Langton Capital Limited

11 Feb 2014

THOMAS COOK (TCG): 181.7p
Q2 & H1 Trading Update

Group reports 'encouraging trading' and 'continued delivery of strategy…'

Year to end-Sep	PBT (£m)	EPS (p)	PER (x)	DPS (p)	Yield (%)
2013 (A)	NA	5.0	NA	Nil	Nil
2014 (E)	199.6	11.2	16.2	Nil	Nil
2015 (E)	311.0	16.9	10.8	2.75	1.5

Source: *Company & Broker Estimates*

Q2 and H1 Trading Update to end-March 2014:

Thomas Cook has this morning updated on trading for the three month period to end-March and our comments are set out below:

Winter 2013/14:

- Re Winter, the group says that 'despite significant market disruption, trading has been satisfactory for the Winter season, which is 93% sold and in line with the booking pattern at the same time last year. '
- Egypt has hit bookings but 'this was successfully mitigated through the more integrated management processes and improved customer service that we introduced last year.'
- Excluding Egypt, the group achieved higher average selling prices 'and bookings and gross margin has been positively impacted by improved yield management and cost efficiencies.'
- In the UK, bookings are up 2% (ex. Egypt) but pricing was down due to more one-week holidays. This was mitigated by cost cutting
- Selling prices are up 4% on the continent and bookings are 5% higher in Northern Europe

Summer 2014:

- Summer is 50% sold (up 1% on last year) and overall bookings are up by 2%
- The group says the 'trading performance across the Group has shown an improving trend since we reported our first quarter results against a strong prior year comparative at this stage in the booking cycle'

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Market Cap: £2.6bn
12m range 78p 186p

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- Selling prices are down a little but margins are higher for summer and the group says this is 'consistent with our profitable growth strategy'
- UK bookings are up 3% with capacity down 1%. Average selling prices are 2% lower 'mainly to product mix and a higher proportion of shorter duration holidays'
- Continental Europe 'continues to trade well'; average selling prices are up 1% and volumes are also up 1%. Germany is 4% better sold than at this stage last year
- Northern Europe is up 2% in bookings but selling prices are down 2%. Margins should be up

Outlook:

- The group says 'going forward, our focus remains on implementing our strategy for sustainable profitable growth and delivering on our targets.'
- It says 'bookings at our higher margin concept hotels are up 49% compared with the same time last year and our hotel development programme remains well on track.'
- The group goes on to say 'we also continue to make significant progress transforming Thomas Cook, further professionalising our business and delivering additional cost out and profit improvement benefits.'

Langton Comment: Thomas Cook has survived its near-death experience and, whilst it has not yet prospered, it should be in a position to do so in FY14 and beyond.

That said, today's statement does have a few cautious strands running through it and the remainder of the group's recovery will be hard-fought.

The two large cost-out programmes have not been commented upon (there is a conference call at 9.30am) and, in such a large and diverse company, it should perhaps be no surprise that there are some areas causing a little concern, others that are OK and some that are performing well.

Profits will not normalise until FY16 at the earliest, when observers are pencilling in 20p and more in earnings. The group's shares, whilst they have performed extremely strongly over the last 18 months and a degree of profit taking may be expected.

Summer 14 looks OK but the heavier mix of low-value holidays will have to be recouped later in the season. Forecasts remain in flux with some brokers preferring to suggest a level of 'recovery' earnings of 20p and more from FY16 with some more modest 'recovery' growth thereafter. Additional growth may be available but the low-hanging fruit is now less easily available.

TUI Travel, with a minimal amount of bid-speculation, trades at 13.8x FY14 estimates and v12.5x FY15. Discounting the next year at perhaps 15%, gives a suitable PER for FY16 earnings of around 10.8x and attaching this multiple to our hazy 'forecast' of 20p gives 217p.

Our thinking could be way off beam but this represents a relatively modest 19% premium to today's share price. There is no dividend (TUI pays around 3.3% this year and 3.6% next) and, stripping this out would reduce the premium further suggesting that the massive gains of 2012 and 2013 may have run their course.

As we have mentioned, there are more caveats re the above than you could shake a stick at. Thomas Cook may perform better (or worse) than TUI. TUI itself could be too cheap. The 20p estimate could be way off the mark, it could be achieved a year early (or late, or never) and the discount rate of 15% could be a nonsense.

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No-one said it would be easy but, with the above in mind, we'd conclude in the absence of evidence to the contrary, that TCG's shares offer fair value (provided a dividend can be seen on or only slightly over the horizon) and, for those who have been on board since mid-2012, it may seem sensible to take some further profits.

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