COAST CAPITAL

May 17, 2021

Coast Capital to Vote Against the Proposed Disposal of FirstGroup's Crown Jewel Businesses at a Negative Premium

- The proposed transaction is the result of a suboptimal and incomplete process at an inopportune time, made worse by a distribution of proceeds which sees long-suffering shareholders receiving just 12% of proceeds
- Coast Capital has already been contacted by many shareholders who express frustration with this deal, and proposed use of proceeds
- Proposal has resulted in a 23% share price decline, equating to approximately £270m in shareholder capital lost since the announcement of this deal
- Shareholders are being asked to vote in favor for a negative premium for their most valuable businesses after just 17 days to review, in the absence of a fairness opinion and in the absence of a concrete timetable for the full distribution of proceeds

Coast Capital, the largest shareholder in FirstGroup PLC, urges its fellow shareholders in FirstGroup PLC to vote against the proposed disposal of the company's crown jewel assets, First Student and First Transit, unless the terms of the proposal are rapidly and substantively improved.

The proposed transaction values these sector-leading assets at a significant negative premium to their book value, and is the result of a questionable and non-exhaustive sale process. The announcement of the proposed sale has led to a 23% share price decline in FGP's stock – a notable and unacceptable underperformance against the sector. The inexplicably rushed window to vote in just 17 days, lack of fairness opinion, opacity around terms of the deal (with shareholders being forced to view the 160+ page SPA document in person during a pandemic) all point to a process that is unacceptable to shareholders, fails to maximize the benefit of proceeds for all stakeholders and make it intentionally difficult for new bidders to present superior offers. Moreover, shareholders stand to receive less than 12% of the proceeds from the transaction, in a timeline they do not control, in exchange for handing over an asset that accounts for 80% of the value of the company.

Indeed, this proposal is unacceptable to any reasonable stakeholder on many grounds:

A. First Student and First Transit compose the largest school bus and transit operations in North America. The company's only true peer, Student Transportation Inc, sold for 5.7x book value, or 12.5x EBITDA in 2018. Meanwhile, FirstGroup's board is incomprehensibly rushing shareholders to support a sale of these market leading businesses at less than its book value and less than 7 times depressed EBITDA. Coast Capital is unable to identify any public transport company of size which has recently sold assets for less than 2x book value.

B. Coast Capital has examined all major disposals of UK corporations and subsidiaries thereof over the prior 2 years, and notes that not one board has recommended a sale of the company, or division of their company, for less than book value. FirstGroup's board marks a new and unacceptable low among the company's peers in the UK.[2]

C. The company's opaque process and rushed request for a vote have hindered shareholders from understanding how inefficient and non-exhaustive the proposal is in terms of viable alternatives that could unlock significantly greater value to the benefit of all stakeholders:

   a. The deal was marketed to and shared with only approximately 10 parties under NDA, during a pandemic when most of the operations were not in service.

   b. Shortly before announcement, Coast Capital presented the company with an alternative route to exit at a notably higher valuation. By the company's own advisers' admission, value under Coast's proposal "could be … 25% greater than the proposed EQT deal". Coast can verify that the board has categorically refused to entertain or study the more attractive alternatives.[1]

   c. Coast has been approached by alternative potential acquirers who were not given access to the process and continue to be declined access, due to a punitive 'No Shop' clause which the board has agreed to in the proposed SPA. Under this clause, the board is now refusing to discuss First Student and First Transit with interested parties who are prepared to pay a (notably) higher price than book value for these assets, but who are afraid of publicly expressing their interest lest they be ruled out as potential bidders

D. The board's extraordinarily inefficient proposed use of proceeds further shifts value away from key stakeholders (including shareholders) and adds to this proposal's demerits. Under this ill-advised proposal, the board seeks to over cash-collateralize liabilities, and stash cash away for management's discretion which could, as management has put it "be released over time". In light of management's track record of mismanagement of assets and value destruction, shareholders cannot trust this board or management to retain shareholder's capital (note that the board and management own just 0.11% of the company.)

E. Upon review of the SPA (which the company is providing access to only in person during a pandemic) Coast Capital was able to deduce that the terms of the £170 million earn-out for First Transit is drafted in a way that gives EQT ample room to not pay this earn-out to FirstGroup should EQT hold the asset beyond 3 years. By implication, the £170m earn-out cannot be regarded as a certainty as management has indicated. In sum, EQT has risked little to potentially gain hundreds of millions in value by acquiring the most important transit operations in North America for less than 3x normalized EBITDA.

F. Despite 3 major multi-national banks advising the company on the transaction, not one has provided a fairness opinion on this disposal (perhaps because there is no justification for this below-market sale through a broken process).

Note that Coast Capital is not in any way seeking a reallocation of proceeds that would leave a deficit to the group's pension obligations or an over-levered FirstGroup. However, unless significant additional proceeds are allocated to shareholders (a path which we have detailed below), shareholders are clearly better off not supporting the board's proposal:

A. After having already over cash-collateralized existing stakeholder liabilities, the board could easily increase distributions to shareholders with an additional £235m capital above the proposed £365m from the following:
   a. Better than expected rail termination proceeds (already announced): £50m
   b. Estimated cash generation from Sept 2020 (mgmt. hasn't shared yet): £50m
   c. Cash released from pro-forma target 2x net debt ratio (managements stated target): £135m

This ***excludes management expected material cash inflows*** from the following:

a. EQT earn-out: £170m
b. Cash released from triennial review: £116m
c. Greyhound real estate sales: c. £40m
d. Divestment of Greyhound operations
e. US CARES Act proceeds & other related receivables from EQT
f. Working capital adjustments

B. With the now £600m cash proceeds, the board should tender for up to 550m shares outstanding at 110p (establishing a baseline valuation), rather than the tax inefficient 30p dividend.

C. If the share price exceeds 110p before all cash proceeds are distributed, reassess use of proceeds for what could be a higher tender, dividend or excess cash on the balance sheet.

The outcome of £600m used for a 110p tender would acquire c. 550m shares, or 45% of the 1.2bn shares outstanding. According to analysts and management, the remaining business would have a value of c.£900m - c. £1.2bn, against just 670m shares outstanding, equating to a value of 135p – 180p.

The proposed use of proceeds is unnecessarily inefficient and the inexplicably abbreviated timeline for this vote is likely meant to sow fear and confusion among shareholders to accept, for no good reason, a negative premium on these market leading businesses. This is made worse by the fact that public support for infrastructure assets and education related enterprises in the United States has never been higher. The Biden Administration has put forth a $2.3 trillion infrastructure bill which allocates $174 billion towards investments in electronic vehicles including the nations school bus fleet. These are grants for operations such as First Student, which EQT will no-doubt capitalize on.

Unless this proposal is meaningfully improved, we recommend that all stakeholders repudiate and vote against this flawed and inadequate proposal on 27 May. If an improved deal is not deliverable within the existing construct, the company should retain its key assets and pursue a complete, competitive, and transparent process that looks at a wide range of value creation alternatives with the benefit of schools reopening, a better market and macro backdrop as the pandemic is progressively brought under control.

Coast Capital welcomes the opportunity to present our detailed thoughts on the shortcomings of the proposed deal and viable alternatives for value maximization directly to our fellow shareholders in the coming week.

References

[1] After Coast presented a credible and superior alternative transaction to the company in April (which the chairman refused to even consider), Richard Perelman the company's advisor wrote in an email to the chairman (accidentally shared by the latter with Coast capital on April 22nd) that "Coast['s] proposal [could be seen as] …at least 25% more attractive than EQT" and that "[Coast] will want to feel we looked at it with an open mind and were not too quick to dismiss it." The company categorically ignored our more compelling proposal and decided to release this ill conceived and destructive deal day after even their advisor said that they should at least pretend to consider Coast's proposal.

[2] Not a single transaction has been conducted in the UK over past two years on a price below book value…(until this proposal!):

Date	Target	P/BV
Mar-21	Tavistock Investments Plc	1.1x
Aug-20	United Oil & Gas Plc	1.1x
Mar-21	ADES International Holding PLC	1.2x
Jan-21	Wolseley UK	1.2x
Apr-21	Equiniti Group plc	1.3x
Apr-21	Elementis plc	1.4x
Nov-20	RSA Insurance Group plc	1.6x
Dec-20	Zoltav Resources Inc.	1.7x
Oct-20	Victoria plc	1.7x
Mar-21	Narragansett Electric Company	1.7x
Jul-20	Deltic Energy Plc	1.8x
Dec-20	Calisen plc	1.8x
Mar-21	Trans-Siberian Gold plc	1.8x
Mar-21	Aggreko Plc	2.0x
Jan-21	AFH Financial Group Plc	2.4x
Jan-21	AFH Financial Group Plc	2.4x
Nov-20	Countrywide plc	2.4x
Oct-20	KAZ Minerals PLC	2.4x
Nov-20	Telit Communications PLC	2.5x
Apr-21	Nortek Air Management	2.5x
Jan-21	Marston's PLC	2.5x
Dec-20	Applegreen plc	2.7x
Jun-20	Rosemont Pharmaceuticals Limited	2.9x
Feb-21	Signature Aviation plc	3.0x
Oct-20	Talk Talk Telecom	3.0x
Aug-20	SDL plc	3.0x
Jan-21	Entain Plc	3.0x
Mar-21	Gamesys Group plc	3.8x
Jan-20	Delphi Technologies plc	4.4x
Jan-21	Cardtronics plc	4.8x
Dec-20	IMImobile PLC	4.8x
Feb-21	Arrow Global Group PLC	4.8x
Mar-20	Viridor Waste Management Limited	5.3x
Mar-21	Aviva Poland Business	5.6x
Feb-21	IDOX plc	5.8x
Feb-21	Nucleus Financial Group plc	6.3x
Oct-20	G4S plc	7.1x
Sep-20	TCS Group Holding PLC	7.3x
Dec-20	Codemasters Group	8.6x
Feb-21	GW Pharmaceuticals Plc	9.4x
Apr-21	Wey Education plc	9.6x
Total Number of Transactions		**41**
Total Number of Transactions with P/BV < 1.0x		**0**
Average P/BV		**3.5x**

Source: Capital IQ, publicly available financial data