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Comeback king

McCarthy & Stone had a bad recession, but after a recapitalisation it now plans to double the business. Sunniva Davies-Rommetveit finds out more

The recession wasn't the kindest to Britain's biggest sheltered living housebuilder, McCarthy & Stone. Nor to the HBOS-led consortium that took the company off the London Stock Exchange in 2006.

Having accumulated debts of almost £519 million by 2013, the company struck a deal in November of that year to get its shareholders to subscribe for £367 million of new equity. It thereby reduced debt to £160 million, which was in turn replaced by a new five-year £200 million revolving credit facility provided by Barclays, HSBC, RBS and Santander in December 2014.

Now, McCarthy & Stone chief executive Clive Fenton is excited about the future, and has aims to double the business' size in the next four years or so. "The company has a robust balance sheet once again, meaning we're in a growth phase at the company. Gearing at the company is now around 10%, which is a very sensible level in my opinion," he says.

Last year, McCarthy & Stone acquired 74 new sites, and aims to acquire around 100 more this year. This growth phase is part of the firm's £2 billion plan to invest in land and build new retirement apartments across the UK over the next four years.

Robust 2014 financial results should support the company's ambitious growth plans. Revenue, for instance, stood at £387.8 million compared to £310.8 million in 2013, while operating profit increased to £75.1 million (2013: £45.2 million). The fact that net interest charges were reduced from £41.3 million to £13.4 million, because of the 2013 debt restructuring, has also made a big difference to the firm.

Interestingly, Fenton is quite open about the potential for changes in the capital structure of the business in future, including a possible flotation. "An initial public offering (IPO) is clearly a possibility but is by no means the only option," he explains. "What I would say is that McCarthy & Stone used to be a listed company, and I think it does lend itself very well to the stock market."

Whichever option the group pursues, it is unlikely to consider any financial transaction until the end of 2015 at the earliest. This is because McCarthy & Stone wishes to add as much value as it can before any deal is considered. Fenton points to the management restructuring – with the likes of Barchester founder and former boss Mike Parsons, former Galliford Try's finance director Frank Nelson and previous chairman and chief executive at Persimmon John White all having joined the company's board recently.

"We're creating a lot of value at the moment by speeding up work flows, streamlining costs and bringing in the best people. This stage won't be over until the end of this year, so this is our main focus until then," Fenton says.

When McCarthy & Stone does choose to bring new capital into the company, demographics mean it should be an attractive choice for investors in whichever form. The Office for National Statistics, for instance, predicts that the number of over 85s will go up 130% by 2033, while over 65s could increase by 50% in the same timeframe; therefore demand for McCarthy & Stone's properties is set to increase.
If it does go down the flotation route, Fenton is confident these factors make the company a viable alternative for investors who want something more interesting than a traditional house building play. "With McCarthy & Stone you're not just betting on house building, but also on the demographics of the market we specialise in - which no one else really does."

Its retirement business is split three-way between assisted living, retirement living and the newer 'over-55 young' retirement living product, Ortus Homes (late seventies being the typical time people buy into retirement living). The company's sites are centrally located, have good public transport links and are mainly built on brownfield sites. Having sold 1,677 new homes in 2013-14, the firm obviously has an effective business model.

One important part of this business model is to standardise the building design, thereby minimising costs. McCarthy & Stone ensures that the buildings fit in with their environment despite this, however. For instance

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"Our experience in this sector means we know what designs our customers want and what works well. Our designs are also influenced by their location, for instance our coastal developments are planned to make the most of their stunning locations and views," Fenton explains.
This contemporary feel should go down well with McCarthy & Stone's newest target audience: younger retirees of 55 or over (but in reality Fenton says customers will likely be between 67 and 75). Flats aimed at this market will have more space and more parking permits. "We have 24 products in our pipeline for Ortus Homes, four of which are under build. We launched our first product for sale in Solihull this year," Fenton says. Though the development hasn't yet been finished, McCarthy & Stone has already sold 16 of the 28 flats – "and at good prices too," he adds.

While business is good, there are still market barriers that McCarthy & Stone would like to see rectified. A major issue for the firm is awareness of retirement living in the UK, or rather the lack thereof. Awareness about retirement flats in the UK is pretty poor – about 1% of Britain's over 65s live in specialist retirement accommodation. Compare this to around 17% and 13% in the US and Australia respectively.

Pointing to the coalition's 'help to buy' scheme for first-time buyers, Fenton thinks that an increased focus on retirement living as well would help to alleviate demand in the property market. "We're spending a lot of time talking to all political parties to encourage them to focus more on the elderly side of the market. It makes sense - our properties free up family homes, which will in turn free up first-time homes."

This general lack of knowledge about retirement living has a knock-on negative effect for the planning permission stage of building, moreover. Typically, the process from land exchange to starting construction on the site takes around two years – something which McCarthy & Stone is aiming to reduce to 18 months.

A Section 106 of 'The Town & Country Planning Act 1990' ruling also provides further legal challenges. The legislation means that sheltered living housebuilders must pay a flat tax rate per square metre – which Fenton says isn't quite fair when its buildings include non-sellable space like laundry and dining rooms.

Getting around this tax by being awarded C2 'care' status by local councils isn't easy either – often because of the above lack of understanding about what the company actually does. When you add in the fact developments must be signed off as 'sustainable' (meaning that relatively unused bike storage has to be included as part of the design) you can see how legal hurdles can make McCarthy & Stone's life very frustrating.

Such lack of awareness means that McCarthy & Stone is going to be pretty busy in the next five years. Promoting the business while reducing the social stigma around retirement living will be high on its to-do list. More imminently, though, a further potential deal with existing and/or new shareholders beckons. For investors interested in McCarthy & Stone, then, 2015 will definitely be a 'watch this space' kind of year.

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