

Centrica

Solid H1 and a price rise amid the transition

Centrica's solid H1 numbers and 12.5% electricity tariff increase announced yesterday morning were both in line with market expectations. Operationally, the business was resilient given this year's warm weather and challenging competitive dynamics. The political impact of the tariff hike was mitigated by protecting 200,000 vulnerable customers, a move we view as sensible given especially high levels of political risk in UK retail energy currently. The bigger story for Centrica shareholders remains the long-term shift away from upstream 'asset businesses' to tech-enabled customer businesses. Yesterday's announcements do not change that strategy and the reality is that Centrica is very early in its strategic change of direction.

H117 results in line and electricity tariffs raised

With EBITDA up 2% h-o-h, underlying adjusted operating cash flow flat and net debt reduced to £2.9bn, Centrica's H117 numbers were "solid", according to the CEO. Given headwinds in the gas business from warm weather, continuing high levels of competition in consumer and high customer switching, we view "solid" as a pretty good achievement, all things considered. The 12.5% electricity tariff increase for standard tariff customers will increase the average standard dual fuel tariff to £1,120 per year, a 7.3% increase. Management attributed the rise, fairly, to increasing renewables subsidy costs and rising transmission and distribution fees.

Guidance retained, but strategic pivot the story

Centrica management retained its FY17 guidance – adjusted operating cash flow over £2bn, capex restricted to £1bn, £250m cost efficiencies (£750m by 2020) and net debt £2.5-3.0bn. However, the repositioning of the business away from asset-intensive activities such as E&P and centralised power generation towards technology-enabled customer businesses such as Connected Home is the main story. Hive and other smart home products are expected to be key growth drivers and, with one million products sold, some progress has been made, although these businesses are still small in a group context.

Consensus unlikely to move; 6% yield still the story

Centrica's in-line H117 numbers and guidance are unlikely to move consensus, which has moderate EBITDA and dividend growth in the coming years. Until a meaningful contribution is witnessed from the new businesses a key attraction is the 6% dividend yield.

Consensus estimates

Year end	Revenue (£m)	PBT (£m)	EPS (p)	DPS (p)	P/E (x)	Yield (%)
12/16	27,102	1,167	16.8	12.0	12.1	5.9
12/17e	28,426	1,244	16.0	12.2	12.7	6.0
12/18e	28,418	1,289	16.7	12.6	12.2	6.2

Source: Bloomberg data, priced on 1 August 2017

Utilities

2 August 2017

Price 203p
Market cap £11bn

Share price graph



Share details

Code CNA
Listing LSE
Shares in issue 5,592m

Business description

Centrica is a vertically integrated electricity and gas utility and service provider with 27.5 million customer accounts in the UK, Ireland and North America. Its customers are split between business and residential.

Bull

- Market leader in UK residential energy.
- 6% dividend yield.
- Medium-term upside from strategic shift to smart home technologies.

Bear

- Heightened political risk post Competition & Markets Authority investigation and government pressure for price caps.
- Execution risk in strategic shift.
- Highly competitive consumer energy landscape.

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