SORTINO M&A GROUP

Apollo's Acquisition of The Restaurant Group for £701m

ALTERNATIVE INVESTMENTS

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Deal Introduction

DETAILS ABOUT THE DEAL

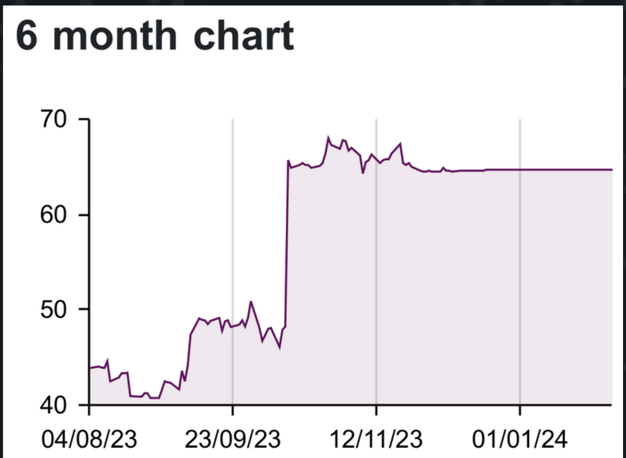
On the 12th of October an agreement between the directors of Bidco, part of Apollo Global Management, and The Restaurant Group (TRG) has been reached. The agreement provides that each TRG Shareholder is entitled to receive 65 pence per share.

TRG's advisors were Lazard, Centerview and Citi.

Apollo had closely monitored TRG over the last few years and believes that the company is **of high quality and of high potential to expand in their industry**. The accolade of brands and strong management team of TRG are also strong characteristics of TRG valued by Apollo.

TRG recently announced the sell-off of their leisure arm. The company will in fact be focusing its attention on the core business of dining. The goal is to foster growth within their already high margins, as well as reducing debt, something Apollo is in favour of.

The deal was officially closed on December 21st 2023, leading to the delisting of TRG from the London Stock Exchange.



REASONS FOR M&A

This deal is consistent with the continued interest PE has shown in hospitality and leisure, a sector Apollo has pursued in the past, but this has been mostly limited to companies in North America (notably the chain Chuck E. Cheese).

Apollo's recent history reveals an increasing focus on publicly traded UK targets, albeit with problems of finality. The target owns about 700 locations (restaurants and pubs) in the UK (including the chain Wagamama and Barburrito). It has been struggling with slow post-pandemic recovery, coupled with soaring costs and consequently falling margins. To this length, pressure to change management and improve profitability from shareholders (activist investors Irenic Capital and Oasis Management) has been mounting, leading to the elaboration of a strategy to cut adjusted net debt dramatically to 1.5x EBITDA (adjusted) by the end of 2025 – both of which are initiatives Apollo said it is "highly supportive" of.

Further statements made by Apollo partner Alex van Hoek suggest that TRG "has proven resilient through macroeconomic cycles, but the outlook is still one of high interest rates and inflationary pressures and the company now needs the support of patient private capital to achieve its ambitions". Despite the challenges the target is facing, it remains a leader in the casual dining market and boasts a substantial portfolio of brands. An established player, it has the capabilities and scale needed to retain customers and attract new ones.

https://www.trgplc.com/wp-content/uploads/2023/10/Rule-2.7-Announcement.pdf

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Industry Overview

The casual dining sector in the UK is subject to a wide variety of challenges, mostly stemming from sluggish post-pandemic recovery, dwindling disposable incomes, and supply-side cost pressures. The industry is not very concentrated, with most restaurants being locally-owned, placing them at the mercy of macroeconomic factors, and at a disadvantage against large chains.

Industry challenges

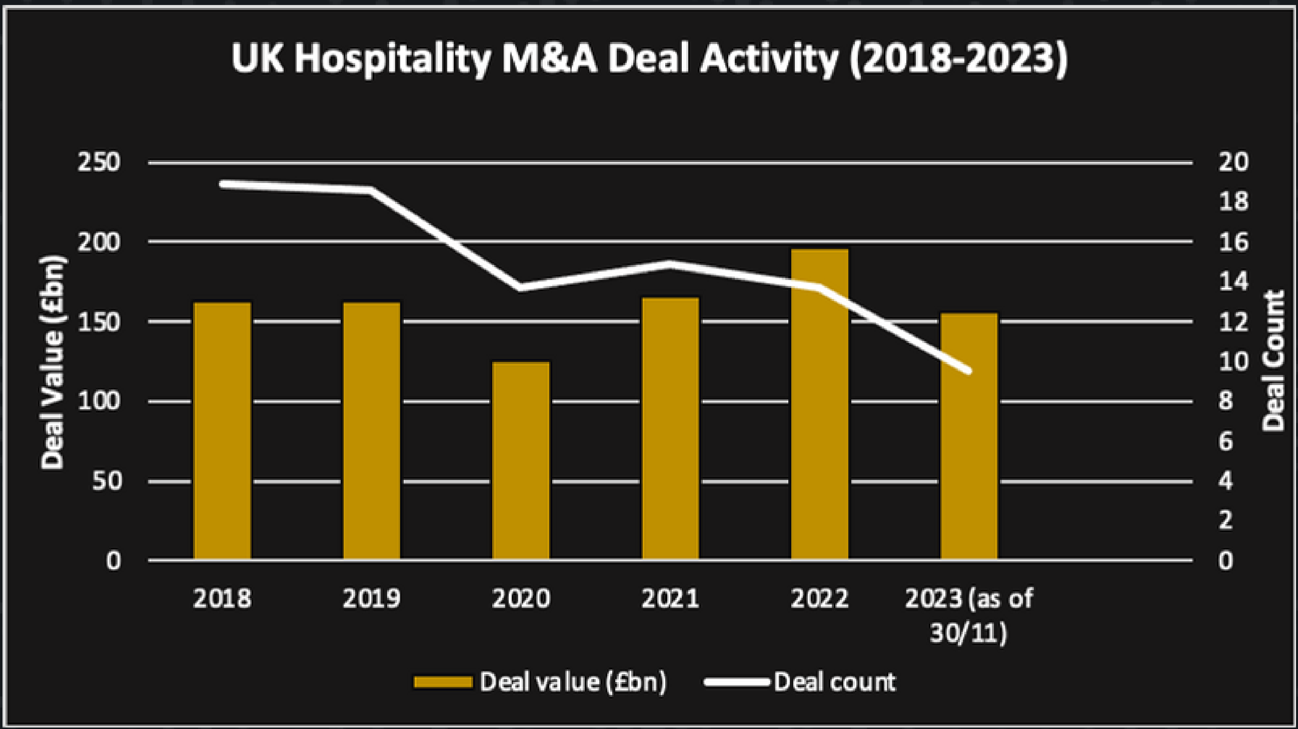
While food prices rose around 26% between December 2022 and December 2023, prices in restaurants rose by 7.7% in the same period, a fact that carries pessimistic implications for operators in this sector.

VAT increases back to 20% after cuts and rent moratoria during the pandemic have had a contractionary effect for the industry, while fallout post-Brexit is evident when considering staffing shortages.

Consequently, the total number of casual-dining locations fell by 4.2% to 5,160, a rate of decline nearly double that of the comparable pub sector. In Q2 2022/23 Industry leaders including TRG have closed a combined 100 locations between them.

	Deal value (£bn)	Deal count
2018	163	18.9
2019	163	18.6
2020	126	13.7
2021	166	14.9
2022	197	13.7
2023 (as of 30/11)	156	9.5

Data from Pitchbook shows a trend of lower valuations in the past years, although the deal count has not dropped significantly, suggesting investors' bearish attitude to the industry. The M&A outlook has remained grim, but the Apollo deal appears to have set a positive benchmark of sorts, as assessed by Barclays analysts, and strong performance in adjacent industries (tourism especially) may predict an uplift in activity.



The outlook for the casual dining sector in 2024 is cautiously optimistic, with several factors driving potential growth. These include a gradual increase in consumer confidence, innovations in the business models coming from VC backed startups, and increase in demand for complementary services such as delivery which could boost demand and increase potential.

Acquirer Overview

Apollo Global Management, founded in 1990 by Leon Black and headquartered in New York, is a private equity firm specialising in credit, private equity and real estate markets. The firm's investments include traditional buyouts, recapitalisations, distressed buyouts, special situations, carveouts and industry consolidation transactions. With over $512 billion in assets under management, Apollo is the third-largest private equity company in the world, behind Blackstone and KKR respectively.

Apollo's recent fundraise in July 2023, of its flagship fund 'Apollo Investment Fund X' raised $20 billion (10th flagship buyout fund) [below its $26.2 billion predecessor fund] (Buyout insider, 2023).

The firm seeks to invest in companies based in North America, Western Europe and Asia.

It employs a combination of contrarian, value, and distressed strategies to make its investments in the average range of $10 million to $2.5 billion. Apollo has deep roots in Drexel Burnham Lambert with all three of its Co-founders, most notably Leon Black being the right-hand man of Michael Milken who revolutionised the credit markets with the commercialization of high-yield debt.

KEY FINANCIALS & INFORMATION

KPIs 2023:

- Total Revenue: $26.4bn
- Net Income: $1.8bn
- Market Capitalisation: $56.2 bn (As of 20.01.24)

Senior Management:
- Marc Rowan (Co-Founder & CEO)
- Richard Ressler (Co-owner)
- Martin Kelly (CFO & Partner)
- Byron Vielehr COO of Asset Management
- David Samber (Co-head of Private Equity)
- Matt Nord (Co-head of Private Equity)

Recent Buyouts:
- ADT (Professional services) in August 2023 for $1.6bn
- Petsmart (Retail) in for $1.8bn in July 2023 [US]
- United Living Group (Machinery) for $371mn in May 2023 [UK]
- Arconic corporation (Metals & Steel) for $4.6bn in May 2023 [US]
- Univar solutions (Chemicals) for $8.2bn in March 2023 [US]

MARKETS DATA

NYSE: Apollo Global Management, Inc. (APO)

Share price: $103.25 (as of 05.02.24)

- up 13% YTD
- up 48.2% in 2023
- 52-week High: $103.81
- 52-week Low: $55.16

Apollo has experienced impressive growth in 2023, nearly doubling in share price

Apollo has reported strong financial results throughout 2023, with increasing revenues and profits. In the past few months, the broader market has been positive towards alternative asset managers like Apollo, with investor confidence increasing.

Target Overview

The Restaurant Group (TRG) is a British-based company operating a portofolio of casual dining and pub chains. Its main brands are: BarBurrito (dining), Brunning & Price (pub), and its flagship subsidiary is the subject of the analyzed Transaction, Wagamama.

As of 2019, TRG operated about 400 restaurants and pubs across the UK and over 50 franchises across non-UK territories.

In recent years, TRG has faced numerous challenges. One of the main issues, which was the one that by far hit the entire dining industry the most, was the COVID Pandemic and the subsequent lockdowns that followed.

Revenue growth of The Restaurant Group has been fairly high in the last few years, although in decline from 38.45% in 2021 to 5.87% in 2023. A concern is its EBITDA margin which dropped from a high 32.82% in 2020 to a much lower 7.83% in 2023. Furthermore, the Net Income of TRG has been negative in the last few years, but it's projected to increase following Apollo's transaction.

The operational values of The Restaurant Group (TRG) are integral to their work culture and approach. These values include:

- **Make it Magic**: Focusing on delivering 'wow' experiences with passion in everything they do, for both customers and team members.
- **Keep it Fresh**: Leading with innovation and staying ahead of the competition.
- **Be Sharp**: Excelling in the basics and focusing on execution.
- **Own It**: Taking responsibility for the success of the business and working towards exceptional results.
- **Do it Together**: Believing in the power of teamwork and collaboration to achieve great things.

The Restaurant Group's stock has experienced a swing in prices over the past 3 years, reaching highs post-pandemic when demand for dining-out stabilised. The stock dipped around the end of 2022 due to poor financial performance but climbed higher as investors were informed of the incoming Apollo takeover. As of December 22, 2023 the stock was delisted from the London Stock Exchange.

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LBO Analysis

LBO MODEL - ENTRY AND EXIT ASSUMPTIONS

Entry Valuation		Exit Assumptions	
Entry EBITDA	3,104	Exit Date	2028
EBITDA Multiple	9,00x	Exit Multiple	9.00x
Entry EV	701	Exit Fees	5
EV/Revenue 2022A	0.79x		
EV/Revenue 2023E	0.75x		
EV/EBITDA 2022A	5.05x		
EV/EBITDA 2023E	9.58x		

Based on historical financial results, the entry multiple for the LBO model was **9.00x**. Exit multiple for 2028 assumed to be **9.00x**, with an estimated €5m in exit fees.

CAPITALIZATION TABLE - PRE AND POST TRANSACTION

Cap Table Summary

	Pre-trx	Post-trx	
		% prefs	% ords
One Equity	100.00%	0.00%	0.00%
New Sponsor	0.00%	98.00%	0.00%
Management	0.00%	0.00%	2.00%
Sweet Equity	0.00%	0.00%	0.00%
Total	100.00%	98.00%	2.00%

Pre-transaction ownership of Wagamama was entirely of the Restaurant Group.

Post-transaction Wagamama displays 98% ownership attributable to TRG, with a 2% participation of the Management Team.

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FINANCIAL FORECAST

	Actuals			Forecast	Operating Case					CAGR	
EURmm	2020A	2021A	2022A	2023FC	2024P	2025P	2026P	2027P	2028P	20-'22	22-'28
P&L											
Revenue	459.80	636.60	883.00	934.80	1,143.13	1,409.32	1,665.06	2,035.35	2,467.33	24.30%	17.56%
% revenue growth		38.45%	38.71%	5.87%	22.29%	23.29%	18.15%	22.24%	21.22%		
EBITDA	150.90	115.80	138.70	73.20	83.38	93.79	104.49	117.65	131.97	(2.77%)	10.32%
% EBITDA margin	32.82%	18.19%	15.71%	7.83%	13.91%	12.48%	11.41%	12.60%	12.16%		
EBIT	(95.10)	11.80	(49.70)	40.60	49.65	61.21	72.32	88.40	107.16	(19.45%)	17.56%
% EBIT margin	(20.68%)	1.85%	(5.63%)	4.34%	4.34%	4.34%	4.34%	4.34%	4.34%		
PRETAX INCOME	(132.90)	(35.20)	(86.80)	14.40	64.40	79.88	71.27	105.72	124.54	(13.24%)	43.27%
NET INCOME	(124.10)	(40.30)	(68.50)	10.80	35.22	56.35	45.70	66.65	82.39	(17.97%)	40.31%

Revenue growth for the model employed rises to a peak of 23.29% in FY2025P and sets itself at 21.22% in the terminal year of FY2028P. EBITDA margin standing at a stable 12.16% on FY2028P, implying a EV of £1,187.69mm.

CASH SWEEP

	Actuals			Forecast	Operating Case					CAGR	
	2020A	2021A	2022A	2023FC	2024P	2025P	2026P	2027P	2028P	20-'22	22-'28
Unlevered Free Cash Flow											
(+) BoP Cash	49.80	40.70	146.50	155.09	189.66	233.82	276.25	337.69	409.36	43.29%	17.56%
(-) Min Cash	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00		
Cash Available for Debt Service	47.80	38.70	144.50	153.09	187.66	231.82	274.25	335.69	407.36	44.59%	17.72%
(-) Interest (assumed i=5%)	4.76	0.59	2.49	2.03	2.48	3.06	3.62	4.42	5.36		
Cash Available for Mandatory Amortization	43.05	38.11	142.02	151.06	185.18	228.76	270.64	331.27	402.00	48.87%	17.72%
(-) Mandatory Amortization	-	-	-	-	-	-	-	-	-		
Cash Available for Dividends	43.05	38.11	142.02	151.06	185.18	228.76	270.64	331.27	402.00	48.87%	17.72%
(-) Dividends	-	-	-	-	-	-	-	-	-		
Excess Cash	43.05	38.11	142.02	151.06	185.18	228.76	270.64	331.27	402.00	48.87%	17.72%
(+) Min Cash	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00		
Cash EoP	41.05	36.11	140.02	149.06	183.18	226.76	268.64	329.27	400.00	50.54%	17.88%
Cash BoP	49.80	40.70	146.50	155.09	189.66	233.82	276.25	337.69	409.36		
Net Change in Cash	8.76	4.59	6.49	6.03	6.48	7.06	7.62	8.42	9.36		
Cash EoP	41.05	36.11	140.02	149.06	183.18	226.76	268.64	329.27	400.00	50.54%	17.88%

Use of cash for principal repayment amortized considering estimated minimum requirement for operational purposes.

RETURNS ANALYSIS

Return Analysis		2023A	2024A	2025A	2026A	2027A	2028A
Equity Contribution		(701.00)	-	-	-	-	-
Dividends		-	-	-	-	-	-
Preference Shares		-	-	-	-	-	-
Ordinary Shares		-	-	-	-	-	-
Total Cash Flows		(701.00)	-	-	-	-	1,187.69
IRR	**11.12%**						
MOIC	**1.69x**						

Equity contribution for acquisition amounted to **£701.00mm**. Exit EV of **£1,187.69mm**, with a corresponding an IRR of **11.12%** and a MOIC of **1.69x**.

SENSITIVITY TABLES

	Actuals			*Forecast*	*Operating Case*					CAGR	
EURmm	2020A	2021A	2022A	2023FC	2024P	2025P	2026P	2027P	2028P	20-'22	22-'28
Capital Employed											
Net Working Capital	(27.00)	5.70	14.30	3.50	3.55	3.63	3.75	3.92	4.13	(19.09%)	2.80%
NWC as % of Revenue	(5.87%)	0.90%	1.62%	0.37%	1.37%	2.37%	3.37%	4.37%	5.37%		
Delta NWC		32.70	8.60	(10.80)	0.05	0.08	0.12	0.16	0.21		

The projected changes in **Net Working Capital** are slightly positive, in order to account for the presence of both positive and negative historical changes.

Deal Analysis

STRENGTHS

- **Strong Brand Portfolio:** TRG, with Wagamama as a key brand, holds a strong position in the casual dining market. This represents an opportunity for Apollo to make sized returns while supporting market expansion of Wagamama's brand using its established global network

- **Resilience and Sales Performance:** TRG's main business, demonstrated resilience in challenging market conditions, evidenced by an 11% rise in like-for-like sales to dine-in customers. This trend continues throughout TRG's secondary businesses underlining the strong competitive position of the brand

OPPORTUNITIES

- **Market Expansion:** With Apollo's backing, there's potential for TRG and its brands to expand and strengthen their market position. Opportunity to exploit network to penetrare new markets

- **Operational Improvements:** The new ownership could bring fresh perspectives and strategies to improve operational efficiency. These opportunities include management team replacement and synergies with other companies in the portfolio

WEAKNESSES

- **Economic Pressures:** The broader hospitality sector, including TRG, faced increasing costs and economic challenges due to inflation. Need to pay careful attention to this aspect in the prospective future characterized by a climate of uncertainty
- **Management Turbulence:** There was turbulence in TRG's management, with several board members stepping down following the acquisition. Ken Hanna, chairman of The Restaurant Group stepped down following investors' pressures

THREATS

- **High Interest Rates and Inflation:** The economic outlook remains challenging with high interest rates and inflationary pressures, which can impact consumer spending in discretionary goods. Need to carefully monitor consumer behavior in the coming months following positive signals of reducing inflation
- **Competitive Market:** The casual dining market is highly competitive, posing a constant challenge to maintain market share. Differentiation is key and needs to be properly implemented in order to be successful.

Sources: ft.com.

GLOSSARY

Asset Turnover Ratio: The ratio indicates the efficiency of a firm to use its assets to generate revenue - calculated by dividing revenue by the total assets of a firm.

Capitalization Table: Breakdown of the company‘s ownership. It serves to show the pre and post transaction change in the composition of the equity in the company.

Current Ratio: The current ratio shows the ability of a firm to cover their short term obligations (liabilities) with their short-term assets - calculated by dividing current assets with current liabilities.

Net Working Capital: The difference between operating assets and operating liabilities.

Senior Notes: Debt that a firm issues which has the most priority to be paid back in the case of a bankruptcy.

Sweet Equity: any form of non-monetary equity that owners/managers of a company contribute to the business.

Terminal Growth Rate: Assumption of the rate that a company is expected to grow forever.

WACC: Cost of capital used to represent a firm's after-tax costs from all resources.

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Graphs:
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