McCarthy & Stone off the bottom but analysts remain concerned over cautious approach to land buying

Uncertainty relating to the government's proposals on ground rents hit the share price of retirement homes builder McCarthy & Stone PLC (LON:MCS).

The shares were down more than 7% at 127.3p in early deals as the builder's half-year statement said it had exercised additional caution in direct response to the uncertainty resulting from the government's proposals on ground rents.

McCarthy & Stone said 22 land exchanges and 21 planning consents were secured in the first half of its financial year (i.e. the six months to February 28), down from 30 land exchanges and 34 planning consents in the corresponding period 12 months earlier.

READ: McCarthy & Stone puts plan in place to offset impact of crackdown on ground rents

The decline reflects a more measured approach to land buying and additional time taken to renegotiate section 106 agreements, often referred to as 'developer contributions' - usually related to ensuring some affordable housing is built alongside the more profitable expensive homes.

The group saw the number of legal completions in the first half of its financial year fall 12% to 760 from 864 the year before but revenue rose 1% to £239.6mln from £238.2mln as the average selling price ballooned to £298,000 from £260,000 the previous year.

The underlying operating margin slumped to 6% from 10% the year before.

Underlying profit before tax halved to £11.5mln from £22.8mln while net debt rose to £75.9mln from £30.4mln.

Despite the profit collapse, the interim dividend was edged up to 1.9p from 1.8p at the halfway stage last year.

>>> Downsizing difficulties dent McCarthy & Stone profits https://t.co/rmizY8tyC7 pic.twitter.com/WSgf08Ov0O

— Nathan Chesters (@NathanChesters) April 11, 2018

Underlying trading has remained resilient despite a challenging secondary market, with forward sales including legal completions currently running around 13% ahead of the prior year, at roughly £581mln as at 6 April 2018 (versus circa £512mln as at 7 April 2017) supported by 54 new sales releases during the period (2017: 35).

The group left full-year guidance unchanged, observing that the lower level of land exchanges in the first half would most probably lead to "a more modest growth trajectory" for the business than previously expected over the next two financial years.

"We released 54 new sites for sale since the start of FY18 and our forward order book, including legal completions, is now c.13% ahead of the prior year. This provides continued confidence in our expectation that the full year out-turn will be within the current range of analyst forecasts, albeit there remains some uncertainty created by the Government's
announced on ground rents,” said Clive Fenton, the chief executive officer of McCarthy & Stone.

“We recognise the need to support first-time buyers but Government must not ignore the many benefits of building more retirement housing. This form of housing frees up existing homes for families and young people, and reduces pressure on social care services, which are set to account for half of all taxes raised by local authorities by 2035,” claimed Fenton.

“The current reviews of planning and social care policy provide an excellent opportunity to rebalance housing policy and help the millions of older people who want to downsize into properties better suited to their needs,” he added.

UBS remains bearish on the house-builder
"McCarthy & Stone has become more cautious in response to the government's announcement on ground rents, and has slowed down new land acquisitions," noted UBS, which said the results were in line with previous guidance.

The consensus forecast for this year's profit before tax is £101mln, which is £10mln above UBS's estimate.

"We expect a negative market reaction given a more cautious approach to land buying which will result in more moderate volume growth over the next 2 years. We also note the heavy reliance on improved trading in H218 in order to meet consensus," said UBS, which has a 'sell' rating on McCarthy & Stone and a 140p 12-month price target.

Shares in McCarthy & Stone, down sharply in early deals, had recovered to 135.2p, down 1.4% on the day, in lunchtime trading.

--- adds broker comment and updates share price ---