Curo Group Holdings - CURO (7/7/19)

Description: CURO Group Holdings is a consumer finance company that provides financing to a range of underbanked consumers in the United States, Canada, and the United Kingdom. It offers unsecured installment loans, secured installment loans, open-end loans, and single-pay loans, as well as ancillary financial products, including check cashing, proprietary reloadable prepaid debit cards, credit protection insurance, gold buying, retail installment sales, and money transfer services. The company CURO Group Holdings Corp. was founded in 1997 and is headquartered in Wichita, Kansas and operates under the following brands:

- Speedy Cash
- Rapid Cash
- Cash Money
- Avío Credit
- Opt+
- Wage Day Advance
- Juo Loans
- LendDirect brand

Ticker: CURO
Price: $11.15
Market Cap: $517M
Performance: +17.5% YTD

Synopsis

CURO is a company that I personally am not a fan of but the valuation is something that makes it tempting. The company trades at around 4.5x earnings and 0.5x sales but there is a catch. When using enterprise value, which takes into account net debt, the company trades around 9x earnings and 1.0x sales because the company has approximately $912M in debt and $83M in cash.

CURO expects to 2019 to bring:

- Revenue in the range of $1.154 billion to $1.173 billion, an increase of 5-7% from 2018
- Adjusted Net Income in the range of $112.0 million to $128.0 million, an increase of 25% - 43% Y/Y
- Adjusted EBITDA in the range of $240.0 million to $260.0 million, an increase of 10-20% Y/Y
- Adjusted Diluted Earnings per Share in the range of $2.35 to $2.65, an increase of 26% - 42% Y/Y

This guidance looks pretty solid at the surface but when taking a closer look at Q1, which management touted as a solid quarter, I see a little bit of a different story.

	2019		2018				2017			
U.S	**Q1**		**Full Year**		**Q1**		**Full Year**		**Q1**	
Revenue	$ 226.1	*100%*	$ 853.1	*100%*	$ 204.6	*100%*	$ 737.7	*100%*	$ 174.3	*100%*
Provision for losses	85.0	*38%*	348.6	*41%*	64.3	*31%*	267.5	*36%*	49.2	*28%*
Net revenue	**141.1**	***62%***	**504.5**	***59%***	**140.3**	***69%***	**470.2**	***64%***	**125.1**	***72%***
Advertising costs	6.4	*3%*	48.8	*6%*	5.2	*3%*	36.1	*5%*	4.7	*3%*
Non-advertising COPS	45.0	*20%*	170.9	*20%*	43.8	*21%*	166.9	*23%*	43.3	*25%*
Total cost of providing services	51.3	*23%*	219.7	*26%*	48.9	*24%*	203.0	*28%*	48.0	*28%*
Gross margin	***89.8***	***40%***	***284.8***	***33%***	***91.3***	***45%***	***267.2***	***36%***	***77.1***	***44%***
Corporate, district and other	43.9	*19%*	112.8	*13%*	30.5	*15%*	120.8	*16%*	25.0	*14%*
Interest expense	14.7	*7%*	80.4	*9%*	22.3	*11%*	82.5	*11%*	23.3	*13%*
Loss on extinguishment of debt	-		90.6		11.7		12.5		12.5	
Segment operating income	**31.2**		**1.1**		**26.8**		**51.5**		**16.3**	
Adjusted EBITDA	**$ 61.2**	***27%***	**$ 193.9**	***23%***	**$ 66.0**	***32%***	**$ 180.1**	***24%***	**$ 57.8**	***33%***
Adjusted EBITDA Margin	*27.0%*		*22.7%*		*32.3%*		*24.4%*		*33.2%*	
Corporate, district and other	43.9	*19%*	112.8	*13%*	30.5	*15%*	120.8	*16%*	25.0	*14%*
Restructuring costs [2]	1.6		-		-		-		-	
U.K. redress and related costs [2]	7.8		-		-		-		-	
Legal settlements [2]	-		(0.4)		-		4.3		-	
Transaction-related costs [3]	-		-		-		5.6		2.3	
Share-based compensation [4]	2.2		8.2		1.8		10.3		0.1	
Other adjustments [5]	(0.1)		0.2		(0.1)		(0.1)		0.0	
Adjusted Corporate, district and other	**32.4**	*14%*	**104.7**	*12%*	**28.7**	*14%*	**100.7**	*14%*	**22.7**	*13%*

Revenue grew 10.8% Y/Y but provision for losses grew 32.2% to $85.0M and made up 38% of revenues vs. 31% last year. The company claims its due to a shift to lower-yielding, higher dollar loan products but this still drastically higher and if it's an indicator of what to expect in future quarters that may be dangerous.

In addition, net revenue after subtracting for the provision for losses only came in $800K higher Q/Q despite lending a lot more. As a result, gross margins fell from 45% to 40%. What's even more worrisome is that EBITDA actually fell Y/Y from 32% to 27%.

Taking it a step further, if we look at FY18 we see the total numbers are much worse on margin basis than Q1 2018 specifically, so this looks like the numbers have been trending downwards for over a year now and have appeared to settle in Q1 2019. If Q1 was the stabilization quarter, I'm still not too pleased with these numbers.

CURO is not going to fetch a premium valuation, let's call it what it is. The only thing that makes this investment attractive is the valuation at which it is trading and therefore it's probably worth entering for a swing but I personally don't like the long-term outlook here. Lending to the underserved market is extremely risky and will be one of the first stocks to plummet if the economy falters in the slightest bit. Some tailwinds are an improving and healthy economy with above normal wage growth and a political backing for a higher minimum wage.

I've personally never heard of the brands CURO owns and believe they are operating in a very competitive space with companies like On Deck Capital, Lending Tree, Kabbage, and many others.

Diamondback Energy - FANG (7/7/19)

Description: Diamondback Energy Inc. is an independent oil and natural gas company that focuses on the acquisition, development, exploration, and exploitation of unconventional and onshore oil and natural gas reserves in the Permian Basin in West Texas. As of December 31, 2018, the company's net acreage position was approximately 461,218 acres in the Permian Basin; and estimated proved oil and natural gas reserves were 992,001 thousand barrels of crude oil equivalent. It also held working interests in 7,279 gross producing wells, as well as royalty interests in 2,645 additional wells. In addition, the company, through its subsidiary, Viper Energy Partners LP (see CUBE's research on VNOM here), owns mineral interests in approximately 532,295 gross acres and 14,841 net royalty acres in the Permian Basin and Eagle Ford Shale. Diamondback Energy, Inc. was founded in 2007 and is headquartered in Midland, Texas.

Ticker: FANG
Price: $107.41
Market Cap: $17.7B
Performance: +16.2% YTD

Synopsis

As mentioned above, FANG is pretty much a pure play on the Permian Basin. The Permian Basin, which is located in West Texas and Southeastern New Mexico, produces more than 30% of the total U.S. crude oil production. The EIA forecasts that Permian production to average 3.9 million b/d in 2019, a 514,000 b/d increase from 2018. To give you some context, if the Permian basin was part of OPEC, it would be the fourth-largest OPEC member, right behind Saudi Arabia, Iran and Iraq. In fact, the Permian basin could soon overtake Iran in terms of oil production.

The Permian Basin has been home to some serious M&A. For example, much of the reason Chevron wanted to acquire Anadarko was for more access to the Permian Basin but it was Occidental that wound up swooping in to make a bigger bid and ultimate purchase of Anadarko. Also, just a few months ago, Exxon Mobil and Chevron both said they planned to grow their Permian Basin production to about 1 million barrels of oil equivalent a day within five years, roughly tripling their current output. Companies like Diamondback and Pioneer (PXD) are pure Permian Basin plays and and I believe there is a solid possibility companies like Chevron and other turns their attention to FANG, PDX, EOG, APA and the like for possible acquisition targets.

FANG itself has been involved in some M&A with its most recent and largest purchase being Energen for $9.2B in late 2018.

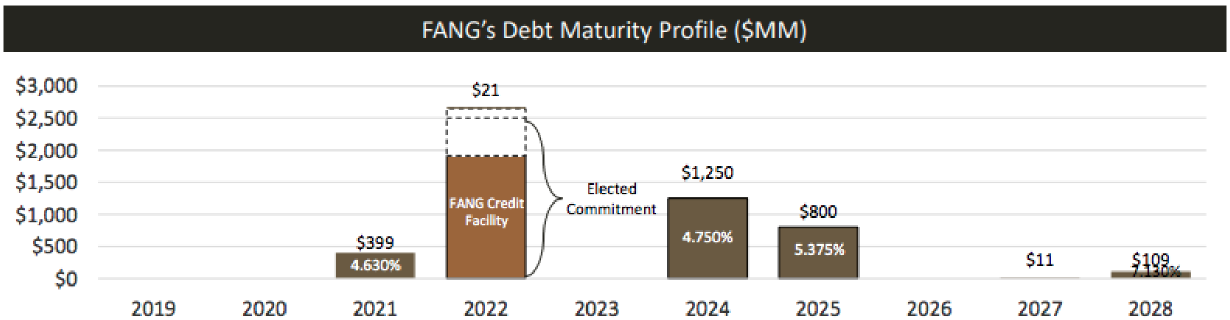
Some pros for FANG:

1. Operating free cash flow over the last twelve months stands at $1.6B
2. FANG expects free cash flow of $750M in 2020 at $55 WTI – super impressive if pulled off and most likely due to synergies with Energen, which are expected to save the company $155-175M in 2019 alone
3. No debt maturation in 2019 or 2020
4. Targeting ~26% annual production growth (30% oil growth) in 2019
5. FANG has also declared a $2B share buyback program through 2020.

Some cons for FANG:

1. Trades almost identically with oil
2. Net debt to adjusted EBITDA stands at 1.7x

3. Long-term debt is $4.7B while cash balance is at $126M and total liquidity is $702M. (Not including $322M in asset sales that recently occurred)
4. Company has drawn $1.91B from its $2.5 billion revolving credit facility which matures in 2022
5. Negative free cash flow due to high CAPEX



On a forward EV/EBITDA and forward EV/Sales, FANG is a bit more expensive than its peers at 6.3x and 4.9x. On a forward P/E, FANG trades towards the cheaper end with at 9x currently.

Overall, I think FANG is one of the better companies in the space and if it means anything, MKM just assigned a $163 PT and BAC gave them a $170 PT based on their free cash flow targets I previously spoke of. If the FANG is able to hit those targets and even implement some of their cash flow to share buybacks and dividends, it will most likely take shares to those levels.