

Cavendish

QUARTERLY CONSUMER NOTE – AN M&A PERSPECTIVE

Q4 2023

Sub-Sector in Focus: Hospitality



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About Cavendish



Henry Wells,
HEAD OF CONSUMER

"Welcome to the Cavendish Quarterly Consumer Note, where we give an M&A perspective on a number of key themes impacting operators and investors in the sector. At the macro level, the focus remains around inflation, interest rates and consumer confidence and how this impacts the operators and their margin and how it impacts investors and their investment appetite. In each of these publications, we take a more detailed look at a particular sub-sector; this quarter we look at Hospitality and next quarter we will be looking at Travel. Our focus in hospitality remains around the challenges of LFL trading and the disparity around valuations of freehold and leasehold estates.

We hope you find this interesting and where you have any questions, or you would like to discuss anything in this document, please contact me or any member of the Cavendish team (contact details on the back page)."

Henry Wells

1. CONSUMER: KEY SECTOR THEMES

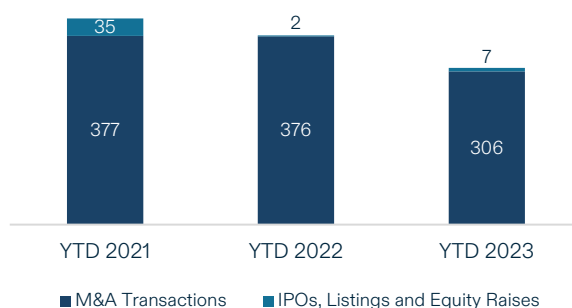
The Consumer sector has encountered various headwinds in 2023, subduing M&A activity. These headwinds are now diminishing and there are emerging indications of positive momentum returning to the sector.

Current Consumer Sector Drivers

- **Inflation** – CPIH¹ inflation appears to have peaked, and has continued to fall from ~9% to below 5% in 2023 so far (see p5 Figure 1). This trend should enable interest rates to follow over time but we are still a long way from the government's 2% target.
- **Interest rates** – The MPC's decision to freeze interest rates at 5.25% in Sep-23 (and again in Nov-23), after 14 consecutive rises, raises hope that we have reached the summit. But the question remains as to the gradient of the descent. The BoE has now suggested it may be willing to consider interest rate cuts by May-24.
- **Consumer confidence** – GfK data (see p5 Figure 2) indicates a high degree of volatility in consumer confidence over the past four months after a steady improvement over the first six months of the year. Consumer confidence now stands at -30 (at Oct-23), well ahead of Oct-22 levels of -47.
- **Job security** – YouGov's consumer confidence index in job security for the next 12 months has dropped to 119 in Oct-23, after rising over summer to a peak of 124 in Aug-23 (see p5 Figure 3).
- **Consumer spending** – Overall consumer card spending in the past three months (to Oct-23) has risen by ~3%² according to Barclays data. Hospitality & leisure, digital content & subscription and travel remain the key focus of consumer spending, while fuel, household items and clothing have seen sharp reductions in share of wallets (see p5 Figure 4).

UK Consumer M&A and IPO Market

- **Private Markets** – There have been 275 consumer M&A transactions in 2023 thus far³, 19% fewer than the respective periods in both 2022 and 2021.
- **Public Markets** – Public markets have been relatively quiet since Q4 2021, but have begun to show "signs of thawing" with IPO activity starting to return to global public markets in Q3 and Q4 of 2023.
- The transaction pipeline remains strong across the Consumer sector. Several live transactions continue, such as Apollo's proposed acquisition of TRG, and Stonegate's disposal of 1,000 of its pubs. Processes are, however, taking longer to complete and the "bar" has been raised both in terms of the quality of opportunities acquirers will pursue and their associated DD requirements.



Market Tailwinds

Falling
Inflation
rates

Rising real
incomes

Consumer
confidence
improving

Autumn
Statement:
fiscal easing

Market Headwinds

Rising
unemployment

Longer term
impact of
higher interest
rates

Sluggish
economic
growth

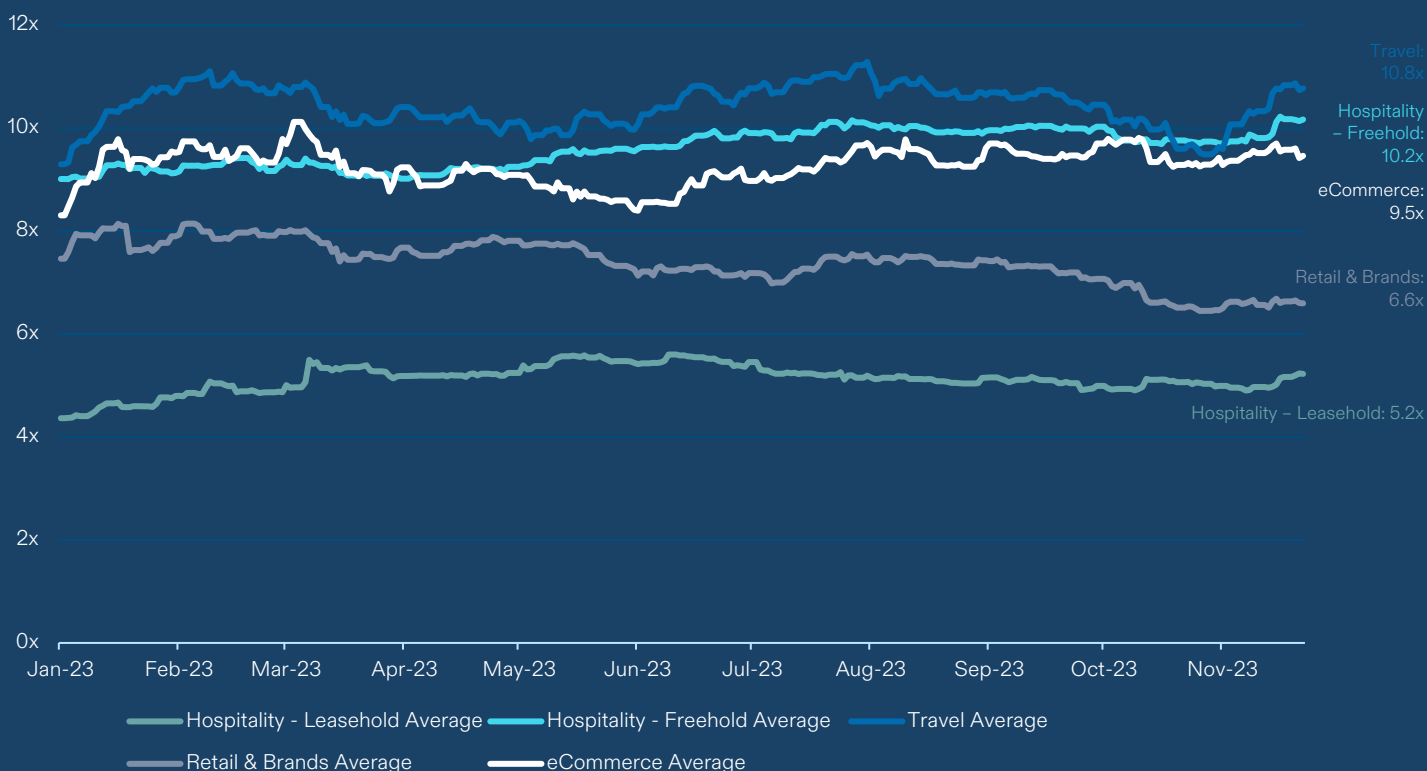
Autumn
Statement:
hesitancy to
feed growth

1. CONSUMER: KEY SECTOR THEMES

Listed valuations – sub-sector trends over YTD 2023.

LISTED VALUATIONS –

Year to Date (EV / EBITDA)



Our Commentary

Listed valuation by sub-sector

- **Hospitality – Leasehold** – Substantial range of valuations across the cohort, with an average of 5.2x Dec-22 EBITDA. Operators have been heavily impacted by food/energy inflation, lease payments and interest rates, and valuations are reflective of these challenges.
- **Hospitality – Freehold** – Valuation has remained resilient throughout the year, now trading at an average of 10.2x Dec-22 EBITDA. The asset-backed nature of these businesses has historically propped up valuations in times of macroeconomic uncertainty.
- **Travel** – 2023 has been a year of positive news-flow in the sector. Strong trading has continued through the year (for most) and that has been reflected in the strengthening valuations over the year. This has been (arguably) the sector's first "normal" year post-Covid and momentum into 2024 "peaks" is now the key for the sector.
- **Retail & Brands** – Several retailers have been affected by the cost of living crisis and curtailed consumer spending. Valuations have fallen from ~8x to below 7x Dec-23 EBITDA over the course of the year.
- **eCommerce** – Impressive performance from the cohort as a whole, currently trading at ~9.3x Dec-23 EBITDA. However, there is significant disparity within the cohort with the likes of musicMagpie trading at ~4.4x while the market values Marks Electrical at ~11.6x.

Source: Capital IQ

Hospitality - Leasehold cohort includes: Loungers, Brighton Pier Group, Revolution Bars, The Restaurant Group, Hostmore and Nightcap

Hospitality - Freehold cohort includes: Marston's, Mitchells & Butlers, Fuller's, Young's, Shepherd Neame. City Pub Group is excluded.

Travel cohort includes: Saga, Norwegian Cruise Line, Royal Caribbean Cruises, Carnival, Tripadvisor, Webjet, Booking, Expedia, eDreams, On the Beach, Hostelworld

Retail & Brands cohort includes: Frasers, Burberry, Dr. Martens, Mulberry, N Brown, Next, Superdry

eCommerce cohort includes: AO World, Marks Electrical, Moonpig, musicMagpie, Science in Sport, THG, CMO, ASOS, boohoo

EBITDA for Hospitality is presented on a Pre-IFRS basis.

1. CONSUMER: KEY SECTOR THEMES

Inflation, consumer confidence and consumer spending data.

Figure 1: Inflation - Consumer Prices Index including owner occupiers' housing costs

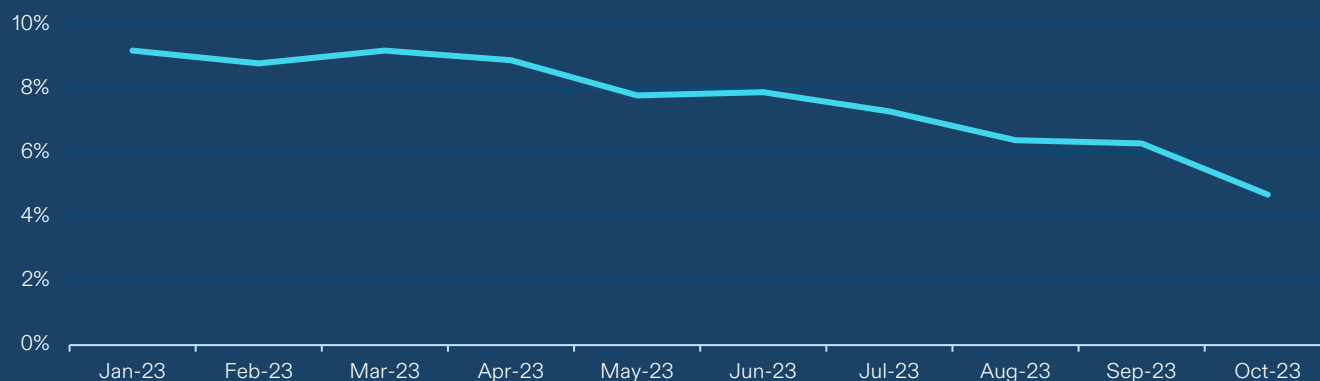


Figure 2: GfK Consumer Confidence

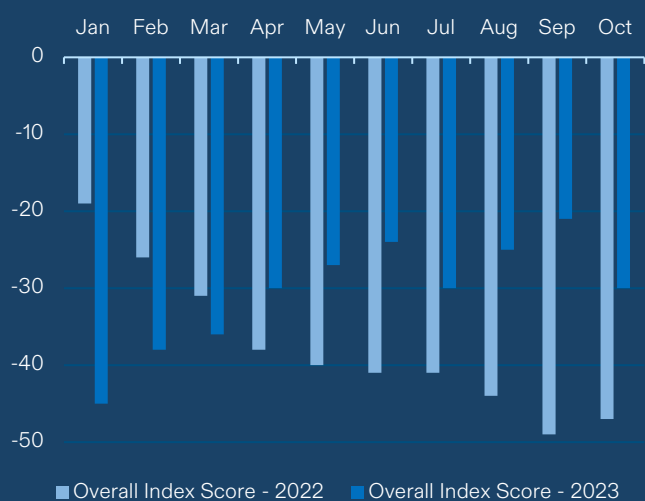


Figure 3: YouGov Job Security

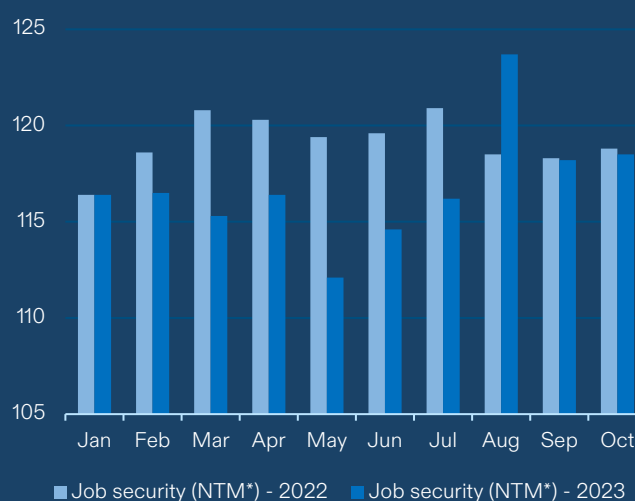


Figure 4: Barclays Consumer Data



2. SUB-SECTOR IN FOCUS: HOSPITALITY

Key themes we are seeing throughout the Hospitality sector.

Poor weather impacting demand over summer

Certain operators (primarily pubs) were hit by subdued summer demand due to the cooler than usual temperatures experienced over the summer. However, restaurant operators performed well over this period as patrons spent less time in pub gardens.

Food and beverage inflation has peaked

After 16 consecutive months of food (and non-alcoholic beverage) inflation topping 10%, we have now seen 7 months of falling inflation. Oct-23 data shows F&B inflation at 10.1%, falling from a peak 19.2% in Mar-23. While this is a positive trend, there is still some way to go until inflation returns to a manageable level for operators.

Energy inflation

We estimate that just about every operator has now felt the brunt of energy price increases with operators falling off fixed price energy contracts over the past 2 years. As with food inflation, operators have felt the worst of it, with energy price inflation now more stable.

Pub closures

Capacity continues to come out of the market, with 383 pub closures recorded in the first half of 2023, almost reaching the annual total for 2022 of 386. Analysts suggest that the “survival of the fittest” period should level out by 2024, with some expecting site number expansion to begin again next year.

The Autumn Statement

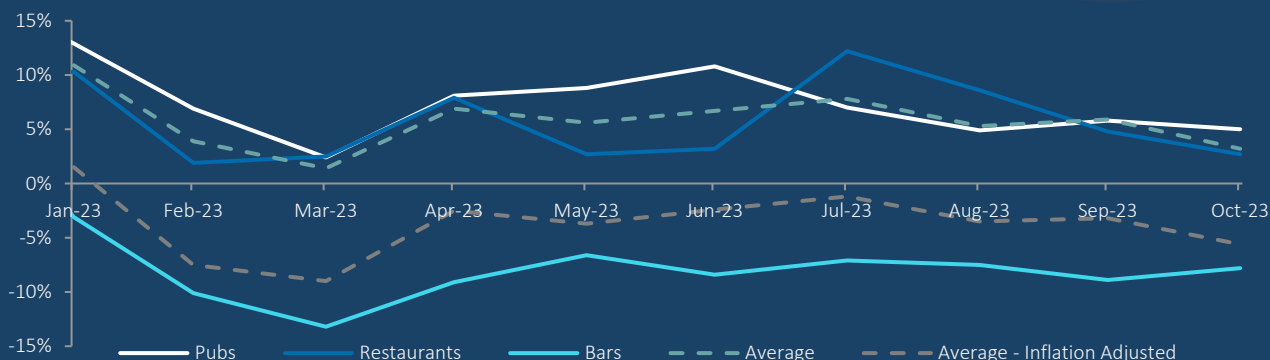
Jeremy Hunt's Autumn Statement confirmed business rates relief for retail, hospitality and leisure operators would be extended and the small business rates multiplier would be frozen, which will be welcomed by the smaller operators in the sector. However, the standard business rates multiplier is to increase next year in-line with inflation resulting in an increase in rates for the medium and larger operators. The decision to freeze alcohol duty is welcome news for all operators, but increases to NLW will impact cost lines.

LFLs across the sector

LFLs for all pubs, restaurants and bars across the UK have had a varied 2023 for the year to date, per the CGA RSM Hospitality Business Tracker:

- **Pubs** (+7.5% YTD Av.) – the strongest performing sub-set of the sector. Pub operators' dynamism in times of volatility has contributed to its outperformance of the rest of the market (and not for the first time). Operators such as Revolution Bars Group's Peach Pubs and Oakman Group have continued to post LFLs of +14.1% and +8.0%, respectively, for financial years to 2023.
- **Restaurants** (+6.0% YTD Av.) – here at Cavendish, we have seen somewhat of a mixed bag in performance of restaurants. Strong performers such as Loungers (+7.7% L6M Oct-23) and TRG's Wagamama (+9.0% L6M Jul-23) have been offset by struggling groups such as TRG's former Leisure division (-1% L6M Jul-23) – now part of The Big Table. Cool temperatures through summer resulted in restaurants outperforming pubs as patrons spent less time in pub gardens.
- **Bars** (-8.2% YTD Av.) – have struggled in 2023. Late night drinking has taken a back seat since the summer of 2022. Revolution Bars Group's latest trading data showed YTD FY24 LFL sales at -5.5%, though this has improved to -3.5% in the L3W.

The graph below sets out the CGA RSM Hospitality Business Tracker, but when we adjust for inflation, LFL profiles are seen in a different light.



2. SUB-SECTOR IN FOCUS: HOSPITALITY

The disparity between freehold and leasehold valuations has increased over the year to date to >5x.

Our Commentary

Freehold Groups

The valuation of freehold pub groups remains resilient (at an average of 10.2x Dec-22 EBITDA). Valuations have increased slightly from ~9x to ~10x throughout 2023, despite the continuing impact of the global macro-economic environment and cost of living crisis. It should be noted that M&B and Young's freehold estates are currently trading below even Apollo's offer for TRG.

Young's offer for City PubCo represents a Dec-23 EBITDA multiple of 15.7x (or 8.9x after £8m of synergies). The market appears to have reacted positively, with Young's share price having edged up in the days after the announcement.

Leasehold Groups

There is more volatility in the valuations of leasehold (than freehold groups) with an average of 5.2x Dec-22 EBITDA.

Apollo's 65p per share recommended cash offer for TRG has resulted in its valuation jumping nearly two turns (1.7x) from 6.7x to 8.4x since the date of the offer. The view of the Cavendish Research Analysts is that the offer of 9.0x undervalues the business (with a 75p target price).

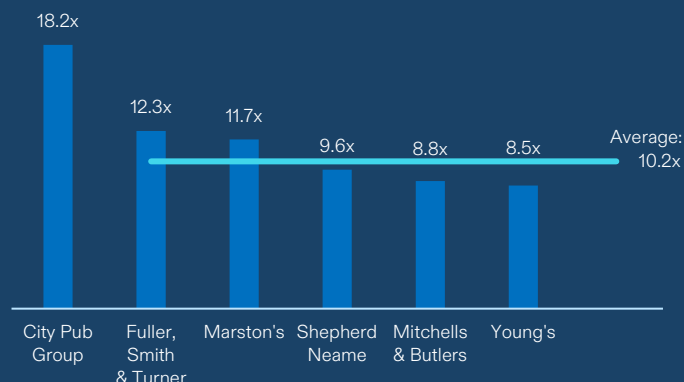
This, in addition to Fulham Shore's acquisition by Toridol and Capdesia in Apr-23, for a reported EV/EBITDA multiple of 9.7x, indicates that the public markets are not currently valuing the listed operators and as a result there could be further interest from trade and private equity buyers in these businesses.

Transactions

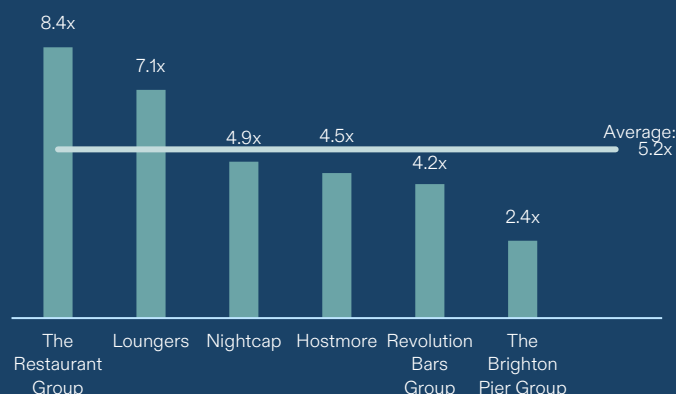
2023 has continued to see M&A activity in Hospitality.

	Target	Buyer
Nov-23	City Pub Company (offer)	Young's
Oct-23	D&D London	Breal & Calverton
Oct-23	TRG (offer)	Apollo
Sep-23	Big Mamma Group	McWin
Sep-23	TRG Leisure Div.	Big Table
Aug-23	South Coast Foods	McDonald's
Jul-23	Popeyes UK	TDR Capital
Jun-23	Dirty Martini	Nightcap
Jun-23	Boojum	Azzurri
Jun-23	Snowfox	Zensho
Apr-23	Ego Restaurants	Mitchells & Butlers
Apr-23	Hakkasan	Mohari Hospitality
Apr-23	Fulham Shore	Toridol / Capdesia
Feb-23	Mowgli Street Food	TriSpan

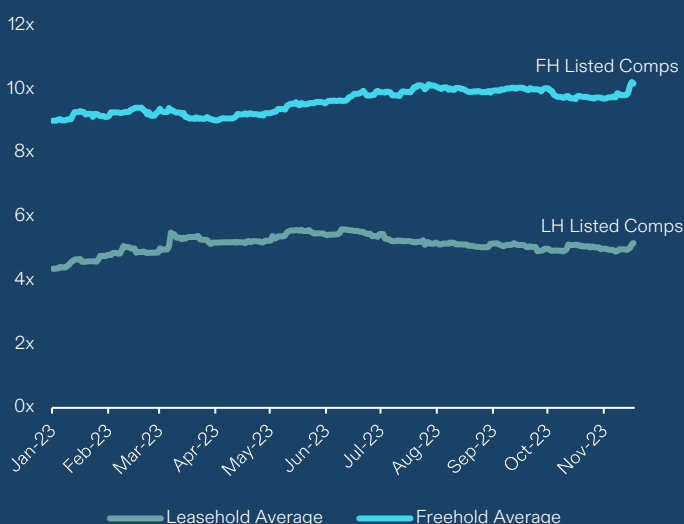
LISTED VALUATIONS: FREEHOLD GROUPS
(EV / Dec-22 EBITDA)



LISTED VALUATIONS: LEASEHOLD GROUPS
(EV / Dec-22 EBITDA)



LISTED VALUATIONS -
Year to Date (EV / Dec-22 EBITDA)



3. ABOUT CAVENDISH

A full-service investment bank and trusted advisor to ambitious growth companies and their investors

Cavendish is a UK champion for ambitious growth and investment companies. The Group is trusted by public and private companies, operating across industry sectors, to deliver expert services in equity capital markets, M&A, debt advisory and growth capital. Cavendish has offices in London and Edinburgh and has a global reach through its membership of Oaklins.

Cavendish is uniquely placed to advise on the various tracks for growth, investment, IPO and exit options.

Cavendish

Investment Banking

- Corporate Finance
- Capital Markets
- M&A Advisory
- Debt Advisory

150+ investment banking professionals

Advised on
c. **£1.0bn** of transactions in
the last 6 months

40+ Deals completed in
the last 18 months

Equities

- Institutional Sales
- Research
- Trading

222 listed clients

#1 NOMAD and Broker on AIM

£14bn+ raised since 2015

21 research analysts covering
c.200 stocks

Alternative Financing

- Private Equity
- VC Funding
- Private Growth Capital

180+ relationships with global
Private Equity and VC funds

40% of deals transacted
with Private Equity

£1.1bn of debt financing
raised since 2017

Cross-border M&A

- International reach through our
membership of Oaklins

Global reach in **45** countries




15 vertical markets with deep
industry expertise

368 deals closed worth
US\$25.1bn
in 2022 across the network



3. ABOUT CAVENDISH

The Cavendish team have a wealth of experience across the Consumer sector.



Selected Hospitality Credentials

 <p>has been acquired by</p> <p>REVOLUTION BARS GROUP</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>NIGHTCAP</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>The Restaurant Group plc</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>REVOLUTION BARS GROUP</p> <p>Nominated Adviser and Broker</p> <p>NOMAD AND BROKER</p> <p>Consumer</p>
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Selected Travel, Leisure & Hospitality Credentials

 <p>has been acquired by</p> <p>EQUISTONE</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>LDC</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>Scott Dunn</p> <p>has been acquired by</p> <p>inflexion</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>Brooklyn Travel</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>
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Selected Retail & Brands Credentials

 <p>has been acquired by</p> <p>EOT</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>Future Business Partnership</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>WILLIAM MORRIS LONDON</p> <p>has been acquired by</p> <p>DESIGN EYEWEAR GROUP</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>Ro&Zo</p> <p>has been acquired by</p> <p>Pembroke</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>
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Selected Consumer Goods & Services Credentials

 <p>has been acquired by</p> <p>epiris</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>neighborly</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has been acquired by</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>Brave Bison</p> <p>Nominated Adviser and Broker</p> <p>NOMAD AND BROKER</p> <p>Consumer</p>
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Selected Food & Beverage Credentials

 <p>has been acquired by</p> <p>Flaviar</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	 <p>has merged with</p> <p>WADDESDON</p> <p>M&A SELL-SIDE</p> <p>Consumer</p>	<p>ParsleyBox</p> <p>£17m Placing and admission to AIM</p> <p>NOMAD AND BROKER</p> <p>Consumer</p>	 <p>secured £3.5m of growth capital from</p> <p>mobeus</p> <p>GROWTH CAPITAL</p> <p>Consumer</p>
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