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Cash Converters (CCV)

COMPANY REPORT | INITIATION OF COVERAGE

Pawn cracker

RESEARCH ANALYST

Nick Caley

+61 3 9602 9283 ncaley@baillieu.com.au

RECOMMENDATIONS

Rating	**BUY▲**
Risk	Medium
Price Target	**$1.45**
Share price	$1.19

Initiation of coverage: We initiate coverage of Cash Converters International (CCV) with a BUY call, DCF valuation of A$1.44 and price target of A$1.45.

History: CCV was founded in 1984 when Brian Cumins, the Company's founder and former Chairman, opened a retail outlet in Perth, Western Australia. In 1990 CCV expanded into other Australian States and in 1991 expanded into the UK. CCV now has representation in 21 countries.

The business: CCV's core business is the ownership and franchising of retail stores which undertake pawn broking services, second hand goods retailing and the provision of consumer credit. Stores in Australia and the UK are a mix of owned and franchised operations whilst the rest of the world is franchised – largely on a passive royalty model.

Pawn cracker: CCV has a number of material revenue streams including franchise fees, operating and marketing levies, personal loan interest, pawn broking and loan administration on behalf of franchisees. The growth engine of the group is the provision of short-term personal loans – this activity accounted for 38% of revenue in 1H13 yet contributed 60% of the group's result.

FY13 – growth interrupted: Whilst the passing of the Consumer Credit Legislation Amendment (Enhancements) Bill 2012 has largely left CCV unscathed, increased procedural requirements for loans under A$2k has resulted in a significant slowing of loan volumes in recent months leading to subdued guidance for FY13. CCV believes many of these procedural issues have now been addressed and growth is resuming.

Major shareholder: NASDAQ listed EZCORP Inc, currently owns 33% of the issued capital of CCV. EZCORP also holds various state based master franchise licences for Cash Converters in the US and Canada.

Financial position: At 1H13 CCV had gross debt of A$34m with net debt to equity of a modest 5%. In March 2013, CCV stated that it had obtained a 2 year A$60m securitisation funding capability through Westpac to fund up to 70% of each loan originated within its personal loan book. We understand that that the recent acquisition of 11 franchised stores in Australia for A$33m was largely debt funded.

Investment view: BUY call supported by: 1) stock looks to be cheap versus our DCF valuation; 2) strong growth track record with 8 year CAGR revenue and EPS growth of 44% and 19% respectively; 3) forecast double-digit EPS growth through FY14 and FY15; 4) multiple growth and yield enhancement options through managing the mix of franchise and owned stores; 5) CCV now appears to be ex-regulatory risk in Australia; 5) securitisation funding underwrites growth; and 6) the stock has pulled back from recent highs based on what we view as a temporary slowing of lending volumes.

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