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Beaufort Securities Breakfast Alert: Provident Financial, Persimmon, Prairie Mining

Today's edition features:

• Prairie Mining (LON:PDZ)

• Persimmon (LON:PSN)

• Provident Financial (LON:PFG)

Markets

Europe

The FTSE-100 finished yesterday's session 0.86% higher at 7,381.74 whilst the FTSE AIM All-Share index was up 0.28% at 1,005.83. In continental Europe, the CAC-40 finished 0.87% higher at 5,131.86 whilst the DAX was up 1.35% at 12,229.34.

Wall Street

In New York last night, Dow Jones ended the day 0.90% higher at 21,899.89, the S&P-500 gained 0.99% to 2,452.51 and the Nasdaq added 1.36% to stand at 6,297.48.

Asia

In Asian markets this morning, the Nikkei 225 was recently up 0.26% at 19,434.64 and the Hang Seng was 0.91% higher at 27,401.67.

Oil

In early trade today, WTI crude was down 0.16% at $47.67 per barrel and Brent Crude Oil lost 0.19% to $51.68 per barrel.

Headlines

Feeling squeezed? You may be imagining it

Household bills are rising more slowly than the rate of inflation, new research has found. The figures suggested that the "cost of living squeeze" may be less severe than previously thought. Research by MoneySavingExpert, based on official data, revealed the rise in the total cost of household bills was less than the inflation rate. It found costs including rent, energy bills, council tax and insurance have risen by 2.1% in the past year. That rise is in line with average earnings growth and lower than the 2.6% rise in the Consumer Prices Index (CPI) in July. CPIH, a measure of inflation that includes housing costs and council tax, also rose by 2.6% over the period. Although the numbers show only a small increase across household running costs as whole, they also revealed large price hikes for electricity and insurance in particular. The cost of insurance rose by 7.6% over the year, including a 12% jump in car insurance premiums. Energy bills went up 5.1%, including a 9% increase for electricity. The data was compiled before British Gas announced a 12.5% price hike on 1 August. Council tax rose by an average of 3.8%, the data showed, while rents went up by 1%. However, some other bills may have fallen over the last year, with a modest 1.2% fall for mobile phone bills and a 1% decline for other financial services. MoneySavingExpert managing director Guy Anker said consumers could save considerable amounts by switching providers. Household bills inflation over the last 12 months peaked in February at 3.2%, but has been falling since then.

Source: BBC News

Company news

Prairie Mining (LON:PDZ, 32.00p) - Buy

Prairie Mining announced it has received formal approval of its spatial development plan (rezoning) for Jan Karski. This is an important part of the approval process which allows Prairie to use agricultural land for mining. The remaining step for Jan Karski is Environmental Consent which follows submission of the ESIA in the coming weeks. As Prairie notes "Jan Karski is now one of the most advanced new large scale coking coal projects in the Northern Hemisphere".

Our View: This is good news and shows how Jan Karski is progressing according to Polish law and with government support. The next major news flow will be the completion of China Coal's Jan Karski feasibility study which we expect in September. This should lead to Chinese debt financing and ultimately mine construction. Jan Karski is a major semi-soft coking coal project with very low production costs and long life. With coking coal prices very strong (semi-soft c.$150/t), Jan Karski's considerable strategic value is increased and in our opinion far exceeds Prairie's current market value. That is before you consider the similar value of Prairie's other project Debiensko (hard coking coal). We have a Buy recommendation.

Beaufort Securities provides corporate sponsored research to Prairie Mining plc

Persimmon (LON:PSN, 2,601.00p) - Hold

Persimmon plc yesterday announced half year results for the six months ended 30 June 2017. Jeff Fairburn, Group Chief Executive, said: "The successful execution of the Group's long-term strategy continues to support excellent trading results as seen again in the first half of 2017. Our focus on meeting market demand to deliver high quality sustainable growth in each of our 29 regional businesses is delivering excellent outcomes for our customers, our shareholders, and all our stakeholders." Revenue were up 12% to £1.66bn (2016: £1.49bn) for the period with legal completions increasing 8% with an additional 556 new homes delivered on an average selling price of £213,262, up 4%. Profit before tax increased by 30% to £457.4 million (2016: £352.3 million), underlying operating margin of 27.6% (2016: 23.8%), cash balances at end-June were £1,120.4 million (2016: £462.0 million) prior to £339.5m capital return paid on 3 July 2017 and the consented land bank totalled 98,712 plots (December 2016: 97,187 plots). Management continued to execute the long-term strategy, which aims to sustain the delivery of superior levels of shareholder value and cash generation through the housing cycle successfully. The Group invested c. £550 million of cash in land over the twelve-month period ended 30 June 2017 whilst also generating c.£740 million of free net cash inflow before capital returns, equivalent to c.239 pence per share. On 31 March 2017, the Group paid an interim dividend of 25 pence per share as an additional return of surplus capital under the Capital Return Plan; on 3 July 2017, after the balance sheet date, the Group paid the sixth instalment under the Plan of 110 pence per share, or £339.5 million, bringing the total returned to shareholders under the Plan to date to c.£1.5 billion (or 485 pence per share). The Board noted its commitment to return surplus capital of at least 110 pence per share to shareholders each July until 2021.

Our View: Another highly impressive report from Persimmon. Its management continues to successfully deliver sector-beating returns for shareholders, including a 26% return-on-equity ('ROE') and 47.3% return-on-average-capital-employed ('ROACE'), which justifies a premium P/NAV of 2.7x against a sector average of 1.90x. Strict control of development costs (despite overall build cost continuing to rise in the 3% to 4% pa range) and a low cost/plot emanating from successful past acquisition of consented/strategic land drove the half-year operating margin up an exceptional 380bp, thereby allowing the Group to deliver pre-tax profits well ahead of expectations. In this respect, there is scope for current year consensus net profit expectations to rise by around 7%. Given also that the value of forward sales (including legal completions from 1 July 2017) is now 15% stronger than at the same point last year at £2.005 billion (2016: £1.747 billion) with an average selling price of c.£231,500 (2016: £224,200), the 2018E figure will also need to rise. Such impressive gains will, however, be tough to deliver again, leaving the market to reflect on just how much longer it might be before one of the UK housebuilding majors blinks? When it happens, and it could still be 12 months away, the sector will likely give back a good chunk of the gains recorded since recovering from the Brexit shock with the most highly valued players, like Persimmon, hurting the most. Experienced investors will no doubt recall just how viciously cyclical the sector has been in the past and, while all players continue to chorus apparently sustained/improving buyer interest, widespread reports of falling prices in the second-hand markets and tumbling consumer confidence amid expectations that the Bank of England will begin hiking base rates early in 2018, suggests some clouds have to be gathering on the horizon. Even if some of the expectation of an early general election have subsided somewhat, the shadow of the Government's prospective 2021 tapering or even phasing-out of its key Help-to-Buy incentive has not gone away. The share price has rapidly risen close to the 2,600p level Beaufort set back in July; re-working forecasts for 2017E and 2018E in response to yesterday's half year report takes our pre-tax estimates to £965m and £1020m, representing earnings per share to 138p and 148p respectively. Given also the scheduled resetting of the capital return plan next February, with management's newly noting its commitment is now to return at least 110p per share, yields for the two years are now forecast at 5.2% and 5.9% respectively . Based on this Beaufort has now raised its target price for Persimmon to 2,750p although, given that this now provides for less than 10% upside from the current level, downgrades its recommendation to Hold. Beaufort remains overweight in the housebuilding sector, however, suggesting better value might now be found elsewhere, such as in Taylor Wimpey, Bellway and Redrow, or those with a higher proportion of social housing (like Galliford Try).

Provident Financial (LON:PFG, 589.50p) - Hold

Provident Financial ('Provident'), the leading non-standard lender in the UK, yesterday provided its trading update for the period since the interim results. The Group warned that its Consumer Credit Division ('CCD') is now likely to deliver pre-exceptional loss in a range of between £80m and £120m, against previous guidance of £60m pre-exceptional profits. The Group blamed the extent of division's performance deterioration arise from home credit business' worse than expected operational disruption, ranging from shortfall of agents moving to a full-time Customer Experience Managers ('CEMs' agents under new operating model), reduced agent effectiveness and issue with IT managing CEMs. Altogether, these all resulted in slower than expected rate of progress to embed the new operating model. The Group is currently taking "thorough and rapid review" of CCD's performance. Apart from CCD, Provident confirmed that the performance of Vanquis Bank, Moneybarn and Satsuma remain in line with management's expectations. Although, the Group announced that one of Vanquis Bank's ancillary product, Repayment Option Plan ('ROP') is now under investigation by the regulator, Financial Conduct Authority ('FCA'), for the period concerning 1 April 2014 to 19 April 2016. The Group has suspended all new sale of the ROP in April 2016. In response to the significant deterioration in the trading performance of the CCD, together with the FCA's investigation at Vanquis Bank, the Board has cancelled the interim dividend declared on 25 July 2017 (43.2p) and said full-year dividend is also "unlikely". In light of the circumstances, Peter Crook has step down from the CEO yesterday, with Manjit Wolstenholme assumed the role of Executive Chairman. Within the statement, Manjit commented "I am very disappointed to have to announce the rapid deterioration in the outlook for the home credit business. Protecting the group's capital base through withdrawing the interim dividend and in all likelihood the full-year dividend is the appropriate response to maintain the highly valuable franchises of Vanquis Bank, Moneybarn and Satsuma. My immediate priority is to lead the turnaround of the home credit business".

Our View: A truly disastrous trading update! Together, four damaging disclosures blew away any remaining confidence in Provident's story while index funds, aware of the Group's imminent demotion from the FTSE100, also looked to offload their positions. The net result was to push the shares down by -66%, one of the largest ever daily falls by a FTSE100 company. Whilst Beaufort had previously noted its concerns regarding the 'self-inflicted' disruption would be created by the surprise revamp of CCD's operating model, along with the possible need for further provisions to finally settle the situation, according to yesterday's statement Providence's previously guided pre-exceptional profits of £60m are now set to plunge into a loss of between £80m and £120m. This was clearly way beyond anyone's worst case scenario. Compounding the situation, the FCA's investigation into Vanquis Bank's Credit Card Repayment Option Plan, cancellation of the interim dividend (probably the final dividend as well) along with the stepping down of the CEO, together made for a day that shareholders would rather forget. Vanquis Bank sold ROP together with its credit card which enables cardholders to freeze repayments for a period of time. ROP currently contributes gross revenues, before impairment and costs, of c.£70m per annum. Although it is not an insurance product, there are some obvious similarities to the extremely costly Payment Protection Insurance (PPI) dilemma and potential mis-selling allegation now being investigated by the FCA, which may result in the payment of fines and/or compensation overhanging the shares for an extended period. During the Analyst conference call, Provident's Board noted it is too early to provide visibility on CCD into 2018 but suggested level of profitability is likely to be "small" as the recovery period for its home credit business will "possibly go beyond" 2017. Whilst scrapping the dividends (interim plus final) previously expected to cost around £200m for FY2017E, will possibly be sufficient to plug this year's losses from CCD, uncertainty over its new operational model as well as outcome of the FCA's investigation must potentially threaten next year's payouts as well. One might argue that there are still some very good and profitable businesses in Provident and that, after such a tumble in the Group valuation, the CEO's stepping down could well signal the equity's 'low water' mark. For volatility traders trying to spot such rebounds, this may be enough. For most investors, however, the risks, including turning around CCD along with uncertainties surrounding the FCA's prospective findings will continue to undermine confidence. Accordingly, until there are convincing signs of progress on these fronts and the business has become reasonably predictable once again, Beaufort will retain its Hold rating on the shares whilst setting no target price.