THE TIMES

Waiting for the trains to arrive

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FirstGroup

There is no reason why FirstGroup should not do as well as its peers in the long term in benefiting from the seemingly inexorable rise in British train and bus journeys. But, for now, the company is having to face up to what analysts politely call “operational issues”.

Those issues affect two divisions of the company in which about 70 per cent of the capital is tied up. There is added uncertainty over how much of the UK rail industry FirstGroup will end up with by the time the present franchise bidding round is over, and whether the company will be able to maintain the dividend.

The problems are First Student in the United States, where pressure on school budgets meant a fiercely competitive environment, and the UK Bus division. The recovery at the first is about halfway down the road, with signs of more rational bidding behaviour by clients. The recovery at UK Bus, the subject of a March profits warning, is just about pulling away from the stop. FirstGroup was too reliant in the past on jacking up fares and cutting routes to cope with cost pressures. A £100 million disposal programme will exit routes that are not profitable enough.

This year, higher fuel costs and reduced state subsidies will hold margins in the division to 8 per cent, though once the disposal programme is completed in a year’s time they should be back to low double digits.

In the year to the end of March, First Student profits were off by almost 17 per cent in sterling terms. In UK Bus, they declined 9.7 per cent even ahead of this year’s added headwinds.

Against this, Greyhound in the US was a strong performer, with profits up by 26 per cent. Across the group, operating profits were 6 per cent lower, after one-offs, at £428.5 million.

This financial year is the last in which FirstGroup is pledged to grow the dividend at 7 per cent. Last year’s payment is 23.67p; this year’s would be barely covered by cashflow and only 1.2 times earnings.

Future payments probably will depend on that competitive rail franchise round. FirstGroup is through to the next round on four, two of which it already operates, First Great Western and First Capital Connect. There can be no guarantees on any of these.

This uncertainty is reflected in the multiple the shares trade on, seven times' earnings, and the 11.5 per cent yield. Limited success would prompt a significant rebound, but they still look highly speculative. For risk-takers only.

HICL

HICL Infrastructure was the first company specifically investing in schools, hospitals, roads and other public sector projects to float in London, in 2006. There are now six, so the market is getting a little crowded.

Such funds aim to offer investors a decent yield and the prospect of some increase in net assets and share price as those assets in the portfolio mature. They are, therefore, on the safe but dull end of the investment spectrum and more than half this company's investors are retail.

The projects in which HICL — the name reflects its past as an infrastructure fund owned by HSBC — invests in are "availability-based", rather than dependent on how much they are used for revenue. The fund takes a straight fee, which is entirely or partly linked to inflation.

HICL has a market capitalisation of more than £1 billion. Yesterday the company reported a March year-end net asset value of 116.3p, pretty close to the 117¼p share price. It has announced a second interim dividend of 3½p for the last financial year, making a total of 6.85p. Include the share price rise and the total return is 8 per cent last year, which is respectable enough.

It is also forecasting a total payout of 7p for the current year, which gives the shares a forward yield of about 6 per cent. Last year was an active one, with £326 million of fresh funds raised, £250 million in an issue of new shares that was oversubscribed.

As is the strategy, much of the money had already been spent — HICL typically borrows money, spends it and then raises fresh funds, so avoiding having huge amounts of low-earning cash in the bank. Unlike some of its rivals, it has little exposure to the eurozone, about 10 per cent of assets and mainly safe ones such as a Dutch high-speed rail link.

There is not a lot else to differentiate HICL from rivals, save its longer track record. Fine, if those investment criteria tick your boxes.

Telecom Plus

Telecom Plus has set some apparently challenging targets over the next couple of years, but such is the nature of the business that, on closer examination, they are rather less challenging than they might seem. The company sells on services such as energy and telecoms to consumers; the two main drivers are how many are signed up and how many can be persuaded to take all four services on offer.

Less significant are the “churn” rate, those leaving, and bad debt. All four measures are moving in the right direction. The number of customers was up by 12 per cent, while more than half are now taking all four.

There is an inevitable lag between signing up new customers and their contribution to profits; Telecom Plus is also refining that customer base by means of loyalty schemes and the like to attract those taking all four and unlikely to fail to pay their bills.

Pre-tax profits in the year to the end of March were almost 12 per cent higher at £30.7 million; that investment in new customers means they will rise by another 10 per cent this year, but thereafter the profits rise should parallel the growth in the number of services provided.

This suggests a 20 per cent rise in both in the year to March 2014; on any reasonable assumption, the dividend, up 23 per cent to 27p last year, should be approaching 40p.

This is good growth and a decent income uplift and suggests the shares, at 703p little changed on six months ago, should have further to go.

Amec

A largely unmarked move is announced by Amec. The oil and gas services company is in talks with Serco to buy the latter’s nuclear Technical Consulting Services business. This maintains Britain’s civil and defence nuclear industries and has revenues of £70 million a year. There is no guarantee a deal will be done, but it looks like at least a small bet that this country might start to build nuclear power stations again in due course.

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