PureGym Q1 2023
Conference call Wednesday 17 May 2023

Humphrey Cobbold (CEO)
Good morning and welcome to the presentation of our Q1 2023 results. We'll be running through the presentation that was posted on our website at 7:00 am this morning dated 17th May. Hopefully you will all have this in front of you and we will guide you, as normal, to the page number references as we go through the document. We recently held our full year results and so this update will be relatively short and focused, a to-the-point summary of our quarterly results and a few points on outlook.

So, turning to page 3, I'd like to give you an overview of the period, where things stand now and what we will cover today.

At the end of Q1, revenue was up 17% ahead of Q1 2022. Run rate adjusted EBITDA showed continued healthy progression to £120 million. We retain a strong cash position, with cash on the balance sheet of £208 million at the end of the quarter and available liquidity of £353 million.

We opened 15 new corporate owned sites in Q1 2023 and 4 new franchise sites across the Middle East. We're pleased to report that the Q1 results are ahead of expectations, with UK like-for-like revenue now back at 100% of 2019 levels. The business has good momentum and a strong and reliable EBITDA tailwind from new site openings in 2022 and early 2023. There is clear underlying progression in EBITDA performance, both in terms of our recent track record, but also as we begin to look out to the future.

Looking to that future and given some of the comments and questions from the last update call, in this update Alex will give you a little more guidance on the run rate adjusted EBITDA and leverage trajectory, which should be helpful as we look to the future and consider the refinancing of the bonds. With that in mind, it's good to recognise, once again, that we have excellent support from and alignment with our business partners, Leonard Green and KKR as we start to explore refinancing options well in advance of the maturation of the bonds in February 2025.

So, with that overview, let me now hand over to Alex to take you through our results in a little bit more detail. Alex, over to you.

Alex Wood (CFO)
Thank you, Humphrey. And good morning, everyone.

Let me start on page 5 with the highlights of our financial results for the 3 months ended 31st March 2023. This page gives a snapshot of some of the most telling statistics from the quarter. In summary, Q1 was a very solid performance indeed, demonstrating strong ongoing recovery, a clear step up in EBITDA, EBITDA trajectory, and growing momentum.

Let me start with revenue, which was up 17% compared with Q1 2022. You will note that the pace of this year-on-year growth has increased by 5% from 12% growth last quarter. The group also achieved 12% membership growth vs Q1 2022, and we now have just shy of 1.9 million members, in total, across the group. Within this, the UK, which is the largest constituent part of the group, delivered 15% growth year-on-year. Again, you will note that the pace of this year-on-year member growth has increased by 4% since we spoke last, up from 8% last quarter. Adjusted EBITDA was up 16% when compared with Q1 2022 and total open sites now stand at 572, which includes 559 corporate owned and 13 franchise gyms in the Middle East.

So, with those as the headlines, let me drill down into a little bit more detail now over on page 6. We're very pleased with the continued healthy progression achieved in the quarter. As you can see from the comparators on this page our progression continues across all key drivers of the business: site numbers, member numbers and average revenue per member (ARPM). These elements compound to deliver that momentum in revenue growth which I headlined just now.

A key number I want to call out is adjusted EBITDA. The business delivered £28 million of adjusted EBITDA in Q1, which is an increase of £5 million vs Q4 2022. As I mentioned last time we spoke, the ramp up of site openings through 2022 reduces profitability to a degree in that year due to the opening losses in the first few months post opening. However, these new sites are performing really well and in 2023 we'll see the benefits of their maturation and continue the very solid EBITDA progression quarter on quarter. We can see run rate adjusted EBITDA grew to £120 million, and this was up £21 million on the prior year, and up £6 million on Q4 2022.

Turning to page 7. There were 19 new sites openings in the quarter, more than double the number of sites opened in the equivalent quarter last year. These new sites openings will further fuel business and EBITDA momentum for the second half of 2023 and beyond. Our ability to deliver this step up in new sites was as a direct consequence of maintaining and continuing to build internal resource and capabilities through and after the pandemic.

Our quarter end cash and liquidity positions remain strong at £208 million and £353 million respectively. As I mentioned last time we spoke, these reserves continue to be a significant differentiator vs competitors, especially in the current capital constrained macro environment. It provides the financial capacity for us to push on with strategic plans in a measured and controlled way.

One final point in relation to operating cash flow of £13 million, if working capital movements were excluded, operating cash flow would have been £20 million, significantly more than our current interest cost of £13 million a quarter. However, I wanted to point out that there were £7 million of working capital outflows in the quarter, temporarily suppressing that operational cash flow, but this simply relates to the timing of the settling of invoices. Ordinarily, the business is neutral from a working capital perspective over the course of the year.

Let's now move on to the latest on like-for-like recovery over on page 8. We shared quite a lot of

detail on this during our full year results just a few weeks back, so please refer to that if you missed that presentation. The headline update is that when we spoke last, we showed that the UK like for like estate was back to 99% of 2019 revenue levels as at the end of February. The gap continued to close in the month of March with UK like-for-like revenue now back to 100% of March 2019's level, taking 2018 and prior cohorts as the base. The equivalent statistic for volume was 87% for March 2023. Our clear strategy has been to push volume numbers from the post COVID low of 66% and at the same time balance revenue optimisation, including carefully judged price increases to help mitigate some of the gap as well as to cover inflation of costs. We've highlighted in the appendix the elements of the price equation that we're applying to help manage this, delivering ARPM growth of 15% vs 2019 across the group.

Turning now to page 9, let's cover progress made since the year end. There's been good progress across our core metrics with a net gain in members of over 200,000, an increase of 12% vs December. Revenue in the month of March was up 12% vs December. Adjusted EBITDA was £11 million in the month of March, that's up 35% vs December, this metric should give you a feel for how the business is currently performing.

Turning to capital expenditure now over on page 10. We invested £12 million of new site capex in the quarter, opening 15 new corporate owned sites across the group. We also spent £7 million in the quarter on maintenance and refurbishment works. Our ability to invest in maintaining the quality of the existing estate is also a differentiator vs competitor, who may find that they need to cut back a little more in this area.

Turning over to page 11, let me provide an update on our liquidity and net debt position. Our senior secured net debt was £645 million at the end of Q1, significantly lower than pre pandemic in absolute terms. The key run rate adjusted EBITDA metric is returning towards the £160 million level that was applicable in 2019. On that basis, our current leverage would be 4x and we highlight that here. Of course, it's clear that while the business continues to progress, we've not recovered to that level of EBITDA yet and if we take the current run rate adjusted EBITDA of £120 million then the leverage multiple is 5.4x, which is above our target range. Let me elaborate now on how we expect to return to within our target leverage range by the end of 2024.

Firstly, over on page 12, let me give a short reminder on the run rate adjustment. We as management look at both adjusted EBITDA and run rate adjusted EBITDA as two key metrics. Adjusted EBITDA gives the current profitability, which is very important for obvious reasons, but this does not take into account the benefits from investment into new sites, which in fact drags EBITDA to a degree in the near term. Given the predictable maturation of new sites, the run rate adjustment reflects the additional EBITDA when the immature sites have matured. As such Run rate adjusted EBITDA shows the underlying level of profitability of the business and gives us a measure of the forward momentum we have.

Over on the right-hand side of the page, we plot the performance of new gyms opened in 2019 and later. These are the actual results of those gyms since they were opened. Having now

established a reliable track record of small box format and medium box format new site performance, we've updated our run rate assumptions for immature MBF and SBF sites to reflect that. You can see that for each of our size formats, actual performance is in excess of the run rate assumptions used showing that we're maintaining a prudent mindset there.

To further underpin the strength of the underlying business momentum, let's turn over onto page 13. Here you can see a couple of other cuts of the new gym performance data showing that recent UK site openings continue to progress well, highlighting that the product and the offering is hitting the mark well. Specifically, these charts show that new sites across all cohorts: 2020, 2021, and 2022, are performing very consistently and are hitting revenue and/or membership volume maturity levels within two years. Our 2023 new sites are also off to a very good start and performing just as well, if not better than this. This is clearly very encouraging on a number of levels, and it naturally follows that strong consistent performance from carefully selected new sites converts into additional profits, and therefore EBITDA growth.

And so, if you turn now to page 14, we thought it would be helpful to set out our run rate adjusted EBITDA over the last five quarters. Firstly, you can see that the business has delivered progression quarter on quarter and that there's increasing momentum in that growth. Secondly, you can see visually how the run rate adjustment in grey reliably converts over to adjusted EBITDA, in teal, over time. And finally, you will note that there were 35 corporate owned sites opened over the last two quarters alone, delivering a higher run rate adjustment and fuelling further growth as those, and other, new sites mature over the next 24 months or so. Hopefully this slide gives you a good feel for the trajectory of the business. Of course, we plan to continue opening new sites each quarter which will continue to fuel this trajectory going forward.

And turning now onto page 15, to tie all this together with respect to leverage, strong growth in EBITDA means the business rapidly grows back into its shoes from a leverage perspective. We expect to be back to 2019's leverage levels over the next 18 to 24 months. Of course, not only does debt capacity measured in terms of multiple improve, as we follow our strategy for recovery, our capacity to bear high interest rates when we refinance improves as well, with cash flow conversion also improving from the currently suppressed levels to the more normal pre COVID levels, which are between 70 and 75% when the business is fully reflated.

So, I hope that this financial and recent trading update was helpful and it's reassuring you that we're thinking of all the key variables as we manage and guide the business trajectory. I hope that these perspectives help you understand that the business is well set ahead of refinancing, and that we as the management team are looking forward carefully to ensure that the process of refinancing will be managed well when the timing is right. So, with that, let me now hand back over to Humphrey to comment on our outlook and to conclude.

Humphrey Cobbold (CEO)
Thank you, Alex, for those details. That just leaves me to provide a reminder of the outlook and to wrap up over on page 17. Firstly, the business is delivering continued steady progression in

the underlying member base, and we will continue to focus on that as we progress towards 2 million members. We plan to open approximately 40 new corporate sites at an average cost of £1.2 million per site over the course of 2023. The unit economics of these sites, as we explained in some detail in the full year update, remain resilient, very resilient in fact, and highly attractive in terms of return on capital employed, which we regard as the key indicator of performance for new site openings. As a reminder, our like-for-like costs are well controlled, with only around 5% inflation expected for 2023 vs 2022. We have fixed the majority of our utility requirements until the end of 2024 and that largely removes volatility risk in that area. And as we explained last time, we expect an increase of only around £5 to £8 million in our utility costs across the whole group when we compare 2024 with 2022. Operating cash flow conversion is expected to return to pre pandemic level of around 70 to 75% over the medium term. We've also included several supporting schedules in the appendix to provide further details on a number of these key areas.

Finally, as you know and as Alex has referred to, our bonds mature in February 2025. Many of you will be wondering and considering what the plans are in that regard. So, let me make some comments on that now, in addition to the points that Alex has made. As we said before, the group's well-placed to explore refinancing options in advance of the bond maturity. We have excellent ongoing support from world class shareholders in Leonard Green and KKR. We have cash on the balance sheet which is very helpful in that it provides us with lots of optionality as we approach the refinancing and watch interest rates and the developments in the bond and credit markets carefully. As we look forward our continuing momentum in EBITDA and cash conversion supports a deleveraging profile and increased debt service capacity as Alex has admirably articulated and explained.

So, hopefully, this update has been informative for you and has given you all a good feel for where we stand at the end of Q1 and gives you a perspective on the momentum and the progression that we have for the year ahead. I'd like to take the opportunity, once again, to thank you all for your continued support of the business and I hope that you appreciate the ongoing transparency that we try and provide. In particular, several of you have reached out expressing support for the business and indicating an appetite to continue to invest in the business as we look to refinancing. Naturally, we're very appreciative of those expressions of support.

Finally, I'd like to call out my thanks to all the management team and colleagues in the business who continue to do a terrific job every single day in an environment that is not an easy one and one which we need to continue to keep working away at and they’re doing a great job in that. It's satisfying to see the fruits of those labours starting to show through in the results and the business momentum that we've been able to generate and show quite clearly today.

Our next results announcements will be late in the summer when we'll be updating you on our Q2 results and we very much look forward to speaking to you again then. With that I'd like to close the formal proceedings and we’d be happy to take a few questions.