Research as a Service

Flash Comment

6 November 2023

Pioneer Credit Limited

AGM signals strengthening position and seeking redress

Pioneer Credit Limited (ASX:PNC) is one of the leading acquirers and managers of impaired credit in Australia and has gained its status by maintaining positive customer engagement, an unblemished compliance record with ASIC, and strong relationships with Australia's largest bank and non-bank lenders. PNC purchases debt from 18 different Australian vendor partners with long-term partnership purchasing arrangements in place with Commonwealth Bank of Australia (ASX:CBA). The company's AGM updates highlighted the strong position PNC occupies in the marketplace and the expected improvement in NPAT following debt refinancing currently in progress. PNC also separately announced that it has commenced proceedings against PWC (the auditor at the time of a reporting standard change in 2018) for negligence, breach of retainer, and misleading or deceptive conduct. PNC believes PWC was responsible for loss and damage to PNC of $27m.

Business model

Pioneer Credit Limited acquires and manages performing and non-performing consumer debt portfolios (PDPs). The company acquires portfolios of defaulted consumer (non-mortgage) debts from the "Big Four" banks and other credit providers. PNC generates revenue by recovering the debts via contacting the debtors and negotiating payment arrangements or settlements. The company borrows at a margin over bank bills to fund purchases of PDPs, paying a discounted face value typically less than $0.20/$ of debt. Profit then depends on ethical and efficient management of the debtor/customer and accurate assessment of the credit risk inherent in the debtor profile.

AGM market update positive. Litigation fully funded

The Chairman and the CEO expressed a high level of confidence in the outlook for PNC's business with strong cash collections and a PDP investment target of $60m for FY23. Negotiation of a refinancing package with a substantial reduction in funding cost is expected to be finalised in the December quarter 2023. A reduction from an interest rate of (currently) 12.99% to 7% would be a $16.2m benefit to FY24 PTP. Additionally, incentive packages for management are based on three-year portfolio performance and a final hurdle of $18m in NPAT in FY 2026 – a level between our base and upside cases for that year. Finally, Pioneer's case against PWC is the result of a change in audit opinion late in FY 2018 which resulted in a delay in lodging of annual accounts, a change in financial ratios and a consequent breach of financial covenants. PNC claims this event disrupted the business and resulted in a substantial increase in funding costs despite a fundamentally sound operating business. PNC highlights that the litigation is fully funded and will not impact the operations of the business.

Valuation base case at $177m ($1.58/share)

Our valuation is based on the discounted cash-flow methodology using a discount rate of 16.5% (beta 2.0, risk-free rate 3.5%). We have modelled three cases mainly differentiated by finance margin, PDP price and cash collection performance, and including a cyclical component in our estimates. Our base-case valuation is $177m or $1.58/share. Our downside case values PNC at $146m ($1.30/share), while we can estimate upside to $236m ($2.11/share). We will reassess valuation following finalisation of the refinancing.

Historical earnings and RaaS' estimates (in A$m unless otherwise stated)

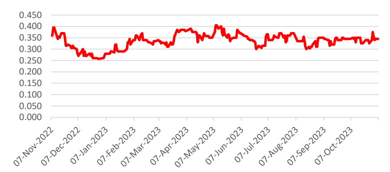
Year end	Revenue	EBITDA	EBIT	NPAT	EPS (c)	P/E (x)	Price/Book (x)
06/22a	62.6	8.9	6.1	(33.1)	(29.2)	n.a.	7.1
06/23a	73.7	36.2	34.0	0.2	0.2	225.9	7.9
06/24f	89.6	41.1	37.6	3.5	3.1	11.1	8.3
06/25f	91.2	40.7	37.3	11.4	10.2	3.4	7.9

Source: Company data; RaaS Advisory estimates for FY24f and FY25f

Share Details

ASX code	PNC
Share price (intra-day)	$0.345
Market capitalisation	$38.6M
Shares on issue	111.9M
Net cash 30-Jun-2023	$8.4M
Free float	~53%

Share Price Performance (12 months)



Upside Case

- PNC retains strong relationships with major banks based on quality of results
- Prices for debt portfolios weaken as majors high-grade their portfolios
- PNC refinances successfully at lower margins over BBSY bill rates

Downside Case

- Portfolio performance weakens more than expected as financial stress increases
- Banks do not sell more debt portfolios as credit growth slows
- Borrowing interest rates remain higher for longer

Catalysts

- Announcement of refinancing at commercial rather than punitive interest rates
- Increased purchases of debt portfolios
- Signs of improved efficiency allowing greater scale benefits

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FINANCIAL SERVICES GUIDE

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- how we transact with you
- how we are paid, and
- complaint processes

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