

S&U

Good loan growth and credit experience on track

FY18 trading update

Financial services

S&U's year-end update confirms strong growth has continued at the main motor finance business with customer numbers up 26%, while credit criteria have been tightened to underpin the quality of receivables prospectively. Confidence in the property bridging business is growing, although it remains at a trial stage. Overall trading is in line with management expectations and our estimates are unchanged.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
01/16	45.2	19.5	132.4	76.0	16.7	3.4
01/17	60.5	25.2	169.1	91.0	13.0	4.1
01/18e	80.0	30.3	201.9	105.0	10.9	4.8
01/19e	95.6	35.5	235.8	117.4	9.4	5.3

Note: *PBT and EPS are reported from continuing operations. FY16 DPS excludes exceptional payment of 125p.

Motor finance customer growth with tighter criteria

Advantage motor finance customer numbers stand at c 54,000, up 26% compared with end-FY17, while the 24,500 new transactions completed during FY18 represented an increase of 22% on the prior year. Advantage has continued to implement tighter criteria, which has resulted in an increase in the credit scores of new customers. This will take time to be fully reflected in the overall impairment rate but should more evident in FY19 and beyond. Helping to bolster customer numbers is Dealflo, an e-signature system that guides customers through terms and conditions and verifies their digital sign-off. This is contributing to a higher rate of conversion from approvals to transactions (c 10% in recent years). While new car registrations in the UK have shown distinct weakness (down 14% in 2017), used car sales have been much more resilient (see overleaf) and S&U suggests lower new car sales could support used car values as more people opt for used versus new.

Aspen, introduction of IFRS 9

The Aspen property bridging business has continued to build its loan book, with over £10m of loans issued. The business remains a pilot but confidence in the viability of the operation is increasing. FY19 sees the introduction of IFRS 9 and S&U has given an initial indication of potential impact of the accounting change on group numbers. IFRS 9 is designed to bring forward provisioning for bad loans where appropriate through the application of an expected loss model for certain loans. The net effect (allowing for deferred tax) could be a c £3m reduction in the level of opening receivables (and shareholders' equity), taking the centre of the range indicated (0.5%-2.5% of receivables). There will be no change in cash flows and the impact is modest relative to overall equity (£143m at end-H118).

Valuation

Our unchanged valuation of 2,700p is based on consideration of an ROE/COE model and peer group valuations. This suggests upside of over 20% from the current share price. On our estimates, the yield for FY18 is 4.8%.

12 February 2018

Price 2,205p
Market cap £265m

Net debt (£m) February 2018	105
Shares in issue	12.0m
Free float	26%
Code	SUS
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



Business description

S&U's Advantage motor finance business lends on a simple hire purchase basis to lower and middle income groups that may have impaired credit records which restrict their access to mainstream products. It has c 54,000 customers currently. The pilot Aspen Bridging finance business is expanding its loan book (c £10m).

Next events

FY18 results 27 March 2018

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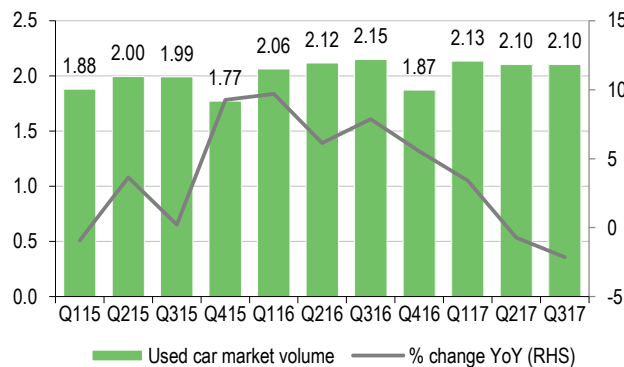
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Indicators for the UK used car market

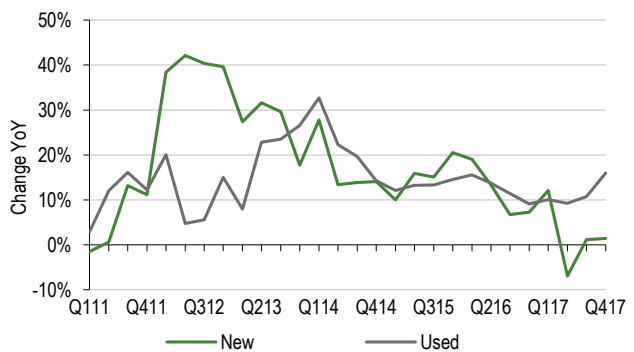
For reference, we include three charts tracking activity and pricing in the UK used car market. The first shows the volume of transactions in the market up to the third quarter of 2017. While there was a small percentage reduction in Q317, the overall picture has been relatively stable. The next chart shows the level of car finance provided through dealerships, including that used for both new and used to show the divergence of trend with used finance remaining buoyant recently.

Exhibit 1: UK used car market volume



Source: SMMT

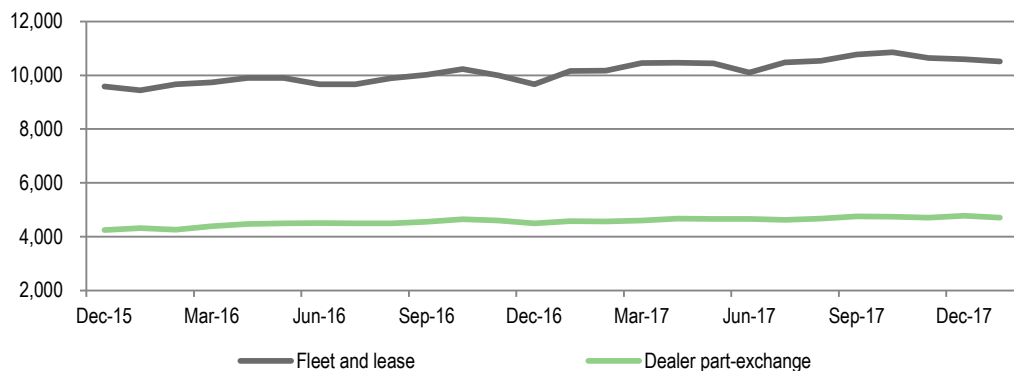
Exhibit 2: Car finance through dealerships



Source: Finance and Leasing Association

Exhibit 3 collates BCA data for auction prices. We have included prices for fleet and lease sales and dealer part exchange, but excluded nearly new cars as they are relatively low in volume and at a much higher price level. A typical price level for an Advantage customer is around £7,000, so between the categories shown on the chart. While the BCA data is contingent on the company's mix of business, which may not reflect overall market trends, it does tend to indicate stability in prices, particularly towards the lower end of the pricing range.

Exhibit 3: BCA auction prices (£)



Source: BCA

Exhibit 4: Financial summary

£000s	2015	2016	2017	2018e	2019e
Year end 31 January	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue	36,102	45,182	60,521	80,014	95,623
Impairments	(5,863)	(7,611)	(12,194)	(18,252)	(21,366)
Other cost of sales	(6,674)	(8,980)	(12,871)	(17,763)	(20,559)
Administration expenses	(6,957)	(7,131)	(8,332)	(10,162)	(12,144)
EBITDA	16,608	21,460	27,124	33,836	41,554
Depreciation	(163)	(209)	(253)	(348)	(626)
Op. profit (incl. share-based payouts pre-except.)	16,445	21,251	26,871	33,489	40,928
Exceptionals	0	0	0	0	0
Non-recurring items	0	0	0	0	0
Investment revenues / finance expense	(1,680)	(1,782)	(1,668)	(3,146)	(5,384)
Profit before tax (FRS 3)	14,765	19,469	25,203	30,343	35,544
Profit before tax (norm)	14,765	19,469	25,203	30,343	35,544
Tax	(2,920)	(3,583)	(4,861)	(5,997)	(7,109)
Discontinued business after tax	6,615	53,299			
Profit after tax (FRS 3)	18,460	69,185	20,342	24,346	28,435
Profit after tax (norm)	11,845	15,886	20,342	24,346	28,435
Average Number of Shares Outstanding (m)	12.0	12.0	12.0	12.1	12.1
Diluted EPS (p)	154.3	576.5	169.1	201.9	235.8
EPS - normalised (p)	99.0	132.4	169.1	201.9	235.8
Dividend per share (p)	66.0	201.0	91.0	105.0	117.4
EBITDA margin (%)	46.0%	47.5%	44.8%	42.3%	43.5%
Operating margin (before GW and except.) (%)	45.6%	47.0%	44.4%	41.9%	42.8%
Return on equity	15.7%	15.2%	15.2%	16.7%	17.7%
BALANCE SHEET					
Non-current assets	76,781	103,653	138,004	182,253	219,322
Current assets	68,578	61,903	57,763	79,351	97,837
Total assets	145,359	165,556	195,767	261,604	317,159
Current liabilities	(8,945)	(6,850)	(17,850)	(8,401)	(23,180)
Non-current liabilities inc pref	(54,950)	(30,450)	(38,450)	(100,450)	(125,450)
Net assets	81,464	128,256	139,467	152,753	168,529
NAV per share (p)	689	1,084	1,177	1,275	1,407
CASH FLOW					
Operating cash flow	(13,404)	(16,017)	(27,431)	(34,873)	(21,543)
Net cash from investing activities	(1,096)	80,716	(308)	(1,618)	(1,618)
Dividends paid	(6,734)	(23,090)	(9,548)	(11,380)	(12,977)
Other financing (excluding change in borrowing)	8	55	21	2	0
Net cash flow	(21,226)	41,664	(37,266)	(47,869)	(36,138)
Opening net (debt)/cash	(32,339)	(53,565)	(11,901)	(49,167)	(97,036)
Closing net (debt)/cash	(53,565)	(11,901)	(49,167)	(97,036)	(133,174)

Source: S&U accounts, Edison Investment Research. Note: FY16 DPS includes an exceptional payment of 125p.

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