PureGym 2019 Results and Investor Presentation

Conference call 10am BST Wednesday 29 April 2020

Humphrey Cobbold (CEO)

All right. Good morning, everybody. It's Humphrey here. Thank you for joining us. We'll be using the presentation posted this morning on our website, dated 29th April and titled, "Investor Presentation." Let's start on page number three of that presentation.

It's an unusual world and a slightly unusual update and agenda today. Clearly, topmost of your mind, and of our minds, is the COVID-19 situation and our cash burn, and we'll be covering that. But we'll also be covering, off in summary form, 2019 results and the Fitness World acquisition. And having done so, we will summarize the group's financial position, both current liquidity and the year-end, pro forma group balance sheet position.

Finally, we thought we should look to the future, as well, to explain how we're addressing this and the challenge of reopening, even if we cannot predict exactly when or how that will happen. And we make no apologies for going above and beyond the minimum requirement for communicating with you, our bond investors, in this regard. You are collectively our single largest providers of capital, and at times like this, we believe you need and merit a much better than minimum necessary briefing and update.

So, turning on to page four. Put simply, there are five messages that we want you to take away from today. Firstly, we're making really good progress on our cash burn rate, and we've reached our target of £4.5 million per week. Secondly, we had an excellent year in 2019 and a really good start to 2020. Why is that important? It's important because we're headed into the pandemic from a position of real business strength.

Thirdly, despite the challenges we obviously face with respect to the Fitness World acquisition, the strategic logic for this acquisition remains intact for the long-term, and we'll help articulate that for you today. Fourth, we've got £150 million of available liquidity today and strong shareholder support, which puts us in a good position to go through the current difficult situation we find ourselves in. And finally, in terms of the immediate outlook, I want you to understand that we're very focused on being ready for the reopening phase, for adjusting our business model, and for reflating the business for the future.

So, let me move forward, and on to page six. Here, we summarise an update on the situation by country, as we did when we updated you back at the end of March. I'm not going to go through every line detail here, but I will pick out a couple of key highlights. First of all, looking across the whole piece, about 98 percent of the group staff are furloughed, and most of these are substantially supported by government schemes across Europe, for which we're very grateful.

Picking out a particular point in the UK, you've got negotiations with landlords -- I very much feel, a work in progress. Many of you will be aware of the new legislation being drafted by government to prevent use of aggressive tactics by landlords against tenants such as ourselves. This is important. In fact, it's very important, as it has been able to provide a much better context for discussion and negotiation. It's pretty hard to negotiate with a loaded pistol being held against your temple.

We're doing everything we can to reach sensible accommodations with our landlords, but I'd be misleading you if I suggested that this was an entirely easy process. In Denmark, government fixed cost support has been very helpful, and Swiss and Polish governments have also provided a degree of support, and on the legal support on rent, that has been very much appreciated.

Turning on to page number seven, and our weekly cash burn rate, the outcome of all of the work that we've been

doing is that we've made very good progress in reducing our forward cash burn rate to around 4.5 million for the expected 12-week closure period. This is at the bottom end of the forecast we gave you when we updated you on March 24th. Key elements to note are that the operational cash burn net of support from governments and landlords is expected to be around £3.5 million per week, across the entire group, and there is around £1 million per week, on average, of interest.

Our look forward P&L burn rate, which takes account of the current operations, as opposed to invoices coming into payment, represents a decline in about 65 percent of operational costs, which I think, overall, is a pretty good achievement to have made in such a short period of time. Given our liquidity of £150 million -- and more on this later from Alex -- this gives us an indicative survival period of over 30 weeks. This is still the same as it was four weeks ago, because of the cash revenue we have gained from Denmark and Switzerland over the last few weeks. So, puts us in a strong position to see through the weeks that lie ahead.

And we note, of course, that this survival period is on an indicative basis, as the burn rate is against a current, on-hand liquidity and does not include any potential equity injections or other forms of support that we might receive. We've highlighted, again, the key assumptions underpinning this at the bottom of the page. And those are, broadly speaking, the same as we laid out at the end of March. So, with that summary of our cash burn position, which I hope is somewhat reassuring, at least, let me hand you over to Alex.

Alex Wood (CFO)

Thank you Humphrey and good morning everyone. I'll start by echoing that, clearly, it is unusual reporting on our 2019 results in such an extreme context, with our entire estate temporarily closed due to COVID-19. However, on one level, I think the results and our track record are very relevant in the environment we now find ourselves. And why is that? Well, because at a time of uncertainty, it's very useful context to see that we've entered this crisis from a position of real strength, as Humphrey mentioned earlier.

It's clear from our results that our product and our proposition was resonating extremely well with members before closedown, and we believe this puts us in good stead for reopening. And our track record is a valid and very useful reference point for the future. So, let me begin on page nine, please, where I set out the headlines for our results for the UK business alone (so, this is prior to the acquisition of Fitness World, which we'll come on to later). And in terms of time period, this is for the 12 months ended 31st of December 2019.

As headlined in the introduction, 2019 was another really strong year for PureGym. I'm just going to pull out four points to highlight on this slide.

Firstly, we delivered a continued progression of growth in Average Revenue Per Member, per months, up 2.4%, versus the prior year, to £18.90, which, when coupled with our member growth, delivered an 11.6% growth in revenue year on year.

Secondly, our Run Rate Adjusted EBITDA reached £104.5 million, which exceeded the £100 million milestone, which was an achievement that we'd had in our sights for a while now, and I've mentioned to you a couple of times during recent investor updates.

Thirdly, 2019 was a really strong year from a property perspective. We opened 41 new organic gyms in the year, 19 in the fourth quarter alone, bringing the total number of gyms in our estate to 263.

And finally, in terms of cash and leverage, operating cash flow conversion was 87%, absolutely in line with the guidance that I gave previously. And given this strong cash conversion, leverage continued to decrease, closing the year at 3.6x, down from 3.8x at December 2018, and down from 4.6x when the bond was first raised, in early 2018.

So overall, it was another excellent year, with consistent and predictable results, and strong cash generation.

Moving now, onto slide 10. Normally, I would go into some more detail on each of the key elements of our performance, but given the COVID-19 context, we thought it more appropriate to stand back for a moment and set out our 2019 key performance metrics against our long-term historical track record. I'm not going to walk through the picture of our long-run performance in the UK in every detail because you all know how strong and consistent that has been at pretty much every level. But the key point I do want to highlight is that this is a very strong business, with a track record of delivering not just growth, but also, in parallel, cash generation and deleveraging. We've done this in the past, and we see no reason why this will not be the case in the future.

Over to the next slide now please, page 11, to touch on the outlook for the first quarter. We continued our strong momentum from 2019 into January and February, and performance in those months was really very strong, with all business units performing well ahead of budget, we peaked at over 1.9 million members across the group. We, therefore, entered the COVID-19 closedown in good health, with a very solid set of foundations. And as I said at the beginning of this section, this gives us confidence that the product and the proposition was resonating extremely well with members.

Looking to post-COVID closedown, the core strengths of the business remain extremely relevant. We believe that high quality, affordable fitness, with no contractual obligation will be doubly important in the recovery phase.

So, on that note, I shall now hand back to Humphrey, to talk through the Fitness World acquisition, which we completed on the 14th of January.

Humphrey Cobbold (CEO)

Thank you very much Alex. So, let's move on to page 12, and the discussion of the Fitness World acquisition. Pausing for a moment, the appendix -- in case you haven't spotted it -- provides you with a lot more detail than I'm going to talk through here; in terms of Fitness World -- the business we bought and everything within it, to the country level, and all that sort of thing. But let me focus today on answering the practical questions around what we bought, why we bought it, how we plan to drive value for the deal over the medium to longer term. And in the nearer term, where we expect to be on the other side of the current COVID situation.

So, turning on to page 13. We acquired a business generating £52 million of Run Rate Adjusted EBITDA on the 14th of January for £345 million. We believe this was a very good price, and we funded it with a bridging loan of €445 million. We bought, to be clear, a market-leading operator with a strong strategic fit with PureGym -- a very strong strategic fit, in fact. They've got a very similar model and approach to ours, so we all speak a very common language of fitness around our assets, even if we're all learning to master a little bit of Danish, Swiss, German, and Polish in the background.

So, the business had a clear number one position in Denmark. It's the number one position in the value segment in Switzerland, and also, has the benefit of an early stage position in Poland. And the end result of this was to move our group into a position as the number two operator in Europe. At the time of the deal, we had over 500 sites and 1.7 million members, which, as Alex said, actually peaked up at 1.9 million by the time we got into February and early March.

Page 14 summarises, in a little bit more detail, the two businesses -- PureGym and Fitness World -- and the combination. Again, I'll pick out a couple of key highlights -- The combination of overall scale, £447 million of revenue for the pro forma numbers for 2019, and diversification -- you know, two key markets and two further markets for growth and profitability, and £132 million of Adjusted EBITDA at the margin of close to 30%. And interestingly, of course, in ways that we could not for one moment have foreseen, diversification is paying off for us currently, as the situation with COVID-19 has played out somewhat differently in the different markets, in terms of how we've been able to gain revenue, and as I'll explain later, in terms of the likely reopening schedule for those markets in the future.

Turning on to page 15, I hope that a key question on your mind is, "How will we drive value for stakeholders from the deal when things return to some kind of normal?" With that question in mind, we see three key pillars making up the path to value creation. First, margin improvement. And here, we note that there are opportunities to deploy the product, revenue, and yield management techniques that support our industry-leading margins in the UK across the entire group. This is something that we think we do as well, if not better, than any other operator in the world, and we'll certainly be deploying that across the entire estate. There are opportunities to optimize the Danish estate and to focus some of the assets and activities there. And there is room to transfer value, from value-added sales and ancillary revenue approaches in Denmark across the whole business portfolio, to the UK, and to Switzerland, and beyond.

Second, there are benefits of diversification and scale, and these will include harnessing the different situations and different geographies, which is something we're effectively, actively doing at the moment; assuming cost synergies from procurement, overhead duplication, and harmonisation of our operating models; and crucially, leveraging scale in key areas, such as IT, digital strategy, and online investment. All these are areas that really do respond to scale investment from large players.

And finally, the acquisition brings into play two further markets which are currently, relatively speaking, underserved by budget fitness, and they provide us, in the medium to longer term, with opportunities for further growth. So overall, the Fitness World deal presents us with some practical challenges currently -- of course it does, we did not expect to have to be managing through this situation -- but both business teams are pulling their weight. In fact, they're pulling their weight exceptionally well and are working as well together as could possibly be expected in the difficult situation in which we find ourselves.

And then finally on Fitness World, let's just turn to page 16. We note, when you look globally at the budget fitness industry, the emergence of a global premiere league of large-scale budget gym-focused operators. We see Planet Fitness in the North American arena, Smart Fit in Latin America, and Basic Fit and PureGym in the European theater. These operators will, over time, benefit from classic advantages of scale and diversification. These are some of the most profound sources of competitive advantage that businesses can enjoy, and I think we can justifiably claim that PureGym group is now a part of this structure-advantaged group of industry leaders. And I think it's important to keep that perspective in mind. So, with that thought, let me pass it back to Alex to go through our financial position.

Alex Wood (CFO)

Thank you, Humphrey. I'm now going to talk through the combined group's liquidity and pro forma leverage status. Let's start with liquidity, please, by turning to page 18, if I could direct the audience there. As Humphrey headlined at the beginning, we still have £150 million of available net cash liquidity. And you'll note that the headline £150 million position is unchanged from when we updated you on the 24th of March.

And this is because we received £14 million of revenue from the Danish Fitness World business unit, in large part. And really, that's a function of the billing dynamics in that geography, which allowed us to be able to take a monthly direct debit payment in exchange for offering members future loyalty and other benefits. So, these revenues have largely offset our cash burn, and we've also actually been very effective at managing working capital during this period.

We've continued to take really decisive action to preserve liquidity, and we spoke at length about that last time. So, I'm not proposing to repeat the same points again, but for anyone who did miss it, full details of that presentation, a voice recording, and a transcript are all available on the website.

Suffice to say that we've temporarily postponed all capex activity, as well as all discretionary expenditure. We've drawn down fully on our revolving credit facility as a precaution and implemented a number of cost-saving and cash preservation initiatives across the group, including, as Humphrey mentioned, asking our landlords to stand shoulder to shoulder with us at this difficult time. Clearly, several of our mitigating activities are still in flight. And so, we continue to keep ourselves on our toes in this regard, and we'll keep you updated on progress at our next public

results announcement, which will be towards the end of May.

Now, looking at the combined group leverage position please, on page 19. As of the 31st of December 2019, the combined Senior Secured Net Leverage was 4.6x, on a pro forma basis. You'll note that this is an increase in leverage of about a tern, versus where we ended the year, prior to the transaction. This increase in leverage to fund the deal puts us back to the level it was when the bonds were originally issued, at the beginning of 2018.

As I said last time, we financed the transaction with a bridge loan from providers we know well. And just a reminder for anyone who wasn't on that call, there's no cliff edge to refinance this loan. If not refinanced by January 2021, it simply converts to a term loan, on terms that are broadly in-line with those of existing senior secured notes.

And finally, I just wanted to be really transparent about the future impact of COVID-19 on the group's leverage position. Clearly, at the time of doing the transaction, we were absolutely comfortable with returning to 4.6x leverage. This was within the historical parameters, and those parameters that we had set ourselves internally. However, the unexpected COVID closure will clearly increase our leverage further than this level as we utilise some of our revolving credit facility to fund cash burn during closure. In addition, I also wanted to flag that we've got approximately £25 million of liability building on the balance sheet as we're deferring working capital and other items into the second half of 2020 or beyond. As you'd expect, we're laser-focused on liquidity, cash burn, and reopening at the moment, and we'll provide more information on the latest leverage position as more of the moving parts begin to settle at our next update at the end of May.

And now to stakeholders, please, if I could direct everyone to page 20. We have excellent key stakeholder support during these challenging times. Clearly, from you, our bondholders, which we really appreciate, and also from our equity sponsors, Leonard Green & Partners.

Leonard Green are extremely pleased with the management team and have been very vocal to us of their appreciation of the speed of the actions that we've taken, our progress on cash burn mitigation, and very pleased with the liquidity position. They've been explicit with us that PureGym is an extremely important and successful investment for them, and they recognise our strong leadership position and actually, on many levels, the potential for us to gain significant market share in a recessionary environment post reopening. And it's also no secret that Leonard Green completed the raising of their next funds prior to COVID-19, and so have over $15 billion in available funds to fund both new investments and to support existing portfolio companies.

Another perspective that we thought was relevant for including is that of the credit rating agencies. So myself, Humphrey, and my finance colleagues invested quite a decent amount of time over the last six weeks or so with each of the teams at Moody's, Standard & Poor's, and Fitch through the crisis to keep them updated on our cash burn mitigation, our proactive management of the situation, our financial disciplines, and our modeling of the various close-down scenarios. And I'm really pleased that we've preserved our B rating.

I just wanted to recognise our appreciation of all the ongoing support we're received from these respective shareholder groups. It's hugely appreciated by us. And with that, I shall now pass back to Humphrey to talk about the future and our outlook. Thank you very much.

Humphrey Cobbold (CEO)

Thank you very much Alex, for that summary of our overall financial position. Let me now turn your attention to the final section but, I would argue, the most important part of this presentation. We can't do much, about the past, but we can have some influence over the future. And we thought we'd try and articulate a little bit about how we see that. Clearly, we're facing an uncertain future, and we need to take that into consideration. But it's not entirely unbounded, and indeed, management's role at a time like this is to think calmly and clearly about how we need to understand likely future conditions and how we should adjust and evolve our operating model and business approach. With this in mind, our clear focus across the whole group in the UK, Denmark, Switzerland, and Poland is to be ready

for a range of possible situations and timings and to be able to act in a considered manner and adapt to whatever happens.

The logical starting point for this is our members, so let's start with them on page 22. As you know, we froze membership of all our customers across the group as soon as we closed. Our focus since then, illustrated on this page, has been on engagement, trust and loyalty. And we've been working on the app and online engagement in the UK and Denmark especially. In the UK, we have had over 400,000 app users since the 20th of March and conducted over 1 million sessions. And our UK app is still number five Apple-ranked fitness center app. And that's not bad for a gym group that is closed at the moment. We've taken an omnichannel approach as well, with over 1.4 million views of on-demand classes and lots of other activity on social channels.

We're not stopping there. We're continuing to put effort into the app, and we're ramping up the amount of content we have. And we'll get to somewhere around 400 home workouts by the end of June. There's clearly been a development in the way consumers use fitness, and we're certainly looking to move with them in that direction, regardless of what the future holds.

Well, that's all very well for what we're doing now, but I'm sure you're concerned to know about the membership base. Well, let's turn to page 24 and look at that. Here you can see that, based on current trends, we expect to have over 80 percent of our forecast members to be in the member base around the time we open in June. And that's shown by the horizontal bars in the top left-hand corner of page 24. Now on the right-hand side of this page, you can see, as an example in the UK, that we did have some leavers through the period around closure. The blue line shows the actual leavers, and the dotted red line shows the budgeted or forecast number of leavers. And unsurprisingly, as we went through closure at the end of March, we had some excess leavers, people choosing to cancel their direct debits, as they canceled many direct debits after we closed.

What's quite interesting is, as we progressed through into April, the blue line has dipped well below the dotted red line, meaning that the actual number of leavers that we're experiencing is now well below the number of forecast or expected leavers that we anticipated we'd have when we put together our original budget. This is good, even if it cannot fully compensate for the fact that we have no new joiners coming into the member base while we are closed, so the overall membership is smaller than it would have been, hence the figures around the 80-percent mark.

But you will also be asking yourselves whether customers will want to come back to the gym. Well, page 25, if I can turn you towards that, shares some perspectives on this. We've clearly remained in touch with our member base and researched them along the way. It’s good to see at the top of this page that around two-thirds of our members are willing or very willing to return to the gym. With that said, we have nearly 20 percent of members who are unwilling to return and a further 20 percent who are indifferent or not sure. Clearly, we will be working hard to encourage the swing voters to come back to the gym and to win back the trust of those who are currently unwilling to return. That is our challenge, and we will embrace it fully as a management team across the entire group. On the question of what will be important to members, at the bottom of this page, I think the answer is crystal clear: cleanliness and hygiene will be what it's all about. No big surprises there, but I'll return to this theme in a few minutes.

So where do we go from here as a business and an industry? Well, moving on to page 26, we've been working very hard with other operators in the UK and across Europe and with the industry associations to play a leading role within the industry to seek government agreement on reopening protocols and approaches. Governments are following a range of different approaches to this, and it's hard to say that there's any real consensus when you look at the different approaches that governments are taking. But we do think it is important that we are involved in the shaping of protocols for the future. And there are a number of key dimensions that we highlight here on page 26. Hygiene standards, limitations on numbers in gyms, a maximum capping of numbers in the gym, social distancing provisions -- these are all likely to be part of the new regime under which we'll have to open and operate for at least some period of time.

The question of timing itself is an important topic. And if we turn to page 27, we've laid out our current view on

possible timings across the different markets in which we operate. Picking out a couple of highlights of this, Switzerland looks most likely to open for gyms in the middle of May or potentially towards the end of May. And at the other end of the scale, our current plan or perspective is that the UK is likely to be in mid-to-late June. But these are and only can be our best estimates of reopening. In reality, we aren't going to know about this until governments make official and formal pronouncements. We are very focused as a management team on being ready for this, however, and that's really occupying probably 70% or 80%of the time of the people who are still working in the business.

Let us try and give you a sense of the sort of things that we're working on and how we're thinking about reopening. Turning first to page 28, this is a schematic of a PureGym site, a typical sort of site, and we show illustratively here how we've begun to look at each and every area of our facilities to consider how the protocols will be set, applied, and managed. To ensure social distancing can be maintained, we're preparing new standard operating procedures for every area of our gyms in the UK and Europe. These standard operating procedures will cover gym entry, cardio equipment spacing, studios, locker rooms, the free weights area, delineation of spaces in the functional areas, all parts of the gym. And we're well advanced in this work so that we're ready when we have the opportunity to reopen.

Now we're fortunate, turning to page 29, that we have very good information on when members tend to visit our sites and what they do when they're there. And we're well-positioned to flatten the peak of demand. Let me explain this page 29 a little bit to you.

On this page, the solid blue curved line shows the average visits at different times of the day for a typical PureGym site. The blue dotted line, towards the top of the graph, shows the typical pre-COVID-19 maximum capacity. And of course, everybody could come to the gym whenever they wanted in the pre-COVID-19 era. We expect that we'll be setting a maximum capacity probably 30 to 50 percent below the prime maximum capacity. And clearly, that is shown by the black dotted line. And you can see from this that this will cut across the natural visit pattern of members. And typically, there'll be members who between 5:00 p.m. and 9:00 p.m., in an average gym, would not be able to enter given that maximum-capped capacity. But at all other times of the day, there's ample capacity. And indeed, for those extra visitors who can't visit in the peak times, there is actually space and time elsewhere, even with this reduced capacity, for them to be able to come to the gym and work out if they want to.

And we know from our research that members are planning to visit more at less busy times. And of course, personal working and commuting patterns will change for at least a period of time after the COVID-19 situation. And that should help us satisfy demand for members who want to come to the gym.

But we won't be leaving that entirely to chance. We turn to page 30. We show that we'll be using the app-based technology to help us and our members make the right decisions. On the left-hand side of page 30, we illustrate that customers will be able to use the app to foresee when the gym is too busy and to avoid the busiest hours if they want to. In the center on the left, they will actually be able to book slots in the busiest gyms at the busiest time periods. And this is an illustration from our Danish business. And we also show here, in the middle of the page, that people have the option to access through QR code scans in the future as well.

And to be clear, these are not dreams for the future. This is all technology that we already have and have been using or is in final-stage beta test. One of the points we, I think, always made to you is that we're a very technology-driven company. And once again, that is paying off by the actions we've been able to take along these dimensions.

On the right-hand side, you can see that we've built our client-side technology as well to ensure that we have, at PureGym, full visibility and reporting in real-time on both member numbers in sites and on member feedback. Technology's going to be a great enabler of the control that we want to have when people want to exercise.

And finally, on the question of overall capacity, and turning to page 31, it's worth remembering that the average PureGym in the UK, and indeed in Fitness World Facility in Denmark, is about the same surface area in size as four or five tennis courts. Put simply, we have adequate space in the majority of sites within which to configure safe social

distancing arrangements. And I think that's quite an important thing to keep in mind.

Coming to the final couple of points on looking to the future, and turning to page 32, the use of space and technology will not be enough. Indeed, as I alluded to earlier, the most important area on which we're focusing our time and attention is around the regimes of cleanliness and hygiene. This is the single most important issue that we, and our members, and our colleagues face. As I said earlier, consumer research confirms this. And it's obvious here to all of us.

As an industry, and specifically within PureGym, we're going to adopt a dramatically sharper focus on standards of cleaning and hygiene and on execution of cleaning regimes. This was something we always gave fair attention to, but clearly, there's been a step function change in the expectations of our members. And we will deliver on those expectations.

Key elements of this will include adopting non-clinical healthcare industry-level standards, a big increase in cleaning frequency and depth, improved materials and products for cleaning, much greater provision of member cleaning equipment, and use of appropriate PPE for staff when undertaking cleaning duties. And we're going to wrap this up, this focus, under the Train Safe banner, the communications and behavioral change device.

And moving on to page 33, we highlight that it won't be enough just to communicate these new rules. We will have to explain the rules, engage with members, encourage them to behave in line with the new norms, and if or when necessary, enforce these norms vigorously. Our belief is that the vast majority of our customers will be looking for us to be setting and upholding such rules as they will be -- in the way in which people can work out while not compromising their health and well-being. That's our full expectation of members. And as I said before, we intend to deliver on those expectations.

So in turning to page 34, it's stating the obvious to affirm that this is clearly a very challenging time for all of us as managers and for all of you as investors as well. And there's no easy way of dealing with it. We just have to hunker down and get on with it. We don't have any other choice. But we will make the absolute best of it that we can.

Despite the challenges, I hope we've done a good job today in setting the context for you for what we face and how committed we are to making the very best of our situation. Specifically, coming out of this session, I hope you are clear that we entered the crisis with as strong a platform of performance as we could hope for. We've acted with calm consideration and appropriate speed to the situation in which we find ourselves. Good progress is evident in getting our cash and P&L burn rates down. The liquidity we have on hand is adequate for the time being. And we have robust support from our shareholders. Management are focusing on the reopening and reflation of the business in a realistic, diligent, and well-thought-through way. A good proportion of our members have stuck with us, although we are neither complacent nor naïve about the challenges of retaining their trust and custom. And while, of course, there are challenges in the near term with respect to the recent acquisition of Fitness World, the strategic logic of that deal remains firmly intact.

Thank you very much for your time and attention. We're happy to take questions. We would just remind you, respectfully, that the purpose of the call and of the Q&A sessions is principally for bond investors, and therefore, we'd particularly welcome questions from that part of the audience. Thank you very much.

Question & Answer session

Operator:
Thank you. If you do wish to ask a question, please press *1 on your telephone keypads. If you change your mind, press *, followed by 2. And please ensure that your line is unmuted locally. There will be a brief pause while questions are being registered. Thank you for your patience.

Our first question today comes from Elizabeth Stapleton of PGIM. Elizabeth, your line is open.

Elizabeth Stapleton:
I have got three questions. Actually, firstly, thank you very much for the presentation and appreciate your transparency. But three questions, if I may, the first is on rent; the second is on weekly running costs as we start to reopen; and the last will be on liquidity.

So firstly, on rent, are you able to confirm what your pro forma annual rent is and remind us of any landlord concentrations and, where you have negotiated, what kind of form that negotiation takes? The second question on weekly running costs would be, appreciate it's early days, but if you're able to give us any sense of, as you start to reopen, what those weekly running costs would start to ramp up to? I'm assuming, the work that you've done will allow you to reduce it, versus the prior norm. The last question on liquidity, in a normal operating situation, what would you view as your minimum liquidity? You mentioned support of shareholders, but have you been in any other talks with any other parties, including government to foster liquidity?

Humphrey Cobbold:
Thank you, Elizabeth. Let me deal with a couple of the points there, and then I'll hand over to Alex. Three questions from you. Firstly, in terms of rent, Alex will deal with the question of pro forma, annual costs on that and weekly costs. On the more strategic level, in terms of landlord concentration, the landlord concentration is very low. We've probably have about a dozen or so landlords, maybe 15 with more than a couple of sites. But the rest is pretty much one-offs. So a low degree of concentration, and certainly nobody has a degree of leverage over us in that regard if that's part of your question there. In terms of the general tenor of those discussions, as I alluded to, that has been greatly helped by the announcement last week from the government that they won't allow landlords in the UK to use aggressive measures on us. And there's a pretty sensible set of discussions coming together about a combination of rent-free periods, rent-free being replaced by end of lease term, rent abatements, and rent deferrals, and a pretty broad spectrum of those.

As I said in the presentation, I won't deny pretty much every discussion is an arm wrestle. It's hard work, but we're helped greatly by the stance the government has taken, which is to say that landlords can't act aggressively towards businesses like ours that have faced the challenges caused by this virus through no fault of our own. I'll ask Alex in a moment to deal with the more specific questions on pro forma rent. On weekly costs, I'll be clear, it's too early for us to comment on those. A reasonable question to ask, Elizabeth, but the reason for that is we don't yet have clarity from government on the regime that we'll be able to operate under. Therefore, we're doing lots of work on it, but it would be misleading of me to give you confidence directionally, even on whether costs are up or coming down, or whatever. Clearly, we're going to put every effort we can to get costs down. I think in general in the long run, important costs like rental and energy are coming down, rather than not, but we are going to have to makes some investments in cleaning services and capabilities as well. We don't yet know how that comes out.

And then finally, in terms of liquidity and normal liquidity levels, I'll allow Alex to deal with that. At the headline level, we're very close in conversation with Leonard Green as we've said and we have an open dialogue with them on current liquidity management and cash flow. We haven't had any formal discussions with them or anybody else about broader liquidity sources for us, simply because we focused on dealing with what we have at the moment. When the future becomes clearer, then we'll be in a position to consider those sorts of discussions. So with that, let me return to Alex on points on rent and normal liquidity.

Alex Wood:
Thank you, Humphrey. Good morning Elizabeth. Just on the rent points, you asked what the pro forma rental costs would be without COVID mitigation, it would be about £2 million pounds a week for the whole group in terms of that rental costs. Hopefully that covers off that question. In terms of the level it is post-mitigation, clearly those conversations are live with landlords, so I can't put a figure on that at the moment. We're getting good government support, as Humphrey alluded to, from the Danish government -- and actually all of the non-UK governments, to support and help mitigate the rental cost. But in the UK, of course, there is no specific government underwrite of rental costs. So we're engaging in negotiations there, and they're ongoing. So I can't get you a clear answer; it's one

of the many moving parts that are evolving over time, but I can give you the start point nice and clearly.

Secondly, in terms of the weekly running costs, as Humphrey said really, it's too early to call exactly what the running costs of the business will be on reopening. Clearly, there are some elements of the cost base that will actually go up, such as cleaning if we're going to present an environment that is differentiated and gives members and our own colleagues an excellent set of cleaning standards. But then there are other elements of the cost base that will be lower. For example, not all of our staff will need to come back straight away, depending on the phasing of the opening regime. So on that level, costs will be lower. And also slightly longer term, clearly the property market will be adjusting post-COVID and so we expect that property costs will be lower, and there could even be a permanent adjustment in the level of rates post this crisis. So all of those will feed into the mix; we've done a whole range of scenario modelling but it's too early to put the number on it for obvious reasons.

Elizabeth Stapleton:
If you could follow up with liquidity in a normal operating scenario. That was one question as well.

Alex Wood:
Could you just elaborate on what you mean, Elizabeth? Normal liquidity?

Elizabeth Stapleton:
So pre-COVID, what would you have needed as cash to run the business?

Alex Wood:
Pre-COVID, the business has a very positive working capital dynamic where it generates cash through rolling out new sites, so working capital inflows. Absent COVID, we would be generating a significant amount of free cash flow. The combined group on a pro forma basis generates around about £100 million, of which half of it would be spent on servicing finance costs and then leaving a significant amount of free cash flow after that. There is no net absorption through working capital requirements. The business, therefore, has a lot of excess cash, so in normal circumstances there's absolutely no issue from a cash flow perspective. Actually, when we went into this position, we had a significant amount of cash on the balance sheets in anticipation of site rollouts. So actually that is one of the reasons for our liquidity capacity at the moment.

Elizabeth Stapleton:
Okay, many thanks. I'll leave the floor to someone else now, thank you.

Alex Wood:
Thanks, Elizabeth.

Operator:
Our next question today comes from Keval Dattani of Aberdeen Standard Investments. Keval, your line is open.

Keval Dattani:
Thank you very much for the presentation; we really appreciate it. I've got three questions and appreciate that you won't necessarily have answers to all of them, given obviously our situation is changing. The first one is that do you think that your business now has structural change in EBITDA margins, but also in the EBITDA going forward? You talked to the impact of cleaning on the cost base and, granted, you said that could be offset with rental yields falling over the longer term, but one imagines other small cost line items to insert. Also given that you're going to have to implement a maximum capacity going forward. I imagine that that would lead to a drop off in revenue, given that people will inevitably have to substitute a way or stop going to the gym if they can't get in it at a certain time. That's question one.

Question two is regarding the app, is that something you intend to monetize going forward? Say hypothetically, you get a shift in fitness perspectives from consumers toward home workout; is that something you'd make current

member-only access, in which case, they would have to be paying you a membership to gain access to the app? And then the third question is, I appreciate it's probably far down the line if it even happens, and I suppose we're all hoping that it doesn't happen, but on the event of a second or even subsequent waves of coronavirus business closures, what planning have you undertaken internally, and how flexible do you think you can be were you to, let's say, reopen in June as expected, and suddenly then be forced to close down in November time? What flexibility do you have?

Humphrey Cobbold:
Keval, let me deal with those. Firstly in terms of business structural change, EBITDA margin, etc, the honest reality is, until we reopen and start to see how the business trades and reflates, I think as you'd understand, that's going to be very difficult to call. However, I would make a couple of comments in that regard.

Firstly yes, there will be some concern about coming back to the gym; we've alluded to that; we're very mindful of that. Also -- and there's very clear evidence of this when you look at markets that are a little bit ahead of us, particularly Asia -- there's going to be a massive upturn in the recognition of the importance of physical activity and wellbeing in the context of personal health and wellbeing, both physical and mental, in the longer run. And I think there is some good reason for optimism in the medium to longer term. It would be logical for more people to be more serious about their physical activity and wellbeing. So, that's one point to keep in mind.

A second point to keep in mind, I showed a graph around how we'll have to think about capacity differently. One of the points behind your question is, how well can we adapt our revenue model to deal with that different capacity management? And there, PureGym group have a particular strength because we've got pretty much the most flexible revenue management and yield management model in the industry, anywhere in the world. And we quite deliberately built it as such.

Why does that matter? It matters because we can price every club differently; we can price different memberships in every club differently; we can even price the access to facilities at different times of the day differently. So, if there are more people who want to go at a capacity constrained time of the day, we would allow base prices to increase and reduce off-peak prices, or quiet time prices, to allow us to use the economics to balance out supply and demand. Now, revenue is the key driver of our EBITDA margin, and the reason that we've got industry-leading margins and EBITDA performance and return on capital is because we've become good at managing revenue. Any operationally-geared business like ours needs to focus on being really good at managing revenue. So, I can't give you specificity about EBITDA margin and EBITDA in the future, but I can offer a measure of reassurance that we're well equipped, and I would argue better equipped than anybody else to manage that.

Secondly, on your question on the app, very simply, at the moment it's freely available to anybody and everybody who has been a member. I think it will shortly become available to all non-members. We're treating that as an approach to engagement and loyalty and trust at the moment. In the future, we might well find ourselves able to charge for that. That's not a focus currently. We've got the facility and the capability to do that from a technical point of view. That's very straightforward, create a paywall and create freemium type models. I think you have to be realistic in that, in the context of a group that was set to do £450 to £500 million in revenue this year, that would be a smaller rather than larger number.

And then, finally, on the question of being ready for and modelling a second wave closedown. Yes, we're absolutely on with that. It is a more complicated question than it seems, in that we've got to think about, well, how long will be the closedown be, how will it be different in different geographies, and how will that play through? And, yes, we're doing that work at the moment, and clearly, we will get ourselves as ready as we can be for that. You know, we'll be better prepared for closedown and reopening next time, if it happens again. I'm not pretending it's going to be easy, but we'll be well-setup and prepared for that. And I'm confident that we'll be able to manage our way through it.

Keval Dattani:
Thank you.

Humphrey Cobbold:
Okay.

Operator:
Our next question today comes from Eleanor Price of Kames Capital. Eleanor, your line is open.

Eleanor Price:
Most of my questions have been answered, but I just wondered if you could comment on how many of your members are currently actually going through furlough themselves because I just wonder if some people haven't cancelled because they hope they're going to have a job coming out of this, but actually, a lot of corporates may have to make some very tough decisions, and gym membership might be a casualty of that?

Humphrey Cobbold:
Hi Eleanor, thanks for the question. I'll be completely straight, I don't know the answer to that question. We haven't researched current furlough status of our members, and we certainly can't predict how many may lose their jobs. Clearly, one of the things we're very sensitive about is when we reopen, we'll be reopening into a very challenging economic environment. So, that's why I think we're very measured and not all complacent about the challenge that we'll face in holding onto our members, but we'll be absolutely up for that challenge to the best of our ability.

Eleanor Price:
And will you be making any special offers to potentially entice members back, or retain members? Because I can envisage a potential race to the bottom, as you see on the mobile phone companies and everything else

Humphrey Cobbold:
We're going to be very careful and considered. And I'll allude to the point that I made in Keval's questions. We've got extremely good what I call “fine motor control” over revenue, and that includes promotional activity, pricing at the individual gym level, and offers to former or current members. So, again, I think we're better positioned than anybody else to deal with and adapt to the dynamics of the trading situation in which find ourselves, and clearly, we'll be very careful to get, to the base of your question, in managing revenue and performance to the best that we can. And we'll be able to target any activity that we take.

Eleanor Price:
Okay. Thank you very much.

Humphrey Cobbold:
Thank you.

Operator:
We have no further questions on the line. So, I'll hand back to Humphrey and Alex for any further remarks.

Humphrey Cobbold:
Well, thank you very much. No further remarks from us except just to say, once again, we know that this is a difficult period for everyone, for us as managers and for you as investors. It's been a very challenging few weeks. I think we all know it's going to continue to be challenging for some time into the future. We're greatly appreciative of your support, and I'd like to reassure you that, I, myself, and Alex, and the whole management team in the entire group is doing everything that we can to get ourselves through this in as strong as shape as possible and to return to the level of performance and trajectory that Alex highlighted earlier in his presentation. Thank you very much.

Alex Wood:
Thank you.

[end of transcript]