Mitchells and Butlers PLC Full Year

Wednesday, 20 November 2019

Tim Jones : Good morning. Thank you for joining us this morning. As always, I'd like to go through the financial results then I'll hand over to Phil. So, let's make a start. Overall, we think this is a really encouraging set of results, building on the progress we've made over the last couple of years. We've had strong sales growth that has been consistently ahead of the market and we're now starting to drive a growth in profits for the first time since the living wage was introduced in 2016. We've been able to do that this year also at a higher percentage margin.

Looking forward, I think the environment still remains tough and it still remains uncertain. We still have cost headwinds in particular and I'll talk a little bit about those. But most importantly, we believe we're really well-placed now to face that challenge. We're getting a lot of the benefits of our Ignite 2 programme. It's starting to have a tangible difference on our income statement, and early in the New Year we're going to look at launching a whole new set of initiatives under Ignite 3. So, we're confident in our ability to maintain investment in what is a fantastic estate and deliver real equity value over the coming years.

Let me start with the income statement. Sales increased just under 4%. So, that's a marked acceleration on previous years. We geared that down well to £317 million EBIT, up 4.6% on the prior year, and that's as I said at 10 basis points richer margin. PBT grew by over 10%, so further benefiting from the progress we're making in paying down debt, and that begins to come through as the lower interest charge. So, overall, a good, solid year of organic growth.

In terms of sales, like for like sales for the full year were up 3.5%. Very well-balanced across food and drink. Well-balanced across our brand portfolio, with all of our individual brands being in like-for-like growth, and also with the uninvested estates being in like-for-like growth as well. Showing that it's not just capital that's driving this improvement. It's the whole raft of initiatives that we've got coming through the business.

Growth has essentially come from an increase in spend per item, especially price and premiumisation. But this year we've also seen a marked improvement in the volume trajectory, both with our food and our drink sales. The last seven weeks have been slightly softer, but most importantly we have continued to out-perform the market. So, it has been a difficult trading period, I think, for the sector. It has been cold, it has been very wet, as you all know, but we have maintained our margin of out-performance, which I think is important.

In terms of cost headwinds, costs have been a tough challenge last year and we expect them to remain so. We think we probably faced an inflationary headwind of about £64 million last year. We've managed to mitigate about £25 million of that directly. The main elements of course come through in wages, particularly in energy last year, and also transitionary increase has been in business rates.

If I look forward, I think the challenge before us is going to be of the same ilk. Perhaps slightly lighter in the year we're in now. We think energy might not be quite as stiff for us year on year, so maybe £60 to 65 million headwinds rather than the 65 we had last year. But essentially, the same challenge.

There are a number of moving parts, as you know, on our EBIT and I've set these out on this chart. Let's start with our capital plan. We have the benefit of the investments we made in the prior year. So, they're starting to annualise at a higher rate, so we get a return on that capital. Then we've managed to generate a positive impact on the P&L from the investments we made in the current year. It's the first time we've done that. It essentially means that those businesses traded so well that within the year, they've been able to fund back the opening costs and the closure periods they've had to bear with their remodel. So, we're really pleased with that result and that has been one of our Ignite workstream focuses.

Cost headwinds I've mentioned and the mitigation of £25 million against that. Then we have the benefit of our like -for-like trading, which is really all the other initiatives we're undertaking across the group. So, in aggregate, both halves growth, total EBIT £14 million higher at £317 million.

You'll know from our previous presentations that building a balanced business remains one of the three pillars of our strategy. Total capex in the year is £152 million. That's a little bit lower than expected on last year. Part of that reduction is a reduction in maintenance spends. Particularly IT spends. We had some large IT spends in the previous year. But also, we've had a lower average project cost. Just the type of project we've done has led to fewer conversions and more remodels, and a little bit of inevitable slippage.

But I think the main positives from our capital programme for me… There are two of them probably. First is, we actually completed more projects this year than we had in the previous year and we remain bang-on our six to seven year lifecycle, which is very important to us. Secondly, returns have shown a dramatic improvement. So, our blended four year return has gone up five percentage points, from 16% to 21%, and that is being led by the success of our current year remodels, which are hitting about a 34% EBITDA return in this year. So, a really, really strong performance on those.

Looking forward, I'd expect our total level of capex this year to drift up back to where it was. So, £170 possibly and at top end to £180 million. Our cashflow has remained strong. It benefited from the slightly lower capex, as I mentioned. We had a small amount of disposal proceeds and a little bit of inflow into working capital. That allowed us to pay down £124 million of net debt in the year, in addition to the £49 million we contributed into our pension fund. So, that's reduced gearing over the course of the year from 4 times down to 3.6 times, continued good progress in our de-levering .

In terms of our distribution policy and dividends, really nothing has changed. A year ago, I spoke about Brexit and political uncertainty, and economic uncertainty and the picture is really absolutely the same as I stand here today. So, we don't really see any change in that. Our priority will remain to meet our fixed charges in our cashflow, to maintain balance sheet investment across the estate and to keep a strong balance sheet going forwards. That will allow us to continue to reduce our gearing and create value.

As a reminder, the last three years we reduced our book gearing down from 4.3 times to 3.6 times. So, we're on good course. That progress will only accelerate because of how our securitisation is structured. So, we'll keep having £200 million of debt service, but more of that will be capital as we go forward. So, you'll see an acceleration in the deleveraging as we go forward and that will create more and more equity value within the business.

Before I hand over to Phil, I would like to say a few words on IFRS16. I'm sure you're all familiar with the standard now, so we won't make this a teach-in. But we're adopting it in this current year, FY 20. We'll use the modified retrospective method, so asset equals liability. There'll be no restatement of the comparatives and I'll remind you of the obvious point there are no cash implications for this. This is purely about accounting.

In terms of the individual impact on us, in our income statement we'll see a reduction in lease charges, which will lead to an increase in EBITDA of about £50 million. We'll have an increased depreciation charge, as we start to depreciate our right of use asset, which will mean that our operating profit will be about £6 million higher. However, we'll also have increased interest charges coming through from the lease liability, which will lead to a negative impact on PBT. When you wrap it all up, it's about £11 million, and that's 2.1p on EPS or 5%.

In terms of our balance sheet, we expect to establish a right of use asset of £500 million. We'll have a lease liability of £546 million. So, if you just do a simple book gearing net debt to EBITDA calculation, that would add 70 basis points to that going forward.

So, I'll hand back to Phil, but we believe this is a really strong set of results. Sales consistently ahead of the market now, really encouragingly we're starting to drive profit growth and doing that at a higher margin. We don't think things are going to get any easier in the environment going forward, but we do think we're really well-placed to meet that challenge or to continue to meet that challenge with the number of initiatives we've got. That will allow us to continue to create real equity value through deleveraging the group.

Phil Urban: Thanks, Tim. Good morning, ladies and gentlemen. Quite clearly, FY 19 was a good year for us, surpassing the expectations we had set ourselves 12 months earlier. I'm pleased to say we've now posted three halves on the trot of profit growth. Understandably, we're delighted with that momentum and being able to demonstrate that we can stabilise the profitability of the business with the next major milestone we've set for ourselves, having previously got the business back into sustained sales growth.

As Tim has outlined, I think the performance was very much driven by a strong sales performance at 3.5% like-for-like growth. Pleasingly, every single brand, I think Tim mentioned, posting positive like-for-likes. That's the first time that has happened for many years within the business, we believe.

I think it also demonstrates that our recovery is quite broad-based. It reflects all the progress on the numerous workstreams we've been working on, beginning to pay dividends as opposed to any one thing. Further evidence that it is the aggregate value of all the Ignite initiatives that drives the business forward. There isn't really a silver bullet.

I think equally pleasing is the fact that we've managed to grow our profit conversion. Despite the cost-increases, I think evidence again is the Ignite initiatives that are looking at efficiency beginning to bear fruit.

Importantly, we have remained consistently ahead of the market in terms of sales growth as the Peach Tracker demonstrates. To remind you, the tracker is a cohort of around 40 plus businesses and this graph reflects all of the contributors, as opposed to any self-selected cohorts. We've now tracked ahead of the market for over three years now, with only the odd weekly blip when a specific event either impacts us more or benefits us less than the competitors. So, one or two weeks over the World Cup, if you like. But other than that, we've consistently traded ahead of the market.

So, we're happy with the progress for sure. But of course, last year is history… We're now seven weeks into a new year and it is fair to say the new year has started a little softer. But given the poor weather, I think that's unsurprising. I think people will have seen that in October the industry sector was minus 0.6. We've remained in positive territory throughout and ahead of our competition. As you can see in the Peach Tracker here, we've remained consistently ahead up until last week. So, we think this is just a blip. We think underlying we are still in very good shape.

So, what I'd like to do over the next ten minutes is to update you on our current interpretation of the macro landscape in which we find ourselves trading in, share an update on our Ignite and capital programmes and then talk a little bit about our aspirations for the year ahead and beyond.

So, let's start with the macro landscape. With Brexit and the impending general election, I can only say that protracted periods of uncertainty are unhelpful to any business and of course we're not exempt from that. However, we have already taken as many precautions as we can regarding Brexit. We did that several months ago, such as securing more warehousing and working with our suppliers to guarantee supply in the eventuality of a hard Brexit. We've also done a lot of work on our own talent pipeline, which I'll talk about a little later.

So, we continue to take the pragmatic view that we'll press on with our plan to drive this business forward and then see how, if at all, those plans are affected once we have greater clarity about the macro environment.

In the meantime, I think rising costs such as employment rate, utilities etc, coupled with at best flat consumer confidence, continue to impact the sector. Total UK supply in June of last year dropped by 2.4%, with the restaurants taking the brunt with closures of 3.4% in the year. Now, whilst we also face those same macro factors, a reduction in supply can only help us over the medium-term and I'm sure that has probably already contributed to our performance.

Now, we remain convinced that having an 83% freehold estate and arguably the strongest line-up or stable brands in the sector, is a strengthening competitive advantage for us. Our leasehold and over leveraged competitors in the sector will continue to struggle due to rising rents or an inability to invest in their estates. We would anticipate further closures in the coming months.

As Tim has outlined, predictive cost increases this year are slightly lower than last, which of course is helpful. But we have to keep moving our top line if we're going to move the business forward.

That brings me nicely onto Ignite, which is our change programme. Now, for those of you who followed us, Ignite is one we kicked off in February 2016 and ran through to about February 2018. Ignite 2 has been underway now for just over 18 months. So, unsurprisingly, we're about to launch Ignite 3. I know not the most creative of titles, but seeing as the vocabulary is now firmly engrained in the business and even some of you guys have played it back to us, it seems sensible to stick with it.

We see Ignite as not about revolution. This is evolution. We call it, filling the hopper. Ensuring that we have a sufficient number of initiatives to work on, which coupled with a capital programme in aggregate means that we actually have more than enough to cover our cost increases and hence move our business forward. I'll update you more about the initiatives coming out of Ignite 3 at our Interims in May.

What I will do, however, is share little details on some of the things we've been working on that perhaps we haven't mentioned before. So, for example, we've had three separate workstreams over the last year, looking at underperforming parts of our business. Now, whilst you could argue that the day job of operations is to sort out underperformance, it is funny how bringing a fresh perspective and a greater profile to an issue can have a big effect.

We've had a team looking at the invested sites that haven't been meeting their appraisals, another team looking at sites with the biggest year on year declines, and a further team focusing on our onerous lease sites. Over and above the day job, the operators have had to develop refocused action plans on each of the sites that fall into one of those three categories. Then we've held a very structured review and visit cycle and we've been able to allocate resources to turn around each individual sites.

All three cohorts have been able to demonstrate real improvement in profit trajectory, with perhaps the trading improvement of over £1 million coming from the onerous lease cohort without any capital investment being the most impressive.

Another workstream that I think I have mentioned before is the menu engineering workstream. This team studied the performance of all our menus across the business and the levels of wastage that we receive. Sometimes, wastage was being caused by ingredients only appearing in one or two dishes on a menu. We call them orphan products. Or where supplier pack sizes were too big and were leading to ingredients coming out of date before we use them.

A year on, we've reengineered our dishes to remove those orphan products and we've worked with suppliers to get appropriate pack sizes. We estimate the annualised value of that work being about £5 million to our margin. So, big numbers.

In the digital world, we've made giant strides this year. Certainly, in our booking platforms, improving the user experience by crucially reducing the number of steps it takes from entering the site to being able to make a booking. Over the last 12 months, we've seen online bookings continue to grow by 25% and the conversion from first entering a page through to making a booking has increased from 10.1% to 11.4%. As the move to digital channels continues at pace, we see this progress as being critical and it also of course brings down our cost of customer acquisition.

We have numerous workstreams still live that are now impacting the business, but the exciting thing for me is that whilst we're pleased with the results we've had, we know they're far from being optimal. In several instances, we've yet to roll out the initiatives to all our businesses, or we have mixed level of user acceptance or ability. Which means there's further work to do to train-in change. We need to do that before we can reap the full reward. So, even before we do Ignite 3, we believe we still have plenty of work to do that should continue to move the business forward.

Whilst I'm keen to stress that the whole business now has momentum, I also recognise that the capital programme is now becoming the engine room that it should be for the business. Four years ago, the business was under-invested. Certainly, in the customer-facing areas. It was on an 11 to 12 year cycle of reinvestment. At the same time, when it was investing, we weren't spending enough to really make an impact on a site by site basis.

Over the last three and a half years, we've moved the business onto a six to seven year cycle of reinvestment and we make sure we spend the right amount on each site, including the externals and the toilets, which were areas that had perhaps been missed before.

In the first two years of the current approach, we've prioritised the brands that were giving us a bit of a headache at the time. Namely the Harvester Refresh programme and moving Crown Carvery and converting them into Stonehouse. Whilst the capital programme undoubtedly succeeded in stabilising those businesses, it meant that the headline return on investments was supressed.

Three years on, today, we have all our brands in like-for-like growth. It means the starting point is far stronger. We have proven investment formats for each of our brands and therefore we're now seeing a step change on our return on investments. The ROI from our FY 19 remodel programme, as Tim said, was 34.2%, the strongest the business has seen in many years. This bodes well for the future, because we're still only halfway through the programme to get the entire estate onto a six or seven year cycle, but I do believe we've now reached what I would call the tipping point.

At the same time, we've been innovating and looking at trialling new design templates in some of our businesses. This on the screen is project Mandarin in our premium country pub estate, where we have invested more heavily in the opulent design, which we believe re-establishes design leadership in that part of the market. It's quite critical in the gastro end.

We have a similar project going on in Vintage under our Very Vintage tag. Again, effectivelyc premiumising what is already a successful offer. Brown's is not a business we often talk about. Over the last two years, we've done a lot of work in the background around the menu and around that offer. But we now believe we have a winning design template, already successfully deployed in Edinburgh and Bath that can now step change the performance of that brand.

I think as mentioned at the Interims, we've also opened a new concept. The George in Harpenden, producing fresh food from an open kitchen in a premium environment, under the working title of Neighbourhood Pubs. We also opened our first Miller and Carter in Frankfurt, Germany. I haven't got a picture because it just looks like a Miller and Carter, surprisingly enough, and we're pleased to see that both it and the George at Harpenden are now producing over 30,000 a week from a standing start. It's a good start, but still too early to draw any conclusions.

So, Ignite and the capital programme continue to underpin all that we do, and drive progress under each of our three strategic priorities. Namely, building and now maintaining a balanced portfolio, which is about accelerating the most successful parts of our business, systematically upgrading our amenity and getting onto that six or seven year cycle of investment, and ensuring that each of the brand propositions remain grounded in deep customer insight.

Secondly, driving a commercial edge to the way we do business, putting the customer at the heart of all that we do and making sure we're really clear on how each pound of sales is converting down to bottom line profits, and finally driving an innovation agenda. Which is about making all the technology we have in the business really work for us. Sweating it if you like. Making digital marketing an engine room for the business and being willing to trial new products and new concept development. These priorities keep us focused and will remain a priority through the Ignite 3 programme.

One part of the business we haven't talked about much in the past is sustainability and the impact our business has on the environment around us. It's a responsibility we've always taken very seriously, but over the course of the last year we've developed a new strategic plan to further our progress in this area. The ambition of this plan is to increase the positive impact we have on people and communities, and to reduce any negative impact our operations have on the environment.

Now, we've developed the strategy to align with the UN sustainable development goals and have set ambitious targets in relation to greenhouse gas emissions, food waste, recycling and use of plastics, all of which we will now report on in our annual report each year.

Now, in a business of our scale, this sort of activity requires a governance process around it. Therefore, we've created a head of sustainability role and a board level subcommittee responsible for moving the business forwards. We have the ambition to genuinely become industry leading.

We've set-up four cross-functional working groups, that are already up-and-running. One focusing on product-sourcing, another on nutrition, one looking at community issues and another one natural resources. Now, our intention is not to create a separate function within the business but to imbed sustainable thinking through everything we do, such that it just become business as usual.

So, we continue to cover a hell of a lot of ground and of course success depends entirely on our people and how we perform as a team. I was therefore delighted to see our engagement scores reach record highs across the business. Amongst our managers, our front-line team and our support team alike, with overall engagement moving up from 78.9 to 81.3 last year.

Our apprenticeship schemes also continue to gather pace. In the year, 900 young people entered the business on an apprenticeship programme and 1,600 of our existing employees also signed-up to apprenticeship opportunities that were available to them.

We also expanded our successful chef academy, from two to seven locations nationwide. This year we had 280 chefs recruited onto the scheme, both internally and externally, and it's now one of the largest schemes in the UK.

Our apprenticeship programme gives us the opportunity to grow our own talent and provide progression opportunities for new and existing employees. We understand that the best way to retain people is to progress their careers. So, we do prioritise their progression through the organisation. In the year, 1,030 people took a step forward in their career with us, either through a promotion to a management role or through additional responsibility of a larger or more complex business.

Looking forward, we have the festive season on the horizon, which will dictate how strong our first quarter will be. As always, it's difficult to really be sure how strong Christmas is looking. So much depends on last-minute walk-ins and of course favourable weather. Fingers crossed for no snow. But we do track bookings obviously.

Now, this year, one of the Ignite workstreams rolled out some software called Collins to our non-food businesses, our non-restaurant businesses, which is effectively a sales tool that allows customers to book directly online with bespoke functions. As expected, bookings in these venues are way up on where they were last year, although we recognise that given the manual nature of last year's process, it's impossible to be 100% sure of last year's base. So, we'll just keep pressing on.

So, I guess we're pleased with the progress being drive by Ignite. We recognise we still have a lot of work to do before we can say we've optimised the rewards we're seeing from that programme, and it's encouraging that we have a lot to go out with Ignite 3 still to come, to fill the hopper in the new year.

We're therefore confident of being able to maintain the momentum we've built and whilst there are still macro factors to consider and the ongoing cost headwinds, we believe that we have the business moving in the right direction. This means as we continue to pay down our debt and our pension commitments, we should at the very least see this reflected in increasing shareholder value. Thank you for listening.