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McColl's Retail Group

Consumer

7 August 2017

Price	256.5p
Market cap	£295m

Supply chain partnership and acquisition

In a significant move, the neighbourhood retailer has partnered with Morrisons for the long-term supply of fresh food and groceries. Financial performance in H117 was robust despite challenging economic conditions. The acquisition of 298 stores from the Co-op creates a platform for further development. We believe that McColl's has identified a clear strategy in the UK convenience channel, which is forecast to grow 18% to £47bn by 2022, according to IGD.

Supply chain partnership with Morrisons

The long-term partnership provides McColl's with a best-in-class fresh food and grocery offer through the relaunched Safeway brand, and is exclusive for 12 months. It significantly improves the company's fresh food presence and enhances the range. It improves commercial terms and simplifies the supply operation.

H117: Increasing neighbourhood presence

H117 results signal that McColl's is on track to deliver its seventh year of sales growth, with revenue up 7.6% y-o-y and like-for-like sales up 0.2%. The acquisition of 298 stores from the Co-op affects FY17 profits, but their successful integration builds business momentum. Performance is supported through investment and estate growth (of 80% in convenience stores since the 2014 IPO), with a focus on customer service, and growing neighbourhood presence and the convenience offer.

Avenues for further development

McColl's is well positioned as the wider convenience sector evolves and grows. Its focus is to increase market share through acquisitions and internal investment. Strengthening the range of products and services and delivering quality service offer opportunities for organic growth. Also, through a wholesale retender, McColl's is leveraging its enhanced scale to develop its customer offer.

Valuation: Earnings growth and favourable yield

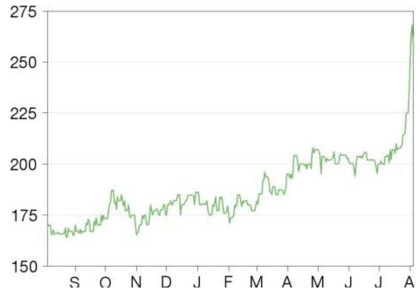
The recent acquisition supports consensus forecast of 16% revenue and 24% PBT CAGRs in FY16-18e. Management's focus is to balance capital investment, deleveraging and dividends. Net debt following the acquisition peaks at £139.6m in H217 according to consensus forecasts, but is then set to decline through to FY19. Consensus forecast free cash flows of £15.9m and £27.1m in FY17 and FY18 suggest further acquisition headroom. Despite re-rating on the Morrison announcement, the P/E remains at a discount to its main quoted peer.

Consensus estimates

Year end	Revenue (£m)	PBT (£m)	EPS (p)	DPS (p)	P/E (x)	Yield (%)
11/15	932.2	21.7	15.9	10.2	16.1	4.0
11/16	950.4	20.8	16.0	10.2	16.0	4.0
11/17e	1119.0	25.0	17.3	10.3	14.8	4.0
11/18e	1254.0	32.2	22.4	10.9	11.5	4.2

Source: Bloomberg

Share price graph



Share details

Code	MCLS
Listing	LSE
Shares in issue	115m

Business description

McColl's Retail Group is a leading neighbourhood retailer with a growing estate of 1,650 managed convenience stores and newsagents. In addition, it is the largest operator of post offices in the UK, with roughly 600 in-store counters/branches.

Bull

- Well-positioned in a growing sector.
- Successful track record of integrating acquired stores.
- Strong brand awareness and reputation.

Bear

- Highly competitive market.
- Reliance on a small number of key personnel.
- Entire operation in the UK, yielding exposure to overall economic conditions in that market.

Analysts

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