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Britain's boozers: two bounce-back belters for 2021

Sam Volkering, Editor

Dear reader,

> *Yes, there will be some type of a decline without a question in the next 10 to 20 months and it will be earth shaking, it will be sabre rattling and will have Wall St. in a tizzy and it will create headlines that will dwarf anything that has happened before this point in time.*

That's Paul Tudor Jones speaking in *Trader*, a documentary filmed in the year leading up to the 1987 "Black Monday" market crash.

The significance of this late 80s documentary is the fact that Jones had seen the rise of one of the greatest periods of investment in US history. In fact, the documentary starts off by saying,

> *It is March 1987, the third month of one of the most dramatic rises in the history of the stockmarket and Paul Jones is taking a holiday…*

Jones is a futures trader, everything from commodities to precious metals and energy. But his speciality was stock index futures. The documentary is now 33 years old, but is worth a watch if you can dig it up online. Note: I would add the link myself, but I'm not 100% sure if it's a copyright violation or not!

It's a look into the markets and traders who soaked up the excess of the market in the 80s – that alone makes it a fascinating watch.

But it also gives Jones the centre stage for his call about one of the greatest stockmarket crashes of all time. The quote I showed you at the top is Jones' opening statement in the film, in early 1987.

But in December 1986 he had a strong position in the market, predicting it was set to soar.

He explains that around this time, "… everyone has to be negative walking in in the morning looking at the newspaper, looking at the fact the bonds are down, and yet [the market futures] are maintaining an enormous premium to the market spot."

All the negatively is there thumping at us, but the market isn't going down. The market continues to build energy, and the short sharp downturns we're seeing haven't broken the market

– which indicates the market is set to pop higher.

Jones predicted about another 40% in the Dow Jones Industrial Average (DJI) on the upside from late 1986 and then – stormy clouds from there. This thesis was the incredible correlation to the market boom and bust of the 1920s.

Jones was predicting something coming, a massive crash with “unprecedented volatility” that will, “leave people gasping”.

He predicted the market continuing higher into Q1 of 1987 and then towards the end of 1987 the market retracing and crashing, dramatically.

He made some astronomical calls buying into the market in late 1986, riding the profit into 1987 and then moving against the market in preparation for its huge correction.

He was almost exactly correct in the timing and direction the markets took from that point.

The chart below is the Dow from 1 July 1986 to 1 July 1988.

It’s exactly as Jones predicted.

His call and moves in the market were what you’d call a “contrarian” play. He moved to a downbeat position, a position where he believed the market would move in one direction while everyone else said otherwise.

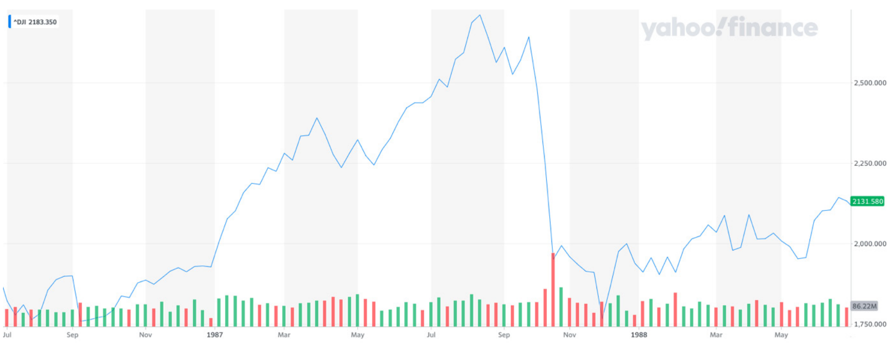
Jones made the unpopular decision, but ultimately the right one when the masses were too caught up in the good times to ignore the fact bad ones were right around the corner.

From January 1985 the Dow rose from 1,286 to 2,709 by late August 1987. That’s a swift rise of 110% in just two and a half years.

Then over the space of about four days, with Monday 19 October being the worst (Black Monday) the markets crashed almost 30%.

At this point the market sentiment, fear and despair that had besieged the market was truly set in with investors.

The next move to make was again the contrarian play. The move against the market. The old contrarian saying, “buy when there’s blood in the streets”.



Source: Yahoo Finance

On Monday 19 October 1987 there was blood in the streets.

Jones had prepared for this eventuation – in fact, he predicted it a year before it happened.

He had the nous to make the rights calls at the right time even when the popular, widespread sentiment didn’t agree. Conviction, courage and an awareness of managing risk is what made his moves so successful, so legendary.

The strategy: be contrarian

There’s a lot to learn from traders like Jones and their stories in previous market crashes.

How he played the market in 1986 and 1987 is one that always springs to mind – it’s considered one of the greatest market calls in history and it helped make him a bundle of money.

Perhaps the most important lesson to learn from his story in the late 80s is his willingness to make a move based on his own analysis and conviction and moving against the popular grain.

It was by no means the consensus view. It was unpopular when the market was shifting higher and higher and higher. It was contrarian. It was also right.

You can take these lessons from the crash of 1987, the crash of 2008, the crash from 2020 and put into play the same kinds of strategies to be a winner in current markets.

These moves are always apparent and don't necessarily have to play out immediately, but if you're prepared to invest in this current market with conviction, courage and the right capital risk management, I believe the conditions that exist right now are some of the best we'll ever see in the UK markets.

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We can't trade the markets and peaks and troughs from history. Too late to do anything about that.

What we can do is play the ball we face today and take our best swing for the fences.

What I'm saying is that we should channel our inner 1986 Jones and make the contrarian play now. It's not a complex strategy, it's simply to use this window of opportunity to buy into stocks that were most viciously hit from the crash in March and haven't yet recovered.

Despair has existed in the UK market, and while there has been elements of a market recovery, there are a huge number of stocks that are still reeling from this market crash yet still stand to bounce back even from their current trading positions.

There is still much risk in taking this kind of position. The fears of the impact of Covid-19 haven't left the community. They remain and they continue to shackle the market, in particular the UK market.

My view is that soon enough, those shackles will break. We've now seen just this week, how quickly things can change and move once good news about the light at the end of tunnel arrives.

Just one early announcement of the potential of a vaccine kicked the market in the backside so hard it reverberated around the world.

We weren't able to predict the response to the pandemic we've faced this year. I doubt anyone really did. We couldn't have expected the government response to it by shutting down economies and effectively single-handedly crashing the market.

But what we can expect is that with these measures in place, when they are released in full and the restrictions disappear, when borders are opened again, when you can walk into a shop without having to wear a mask, when you can stand behind someone in a queue without them freaking out, the market will be wildly different from where it is now.

This is a view that I've maintained throughout the period from the market bottoms in March through to today. And I've been preparing since your last recommendation to deliver to you more of the beaten-down stocks that I think are primed to bounce back as the world moves beyond the Covid-19 debacle.

The thing which I wasn't able to anticipate was the release of the recent Pfizer vaccine announcement. That caught us off guard. The good news however is it's not too late to make a move into these Covid beaten-down bounce-back belters.

What happened this week on the market, the explosion that took place when Pfizer released the vaccine success announcement, shows us just what's in store if you've got your positions in these kinds of stocks early as the world wakes up to the fact things won't be like this forever.

That's why today I'm presenting two new bounce-back belters to you that I believe are primed to soar as we leave 2020 behind us.

Introducing your first bounce-back belter…

The City Pub Group (LSE:CPC) is one of those great stocks that does exactly as it says on the tin. It's a pub group that owns and operates a number of pubs across the country, with a focus on London and a number of Britain's "cathedral cities".

What you won't find is its estate of pubs all branded "The City Pub Group". They are what you'd call "free houses" with a focus on individualism and what I'd consider to be the upper-end of the pub game.

The term "gastropub" gets bandied about quite a bit, but it's a term that fits the bill. Pubs that focus on a high level of quality in their total offering across food, atmosphere, the establishment itself and the service that's delivered.

Of course, its pubs also shift plenty of booze, again with a focus on independent brewers, craft alcohol selections and the kinds of higher margin offerings that take its business model and its pubs to that step-up from most people's local corner "boozer".

It's a model that works, which I've seen work in my native Australia. Successful pub operators not only know how to tailor to the right market with the right offering, but they know how to extract maximum margins from their patrons without being overpriced and undervalued.

Its pubs are located in the areas where they can affect this business model, with pubs in London (Wandsworth, Chelsea, Central London, Covent Garden, Clapham), Bath, Brighton, Cambridge, Oxford and Cambridge (just to name a few).

All in all, it's got 48 free houses and a growing stable of pubs and accommodation that up until this year were in a period of growth.

In June this year City Pub Group released its full-year (ending 29 December 2019) results for 2019.

It had increased revenues by 31%, like-for-like sales 1.7% and adjusted profit before tax 4%. Its profits were £1.3 million, down slightly from a £2 million profit in 2018.

The company is also strongly asset-backed with £97 million of freehold and leasehold properties as at 28 June 2020. The net book value of the company alone, when you also add fixtures and fittings, comes in at £110 million (as at 28 June 2020).

Looking at its balance sheet again at 28 June 2020, the company is in a net asset position of £96.8 million. All this on a current market capitalisation valuation of just £86 million. For me this puts the company as one of the best under-the-radar value stocks on the UK market.

Of course, we can't ignore the fact its revenue model is in a precarious position right now. Simply put, if its pubs are shut, there's no money coming through the door.

Its pubs were shut in the first lockdown in March. It had to swiftly ensure the company had liquidity to remain a going concern, which it did – providing it with liquidity as it explains, "… well into 2021 and the long-term future of the Company."

It trimmed staff, reduced its costs base and took the time to streamline the business to ensure it could operate lean to get through the crisis without any certainty about how long it would last.

It did what all smart companies would do and strengthened the company in a time of utter devastation.

Don't underestimate how challenging this year has been for a company like this. To have your business forcibly shut overnight by the government would kill many who were operating on the brink before all this.

City Pub Group was strong, profitable before it all, and that's the position I'm expecting it will return to as we now move beyond this crisis that's plagued the market since March this year.

The company also has a strategy of acquisition and refurbishment, ensuring it retains the individualism but increases the quality of pubs as the company looks to grow.

I believe that as we move out of this 2020 Covid-led mess, City Pub Group is one such company that stands to grow faster than others due to this acquisition strategy.

I'm expecting consolidation within the pub industry, as smaller independents that have been pushed to the brink in 2020, will look to either exit the industry or fish for larger groups like City Pub to come along and acquire.

Likewise, I would expect City Pub Group to be on the hunt for quality estate in the pub sector, as it looks to add to and grow out the company. That period of transition from an uncertain Covid-situation, now looks to be clearing and we finally see a pathway that has a greater degree of certainty out of the crisis.

It must also be said that its stock price has bounced from its March lows of 36.43p and is now trading around 83p. That's a hefty rise already. But I believe where it's at now still presents a significant opportunity to buy into a small-cap UK pub owner and operator primed for a bounce-back recovery to pre-Covid levels.

Now, I also believe City Pub Group to be just one smart play in an area of bounce-back potential that this market has to offer. There is another…

What's better than one bounce-back? Two of course!

Your second bounce-back belter isn't a far cry from City Pub Group – actually, it's technically a competitor…

Mitchells & Butlers (LSE:MAB) is an operator of pubs and restaurants across the UK. In fact, within a five-minute walk from my own house is one of its pubs that falls under its "Premium Country Pubs" group.

Another, which is perhaps a ten-minute walk from my house, is an Ember Inns pub that I frequent with my dog in summer when I need a cold pint before trundling over to the park.

Needless to say, over the years I've contributed to the bottom line of Mitchells & Butlers and it's very likely you have too.

> The pub and restaurant industry has the capacity to bounce back faster than any other industry that's been crippled by the crisis beset on us this year.

The very first place I went to after the first lockdown was eased was my local pub for dinner and drinks with my wife. The place was booked out, and before the latest lockdown, was booked out regularly.

If we're to move out of this crisis, then I believe people will realise how important it is to be able to do something as simple as go out for a meal and a drink with family and friends. They will appreciate this simple pleasure in life all that much more.

And I believe it will be a boom for the pub and restaurant industry, of which Mitchells & Butlers is perfectly placed to capitalise on.

I'd consider Mitchells & Butlers a more holistic pub and restaurant operator. Its venues range from, well, let's face it you'd probably call them a little "dingy" right through to the higher end gastropubs that I described City Pub Group as really aiming at.

Some of the brands that Mitchells & Butler operates you'll be familiar with, including:

- Vintage Inns
- Harvester
- Toby Carvery
- O'Neill's
- All Bar One
- Miller & Carter
- Premium Country Pubs.

That's not all the brands, but it gives you a good insight as to the variety and scope of the pubs and restaurants it operates.

The story about why Mitchells & Butlers is appearing now as a recommendation is very clear as it's the same rationale as to why City Pub Group is being added to our portfolio.

These are two companies that were in an industry that was savagely beaten by the actions and restrictions that were placed on us in 2020. They're both still suffering at the mercy of lockdowns and the impact to their businesses.

But I don't expect this to be a long-term situation they have to deal with.

The pub and restaurant industry has the capacity to bounce back faster than any other industry that's been crippled by the crisis beset on us this year.

They can scale up operations a lot faster than many others. That be the recruitment of staff, the provision of "regular" services and the ability to return to more normal, pre-Covid trading.

That's why I believe their path back to trading conditions pre-Covid will be faster than all other industries crippled by the events of this year.

If you look at Mitchells & Butlers' full-year performance for the 2019 year, ended 28 September 2019, before everything kicked off, you can see a robust company:

- Total revenues of £2.2 billion
- Operating profit of £297 million
- Profit before tax of £177 million
- Earnings per share of 33.5p.

All of those figures were an increase from the year prior.

It had 1,748 pubs, bars and restaurants in its estate, more than 80% being long-leasehold and freehold. It was also looking to the future with innovation in technologies to improve its customer and staff experiences.

It noted in its full-year results:

> *During the year we have developed our technology to facilitate an improved online booking experience, have developed an employee app allowing our staff greater flexibility and have continued to work with Just Eat and Deliveroo, with 273 sites now offering delivery. In addition to this, we have three delivery only brands in trial, utilising existing kitchens which have additional capacity.*

This was a group that was growing, innovating and a great company before 2020 kicked off.

But then 2020 did kick off, and just like City Pub Group, Mitchells & Butlers was ravaged by the market.

The lows in March after the initial market crash and first lockdowns arrived saw Mitchells & Butlers' stock price plummet to 92.5p as a 52-week low.

It had been trading up around £4.60 in December 2019.

The shutdowns, lockdowns and restrictions hurt the company. It will continue to hurt until it is able to fully reopen its entire estate again. There may even be a situation where certain sites will need to be permanently closed, but like City Pub Group, there may also be potential for new sites to be acquired.

Either way, the company announced liquidity measures in June to ensure it survives this crisis and come out the other side. As it explains:

> *On 12 June the group announced revised financing arrangements that had been agreed with our main creditors to provide a platform of both additional liquidity and improved financial flexibility in order to meet the challenge presented by Covid-19. The group currently has unsecured cash balances of c.£100m, in addition to undrawn committed unsecured facilities of c.£140m.*

It will get through this. I also believe the company could come out of the other side even stronger than before it went into 2020. It reinforces this by saying in its recent half-yearly update:

> *In the short to medium term, our focus will be on successfully re-opening the business in the current challenging environment, ensuring the safety of our team members and guests, and on growing the business back to, and beyond, the levels of trade that we were enjoying before the pandemic.*

While there are financials to consider for 2020, these numbers are also an anomaly due to the impact on its business model and industry because of the Covid-19 crisis. Hence, it's important to note them, but in our view of where I expect the company to return to, 2020 becomes somewhat of a "write-off" due to everything that's taken place.

What will be the real litmus test is its ability to deliver in 2021, assuming that restrictions and lockdowns are eased. If Mitchells & Butlers can even just reach where it was before 2020, then we could be looking at a potential 110% upside from its current trading price.

This is based on the pent-up demand due to restrictions and closures of its pub and restaurant estates during this year's crisis. Under more normal, less restrictive operating environment, I don't see any reason why Mitchells & Butlers couldn't achieve the same kinds of revenues and profits it was achieving before the Covid-19 crisis.

If that takes it back to the same kind of market valuations as before, then the upside is significant.

Now, while it was hit hard in March, the stock has recovered somewhat and now trades around 215p. Again, like City Pub Group, that's a big leap higher from the lows, but it still remains suppressed from its December 2019 highs. The stock got a big kick along this week from the Pfizer announcement as well, but it is still more than half its value from December 2019.

I see Mitchells & Butlers as another bounce-back belter as we come through the Covid-19 crisis and back to the world we once knew.

Risks to consider for both

While I'm hugely positive about the bounce-back potential of City Pub Group and Mitchells & Butlers, there's obviously still a lot of risk involved here too.

These aren't complicated businesses. They do run on small margins, but they are both leaders in the industry.

These moves into them now, isn't a complicated strategy – it's a pure contrarian play into an industry and two stocks I think are primed to bounce back hard and fast.

They both exist in an industry that in no way could have foreseen the mess that would be thrown at them in 2020. They're both companies that were smashed in March and at one point looked like they may not survive had things got even worse in 2020.

> I'm making the call the news will progressively be good, and get better.

But now even though the stocks have taken a leap forward with the wider market this week, you'll find they're still trading at more than half their pre-Covid values.

That means if we clear the current crisis, if the world pushes past 2020 and into a more positive, optimistic, "normal" way of life again, then the potential upside I see from City Pub Group to bounce back is in the realm of 159% from here and Mitchells & Butlers 110%.

What's important in this situation is the nature of this strategy. There's still a lot of uncertainty in the market and amongst investors. Even with the potential for a successful vaccine imminently on our doorsteps, the market won't be satisfied until the vaccine is in the hands of people and being administered. Not until cases fall and deaths become almost negligible will full confidence restore.

That means there could still be considerable short-term volatility ebbing and flowing on good news or bad in relation to a Covid-19 vaccine. Good news is good for stocks like City Pub Group and Mitchells & Butlers, bad news is bad for their stock prices.

I'm making the call the news will progressively be good, and get better.

There's also significant political risk here too. Now you usually don't associate political risk with two pub and restaurant stocks – but clearly this year we do.

We're still in a nationwide lockdown (although my local high street begs to differ). And pubs are supposed to be shut, aside from a few conditions in which some can remain open. They say it's going to end at the start of December. They say that we'll not go into another national lockdown again.

I don't trust a single thing the government tells us in relation to that. And even if they don't send us into another national lockdown, there is likely to still be short-term regional restrictions until the Covid-19 cases are negligible and deaths are nearly non-existent.

That's why the news of a vaccine was taken so well by the market.

Should harsh restrictions on this industry remain and continue to impact the footfall and revenue opportunities of City Pub Group and Mitchells & Butlers, it's going to be a handbrake on their stock price.

You should be prepared that the path to recovery may take longer than expected in this situation, or worse, it hits their stock price in a negative way, taking them into a loss position.

Also to many, investing in these kinds of stocks while the industry is reeling isn't the most popular thing to do.

Much of the community is still calling for more lockdowns, and for things to remain under control and restraint. This move is the ultimate contrarian play.

I expect in the next few weeks more positive vaccine news to come. I expect that as we turn into 2021 the world will get the pandemic under control and the markets will then turn up a gear.

I don't believe waiting for that to occur first and then investing is the way to do it.

I believe investment should be now, ahead of the masses, into these areas that stand the best potential to bounce back to previous conditions the fastest.

City Pub Group is also a small-cap play with a market capitalisation around one tenth that of Mitchells & Butlers. That's due to the size and scale of both companies. It does bring another element of risk to City Pub Group as a small-cap stock and you should ensure that you manage your capital risk in these two plays accordingly.

However, in my analysis, the pub and hospitality industry can bounce back fast as demand continues to build particularly during the current nationwide lockdown.

I don't expect going to the pub for a drink and a feed will be as terrifying to people as sitting on a six-hour flight wedged in next to a complete stranger might be. This positions the pub and hospitality industry to recover with greater speed than other Covid-ravaged industry.

I see these two in particular bouncing back fast and hard as the good news around control of the virus comes over the coming weeks and months. I see taking a position in that industry now with City Pub Group and Mitchells & Butlers as the most obvious investment play to make.

Buying instructions

The City Pub Group (LSE:CPC) stock is trading at 83p with volume around 150,000 per day. It carries a market cap of £86 million and could see another sharp rise from our recommendation.

The stock has already bounced hard this week off the back of the Pfizer vaccine announcement. However, the stock price is still at levels where I see strong upside opportunity for investors that are willing to take a risk, and make that contrarian play while the wider market still sits on their hands.

See buying information at the bottom of this page.

Mitchells & Butlers (LSE:MAB) stock is trading at 215p with average volume around one million stocks per day. It carries a market cap of £922 million and I consider this to be a very liquid stock.

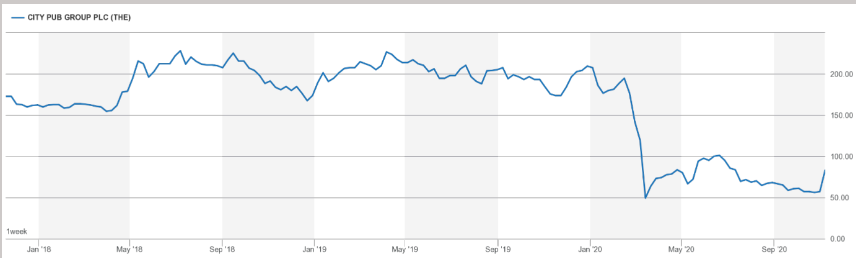
The stock has also bounced hard this week off the back of the Pfizer vaccine announcement. However, just like City Pub Group the stock price is still at levels where I see strong upside opportunity for investors that are willing to take a risk, and make that contrarian play while the wider market still sits on their hands.

See buying information on page 9.

Regards,

Sam Volkering
Editor, *Frontier Tech Investor*

Action to take:	**Buy The City Pub Group (LSE:CPC)**
Ticker:	LSE:CPC
Price as of 12.11.20:	83.00 GBp
Buy up to:	100p
Market cap:	£86.12 million
52-week high/low:	215.70p/36.43p



Action to take:	**Buy Mitchells & Butlers (LSE:MAB)**
Ticker:	LSE:MAB
Price as of 12.11.20:	215.00 GBp
Buy up to:	230p
Market cap:	£922.78 million
52-week high/low:	483p/92.30p

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