ORD MINNETT

Company Review

Ord Minnett Research — Tuesday 22 February, 2011

Cash Converters

1H11 results review

- Cash Converters again pumped out solid 1H11 results. Revenue was up 48.3% to $87.9m and NPAT up 42.2% to $14.3m. EPS was up 8.6% to 3.8cps due to the greater share count compared to the pcp.
- The positives included extremely strong results from the corporate stores division and continued strength in the financial services business for both the cash advance and the loan businesses.
- The corporate store count is now 80 compared to our expectation of 72 with a further seven in various stages of negotiation. We have modelled a greater corporate store rollout into the future – particularly given the business has over 507 franchised stores on its books – which it can select from.
- We are upgrading forecasts as a result for the full year and particularly the outer years driven by corporate stores and the ongoing rollout and success of the finance business. The loan book in Australia now stands at $47.3m and given the rapid growth and momentum will continue to deliver earnings.
- Given the large UK market, existing large franchise base, a shortage of micro finance and alternative finance, this business has the potential to keep on growing into the future.
- The only cloud on the horizon is regulation of the industry and this remains an ongoing risk for the business. In the meantime Cash Converters continues to produce excellent results. Pricing this risk is hard; however, the bigger and more diverse Cash Converters becomes the less of problem this is. Retain Accumulate – it is a solid and well positioned business but with some degree of risk.

Key Financials

Year-end June (A$)	FY10A	FY11F	FY12E	FY13E
Revenue ($m)	126.6	188.6	235.4	275.1
EBITDA ($m)	33.7	43.6	52.4	61.3
Net profit after tax ($m)	21.6	29.2	34.6	40.6
EPS (¢)	6.6	7.5	8.9	10.4
P/E (x)	12.7	11.2	9.5	8.1
EV/EBITDA	8.4	7.5	6.4	5.4
Dividend (¢)	3.0	3.8	5.5	7.5
Net Yield (%)	3.6%	4.6%	6.5%	8.9%
Franking (%)	100%	100%	100%	100%
Normalised NPAT ($m)	21.6	29.2	34.6	40.6
Normalised EPS (¢)	6.6	7.5	8.9	10.4
EPS Growth (%)	-0.4%	13.3%	18.4%	17.6%
Normalised P/E (x)	12.7	11.2	9.5	8.1
Relative P/E (%)	80.2%	70.8%	59.8%	50.8%
Normalised ROE (%)	13.3%	16.4%	18.0%	19.8%

Source: Iress, Company Data, Ord Minnett Est. Share price: $ 0.84 Feb 21, 2011

CCV $0.84

Recommendation
Accumulate

Risk Assessment
High

Sector – consumer discretionary

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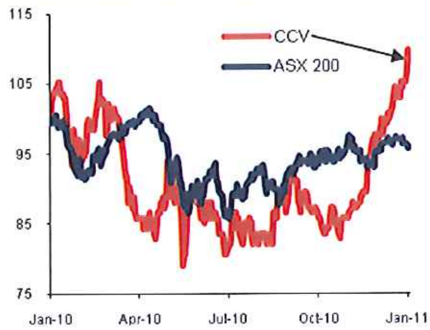
Cash Converters	
ASX Code	CCV
52 week range	A$0.5 - A$ 0.87
Market Cap	321
Shares Outstanding	379.6
Av Daily Turnover	420,719
ASX All Ordinaries	4,991
ASX200 Industrials	3,849
NTA FY11E (¢ per share)	21.6
Net Debt FY11E	5.6

Relative price performance



Source: Iress

Consensus earnings

	FY11F	FY12F
NPAT (C)*	27.5m+	30.5
NPAT (OM)	29.2	34.6
EPS (C)		8.3
EPS (OM)	7.7	9.1

Source: CCV guidance Feb 2011

1H11 results review – strong

This was a strong result driven by corporate stores and the finance business. The business has a further seven stores under various stages of negotiation and this greater store and loan book balance should continue to help the business into 2H11 and beyond.

Another strong result

Table 1: 1H11 financial result review

Item	1H10A	1H11A	% change	1H11F	% differ
Revenue ($m)	59.3	87.9	48%	84.7	3.8%
EBITDA	15.9	21.6	36%	19.5	10.8%
EBIT ($m)	15.3	20.9	36%	18.9	10.6%
NPAT reported ($m)	10.1	14.3	42%	13.4	6.7%
EPS reported (cps)	3.5	3.8	8.6%	3.6	7.0%
DPS total (cps)	1.5	1.75	16.7%	2.0	-12.5%
Corporate stores	72	80	11%	72	11.1%

Source: Company data, OM

The business opened some greenfield sites during the period that we had not factored into our store forecasts. Management believes that the UK can sustain 600 stores including 80 in Scotland. Australia in total currently sustains 139 stores (39 corporate stores and around 100 franchise stores). Give there is currently 178 stores in the UK in total this implies much more growth for the business even if competition plugs some of this gap.

Plenty more store opening and acquisitions possible

Lifting estimates – retain Accumulate

We are putting through some fairly major changes to the model reflecting the good industry growth prospects, store rollout and ongoing success from the rollout of the corporate business. There is upside risk for FY11 with 1H11 NPAT of $14.3m, leaving only $14.9m for 2H11 to realise our forecasts.

Only modest growth in 2H11 required to hit our forecasts

Table 2: Changes to estimates

A$m June	FY11F	FY11F	%Δ	FY12F	FY12F	%Δ
Profit and loss	Previous	Current		Previous	Current	
Revenue	171.6	188.6	+9.9%	198.9	235.4	+18%
EBIT	40.7	41.4	+1.7%	45.1	50.2	+11.3%
Reported NPAT	28.9	29.2	+1.0%	31.3	34.6	+10.5%
Reported EPS	7.6	7.5	-1.0%	8.3	8.9	+7.2%
DPS	4.6	3.8	-17%	5.0	5.5	+10%
Corporate stores	75	86	+14.6%	84	101	+20%

Source – OM

We retain our Accumulate recommendation and have lifted the price target to 93 cents per share. Any weakness (not driven by fundamentals) should be used to add to the position.

Retain Accumulate

Risk factors

Three areas of caution and risk:

1. The business is now ageing its new lending books. Bad debt levels were rising as a percentage of loans and are now falling compared to 2H10 which is positive. Maintaining a sound bad debt profile is important to the business's ability to grow in a controlled fashion in the UK.
2. Christmas was not as buoyant as expected in Australia but was offset by other areas of the business.
3. The federal government is taking over regulation of the National Credit Code. Phase two is to consider implementing a possible interest rate cap by mid 2012.

The UK Office of Fair Trading has recently looked at the issue and according to Cash Converters concluded "price controls would not be an appropriate solution to the particular concerns we have identified".

Operational failure – system problems.

Increased competition.

Gold prices – a decline would be problematic for the scrap market and loan values.

Business description

Cash Converters is one the largest corporate second hand goods dealers, pawn brokers and providers of alternative credit in the world (albeit in what is in a highly fragmented industry) with over 600 outlets (528 franchisee and 80 corporate stores). It has four divisions:

1. Australia – including growing corporate store presence
2. UK – including a growing corporate store presence
3. Finance – alternative finance and/or micro credit
4. Franchisee operations (rest of world) – tiny percentage of revenue despite large footprint.

Financial statements

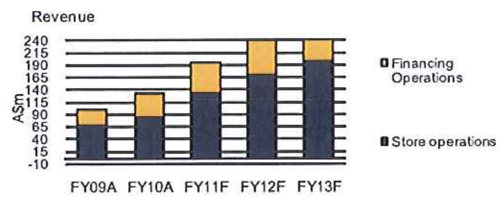
Cash Converters

Accumulate

Profit & Loss Statement (A$m)	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	94.4	126.6	188.6	235.4	275.1
Operating Costs	0.0	0.0	0.0	0.0	0.0
EBITDA	**25.5**	**33.7**	**43.6**	**52.4**	**61.3**
Depreciation & amortisation	-1.1	-1.5	-2.2	-2.2	-2.2
EBIT	**24.4**	**32.2**	**41.4**	**50.2**	**59.1**
Net Interest	-1.1	-1.0	0.3	-0.9	-1.0
PBT pre-unusual items	**23.3**	**31.2**	**41.7**	**49.4**	**58.1**
Unusual non-operating items	0.0	0.0	0.0	0.0	0.0
NPBT	**23.3**	**31.2**	**41.7**	**49.4**	**58.1**
Income Tax Expense	-7.2	-9.6	-12.5	-14.8	-17.4
NPAT pre-OEI	**16.1**	**21.6**	**29.2**	**34.6**	**40.6**
Minority interest	0.0	0.0	0.0	0.0	0.0
NPAT	16.1	21.6	29.2	34.6	40.6
Abnormals / convertible dist.	0.0	0.0	0.0	0.0	0.0
Reported NPAT	**16.1**	**21.6**	**29.2**	**34.6**	**40.6**
Normalised NPAT	**16.1**	**21.6**	**29.2**	**34.6**	**40.6**
Effective Tax Rate	30.9%	30.8%	30.0%	30.0%	30.0%
Reported - diluted EPS	6.6	6.6	7.5	8.9	10.4
Normalised (diluted) EPS	6.6	6.6	7.5	8.9	10.4
DPS (cps)	3.0	3.0	3.8	5.5	7.5
Dividend Yield (%)	3.6%	3.6%	4.6%	6.5%	8.9%
Payout Ratio	44%	45%	50%	60%	70%
Franking	100%	100%	100%	100%	100%
Free cash flow (cps)	5.6	3.5	-0.8	4.0	6.4
FCF Yield (%)	6.7%	4.1%	-1.0%	4.8%	7.6%

Cash Flow Statement (A$m)	FY09A	FY10A	FY11F	FY12F	FY13F
Gross cashflow	8.6	7.4	19.1	33.9	45.6
Net Interest (paid)/received	-0.6	0.4	0.3	-0.9	-1.0
Tax Paid	-6.6	-7.3	-12.5	-14.8	-17.4
Other Operating Items	13.9	16.0	0.0	0.0	0.0
Operating Cash Flow	**15.3**	**16.5**	**6.9**	**18.3**	**27.2**
Capex	-1.5	-3.4	-10.0	-3.0	-3.0
Net Acquisitions and Investments	-18.5	-23.9	-25.0	-5.0	0.0
Other investing items	0.3	-1.9	0.0	0.0	0.0
Investing Cash Flow	**-19.7**	**-29.2**	**-35.0**	**-8.0**	**-3.0**
Inc/(Dec) in Equity	0.0	68.3	0.0	0.0	0.0
Inc/(Dec) in Borrowings	4.0	-2.3	0.0	0.0	0.0
Dividends Paid	-7.3	-9.2	-14.2	-20.2	-27.7
Other Financing Items	-0.5	0.1	0.0	0.0	0.0
Financing Cash Flow	**-3.8**	**56.9**	**-14.2**	**-20.2**	**-27.7**
Net Inc/(Dec) in Cash (ex-FX)	**-8.2**	**44.2**	**-42.4**	**-9.9**	**-3.5**

Balance Sheet (A$m)	FY09A	FY10A	FY11F	FY12F	FY13F
Cash and Cash Equivalents	7.0	50.7	8.3	0.0	0.0
Current Receivables	31.8	49.8	74.2	92.6	108.2
Other Current Assets -Inv	7.7	12.1	17.3	21.3	24.7
PP & E	4.6	6.8	14.6	15.4	16.2
Intangibles	60.3	70.6	95.6	100.6	100.6
Other Non Current Assets	3.2	7.1	7.1	7.1	7.1
Total Assets	**114.6**	**197.1**	**217.2**	**237.0**	**256.8**
Short term Debt	3.9	3.3	3.3	3.3	3.3
Current Payables	8.4	10.5	15.6	19.5	22.8
Other Current Liabilities	5.8	8.5	8.5	8.5	8.5
Long term Debt	12.9	10.6	10.6	10.6	10.6
Other Non Current Liabilities	1.3	1.3	1.3	1.3	1.3
Total Liabilities	**32.3**	**34.2**	**39.3**	**43.2**	**46.5**
Total Equity	**82.3**	**162.9**	**177.8**	**192.2**	**205.1**
Net Debt/(cash)	9.8	-36.8	5.6	13.9	13.9



Source: Ord Minnett, Company Data.

Divisions (A$m)	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue					
Store operations	70.1	85.4	133.2	170.8	199.8
Financing Operations	30.1	47.4	61.6	70.9	81.5
Intersegment	-5.8	-6.2	-6.2	-6.2	-6.2
Total	**94.4**	**126.6**	**188.6**	**235.4**	**275.1**
Drivers					
Corporate stores	37	58	86	101	116
Comp sales		0.0%	2.0%	2.0%	2.0%
Financing book Y/E $m	21.4	38.7			

Operational Metrics (%)	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue growth	27.1%	34.1%	49.0%	24.8%	16.9%
EBITDA margin	27.0%	26.6%	23.1%	22.3%	22.3%
EBITDA growth	9.0%	32.2%	29.3%	20.3%	16.9%
EBIT margin	25.8%	25.4%	21.9%	21.3%	21.5%
EBIT growth	4.6%	32.0%	28.5%	21.4%	17.7%
Normalised EPS growth	3.1%	-0.4%	13.3%	18.4%	17.6%
Return on asset	14.7%	11.3%	13.3%	14.8%	16.1%
Normalised ROE	19.6%	13.3%	16.4%	18.0%	19.8%

Valuation Ratios (x)	FY09A	FY10A	FY11F	FY12F	FY13F
Reported P/E	12.7	12.7	11.2	9.5	8.1
Normalised P/E	12.7	12.7	11.2	9.5	8.1
Price To Free Cash Flow	14.9	24.3	-102.0	20.9	13.2
EV / EBITDA	8.3	8.4	7.5	6.4	5.4
EV / EBIT	8.7	8.7	7.9	6.6	5.6

Leverage	FY09A	FY10A	FY11F	FY12F	FY13F
Net Debt / Equity	12%	-23%	3%	7%	7%
Net Debt / (ND + Equity)	11%	-29%	3%	7%	6%
Net Debt / Total Assets	9%	-19%	3%	6%	5%
EBITDA Interest Cover (x)	23.2	n.m	n.m	n.m	n.m
EBIT Interest Cover (x)	22.2	n.m	n.m	n.m	n.m

Substantial Shareholders	m	%
Ezcorp	124.4	32.8%
Staff	21.0	5.5%
Rand Holdings	14.9	3.9%

Valuation			
WACC (%)			10.9%
Fully Diluted Number of shares (m)			389.6
Cost of Equity			12.0%
D/EV			20.0%
Risk Free Rate			5.5%
	A$m	A$	
Operational NPV (5 year Forecast)	77.4	0.20	
Terminal Value	273.8	0.70	
Less Net Debt	-5.6	-0.01	
Franking Credits Value (50% weight)	16.6	0.04	
Group NPV	345.6	**0.93**	
Current Share Price		0.84	
NPV Discount to Share Price			**10.7%**

Sensitivity Analysis

		WACC				
		9.9%	10.4%	10.9%	11.4%	11.9%
Terminal Growth Rate	1.6%	$1.01	$0.95	$0.90	$0.85	$0.80
	1.8%	$1.03	$0.97	$0.91	$0.86	$0.82
	2.0%	$1.06	$0.99	$0.93	$0.88	$0.83
	2.2%	$1.08	$1.01	$0.95	$0.89	$0.84
	2.4%	$1.10	$1.03	$0.97	$0.91	$0.86

		β				
		0.9	1.0	1.0	1.1	1.1
Equity Risk Premium	5.2%	$1.12	$1.09	$1.06	$1.03	$1.00
	5.9%	$1.05	$1.02	$0.99	$0.96	$0.94
	6.5%	$0.99	$0.96	$0.93	$0.90	$0.87
	7.2%	$0.94	$0.90	$0.87	$0.85	$0.82
	7.8%	$0.89	$0.85	$0.83	$0.80	$0.77

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Guide to Ord Minnett Recommendations

BUY	The stock's total return (nominal dividend yield plus capital appreciation) is expected to exceed 15% over 12 months.
ACCUMULATE	The stock's total return is expected to be between 5% and 15%. Investors may add to existing holdings, or initiate holdings on share price weakness.
HOLD	The stock is fairly priced, and its total return is expected to be between 0% and 5%.
LIGHTEN	The stock's total return is expected to be less than 0% and possibly down 15%. Investors should consider selling into share price strength.
SELL	The stock's total return is expected to lose 15% or more.
RISK ASSESSMENT	Classified as High, Medium or Low, denotes the relative assessment of an individual stock's risk based on an appraisal of its disclosed financial information, volatility, nature of its operations and other relevant quantitative and qualitative criteria.