

Analyst: Sung Nam

Town Sports International Holdings Inc (CLUB)

Market Price:	\$7.26	EBITDA/Share:	\$3.09	Net Asset/Share:	-\$1.74
DCF: EV/EBITDA Terminal Value	-1.801%	DCF: Net Tangible Asset excluding Cash/Debt Terminal Value	-196.448%		
EBITDA-Cap Ex/Share	\$1.78	EVA Analysis:	-2.004%		

Overview

The fitness club space hasn't performed well for the past 2 years. As the economy turned sour, membership dropped as the general public had to cut discretionary spending. The same goes for Town Sports.

Growth is negative, cash flow is negative. EBITDA can cover the debt interest, but principal reductions will be slim based on the cash flow. Also, the book value is negative.

We have a cautious stance on the stock, which has rallied 83% in the past year.

Dividend?

Dividend yield is 0.0%.

Cashflow Generation

Cashflows are \$2MM from operating cashflow.

Capex is \$22 MM, minority interest payment is \$0 MM, intangibles are \$50 MM and dividend is \$0 MM.

Free cash flow is about -\$20 MM.

4.0% EBITA margin and FCF yield is 7.0%.

The company has \$39 MM in cash/short term investment and \$317 MM in debt.

We are projecting a \$0 MM paydown annually.

Profitability

ROA is -0.1%, and ROC is 4.2%.

LBO?

We don't believe a 60% debt/40% equity would be sustainable.

Price

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LBO Analysis

WACC Terminal Value:		Intrinsic Price in 5 Years:	2.64	Non-LBO Forecast	Year 1 Target	5.93	Non-LBO Forecast	Desired Return Rate	20.00%
EV/EBITDA with 5X Multiple Terminal Value:	\$6.63	Market Price:	7.26		Year 2 Target	4.84		Implied Today's Price	1.06
Net Tangible Asset Terminal Value:	\$0.00	LBO Price:	7.26		Year 3 Target	3.96		Overvalued/(Undervalued)	584.16%
EV/EBITDA with Today's Multiple Terminal Value:	\$0.09	Premium to Market Price:	0.00%		Year 4 Target	3.23			
EVA Enterprise Value:	\$3.84	LBO Price/Intrinsic Price Target:	-18.31%		Year 5 Target	2.64			
Dividend Discount Model:	N/A	LBO Price/EV/EBIT Exit Price:	-66.20%	Implied IRR (Market Price):					
Average (Excluding Dividend Discount):	\$2.64	Implied IRR at today's EV/EBITDA:	-58.15%						
		5 Year Return:	-63.63%						

Current Evaluation				Exit Evaluation			
Current Market Price:	7.26	LBO Price:	7.26	Exit Price:	2.64	Exit Price:	0.09
Outstanding Shares:	22,850,000	Outstanding Shares:	22,850,000	Outstanding Shares:	22,850,000	Outstanding Shares:	22,850,000
Market Capitalization:	165,891,000	Market Capitalization:	165,891,000	Market Capitalization:	60,334,952	Market Capitalization:	2,129,596
Available Cash:	38,800,000	Available Cash:	38,800,000	Available Cash:	94,611,641	Available Cash:	94,611,641
Debt:	316,510,000	Debt:	316,510,000	Debt:	316,510,000	Debt:	316,510,000
Net Cash:	-277,710,000	Net Cash:	-277,710,000	Net Cash:	-221,898,359	Net Cash:	-221,898,359
Enterprise Value:	443,601,000	Enterprise Value:	443,601,000	Enterprise Value:	282,233,311	Enterprise Value:	224,027,955
Original EV/EBITDA:	24.06	EV/EBITDA:	24.06	EV/EBITDA at 5 Years:	14.34	EV/EBITDA at 5 Years:	3.00
Original EV/EBITDA:	6.28	EV/EBITDA:	6.28	EV/EBITDA at 5 Years:	6.44	EV/EBITDA at 5 Years:	3.26
Competitor Average EV/EBIT:	N/A						
Competitor Average EV/EBITDA:	N/A						

Enterprise Valuation Calculation During Holding Period							
Time Period	0	Adjusted for LBO	1	2	3	4	5
Annualized Price Targets based off LBO Price:	7.26	7.26	5.93	4.84	3.96	3.23	2.64
Shares Outstanding:	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000
Market Capitalization:	165,891,000	165,891,000	135,510,221	110,693,287	90,421,251	73,861,775	60,334,952
Available Cash:	38,800,000	38,800,000	39,113,092	52,604,300	66,908,692	80,813,690	94,611,641
Debt:	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000
Net Cash:	-277,710,000	-277,710,000	-277,396,908	-263,905,700	-249,601,308	-235,696,310	-221,898,359
Enterprise Value:	443,601,000	443,601,000	412,907,129	374,598,987	340,022,559	309,558,085	282,233,311
EBIT	18,440,000	18,440,000	6,497,870	19,675,985	19,675,985	19,675,985	19,675,985
EV/EBIT:	24.06	24.06	63.54	19.04	17.28	15.73	14.34
EBITDA	70,640,000	70,640,000	55,245,892	68,424,007	69,237,192	68,837,798	68,730,751
EV/EBITDA:	6.28	6.28	7.47	5.47	4.91	4.50	4.11

Enterprise Valuation Calculation During Holding Period							
Time Period	0	Adjusted for LBO	1	2	3	4	5
Annualized Price Targets based off LBO Price:	7.26	7.26	-5.30	9.17	9.79	10.40	11.00
Shares Outstanding:	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000	22,850,000
Market Capitalization:	165,891,000	165,891,000	-121,081,201	209,428,715	223,733,107	237,638,105	251,436,056
Available Cash:	38,800,000	38,800,000	39,113,092	52,604,300	66,908,692	80,813,690	94,611,641
Debt:	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000	316,510,000
Net Cash:	-277,710,000	-277,710,000	-277,396,908	-263,905,700	-249,601,308	-235,696,310	-221,898,359
Enterprise Value:	443,601,000	443,601,000	156,315,707	473,334,416	473,334,416	473,334,416	473,334,416
EBIT	18,440,000	18,440,000	6,497,870	19,675,985	19,675,985	19,675,985	19,675,985
EV/EBIT:	24.06	24.06	24.06	24.06	24.06	24.06	24.06
EBITDA	70,640,000	70,640,000	55,245,892	68,424,007	69,237,192	68,837,798	68,730,751
EV/EBITDA:	6.28	6.28	2.83	6.92	6.84	6.88	6.89

LBO Price	7.26	Equity Partners:	482,401,000	Weighting	100.00%	Annualized Return for Equity Partners: -66.20%
Shares Outstanding	22,850,000	Debt Partners:	0		0.00%	
Market Capitalization	165,891,000	Total Funds for LBO:	482,401,000		100.00%	
Debt	316,510,000					
Cash	38,800,000					
Enterprise Value	443,601,000					
Capital Investment	482,401,000					

Book Value		Enterprise Value		Stock Valuation		Debt Reduction	
Beginning Book Value	-6.95	Beginning Enterprise Value	443.60	Current Market Price	\$7.26	Starting Debt	301.96
Year 5 Book Value	-46.41	Year 5 Enterprise Value	224.03	Year 5 Market Price	\$0.09	Debt Repayment	0.00
Annualized Return	46.19%	Annualized Return	-12.77%	Annualized Return	-58.15%	Year 5 Ending Debt	301.96
						% of Starting Debt	100.00%

	Historical				Forecasted				
	12 months ending 2007-12-31	12 months ending 2008-12-31	12 months ending 2009-12-31	12 months ending 2010-12-31	2011	2012	2013	2014	2015
Revenue	472.92	506.71	485.39	462.39	439.27	439.27	439.27	439.27	439.27
COGS	156.66	172.41	178.85	174.13	171.32	166.92	166.92	166.92	166.92
Gross margin	316.26	334.30	306.54	288.26	267.96	272.35	272.35	272.35	272.35
SG&A	212.45	227.53	225.48	214.36	206.46	197.67	197.67	197.67	197.67
R&D	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Unusual expense	12.52	21.48	16.90	3.25	0.00	0.00	0.00	0.00	0.00
Other operating expense	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Depreciation is: Included within COGS	45.97	52.47	56.54	52.21	55.00	55.00	55.00	55.00	55.00
Operating Income (EBITA)	45.32	32.82	7.82	18.44	6.50	19.68	19.68	19.68	19.68
Interest income/(expense)	-23.53	-21.28	-19.09	-18.87	-24.93	-24.93	-24.93	-24.93	-24.93
Gain (loss) on sale of asset	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Other	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Income before tax	21.79	11.54	-11.47	-0.43	-18.43	-5.26	-5.26	-5.26	-5.26
Tax	8.14	9.20	-5.80	-0.14	0.00	0.00	0.00	0.00	0.00
Income after tax	13.65	2.34	-5.67	-0.29	-18.43	-5.26	-5.26	-5.26	-5.26
Minority Interest	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Equity in affiliates	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net income	13.65	2.34	-5.67	-0.29	-18.43	-5.26	-5.26	-5.26	-5.26
*Figures are in millions (\$)									
Revenue Growth	N/A	7.14%	-4.21%	-4.74%	-5.00%	0.00%	0.00%	0.00%	0.00%
Tax Rate	37.36%	79.72%	50.57%	32.56%	30.00%	30.00%	30.00%	30.00%	30.00%
Implied Debt Interest Rate	-7.45%	-6.30%	-6.00%	-5.96%	-8.26%	-8.26%	-8.26%	-8.26%	-8.26%
Margins									
COGS	33.13%	34.03%	36.85%	37.66%	39.00%	38.00%	38.00%	38.00%	38.00%
Gross margin	66.87%	65.97%	63.15%	62.34%	61.00%	62.00%	62.00%	62.00%	62.00%
SG&A	44.92%	44.90%	46.45%	46.36%	47.00%	45.00%	45.00%	45.00%	45.00%
R&D	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Unusual expense	2.65%	4.24%	3.48%	0.70%	0.00%	0.00%	0.00%	0.00%	0.00%
Other operating expense	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Depreciation is: Included within COGS	9.72%	10.36%	11.65%	11.29%	12.52%	12.52%	12.52%	12.52%	12.52%
Operating Income (EBITA)	9.58%	6.48%	1.57%	3.99%	1.48%	4.48%	4.48%	4.48%	4.48%
Interest income/(expense)	-4.98%	-4.20%	-3.93%	-4.08%	-5.68%	-5.68%	-5.68%	-5.68%	-5.68%
Gain (loss) on sale of asset	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Other	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Income before tax	4.61%	2.28%	-2.36%	-0.09%	-4.20%	-1.20%	-1.20%	-1.20%	-1.20%
Tax	1.72%	1.82%	-1.19%	-0.03%	0.00%	0.00%	0.00%	0.00%	0.00%
Income after tax	2.89%	0.46%	-1.17%	-0.06%	-4.20%	-1.20%	-1.20%	-1.20%	-1.20%
Minority Interest	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Equity in affiliates	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Net income	2.89%	0.46%	-1.17%	-0.06%	-4.20%	-1.20%	-1.20%	-1.20%	-1.20%

					Adjustment		Adjusted Proforma	2011	2012	2013	2014	2015
	As of 2007-12-31	As of 2008-12-31	As of 2009-12-31	As of 2010-12-31	+	-						
Cash	5.46	10.40	10.76	38.80			38.80	39.11	52.60	66.91	80.81	94.61
Short term investment	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Cash and Short term	5.46	10.40	10.76	38.80			38.80	39.11	52.60	66.91	80.81	94.61
Accounts Receivable	8.81	4.51	4.29	5.26			5.26	5.26	5.26	5.26	5.26	5.26
Other receivables	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Total Receivables	8.81	4.51	4.29	5.26			5.26	5.26	5.26	5.26	5.26	5.26
Deferred Income Tax	0.01	0.00	0.01	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Total Inventory	0.23	0.14	0.22	0.22			0.22	0.22	0.22	0.22	0.22	0.22
Prepaid Expenses	11.33	22.27	11.54	20.55			20.55	20.55	20.55	20.55	20.55	20.55
Other Current Assets	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Current Assets	25.84	37.32	26.82	64.83	0.00	0.00	64.83	65.14	78.63	92.94	106.84	120.64
PP&E, Gross	595.86	674.12	680.01	659.91			659.91	689.91	719.91	749.91	779.91	809.91
Change in Depreciation	45.96	52.48	56.53	52.20			52.20	48.75	48.75	49.56	49.16	49.05
Accumulated Depreciation	258.71	301.00	357.53	409.73			409.73	458.48	507.23	556.79	605.95	655.00
PP&E, Net	337.15	373.12	322.48	250.18			250.18	231.43	212.68	193.12	173.96	154.91
Goodwill	50.16	32.61	32.64	32.79	0.00		32.79	32.79	32.79	32.79	32.79	32.79
Intangibles	0.48	0.28	0.15	0.04			0.04	0.04	0.04	0.04	0.04	0.04
Long term investments	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Other long term assets	75.13	68.31	67.59	57.12			57.12	57.12	57.12	57.12	57.12	57.12
Long Term Assets	721.63	775.32	422.86	340.13			340.13	321.38	302.63	283.07	263.91	244.86
Total Assets	488.76	511.64	467.47	464.17	0.00	0.00	404.96	366.53	381.27	376.01	370.75	365.50
Accounts Payable	10.89	7.27	6.01	4.01			4.01	4.01	4.01	4.01	4.01	4.01
Accrued Expense	34.92	36.09	30.23	34.06			34.06	34.06	34.06	34.06	34.06	34.06
Other current Liabilities	42.61	40.33	35.35	35.11			35.11	35.11	35.11	35.11	35.11	35.11
Total Current Liabilities	88.42	83.69	71.59	73.18	0.00	0.00	73.18	73.18	73.18	73.18	73.18	73.18
Notes Payables/Short Term Debt	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Current port. Of LT Debt/Capital Leases	10.90	20.85	1.85	14.55			14.55	14.55	14.55	14.55	14.55	14.55
Long term Debt	305.12	317.16	316.51	301.96	0.00	0.00	301.96	301.96	301.96	301.96	301.96	301.96
Capital Lease Obligations	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Total Interest Earning Debt	316.02	338.01	318.36	316.51	0.00	0.00	316.51	316.51	316.51	316.51	316.51	316.51
Deferred Income tax	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Minority Interest	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Other liabilities	84.13	89.17	85.75	81.43			81.43	81.43	81.43	81.43	81.43	81.43
Total Liabilities	488.57	510.87	475.70	471.12	0.00	0.00	471.12	471.12	471.12	471.12	471.12	471.12
Redeemable Preferred Stock	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Non-redeemable Preferred Stock	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Common Stock	0.03	0.03	0.02	0.02		0.00	0.02	0.02	0.02	0.02	0.02	0.02
Additional Paid-in capital	-16.98	-18.98	-22.57	-21.79	0.00	0.00	-21.79	-21.79	-21.79	-21.79	-21.79	-21.79
Dividends Paid	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Retained Earnings	16.32	18.66	12.99	12.70		0.00	12.70	-5.73	-10.99	-16.25	-21.51	-26.76
Treasury Stock	0.00	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00
Other Equity	0.81	1.07	1.33	2.12		0.00	2.12	2.12	2.12	2.12	2.12	2.12
Total Equity	0.18	0.78	-8.23	-6.95	0.00	0.00	-6.95	-25.38	-30.64	-35.90	-41.16	-46.41
Liability + Equity	488.75	511.65	467.47	464.17	0.00	0.00	464.17	445.74	440.48	435.22	429.96	424.71
Variance	0.01	-0.01	0.00	0.00			-59.21	-59.21	-59.21	-59.21	-59.21	-59.21
Debt/Equity	1,755.67	433.35	-38.68	-45.54			-45.54	-12.47	-10.33	-8.82	-7.69	-6.82
Inventory Turnover	2,056.17	3,619.36	2,206.32	2,101.77			2,101.77	1,996.68	1,996.68	1,996.68	1,996.68	1,996.68
Inventory Turnover Days	0.18	0.10	0.17	0.17			0.17	0.18	0.18	0.18	0.18	0.18
Days Inventory Outstanding	0.54	0.30	0.45	0.46			0.46	0.47	0.48	0.48	0.48	0.48
Accounts Receivable Turnover	53.68	112.35	113.14	87.91			87.91	83.51	83.51	83.51	83.51	83.51
Accounts Receivable Turnover Days	6.80	3.25	3.23	4.15			4.15	4.37	4.37	4.37	4.37	4.37
Days Payable Outstanding	25.37	15.39	12.27	8.41			8.41	8.54	8.77	8.77	8.77	8.77
Days Sales Outstanding	6.80	3.25	3.23	4.15			4.15	4.15	4.37	4.37	4.37	4.37
Cash Conversion Cycle	-18.04	-11.85	-8.59	-3.79			-3.79	-3.92	-3.92	-3.92	-3.92	-3.92

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LBO Debt Schedule

	Proforma	2011	2012	2013	2014	2015
Net Change in Cash	28.05	0.31	13.49	14.30	13.90	13.80
Current Portion Debt Repayment						
Long Term Debt Repayment						
Outstanding Debt	316.51	316.51	316.51	316.51	316.51	316.51
Current Portion Debt Balance	14.55	14.55	14.55	14.55	14.55	14.55
Long Term Debt Balance	301.96	301.96	301.96	301.96	301.96	301.96
Forward Libor Curve		4.00%	4.00%	4.00%	4.00%	4.00%
Spread		4.00%	4.00%	4.00%	4.00%	4.00%
Interest Rate		8.00%	8.00%	8.00%	8.00%	8.00%
Interest Expense		25.32	25.32	25.32	25.32	25.32
Cash Balance		38.80				
Interest @ 1.0%		0.39	0.39	0.39	0.39	0.39
Net Interest Expense/(Income)		24.93	24.93	24.93	24.93	24.93
Net Interest Rate		8.26%	8.26%	8.26%	8.26%	8.26%
EBITDA		6.50	19.68	19.68	19.68	19.68
EBITDA/Interest Expense Coverage		0.26	0.78	0.78	0.78	0.78

Interest Rate Coverage Table

Debt Rating					
AAA					
AA					
A+					
A					
A-					
BBB					
BB+					
BB					
B+					
B					
B-					
CCC					
CC					
C		C	C	C	C
D	D				

*Source: NYU; Professor Damodaran