12th September 2017

Travel & Leisure

Source: Eikon Thomson Reuters

Market data

EPIC/TKR	PPH
Price (p)	1005
12m High (p)	1020
12m Low (p)	665
Shares (m)	42.2
Mkt Cap (£m)	424
EV (£m)	1075
Free Float*	26%
Market	Main

**As defined by AIM Rule 26*

Description

PPHE owns, co-owns, leases, franchises and manages a portfolio of 4* hotels with 8,300 rooms in Europe, with a strong emphasis on Central London. Real net asset value per share is significantly higher than the share price.

Company information

CEO	Boris Ivesha
CFO	Chen Moravsky
Chairman	Eli Papouchado

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www.pphe.com

Key shareholders

Red Sea (Board)	47%
Molteno (Board)	16%
AroundTown Property	9%
Hargreave Hale	6%
Red Sea (Board)	47%

Next event

March 2018	Finals

Analysts

Steve Clapham
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PPHE Hotel Group

Strong results spark upgrades

PPHE reported interim results which were higher than our expectations and we are modestly increasing our forecasts for this year and next. Current profitability is constrained by a combination of cost pressures (labour shortages in London, weak sterling and business rates) and by ongoing renovation in London and Amsterdam which means that full operational capacity will only be achieved in 2019. The group has excess liquidity and is seeking to make investments, which we perceive positively given an outstanding track record. The rating remains extremely low for a company with this record and asset backing.

- **Interims:** The results surprised on the upside in spite of some significant cost pressures from business rate increases, labour shortages in London and the lower pound adding to costs. These will be a drag in H2 and have limited our upgrades. Underlying trends remain positive.
- **Strategy:** The group has a high growth trajectory from a combination of excellent assets, shrewd acquisitions of development sites and existing assets, and renovation of older properties. Its expansion in Croatia and substantial liquidity offer the opportunity for incremental growth.
- **Valuation:** The market cap continues to stand at a significant discount to the value of the hotel assets whose recent valuation showed a huge uplift, before the Waterloo deal. The real value is c.£18 per share with further upside in prospect. Hence the current discount will widen unless the shares perform.
- **Risks:** The company has debt, and the hotel business is susceptible to economic downturns, and can be affected by terrorist attacks. Currently, the London assets are suffering from a shortage of available labour which is adding to cost pressures from the weak pound and business rates.
- **Investment summary:** The discount to the real asset value seems anomalous in our view, although gearing used to be a pushback from investors. Financing deals illustrate that lenders are comfortable with the assets and the company has now realised further cash. The asset value continues to grow, and we believe the multiples, especially on price:book, are too low for a company of this quality and with its record.

Financial summary and valuation

Year end Dec (£000)	2015	2016	2017E	2018E
Sales	169.3	272.5	323.0	338.0
EBITDA	80.1	94.1	105.8	112.0
Operating profit	61.0	68.8	71.8	76.0
Underlying PBT	29.8	31.7	30.8	36.3
EPS (p)	71.5	67.9	62.2	71.7
DPS (p)	20.0	121.0	23.0	25.0
Net (debt)/cash (€m)	-397.7	-590.2	-562.8	-518.8
Net debt/EBITDA (x)	5.0	6.3	5.3	4.6
P/E (x)	14.0	14.8	16.1	14.0
EV/Sales (x)	4.9	3.7	3.1	2.8
EV/EBITDA (x)	10.3	11.4	9.7	8.8
Dividend Yield (%)	2.0	12.0	2.3	2.5

Source: Hardman & Co Research

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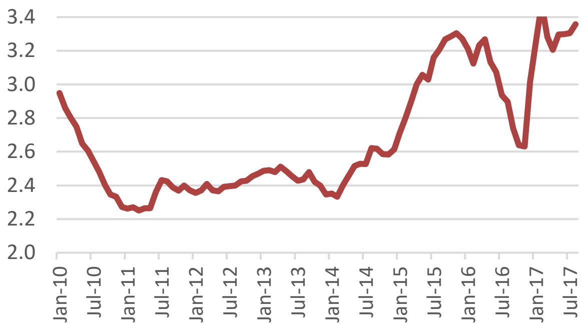
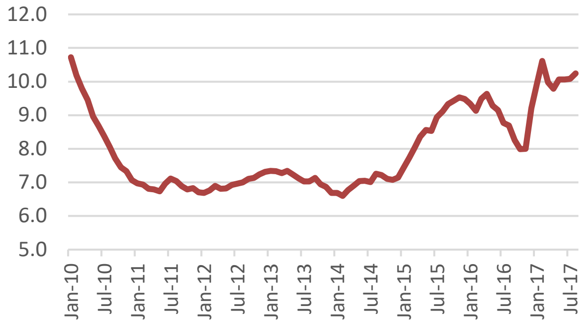
EV:Sales (Prospective)



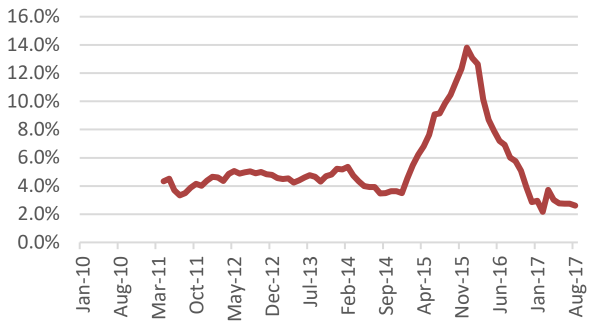
- The valuation is starting to trend down as the Croatian subsidiary has been consolidated and as the new hotel assets start to drive the revenue upwards.
- This trend will continue over the next 18 months.
- The rating looks modest given the growth record and the margins.
- We have adjusted the basis this year to reflect the market value of the Croatian subsidiary in the EV.

EV/EBITDA (Prospective)



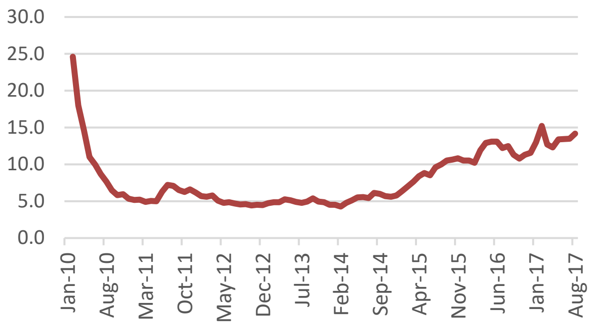
- The valuation on this measure has undergone a rerating
- We have adjusted the basis this year to reflect the market value of the Croatian subsidiary in the EV, which is more representative of the true minority value in the EV.
- The picture was complicated by the large level of assets under construction which inflates debt but is not fully reflected in the EBITDA forecast, but is now normalising.

Dividend Yield



- The yield chart is distorted by the special dividend.
- PPHE offers an attractive income, and a growing dividend.
- If management are unable to invest at satisfactory rates of return, another special dividend is possible in say 18 months' time.

Prospective P/E



- The company has enjoyed a steady rerating on this basis.
- The absolute level remains modest in our view, especially given the growth record and the asset backing.
- The stock remains at a discount to most larger hotel groups in the UK and internationally.

Source: Company data; Hardman & Co Research

Interim Results

Overview

The group reported a really impressive set of interim results, in spite of some formidable headwinds, including

- The tragic terrorist incidents in London in the period
- Pre-opening costs and build up of two large openings in London
- Refurbishment of half of a major hotel in Amsterdam for part of the period
- Inclusion this year for the first time of the loss-making Q1 period in Croatia
- Upward cost pressures, especially in London

In spite of these headwinds, the group showed a strong increase in EBITDA, which was equivalent to the increase we had factored in for the year, this for a company which has a seasonally stronger H2.

Overview of Results

	Reported			Like for Like		
	H1 2017	**H1 2016**	**Chg**	**H1 2017**	**H1 2016**	**Chg**
Total revenue	£141.8	£111.6	27.0%	£129.6	£111.9	15.8%
Room revenue	£98.4	£75.0	31.1%	£88.1	£75.0	17.4%
EBITDAR	£ 44.5	£37.1	19.7%	£41.9	£34.8	20.5%
EBITDA	£39.9	£32.5	22.9%	£38.0	£31.5	20.5%
EBITDA margin	28.1%	29.1%	(100) bps	29.3%	28.2%	115 bps
Reported PBT	£3.4	£12.1	-71.9%	N/A	N/A	N/A
Normalised PBT	£3.1	£2.8	10.3%	N/A	N/A	N/A
Occupancy	72.2%	70.5%	170 bps	72.1%	67.8%	430 bps
Average room rate	£115.8	£103.5	11.9%	£114.7	£103.4	10.9%
RevPAR	£83.6	£73.0	14.6%	£82.7	£70.1	17.9%

Source: Company data, Hardman & Co Research

The key group level statistics are shown in the table and we would flag the strong, double digit underlying, increase in room rate which combined with improved occupancy to deliver a strong increase in RevPAR, up 18% underlying. This drove a similar underlying increase in room revenue, which combined with the new openings led to a 31% increase in reported room revenue and a 27% increase in total revenue. These reported figures are also flattered by the weakness of sterling vs the Euro, which will be a more significant factor in H2.

This in turn drove a 23% increase in reported EBITDA, up £7.4m, which was reduced by higher depreciation and interest (mainly in the Croatian subsidiary) to a more modest improvement at the pretax level. We explore the trading performance in more detail by geographic region below.

UK

There was a significant increase in turnover, driven by a 10% increase in rates, offset by a small decrease in occupancy, which combined with the new openings at Waterloo and Park Royal to drive a 35% increase in room revenue and a 29% increase in total revenue. This led to a 24% increase in reported EBITDA, which was better than our expectations.

UK Hotel Results

	Reported			Like for Like		
	H1 2017	**H1 2016**	**Chg**	**H1 2017**	**H1 2016**	**Chg**
Total revenue £m	85.6	66.4	28.9%	75.8	66.4	14.2%
EBITDAR £m	27.1	21.7	24.9%	25.1	21.7	15.7%
EBITDA £m	26.0	21.0	23.8%	24.2	21	15.2%
EBITDA Margin	30.4%	31.6%	-1.3%	31.9%	31.6%	0.3%
Occupancy	81.20%	81.70%	-0.6%	81.50%	81.70%	-0.2%
Average room rate	143.4	133.5	7.4%	147.2	133.5	10.3%
RevPAR	116.4	109	6.8%	119.9	109	10.0%
Room revenue	60.5	44.8	35.0%	52.1	44.8	16.3%

Source: Company data, Hardman & Co Research

In one sense, these numbers are not THAT surprising given the two major new openings, but this was achieved in spite of a number of headwinds alluded to above. We were not expecting much contribution from the new openings, as they take some time to ramp up to full capacity, and there can be significant pre-opening costs, which are not capitalised.

We were relieved that the two significant terrorist incidents did not have a more significant impact on the market and on the group's business, given that the Westminster attack was very close to PPHE's Waterloo hub. We had been conservative in our forecasts, given the new openings, these attacks and the upward pressure on costs which the company discussed at the analyst meeting.

RevPAR was up 6.8%, and 10.0% excluding the new openings, while the RevPAR for the Greater London hotel market increased by 9.7% to £114.5, with a 3.2 point increase in occupancy to 79.8%, and an increase in average room rate of 6.2% to £143.6. In Leeds, rates were down and In Nottingham slightly up.

The fall of the pound post Brexit is having a significant impact on the group's labour costs in London. It has the effect of reducing immigrants' Euro earnings, significant where a large portion of earnings are remitted home, often to eastern Europe (akin to the Philippine philosophy). With the fall of the pound, and a strengthening

European economy (notably Poland), many lower paid workers have decided to return home.

Management talked of a shortage of 90 chambermaids, out of a complement of 400, which illustrates the extent of the problem. The group is resolving this by increasing wages, with chambermaids for example now earning quite a bit more than the minimum wage. In food and beverage, there is a smaller problem, with the staff being sourced largely from southern Europe, eg Spain and Italy, and able to augment their income through tips. The weakness of sterling is an issue for F&B input costs, however, and although they are attempting to source more locally, there is simply not enough local food production.

Given that the move down below £1=€1.10 has been quite recent, given that there are no immigration restrictions yet, and given that the pound may not stop here, the group is making some longer term plans to address this problem. Cost pressures are likely to be an ongoing feature, although the good news is that it affects all players and with demand strong, they have so far been able to keep margins flat.

The UK Government is still arguing about Brexit with Brussels and the hospitality industry including PPHE is fortunate in that the weakness of sterling increases the demand in London and allows higher room rates. Other industries may not be so fortunate, and this is an important consideration when looking at other UK stocks.

The group is also facing a steep (c.30%) increase in business rates, which is a £3m drag this year; they have appealed against the increase and management pointed out that business rates are c.0.5% of revenue in Europe but 6% in London.

Management appear confident about the new openings and there is a pipeline of a further 550 rooms:

- **Hoxton:** planned 320 rooms, although they are testing the market for value, and may flip the site or buyout their partners, depending on values ascribed. The area has become more competitive with other openings planned.
- **A40:** The group is filing planning applications for an additional hotel adjacent to the recently opened asset.
- **Battersea:** The group has the management contract for a new hotel on the Power Station site and this should open in 2020. The art'otel concept should work well with Apple hipsters, as the tech company opens its HQ in the development.

The outlook in the UK is one of continued cost pressure, but there should be some useful offsets in:

- **New Openings:** the Waterloo and Park Royal units (706 rooms in total) should start to drive growth, as they mature.
- **Riverbank:** the hotel redevelopment continues but once it has opened, there should be good scope for significant revenue improvement, as the renovations add to the room rate, and the hotel has been significantly expanded. The renovations have clearly impacted the current performance.
- **Sherlock Holmes:** This is currently being refurbished and should re-open next year, with a significant uplift in room rate, in this trendy area of London, with an entrance near the Chiltern Firehouse. Management indicated that an increase of £50 per night might be possible, which could mean a profit increase of c.£1.5m p.a. from this unit alone.

The outlook in the UK is positive, driven by a strong revenue increase in 2017/18 vs 2016; we do not expect margins to improve, given the cost pressures and lease costs at Waterloo, but the EBITDA growth should be good, and there will be a flow through to the PBT level. Importantly, the CEO was very positive on the outlook for London in the medium term, citing his 47 years of experience in the operation of London hotels. This is a strong management team, who remain positive on the London outlook.

Netherlands

The small decline in H1 Euro performance reflects disruption from the extensive renovation programme currently underway at Park Plaza Victoria Amsterdam, where only half of the rooms were available for part of H1, and all of H2. Room numbers declined at Park Plaza Vondelpark, after one of the hotel's three buildings was sold.

The Netherlands

	Reported in £		Likeforlike €		
	H1 2017	H1 2016	H1 2017	H1 2016	Change
Total revenue M	£24.9	£23.2	28.9	29.6	-2.4%
EBITDAR M	£7.6	£7.5	8.8	9.5	-7.4%
EBITDA M	£7.5	£7.4	8.8	9.5	-7.4%
Occupancy %	83.6	80.3	83.6	80.3	4.1%
Average room rate	£114.1	£104.0	132.50	132.80	-0.2%
RevPAR	£95.4	£83.5	110.80	106.60	3.9%
Room revenue M	£18.4	£17.0	21.40	21.70	-1.4%

Source: Company data, Hardman & Co Research

Therefore revenue was slightly down in Euros, with a greater impact on underlying EBITDA, down 7.4%. Room rates were slightly down but a good increase in occupancy helped RevPAR grow, although with fewer rooms, turnover fell.

The greater Amsterdam hotel market continues to be strong and RevPAR increased 8.1% to €114.1, with a 3.9% increase in average room rate to €145.1 and a 4.0% increase in occupancy to 78.6%. There have been a number of new openings in the city, and the strength of the market augurs well for the re-opening of the renovated principal asset there.

In sterling terms, the strength of the Euro flattered the H1 results and there will be an increased effect in H2, with the Euro at 1.08 as we write; the Euro is widely expected to continue to be strong, and this analyst has no reason to doubt that Euro – Sterling could reach parity, especially if Brexit discussions show no sign of resolution. But part of the reason for Euro strength is dollar weakness and that may have run its course, so we are assuming that 1.08 is a sensible rate for 2017/18. We shall certainly be wrong, but it's a sensible starting point, and our forecasts incorporate a slightly more conservative assumption.

Germany/Hungary

The first table shows the sterling reported results and the like for like in Euros as above. The second table gives a sterling like for like and a further adjusted Euro like for like which 1) excludes Park Plaza Nuremberg for the first five months of 2017, and 2) takes out the Park Plaza Prenzlauer Berg Berlin, the lease for which was terminated on 30 June 2016). In addition 3) the EBITDA data for both years have been adjusted to reflect the new freehold position of art'otel cologne and art'otel berlin kudamm (rental costs adjusted).

Germany/Hungary

	Reported in £		Likeforlike €		
	H1 2017	**H1 2016**	**H1 2017**	**H1 2016**	**Change**
Total revenue M	£14.4	£10.6	16.7	13.6	22.8%
EBITDAR M	£4.1	£2.7	4.8	3.4	41.2%
EBITDA M	£1.7	£(0.8)	1.9	-1.0	n/a
Occupancy %	72.1	67.4	72.1	67.4	7.0%
Average room rate	£81.0	£61.1	€ 94.10	€ 78.00	20.6%
RevPAR	£58.4	£41.2	€ 67.80	€ 52.60	28.9%
Room revenue M	£11.1	£7.9	12.9	10.1	27.7%

Source: Company data, Hardman & Co Research

We have not tried to replicate the company’s adjustments which we simply reproduce, but we use the adjusted like for like data to try to understand the underlying trends and then use the Euro data in the first table for our forecasts. Hopefully, this complexity is helpful rather than confusing.

Germany/Hungary LFL

	Reported in £		Likeforlike €		
	H1 2017	**H1 2016**	**H1 2017**	**H1 2016**	**Change**
Total revenue M	£12.0	£9.6	14.0	12.2	14.8%
EBITDAR M	£3.5	£2.5	4.1	3.2	28.1%
EBITDA M	£1.5	£0.7	1.8	0.9	100%
Occupancy %	75.6	67.0	75.6	67.0	12.8%
Average room rate	£74.3	£64.4	€ 86.20	€ 82.20	4.9%
RevPAR	£56.2	£43.2	€ 65.20	€ 55.10	18.3%
Room revenue M	£9.2	£7.1	10.7	9.0	18.9%

Source: Company data, Hardman & Co Research

Revenues like for like grew by 15%, which increase was almost doubled at the EBITDAR level. With the acquisition of freeholds, the rental expense disappears, and the EBITDA margin is much enhanced, and indeed EBITDA doubled like for like.

The hotel markets in Germany are strong, as would be expected given the economic backdrop. Hotels in greater Berlin reported a year-on-year increase of 4.3% in RevPAR to €71.6, while in Cologne, RevPAR increased by 18.1% to €85.5, and hotels in Nuremberg reported a 4.2% decrease in RevPAR to €72.2 (3.5% decrease in occupancy to 67.7% and a 0.7% decrease in average rate to €106.7). In Hungary, hotels continued to report improvements with RevPAR increasing by 17.0% to €58.8. PPHE’s hotels are seeing similar pattern, with the new opening in Nuremberg outperforming its local market.

Croatia

The Croatian business is performing well, but the first half effectively only has six weeks of normal business. The hotels open at Easter, but only start to fill up from mid-May and are really only reaching normal occupancy in June. The second half is a much more significant period for this segment. Encouragingly, the management were extremely enthusiastic about the outlook for this business.

Croatia

	Reported in £		Likeforlike €	
	H1 2017	**H1 2016**	**H1 2017**	**H1 2016**
Total revenue M	£14.5	£10.9	HRK 125.2	HRK 105.5
EBITDAR M	£0.5	£(0.2)	HRK 4.3	HRK (2.3)
EBITDA M	£0	£(0.8)	HRK ()	HRK (7.8)
Occupancy	47.0	40.1	47.0	40.1
Average room rate	£64.9	£52.7	HRK 561.2	HRK 507.7
RevPAR	£30.5	£21.1	HRK 263.8	HRK 203.6
Room revenue M	£8.4	£6.1	HRK 72.2	HRK 59.2

Source: Company data, Hardman & Co Research

The most relevant indicator here is that the H1 loss last year has been eliminated, in spite of the current year including the loss-making Q1, which was not included last year because of the timing of the acquisition. We had expected a loss at the EBITDA level of over £1m.

This is explained by a 10.5% increase in room rate and a 17% jump in occupancy, leading to a like for like 19% increase in revenue. But it was the plans for the future and the management's enthusiasm for current trading which particularly caught our interest.

I should add here that your analyst visited Croatia for the first time this summer. This was not some fabulous jolly at vast expense courtesy of PPHE but a trip to the south of the country, and I did not visit PPHE's assets. But I was impressed by the country, amazing views, lots of islands with beautiful clear water, many historic monuments, and some very nice hotels, and a lot more hotels which need considerable refreshment. This looks a clear opportunity for the group, and they have some exciting plans.

The quoted Arena Leisure subsidiary has c.£100m in cash and about 75% of this will be invested, roughly equal amounts we guess in:

- reserve - some cash will be set aside for future opportunities
- acquisitions in Croatia, preferably with local partners. The group is filing planning applications for an additional hotel adjacent to the recently opened asset.
- renovation of two existing hotels, one large which will be extended and the other smaller which will be refurbished
- redevelopment of existing properties: about 25% could be spent on redeveloping the existing campsites. The first test will be a 250-pitch site, currently used by caravans, where they are investing €5m to convert it into a a luxury camp (glamp) with modern tents, a swimming pool, and theatre. The idea is to offer the facility not simply to tourists but also as a corporate getaway

destination. If this is successful, the formula will be rolled out to the other seven sites.

- JVs in Hungary and Germany: management see opportunity to acquire and build assets especially in Budapest and Prague and in Germany, and apparently, and surprisingly, there is a lot of capital available for such investment in Croatia.

Management confirmed that summer trading had been strong, and that this had continued into September for the Pula hotels, where the shoulder months have been boosted by music festivals and an Ironman competition – this filled the hotel for a week, as competitors come out early to prepare for the event (and presumably eat quite a lot of high margin pasta).

Central results

PPHE charges the operations for centralised services and tries to manage this as a profit unit in its own right. EBITDA from central activities increased in the period, with activity levels considerably higher than last year. There was in addition a small property sale profit in H1 of £1.35m which is included "below the line" as a non-trading item.

Management and Holdings

£m	H1 2017	H1 2016
Total revenue	£17.9	£15.2
Revenue elimination	£(15.5)	£(13.4)
Total revenue	£2.4	£1.8
EBITDA	£4.7	£3.3

Source: Company data, Hardman & Co Research

Profit and Loss

The strong performance at the EBITDA line has been consumed by higher depreciation charges – the impact of Croatia and the opening of the new assets, mainly London – and some slightly higher interest costs, on a larger debt base. This has resulted in a slight increase in the normalised profit. Note that the real value of the assets are a multiple of book value and growing, so the depreciation, while important, is non-cash and more a book-keeping entry than a reflection of economics.

The table shows the reconciliation of reported to normalised profit which requires a lot of adjustments for the "one-off" items which are not part of the normal trading. Although a fast moving business like PPHE is incurring costs for refinancing etc on a regular basis, we think it's correct to exclude these items when looking at the underlying performance of the business and when looking at valuation.

P&L

£ '000	H1 2017	H1 2016
Revenues	141,770	111,641
Operating expenses	-97,290	-74,539
EBITDAR	44,480	37,102
Rental expenses	-4,552	-4,604
EBITDA	39,928	32,498
Depreciation and amortisation	-17,426	-11,798
EBIT	22,502	20,700
Financial expenses	-14,813	-13,569
Financial income	244	1,466
Other income	1,351	33,698
Other expenses	-928	-24,317
Income Units Interest Charge	-4,874	-4,253
Associate and joint ventures	-91	-1,638
Profit before tax	3,391	12,087
Income tax benefit	-414	168
Profit for the period	2,977	12,255
Profit attributable to:		
Equity holders of the parent	3,609	13,051
Minorities	-632	-796
	2,977	12,255
Basic and diluted earnings per share (in GBP)	0.09	0.31

Source: Company data, Hardman & Co Research

The tax rate has ticked up with the company formerly having been in a zero tax position; it is now providing for some deferred tax and we have increased our tax forecasts for this year and next. The minority interest is £0.6m loss, which suggests that the Croatian subsidiary made a loss of £1.2m in total, having been at break-even at the segmental EBITDA level, but at a small loss after depreciation and interest. This is purely a seasonal phenomenon.

We should add that the cash balances are currently contributing very little income, while the interest rate on the long term debt is considerably higher. This negative arbitrage provides flexibility, but is depressing current reported earnings, and this inflates the reported P/E.

Reconciliation of reported profit to normalised profit		
£ '000	**H1 2017**	**H1 2016**
Reported profit	3.4	12.1
Fair value movements on derivatives recognised in the profit and loss	-0.1	
Negative goodwill and capital gains after the acquisition of the remaining interests in Arena	-26.2	
Refinance expenses	22.9	
Loss on buy back of units from private investors	0.7	0.4
Fair value adjustment on income swaps with private investors of Income units in Park Plaza Westminster Bridge London	0.2	0.2
Other nonrecurring expenses	0.2	
Results Marketable securities	0.1	
Gain on sale building Park Plaza Vondelpark, Amsterdam	-1.4	
Forfeited deposits		-6.6
Normalised profit	3.1	2.8

Source: Company data, Hardman & Co Research

Cash Flow

The company is in a significant investment phase, with a capex programme running at close to £100m last year and this year, as well as the investment in the Croatian subsidiary. The Waterloo sale and leaseback deal has further enhanced the cash balances which are close to £300m today, with c.£200m in PPHE itself and £100m in the Croatian subsidiary. The offset is increased debt, as the former bank facility has effectively been replaced by a finance lease. As explained earlier and below, the company has ambitious expansion plans, but there is ample capacity, and the balance sheet has a significant real valuation surplus.

The table shows that in H1, the group generated £50m cash from operations and spent £20m on financing and invested around £100m. Financing has come from new loans, the H2 sale and leaseback and an equity raise in the Croatian listed subsidiary.

The balance sheet remains very comfortable and the group has an excess of liquidity which it is seeking to invest.

Cash Flows

£ '000	H1 2017	H1 2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Profit for the period	2,977	12,255
Financial expenses	19,687	17,863
Financial income	-244	-1,507
Income tax expense (benefit)	414	-168
Loss on buy back of Income Units sold to private investors	721	369
Gain on acquisition Arena		-26,180
Refinance expenses		22,971
Income from forfeited deposits		-6,541
Gain on sale of property	-1,351	
Share in loss of associate and joint ventures	91	1,638
Depreciation and amortisation	17,426	11,798
Cash from operations pre working capital	39,721	32,498
CHANGES IN OPERATING ASSETS AND LIABILITIES:		
Increase in inventories	-207	-114
Increase in trade/other receivables	-6,312	-7,256
Increase in trade/other payables	18,208	6,760
Cash from operations	**51,410**	**31,888**
CASH PAID AND RECEIVED DURING THE PERIOD FOR:		
Interest paid	-20,201	-17,980
Interest received	42	119
Taxes paid	-370	-29
Net cash flows from operating activities	**30,881**	**13,998**
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investments in property, plant and equipment	-81,058	-50,652
Proceeds from disposal of property, plant and equipment	7,146	
Investments and loans to jointly controlled entities	-250	
Net change in cash upon acquisition of Arena	-14,002	
Decrease in restricted cash	1,009	
Investments in marketable securities	-23,087	
Cash outflow before financing	-65,109	-50,906
CASH FLOWS FROM FINANCING ACTIVITIES:		
Dividend distribution	-4,642	-4.22
Issue of shares	380	
Draw down of longterm loans	41,738	591,686
Repayment of longterm loans	-10,918	-410,544
Buyback of Income Units previously sold	-1,900	-1,359
Net proceeds from minorities transactions	78,794	5,184
Net cash flows provided by financing	**103,072**	**181,127**
Increase in cash and cash equivalents	37,963	130,221
Net foreign exchange differences	3,413	4,609
Cash and cash equivalents at beginning	144,732	50,623
Cash and cash equivalents at end	186,108	185,453
Non cash items:		
Outstanding capex payables	2,206	9,827
Acquisition of freehold interests in hotels	8,268	

Source: Company data, Hardman & Co Research

Balance Sheet

The most important factor in the balance sheet is the significant surplus over book at current asset valuations, which is discussed in more detail in the outlook section.

Reconciliation of reported profit to normalised profit

£ '000	H1 2017	H1 2016
NONCURRENT ASSETS:		
Intangible assets	24,549	25,158
Property, plant and equipment	1,145,818	1,069,702
Investment in joint ventures	18,695	18,409
Other noncurrent financial assets	2,404	3,090
Restricted deposits and cash	5,241	5,235
Deferred income tax assets	1,009	713
	1,197,716	1,122,307
CURRENT ASSETS:		
Restricted deposits	25,213	25,513
Inventories	2,691	2,412
Trade receivables	20,218	12,576
Other receivables and prepayments	9,070	10,370
Investments in marketable securities	22,921	
Cash and cash equivalents	186,108	144,732
	266,221	195,603
Total assets	**1,463,937**	**1,317,910**
EQUITY:		
Issued capital	0	0
Share premium	129,527	129,527
Treasury shares	-3,208	-3,208
Foreign currency translation reserve	17,802	14,391
Hedging reserve	-649	-895
Accumulated earnings	182,176	159,814
Attributable to equity holders	325,648	299,629
Non controlling interests	91,890	30,573
Total equity	417,538	330,202
NONCURRENT LIABILITIES:		
Bank borrowings	666,275	642,120
Provision for litigation	3,605	3,392
Provision for concession fee on land	3,307	2,885
Financial liability re Income Units sold	132,188	133,983
Other financial liabilities	31,458	22,979
Deferred income taxes	9,536	9,345
	846,369	814,704
CURRENT LIABILITIES:		
Trade payables	14,978	10,754
Other payables and accruals	52,785	43,959
Bank borrowings	132,267	118,291
	200,030	173,004
Total liabilities	1,046,399	987,708
Total equity and liabilities	**1,463,937**	**1,317,910**

Source: Company data, Hardman & Co Research

Outlook

We have nudged up our forecasts for this year and next, but given the cost pressures being experienced in the UK, we have been deliberately conservative. Our forecasts for profits and cash flow are in the tables, and the changes are relatively modest. We would simply highlight the cash flow, where the sale and leaseback deal increases cash, and similarly the fund raising from the subsidiary minorities, which also boosts the cash position relative to our previous forecast.

This sale and leaseback deal warrants further comment because Waterloo had a book cost of £124m and an all-in cost, including "soft" costs of £125m; the valuation was £250m, with this doubling of value being achieved in under 3 years. The cost of course was only partly equity, and this is illustrative of a management team capable of delivering extremely high IRRs. In our view, this is remarkable, and normally management of this calibre attracts a premium stockmarket rating.

The position is similar in Croatia where the slides accompanying the results illustrated that for an investment of £79m, the Croatian market ascribes a value to PPHE's holding of £161m. Given the outlook for Croatia, and the company's investment plans as described above, this is likely to increase significantly over time.

Management indicated at the analyst meeting that they intended to invest c.£120m of the £200m cash on PPHE's balance sheet (excluding the cash in the Croatia subsidiary) by doing probably a number of deals to acquire assets in the UK. They have bids in currently both for individual London based assets, and for portfolios of UK assets. They continue to believe in the London market, although clearly it may be more difficult to achieve uplifts like Waterloo. They continue to explore opportunities for office to hotel conversions – there may be more opportunities with Brexit worries and with less scope to do office to residential given the overhang of supply and weakness in the top end of the London residential market. Management also plan to keep a substantial reserve of cash to exploit opportunities as they may arise, if markets cool.

The outlook is therefore one of continued underlying growth and of a strong liquidity position, giving the team flexibility to accelerate the growth through acquisition. Organically, the new assets should continue to boost the top and bottom line and as the renovations are completed in London and Amsterdam, there should be a further benefit over the next 24 months. The group looks well-placed.

Forecasts

Our forecasts for P&L and cash flow are shown in the following tables.

P&L	FY14	FY15	FY16	FY17	FY18E
UK Sales £	142.8	147.4	148.7	189.3	196.1
Netherlands Sales £	43.1	42.3	48.3	42.5	44.7
Germany Sales £	22.9	21.9	25.0	31.3	32.1
Croatia Sales £			46.1	55.0	60.0
Management Sales £			4.4	5.0	5.0
Total Revenue	**165.7**	**169.3**	**272.5**	**323.0**	**338.0**
UK EBITDA £	51.6	54.4	51.1	61.0	63.9
Netherlands EBITDA £	12.5	13.4	14.6	12.4	12.9
Germany EBITDA £	0.3	-0.4	0.9	3.9	4.2
Croatia EBITDA £	0.0	0.0	16.8	17.5	19.0
Management EBITDA £	11.6	12.6	10.7	11.0	12.0
Total EBITDA	**76.1**	**80.1**	**94.1**	**105.8**	**112.0**
UK EBITDA £	51.6	54.4	51.1	61.0	63.9
Depreciation and amortisation	19.6	19.1	25.3	34.0	36.0
EBIT	**56.5**	**61.0**	**68.8**	**71.8**	**76.0**
Margin	*34.1%*	*36.0%*	*25.2%*	*22.2%*	*22.5%*
Associates	-2.3	-1.9	-1.8	0	0
Other income	2.6	1.3	-0.2	0.0	0.0
Income units liability payments	-9.9	-11.6	-10.7	-11.5	-12.0
Interest	-20.4	-19.4	-24.6	-29.8	-28.0
Profit before tax (adjusted)	**26.8**	**29.8**	**31.7**	**30.8**	**36.3**
Tax	0	0.1	-0.1	-1.0	-2.0
Profit after tax	26.8	29.9	31.6	29.8	34.3
Minorities			-3.0	-3.5	-4.0
Earnings	26.8	29.9	28.6	26.3	30.3
Profit before tax (adjusted)	26.8	29.8	31.7	30.8	36.3
EPS (pence)	64.6	71.5	67.9	62.2	71.7
DPS (pence)	19.0	20.0	121.0	23.0	25.0

Source: Hardman & Co Research

Cash Flow

	FY14	FY15	FY16	FY17	FY18E
EBITDA	76.1	80.1	94.1	105.8	112.0
Working Capital	1.8	5.0	-12.8	-2.0	-2.0
Operating Cash flow	77.9	85.1	81.3	103.8	110.0
Interest - cash impact	-32.1	-32.5	-37.3	-41.4	-40.0
Tax paid	-0.1	-0.1	0.0	-1.0	-1.0
Cash flow after financial items	45.7	52.5	44.0	61.4	69.0
Capex	-37.0	-63.1	-87.7	-100.0	-15.0
Croatia transactions				80.0	
Acquisitions		-3.3	-22.0		
Buyback of income units	-1.7	-3.2	-1.3	-3.0	
Total capital outflow	-38.7	-69.6	-111.0	-23.0	-15.0
Cash flow after capex etc	7.0	-17.1	-67.0	38.4	54.0
Dividends	-7.1	-8.4	-50.6	-9.7	-10.6
Cash flow after dividends	-0.1	-25.5	-117.6	28.7	43.5
Share issues	0.2	0.6		0.5	0.5
FX/other/exceptionals	-0.3	1.9	-74.9	-2.0	
Overall move	-0.1	-23.0	-192.5	27.2	44.0
Opening Net Debt	-374.5	-374.6	-397.7	-590.2	-562.9
Closing Net Debt	-374.6	-397.7	-590.2	-562.9	-518.9

Source: Hardman & Co Research

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