EQUITY RESEARCH

Cash Converters (CCV)

Initiation of coverage

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KEY POINTS

- Initiation of coverage with a Buy recommendation.
- Cash Converters (CCV) has worked hard over the last few years to resolve and settle many of legal disputes/regulatory changes and enters FY23 de-risked in this respect.
- We believe that it is highly likely that the Financial Sector reform 2022 bill gets passed by the Senate and becomes active in July 2023. The regulation set guidelines terms for small amount credit contracts that limit the amount lent to 10% of net borrower income. This will reduce demand for this form of credit.
- CCV has a series of growth initiatives that will offset this regulatory headwind including the recent acquisition of 75% of the New Zealand business (CCV already owned 25%), strong momentum, some increased demand for medium amount credit contracts, new products (line of credit) – replacing small amount contracts, the ability to consolidate the industry and benefitting from store acquisitions. We also believe traditional pawn broking will regrow. Combined – we believe this will offset the regulatory change's impact.
- Normal trading conditions vs the substantial lost trading days in FY22 due to COVID19 (1H22=24% of available trading days) and government stimulus payments (and reduced economic activity)
- Recent results demonstrated solid loan growth and future loan book income (fees and interest) of $66.2m underpins a strong FY23 with a replenished loan book up 28% pcp to $214.6m with 1Q23 revenue up 24.5% to $69m.
- Continued lower levels of unemployment and bad debt levels under control due to loan mix improvement, past /current tighter credit standards, and use of electronic bank statements also supportive helped by the recent in-sourcing of loan collection in 2H21.

INVESTMENT VIEW

- CCV is profitable, has a PE of 7.0X FY23F, is self-sufficient in terms of capital requirements and pays a fully franked dividend (helped by a massive franking credit balance of $67m).
- We have chosen a blended valuation method of both P/E relative and price to book valuation for the business. NTA is also $0.30/share. Target price $0.30/share with a fully franked dividend is supportive.

KEY DRIVERS

- Recent results showing continued positive trading conditions and reasonable underlying demand. Continued need for sub-prime credit due to higher than normal inflation and reluctance or inability of others to provide credit for those that need it and can adequately service/repay
- Improved small store, high end jewellery format(s) – as greenfield and existing re-formats. New product development and existing product enhancement.

RISKS

Include (but are not limited to) – additional regulation, class actions, legal action and disputes, intensification of competition, falling gold price in AUD$ terms, debt debts, inappropriate valuation of goods, franchisee dissatisfaction, poor acquisitions, financial technology reducing demand (Gumtree/fintech/micro finance apps), severe economic recession/job losses, product deflation, timely and well-priced access to debt.

Recommendation	Buy
12 mth share price target	$0.30
Risk rating	High
Current share price	$0.24
Previous recommendation	Initiation
Price target methodology	P/E, P/BV
Total return	32%
FY23 NPAT growth	6%
Market capitalisation $m	151
Liquidity $ per day	112,888

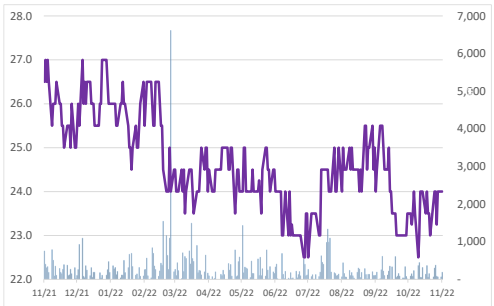
Source – PAC Partners

Financial Forecasts & Valuation Metrics

June y/e $m	Jun-21A	Jun-22A	Jun-23F	Jun-24F
Revenue	201.3	245.9	297.9	299.5
EBITDA	44.0	52.7	59.7	59.5
NPAT (normalised)	16.7	19.0	22.1	18.0
EPS Adj (c)	2.6	2.9	3.4	2.8
EPS growth	n.m	12.0%	16.5%	-18.6%
DPS (c)	1.0	2.0	2.0	2.0
Yield (%)	4.2%	8.3%	8.3%	8.3%
NTA	30.6	29.9	29.2	30.9
PE Underlying (x)	9.1	8.1	7.0	8.6
Net Cash (debt)	(61.6)	(75.1)	(107.6)	(98.3)

Source: PAC Partners estimates

12-month Share Price and Volume (000's)



Source: IRESS

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Executive Summary – momentum retained ….

We have commenced coverage of CCV with a Buy recommendation. Our investment thesis is predicated on:-

Six reasons to revisit CCV

1. Resolution of a substantial number of legal disputes from past business activity helping to materially reduce legal and financial risk and the legal cost budget – offset in part by the new regulation from the Financial Sector reform bill of 2022 that will introduce protected earnings amounts within small credit contracts.
2. The business will face a FY23/24 headwind from the reform. We believe that a combination of new products, some time before the change hits (July 2023), moving some customers to Medium credit contracts, adaptation of customer behaviour such as greater use of pawn loans, reduced competition from players unable to adapt and overall general business momentum will create sufficient offsets to still enable flat to modest earnings growth.
3. An ability to acquire existing Australian franchisee stores on a reasonable basis and convert those into fully owned corporate stores. Nine recently (past 24 months) acquired stores set up drive profitability growth into the future (estimated to be at least 5% p.a just from acquired stores annualised contribution.
4. The recent acquisition of the 75% of the New Zealand business that CCV did not own for $15m. The entire NZ business reported pre-tax profit of $3.42m in FY22.
5. Post COVID19 recovery. Increased government payments and reduced economic activity resulted in a big lockdown paydown of the loans outstanding. With COVID19 now part of life – economic activity has resumed. Higher levels of inflation and the rising cost of living pressures are creating additional demand as customers look for cash to fund gaps between income and expenditure.
6. Funding lines established, renewed with reliable and committed parties (Fortress) and controlled by a reliable offshore lender with available capacity. Recent renewal of the Fortress $150m securitisation facility on more commercial terms and this provides funding certainty for CCV.

Other general factors of note include banks reduced desire in be involved in the industry

7. Low unemployment keeping bad debts under control. In part due to economic circumstances but also due to mix/past changes/past regulatory issues and generally tighter credit standards. CCV needs to take some risk and will always incur bad debts – the main issue is that they are largely predictable and reasonable care was taken when the loans were first originated.
8. Further development of the online business to provide reliable and competitive methods of disposing of goods from expired pawn loans and sourcing quality loans.

Cash Converters (CCV) is an Australian business that specialises in sub-prime, non-bank lending and second-hand goods retailing.

Fintech and smaller operators have less access to equity and/or loan capital

The business started as a single store in Perth in 1984[1] and has expanded to 155 stores in Australia with approximately 51% corporately owned (79) and approx. 49% franchised (76). CCV has 548 a further 548 stores across 12 countries which operate under a trademark/franchisee agreement. CCV's material part of the business is in Australia. CCV generates the majority of its earnings from its Australian operations, and of that operation, its personal finance business is the key contributor (~50% of the EBITDA). CCV has a 25% equity interest in the 22-store New Zealand network and receives royalties from the remaining international franchises.

Regulation also is reducing aggressive players in the industry. Less adverts on TV is one such manifestation of this

CCV has a major shareholder namely the larger US listed pawn broker and sub-prime lender Ezcorp (EZPW.US). Ezcorp owns circa 41% CCV shares and has two representatives on the CCV board, one of which is the Non-Executive Chair. Ezcorp has supported past capital raising initiatives from CCV.

Ezcorp has a market cap of US$517m turned over US$652m in revenue (9 months to June 2022) and reported an operating income of US $60m and net income of $42.8m. Revenue was hit by

[1] The Lindy Effect (named after a NYC delicatessen that was frequented by comedians that conducted post-mortems on recent performances) states the future life expectancy of technology, idea or practice is proportional to its current age. We believe that money lending has been around for at least 2,000 years or even greater (refer to the Bible). Given the longevity of the money lending (probably as pawn broking) it is quite likely that Cash Converters' business model has many years left in it.

COVID19 and is bouncing back. Ezcorp has approx. 1,149 stores in total - split about 45%/45% in the US and Mexico and smaller presence in Central America.

CCV has over many years expanded into the personal loan market and vehicle finance out of being a pure pawn broker and second-hand retailer. CCV has a substantial online presence that augments the physical store network and provides lending to an expanding number of customers.

On a fundamental level – CCV make their money – by lending money and earning interest on that money as/when it is paid back and by buying/selling quality second-hand goods.

There are a few basic revenue streams of business:-

The loan mix is changing from low value /very high risk to bigger value /perhaps lower risk = therefore and improving

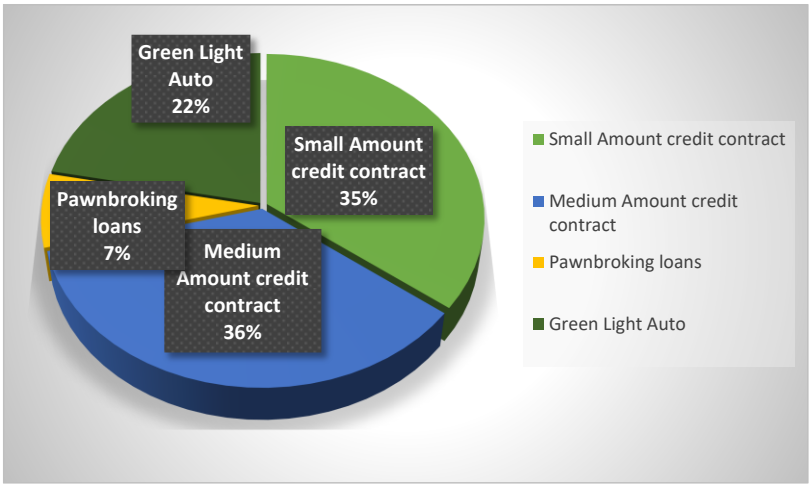
1. Interest from pawnbroking loans.
2. Sale of second-hand goods from loans that are not redeemed.
3. Interest and establishment fees from personal and small loans where goods are not offered as security i.e. unsecured loans.
4. Retail sales from purchased second-hand goods bought from customers who wish to sell/not pawn unwanted items. The majority of goods sales are in this category. There are very limited sales of brand-new goods.
5. Standard style Auto loans – interest /fees - distributed via stores and auto dealers/auto and loans brokers.

Now more mix between different types of loans

The actual contribution for CCV in order is:-

- Personal Finance
- Second-hand goods retailing
- Vehicle finance - Auto Loans (Green Light Auto)

Table 1 – CCV's loan book composition – total book is $213.9m (30 June 2022)



Source:– CCV recent trading update

610k active customers – 5% of the Australian working population have an active account with CCV

1.5k accredited auto dealers/brokers

1.1m transactions in store, 129k in loans

CCV is a big business

The business has been growing the auto finance and medium size loans in recent years, Loan book growth in recent times has recovered well from COVID19 lockdown paydown of loans with gross loan book growing 20% yoy.

1.4m items sold

Table 2 – Revenue by product lines in $m

Division	Jun 22A
Personal Finance Int	104.0
Store operations Int	42.9
Goods sales	80.7
All revenue x auto	**227.6**
Vehicle Finance Int	12.2
Franchisee opers. Fees	16.9
Other	(10.9)
Total	**245.9**

Personal finance – Cash Converters personal small cash loans, admin for these loans Australian wide
Store operations – purchase/sale of 2nd hand goods, cash advance /pawnbroking of corporate stores in Australia
Vehicles – Green Light Auto loans – Vehicle finance.
Franchisee – license fees and service fees.

Source: CCV and PAC Partners

Often the borrowers don't immediately buy from the store (they need the money for reasons other than shopping in the CCV shop). Most of the time customers seek funding for needs such as paying a bill, groceries or plugging a short-term cash flow need in life/business. Most buyers tend to be members of the public that have more wealth and are looking for a bargain than those borrowing.

The pawn broking and small loans business is seasonal with Xmas normally very busy in terms of loans

This separation of intent/need is partly why potential lenders come into a different part of the store to negotiate a loan vs the retail shop front. By retailing goods that are not redeemed (loans not paid back) – the pawn broker recovers the loans and also has an intimate knowledge of the value of goods that are pledged as future collateral for loans.

Easter is also busy

The majority of retail sales are on items that have been purchased from other customers. Retail sales are due to goods that were (pawned) pledged but not redeemed – and are an outcome (by-product) of the loan that has not been paid. CCV can also buy second-hand goods that might appeal to retail customers to generate additional income. Generally speaking, these have to be very saleable and might be to supplement the store /create interest. Buying gold for example is highly profitable and low risk with it valued as a % of the scrap price.

Early New Year – unwanted new gifts get sold for cash, which can be great business – sellers less fussy about price

All pawnbrokers prefer to count cash not stock…

Figure 1- Ezcorp example of goods that might be pawned /and /or for sale

Loans tend to be repaid in January-March

July /August loans get paid back after tax returns (refunds)

The business ins 2/4 weekly with pay and Centrelink cycles important

Source: Ezcorp

Fridays (after Thursday pay cycle) are normally busy

Pawn broking terms

Pledge – use goods to get loan

Redeem – pay loan back and get goods back

Pay interest – some people will simply pay some of the interest and leave good pawned – can extend loan

Expire – the loan has ended and the good are now able to be sold

PAC Partners is in a slightly unique situation – with the author (Stephen Scott) - having worked in a family pawn broking business in Western Sydney (Kingswood) for 6 months. We believe we bring hands-on experience to the analysis of CCV.

Franchisee operations – royalties and fees (including software/service) from over 548 franchisee/licensed stores and 155 stores in Australia (split with 79 corporately owned and 76 franchised). The franchise/royalties fee stream (in the UK and Australia) was cut during the pandemic to help support franchisee stores. We expect it to gradually improve as conditions now normalise. CCV may choose to keep some fees low to help stores recover and prosper. For franchised stores, CCV provides both the software and some funding capital for some loans and this is a profitable business for CCV and reduces the funding capital demand for the franchisees.

Over time we believe CCV are interested in prudentially acquiring more Australia franchised stores and converting them into 100% corporate stores. In FY21/22 CCV bought 6 Australian franchised stores including Morley, Melbourne, Blacktown, Richmond, Coconut Grove and Palmerston. In 1H22 CCV bought another 3 stores and has at least two potential greenfield sites in the pipeline.

CCV is aware this franchisee acquisition program will take time and needs to be a fair deal for those franchisees that wish to sell and move on.

Store operations – the retail sale of new and mainly second-hand goods bought from customers and goods from loans that were not repaid, cash advances and pawn broking operations of 79 company owned stores in Australia. Store operations include all loan and retail activities within these 100% owned stores.

Personal Finance - this segment includes all unsecured personal loans (excluding Cash Advance) distributed through stores and online.

There are two types of loans within the personal finance division:-

1. SACC (Small amount credit contracts) generally between $400 - $2,000 with a duration of between 6 weeks and 12 months with a 9-month default period. The average loan is estimated to be c$1,150 (2022). These loans can be transacted in-store or online.

Bigger store format – note loans is split from retail

2. MACC (Medium amount credit contracts) are larger loans and vary from between 4 to 24 months and range from $2,000 - $5,000 with a default term of 12 months. The average loan amount is c $3,500 (2019). These loans can be transacted in-store or online.

These two unsecured credit formats are of interest to regulators – to ensure that borrowers don't borrow more than they can afford. The main laws regulating the industry include *the National Consumer Protection Act 2009* namely the responsible lending laws.

Hybrid – combines both but is split. Typically customers borrowing don't buy in the shop after the loan is made

Traditional pawn broking loans – if not paid back, expire, the goods are sold and the debt is closed out. No more to pay. Failure to pay back a pawnbroking loan – however then becomes a relevant fact in the decision to extend a new one /or provide other unsecured forms of credit. CCV can benefit from having an extensive database that informs these lending decisions across the network. Independent pawn brokers obviously can't easily share information between themselves and this puts them at a big disadvantage to CCV. The average pawn broking loan is now $190 (vs $160 pre-COVID,

CCV is using technology such as sourcing electronic bank statement data for over 5 years and has been using the new electronic payments platform for disbursements.

Vehicle Financing – Green Light Auto provides vehicle financing that is primarily distributed through broker networks/car dealerships, the other major distribution is via Green Light Auto

website. CCV stores and online. Secured loans vary from $5,000-$45,000 for a term of up to 5 years. The average loan was C$17k and had a term of 38 months.

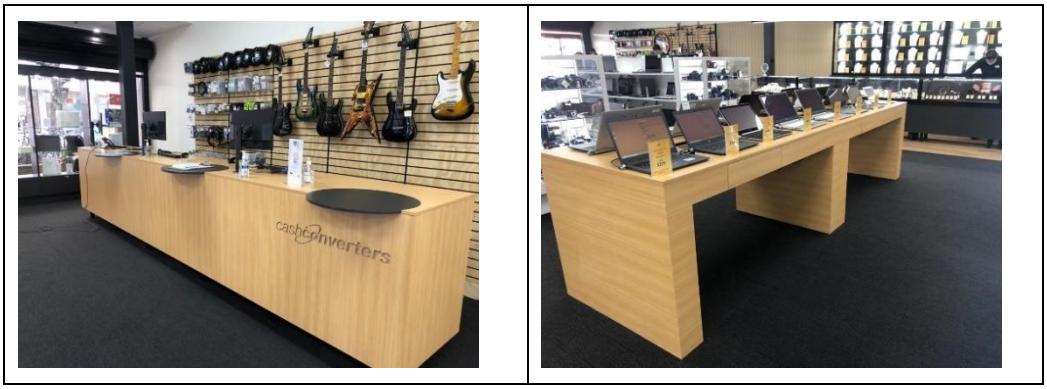
Picture 1 – CCV stores

Source:CCV

Picture 1 - building exterior is the Browns Plains (QLD) store, which is franchise owned.

The interior shot of the chairs (picture 1) is an example of a 'Hybrid' shop which is basically a mix between a large and small format location.

Picture 2 - CCV updated tech and retail counter



Source – CCV

Competitive advantage – compelling /extensive

CCV's competitive advantage and market position

We believe that CCV has a **series of solid competitive advantages**, including

- ✓ Established relationships. Customers know the stores, what they have in them, where they are and might even know the staff.
- ✓ CCV have live (and historic) statistics on the various customers' propensity (or not) to repay loans.
- ✓ Past pawn broking loan applications (account opened) make it **FAR** easier for customers to establish a repeat loan rather than having to completely reapply. For unsecured loans being an existing customer does not speed up the processing time – but does provide information to CCV to help make a more accurate decision.
- ✓ Pawn broking and second-hand goods licensing is strict and can take time with diligent police checks a feature. Licensing to lend unsecured money would also be strict.
- ✓ The brand is well known. *A quality bottle of red wine is available for the first reader (PAC client) that nominates which AFL side they sponsor. Email me. First correct answer wins.*
- ✓ Advantage of a network. Goods can be moved to the right market - the Mt Isa surfboard can be moved to the Gold Coast shop.
- ✓ Data – huge access to the value goods via its own second-hand network. This means that as goods are pledged – the right loan amount can be ascribed to them – because they have recently sold such an item. The other tangible value of the database in personal finance, allowing CCV to use machine learning to supplement manual assessment. The database also allows Cash Converters to observe credit performance, which in turn allows new products to be identified and policy fine-tuning opportunities.
- ✓ Data sharing across the network can prevent dealing with customers with poor credit history who shop around to evade controls. A simple adverse note in the company database can prevent further mistakes.
- ✓ Data sharing also enables businesses to have unilateral policies to avoid goods that might be problematic. An example might be an electric scooter than has a product recall.
- ✓ A larger network with specialised expertise can enable fast and skilful repair of damaged /broken goods.
- ✓ A Corporate entity can fractionalise the cost of managing regulations and licensing and other obligations (across a major store base).
- ✓ CCV also benefit from a diversity of geographies, loan types and format. This offers risk reduction and is appealing to securitisation funders. A particular market can be in decline and offset by another. A particular area (tourism can be up and another down (mining).
- ✓ A corporate website that can quickly and efficiently check/photograph/put online goods that can't readily be sold by a store or are highly specialised. Smaller operators lack the investment/skill and expertise to do this in a disciplined and cost-effective way.
- ✓ Stores that are able to attract specialised staff can develop product knowledge and expertise (such as an expert jeweller). Stores with a few staff are more secure, happier places, where ideas and decisions can be shared/checked – compared to smaller independent players.
- ✓ Increasingly complex compliance and systems required to deal with this compliance can be developed and the cost amortised across a wide store base. Errors and problems can be more readily fixed.
- ✓ Increasingly CCV have access to well-priced capital compared to smaller fintech players and independent pawn brokers.
- ✓ Lending and pawn broking, in general, has large start-up costs such as lending the money, rent/lease, and stocking the store. Start-up pawnbrokers/lenders generally make poor initial credit decisions without the benefit of prior history. New stores in order to build volume lend more per item than others or make less vigorous loan decisions and this generally is expensive. CCV doesn't face this problem.

Already having an account is a big time saving.

It is quicker because the lender has already been ID – saving time, CCV have your history and you can be in/out quickly if you are a repeat customer

ID'ing customers takes time and has to be carefully done.

News goods offered as pawn loans also have to be carefully checked /identified vs the same item being re-pawned – where I can be done a bit faster

At least the majority / perhaps 80% plus of pawn broking customers are regulars. Often pawing the same items habitually

Items sold or pawned get identified and the serial numbers and detailed upload to police crime system - every night

It is a highly regulated business

CCV works closely with the police, all purchased items are uploaded into a police database every night.

Everyone is ID'ed

Items are then held for a holding period prior to sale. It is a highly regulated industry.

DRIVER ONE - REDUCED LEGAL UNCERTAINTY

In the past - CCV has been subject to a complex series of legal cases, ASIC investigations and legal settlements over past business practices. The various legal disputes have been costly in terms of settlements, ongoing legal costs and management time and effort. It has been hard to develop/reinvest in growing the business when the legal framework changes.

Table 3 – CCV's past legal disputes

Settled many of the legal disputes/regulatory issues

Gray vs Gray – class action – Personal Loans	Settlement 2015	$23m (without admitting fault)
McKenzie vs Cash Converters International – class action – fees/interest charged	Settlement 2016	$16.4m (without admitting fault)
Lynch vs Cash Converters Personal Finance – brokerage fees	Settlement 2020	$42.5m (without admitting fault)
Enforceable undertaking ASIC – small loan contracts – new processes put in place	Nov 2016-Feb 2017	$12m including refunds
	Total cost	**$93.9m plus legal costs**

Source – CCV and PAC Partners

Notable legislative changes include the introduction of the *National Consumer Credit Protection Act 2009*. This replaces a series of complex state-based credit codes and the uniform codes apply to all Australian credit license holders. CCV is supportive of this reform. This change helped establish responsible lending obligations, licensing of all lenders and brokers and mandatory membership of AFCA (Complaints Authority).

We are unaware of further class actions or ASIC activity, however, as mentioned in this report, the AUSTRAC inquiry is ongoing and there are possible changes to protected earnings earning amounts and related small amount credit contract legislation. This should enable the business to reduce legal costs and settlements and focus on a better more sustainable business.

Current outstanding legal/regulatory actions include an **AUSTRAC notice dated August 2020** – asking for records spanning up to 6 years to 2020. CCV is cooperating and is continuing to strengthen its anti-money laundering and counter-terrorism processes and programs. The outcome is unknown and the investigation is not completed.

The other **outstanding regulatory issue is the small account credit contracts** protected earning amount (PEA) review (Small amount credit contracts)[2]. **This has been in discussion since 2016 but has now been passed by the lower house and is in the Senate for a second reading. It is likely to pass through the Senate (the last sitting days are early December before long Christmas break) and we estimate implementation – starting in July 2023**. Once the Bill passed the Senate – the Bill has to receive royal ascent by the Governor General and then it becomes law.

The impact of the proposed extension would extend the mooted regulations to **All borrowing customers and cap payments from 20% of the customers' gross income to 10% (of net income).** The New minister for Financial Services is Mr Stephen Jones and he is the Minister responsible for the change.

We believe the that regulatory focus of the new federal government might now move to review and regulate the BNPL market – with greater regulation levelling the playing field between credit providers and other BNPL providers. This is likely a positive for CCV. Some customers are taking on too many of these BNPL arrangements (across providers) without their welfare or ability to pay back – being in totality – assessed.

[2] *https://treasury.gov.au/sites/default/files/2019-03/c2017-t229374-Explanotory-Memorandum-1.pdf*

DRIVER TWO – STORE ACQUISITION

We estimate the 9 stores bought in a 24 month period

Might add about 5% to EPS in terms of a run-rate.

CCV can acquire franchisee stores from its network and convert these into corporate stores. In the last financial year – CCV bought 6 Australian franchised stores including Morley (WA), Melbourne City, Blacktown (Western Sydney), Richmond (Western Sydney), Coconut Grove (NT) and Palmerston (NT). Currently, CCV corporately owns 79 stores in Australia and has approx. 76 stores under franchisee arrangements. This gives a natural deal flow of stores that CCV can look to acquire within Australia that might make a natural fit into the current network.

In FY21, CCV paid a total of $6.7m for these stores which added proforma $6m in revenue and NPAT of $744k. This equates to about 9X the earnings of each store in FY21. Given the purchases stores have second-hand goods and loans on their books –there is solid book value behind them. The goodwill is quite low at 34% of the cost – with hard NTA supportive of accretive acquisition multiples. CCV would also have a reasonable understanding of the stores having provided them with systems, software and capital over the years.

CCV bought a further 3 franchisee stores in 1H22 including Corio, Dandenong and Geelong (all Victoria) paying $3.1, with about $1.176m in goodwill. These three stores contributed revenue of $2.6m and were just above break-even. in terms of profit.

Table 4 – CCV past acquisition regime and likely earnings uplift

Franchisee buyback model		
Item $m	**FY22 proforma**	**6 more FY23**
Revenue	5.98	6.0
NPAT	0.7	0.7
NPAT FY22		11.2
NPAT FY22 plus new stores		12.0
Theoretical uplift		6.6%
Price paid $m	6.7	6.7
Earnings multiple X	9.0	9.0
Stores	6	6
NPAT per store $m	0.124	0.124

Source – PAC source SsSource :PAC Partner analysis

CCV has a sizable offshore franchise network with 548 stores and while not material provides medium to longer-term future offshore optionality.

In the short to medium term – the focus will be selectively buying franchisee stores (76 in total) in Australia.

We believe the CCV corporate desire to acquire these overseas licensed stores is not nearly as great as buying further Australian stores - apart from perhaps some stores that can be acquired and improved in the UK market.

We estimate that for the 6 stores recently in FY21 – CCV could add ~5% to EPS in the first full 12 months of ownership. CCV enters FY23 with the uplift of six bought in 2021 match fit and feeding into FY23 full year plus three stores (Dec – 2022) feeding into the profitability of the overall business into FY23.

DRIVER THREE – COVID19 ENDS – LOAN BOOKS REPLENISHED

CCV was hit hard by the COVID19 lockdowns. The first National lockdown was for about 6 weeks in March 23-May 11 – 2020 (2H20) and as we all know kept going. The major impact was in FY21 and 1HFY22 with significant times and conditions attached to the lockdown and this prevented CCV from trading in some major markets.

Table 5 – Major lockdowns in Australia

FY20		FY21	
Victoria		**Victoria**	
Starts	07 Jul 2020	Starts	15 Jul 2021
End	26 Oct 2020	End	27 Jul 2021
Starts	12 Feb 2021	Starts	05 Aug 2021
End	18 Feb 2021	End	21 Oct 2021
Starts	27 May 2021	**NSW**	
End	11 Jun 2021	Starts	23 Mar 2021
		End	02 Jun 2021
		Starts	25 Jun 2021
		End	11 Oct 2021

Source: PAC Partners analysis /Health departments

The Lockdown had an impact on CCV with borrowers wisely taking government stimulus money and paying down their debts. This reduced future income for CCV. The lockdown will have also reduced the ability of shoppers to buy second-hand goods from stores that were essentially shut. The lockdown did help increase website activity. Reduced economic activity also reduced the demand and need to borrow for the various needs the borrowers might have. Increased government payments will have also reduced some borrower's need to access credit.

Table 6 – Major lockdowns trading days lost for CCV

CCV impact	FY21
Australian store trading days	23,336
Lost to lockdown Australia wide	2,374
% of total	10%
Victoria's normal trading days	6,312
Victoria days lost	2,083
% Victoria days lost	33%
1H22	
Days lost	25%
1Q22 - annualised	13%

Source – CCV Annual report and 1HFY22

DRIVER FOUR – DEBT FUNDING LINES – SORTED OUT

CCV like all financial services businesses of scale needs access to reliable, well-priced debt to fund its loan books. Traditionally Australian banks such as Westpac have provided this access/debt.

In August 2015 Westpac decided to exit the short-term credit contracts market. Westpac did provide CCV with a long lead time. The Westpac facility was able to be replaced by the Fortress facility. This facility was first established in 2016 for 5 years.

CCV also need reliable access to payment processing, and this has also been sorted out with Westpac successfully replaced. This Fortress loan securitisation facility was renewed in June 2022 for four years with a $150m capacity with improved advance rates and refinancing on a "competitive" term.

This is a vital renewal and provides certainty for CCV – as its loan books regrow post-COVID1919 and growth initiatives gain traction.

At the 30th June 2022 balance date - $70.2m of the $150m Fortress securitization facility had been drawn down by CCV – leaving $79mm unused (plenty of capacity). Recent loan growth will result in this being further drawn in into FY23.

Who is Fortress Investment Group?

Fortress Investment Group is a diversified global investment manager with approximately US $53.0 billion of assets under management as of March 31, 2022. Founded in 1998, Fortress manages assets on behalf of over 1,900 institutional clients and private investors worldwide across a range of credit and real estate, private equity and permanent capital investment strategies. Fortress was acquired by Softbank (9984.JP) in 2017 – but operates independently by the incumbent management team post the acquisition of the business. PAC would characterise Fortress as seasoned and tough operators and an ideal partner for CCV to use.

Fortress has approximately 872 employees and 203 investment professionals as of March 31, 2022, and is headquarters in New York and has offices around the globe:-

Fortress businesses, across its private equity funds and credit funds, specialize in asset-based investing and bring to bear significant experience in investing broadly and deeply in a diverse set of asset types. Fortress's expertise extends to pricing, owning, financing and overseeing the management of physical and financial assets ranging from real estate and capital assets to financial assets secured by diversified long-term cash flows.

Figure 2 – Fortress Investment product set in USD$bn.

Business Segments	Credit Private Equity	Credit Hedge Funds[1]	Private Equity & Permanent Capital Vehicles[2]
Assets Under Management ($ in bn)	$33.3	$7.7	$3.4
Strategy	Distressed and undervalued assets (some with limited current cash flows and long investment horizons) and tangible & intangible assets (real estate, capital assets, natural resources and intellectual property) Long-term investments in established or emerging category-leading businesses, partnering with management teams to unlock potential for growth and value creation.	Opportunistic lending situations & distressed assets (loans, assets and corporate securities)	Publicly traded companies that invest in a wide variety of real estate related assets, transportation & infrastructure and media related assets. General buyout and sector-specific funds focused on control-oriented investments in cash-flow generating assets and asset-based businesses in North America, the Caribbean and Western Europe

Source :Fortress website

DRIVER FIVE – BAD DEBT MANAGEMENT/CONTROL

CCV has been subject to a series of legal settlements and regulatory changes over the last several years.

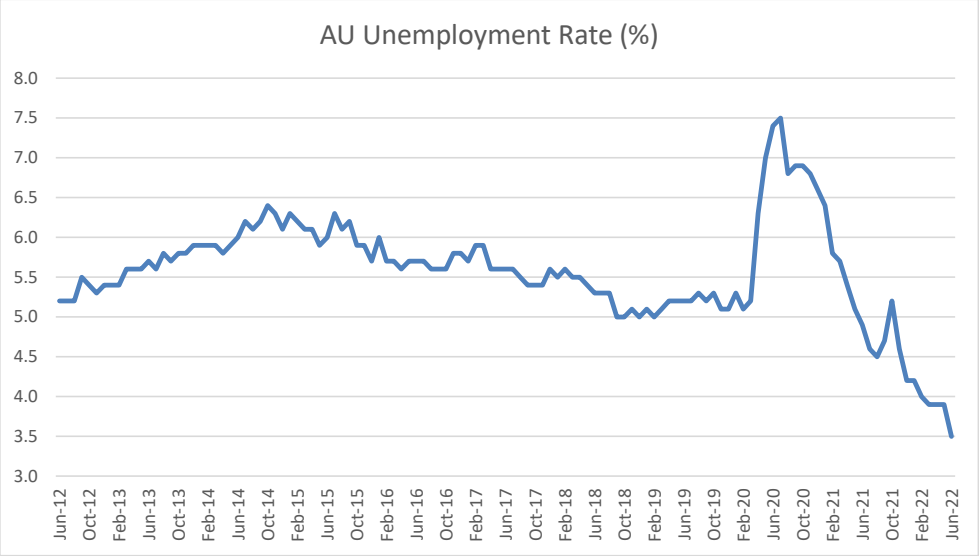
As part of this process – the business has moved to alter and tighten lending criteria, process and product features. This has had the impact of lowering the level of bad debts. In essence – capping of interest rates has meant that some lenders cannot afford to economically provide very high risk/high return small loans to very risky clients for very small unsecured loans. CCV can afford to lend to high-risk, high-return customers and are arguably best placed to continue to do so even if the PEA regulations come in.

CCV has also redesigned existing products and improved its application processes, products limit and features, the application process has been improved to source the direct bank statements of each individual client – reducing the scope for error. CCV has also redesigned the website (including suspending online cash advances in 2016 and redesigning and resuming this form of lending in 2018). Product mix and design have also been improved. CCV have some learnings that have been applied to reduce losses and improve the quality of decisions. The mix towards higher value longer-term loans has reduced the amount of lower value/higher risk loans.

Pawn broking loans are different to unsecured loans in that if the loan is not paid off – the loan liquidates and is paid via the second-hand goods sale – preventing any form of a debt trap from developing.

CCV has noted that unemployment is a key driver of bad debts. Despite some signs of slower economic growth – unemployment remains very low in Australia and lower unemployment augurs well for CCV's future bad debt profile.

Figure 3 – Australian unemployment



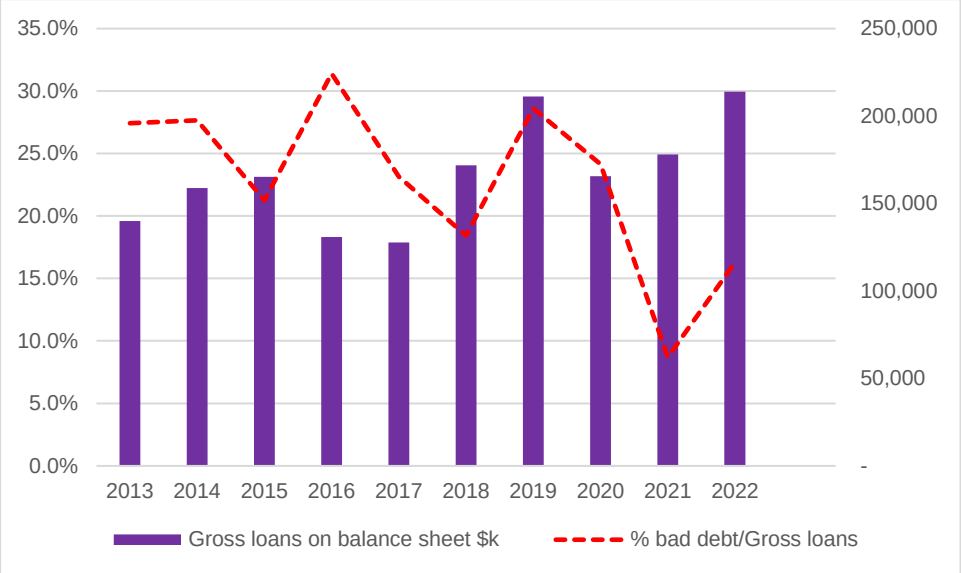
Source : ABS

We have depicted CCV bad debt experience over the last 8 years, it has improved due to lower unemployment and a conscious reduction in higher risk/higher return unsecured lending due to regulatory change. The recent pandemic also saw lenders deliberately and rationally pay down debt which also helped.

CCV had also provided an additional provision for rising unemployment (COVID19) – this is now looking like a conservative approach given unemployment is at the moment very much under control. COVID19 also saw credit standards tightened which is also looking like a prudent approach.

Bad debts have again increased as COVID19 normalised but remain well under control.

Figure 4 – CCV's bad debts

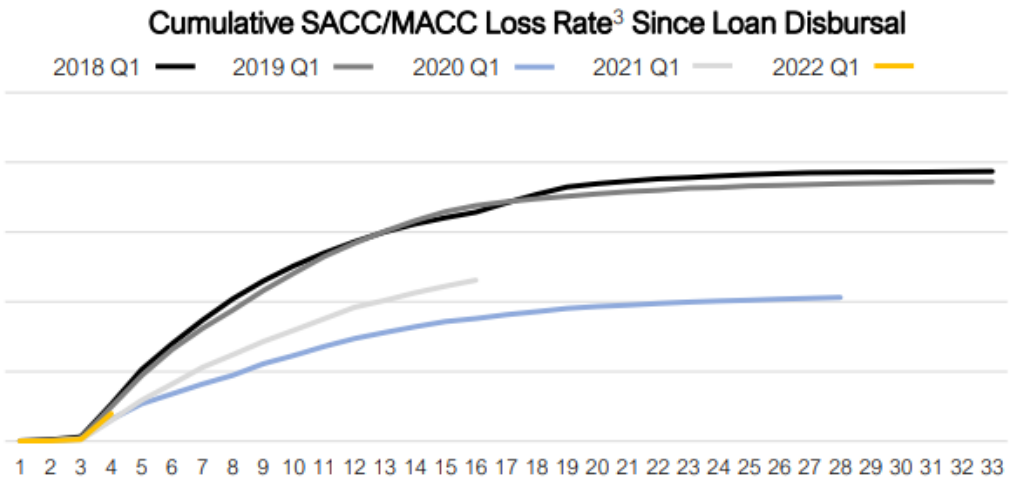


Source: CCV and PAC analysis.

The gross loan book has also altered with medium-sized loans outgrowing small loan contracts over the last few years. CCV also have put a lot of time and effort into systems, processes and software after recent regulatory changes and past legal action.

Importantly bad debt collection was in-sourced in 2H2021 and should lead to higher collection rates, better control and avoiding the problems within some parts of the collection industry such as the collection agents themselves facing financial difficulty. The original decision was made to outsource collections after the ASIC EU (circa 2016) required substantial resources to sort out.

Figure 5 – improved loss rates/ but not as low – as the artificial impact of COVID1919



1. Loss rate based on principal written off as a % of principal advanced (outgoings).

Source : CCV 1H22 presentation

SACC = Small Amount credit contract, MACC = Medium Amount credit card

Brand recall is high, most Australian adults has an idea of what the brand might mean

What's is it worth (WiWo) campaign helped drive sales/traffic

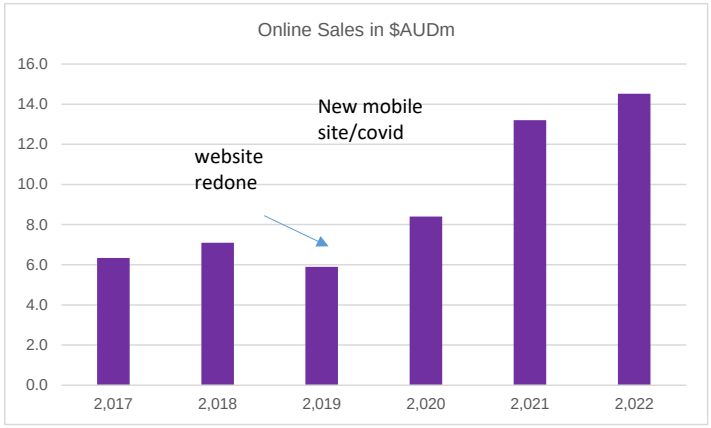
Originating / Controlling the loan via a mobile app is critical, smaller operators wont be able to compete

DRIVER SIX – ONLINE OPTIMISATION AND OTHER BUSINESS DEVELOPMENT ACTIVITIES

Over many years CCV has been developing its website shop (known as WebShop to quickly and effectively sell second-hand goods that have not been redeemed. The website provides a chance to sell goods at a faster rate and at a higher value as the natural demand may not be within the local area where the goods were taken in as collateral. A surfboard might not appeal to someone in country NSW but be very interesting to someone in the Northern Beaches of Sydney. The internet provides the ability to sell the goods to the person that really wants it and has the money for it – anywhere in Australia. Other examples include collectors. There is for example a cohort of collectors of old cameras and jewellery that may not live near the local pawn broker, have little need to attend the shop but are very interested in some of the goods on offer, but may not be aware that they are for sale.

The website was upgraded and remodelled to be more usable on mobile in October 2018. COVID1919 will have also helped drive demand for the website. The website has a massive scale with over 29.3m website views in FY21, 84k transactions, 393k applications and 75k in loans. CCV sold (as a group) over 1.4m items in FY22.

Figure 6 – increased online sales in $m

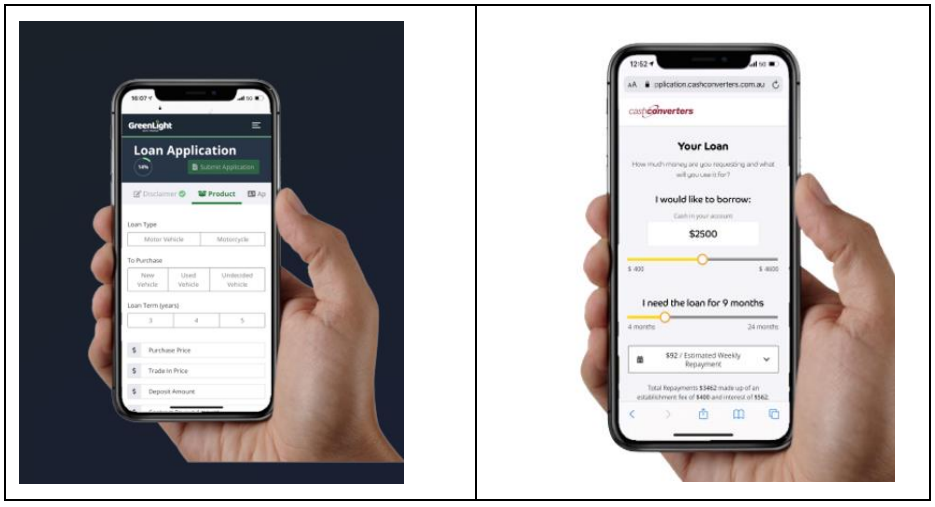


Source – PAC analysis and CCV

We also note that an improved website selling second-hand goods also has value in terms of driving online loan demand and enquiry levels more generally. CCV can offer a much better website for both sales of goods and for lending compared to smaller operators. The breadth of goods on offer and suite of loan products is a clear competitive advantage and provides operating leverage to the business and the franchisees within the network.

The website also provides a steady stream of loan enquires and business. The site has scale. A google search of pawn broking returns CCV as the first entry and Cash Converters notes that over 60% of lending is transacted online.

Picture 3 – online /mobile applications



Source – CCV

Risks (include but not limited to)

Changes in regulation and government legislation of the sub-prime lending industry. The federal government has engaged a series of reforms to prevent the industry from lending in a predatory fashion. Lending terms have to be clear, upfront, disclosed and clearly suitable and serviceable for the individual borrowers' needs. In particular debt spirals/traps are to be avoided when lending. Saying no in a respectful way is a key skill.

AUSTRAC investigation. This investigation is not completed. Notices have been issued from AUSTRAC for the period 14 February 2014 to October 2021. CCV has worked hard to strengthen Anti-money laundering and counter terrorist financing procedures and processes. CCV has undertaken independent review into these issues and implemented strengthened practices.

Falling gold price. In AUD$ terms. A much lower gold price reduces the ability to lend and reduces consumers' propensity to scrap and/or buy more jewellery. CCV are a major scrap player – if the jewellery does not sell it (ugly/broken/out of date) can be scrapped. We estimate that perhaps $500k $1m per month is sold as scrap.

Bad debts / estimated correctly. The loan book is adequately provisioned for loans are priced properly and approved for appropriate suitable borrowers. Loans must be serviced adequately, and paperwork correctly processed.

Rising levels of bad loans/debts.

Inappropriate valuation of goods. This issue relates the systemic problems such as constantly overvaluing a new product or system weaknesses that enable fraud or even present risks.

Fintech competition.

Major changes to how currency notes are used within the economy. A ban/restriction on the use of currency notes may for example be highly disruptive. Changes to welfare payments to restrict certain categories of spending might also prove disruptive.

Franchise dissatisfaction/ revolt.

Loss of new /material legal/class action cases.

Product deflation. Tools for example have been deflated in value and have become harder to lend against. This also devalues goods pledged as collateral.

Poor acquisitions. This is somewhat mitigated by having an established franchisee business to source new deals from.

Redemption rate not deteriorating-i.e.- clients can pay back loans quickly then don't redraw.

Re-engagement of high-street banks into the micro-credit markets- Unlikely in the short-medium term.

Internet disintermediation impacting the store network- however as described earlier the internet also helps to price, dispose and drive consumer cycles.

Severe economic recession/job losses,

Timely and well-priced access to debt to fund the business.

Renewed adverse publicity.

Excessive inventory – carrying too much inventory can consume cash and is costly to manage, store, and maintain and can be deflated in value. The pandemic may have actually helped here – with loans pay down and goods redeemed, increased online activity and a focus on aged inventory in early period. We believe that clean inventory is a benefit. We note the decline in the gold price may hurt efforts to scrap unsold gold jewellery.

PROTECTED EARNINGS AMOUNT (PEA) /NATIONAL CONSUMER CREDIT PROTECTION AMENDMENT – DEMAND REMAINS AN WILL NEED TO BE MET

The new feral government under Assistant Treasurer (Minister for Financial services Mr Stephen Jones has re-introduced this bill and it is now up to the second reading by the senate and is now highly likely to be passed and become new legislation.

In particular a proposed amendment to the *National Consumer Credit Protection Amendment (2020)* – the Bill will impact CCV (and others.

This bill would seek to introduce further (and extensive) interest rate /charge caps for Small Loan amount contracts (SACC). **The major changes would include limiting repayments from 20% of gross income to 10% of consumer net income. This will limit access to this sort of credit.**

CCV note that such a change would impact the business with reduced consumer demand (ability to qualify) for smaller loans. The cost would rise and availability of this form of loan will fall.

We have modelled the likely outcome based on past CCV annual report modelling on the possible outcome of such as change.

Table 7 – Possible impact of protected earnings changes on CCV year +1 - assuming nothing is done to mitigate the impact.

Current loan book FY22 $m	Amount	%	What if change $m	Amount
Small loans/SACC	75.6	35%	Small loans/SACC	75.6
Medium Amount credit contract	76.1	36%	50% reduction SACC	37.8
Pawnbroking loans	15.5	7%	Medium Amount credit contract	76.1
Green Light Auto	46.7	22%	No change Medium Loans	76.1
Total loans	213.9	100%	Pawnbroking loans	15.5
			Green Light Auto	46.7
			Total loans	**176.1**
			Loans book reduction	37.8
FY22 Yield (Per. EBITDA/ SACC Loans)	57%		Yield - assumes 50%	50%
			Lost EBITDA	18.9

Source – PAC estimates.

We have assumed a 50% reduction in small amounts credit contracts (SACC) post the change IF CCV did nothing to react after Y+1.

We then use an "average yield" on the lost loan book of 57%. Medium loan contracts will not be impacted by the proposed change.

There are some offsets such as a reduced cost base, reduced funding costs and the ability of the business and consumers to adapt and adjust to the change. More conservative credit assessment in recent years for small loans (and mix changes) also provides mitigation. Finally, any changes may be subject to a degree of grandfathering that helps to reduce the immediate impact and allows the industry/borrowers/regulators to adjust to any changes. New products and some movement of some customers to medium credit contracts (as circumstances dictate) and even renewed growth in pawn broking will act as offsets.

CCV also note that with this proposed change – the cost of these loans will rise and the might be some material industry consolidation as others look to exit /sell as a result of these changes. CCV is well positioned to participate in the consolidation.

Table 8 - EBITDA mitigation – FY24

FY23 EBITDA	59.7
Lost EBITDA - PEA	-18.9
FY24 EBITDA re-based	40.8
FY24 EBITDA	40.8
Add back	
NZ - Acq of 75%	**4.0**
Some SAC /MAC -15% convert	**5.7**
New products - 15% convert	**5.7**
Some growth -5%	**2.4**
FY24 base EBITDA	**58.6**

Source: PAC estimates.

Investors need to be aware of this legislative change.

We also note that after a major change in the last 10 years and substantial legal action and reduced capital access – the industry collectively is better regulated and more sustainably run and this should assist in reducing regulatory involvement including the proposed amendment.

It is hard to assess the probability of the change with a new federal government, a new parliamentary composition and ministerial (and staff) changes.

We are seeking to be conservative and assign a 30% probability of change – hence we will place a 10% discount on the valuation of the business. We believe that this risk is priced in but if it moves to 100% - it is not and a 30% decline in earnings is possible.

COMPS

CCV has a series of sub-prime and no traditional lenders that it competes with and are comparable within Australia. We believe that a low double-digit P/E is appropriate and comparable to other similar businesses.

We would split the cohort into more traditional non-bank lenders that are generally profitable, focus on providing credit, require capital to lend and are generally profitable and focus on predictable bad debt outcomes that capture the risk vs the reward of the loan and comply with traditional regulation.

The second group are fintech lenders that generally are more focussed on the less regulated BNPL segment, are loss making and generally need capital to lend /grow and are not self-sufficient in this regard.

There are also offshore businesses including CCV offshore major shareholder Ezcorp. A major listed UK player Abermale and Bond went bankrupt in the UK (September 2019) and is no longer in business. Abermale and Bond had 116 shops. Other that have failed in the UK include Money Shop. There are also some other US players that have had mixed fortunes in the last 10 years. The successfully UK business is H and T.

Table 9 - CCV comps

Cash Converters peer Comps											
	Share	Mkt	FY22 Net	Div (x)		PER (x)		EV/Rev	Price/book	EPS Growth %	
Company	Price A$	Cap $m	Debt A$m	FY22A	FY23F	FY22A	FY23F	FY22	FY22	FY22A	FY23F
Money lending											
Money3 Corporation Limited	2.02	425	207	6.1%	6.8%	8.3	7.9	2.9	1.2	33.4%	5.8%
Prospa Group Limited	0.69	112	286	0.0%	0.0%	16.4	17.3	1.7	0.8		(4.8%)
FSA Group Limited	1.08	132	396	0.0%	0.0%				1.4		n/m
Harmoney Corp Limited	0.61	62	201	0.0%	0.0%			2.3	1.1		
Judo Capital Holdings Limited	1.25	1,371	3,206	0.0%	0.0%			13.7	1.0		
MoneyMe Limited	0.38	107	275	0.0%	1.6%			1.7	1.2		
Latitude Group Holdings Limited	1.29	1,341	5,340	12.2%	9.2%	8.9	7.3	7.6	0.9	(8.9%)	22.3%
Humm Group Limited	0.49	240	2,225	3.8%	4.5%	8.1	19.4	4.9	0.4		
Average				**2.8%**	**2.8%**	**10.4**	**13.0**	**5.0**	**1.0**	**12.2%**	**7.8%**
Median				**0.0%**	**0.8%**	**8.6**	**12.6**	**2.9**	**1.0**	**12.2%**	**5.8%**
Cash Converters (FY22)	**0.24**	**151**	**107.6**		**8.3%**		**10.6**	0.9	0.5		**16.5%**
Internationals (USD)											
EZCORP, Inc.	9.44	535	224	0.0%	0.0%	13.9	12.3	0.8	0.8		13.2%
FirstCash Holdings, Inc	95.35	4,416	1,467	1.3%	1.4%	18.7	15.3	2.0	2.4		22.1%
H&T Group plc	4.59	201	1.3	3.3%	5.0%	12.6	7.9	1.0	1.4		59.5%

Source – PAC Partners and Capital IQ

EZCorp (EZPW.US) – 43% shareholder CCV / market cap US$506m

Formed in 1989, EZCORP is a leading provider of pawn loans in the United States and Latin America. Ezcorp has about 1,149 stores and in terms of the network – at least twice CCV's size. EZCORP also sell merchandise, primarily collateral forfeited from pawn lending operations and used merchandise purchased from customers. EZCORP has focused on the short-term cash needs of consumers who are both cash and credit constrained, focusing on an industry-leading customer experience. Ezcorp has been buying more shares in CCV in recent times. EZcorp's share price is also been on the rise in recent times.

FSA Group (FSA.ASX) -$130m market cap

FSA is Sydney Headquartered. FSA offers home loans, personal loans and asset finance and specialised financial services (payment arrangement with creditors). The business is profitable, pays and a fully franked dividend.

H and T (HAT.GB) -www.handt.co.uk – UK-based sub-prime /pawn broker

H&T Group Plc engages in the business of pawn broking, gold purchasing, retail of jewellery, cheque cashing, unsecured lending and other related services. It operates through the following segments: Pawnbroking, Gold Purchasing, Retail, Pawnbroking Scrap, Personal Loans, and Other Services. The largest UK (and listed) pawnbroker – H and T is also reporting strong trading (May 2022) due to adverse UK economic conditions with recent media reports suggesting quote:-

Trading performance has been very strong in 2022.

Demand for pledge lending remains strong and at record levels, with positive momentum across the customer spectrum and in all geographies. H&T continues to see customers returning, in many cases after a long absence, as well as increasing numbers of pawnbroking customers who are new to H&T, the company said in a trading update.

Media and analysts noted that higher inflation and cost of living pressures in the UK are also generating increased demand. While economic conditions differ to Australia CCV has some stores in the UK (under license) and some of the economic challenges are similar between markets. H and T and CCV would also benefit from reduced competition after Abermale and Bond's demise. Some selected quotes from the recent result (9th August 2022).

Further H and T commentary – quote:-

FOR THE SIX MONTHS ENDED 30 June 2022

H&T Group plc (AIM:HAT), the UK's largest pawnbroker and a leading retailer of high quality new and pre-owned jewellery and watches, today announces its interim results for the six months ended 30 June 2022 ("the period").

Highlights

- Profit before tax of £6.7m (H1'2021: £4.7m) as the continued momentum in our core pawnbroking business underpinned a strong performance.
- The pledge book grew 27% to £85.1m (December 2021: £66.9m) with demand for pledge lending remaining at record levels. Daily average lending volumes are more than 40% above pre-pandemic norms.

Very positive and likely CCV is also enjoying better trading conditions in the UK. H and T also note that demand for credit is strong, supply of credit is very constrained.

Chris Gillespie, H&T chief executive, said:

"This year is the 125th anniversary of the founding of H&T. We have a proud history and the growth we have seen in the first half of this year has been very encouraging. We experienced increasing momentum across our product set, customer base, and geographical locations. This has continued into the second half.

Financial forecasts and valuation

SALES FORECASTS

CCV earn revenue from interest and fees when they lend to customers, from selling second-hand goods bought from customers and from second-hand goods that they sell if a loan is not paid back (redeemed). There is also revenue from the franchisee royalties and fees for services and funding provided to franchisee stores.

The gross loan book has risen 20% to $213.9m in FY22 and this sets up FY23.

The business also benefits from recently acquired stores feeding into FY23 revenue growth and improved demand now that COVID19 lockdowns have ended.

Table 10 – Revenue/interest/fees forecasts

Cash Converters CCV AU Equity	1H22 Actual	2H22 Actual	Jun 22 Actual	Jun 23 Forecast
Segment revenues				hold mix steady
Personal Finance Int	41.3	62.8	104.1	
Store operations Int	15.0	27.9	42.9	
Goods sales	39.5	41.2	80.7	
All revenue x auto	95.8	131.9	227.7	267.5
Vehicle Finance Int	5.9	6.2	12.1	13.3
Franchisee opers. Fees	8.3	8.6	16.9	17.0
Other	5.2	-16.1	-10.9	
Head office				
Total	**115.2**	**130.6**	**245.8**	**297.9**
% change	22.7%	21.8%	22.2%	21.2%
Revenue /Loans x auto	65%	79%	136%	136%

Source – PAC Partners

Drivers of future sales include:-

- Improved website.
- New products/features.
- Recently acquired stores.
- Greenfield expansion in Australia
- Smaller high-end stores with a focus on jewellery/high-end luxury goods to maximise retail space.
- greater focus on new goods retailing.
- COVID19 – normalising.
- Increased demand for credit due to cost of living pressures and at the same time less supply.

We also expect that lower value, bulky household items such as garden equipment, power tools, low-end bikes, golf clubs, and sporting equipment will be down-weighted. These items might be better sold from a central location/over the internet or not taken in at all.

Table 11 – loan book forecasts

Cash Converters	1H22 Actual	2H22 Actual	Jun 22 Actual	Jun 23 Forecast
Gross Loan book		as at	actual	
Small loans	69.0	75.8	75.6	
Medium loans	65.1	76.1	76.1	
Corporate pawn broking	14.4	15.5	15.5	
All loans X auto	148.5	167.4	167.2	196.5
Green light / Auto	43.4	46.6	46.7	51.4
Gross loan book	191.9	214.0	213.9	247.8
Average loan book	185.0	196.05	196.0	230.9
Average loan book growth			14%	18%

Source – PAC Partners

EBITDA MARGINS

CCV reports EBITDA by segments. The lending segment includes interest and loan fees. The sale of second-hand goods that are not redeemed (which is also profitable) and linked to pawnbroking loan volumes is reported in-store operations. Vehicle finance relates to Green Light Auto loans and Franichsee fees are the royalties/ funding supplied from Franchisees and the sale of some service to the franchisee network. During the pandemic, some fee relief was provided and we expect that this segment should bounce back.

Table 12 – CCV EBITDA forecasts

Cash Converters CCV AU Equity	1H22 Actual	2H22 Actual	Jun 22 Actual	Jun 23 F'cast
Personal Finance Int	19.9	24.2	44.1	
Store operations Int	7.6	8.8	16.4	
Operational EBITDA	27.5	33.0	60.5	69.6
Vehicle Finance Int	3.7	4.2	7.9	8.3
Franchisee Fees	5.9	5.8	11.7	11.9
Other				
Head office/legals	-12.6	-14.9	-27.5	-30.0
Total	24.5	28.1	52.6	59.7

Source – PAC forecasts

BAD DEBTS

In FY23, bad debt expense was about 16% of gross loans. Given the loan growth we expect bad debts as % of loans to remain steady but that the absolute level of bad debts to grow as the loan book increases. We also note an increased amount put aside for credit loss for FY22. We believe management has taken a conservative view for loss provisioning into FY23.

CCV has also reduced the amount of risk that they are prepared to lend against after a change in regulation rendered small low value high-risk loans uneconomic. The pandemic has also seen thloanon book shrink, credit standards tightened and enables some fine-tuning of credit algorithms. CCV loan mix has also changed with Auto loans and medium value loans growing as an increasing percentage. CCV has also bought loan collection in-house during 1H21 and this should also help to control bad debts and improve collection into the future. CCV has also to be careful with respect to Auto loans given the inflated (COVID19) price of some second hand vechiles.

FUNDING

The business has access to the Fortress securtisation facility which has recently been renewed on better terms. This combined with cash reserves should provide sufficient funding for the business. We have factored in some rising interest rates costs into our financial forecasts.

CCV has some exposure to rising interest rates in terms of its funding costs. If we assume net $80m outstanding (on average during the year) each 1% increase in interest rates detracts $800k pretax ($80m*1%). We would note this is currently not the case with substantial undrawn debt.

We postulate that with bigger, more diverse books and better trading, the Fortress facility may have been renewed at more favourable rates and this should provide an offset to rising rates. Rising rates also reduce the ability of less mature businesses to fund themselves and reduce credit supply.

Tax and franking

We expect CCV to pay a full tax rate into the future despite some recent losses as it appears many of the losses have been used up.

All dividends are fully franked.

CCV has $67m in franking credits

VALUATION

We use few separate valuation techniques for CCV.

We firstly derive a relative P/E based valuation. This looks at comparable business. It is superior to an EV/EBITDA valuation as it captures interest costs as a key part of the financial business metrics (and cost of doing business).

Table 13 – Relative P/E valuation

Segment / $m	FY23F NPAT	P/E X (x)	Value $m
NPAT (norm)	**22.1**	**10.0**	**221**
P/E valuation			**221**
Discount /risk			10%
Valuation			199
No. Shares (diluted)			644
Value per $/share			**$ 0.31**

Source: PAC Partners estimates.

We remove goodwill and conduct a relative price to NTA valuation. We'd note that book value includes inventory and a bank of self-liquidating loans and has intrinsic value and it not a stranded piece of PPE.

Table 14 - price to NTA valuation

P/BV	FY23F	P/BV X	
NTA ps	**183**	**1.00**	**183**
P/BV valuation			183
No. Shares (diluted)			644
Value per $/share			$ 0.28

Source – PAC estimates**.**

We further breakdown the NTA – provides solid underpinnings. This approach does blend price to book against NTA.

Table 15 – NTA breakdown $m

	FY23F
NTA breakdown $m	FY23F
Cash	69
Inventory	30
Loans assets	211
Goodwill	134
Other	85
Total	529
Less debt	176
Less other liabilities	36
Less goodwill	134
NTA	183
No. Shares (diluted)	644.3
Value per share	$0.28c

Source : PAC /CCV FY22 balance sheet.

We finally blend the two valuation techniques 50/50 to derive a price target of $0.30/share with further upside into the next few years.

Table 16 – combo valuation

Blended Valuation		Value $	Weight
P/E valuation	$	0.31	50.00%
P/bv	$	0.28	50.00%
Blended	**$**	**0.30**	
Current Price	$	0.24	
Difference		23.7%	
FY23 div yield		8.3%	
TSR		**32.1%**	

Source :PAC Partners

Summary

WE RATE CCV AS BUY

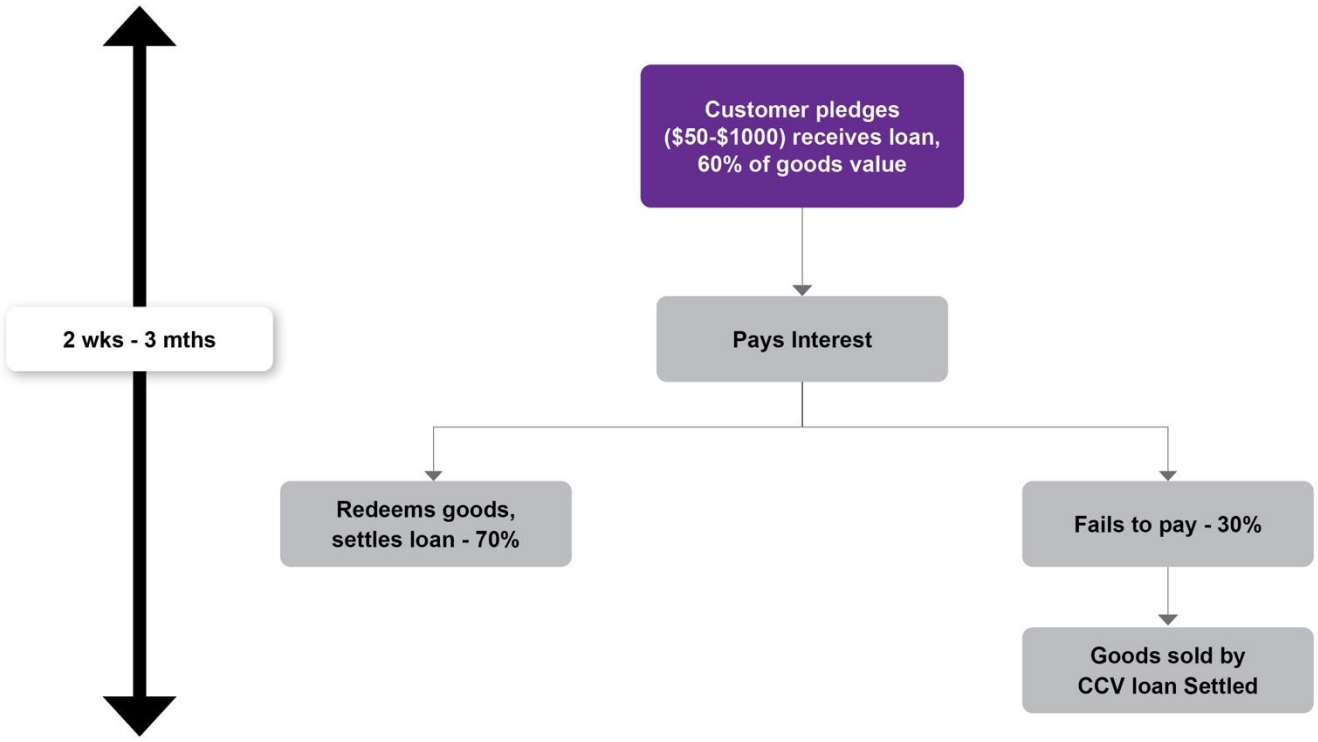
We have commenced coverage of CCV with a buy recommendation with higher risk.

Our investment thesis is predicated on:-

- Positive trading from similar businesses in the UK (and where CCV has some exposure) and in other similar western markets (UK/US) suggest improved trading is highly probable for CCV into FY23.
- The ability to manage the transition from Protected Earning amounts from 20% to net 10% and find way to mitigate the impact of this change.

- Resolution of a substantial number of legal disputes from past business activity helping to materially reduce legal and financial risk (and the legal cost budget).
- Possible regulation of BNPL – providing a more level playing field between CCV and these non-credit providers.
- New product launches.. stay tuned.
- An ability to acquire existing Australian franchisee stores on a reasonable basis and convert those into fully owned corporate stores. The recently (last 24 months) acquired stores should drive drive profitability growth into the future (estimated to be at least 5% p.a just from acquired stores annualised contribution.
- Post COVID19 recovery. Increased government payments and reduced economic activity resulted in a big lockdown paydown of the loans outstanding. With COVID19 now part of life – economic activity has resumed. Higher levels of inflation and the rising cost of living pressures are creating additional demand as customers look for cash to fund gaps between income and expenditure.
- Funding lines established, renewed with reliable and committed parties (Fortress) and controlled by a reliable offshore lender with available capacity.
- Low unemployment keeping bad debts under control. In part due to economic circumstances but also due to mix/past changes/past regulatory issues and generally tighter credit standards. The business needs to take some risk and will always incur bad debts – the main issue is that they are predictable and was reasonable care was taken when the loans were first originated.
- Further development on the online business to provide reliable and competitive methods of disposing of goods from expired pawn loans and sourcing quality loans.

Appendix 1 – CCV pawn broking – the basics



Source – PAC – % are estimates and might vary -from between -60-70% (repayment) and fails to pay 30-40% The average loan amount is $190.

Appendix 2 - Financial sector reform bill (2022)

Snippet of CCV submission to the Senate Economics Legislation committee.

7 October 2022

Committee Secretary
Senate Economics Legislation Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600
AUSTRALIA

Financial Sector Reform Bill 2022

Introduction

To the members of the Senate Economics Legislation Committee.

Cash Converters welcomes the opportunity to comment on the Financial Sector Reform Bill 2022.

The response addresses the proposed new laws to consumer credit reforms to Small Amount Credit Contracts ("SACC") contained within Schedule 4 of the Financial Sector Reform Bill 2022 only, as Cash Converters is not engaged in the consumer lease market.

Financial sector reform bill 2022– Protected earnings amount

12 Subsection 133CC(1)

Repeal the subsection (not including the heading), substitute:

(1) A licensee must not enter into, or offer to enter into, a small amount credit contract with a consumer who will be the debtor under the contract if the repayments that would be required under the contract would not meet the requirements prescribed by the regulations.

Civil penalty: 5,000 penalty units.

Note: For example, the regulations may provide that the amount of a repayment must not exceed a specified percentage of the consumer's income.

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Financial sector reform bill 2022 – explanatory memorandum pg 119

4.35 It is expected that the regulations will provide a protected earnings amount of 10 per cent of a person's net (after tax and other deductions) income for all consumers. This will mean that a licensee cannot enter into a small amount credit contract with a person if the total repayments under the small amount credit contract, and any other small amount credit contracts or that the consumer has, would exceed 10 per cent of the consumer's net income.

Parliament of Australia – Palrimanetary business – Financial sector reform bill 2022 – website

Progress

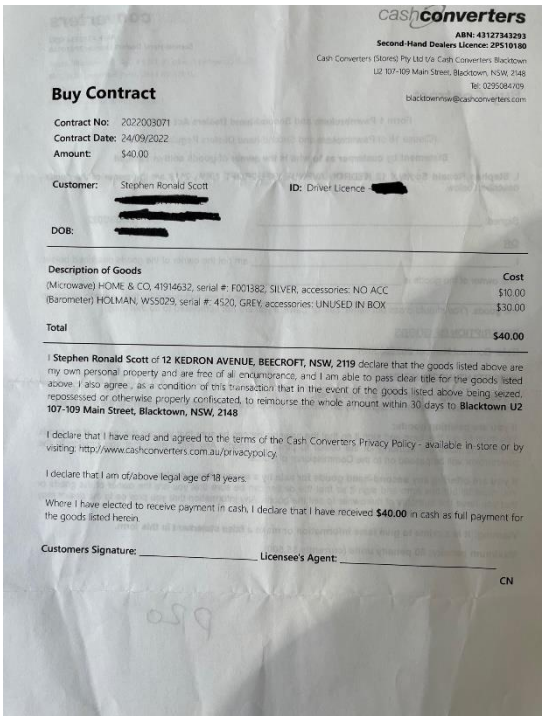
House of Representatives	
Introduced and read a first time	08 Sep 2022
Second reading moved	08 Sep 2022
Second reading debate	28 Sep 2022
Second reading agreed to	28 Sep 2022
Third reading agreed to	28 Sep 2022

Senate	
Introduced and read a first time	25 Oct 2022
Second reading moved	25 Oct 2022

Appendix 3 - picture gallery

Example of competitors' city (Melbourne) offer

Live example of sale of a second-hand item



cashconverters
ABN: 43127343293
Second-Hand Dealers Licence: 2PS10180
Cash Converters (Stores) Pty Ltd t/a Cash Converters Blacktown
U2 107-109 Main Street, Blacktown, NSW, 2148
Tel: 0295084709
blacktownnsw@cashconverters.com

Buy Contract

Contract No: 2022003071
Contract Date: 24/09/2022
Amount: $40.00

Customer: Stephen Ronald Scott ID: Driver Licence [redacted]
DOB: [redacted]

Description of Goods	Cost
(Microwave) HOME & CO, 41914632, serial #: F001382, SILVER, accessories: NO ACC	$10.00
(Barometer) HOLMAN, WSS029, serial #: 4520, GREY, accessories: UNUSED IN BOX	$30.00
Total	$40.00

I **Stephen Ronald Scott** of **12 KEDRON AVENUE, BEECROFT, NSW, 2119** declare that the goods listed above are my own personal property and are free of all encumbrance, and I am able to pass clear title for the goods listed above. I also agree , as a condition of this transaction that in the event of the goods listed above being seized, repossessed or otherwise properly confiscated, to reimburse the whole amount within 30 days to **Blacktown U2 107-109 Main Street, Blacktown, NSW, 2148**

I declare that I have read and agreed to the terms of the Cash Converters Privacy Policy - available in-store or by visiting: http://www.cashconverters.com.au/privacypolicy.

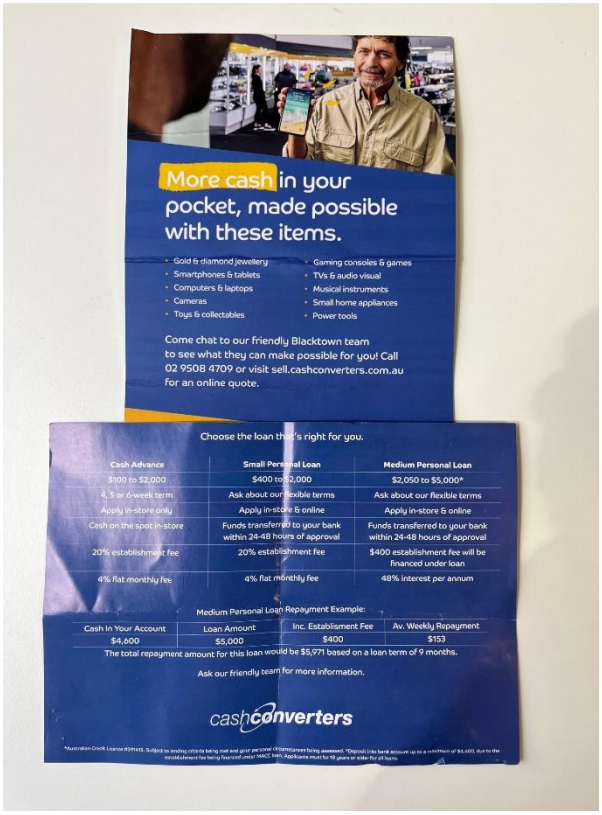
I declare that I am of/above legal age of 18 years.

Where I have elected to receive payment in cash, I declare that I have received **$40.00** in cash as full payment for the goods listed herein.

Customers Signature: _____ Licensee's Agent: _____

CN

Brochures – Sydney store – CCV



Source – PAC field work

Appendix 4 - Product set

Short Term – High Loss

Long Term – Low Loss

	Early Wage Access	SACC[1]	MACC[2]	Risk-rated	Vehicle Finance
Status	NEW (FY 2022)	Existing		NEW (FY 2022)	Existing
Max. Term	60 days	1 year	2 years	2 years	5 years
Max. Loan Amount	$200	$2,000	$5,000	$10,000	$45,000
Avg. Loan Term	4 weeks	10 months	16 months	24 months	4 years
Secured	No	No	No	No	Yes (recourse)
Interest Rate & Fees	No est[3]. fee, 5% single arrangement fee	4% monthly fee 20% est. fee	48% APR $400 est. fee	<=48% APR No other fees	<=48% APR Inc. all fees
National Credit Act Regulated	Exempt We will responsibly assess	Yes		Yes	Yes
Channel	B2C Digital	B2C Digital & In-Store		B2C Digital & In-store	B2B & B2C Digital

Source : Cash Converters

History of Cash Converters (legal settlements covered elsewhere)

1984	First store was opened by Brian Cumins in Perth.
1988	7 stores opened; franchise model was developed.
1990	Australia-wide expansion- 100 stores rolled out.
1991	Expands into UK, the first store opens in Essex.
1994	The first non-English speaking store in France opened.
1999	First Cash Advance loan.
2000	GST slows business.
1999-2001	Records large financial losses after losing legal cases and expanding too rapidly overseas. Franchisee dissatisfaction becomes a material issue (and the leaving system as a result).
Mid -2001	Share price falls below 3 cents- due to issue outlined above.
2003	Returns to profitability start new consumer trials $1000+
2005	Opens first corporate store in Bolton UK
2006	Acquires MON-E (payday loan software) for $15 million. Buys Safrock Group (larger unsecured lending) for $17.5 million.
2007	Acquires first franchise stores in UK and Australia
2008	Launches CCV online
2009	Launches financial services online
Sep-2009	Raises $54 million from Ezcorp via issue of $108 million to fund loan book expansion and buyback of franchisee businesses.
2009-14	Enjoys steady growth and reasonable trading
2010/11	Moves into Auto – financed entire car as a package deal (finance, tyres, maintenance, insurance)
2013	Australian rate caps come in – EBITDA fall
2014	Stuart Grimshaw becomes involved and also with Ezcorp
2014/2015	UK rate caps
2015	Buys back software from Cliffview/Kentleigh – material cost
2016/17	Winds down direct UK operation/moves to franchisee model – acts to stop continued losses in this market
2016/15	Westpac withdraws finance and payment processing – replaced in time by Fortress
2016	Restructures Auto loans to be traditional Auto loans – sold by car dealers/brokers/CCV – much easier to understand and market than a pre-packaged solution.
2016	Enters into Medium amount loan credit contracts (MACCs) – large amount/lower risk/long term.
2018	Fortress loan increased to $150m from $100m
2018	Raises $39m repay FIG / Ezcorp assists
2020/21	Pandemic hits loan volumes and store openings
2022	Fortress renewed for another 4 years $150m in total securitisation – covers various lending classes

Financial Models

Cash Converters International Ltd Share Price $ 0.240 Mkt Cap: (m) $ 151 **Rating** Buy

PROFIT & LOSS ($m)	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
Operating Revenue	**201**	**246**	**298**	**300**	**328**	**353**
EBITDA	**44.0**	**52.7**	**59.7**	**59.5**	**68.9**	**76.2**
Depreciation	(1.8)	(1.7)	(1.8)	(1.8)	(1.8)	(1.9)
Amortisation	(14.4)	(11.9)	(13.0)	(13.0)	(14.0)	(14.0)
Associates	1.7	0.0	0.0	0.0	0.0	0.0
EBIT	**29.5**	**39.1**	**44.9**	**44.7**	**53.1**	**60.3**
Net Interest	(11.7)	(12.5)	(15.0)	(20.4)	(18.7)	(18.5)
Income tax expense	(1.1)	(7.6)	(7.8)	(6.3)	(8.9)	(10.9)
Underlying NPAT	**16.7**	**19.0**	**22.1**	**18.0**	**25.5**	**31.0**
Abnormal Items	(0.5)	(7.8)	(7.5)	(2.5)	0.0	0.0
Reported NPAT	**16.2**	**11.2**	**14.6**	**15.5**	**25.5**	**31.0**

BALANCE SHEET ($m)	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
Cash	72	58	69	69	75	81
PP&E	66	55	54	54	56	57
Inventory	24	24	30	30	33	35
Intangibles	129	127	134	126	114	102
Loans/other	189	214	243	244	267	287
Total Assets	**481**	**478**	**529**	**523**	**545**	**563**
Borrowings	134	133	176	167	173	168
Trade Creditors	1	1	1	1	2	2
Other Liabilities	25	29	34	34	38	41
Total Liabilities	**160**	**163**	**212**	**203**	**212**	**211**
Shareholder Equity	**321**	**315**	**317**	**320**	**333**	**352**

CASHFLOW ($m)	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
Operating EBITDA	**44.0**	**52.7**	**59.7**	**59.5**	**68.9**	**76.2**
Interest/Tax Paid/other	(29.0)	(33.7)	(37.6)	(41.5)	(43.4)	(45.2)
Working Cap./other	(13.3)	(11.1)	(21.7)	11.0	(6.3)	(3.8)
CF from ops	**1.7**	**7.9**	**0.4**	**28.9**	**19.1**	**27.1**
Maintenance Capex	(2.7)	(1.4)	(0.4)	(2.1)	(3.7)	(2.6)
Acquis/exp capex	0.0	0.0	0.0	0.0	0.0	0.0
Investing Cashflow	**(6.5)**	**1.9**	**(20.4)**	**(7.1)**	**(5.7)**	**(10.9)**
Dividends	(6.2)	(12.6)	(12.6)	(12.6)	(12.6)	(12.1)
Equity/other/debt	(23.4)	(11.3)	42.9	(8.9)	5.6	(4.6)
Net Cashflow*	**(34.4)**	**(14.1)**	**10.4**	**0.4**	**6.5**	**5.8**

GROWTH PROFILE %	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
Revenue		22%	21%	1%	9%	8%
EBITDA		20%	13%	(0%)	16%	11%
EBIT		33%	15%	(0%)	19%	14%
NPAT (Underlying))		(31%)	30%	6%	65%	22%

DIVISIONAL Summary	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
EBITDA						
Personal Finance Int	38.6	44.1				
Store operations Int	13.8	16.4				
Operational EBITDA	52.4	60.5	69.6	68.2	76.5	82.6
Vehicle Finance Int	11.7	7.9	8.3	8.7	9.1	9.6
Franchisee opers. Fees	8.4	11.7	11.9	12.6	13.3	14.0
Other	0.0	0.0	0.0	0.0	0.0	0.0
Head office/legals	-27.2	-27.5	-30.0	-30.0	-30.0	-30.0
EBITDA (norm)	45.3	52.6	59.7	59.5	68.9	76.2
Average loan book		**196**	**231**	**249**	**262**	**283**

KEY RATIOS/metrics	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
EBITDA Margin (%)	n.m	21.4%	20.0%	19.9%	21.0%	21.6%
ROE (%) y/e	5.2%	6.0%	7.0%	5.6%	7.6%	8.8%
NTA per share ($)	30.6	29.9	29.2	30.9	34.9	39.8
Eff Tax Rate (%)	(6.1%)	(28.7%)	(26.0%)	(26.0%)	(26.0%)	(26.0%)
EBITDA Interest Cover (x)	3.8	4.2	4.0	2.9	3.7	4.1
Gearing ND/ND+E (%)	16.1%	19.2%	25.3%	23.5%	22.6%	19.8%
OPCF / EBITDA (%)	n.m	15.0%	0.7%	48.7%	27.8%	35.6%
Share count (dil) munits	634.7	646.1	644.3	642.5	642.5	642.5
Operating leverage analysis - this measures % of new sales converted to new EBITDA						
Sales delta $m (FYX-FYX-1)		44.6	51.9	1.7	28.5	25.3
EBITDA=(FYX-FYX-1) $m△		8.7	7.0	(0.2)	9.4	7.3
% of sales delta = EBITDA △		20%	14%	-14%	33%	29%

VALUATION METRICS	Jun-21A	Jun-22A	Jun-23F	Jun-24F	Jun-25F	Jun-26F
Dil. Normalised EPS (cps)	2.6	2.9	3.4	2.8	4.0	4.8
Dil. Reported EPS (cps)	2.6	1.7	2.3	2.4	4.0	4.8
EPS (norm) growth		12.0%	16.5%	-18.6%	41.9%	21.5%
Dil. Normalised PE (x)	**9.1**	**8.1**	**7.0**	**8.6**	**6.1**	**5.0**
Dil. Reported PE (x)	**9.4**	**13.8**	**10.6**	**10.0**	**6.1**	**5.0**
Enterprise Value ($m)	212	226	258	249	248	238
EV / EBITDA (x)	4.8	4.3	4.3	4.2	3.6	3.1
Price/Book value cps	**0.51**	**0.50**	**0.51**	**0.51**	**0.53**	**0.56**
DPS (cps)	1.0	2.0	2.0	2.0	2.0	1.9
Dividend Yield (%)	**4.2%**	**8.3%**	**8.3%**	**8.3%**	**8.3%**	**8.0%**
Franking (%)	0%	100%	100%	100%	100%	100%
Payout Ratio (%)	38%	68%	58%	72%	50%	40%
Free Cash / Share (cps)	(0.2)	1.0	0.0	4.2	2.4	3.8
Price / FCF PS (x)	-157.7	23.8	1939.9	5.7	10.0	6.3
Net Debt / EBITDA (x)	1.4	1.4	1.8	1.7	1.4	1.1

P/E valuation

	FY23F NPAT	P/E X (x)	Value $m
Segment / $m			
NPAT (norm)	22.1	10.0	221.1
P/E valuation			221.1
Discount /risk			10%
Valuation			199.0
No. Shares (diluted)			644.3
Value per $/share			**$ 0.31**

P/BV valuation

	FY23F
NTA ps	183
P/BV X	1.00
value	183
Shares	644
Value	0.28
Blended value	
P/E valuat	**0.31**
P/bv	**0.28**
50/50	**$ 0.30**

DIRECTORS/Snr Executives	%		%
Mr Timothy Jugmans - Chair/Ezcorp	43.8%	Mr Robert Hines - NED	0.1%
Mr Sam Budselik - MD	0.04%	Mr Henry Shiner - NED	
Mr Peter Cumins - Exe. Dep Chair	1.31%	Ms Sue Thomas - NED	
Mr Lachlan Given -NED			
Ms Julie Elliott - NED		**Total**	**45.2%**
Mr Budselik has material options package			

SUBSTANTIAL HOLDERS	%		%
Ezcorp	43.8%	KKR Entities	5.9%
Carol Australia	6.6%	Ryder Capital	5.7%
First Sentier	6.1%	**Total**	**68.2%**

Explicit Co. guidance commentary grow ing loans books should generate earnings momemtum, Q1 starts w ell
Date of guidance Aug-22

Source – PAC Partners

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RECOMMENDATION CRITERIA

Investment View
PAC Partners Investment View is based on an absolute 1-year total return equal to capital appreciation plus yield.
A Speculative recommendation is when a company has limited experience from which to derive a fundamental investment view.

Buy	Hold	Sell
>20%	20% – 5%	<5%

Risk Rating
PAC Partners has a four tier Risk Rating System consisting of: Very High, High, Medium and Low. The Risk Rating is a subjective rating based on: Management Track Record, Forecasting Risk, Industry Risk and Financial Risk including cash flow analysis.

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