

Work Project, presented as part of the requirements for the Award of a Master's degree in
Finance from the Nova School of Business and Economics.

Private Equity Challenge: Investment Committee Paper of Planet Fitness
Financial Modeling

Vincent Ringlstetter (48806)

Work project carried out under the supervision of:

Inês Lopo de Carvalho

15/12/2022

Abstract

Planet Fitness is a market leading fitness studio chain and franchisor with over 2,324 stores in the US. It provides high and recurring cash flows, making it a good LBO target. 2022 EBITDA reaches 336\$M, exceeding pre-covid levels. The company offers value creation potential in internationalization through M&A, Greenfield possibilities, and further organic growth levers. Entry Multiple of 9.2x results in an EV of 3.1\$B. With 5.2x Leverage an LBO yields 4.0x Money Multiple and 26% IRR.

Keywords

LBO, Investment Committee Paper, Gym Chain, Private Equity, Value Creation

This work used infrastructure and resources funded by Fundação para a Ciência e a Tecnologia (UID/ECO/00124/2013, UID/ECO/00124/2019 and Social Sciences DataLab, Project 22209), POR Lisboa (LISBOA-01-0145-FEDER-007722 and Social Sciences DataLab, Project 22209) and POR Norte (Social Sciences DataLab, Project 22209).

I. Table of Content

1. Investment Committee Paper summary – Group Component	3
1.1. Company Overview	3
1.2. Historic Financials	5
1.3. Market Overview	6
1.3.1. Trends and Forecast	7
1.3.2. Competitive Positioning.....	8
1.4. Investment Thesis	9
1.5. Value Creation	9
1.6. Business Plan and Forecast incl. Financials	14
1.7. Valuation	15
1.8. Capital Structure and returns	15
1.9. Exit Opportunities.....	16
1.10. Key Areas for Due Diligence	17
2. Financial Modelling – Vincent Ringlstetter, 48806	17
2.1. Revenue	17
2.1.1. Corporate-owned Store Revenue	18
2.1.2. Franchise Revenue	20
2.1.3. Equipment Revenue	23
2.1.4. PF-App Revenue	24
2.2. Profitability and EBITDA	24
2.2.1. Corporate-owned store’s EBITDA	24
2.2.2. Franchise EBITDA	25
2.2.3. Equipment EBITDA	25
2.2.4. PF-App EBITDA	26
2.3. Balance Sheet	26
2.4. Cash Flow	27
2.5. Cases Assumptions	27

1. Investment Committee Paper summary – Group Component

1.1. Company Overview

Planet Fitness is the largest franchisor and operator of high value low price gyms, founded by Marc and Michael Grondahl in 1992 in New Hampshire, USA. The company is the market leader in the high value low price fitness sector with an expectedly 16.3 million members and 2,324 stores worldwide in 2022. The 233 corporate-owned and 2,091 franchised gyms are mainly located in the US, followed by a small share in Canada, Mexico, Australia, and Panama. At the beginning of 2022, Planet Fitness acquired one of its franchisees Sunshine Fitness (hereafter Sunshine Acquisition), to gain the team behind one of the best-performing franchisees of its network. Hence, 114 stores were acquired and shifted from franchisee-owned stores to corporate-owned stores, almost doubling the number of corporate-owned stores. Besides operating and franchising gyms, the company sells equipment to its franchisees in US and Canada as the third line of business. As contracted in the franchise obligations, franchisees must purchase the equipment exclusively from Planet Fitness (except internationally, as they buy equipment from approved vendors and Planet Fitness receives a commission). Planet Fitness acquires the equipment directly from suppliers at lower prices and sells it at a markup, providing a recurrent stream of income. The franchisees are obliged to stick to the mandatory renewal of equipment every 5 to 7 years to maintain the company's quality standards.

Hereby, the corporate-owned store revenue accounts for 44%, the franchise business for 39%, and the equipment sales for 17% of total revenues. The strongest EBITDA of 58% margin, however, is generated via the franchise model as it is characterized by a low level of fixed costs and focused on selling and licensing franchise agreements.

Furthermore, the company has demonstrated double-digit past growth rates. Total revenue approximately doubled from 430\$M in 2017 to 839\$M expected in 2022 while the EBITDA increased from 180\$M in 2017 to 337\$M in 2022. With this track record, the company has

outgrown the market by, on average, 17 percentage points year-on-year, demonstrating the company's strong capabilities. This is enabled by the four major pillars the business model is built upon: The high value low price strategy, the "Judgement Free Zone" Concept, high-quality equipment standards, and the attractive franchise structure. Firstly, the high value low price segment has increasingly gained popularity among gym goers as it offers, as the name implies, high-quality amenities at a low price point. The company offers its classic membership for a fee of \$10 per month. This fee has never been increased and is one of the lowest in the market. While it is acting as a flagship for the company, it has also been attracting new joiners ever since. However, a premium option, the Black Card membership, with an increased number of services available is offered for 22.99\$ per month. Secondly, by being recognized for the "Judgement Free Zone", Planet Fitness distinguishes itself by providing a non-intimidating environment that creates a space for "everyone" and not only the bodybuilding athlete. Thirdly, high-quality standards can be ensured by strict equipment renewal and purchase standards for its franchisees. This leads to high levels of customer satisfaction. Lastly, by offering an attractive franchise option with solid potential returns (an IRR of 17% over 10 years), strong brand awareness, continuous support, and an overall streamlined model, Planet Fitness has been able to grow its number of franchisee-owned stores with an 10% CAGR from 2017 to 2021. Currently, the company follows several strategies to attract new members such as further internationalization in New Zealand and Mexico or marketing strategies with memorable, and creative advertising. Moreover, it offers a free mobile app that entails selected features such as equipment tutorials, live workouts or digital gym check-in. Lastly, as ESG ratings are increasingly important, Planet Fitness has set up a strategy to mitigate the risk associated with a relatively weak current rating. The history of the company has demonstrated the capabilities of the executive team. Therefore, the combined more than 17 years of executive experience at Planet Fitness, will also pave the way for future growth.

1.2. Historic Financials

Planet Fitness has demonstrated solid member growth with a 2017-2022 CAGR of 9%. Furthermore, total number of stores increased consistently, starting with 1,518 in 2017 to 2,324 in 2022. This amount of store openings is mainly impacted by the store openings of Planet Fitness franchisees.

Total revenue grew with a 2017-2022 CAGR of 14%, already exceeding pre-covid revenue in 2021. Total revenue can be separated into three streams: Franchise revenue, corporate-owned store revenue, and Equipment revenue. Franchise revenue consists of royalty- and other fees (~70%), National Advertising Fund revenue (~20%), and commission income from vendors (~10%). Despite a slight decrease during covid, franchise revenue consistently grew in the past, exceeding pre-covid numbers already in 2021. This growth has slowed down in 2022 related to the sunshine acquisition. Due to this event, corporate-owned revenue more than doubled in 2022 as it is driven by the number of stores, which also doubled. Equipment revenue heavily suffered during covid due to related closures of stores and postponement of new equipment purchases. However, this segment already started to recover, reaching almost pre-covid levels despite the loss of 114 deliverable stores (sunshine acquisition).

Planet Fitness shows a strong EBITDA margin of 40% in 2022, achieving pre-covid levels. The strongest driver of the EBITDA is the franchise segment, which in 2021 made 72% of total EBITDA (Corporate-owned: 18%, Equipment: 10%). In 2022, the corporate-owned impact on EBITDA increased to 37% (Franchise: 56%, Equipment: 7%) due to the sunshine acquisition. Furthermore, the franchise segment itself has the highest EBITDA margin as pct. of franchise revenue (58% in 2022) as franchise costs are only consisting of NAF expenses.

In the years 2017 to 2019, Planet Fitness' net income rose from 17% to 21%. During Covid, the net income became negative due to the related closure of most operated stores. However, 2021 and 2022 show signs of recovery with margins of 11% and 12% respectively.

The Net Working Capital (NWC) has been negative in the past (2017-2022) and further decreasing in 2021 and 2022 (-80,802 \$M in 2022). This is driven by multiple factors. Firstly, Planet Fitness has an inventory-light business model. Revenues are achieved by delivering service instead of goods, which must be stored. Secondly, as opposed to low inventories are high deferred revenues. As many memberships are paid at the beginning of the year for a service, that will last the year, the revenue cannot be immediately recognized. So, the money is already received while the service wasn't provided. Those revenues must be deferred.

1.3. Market Overview

The US health club and studio market is currently valued at 33.3\$B¹ and has shown solid growth until 2019 before the covid crisis hit. Going forward, it is expected to grow at a similar speed. In other words, a 2008 to 2019 CAGR of 5.7% was estimated while 2022 to 2030 growth is projected with a CAGR of 5.8%². During the pandemic, things looked different due to several closures and restrictions majorly affecting leisure institutions such as gyms. The market dropped by approximately 58% in 2020. In the following year, the market was down by 22.5% compared to a pre-Covid level³. This growth trend also translated into the number of health clubs (31 thousand in 2012 vs. 41 thousand in 2019)⁴ and respective number of members which have increased by more than 14 million from 2012 to 2019⁵. But they did not only increase in absolute number but also as a share of the US population from 18.37% in 2012 to 22.48% in 2019⁶. The trend of increasing penetration is expected to continue.

¹ Proprietary Market Model

² Ibid.

³ Expert Interview, Rizzo, Nicholas, "Fitness Industry Statistics 2021-2028 [Market Research]."

⁴ Statista, "US Fitness Centers and Health Clubs."

⁵ IHRSA Media Center, "Total U.S. Health Club Membership by Year."

⁶ Proprietary Market Model

1.3.1. Trends and Forecast

Besides increased penetration, the fitness market is influenced by majorly five macro trends, all of which started pre-COVID and are generally anticipated to continue going forward. Firstly, customers become increasingly health concerned. Secondly, boutique studios gained popularity. They have grown with a CAGR of 6% year-on-year. Thirdly, the rise of wearables and new technology concepts largely influence customer fitness behavior. Fourthly, favorable changes in demography lead to an increase in the share of younger populations, i.e. 6-34 years, which is in other words a growth in the number of future gym goers. Lastly, customers increasingly appreciate high value at a low-price offering. This trend fuels the erosion of the mid-tier segment and buttresses the growth of value players such as Planet Fitness as these enter mid-tier offerings at attractive price points⁷.

The latest trend reveals that the health and fitness market can be further divided into four sub-segments: Community centers and clubs, studios, independents, and large chains. The large chains making up approximately 32% in 2022 themselves are usually split into corporate-owned and company owned which again are split into the three major segments⁸.

The major differentiator between the three segments is the price point. Low-cost players are characterized by starting fees lower than or equal to \$20 while premium players have starting fees of \$60 and beyond. Mid-Tier ranges in between. Hereby, Premium accounts for 10% or 1\$B, Mid-Tier for 30% or 3 \$B and High Value Low Price (HVLP), for 60% or 7\$B generate a combined market value of approximately 11\$B. Going forward, Premium and HVLP market revenues are expected to grow with a CAGR of 7.8% and 8.1% respectively. The Mid-Tier

⁷ IHRSA, "IHRSA Media Report 2021.", Expert Interview

⁸ Proprietary market model

segment is, however, expected to further lose share growing with a CAGR of approximately 5.5 percent⁹.

1.3.2. Competitive Positioning

Market competitors vary in scale and business model. However, considering current trends and developments, the rivalry between HVLP and mid-tier appears to be the fiercest. But also, online offerings widely gained popularity during the pandemic¹⁰. Nevertheless, Planet Fitness shows strong economics and established successful strategies to win in the competition for members but also franchisees.

Firstly, Planet Fitness holds a market share of approximately 57% of the HVLP segment while showing an above-average monetization per square foot of gym of 84\$. Hereby, the company benefits from a staff-light business model as well as cost-efficiency and leaves the major competition behind. Secondly, Planet Fitness has appropriate offerings matching the five key determinants of membership sign-up and retention: Price point, quality and retention, location, network, and complementary online offering and app. Especially the basic fee is the flagship of the company and has never been raised beyond 10\$ while the quality of amenities and customer satisfaction ratings are high¹¹.

Secondly, franchisees are especially attracted by five characteristics: A franchisor's reputation, the support offered, growth potential, cost, and profitability. The factors are especially given the HVLP segment. This combined with the strong profitability, support and reputation makes especially Planet Fitness stand out and an attractive option for franchisees.

All in all, Planet Fitness has built upon several successful strategies to win the market. Not only in terms of competition for members but also in terms of competition for franchisees.

⁹ Ibid.

¹⁰ ABC Fitness Solutions, "The next fitness consumer – 10 Key findings."

¹¹ Expert interview, company information

1.4. Investment Thesis

Planet Fitness qualifies as a promising target due to the attractive market it operated in, its proven business model, and its strong value creation levers and returns. The company is the market leader in the HVLP segment with a vast presence, especially in the US. With 2,242 stores in 2022 in the US only and 2,324, PF is the largest HVLP player in terms of units and revenue across the country. The second largest HVLP player is only one-seventh of its units. The company has strong brand recognition as an attractive franchisor and partner. Moreover, the company constantly outperformed the health club market growth year-on-year, and the trend is expected to continue. The HVLP segment especially is expected to grow stronger with a CAGR of approximately 8 percent¹² as customers highly value strong value proposition at low cost. Moreover, selling membership options brings predictable and recurring revenue income, which is beneficial for e.g. servicing debt payments. Lastly, strong value creation levers will yield a money-on-money multiple of 4.0x or an IRR of 26%. This is based on the scalable business model which can be further exploited by an increase in the number of gyms from 2,324 to 3,802 worldwide. However, most importantly strong value creation levers were identified that should yield the expected return focusing especially on the top line, bottom line growth, and financial structure.

1.5. Value Creation

Top-line growth will be achieved in four ways. Firstly, to further increase market share and penetration, organic growth is fostered by introducing measures to attract new members such as special marketing on social media or leveraging the Planet Fitness app. On the other hand, measures to increase revenue per member will be introduced such as price increases for the Black Card membership and focus on upselling i.e. to increase the share of Black Card members

¹² Proprietary market model

will be implemented. Secondly, Greenfield projects with a major focus on three areas in the US will exploit underrepresented areas in California, Florida, and New York. Thirdly, a new revenue stream will start in 2023, the extended Planet Fitness App. Lastly, international M&A in Germany and UK to kickstart internationalization. Although the focus is set on top-line improvements bottom-line improvements cannot be neglected. To fully exploit EBITDA margin potential, major improvements due to exploiting economies of scale to their fullest and small-scale projects to foster more specific improvements are proposed. This in the end will further enhance the value at exit.

The final lever block is CAPEX and NWC improvements. Decreasing maintenance CAPEX per store following the historical trend and boosting cashflows after an initial increase in IT CAPEX as a percentage of revenue. The increase in investments in the first years will boost revenue and EBITDA margin. Afterward, a decrease in reinvestment rate and focus on cash generation is planned closer to the exit year.

1.5.1. Organic revenue growth

Increasing revenue per gym is twofold. On the one hand, the average number of members should be further increased up to a threshold of 8.5 million. On the other hand, getting the most revenue out of a single member will further increase monetization per member beyond the capacity restriction.

Increasing the number of members per gym

Firstly, the proposed marketing strategy will especially focus on Generation Z as the future generation of gym goers. This includes the introduction of regular TikTok Challenges and cooperation with influencers. Hereby, Planet Fitness members participating in the challenge are eligible for a small goodie. Secondly, by introducing corporate fitness options, Planet Fitness can leverage the acquired knowledge e.g. from beneFit or Fit/ One to especially target the largest population of gym goers, the Millennials. As in Europe and the US, no large chain does

not offer classes, so it is proposed to introduce live classes for Black Card members. Starting with a test in Europe and a potential rollout across the US after a successful test. To stick to the cost-efficient and staff-light business model, classes will not be held by personal trainers live in the studios, but one personal trainer will be streamed into many local studios. This will attract new members and avoid a churn of members from potential targets while keeping costs low but the effect high. Moreover, small changes such as a limited number of bring-a-friend days for Black Card members should trigger the conversion of the guest brought to a real member. But also, the Planet Fitness App can be further leveraged to act as a gateway to a gym membership.

Increasing revenue per member

By introducing five measures to increase the share of black card members we expect to reach a share of approximately 68% by 2028. An average price increase to \$24.99 in 2024, the introduction of a free Black Card trial period for basic members and non-members should be introduced. Moreover, a minimum contract duration of 24 months will be linked to the Black Card option and will be combined with an attractive discounted lump sum payment possible for the whole period. Thirdly, regular pre-announced cooperation with partner companies should be implemented. Hereby, actions will be promoted as limited to create hype and trigger the decision not to wait and immediately to enroll. Recent cooperations such as the one with the new Amazon wearable were the first sign of success for PF and the cooperating party. Lastly, into crease the attractiveness of the Black Card membership compared to the classic option, the limited offerings for black card members only should be extended. This will on the one hand affect in-store options but also Planet Fitness App options.

1.5.2. Greenfield

New store openings will focus on the three areas of New York, California, and Florida as identified white spots and for strategic reasons. This is expected to yield an increased market share and higher-than-average potential in these gyms. New York is the state with the lowest

gym density per 100 thousand people which leaves sufficient room to easily attract new members. The potential in California is similar¹³. Moreover, as Planet Fitness already has the highest location share at this stage, the company can leverage its strong existing knowledge and presence. Also in Florida, Gym density is at the lower end. Additionally, the major US mid-tier player Anytime is more strongly represented¹⁴, making it a good place for Planet Fitness to keep up with the competition and eventually convert their members to new Planet Fitness following the erosion of the mid-tier trend.

1.5.3. A new revenue stream

During the global COVID-19 pandemic, Planet Fitness launched “United We Move” to provide free, live digital workouts to millions of people around the globe to keep people active, moving and engaged with the Planet Fitness brand¹⁵. This led to a strong increase in users of the free Planet Fitness App and currently approximately 6 million weekly users. However, the model is currently offered for free but offers high revenue potential. Therefore, the existing membership base and awareness lay the foundation to kickstart a new revenue stream in 2023 by broadening the offerings and meeting the demand of the post covid fitness community¹⁶. The app is forecasted to contribute 5% to total Planet Fitness EBITDA in 2028 with a revenue of approximately 62\$M annually and 14.3 million active users. The app strategy is built upon four major Pillars: the Freemium Model, Optimization for wearables and smart TV, community, and internalization of knowledge to be the 24/7 connection to the current members and new community acting as the perfect extension to the limited and cost-effective studio offerings. This will act as an effective presales tool or standalone membership.

¹³ Morris, Kathy, “THE 10 STATES WITH THE MOST GYMS (AND THE LEAST).”

¹⁴ ScrapeHero, “Number of Planet Fitness locations in the United States.”

¹⁵ Company information

¹⁶ ABC Fitness Solutions, “The next fitness consumer – 10 Key findings.”

1.5.4. Kickstart internationalization via M&A

Acquisitions in Germany and UK were chosen to become the starting point for further franchise openings across Europe. Europe itself is an attractive market worth approximately \$23 billion and 56.3 million health club members as well as a highly fragmented structure. Moreover, it is expected to outgrow the US market with a CAGR of 7.25% from 2021 to 2026¹⁷. The United Kingdom and Germany are the top two countries in terms of gym revenue making up together approximately a quarter of the European market. In both countries, low-cost gyms have been on the rise and increasingly gained popularity, so the average monthly dues paid by members in both countries are below the current US average (UK: \$48, Germany: \$44)¹⁸.

Target Selection Criteria

Potential targets were screened based on six criteria to ensure a strategic fit, reduce the risk associated with potential acquisitions and ensure that excess cash is sufficient to finance the deal as all deals are proposed to be paid in cash only. Small- to medium-sized gym chains with 10 to 50 gyms are targeted since smaller operators are not worth the effort. These clubs are cheaper and bear more potential for multiple arbitrage. Consequently, the proposed acquisition price should be below \$150 million, and the EV/EBITDA multiple should be below the planet fitness entry and exit multiple. As described prior, the target's geographical focus should be in the United Kingdom or Germany. Moreover, the business model should fit the high-value low price model of Planet Fitness with a similar target customer and high-quality standards that ensure a smooth transition of members to the rebranded gyms and avoid churn of existing members. Franchise experience is a plus but not required as the targets will be converted to corporate-owned gyms. Lastly, financial health and profitability are a prerequisite to not threaten Planet Fitness' margins. However, due to the substantially smaller size compared to

¹⁷ EuropeActive, & Deloitte, "European Health and Fitness Market Report 2022."

¹⁸ Ibid.; Statista, "Average membership fee per month for fitness clubs in Germany from 2014 to 2019."

Planet Fitness, it is expected that margins of targets are lower at acquisition but are expected to rise due to a successful post-merger integration. Especially target price, number of clubs and portfolio fit are the most relevant criteria.

Selected Targets

Based on the above criteria, three targets with a major focus in Germany and one target in the United Kingdom were selected. In total 85 locations will be acquired: 64 in Germany, 16 in the UK, 4 in Austria and 1 in Poland. The acquired targets will become new corporate-owned stores. These stores will act as well-functioning hubs in the respective countries and centers of knowledge. Further expansion will start with a franchise system and area developer contracts in these two countries and across Europe. The new acquisitions will bring know-how e.g. on corporate membership options, new online content can be acquired and new national talent.

The acquisition series will start with the largest German target Fit/One with 41 locations in 2024. This will be followed by the two German low-cost chains beneFit and World of Fitness (WOF) and the UK chain 24/7 Fitness in 2025 with 15, 13 and 16 gyms respectively. On average targeted locations are larger creating revenue upside potential per gym¹⁹. The timing of the acquisitions is on the one hand based on the forecasted cash availability. On the other hand, it is expected that the ramp-up period of the gyms will be finished in year three after opening or acquisition. Therefore, all acquisitions are expected to have fully realized potential until the planned exit in 2028.

1.6. Business Plan and Forecast incl. Financials

Revenue is increasing from 839\$M in 2022 to 1,950\$M until 2028. In the same period, EBITDA increased by 446\$M (138%) to 803\$M in 2028. The increase in EBITDA is mainly driven by greenfield (27%) and organic growth (27%). An increase in equipment revenue accounts for

¹⁹ Respective company websites

19% and the internationalization kickstart via M&A for 18%. The new revenue stream of the PF-App accounts for 5% of the revenue increase and EBITDA margin improvements for 5%. Free cash flow increases to 493\$M in 2028. To calculate the financial forecast, the key main revenue drivers were identified for each segment. For corporate-owned stores and franchise stores, these are mainly the number of stores, members per store, and revenue per member. Equipment revenue thereby is driven by franchise stores and (re)equipment costs per store. The app revenue is forecasted based on monthly downloads, percentage of paying users, and price per online membership. On the other hand, costs are mainly driven by revenue or the number of stores. CAPEX is mainly depending on stores in operations and store openings. Balance sheet items are either forecast through D&A and CAPEX or by a revenue-dependent driver.

1.7. Valuation

The valuation is based on the 2022 expected EBITDA as this accounts for the changes that occurred due to the sunshine acquisition and related increases in revenue and EBITDA while no more covid effects prevail. By applying the median past HVLP transactions EV/EBITDA multiple of 9.2x²⁰, which is accounting for the specialties of the HVLP segment, Planet Fitness is valued at 3.1\$B. This valuation and multiple will lay the foundation for the entry valuation. A DCF with a WACC of 8.18% was conducted as well, resulting from a levered historical 5Y monthly beta of 1.21, a cost of equity of 9.25%, and a 4.82% cost of debt based on a BBB rating²¹.

1.8. Capital Structure and returns

The total sources of the deal are separated into equity and debt. The optimal debt structure was analyzed, accounting for 52.8% of the Deal Value being split between senior and subordinated

²⁰Merger Market, Refinitiv Eikon, Capital IQ as of November 13, 2022

²¹ Bloomberg as of November 11, 2022

debt which equals 4.2x and 1.0x of the 2022 EBITDA respectively. While the subordinated debt is based on mezzanine financing, with a bullet payment in the 9 years horizon, the senior debt is structured in three tranches: Tranche A with amortization payments throughout the 6 years maturity equating to 1.2 x the EBITDA, Tranche B with a bullet payment in the 7 years' horizon amounting to 1.5x the 2022 EBITDA and, finally, Tranche C with a bullet payment as well of 1.5x the EBITDA, 8 years after the acquisition.

In terms of equity financing, 1,564,883\$ will be raised, equating to the remaining 47.2% of the Deal Value, and a multiple of 4,6x the 2022 EBITDA. This value is divided between two different segments: preferred shares, providing financing of 4.5x the EBITDA, and ordinary equity, with 0.2x EBITDA. Invested into the equity part are institutional investors (the fund) and the management. When exiting in 2028, the EBITDA is estimated to achieve 835\$M, and as we don't assume any multiple arbitrage, we result in an exit multiple of 9.2x and the subsequent Enterprise Value of 7,683\$M. At the exit, management returns add up to a Money Multiple of 24.2x or an IRR of 70%. Institutional investors yield 4.0x or 26% IRR.

1.9. Exit Opportunities

Due to the size and popularity of Planet Fitness, it is proposed to exit via an IPO. Although an IPO is highly dependent on market conditions, the past has shown that the fitness segment can be considered rather resilient, and Planet Fitness has shown strong growth and is expected to do so going forward. Moreover, the market highly values a scalable, well-functioning franchise system that is considered low risk²². As the second-best option, a strategic sale should be considered. Selected national and international competitors or market participants could be interested in horizontal, forward, or backward integration. These candidates are potentially willing to pay a strategic upside on the true value at exit. For example, LifeTime Fitness, a

²² Capital IQ, Merger market, Bloomberg, Company information

premium gym chain operator in the US, fit bit an international company selling budget-friendly wearables, or Life Fitness, a current supplier and global gym equipment manufacturer are proposed.

1.10. Key Areas for Due Diligence

The due diligence should mainly focus the legal and financial due diligence, followed by commercial, valuation, and exit. The legal part should mainly cover the contractual relations with the franchisees and the correctness as well as sufficient of the franchise disclosure document (FDD). The financial part should focus on a detailed split of SG&A and labor costs to further understand improvement levers as well as profitability analysis on gym levels for the same reasons. Thirdly, the commercial due diligence should further elaborate on and validate the attractiveness and adequate documentation of the Planet Fitness franchise system, the impact of contractual obligations on franchisee performance plus validating characteristics of the market and proposed targets. Lastly, exit and entry multiples should be verified via fair value opinions as multiples are one determinant of return potential. However, not only wrong multiples could have a negative impact on returns but also competition laws which could prevent a potentially profitable strategic sale.

2. Financial Modelling – Vincent Ringlstetter, 48806

2.1. Revenue

Total Revenue will increase from 839\$M in 2022 to 1,937\$M in 2028, which represents a CAGR of 15%. The increase in revenue is mainly driven by corporate-owned store revenue (488\$M increase or 44% of total revenue increase) and franchise revenue (315\$M, 29%). The increase in equipment revenue accounts for 232\$M (21%) and PF-App revenue for 62\$M (6%).

2.1.1. Corporate-owned Store Revenue

Corporate-owned store revenue is 368\$M in 2022, which is equal to 44% of total revenue. The revenue increases by 488\$M to 857\$M in 2028 (15% CAGR 21-28), which is equal to 44% of total revenue. The increase in revenue is mainly driven by the value creation levers “Organic growth”, “Greenfield” and “Internationalization via M&A”. Further, corporate-owned store revenue is driven by two main pillars, the number of corporate-owned stores and the revenue per store.

The number of corporate-owned stores is increasing from 233 in 2022 to 373 in 2028 (66% increase). Greenfield openings account for 51 new stores in this period. The number of stores opening every year is increasing from 6 (historical average 17-22) to 11 in 2028. All stores will open in the US and are mostly focused on New York, Florida, and Florida as discussed in the value creation lever “Greenfield”. Besides the organic openings, Planet Fitness will acquire 85 stores in Europe through M&A and will thereby kickstart its presence in Europe. All acquired stores will be incorporated as corporate-owned stores. In 2024 the fitness company Fit/One, with studios in Germany, Austria, and Poland will be acquired adding 41 corporate-owned stores to the company. Further, in 2025 two German fitness studio chains, BeneFit and World of Fitness (WOF), as well as one UK-based chain, 24/7 fitness are expected to be acquired, leading to 44 additional corporate-owned stores.

Further, it is expected to acquire 3 stores per year from franchisees. In historic periods, the number of franchise stores bought back fluctuate heavily. Reason for the acquiring of stores from franchisees are among others, contract breaches and corporate interests in buying back stores. The historic average (excluding 2022 due to an abnormal number of stores acquired through sunshine acquisition) is 6 per year. Because the acquisition of stores from franchisees will have a negative effect on the EBITDA margin (Franchise segment has a better margin than corporate-owned stores) and leads to an increase in CAPEX, management will be focused to

decrease this number of acquired stores. Therefore, it will be assumed that in the investment period 3 stores per year will be acquired from franchisees leading to 18 additional corporate-owned stores. In the investment period, no store will be closed. For each store, which will be opened or acquired, the same revenue potential as the average PF-Gym is assumed. However, for each type of new store a different ramp-up period will be assumed. Stores opened organically will achieve 25% of the full revenue potential in the first year, 50% in the second year, and 100% in the third year.²³ Stores acquired through M&A will be generating 100% of the revenue pre-acquisition in the first year. In the second year, the gap between the average revenue per store of Planet Fitness and the revenue of the acquired store will decrease to 50%. In third year, stores acquired through M&A will achieve their full revenue potential. Stores acquired from franchisees, however, will achieve 50% potential in the first year, since they will be acquired on average in the middle of the year. In the second year, the full revenue potential will be achieved.

With these ramp-up assumptions, a weighted average of corporate-owned stores can be calculated, based on their percentage of revenue potential. In 2028 the weighted number of corporate-owned stores is 372.

The second driver for corporate-owned store revenue is the average revenue per store. This revenue is calculated by revenue per customer and number of costumers per gym. Revenue per costumer is based and monthly membership fees and other fees attributed to enrolment and yearly fees. These other fees are equal to the pre-corona average (2.4\$ per month), however in 2023, being a transition year to the new level, only 1.3\$ per month in other fees will be paid. Dues attributed to monthly membership fees are depending on percentage of Black Card members compared to standard members and the price of each membership. The standard

²³ Expert Interview

membership fee will stay at 10\$ per. Monthly fees for Black-Card members will increase from 22.99\$ to 24.99\$ in 2024. This price increase will lead to churn-rate of 10% of Black Card members, whereby half of these costumers will switch to the standard model.²⁴ The percentage of Black Card members is 63% in 2022. This number will increase by 2.2% yearly, based on historical growth values and further potential trough upscaling incentives explained in the revenue lever “Organic Growth”. Including this growth rate and churn in 2024, the percentage of Black Card members will increase to 68% in 2028. Therefore, the average membership fee per member will be 20.2\$ per month. In 2022 the average number per stores is 7.4 thousand. Based on the historic pre-Covid averages and further management potential due to organic growth incentives, members per store will grow by 5.7% per year. The maximum number of members per store is capped at 8.5 thousand due to limited space capacity per gym²⁵. In 2028 the average number of members per store will be 8.5 thousand, monthly dues attributed to membership fees will be 20.2\$ and other monthly fees will be 2.4\$ leading to a revenue per store (year) of 2.6\$M. This, multiplied by the weighted number of stores, will translate to the corporate-owned store revenue of 857\$M in 2028.

2.1.2. Franchise Revenue

Franchise revenue is 325\$M in 2022, which is equal to 39% of total revenue. Franchise revenue will increase by 315\$M to 640\$M in 2028 (12% CAGR 22-28), which is equal to 33% of total revenue in 2028. The increase in revenue is mainly driven by the value creation levers “Organic growth”, “Greenfield” and “Internationalization via M&A”. Total Franchise Revenue consists

²⁴ Bespoke Intel, “PLNT (Planet Fitness) Longitudinal Survey Excerpt (Buyside Questions).”, Following further key assumption are used in this model: 1. 25% of people who stated “definitely cancel” will actually cancel 2. 15% of people who stated “I would consider to cancel” will actually cancel 3. 50% of people who will cancel the membership will stay at Planet Fitness as standard member 4. Churn percentage will decrease over time by 5% per year

²⁵ 8.5 thousand as cap is based on Expert interview and Peer analyses

of (direct) Franchise revenue, Commission income, and National Advertising Fund (NAF) revenue.

Direct Franchise revenue accounts for 80% of total Franchise revenue and is 260\$M in 2022. This number will rise by 224\$M to 528\$M in 2028 (13% CAGR 22-28). Direct Franchise revenue consists of royalty revenue (88%) and other franchise revenue (12%). Royalty revenue increases from 228\$M in 2022 to 469\$M in 2028 (13% CAGR 22-28). Royalty revenue is driven by system-wide sales attributable to franchise-owned stores and the royalty fee in percent. System-wide sales are sales attributed to monthly dues and annual fees billed by franchisees. These system-wide sales are driven by the number of franchise stores and revenue per franchise store. In 2022, Plante Fitness franchisees operate 2,091 stores worldwide (2,060 in US/Canada; 31 outside US/Canada). In 2023, 196 franchise stores will open in US/Canada (based on historical averages 17-21). Due to “Greenfield” incentives, the number of yearly openings will increase by 4 store openings per year, leading to 1,236 franchise store openings in US/Canada. Further franchise stores will also open outside US/Canada. From 2023 onwards, it is expected that 15 franchise stores will open yearly, outside the US/Canada. This is driven by an already signed area development agreement (ADA) in Mexico and New Zealand. From 2025 onwards after the acquisition of the first gym groups in the UK and Germany, 10 franchisors will open yearly in Europe, leading to 25 yearly franchise stores opening outside US/Canada. From 2023 to 2028, 130 franchise stores outside the US and Canada will open. In the same period, it is expected that 4 stores per year will be debranded, sold, or other, which is in line with historic figures (24 franchise stores in total). Further, as mentioned above, 18 franchise stores will be acquired by the parent company Planet Fitness, until 2028. All in all, 1,324 franchise stores will open (net) until 2028, which will lead to 3,415 franchise stores in total. The ramp-up phase for franchise stores is the same as for organically opened corporate-owned stores. For stores sold to Planet Fitness or others, it is expected to generate 50% of the

full revenue in the last period (assumed to be sold in the middle of the year). Therefore, the weighted number of franchise stores in 2028 is 3,117. Revenue per franchise store is 1,716 in 2022. The number of members per franchise stores are equal to them of corporate owned stores (2022: 7.4T; 2028: 8.5T). The monthly dues attributed to memberships are equal to the ones of corporate stores (2022: 18.2\$; 2028: 20.2\$). However, other dues attributed to enrolment and yearly fees are different. These are 1.1\$ in 2022 and they will decrease to the pre-Covid average of 0.9\$ in 2024 and staying constant until 2028. Therefore, the average revenue per franchise store in 2028 will be 2.2\$M and the system-wide sales attribute to franchise-owned stores will 6,699\$M. A stable royalty fee of 7% of system-wide sales will lead to royalty revenue of 469\$M in 2028.

Another franchise revenue is based on other franchise fees (22\$M in 2022) and placement revenue (10\$M in 2022). Other franchise fees per store are driven by a number of franchise stores and other franchise fees per store. Other franchise fees per store are 11\$T in 2022 and will increase by 2% yearly, along with the long-term inflation, to 12.5\$T in 2028. In 2028 other franchise fees accounts for 39\$M (10% CAGR 22-28). Placement fees are driven by franchise stores in US/Canada and placement fees per store (US/Canada). Placement fees per store (US/Canada) is 4.9\$T in 2022. These numbers increase by 4% yearly, due to long-term inflation an increase in prices due to high demand for construction services. In 2028, placement fees per store (US/Canada) are 6.2\$T, leading to total placement fees in 2028 of 20\$M (12% CAGR). Other franchise revenue in 2028 accounts for 59\$M. Total direct Franchise revenue is 528\$M in 2028.

Commission income accounts for 0.3% of total Franchise revenue and is 1\$M in 2022. This number will rise by 4\$M to 5\$M in 2028 (29% CAGR 22-28). Commission income is driven by a number of stores outside the US and Canada and the total Equipment bought per store

(Outside US/Canada). These number increases by 3% yearly until 2028, due to inflation of more complex equipment and resulting higher prices.

NAF revenue accounts for 20% of total Franchise revenue and is 63\$M in 2022. This number will rise by 43\$M to 107\$M in 2028 (9% CAGR 22-28). NAF revenue is paid from franchisees as % of system-wide and will only be used for marketing purposes. In 2022 1NAF revenue was 1.9% of system-wide sales. However, this number will decrease to 1.6% (pre-Covid level) from 2023 onwards.

2.1.3. Equipment Revenue

Equipment revenue is 146M in 2022, which is equal to 17% of total revenue. Franchise revenue will increase to 378\$M in 2028 (17% CAGR 22-28), which is equal to 20% of total revenue in 2028. Equipment revenue consists of replacement revenue and new equipment sales.

Replacement revenue is 109\$M in 2022 and is driven by replacement revenue per store and the number of franchise stores in the US/Canada. The replacement revenue per store will reach pre-Covid levels in 2024 and will increase by 3% yearly afterwards due to increase in prices driven by inflation and increase in complexity of equipment. In 2028 the replacement revenue per franchise store in US/Canada will be 72\$T, which leads to total replacement revenue of 235\$M (14% CAGR 22-28).

New equipment sales in 2022 equal 36\$M (25% of total equipment revenue). New equipment sales are driven by number of franchise stores opened (US/Canada) and new equipment revenue per new franchise store opened (US/Canada). New equipment revenue per new franchise stores open (US/Canada) is 511\$T in 2023, which is equal to the pre-Covid average (2017-2019). Afterwards, this number will increase by 3% yearly, due to inflation and increase in complexity. In 2028 sales from new equipment per franchise stores open (US/Canada) will be equal to 592\$T. Total new equipment sales in 2028 will reach 143\$M (26% CAGR 22-28)

2.1.4. PF-App Revenue

PF-App revenue is 0\$M in 2022, due the fact that the app is not monetized yet. The revenue is driven by the value creation lever “New Revenue stream”. App revenue will be 62\$M in 2028, which is equal to an 45% yearly increase from 2023 onwards. The revenue is driven by monthly downloads, number of frequent users, percentage of paying users and average price per app. In 2022 number of monthly downloads 333 thousand.²⁶ These number will increase by 13% yearly to 694 thousand in 2028. Percentage of downloads leading to frequent user increases from 29% in 2022 to 41% in 2028 and Churn rate is constant of 10%²⁷. Following this, the number of frequent users will increase from 6M to 14M in 2028. Percentage of paying user will increase from 3% in 2022 to 6% in 2028 leading to 864 thousand paying users in 2028. Average price per month will thereby increase steadily from 3.99\$ to 5.99\$ in 2026. Afterward the price stays stable. This will lead to a monthly app revenue of 5\$M in 2028.

2.2. Profitability and EBITDA

Planet Fitness EBITDA will increase from 337\$M in 2022 to 835\$M in 2028 (16% CARG 22-28). The EBITDA margin will increase from 40% in 2022 to 43% in 2028.

2.2.1. Corporate-owned store’s EBITDA

Corporate-owned store EBITDA increases from 126\$M in 2022 to 299\$M in 2028 (16% CAGR 22-28). Corporate-owned store EBITDA margin increases from 34% in 2022 to 35% in 2028. The main costs related to corporate-owned stores are costs related to store operations (86% of total corporate-owned costs in 2022) and SG&A costs related to corporate-owned stores (14%).

²⁶ JP Morgan, “Planet Fitness Equity Report Sept 2022.”

²⁷ Expert Interview

Store operation costs are 209\$M in 2022, which is equal to 57% of corporate-owned revenue. This number will be stable and 59% from 2023 onwards, reflecting pre-covid averages and market price pressure. In 2028 store operation costs will amount to 50\$M.

SG&A related to corporate-owned stores is 33\$M in 2022. SG&A costs as a percentage of revenue will decrease from 6% to 3% until 2028, due to economies of scale. SG&A costs related to corporate-owned stores will amount to 51\$M in 2028. Total costs for corporate-owned stores is 557\$M in 2028 (15% CAGR 22-28).

2.2.2. Franchise EBITDA

Franchise EBITDA increases from 187\$M in 2022 to 439\$M in 2028 (15% CAGR 22-28). Corporate-owned store EBITDA margin increases from 58% in 2022 to 69% in 2028. In 2022, 56% of total EBITDA is generated through the franchise segment, this number will decrease to 53% in 2028. Franchise costs consist of SG&A costs (54% of total franchise revenue) and NAF costs (46%). SG&A costs as percentage of revenue decreases from 23% in 2022 to 15% in 2028. The reasons for that are economies of scale as well as improvement in the IT infrastructure (Value Lever “Margin Enhancement”). SG&A costs related to franchises are 94\$M in 2028.

Costs of the NAF are 64\$M in 2022. NAF will be 100% of NAF revenue in future periods. Therefore, NAF revenue will not have an EBITDA impact. However, the EBITDA margin will be diluted.

2.2.3. Equipment EBITDA

Equipment EBITDA will increase from 23\$M in 2022 to 54\$M in 2028 (15% CAGR 22-28). Equipment margin decreases from 16% in 2022 to 14% in 2028. Equipment costs are 122\$M in 2022 and consist of the cost of revenue (94%) and SG&A costs (6%). From 2023 onwards, the cost of revenue as a percentage of sales is 82%, based on the pre-Covid average and high market price pressure. In 2028, the cost of sales accounts for 311\$M. SG&A costs accounted

for equipment sales will rise from 7\$M in 2022 to 13\$M in 2028 (10% CAGR 22-28). Total Equipment costs in 2028 account for 324\$M (18% CAGR 22-28).

2.2.4. PF-App EBITDA

PF-App EBITDA is expected to be 43\$M in 2028 (45% CAGR 23-28). The app's EBITDA margin will be 69% in 2028. PF-App costs amount to 19\$M in 2028 and consist of external development costs (10\$T in 2028), internal development costs (163\$T), management costs (123\$T), content costs (206\$T), server costs (3\$,T) and App-Store commission (18,635\$T). App-Store commission is equal to 30% of revenue generated in the App. This corresponds to the costs for the Apple App-Store and Google Play-Store.²⁸

2.3. Balance Sheet

Net Working Capital increases from -80\$M in 2022 to -43\$M in 2028. Operating Cash remains stable at 2% of revenue (38\$M in 2028). Receivables are forecasted with DSO, Inventory with DIO, and Payables with DPO. Prepaid expenses, Accrued Expenses, Equipment deposits, and current deferred revenue are forecasted as a percentage of sales. All NWC drivers (except operating cash) will reach their pre-covid average in 2024. Afterward, they will increase (decrease) by 1% yearly.

PP&E, Intangible Assets (net) and Goodwill is forecasted by D&A and CAPEX (including acquisitions). Deferred income taxes are staying constant in the investment period. Right-of-use assets per corporate-owned store stay constant until 2028. Operating lease liabilities will be negatively equal to the right of used assets. Core Invested Capital will increase from 1,97\$M in 2022 to 3,834\$M in 2028. Non-Core Invested Capital is assumed not to be changed..

²⁸ Statista, "Commission rates for leading app stores worldwide as of July 2022."

2.4. Cash Flow

Free cash flow will increase to 539\$M in 2028. Depreciation and Amortization account for 189\$M in 2028, which leads to an EBIT of 646\$M in 2028. D&A is calculated based on the historic rates. Tax rates will stay constant at 21%. Net Operating Profit Less Adjusted Taxes (NOPLAT) will be 536\$M in 2028. Total CAPEX accounts for 198\$M in 2028. Maintenance CAPEX increases to 114\$M in 2028. This includes IT-CAPEX, CAPEX on existing stores and other CAPEX. CAPEX on existing stores per corporate owned store will decrease from 157\$T to 146\$T, which follows the historic trend reflects the rationalization of investment at the end of the investing period. IT CAPEX as percentage of revenue increases in 2023, due to the investment in the IT-system. The following periods this number will decrease as consequent of the rationalisation of investment. CAPEX for acquisition from franchisees is calculated based on the average revenue and the historical EV/Revenue multiple (5.3x). All acquisitions are paid in Cash. CAPEX related to M&A activities in Europe are calculated based on a 7.3x EV/EBITDA multiple. All acquisitions are paid in Cash.

2.5. Cases Assumptions

In the Bank Case, a 10% decrease of main revenue drivers are assumed. These drivers include drivers for franchise revenue, equipment revenue, corporate-owned store revenue (except. number of stores) and app revenue. Number of stores open decreases by 1 or 10% (rounded) depending on size. Costs of revenue drivers increases by 5%. The Balances Sheet drivers which are not affected by D&A and CAPEX increases on the Bank Case by 5%. In the Case “No international M&A”, no M&A activity in Europe is assumed as well as no openings of Franchise stores in Europe. In the Case “Next Pandemic”, a pandemic with the hard restrictions for 2023 and 2024 is assumed. For the affected driver, the Covid averages (2020 and 2021), are assumed, afterwards the investment case scenario will apply. Meanwhile, the app revenue driver increases in the same period.

Bibliography

- ABC Fitness Solutions.” The next fitness consumer – 10 Key findings”. Accessed October 10, 2022. <https://www.ihrsa.org/publications/the-next-fitness-consumer-key-findings/>
- EuropeActive, & Deloitte. “European Health and Fitness Market Report 2022”. Accessed November 13, 2022. <https://www2.deloitte.com/de/de/pages/consumer-business/articles/report-european-health-fitness.html>.
- IHRSA. “IHRSA Media Report: Part 2. Accessed September 10, 2022. <https://hub.ihrsa.org/en/2021-ihrsa-media-report-fall21>
- IHRSA Media Center.” Total U.S. Health Club Membership by Year”. Accessed September 9, 2022. <https://www.ihrsa.org/about/media-center/>
- JP Morgan. “Planet Fitness Equity Report, Sep 2022”. September 2022
- Morris, Kathy “THE 10 STATES WITH THE MOST GYMS (AND THE LEAST)”. Accessed October 15, 2022. <https://www.zippia.com/advice/states-most-gyms/>
- Rizzo, Nicholas. “Fitness Industry Statistics 2021-2028 [Market Research]. Accessed October 10, 2022. <https://runrepeat.com/fitness-industry>
- ScrapeHero. “Number of Planet Fitness locations in the United States“. Accessed October 16, 2022. <https://www.scrapehero.com/location-reports/Planet%20Fitness-USA/>
- Statista. “Average membership fee per month for fitness clubs in Germany from 2014 to 2019”. Accessed November 14, 2022. <https://www.statista.com/statistics/1044239/average-membership-fee-fitness-clubs-germany/>
- Statista.” Number of health clubs in the United States from 2008 to 2022”. Accessed September 9, 2022. <https://www.statista.com/statistics/244922/us-fitness-centers-und-health-clubs/>
- Statista.” Commission rates for leading app stores worldwide as of July 2022.” Accessed November 21, 2022. <https://www.statista.com/statistics/975776/revenue-split-leading-digital-content-store-worldwide/#:~:text=As%20of%20July%202022%2C%20Apple,after%20the%20subscriber's%20first%20year>