

Exit National Express: No debt reduction in sight

| | | | |
|------------------|----------------------------|------------------------|--------------------------|
| Company: | National Express (NEX LN) | Market Cap: | £600mio |
| Industry: | Bus and railway operator | Net Debt: | £1,143mio (incl. leases) |
| Country: | US, Spain, UK, Germany | Revenue: | £2.8bn |
| Date: | 27 th July 2023 | Net Income: | £115.6mio (15.4%) |
| Dividend: | £41mio (5.5%) | Free Cash Flow: | £160.5mio (21.4%) |
| Entry: | £650mio | Exit: | £600mio |

Why exit National Express?

- Management talks about cutting debt, but has no specific plan and increased debt in H1
- Profit expectations for full year came in £60mio below my expectations
- UK labour pay agreement only valid for one year, which has caused losses this year
- Interest on refinancing comes in higher than estimated, bringing their total annual interest expense to £100mio
- No plans to sell their US business, which could mean an equity raise in 2026 to repay the hybrid bond
- Their investor relations team keeps ignoring me, which shows poor governance
- Their CFO seems to disrespect the CEO, answering strategy related questions ahead of him

Weak governance and poor numbers triggered the sale

Despite insider buying and strong volume performance, the weaker than expected UK and US profitability led me to sell the position. Usually, I try to stay away from activism, as management should be able to judge a situation better than me. However, when the valuation of a company declines continuously without the management trying to intervene, either with a trading update or a strategic change, I begin to reach out to show my ideas and gather the interest from management. With National Express/Mobico I have suggested to seek a buyer for their US business, as all their competitors have done so. Given the bad macroeconomic environment we are in, this sale might only achieve \$1bn instead of \$2bn in normal

times. However, the proceeds could be invested in UK Gilts and aligned with their debt maturities, reducing their interest expense by £50-60mio annually. At the current valuation, Mobico could return 10% annually to shareholders instead. Unfortunately, the head of investor relations, John Dean, ignored me and then wouldn't arrange a call with management or himself. I understand that it might be hard to sell the US business at a time when the profitability is way below 2019 profitability. Nonetheless, it could be communicated to markets that this would at least be an option to repay the hybrid bond in 2026.

US business sold scenario vs. competitors

| North America sold | Revenue in \$mio | Operating Profit in \$mio | Cash received in \$mio | Multiple |
|--------------------|------------------|---------------------------|------------------------|----------|
| Stagecoach | 619 | 22 | 271 | 12.49x |
| FirstGroup | 3,800 | 180 | 3,066 | 17.03x |
| Mobico* | 1,570 | 157 | 2,000 | 12.74x |

Figures use 2019 numbers and exchange rates

*to be sold scenario (very positive scenario)

A negative correlation to interest rates is luring short sellers

Since May this year, Mobico's share price performance began negatively correlating to 5yr UK Gilt yields. This has led short sellers to become active in the name and is indicating that there is concern about Mobico's high debt load. Analysts have raised concerns regarding the high debt and also wondered about potential disposals. When I entered National Express 31st May, I believed interest rates might have peaked. However, during June the UK yield curve moved up to 1% higher and current central bank guidance continues to surprise me as PPI is negative and CPI is coming down just with a lag due to the Ofgem energy tariff that lags behind by around 5 months. The uncertainty of higher rates have helped me cut the position quickly on the day of the half year results were released as they increased debt further. Although the current valuation of Mobico's equity is close to £500mio (my downside scenario), I would be cautious on entering the position again given the weak governance and a potential equity raise further in the future.

5yr Gilt yield (turquoise) vs. Mobico share price (navy blue) last 3 months



Source: Tradeview

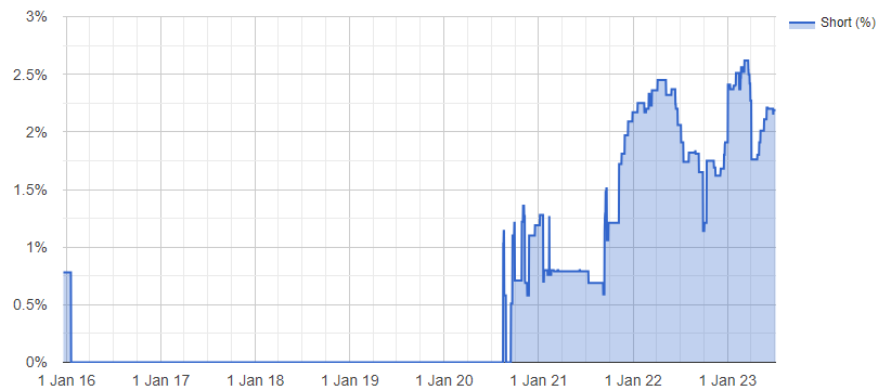
Mobico short seller activity

Disclosed positions in NATIONAL EXPRESS GROUP PLC (NEX)

Notice: We no longer track disclosures after they drop below 0.5%. It is possible that the manager still holds a short position even if we are showing it as zero.

| Fund | % short | change | Date changed |
|---------------------------------|---------|----------|--------------|
| GLG Partners LP | 1.10% | ↑ 0.04% | 28 Jun 2023 |
| Systematica Investments Limited | 1.09% | ↓ -0.01% | 7 Jun 2023 |
| Total | 2.19% | | |

Chart - changes in disclosed short position over time



Source: Shorttracker.co.uk



Legal Disclaimer

The contents of this publication have been prepared solely for the purpose of providing information about AozoraStep Capital LLP and the services and products it is intending to offer, which are targeted for professional investors only. The opinions and views expressed are those of AozoraStep Capital LLP, may change without notice and should not be construed as investment, tax, legal or other advice. AozoraStep Capital LLP does not guarantee the completeness and accuracy of the information provided and all content can become out of date. Products or services mentioned on this site are subject to legal and regulatory requirements in applicable jurisdictions and may not be available in all jurisdictions. Accordingly, persons are required to inform themselves and observe any such restrictions. In respect to investments described in this document, past performance is not a guide to future performance. The value of investments and the income of any financial instruments mentioned in this document may fall as well as rise and may have tax consequences. The performance of the investment strategy that AozoraStep Capital LLP is planning to offer is based on a personal track record and approved by Sedulo for the time period Q1 2019 - Q1 2021, only with further examinations being done on an occasional basis. AozoraStep Capital LLP is currently not authorized and regulated by the FCA, and therefore, is not allowed to provide financial products and services. AozoraStep Capital LLP is registered in England and Wales with registered number OC436835. Registered Office: 57 Lansdowne House, Berkeley Square, London W1J 6ER, United Kingdom. Reproduction or distribution of any materials obtained in this presentation or linking to this presentation without written permission is prohibited. Reproduction or distribution of any materials obtained on this website or linking to this website without written permission is prohibited.