Langton Capital Limited

25 Feb 2014

RESTAURANT GROUP (RTN): 638p
FY to 29 Dec 2013 – Analysts' Meeting

***Comment:** Good co. but investors should consider switching into the larger, cheaper, faster growing JD Wetherspoon…*

Year to end-Dec	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2012 (A)	64.6	24.1	27.1	11.8	1.8
2013 (E)	72.7	28.0	23.4	14.0	2.1
2014 (E)	80.3	30.3	21.6	14.9	2.3
2015 (E)	90.1	33.9	19.3	16.5	2.5

Source: *Company & Broker Estimates*

FY to 29 Dec 2013 – Analysts' Meeting:

Following the announcement of its results for the full year to 29 December this morning, Restaurant Group hosted a meeting for analysts and our comments are set out below:

- Restaurant Group remarked that these were good figures across all of its businesses and pointed out that its dividend, over the period of the recession and its aftermath, had risen four-fold
- It says that some 1% fewer sales were discounted but we weren't given an absolute proportion
- Prices 'may rise by 1.5% to 2% in Q3
- The LfL outlook is good as Q1 provided the toughest comps and the group is now two thirds of the way through
- The brands:
    - Frankie & Bennie moves from strength to strength. The estate comprises 232 units and could move to 350 'or even 400' sites; payback on leasehold units at the better sites is now 2.5 years or less and the group 'is an anchor tenant'
    - Chiquitos has 73 sites and 'could grow to more than 100'
    - Coast to Coast is up to 10 at year end and 11 now and 'could move to more than 100'
    - Garfunkels is at 16 sites and increased sales by 19% on a LfL basis during 2013 courtesy of good trading and the London effect; the estate 'could double'

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Market Cap: £1.31bn
12m range 390p 665p

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- The group has 49 pubs, 28 of which are freehold. It opened four sites last year and could do five or six this year; this will be steadier growth but could move 'to 100 to 200 units'
- Concessions performed well. The group has 60 (54 at airports) and will benefit as passenger numbers (2013: 224m) move back towards the 2007 peak of 241m

- The numbers (information additional to that on earlier email(s)::
  - EPS growth was slightly flattered by a move in the tax charge from 25% to 22.7%
  - Cost rises 'have abated'; F&B rose by c3% in 2013 but could be 2% this year. Labour costs depend on NMW but 'modest above inflation rises could be dealt with'
  - Utility costs should increase by 6% to 7% and rents are up by 8% to 10% over the typical five year lease
  - The group pays £61m in rent, a figure that dwarfs the £2.2m paid in interest; fixed cost cover nonetheless increased slightly from 2.6x to 2.7x

- Group's conclusion:
  - The group concluded that 'things are getting brighter'; the economy is picking up, employment levels are high, NMW may rise, etc.
  - RTN believes that independent operators may lose out as major landlords move to branded operators as their first choice for an F&B solution
  - The pipeline of openings means the c40 units should be nailed down for each of the next three years; Nandos is competing for sites but M&B has backed off as have Tragus and Gondola

Langton Comment – RTN is a good company but consider switching to JD Wetherspoon:

Restaurant Group is a good company. It passes that test with flying colours but it may not be cheap. It should, on the balance of probabilities, deliver on its forecasts but there is little room for slippage given the group's PER.

The group's shares trade on a multiple of around 21.6x this year's earnings, falling to perhaps 19.3x 2015 and should yield around 2.3% this year and perhaps 2.5% next.

Certainly RTN can point to its strong cash flow of c£80m. Some third will be paid out as dividend and the balance will go towards opening c40 units per annum without debt increasing.

And that's wonderful but you could say the same thing about Wetherspoon. And that group trades on a caledarised PER for 2014 of around 16.5x whilst having many of the same characteristics as RTN.

Indeed JDW has twice as many units as does RTN. They tend to be larger in terms of revenue and group sales at JDW (caledarised for 2013) were £1.34bn against the £0.58bn for that year just reported by RTN.

Margins are admittedly lower but JDW is, if anything, a more widely recognised brand. It has a functioning estate and growth prospects in the nation's city centres, in its suburbs, on the nation's motorways and now in Ireland and may, at these relative prices, offer a better option to would be shareholders than does Restaurant Group.

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