EDISON

S&U

Upbeat update

Trading update

Financial services

S&U's trading update (for the period since its July half-year end) was upbeat, reporting growth accelerating in both Advantage motor finance and Aspen bridging finance. Recent developments in the pandemic could temper near-term consumer confidence but, looking beyond this, S&U has successfully navigated the onset of COVID-19 while continuing to develop both its businesses, creating a good basis for longer-term growth.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
01/21	83.8	18.1	120.7	90.0	22.1	3.4
01/22e	86.5	38.7	258.2	115.0	10.4	4.3
01/23e	95.2	38.0	253.1	127.0	10.6	4.8
01/24e	103.7	41.0	256.7	129.0	10.4	4.8

Note: *PBT and EPS are reported. EPS are diluted.

Advantage motor finance

Advantage is reported to be seeing a strong recovery in both profitability and new business transactions, which were up 30% y-o-y in the period, despite a shortage of used cars in showrooms and a fall of 6% in UK used car sales in calendar Q321. S&U looks for net loan advances of over £140m for the full year (in line with our estimate). Collections remain very strong and credit quality has at least maintained the improvement reported at the half-year end, mirroring the positive comments on this front by Provident Financial in its Q3 update and suggesting the possibility of lower impairment than we currently factor in. Looking beyond the current year, Advantage continues to work on enhancing customer service, underwriting and marketing to underpin longer-term growth.

Aspen bridging finance

The receivables book at Aspen has grown to £60m compared with £57.6m at the end of H122 and £34.1m at end FY21. Transaction numbers are up 38% year to date versus the prior year period despite a quieter housing market. Profits are reported to have made further excellent progress, with margin maintained and credit quality remaining strong. The current pipeline of deals has doubled over the period and a new Bridge to Let product has been introduced to address a market opportunity identified by Aspen. The lumpy nature of Aspen's loans makes forecasting the level of loan growth for specific periods difficult, but the scope for substantial medium-term growth remains in place.

Valuation

We have not changed our estimates at this stage and on this basis the FY22e P/E ratio is 10.4x and the yield 4.3%. Note that our FY24 earnings estimate allows for the introduction of a 25% corporate tax rate. Using a return on equity (ROE)/cost of equity (COE) model, the current share price appears to imply an assumed ROE of less than 16% compared with our current year estimate of 16.5% (see page 4).

10 December 2021

Price	**2,673p**
Market cap	**£323m**

Net debt (£m) at 8 December 2021	113
Shares in issue	12.1m
Free float	28%
Code	SUS
Primary exchange	LSE
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(7.2)	(3.2)	38.5
Rel (local)	(7.5)	(5.8)	22.9
52-week high/low		2,950p	1,930p

Business description

S&U's Advantage motor finance business lends on a simple hire-purchase basis to lower- and middle-income groups who may have impaired credit records that restrict their access to mainstream products. It has c 62,000 customers. The Aspen property bridging business has been developing, following its launch in early 2017.

Next events

Q4 trading update	10 February 2022

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Edison profile page

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Funding

The high level of collections in both businesses has contributed to current borrowings of £113m compared with £115.5m at end H122. There is substantial headroom for the accelerated growth the group looks for in FY23 given its banking facilities (£180m at end H122).

Background

In this section, we update background data we track as indicators for Advantage and Aspen, starting with economic and industry figures relevant for the used car finance market.

Exhibit 1 shows independent forecasts for UK GDP and unemployment as collected by the UK Treasury in November. Compared with the September data shown in our last note, movements are limited although estimates for unemployment are slightly lower. This should be positive for Advantage as unemployment is an important sensitivity for credit risk and ties in with S&U's recent experience of credit quality.

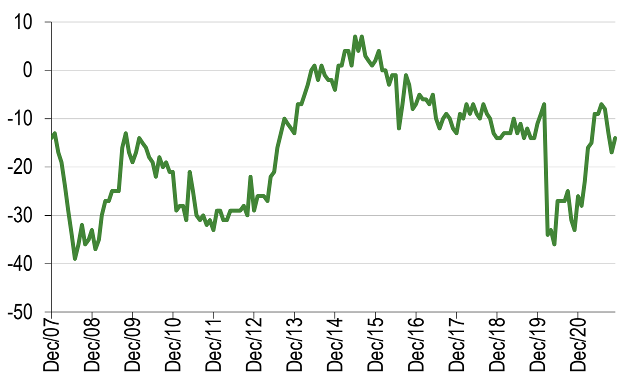
Exhibit 1: Comparison of independent economic forecasts for the UK (November)

%	Average	Average of new forecasts	Low	High
GDP growth				
2021	7.0	7.0	6.0	8.1
2022	5.1	5.0	3.5	8.1
Labour Force Survey unemployment rate Q4				
2021	4.9	4.8	4.5	5.5
2022	4.6	4.5	3.9	6.0

Source: HM Treasury

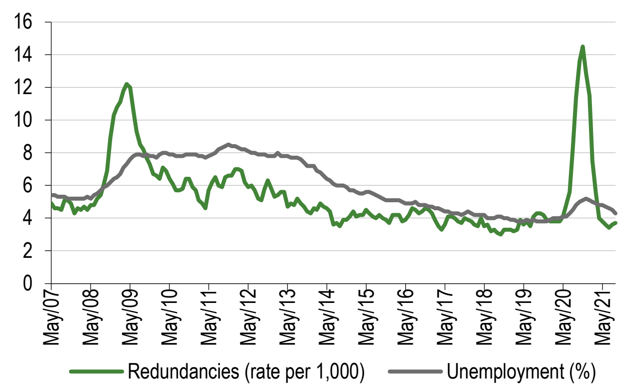
Exhibit 2 shows that consumer confidence has staged a major recovery, albeit with a recent softening. Uncertainties remain and the influence of COVID-19, supply bottlenecks and inflation fears is likely to fluctuate, but in due course a progressive normalisation in economic activity seems likely to continue. Exhibit 3 shows that, after an increase, the unemployment rate has moved down towards prior levels. Redundancies, a more immediate measure, saw a very sharp spike as the pandemic took hold, but fell rapidly and are now at pre-pandemic levels.

Exhibit 2: GfK UK consumer confidence indicator



Source: Refinitiv (last value September 2021)

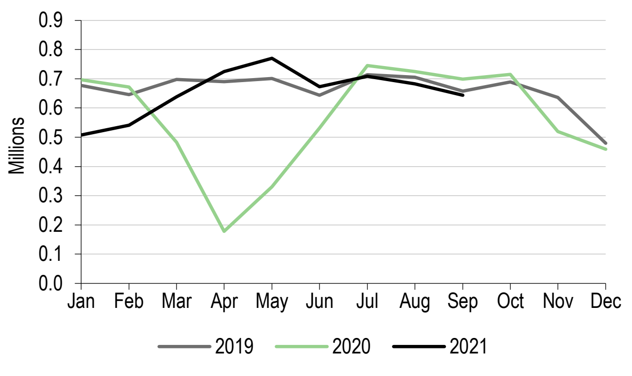
Exhibit 3: UK redundancies and unemployment



Source: ONS (last value September 2021)

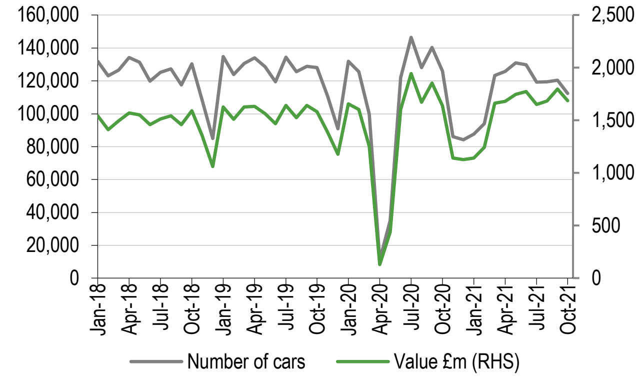
We now turn to data on used car transactions and used car finance. Exhibit 4 shows the sharp drop in used car transactions in April 2020. Volume recovered very well following the initial lockdown, albeit with a further dip following subsequent lockdowns. Since April 2021 there has been a return to activity close to pre-pandemic levels, as represented here by the 2019 monthly figures, although the April bounce was smaller than industry participants had thought possible and, as noted earlier, for Q321 there was a 6.2% reduction against a relatively strong Q220 period. Exhibit 5 shows a similar pattern in used car finance.

Exhibit 4: Monthly used car transactions 2019–21



Source: SMMT. Note: Last value September 2021.

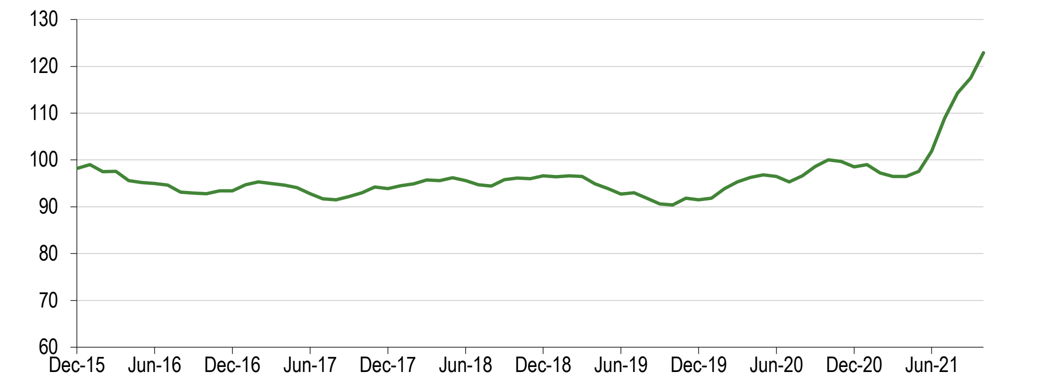
Exhibit 5: Used car finance through dealerships



Source: Finance and Leasing Association. Note: Last value October.

Used car prices (see Exhibit 6) were buoyant in 2020 and have seen a sharp step up in the data since July this year, with strong consumer demand and reduced supply pushing prices up. The ONS data are supported by a similarly marked strength in the Autotrader retail price index. An improving supply of new cars and hence used stock seems likely during 2022 but Advantage's exposure to auction prices for repossessed cars is moderated by the relatively low value of vehicles it finances. Also, for the moment, the demand side of the equation seems likely to remain robust.

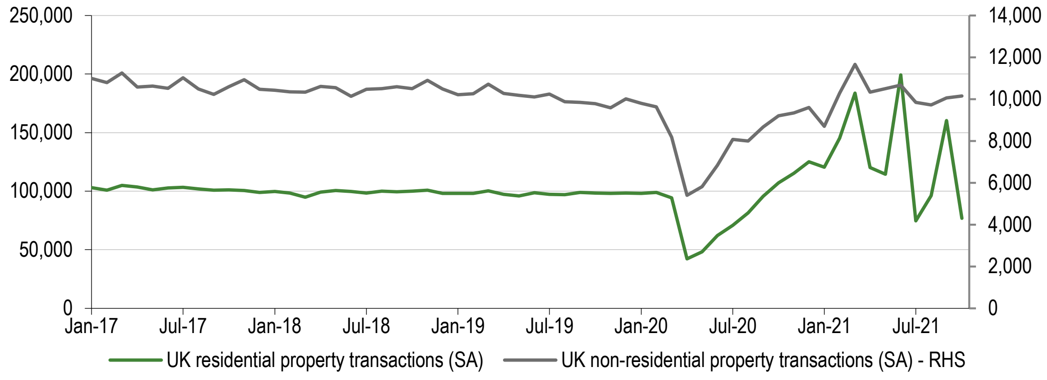
Exhibit 6: Second-hand car prices (CPI index)



Source: ONS (last value October 2021)

Looking at the background for Aspen Bridging, Exhibit 7 shows the number of UK non-residential and residential transactions, with residential being most relevant for Aspen. Both saw sustained improvement following the initial lockdown in 2020 with residential data fluctuating sharply as buyers sought to take advantage of the temporary increase in the stamp duty land tax nil rate band. On a longer view, S&U sees an imbalance between supply and demand for good-quality homes as a favourable backdrop for its customers who are refurbishing and developing properties. As a small business, Aspen should also have significant scope for expansion now that it is more established in the market. Aspen's involvement in the Coronavirus Business Interruption Loan Scheme has given it useful access to larger and more established developer customers as well as expanding the loan book in the short term.

Exhibit 7: UK property transactions (seasonally adjusted)



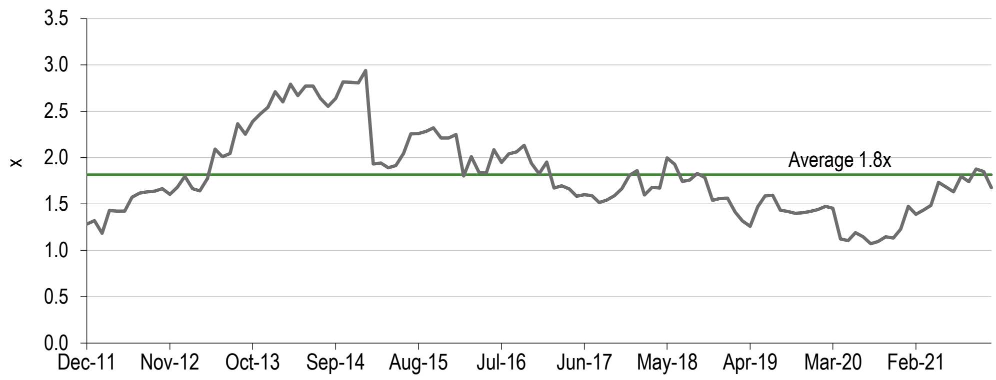
Source: HM Revenue & Customs. Note: Figures for August to October 2021 are provisional. SA = seasonally adjusted.

Valuation

P/E comparisons with peers remain difficult to interpret given differences in business mix and significant changes in provisioning levels following the initial impact of COVID-19. We therefore frame valuation using our ROE/COE calculations and the price to book ratio. If we assume a COE of 10% and long-term growth of 2%, then the share price at the time of writing (2,673p) would be consistent with an ROE of below 16%, compared with our 16.5% estimate for FY22.

Looking at the history of the price to book ratio (Exhibit 8), the current level of 1.7x is slightly below the 10-year average following a period of recent weakness in the shares (down 8% over a month but still up 37% over 12 months).

Exhibit 8: 10-year price to book value history



Source: Refinitiv, Edison Investment Research

Exhibit 9: Financial summary

£'000s	2018	2019	2020	2021	2022e	2023e	2024e
Year end 31 January							
PROFIT & LOSS							
Revenue	79,781	82,970	89,939	83,761	86,484	95,158	103,738
Impairments	(19,596)	(16,941)	(17,220)	(36,705)	(11,698)	(17,294)	(20,571)
Other cost of sales	(17,284)	(15,751)	(19,872)	(14,264)	(18,922)	(21,559)	(21,675)
Administration expenses	(9,629)	(10,763)	(12,413)	(10,576)	(12,896)	(13,132)	(14,316)
EBITDA	33,272	39,515	40,434	22,216	42,968	43,173	47,176
Depreciation	(294)	(414)	(450)	(520)	(527)	(487)	(451)
Op. profit (incl. share-based payouts pre-except.)	32,978	39,101	39,984	21,696	42,440	42,686	46,724
Exceptionals	0	0	0	0	0	0	0
Non recurring items	0	0	0	0	0	0	0
Investment revenues / finance expense	(2,818)	(4,541)	(4,850)	(3,568)	(3,721)	(4,727)	(5,680)
Profit before tax	30,160	34,560	35,134	18,128	38,720	37,959	41,045
Tax	(5,746)	(6,571)	(6,252)	(3,482)	(7,357)	(7,212)	(9,861)
Profit after tax	24,414	27,989	28,882	14,646	31,362	30,747	31,184
Average Number of Shares Outstanding (m)	12.1	12.1	12.1	12.1	12.1	12.1	12.1
Diluted EPS (p)	202.4	232.0	239.4	120.7	258.2	253.1	256.7
EPS - basic (p)	203.8	233.2	239.6	120.7	258.3	253.3	256.9
Dividend per share (p)	105.0	118.0	120.0	90.0	115.0	127.0	129.0
EBITDA margin (%)	41.7%	47.6%	45.0%	26.5%	49.7%	45.4%	45.5%
Operating margin (before GW and except.) (%)	41.3%	47.1%	44.5%	25.9%	49.1%	44.9%	45.0%
Return on equity	16.7%	17.6%	16.8%	8.1%	16.5%	14.8%	13.9%
BALANCE SHEET							
Non-current assets	181,015	185,383	197,806	173,413	205,170	228,083	247,250
Current assets	84,178	95,430	108,275	111,426	121,109	142,403	154,166
Total assets	265,193	280,813	306,081	284,839	326,279	370,486	401,416
Current liabilities	(7,927)	(6,722)	(7,424)	(5,309)	(6,261)	(6,724)	(7,052)
Non current liabilities inc pref	(104,450)	(108,724)	(119,183)	(98,501)	(119,878)	(146,798)	(161,718)
Net assets	152,816	165,367	179,474	181,029	200,141	216,964	232,646
NAV per share (p)	1,276	1,375	1,493	1,490	1,648	1,786	1,916
CASH FLOW							
Operating cash flow	(43,418)	10,530	4,946	32,940	(7,399)	(10,955)	667
Net cash from investing activities	(1,040)	(785)	(265)	(1,112)	(302)	(300)	(300)
Dividends paid	(11,377)	(13,080)	(14,461)	(13,098)	(12,268)	(13,962)	(15,540)
Other financing (excluding change in borrowing)	12	14	14	2	1	0	0
Net cash flow	(55,823)	(3,321)	(9,766)	18,732	(19,968)	(25,216)	(15,173)
Opening net (debt)/cash	(49,167)	(104,990)	(108,311)	(118,077)	(99,345)	(119,313)	(144,530)
Closing net (debt)/cash	(104,990)	(108,311)	(118,077)	(99,345)	(119,313)	(144,530)	(159,702)

Source: S&U accounts, Edison Investment Research. Note: EPS on a reported basis.

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