Affinity Education latest childcare operator to join buying spree

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EXCERPTS

Childcare operator Affinity Education has increased the price it is willing to pay for growth, announcing it will buy 51 centres in an $80-million deal that is equivalent to about two-thirds of its market value.
The deal is a sign that two major corporate operators, Affinity and G8 Education, are willing to break their own internal rules on how much they will pay to buy up centres in the fragmented sector, which is dominated by independent operators.

After listing on the Australian Securities Exchange in December 2013 with a promise to keep the price of acquisitions under 4.1-times future earnings before interest and tax, Affinity said it would pay 5.2-times EBIT, on a rolling 12-month basis, for the latest collection of centres. The $80 million purchase price is composed of $65 million in cash and about $15 million in shares.

The deal follows G8's acquisition in late March of 91 centres for $228 million, at a price of 5.79-times EBIT in the 2015 financial year. G8, which is the largest for-profit childcare operator with 388 centres and about 6 per cent of the market, said this latest acquisition was a one-off and it would return to paying lower prices in future.

So far, investors have lapped up the aggressive growth strategies of G8 and Affinity. The share price of G8, which has a market value of $1.5 billion, has risen 122 per cent in the past year. Affinity shares have gained 29 per cent since the December listing.

But Affinity's latest deal, which takes the total amount outlaid in 2014 by the two companies to $413 million, may be a sign that owner-operators have cottoned on to the corporate players' strategy and will demand higher prices before selling their assets. This scenario may remind investors of Eddy Groves' ABC Learning, which collapsed in 2008 under billions of dollars in debt after overpaying for centres.

Affinity chief executive Justin Laboo said it was difficult to get transparency across the sector when EBIT multiples were used as measure of price. ''It's not clear what others in the market actually include in that multiple,'' he said.

Affinity, which has a market value of $120 million, would begin to describe deals on the basis of whether or not they would add to future profit, he said. Mr Laboo said the latest deal would be ''very accretive'' on an earnings per share basis.

He denied the latest price paid was a sign Affinity was growing at an unsustainable rate. ''We certainly haven't secured every asset in terms of that we've looked at,'' he said.

The deal takes Affinity's footprint to 119 centres and gives it access to Perth for the first time. Mr Laboo called it a ''step change'' acquisition. ''Growth has been a very important part of the Affinity story,'' he said.

The 51-centre buy included 29 centres from one unnamed corporate operator. The vendor will take on 11 million Affinity shares at $1.365 a share (2¢ higher than the closing price on Friday), which will be held in escrow for six to 12 months.

Affinity is seeking to raise $75 million in a three-for-four renounceable entitlement offer to shareholders, priced at $1.12 a share. The firm is also negotiating with banks to increase its available debt funding. Its shares remain in a trading halt.

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