

09-Feb-2021

**SATS ASA** (SATS.NO)

Q4 2020 Earnings Call

## CORPORATE PARTICIPANTS

### Sondre Gravir

*Chief Executive Officer, SATS ASA*

### Cecilie Elde

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## MANAGEMENT DISCUSSION SECTION

### Sondre Gravir

*Chief Executive Officer, SATS ASA*

Good morning, everyone, and welcome to the SATS Fourth Quarter Presentation. My name is Sondre Gravir, the CEO of SATS. And together with me here today, I also have Cecilie Elde, our CFO. We will not have a live Q&A directly following the presentation today, so please follow up with any questions you might have with our responsible, Stine Klund, either on mobile or e-mail. We will also have a Q&A session for the analysts following SATS later today.

As usual, I will give you an operational update to start with and then Cecilie will cover the financials before we end the presentation commenting on the outlook. 2020 has financially been significantly impacted by the pandemic and the related governmental-imposed club closures, both through the direct effects of revenue loss during the closures and through the indirect effects mainly related to lower sales during closure affecting the member base and Q4 was no exception. The member base coming out of Q4 was 628,000. The top line summed up to NOK 846 million, representing an 18% decrease compared to last year. Adjusted EBITDA before IFRS 16 impact was negative by NOK 32 million, 120% lower than last year. Cecilie will come back to the financials more in detail later in the presentation.

If we take a step back and look at the restrictions throughout 2020, we see significant differences between the countries we are operating in. And in Q4, there have been several changes especially in Norway and as a result of the second wave of the pandemic.

We have been very active in the dialogue with both national and local governments and politicians in order to give input to the restrictions and to accelerate our opening dates. We have been following the governmental restrictions and recommendations in the different markets and adapted our operations continuously. Our clubs in Sweden and Finland were only closed for two and six weeks respectively in 2020 during the spring while our clubs in Norway and Denmark have been closed for several months throughout the year.

Then let's look at the situation in the different countries as of today. In Norway, 71 of our clubs have been closed for a longer period of time during Q4. The status changed last week as we opened most of our clubs around Oslo in the so-called [ph] Ring Two (03:12) municipalities, Wednesday and Thursday. And the clubs in Stavanger will open on Friday. Then on Sunday, unfortunately, we were forced to close our clubs in Bergen. Hence, today, we have 33 SATS clubs opened and 45 closed in Norway. And we have 16 Fresh Fitness clubs opened and 15 closed. We are operating the open clubs under strong restrictions that we will describe later on.

In Denmark, we operated the clubs until December 9 with strong restrictions. Then on December 9, the government imposed a new lockdown in the Danish society and we closed all our clubs and the closure is still enforced until the end of February.

In Sweden, all clubs are open, but the Swedish government has strongly recommended everyone to stay home and avoid public spaces. And we have taken several measures to reduce visits in our Swedish clubs temporarily based on the recommendations from the government. The Swedish government also implemented a new pandemic law in January. We had a good dialogue with [indiscernible] (04:31) and gave our input to the pandemic law restrictions for the fitness industry over the Christmas period. The new law has not resulted in any major changes to our operations as we had already implemented strong measures. Capacity in all retail spaces including fitness clubs in Sweden has been limited to accommodate for a minimum 10 square meter per person. We have supported this law as it ensures that all businesses will need to adhere to the same strict standards as we have been operating with throughout the fall. And we have recently had several inspections from the authorities in Sweden in many of our clubs with the positive feedback following all the inspections.

In Finland, the situation has been more stable throughout the quarter, and the current restrictions have been prolonged to March 1. Our clubs have been operated according to these restrictions for several months, but we aim to be able to increase our capacity limits somewhat going forward, especially related to group training.

So, if you look at 2020 overall, our financials have been severely negatively affected by all the governmental restrictions and club closures. When comparing 2020 to 2019, we see a negative revenue effect of around NOK 800 million and an EBITDA effect of just about NOK 600 million.

We started the year with a very positive growth in January and February. So, this development is fairly related to the pandemic. The governmental support packages in Norway and Denmark are very positive and highly appreciated. But as you can see, they're only covering a small share of the loss.

In SATS, we have a strong vision. We are making people healthier and happier, and this has been difficult during the pandemic. And facts are clear. Public health has suffered significantly as a result of closed fitness clubs in the society. During a normal year, we have around 40 million visits in our clubs and only a small share of these 40 million hours of physical activity has been replaced by other form of training either outdoor or at home.

The training enthusiasts have managed to stay active also during the pandemic. But for most people, this has not been the case. They have been passive, and the majority of the population are much less active now and training much less now than before the pandemic. And this will have serious long-term effects on physical and mental health.

We have been active in our member communication, motivating our members to stay active using our digitals offering and training outdoor. And we are very impressed by the efforts our members have made. But now, we really urge politicians to prioritize public health when the society is gradually opening up.

And after reopening our clubs following the first lockdown, we have proven that it's safe to visit the SATS club also during the pandemic. Together with the industry in the various countries, we have implemented a wide range of industry-wide actions to make fitness club a safe place to visit. And in SATS, we have taken even additional measures. We have full access control and tracking of all visitors in our clubs. We ensure social distancing in our clubs. We have strong cleaning routines in our clubs and many, many other measures being implemented. And all these measures are supported and being acknowledged by our members.

And the numbers are very clear. In Norway, we have full infection tracking in the period we had opened clubs last fall. We have had more than 5 million visits in our Norwegian clubs since opening mid-June 2020. 227 members tested positive in the days following their visit to SATS. But none of these members had been infected in the SATS club nor infected others. So there has been none confirmed transmission of COVID-19 between members in the SATS club based on comprehensive infection tracking routines. So, our message is clear and fact-based. It is safe to visit a SATS club even during the pandemic.

Hence, we are very pleased to see that we, last week, were able to open some of our closed clubs in Norway in a controlled way and with good dialogue with the authorities. And the openings, they went well. The combination of strong operational routines and a strong technology platform enable us to implement a series of measures to keep our clubs safe.

With such extensive club network, most members have a club close to their homes. Before the pandemic, this was beneficial for the members who could choose between a wide range of clubs and a whole universe of group training classes and instructors. In the current situation, with the pandemic, this is beneficial as a facilitator for keeping the social mobility low as most member have a SATS clubs close to their home. And in several municipalities in Norway, we are now limiting the access only to members living in the same area as the club.

Given the negative consequences on public health and our strong, fact-based track record of operating safe clubs, we expect to open all clubs both in Norway and Denmark soon. We have full access control, full data tracking, strong hygienic protocols, and strict capacity measures. And we think it's a paradox that we still have to be closed, for example in Oslo, while other businesses and shops are allowed to be open, operating with much lower restrictions and no visitor tracking. So, again, we have a good dialogue with the governments – we have had a good dialogue with the governments all the way and followed all recommendations and the restrictions to contribute in the fight against COVID-19. But now, when we see that the society is opening up, [indiscernible] (12:02) in Norway is busier than ever, restaurants and bars are being opened, we expect and urge politicians to prioritize public health and open fitness clubs.

And when we open the clubs with COVID-19 measures in place, running them in a safe way, members are coming back. They want to get active again. This was proven when opening our clubs after the first lockdown in the summer. And we have seen it also in, for example, Bergen where we opened our clubs before Christmas before, unfortunately, closing them again on Sunday, that visits are coming quickly back to the levels of last year even with capacity restrictions being enforced because visits are more equally distributed throughout the day.

And in addition to activating the current member base quickly after reopening, we also expect new members to join and to quickly recover the member base. Then looking at the member development throughout 2020, we had a strong growth in the beginning of the year before the lockdown. Then the member base developed negatively mostly due to lacking sales, more than increased falloff during the first lockdown. Then after being able to open all our clubs again into Q3, we saw a rapid member comeback. The member base grew with 26,000 during Q3 2020 compared to 1,000 in growth during Q3 2019.

Then we had the second wave of club closures in Q4 with lacking sales bringing the member base down again. But we are confident that we will see a rapid recovery of the member base when we return to a more normal operation with open clubs and lower restrictions in the society. We will get back on track.

Then looking ahead. We are positive to the underlying growth momentum in the market and the strengthened position of SATS. The pandemic has changed our societies, among other by accelerating consumer trends that were also clear before the pandemic. And the strong trend around health and lifestyle has been clearly

accelerated. Fitness is in the center of the health and wellness ecosystem, and we expect the market growth to be very positive going forward. People will become more active and invest in their health.

Another important trend that has been accelerated is digitalization and the use of technology in people's everyday life. This is also positive for SATS as we have a strong digital platform in our business. Hence, we see strong growth opportunities for SATS going forward.

And every crisis contains seeds of opportunities. And we have tried to spend our time well during the pandemic. And we would like to highlight three main areas that we have been working on, improving member activation, operational routines, and cost control, as well as increasing our physical and digital presence. Let's look into those three.

Firstly, on member activation, we have been working systematically with member activation during the last few years and also spend some time in our quarterly presentations talking about it. There is a common misunderstanding that passive members are profitable for fitness clubs. This is a myth. Passive members cancel their memberships. It's just a question of time, and it doesn't take too long.

Usage and engagements are key metrics in both physical and digital subscription businesses. Hence, to increase the activity level in the member base is important both strategically and financially but also a very positive contribution to public health. And we have now really stepped up our efforts in this area. And going forward, we will take many actions to further increase engagement in our member base. And from the pilots we have done, we see clearly positive results both in the onboarding of new members and in the activation of existing members supported by our strengthened data and technology platform.

We have also standardized and improved our operating model across countries during the pandemic and sharing best practice implementation of routines and scheduling in all clubs in all countries. And we have also reduced operating costs in selected areas to make sure that we are able to operate our clubs with the new COVID-19 measures in place without increasing the total operational costs as Cecilie will also come back to this point in her presentation.

Overall, the SATS total product offering to our members are really unique. With our strong clusters, members have access to a wide range of clubs, more than 150 different concepts and classes. In the normal week, we have more than 3,000 classes in our clubs in, for example, Oslo or in Stockholm. And we will further strengthen our clusters going forward.

We see significant growth opportunities, and we have during 2020 accelerated our club expansion both through greenfields and M&A. And during 2020, we added 17 new clubs to our clusters, two of them being relocations. And this expansion will continue now into 2021.

Going into the year, we have already signed eight greenfields and two relocations, and more will come. The pandemic is changing the fitness market but also the retail market in general. And we see several interesting M&A opportunities and access to new attractive locations coming up. And we are in a strong competitive position compared to many other players in the industry.

So as you can see from this map, we are strengthening our already strong clusters. This will further improve our competitive advantage driven by scale in operations and the member value through increased offering both to new but also to existing members, because remember when we open a new club in, for example, Oslo or

Stockholm, we get many new members to that new club. But our existing members are also getting an improved offering as they can access all clubs in the cluster.

In addition to expanding our core product, we are also exploring supplementing offerings such as padel. This will be a positive additional offering to our members and to new members. The demand for padel is growing but still at an early stage. And we are well-positioned with our strong connections to landlords and with scale benefits in operations.

So we have already concluded and signed plans for establishing around 25 padel courts during 2021 and we expect to further grow this number. And even though 2020 has been challenging, we have experienced significant growth in one area, our digital product offering and usage. We have also commented on this in presentations throughout 2020, but during the year, we have launched several new digital products, engaging our members in periods where our clubs have been closed.

We are currently offering a digital universe, consisting of digital group training and classes, digital concepts, digital training programs, PT online and other services. And in 2019, we establish our own internal technology team, and we have scaled this team to 23 talented employees during 2020. And we are truly now seeing the effects of this great team in our digital offering. And this is resulting in increased digital engagement and usage among our members, with strong growth both in app and Web usage.

Online training got a really boost during the lockdown, with an impressive 3.6 million workouts during 2020 and a significant increase during the fourth quarter. These results gives us confidence that we have a solid foundation for further digital growth. And digital will be a central part of our growth strategy going forward. 80% of the Nordic population is not a member of a fitness club, and 80% of the population wants to work out more. And the main reason for not working out are lack of time or motivation.

There is a need out there and we want to fulfill it, and we believe we have the knowledge to help people to overcome these obstacles. So our ambition is truly to be the leading platform for digital training in the Nordics. The fitness market growth is accelerated by the growth in digital fitness especially during the pandemic, but we believe this will also continue after the pandemic. This will expand the market rather than cannibalize on the 20% already being members in the physical club. And we see that this enables SATS to grow into geographies where we don't have a physical presence today.

With our strong member base and brand, with our knowledge around training and what really motivates people, and our strong digital starting point, we believe that we are very well-positioned to become this Nordic leader in digital fitness. Hence, we have stepped up further our digital investments and will continue to do so. And we have big ambitions and we are piloting some very exciting products in the market in the period to come, and we'll share some more results from these experiments later on.

So to sum it up, we have seen negative financial impact from our – from the governmental restrictions, fighting the pandemic in Q4 going into 2021. We expect politicians to prioritize public health. We're now opening up to society due to the increased inactivity in the population during the lockdown. We believe we have spent the time well during the pandemic, strengthening the operational routines and laying the foundation for future physical and digital growth. And lastly, we do expect to deliver another strong comeback when opening our clubs and lifting the restrictions driven by owned initiatives and a very positive market momentum.

I'll now leave it over Cecilie for the financials.

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## Cecilie Elde

*Chief Financial Officer, SATS ASA*

Thank you, Sondre, and good morning, everyone. As we've seen, SATS is highly affected by the governmental restrictions and the recommendations from the authorities, as well as the member behavior in these uncertain times. And the fourth quarter financials are severely impacted not only by the direct effect of the club closures in Norway and Denmark, but also significantly tighter restriction and communication in the Swedish and Finnish governments. In Q3, we proved our ability to quickly recover both in terms of member development and profits. And as we presented previously, this is the clear benefit from our subscription-based business model, where revenues literally can be turned back on when we are allowed to return to normal operations.

Across the group, we closed the quarter with 628,000 members in total, which is 94% of the total number of members as of the end of Q4 2019. This is including members acquired from Bare Trening, adding six clubs and 9,000 members to our portfolio. And the typical pattern seasonally is normally flattish in Q4, but this year the decline in the member base was higher than expected due to closed clubs in Norway and Denmark but also due to increasing restrictions from all Nordic governments and local authorities which has put a damper on both visits and new sales.

And as we saw in the first round of club closures, the member decline of 6% is mainly caused by loss in new sales. But with increasing restrictions and continued uncertainty in the society, churn was also somewhat higher than last year especially in the first part of the quarter.

During the quarter and in-line with escalating contagion levels, we saw a continued increase in freeze as tighter restrictions affected member behavior. That said, we are happy to see that members choose to put their memberships on hold rather than resigning which shows that members have the intention to restart their training habits when the society starts to open up to more normal conditions.

Average revenue per member continues to improve in the fourth quarter, and after adjusting for closure-related freeze campaign effects from previous quarters, we see an increase also in the fourth quarter. And just to repeat what we commented on last quarter, the tactical sales campaigns from the third quarter did not affect the contractual price. But as the discount from free months are deferred over the full binding period of 12 plus 2 months, the yield takes a short-term hit and we will continue to be affected until Q3 this year.

In the fourth quarter, the reported negative yield effect of campaigns amounts to NOK 20 million and will be around NOK 15 million per quarter in the coming three quarters. The underlying membership yield in the quarter is, as said, up 1.4% when you adjust for currency, temporary discount effects and freeze. And as you can see on the right-hand side, the average contractual membership price in the base is not significantly affected by the club closures and continues to show a strong positive underlying development, following the ongoing yield management initiatives that we had from last year and an increase of 3.2% year-on-year.

And as said, the fourth quarter financials are heavily affected by COVID-19, as the majority of the clubs in Norway and all clubs in Denmark have been partly closed throughout the quarter. Compared to the fourth quarter last year, revenues of NOK 846 million are down by 18%. Revenues are also impacted by an increase in members on freeze due to tighter restrictions and stronger communication, encouraging people to reduce mobility in the society. And this also impacts new member revenue and lacking additional revenues like personal training and retail revenues.

The loss in revenues is partly compensated by the governmental fixed compensation packages, which are offered in Norway and Denmark, which is recognized as other revenues, and this amounts to NOK 56 million in the

quarter. But still, COVID-19 revenue is severely impacted in all markets. Adjusted EBITDA of minus NOK 32 million in the quarter is down 120% from last year, as a result of the massive loss in revenues from club closures and higher number of members on freeze.

The EBITDA margin is consequently down to minus 4% in the quarter. And the result is fairly similar per segment relative to size. But despite the governmental compensation packages for fixed costs, the Norwegian segment again takes the hardest hit in profit. And we have some cost reductions mainly as a result of temporarily laying off employees in Norway in the closed clubs and all club employees in Denmark.

So operating under these new normal does result in some additional cost-driving measures especially within cleaning and sanitation products. But we have, as Sondre talked about earlier, compensated for this cost increase by cost reduction in other areas. So to be clear, the decline we see now in profits in the fourth quarter is fully a result of loss in revenues.

As we communicated last quarter, we have continued to invest in our club portfolio throughout this period because maintaining our clubs is important to ensure sustainability and in future earnings. And full year maintenance CapEx ends in-line with what we've communicated of keeping a stable level of around 5% of revenues. And further on, we will continue to invest. We are open to acquisition opportunities arising and already signed greenfields and planned acquisitions, and relocations will be continued as planned.

Operating cash flow for the fourth quarter is negative at NOK 60 million. Working capital would normally be negative in the fourth quarter, but is positively affected by deferral effects on prepaid membership fees as we saw in the second quarter as well, because the freeze in memberships are reflected in revenues does not impact cash flow until the clubs are reopened and members get the membership days refunded by lower invoices.

So in terms of liquidity, we remain strong helped with a cash balance of NOK 456 million after Q4. And this provides a cash buffer in the event of prolonged local or national lockdowns or additional restrictions being reimposed, while at the same time facilitating the return to a growth strategy focused on developing and opening new clubs when the right opportunities arise.

In addition, we did a precautionary drawdown on the revolving credit facility of NOK 200 million in January to secure available liquidity and further strengthen our confidence in having sufficient liquidity and financial strength in the foreseeable future.

And finally, looking at the group's net debt and leverage position. As a result of the COVID closure, net debt is temporarily increased to NOK 1.5 billion last quarter but has remained fairly stable throughout this year. Weakening of the LTM EBITDA due to effects of the lockdown both in Q2 and in the fourth quarter results in temporarily elevated leverage ratios ending at 10 times adjusted EBITDA in the fourth quarter.

But as previously communicated, an amendment to the revolving credit facility was signed last year waiving the original leverage based covenants until June 2021. And the financial covenants that are applicable in this period until then are minimum levels of LTM EBITDA and maximum levels of CapEx. We do, however, have the flexibility to continue growing inorganically as proven through the acquisition of the Bare Trening clubs. But we do not expect to distribute any dividends to the shareholders during this amendment period.

And operating under normal conditions, we have historically shown strong deleveraging profile both through cash generation and growth in EBITDA. And in the immediate term, we have the mentioned deferral effects to clear over the coming months as well as continued restrictions in this first half of the quarter. So you should expect net



debt to increase slightly over the coming quarters. But we are extremely confident that once we are through the COVID closure impacts, we will return to the same approach to responsible deleveraging again in the future as we have shown in the past.

So I leave the word over to you again, Sondre, for outlook.

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## Sondre Gravir

*Chief Executive Officer, SATS ASA*

Thank you, Cecilie. So I will round off with a summary of how we see the outlook SATS and the industry. Short term, governmental club closures and restrictions will continue to have negative financial impact. But this is temporary, as Cecilie illustrated. We expect to recover quickly, both getting members back to our clubs and strong sales of new memberships when clubs are open and restrictions gradually lifted.

We expect to further grow both our physical and digital presence during 2021 fueled also by a very positive market trend around living a healthy lifestyle. After the pandemic, a new [indiscernible] (35:14) is starting, and that [indiscernible] (35:17) is to get the population active again. And we are here to contribute. We will make people healthier and happier again. Thank you.

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