised debt with no short-term bank debt and we have a clear path to further debt reduction.'
- He concludes 'I am delighted that Duncan Garrood will be joining Punch as Chief Executive Officer in June. Duncan is joining an experienced management team and Duncan's retail and franchise background will be of great value to Punch's future development.'

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Langton Comment: At the time of the group's FY numbers back on 12 Nov 2014. Chairman Stephen Billingham said 'we can now focus on improving our business through investment in our pubs, attracting the best partners to work with us and providing industry leading support to our partners to launch and develop their pub businesses.'

Unfortunately, the above statement was followed closely by news that a Market Rent Option was to be given to tenants and, though the details as to any potential carve out of pubs where there has been 'substantial investment' remain to be worked out, the uncertainty caused by this development has weighed heavily on the group's shares since the company last reported.

Punch's restructuring straddles two financial periods meaning that there will be no shortage of exceptional items in FY15's numbers but, on looking through this at underlying trading, observers should be able to discern value.

Whilst trading is in line with expectations and the group remains in positive territory, the overall numbers remain in something of a flux. We are of the view that around 21p (1.05p in the old form) should be achievable and, though there may be further forecast changes as the impact of the MRO becomes clearer, this represents something upon which the company should be able to build.

Uncertainty clearly remains but we would suggest that there is material upside potential within Punch. We have commented before that profit is the difference between two large numbers, EBITDA and interest paid and it, profit that is, could move markedly higher.

Similarly, re the balance sheet, shareholders' funds are the difference between freeholds and debt. A bout of inflation could move this number materially and, whilst that is not particularly likely, the group should be able to de-gear under its own steam.

Whilst many will be put off by the lack of clarity with regard to the MRO, Punch's shares will comprise a large part of the small cap index and, as such, the upside represents a risk to those non-holders who are benchmarked against it. We would suggest that the shares are worth a look.

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