MONEY & INVESTING

Brait: take the rights or run?

For the second time in two years, Brait is back with its begging bowl. But, says its CEO, that's better than an asset fire sale

BL PREMIUM

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Virgin Active: The fitness chain is valued at just under R8bn. Picture: Freddy Mavunda

Timing is everything ...

Like a debt-culling rights issue when the worrying whiff of burnt sugar still hangs heavy in the air, following Tongaat Hulett's proposed R4bn cash call.

So you can understand why Brait's bid to raise R3bn from investors via a convertible bond offer — at half the company's last stated NAV per share — hardly elicited an enthusiastic response from the market.

Over a week the share price is down more than 12%. This is a combination of the dilution of the proposed capital raise and, predictably, speculation that the banks might have forced Brait's hand. Punters are also worried that the rights issue, Brait's second in less than two years, is a dire pronouncement on the chances of extracting value from its portfolio — which revolves mainly around consumer brands business Premier Group and international fitness chain Virgin

One of the more forceful questions at the Brait investment presentation was whether the group — now managed by highly regarded private equity experts Ethos — should rather have opted for an asset sale before a capital raise.

The questioner pointed out that with a NAV of more than 800c a share, Brait is effectively swapping 100 for 50 in the proposed rights offer.

But Brait CEO Peter Hayward-Butt said there's absolutely no chance Brait could extract a premium price for Virgin Active today.

Peter Hayward-Butt: No chance Brait could extract a premium price for Virgin Active

"We are on the back foot, and still working a trajectory towards 2019 levels of profitability. If we tried now, and we have spoken to people about this, we would not be doing shareholders justice. The only other option is to sell Premier. But why would we be price takers in an asset that is outperforming its peer group, and an asset we think will be well liked by the market?"

If Brait's long-suffering shareholders take up their rights, said Hayward-Butt, "then the dilution to the NAV does not matter. Rather this than sell assets at a discount."

Paul Whitburn, portfolio manager at Rozendal Partners, agrees, and says a rights offer would allow the company to remain the master of its own destiny.

"Brait is being supported by big shareholders like [retail tycoon] Christo Wiese and Ethos, rather than the big banks. It gives it breathing space to get Virgin Active across the river and closer to the £100m ebitda [earnings before interest, tax, depreciation and amortisation] target," he says.

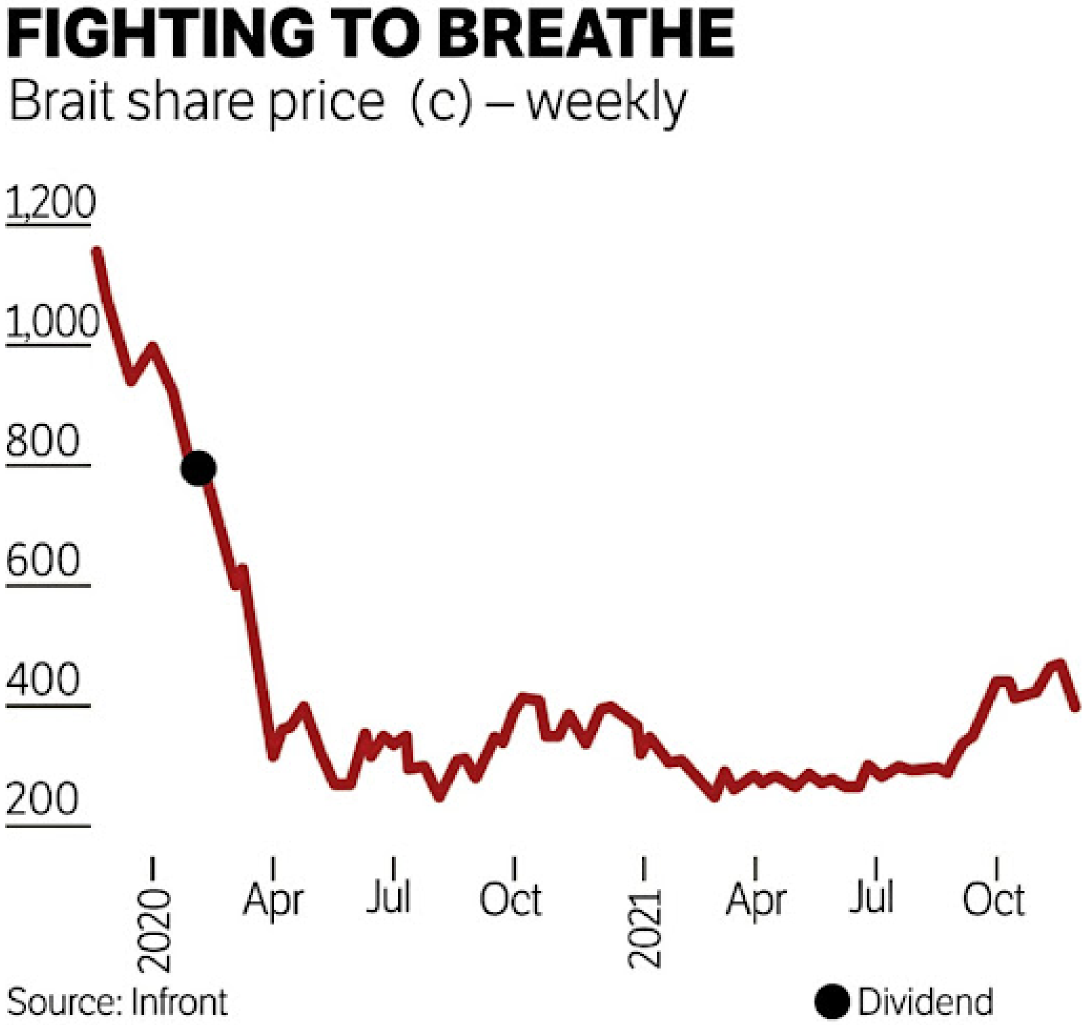
"Meanwhile, Premier is going from strength to strength … and should be at peak margins when it has an IPO next year."

The rights issue should also be seen in light of what Brait has to pay in interest costs: R650m a year at the moment. Hayward-Butt reckons the offer could save as much as R800m in interest charges over three years.

Scanning the latest Brait financials — interim results to end-September — i it seems Hayward-Butt might have a point about the short-sightedness of selling assets at a discount. Premier's performance has been outstanding, and looks like continuing into the new financial year — which will coincide with plans to list it on the JSE.

Talk is that Brait might look at a listings window between June and July. Hayward-Butt said much will depend on Premier extending its robust profit performance and the market being open to a new consumer brands listing.

While details are still relatively scant, it would be likely that Brait will sell off a chunk of Premier to new investors at listing. The proceeds can be used to cull debt, and then, when Brait's balance sheet is better reinforced, it could unbundle its remaining stake. This would effectively allow Virgin Active to list by default in being the sole remaining asset in Brait (presuming its stake in fashion group New Look is sold too).



Virgin Active, for the record, is valued at just under R8bn. This means Premier is, for now, Brait's largest investment. The market is, of course, mostly at odds with the Virgin Active valuation, since Brait is basing its assessment on expected earnings of more than R2.2bn for the 2023 financial year.

Yet in the three months to end-September — when the gyms in the UK and Italy were mostly open, partially open in SA and mostly closed in Australia and the Far East — Brait managed to generate just R140m in ebitda.

Not surprisingly, it was forced to pump more capital into Virgin Active, which is why net debt has surged to R3.9bn.

With all Virgin Active clubs now open (though some are still subject to Covid restrictions) the gym group's earnings should be considerably higher in 2022, but still well off the R2.2bn target.

And the market's view on Premier is difficult to gauge too, simply based on the share price discount to NAV — that Virgin Active is accorded no value at all.

Officially, Brait, at the end of September, slapped a R8.4bn valuation on its controlling stake in Premier, 20% higher than a year ago. But this strong gain doesn't reflect in Premier's listed peers — most notably Tiger Brands (whose shares are down 10% over a year), Rhodes Food Group (down 2%), Libstar (up 2.54%) and even AVI (up only 8.74% despite pending corporate action).

The valuation is based on an ebitda multiple of eight, which in isolation might seem cheeky (albeit at a 9% discount to its peer average multiple of 8.8).

Paul Whitburn: Premier is going from strength to strength ... and should be at peak margins when it has an IPO next year. Picture: Supplied

But the multiple is arguably quite justified by Premier's performance in recent years, when margins have begun to bloom.

animal feeds, wheat flour, biscuits, pasta, feminine hygiene brand Lil-Lets, sweets, confectionery and beverages — also fared stoutly.

The financial year ahead should benefit from the integration of its Mister Sweet acquisition (including for only two months in the year to end-September numbers). There will also be operational benefits from the R450m spent on an inland bakery project in the second half of the new financial year.

Assuming the current valuation on Premier is reasonable and pencilling in solid interim results, if Brait sold down its 96.9% stake in the business to about 70% it could raise between R2bn and R2.5bn, conservatively.

Still, Premier's listing should do enough to unburden Brait's balance sheet — which already is primed to receive a not insubstantial cash inflow of R400m for the sale of its minority stake in glassmaker Consol.

Whitburn says Brait has shown an ability to sell assets at a premium. This includes Iceland, the UK-based grocery business that was sold in mid-2020.

And compared with Iceland and Consol, offloading a few Premier shares at or around the latest inferred value should be a cakewalk.

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Last Price	Day Change
3.85	▼ 0.10 | 2.53%

Mon Dec 6, 2021 10:37 AM

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David Wolpert • 2 hours ago

VA is probably a business with excellent potential but it’s equipment is now dated and barely functional in some clubs. It would cost a few billion to rectify. Suggest Discovery/Vitality makes a bid.
The collapse of VA would hurt Discovery which operates excellent and attractive health linked reward schemes for members of VA