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Viability Report for The Save The Windmill Group on The Windmill Public House, Charlton, Hitchin, Hertfordshire, SG5 2AE, October 21st, 2015.

All the information contained in this report relates to documents provided by The Save The Windmill Group, in respect of a planning application for change of use to the above premises. The author is not, and has never been, associated with the business and has no prior knowledge of the business.

About the Author

The author is a Fellow of The British Institute of Innkeeping and during a career spanning 35 years has been a manager, a tenant, a lessee and a freehold/free house owner of public houses.

In addition, the author was, for over ten years, the Chief Operating Officer of an estate of 1,200 public houses made up of both tied and free of tie tenanted and leased public houses.

The author now publishes an industry leading website (How To Run A Pub), is the principal tutor at "Pub School" (run by leading training provider Brew School), is a regular contributor to pub industry publications and newsletters and is an independent consultant to those engaged in the public house industry in the UK.

Methodology

By utilising the British Beer and Pub Association (BBPA) and Association of Multiple Licensed Multiple Retailers (ALMR) benchmarks for a "character rural pub*" trading at up to £5,000 per week certain percentage of sales for specific lines in the overhead, can be applied to both a reconstituted and a forecast Profit & Loss Accounts. (See attached).

*This classification is most suited to The Windmill from a reading of the provided.

Reconstituted Profit & Loss Account - [redacted]

The information provided by the Applicant in respect of their planning application provides an extract of the Management Accounts for "[redacted] t/a Windmill". For the sake of clarity, the landlord was Charles Wells a family brewer based in Bedford.

These accounts would have been compiled by the landlord's authorised accountancy firm in accordance with clauses contained in the tenancy agreement to use a specific accountant. The tenancy would have also made provision for the services of an independent licensed stock taker to assist the tenant in "taking stock" and analysing concomitant stock take reports.

This author has reconstituted Mr [redacted]'s Management Accounts into the format used by the BBPA in analysing profit and loss figures supplied by its constituent members. The BBPA receives returns for many thousands of public houses throughout the UK via its constituent members and produces benchmarks for the tied pub industry from time to time.

As the information from Mr [redacted], who appears to have only traded for 9 months at The Windmill, is for a fully tied pub and the trading period ends in January 2015, this author has applied the BBPA benchmarks for January 2015 to the reconstituted profit & loss account, as being the most pertinent.

It should be noted there are two major exceptions to the profit & loss account, which in a normal trading year (i.e. not the start-up or initial year) would play no part in the ongoing profitability of a public house. The first is a charge for "surveyors and architects" and the second an entry marked as "queries" under finance charges.

It is this author's opinion both these charges related to the setting up of the tenancy agreement and should be excluded from a "normal" profit & loss account, as they would be funded from any initial investment and not from revenues.

First 9 Months Trading

Whilst the accounts provided by the applicant show them to be for the period ending January 31st, 2015 no start date is given for the first month (May 2014) and the relatively low numbers associated with sales, costs, overhead etc. indicate to this author a commencement date mid-month. In consequence, this author prefers to deal with complete months and has made calculations made upon this basis.

As one can see from the attached reconstituted profit & loss account the business operated at a trading profit of £840. Even if the applicant was to argue the exceptional charges were to be included in the account the business operated at a loss of £6,572. A small loss, such as this, would not be unusual for any business in it's first nine months, and had Mr [redacted] sufficient working capital would have been manageable. (See notes on Working Capital below).

12 Months Projected Trading

If one uses a straight-line projection of the trading information relating to the full months Mr [redacted]'s time at the pub to imagine a full year, one can see a trading profit of £748 and again if exceptional charges to the account are included the business would have operated at an, albeit smaller, loss of

£6,664. Again, a small overall loss during the first year of a business would not be unusual and Mr [redacted] may well have managed to absorb this loss.

R.E.O. & BBPA Benchmark

Many commercial landlords operating in the public house industry (brewers and "pubcos") and the Government Valuation Office use the concept of a Reasonably Efficient Operator (R.E.O.) when determining rents charged by the former and in assessing the rateable value of pubs by the latter. This is taken to be a business under the control of an experienced publican who would operate the business to maximise its trading potential and profitability.

By applying an R.E.O.'s business acumen and experience to a business such as The Windmill, a trading profit of £14,525 for a full year's trading can be extrapolated. Again, if the exception charges (sic) were applied to the account there would still be a trading profit of £7,113.

Notes on Mr [redacted]'s Management Accounts

Working Capital

In my experience, a tenant needs to have at least £20,000 working capital available to them. If they can have a further £10,000 in reserve then even better.

In the normal course of events, when a well-funded tenant takes on the tenancy of a pub such as The Windmill, they would purchase the outgoing tenant's fixtures and fittings (inventory) and these costs would form part of the initial capital injection made by a publican into their business.

It would appear from Mr [redacted]'s accounts he was unable to either part or fully purchase the inventory at The Windmill as the landlord was charging the business under the section titled Service Charges a line item of "Rentalisation of Inven" - which this author would take to be the Rentalisation of Inventory.

One can infer from this charge Mr [redacted] was under-capitalised when he took on The Windmill, which may have contributed to Mr [redacted]'s eventual business failure.

As is evinced from Mr [redacted]'s management accounts it would appear The Windmill is a seasonal business, with significant uplift in trade over the summer. This would be in keeping with the information available about the size and layout of the internal and external trading areas at the pub. Not considering, or perhaps not being aware of, the seasonal nature of the business may well have had an adverse effect on Mr [redacted]'s cash-flow. Being under-capitalised (sic) to start with it is likely Mr [redacted] would not have had sufficient working capital to allow the business to function during the quieter off-season.

Given January and February are notoriously quiet months in the pub industry it is hardly surprising Mr [redacted] did not continue trading after January 2015 as the business would have simply run out of money.

Gross Profitability

Whilst Mr [redacted] was achieving a satisfactory level of gross profit on the wet (drinks) sales at the pub of 54.41% (£40,974) against a BBPA benchmark of 53.1%, the dry (food) operation was clearly operating at a hugely depressed level of gross profitability at 32% (£9,596).

The BBPA reckon a REO will operate their food business at a gross profit of 61.9% for a pub of this nature. The low level of gross profit derived from the food operation by Mr [redacted] (32%) would have a demonstrably negative effect on overall profit, to the tune of approximately £8,965.

This amount of "lost profit" might have meant an overall trading profit of some £9,806 in the first nine months (£2,394 allowing for exceptional costs detailed above). A full 12-month projection may have produced an overall trading profit of £13,931 (£6,519 with exceptional costs included).

It is unclear why Mr [redacted] chose to operate his food operation at such a reduced level of profitability, however inexperience in commercial catering or an ill-advised level of promotional pricing (loss-leading) are highly likely.

It is the opinion of this author, The Windmill if operated by a REO would have achieved in the region of £14,525 overall trading profit (£7,113 with exceptional costs included) on the sales generated by Mr [redacted].

Control of Costs

For whatever reason, certain line items of cost are at variance with what the BBPA reckon to be average operating costs for a pub similar to The Windmill.

Whilst Mr [redacted] might be commended for controlling certain costs from a reading of the information provided clearly there were some unexpected levels of expenditure, which, had he been sufficiently capitalised would have been bearable. For instance, Repairs, Maintenance & Renewals are very high for such premises, as are the professional fees (although these may be beyond the control of a Charles Wells tenant), equipment hire and the total of other costs.

The overall effect on trading profit was to increase overheads by £1,946 against reasonable expectations with a concomitant effect on trading profit.

Viability of The Windmill

Also attached to this report are projected Profit & Loss accounts for The Windmill detailing how it might operate under the management of a REO under various tenure arrangements and experiencing those costs the BBPA would associate with a similar public house.

Mr [redacted]s sales figures and those extrapolated for a full year are used as the base for all calculations and no assumption of an uplift in business have been applied to these projected accounts.

Tied Lease/Tenancy Agreement

It is the author's belief The Windmill, if operated by a competent operator could achieve a trading profit of £14,567 under a tied agreement.

Free of Tie Lease/Tenancy Agreement

It is the author's belief The Windmill, if operated by a competent operator could achieve a trading profit of £22,516 under a free of tie agreement.

Considerable saving is available to free of tie customers compared to their tied colleagues, in this case somewhere in excess of £17,000 per annum on purchases for the bar alone, which would more than mitigate the expected increase in overheads approaching £13,000 per annum.

Freehold Free House

It is the author's belief The Windmill, if operated under competent ownership and management could achieve a trading profit of £28,249 with the benefit of the freehold and annual finance costs of 5% on a total start-up cost of £400,000. Similar savings on purchasing of wet stocks as a Free of Tie lessee/tenant would be experienced, in addition to a reduction in overhead as certain "landlord costs" are eliminated to the tune of £4,000 per annum.

Conclusion

The applicant has shown no real understanding of the financial workings of a public house and presents no evidence to support their assertion the pub is unviable apart from anecdotal evidence and opinion.

The fact the pub was disposed of by Charles Wells is neither here nor there in terms of assessing its viability if operated by a reasonably efficient operator. The applicant can have no knowledge of Charles Wells' motives or criteria for retaining or disposing of their commercial property portfolio and no conclusions as to the pub's viability on an owner/operator basis can be drawn from its sale.

It is the professional opinion of this author The Windmill is viable as a public house with either a willing landlord, whether operated on a tied or free of tie basis; or with the benefit of the freehold being owned by the pub's operator.

This would be especially true of a well-funded and committed community group purchasing the freehold interest in the property. The Save The Windmill Group is one such organisation and is an interest group of many hundreds of local people who would be ready to not only invest in the business but would, as experienced in many hundreds of community-run pubs, also become regular patrons of the business.

In terms of true viability, that is the ability for a business to break-even, a freehold free house operator would experience a considerably lower break-even point than their tenanted or leased colleagues. Break-even is calculated by dividing the total overhead of a business by its Gross Profit percentage.

In this case break-even would be achieved at £2,071 per week, which would allow some comfort during off-season months and when the inevitable unforeseen happens and additional expenditure is required.

This figure is considerably less than the levels of sales generated by the last tenant at the pub who was trading at a level fully 23% above this threshold.

Philip Sambell FBII

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