Chief Financial Officer's Operational and Financial Review

The Group has been able to maximise the opportunity created by structural changes in the UK Home Collected Credit market leader. This has helped to achieve a careful balance between customer and lending growth, investment in the future business with increased profits and asset returns as a result.

Andy Thomson
Chief Financial Officer

Overview

The results for the Group for the 52 weeks ended 24 February 2018 continue to demonstrate how we are able to grow the business, invest in the up-front costs of building new territories and still deliver improved earnings. As a result we delivered year on year sales growth[1] of 21.0%, revenue growth of 17.1% and an increase in adjusted profit before tax[1] of 8.5%. Statutory profit before tax grew by 43.8%.

The impairment charge as a percentage of revenue[1] for the year was 26.1%. This is higher than the 24.4% reported for last year but still within our guidance range of 22% to 27%, and lower than the 26.6% reported at the half year. Our guidance range was set in 2016 for lower levels of sales growth[1], and the fact that the impairment figure remains within the range despite 21% growth in credit issued[1] demonstrates the priority we continue to place on quality of lending.

Net tangible assets (net assets less intangible assets arising from acquisitions) increased by 12.8% to £61.5m with net receivables increasing by 19.0% to £72.8m.

1 Definitions are set out in the Glossary of Alternative Performance Measures on pages 98 to 99

£'m (unless otherwise stated)	52-week period ended 24 February 2018	52-week period ended 25 February 2017
Customer Numbers ('000s)	**229**	216
Period end receivables	**72.8**	61.2
Average receivables	**66.4**	58.2
Revenue	**116.6**	99.6
Impairment	**(30.4)**	(24.3)
Agent Commission	**(28.0)**	(22.4)
Gross Profit	**58.2**	52.9
Administration expenses, including depreciation (pre-exceptional, restructuring and non-recurring costs and amortisation of acquisition intangibles)	**(37.6)**	(34.3)
Operating Profit before exceptional costs, restructuring and non-recurring costs and amortisation of acquisition intangibles	**20.6**	18.6
Exceptional Income/(Costs)	**0.1**	(2.2)
Restructuring and non-recurring costs	**(1.0)**	(0.6)
Amortisation of acquisition intangibles	**(2.1)**	(3.7)
Operating Profit	**17.6**	12.1
Funding costs	**(1.5)**	(0.9)
Reported Profit Before Tax	**16.1**	11.2
Tax	**(3.0)**	(2.6)
Profit after Tax	**13.1**	8.6
Basic EPS	**10.1p**	6.6p

Reconciliation of Reported PBT to Adjusted PBT[1]		
Reported PBT	**16.1**	11.2
Exceptional (Income)/Costs	**(0.1)**	2.2
Restructuring and other non-recurring costs	**1.0**	0.6
Amortisation of acquisition intangibles	**2.1**	3.7
Adjusted Profit Before Tax	**19.2**	17.7
Tax	**(4.0)**	(3.7)
Adjusted Profit After Tax	**15.2**	14.0
Adjusted EPS	**11.7p**	10.8p

1 Definitions are set out in the Glossary of Alternative Performance Measures on pages 98 to 99

Chief Financial Officer's Operational and Financial Review *continued*

Group Results

Sales to customers for the year increased by 21.0% to £174.4m (FY17: £144.1m), with this growth attributable to the increased level of new territory builds, as no acquisitions were made during the period. In light of the territory build opportunity, we reduced spend on other lead sources for the recruitment of home collected credit customers to maximise the investment opportunity. We estimate that this change in focus reduced credit issued[1] on a like for like basis by £2.8m and resulted in up to 3,500 fewer customers at the year end. However, we believe that the resulting cost savings and lower impairments more than offset any reduction in income.

Revenue increased by 17.1% to £116.6m (FY17: £99.6m), with gross profit increasing by 10.0% to £58.2m (FY17: £52.9m). Agent commission as a percentage of revenue[1] reduced from 21.3% in FY17 to 20.2% in FY18, reflecting changes in the operating model.

Whilst impairment increased from 24.4% of revenue in FY17 to 26.1% in FY18, this remains within our guidance range of 22% to 27%. The guidance range was set with a lower level of growth in credit issued[1] in mind, which is relevant because the faster a loan book and lending increases, the more adverse the impact is likely to be on impairment as a percentage of revenue[1]. Encouragingly, impairment in the second half year was down to 25.6% from the 26.6% reported in the first half of the year as debt repayment performance exceeded our projections. Impairment as a percentage of credit issued was 17.4% in FY18, a slight uplift on the 16.9% reported for FY17.

Gross profit before territory build subsidies increased by 15.9% from £54.1m in FY17 to £62.7m in FY18. Territory builds increased to 463 in FY18 compared to 186 in FY17, with the cost of the agent subsidies increasing to £4.5m in FY18 from £1.2m in FY17. In addition, 25 of the FY17 territory builds occurred in the last two weeks of that year and so the majority of their costs were incurred in FY18.

After the territory build subsidies are taken into account, gross profit increased by 10.0% to £58.2m (FY17: £52.9m).

	FY2018		FY2017	
	£'m	**% of rev**	£'m	% of rev
Revenue	**116.6**		99.6	
Agent commission excluding territory build subsidy	**(23.5)**	**20.2%**	(21.2)	21.3%
Impairment	**(30.4)**	**26.1%**	(24.3)	24.4%
Gross profit before territory build subsidy	**62.7**	**53.8%**	54.1	54.3%
Territory build subsidy	**(4.5)**	**3.9%**	(1.2)	1.2%
Reported gross profit	**58.2**	**49.9%**	52.9	53.1%

Administration expenses increased from £34.3m in FY17 to £37.6m in FY18, reflecting not only the increased field infrastructure to support the business growth but also the costs associated with the development of the Dot Dot Loans online product, increased investment in our IT infrastructure and additional compliance costs. However, the administration expenses as a percentage of revenue fell from 34.4% in FY17 to 32.3% in FY18, an efficiency gain of 6.1%, driven by the productivity gains achieved from the implementation of technology improvements.

The adjusted profit before tax[1] increased to £19.2m from £17.7m last year, an improvement of 8.5%. The statutory profit before tax improved to £16.1m from £11.2m last year, an increase of 44.6%. This increase was boosted by the reduced amortisation of acquisition intangibles, and non-recurrence of the £2.2m IPO costs recognised in FY17.

A table of adjustments between reported profit before tax and adjusted profit before tax[1] is shown over the page.

For illustrative purposes, the table also shows the improvement in the core home collected credit business excluding the development costs in Dot Dot Loans and the investment costs in the new territory builds. On this basis the underlying performance of the core home collected credit business improved by 29.1%.

1 Definitions are set out in the Glossary of Alternative Performance Measures on pages 98 to 99

Group Results continued

£'m	FY18	FY17	Increase
Statutory PBT	**16.1**	**11.2**	**43.8%**
Amortisation of acquisition intangibles	2.1	3.7	
Cost of flotation on AIM	(0.1)	2.2	
Restructuring and other non-recurring costs	1.0	0.6	
Adjusted PBT[1]	**19.2**	**17.7**	**8.5%**
Territory build subsidies	4.5	1.2	
Dot Dot Loans development costs	0.8	–	
Adjusted PBT (Underlying HCC)[1]	**24.4**	**18.9**	**29.1%**

The amortisation of intangible assets reflects the unwinding of intangibles in connection with acquisitions. This reduction is a result of both the lack of acquisitions in the current year and reduced levels of amortisation in connection with prior year acquisitions. Intangible assets are amortised over the asset's useful economic life, which is based on the expected life of the acquired customer relationships. Due to the behavioural profile of our customers, this will naturally result in a greater amortisation charge in the early years with a corresponding reduction in later years.

Other non-operating costs relate primarily to non-recurring restructuring costs of the business and were higher in FY18 as a result of restructuring costs in operations.

Earnings Per Share

The adjusted earnings per share for FY18 is 11.7p, an increase of 8% relative to the 10.8p for FY17.

The reported earnings per share for FY18 is 10.1p compared to 6.6p for FY17, an increase of 53%.

Dividend

Subject to shareholder approval at the Annual General Meeting on 26 June 2018, the Board proposes to pay a final dividend of 4.8p per Ordinary Share (FY17: 4.3p) payable on 27 July 2018 to shareholders on the register at the close of business on 29 June 2018.

This payment is in addition to the interim dividend already paid of 2.2p per Ordinary Share, making a total dividend for the year of 7.0p (FY17: 6.4p). The continued high level of dividend payments reflects the Board's confidence in the business prospects, particularly the opportunity to create further growth from historic territory builds, and our commitment to provide a strong income yield to our shareholders.

Net Margin

The adjusted net margin[1], which excludes amortisation of intangibles on acquisitions, the one-off costs of the IPO and other non-operating costs, decreased to 16.5% from 17.8% last year, due to the impact of the cost of the territory builds. The cost of the territory builds impacted margins by 3.9% in FY18 against only 1.2% in FY17. Without this 2.7% adverse impact, the adjusted net margin[1] would have shown a favourable improvement of 1.4% rather than the decline of 1.3%.

The net margin for the period increased to 13.9% from 11.2% last year, driven by several factors: the non-recurrence of the one-off IPO costs of £2.2m, the reduction in the amortisation of intangibles on acquisitions charge (which reduced to £1.9m from £3.7m last year as a result of there being no new acquisitions in FY18) and the lower write downs on prior year acquisitions. These favourable movements more than offset the adverse movement in the adjusted net margin[1].

Acquisitions and Goodwill

There were no new acquisitions in the current accounting period, reflecting our focus on embedding the agents that joined us during the year. However the Group will continue to evaluate acquisitions in both the home collected credit market and other related non-prime sectors.

1 Definitions are set out in the Glossary of Alternative Performance Measures on pages 98 to 99

Chief Financial Officer's Operational and Financial Review *continued*

Funding

We were pleased to announce in August 2017 that we had increased our debt facility from £25m to £40m, with a major high street bank joining the existing facility we had in place with Shawbrook Bank. The expiry date of the facility was also extended from March 2019 to August 2020.

The current facility is sufficient to meet our immediate strategic objectives, with the peak drawdown this year being £28.0m in December 2017. We remain focussed on seeking to increase our gearing in order to maximise equity returns, but not to a degree that we feel that we are putting the Group at a significantly higher level of financial risk.

Balance Sheet

The total equity for the Group increased by 7.2% from £61.4m to £66.5m, reflecting the proportion of profits that we retain for future expansion.

The main asset of the Group is our loan book, which on a net basis increased by 19% from £61.2m last year to £72.8m in FY18. This increase was in part funded by our closing debt position, which increased to £16.0m from £10.0m over the same period. This increase of 19% was greater than the increase in gross loan book of 12% due to the improved quality of our customers reducing the relative impairment provision.

IFRS 9

IFRS 9 'Financial instruments' is effective from 1 January 2018 and replaces IAS 39 'Financial instruments: Recognition and measurement'. The standard has been applied prospectively and prior year comparatives will not be restated.

IFRS 9 requires the recognition of impairment on customer receivables through an expected loss model. Impairment provisions are therefore recognised on inception of a loan based on the probability of default and the typical loss given default. This differs from the current incurred loss model under IAS 39, where the requirement is that impairment provisions are only reflected when there is objective evidence of impairment.

However, for home collected credit businesses (HCC) the application of IAS 39 was conceptually difficult as the nature of our product is that customers will, from time to time, miss a payment and, up to a level, we are comfortable with this. Indeed, we apply no additional charges associated with missed payments and are proud of this aspect of forbearance in our products.

The Group has performed a preliminary assessment of the potential impact of adopting IFRS 9 based on the financial instruments as at the date of initial application of IFRS 9 (25 February 2018). IFRS 9 prescribes: (i) classification and measurement of financial instruments; (ii) expected loss accounting for impairment; and (iii) hedge accounting.

No changes are expected to the classification and measurement of the Company's assets, liabilities or equity nor does the company adopt hedge accounting. The only area which materially affects the Group is expected loss accounting for impairment. Under this approach, greater impairment provisions are recognised on inception of a loan based on the probability of default and the typical loss given default.

Provisions are calculated based on an unbiased outcome which take into account historic performance and considers the outlook for macro-economic conditions.

The impairment approach under IFRS 9 differs from the current incurred loss model under IAS 39 where impairment provisions are only reflected when there is objective evidence of impairment, typically a missed payment. The resulting effect is that impairment provisions under IFRS 9 are recognised earlier. This will result in a one-off adjustment to receivables, deferred tax and reserves on adoption and will result in delayed recognition of profits.

Based on current estimates, the adoption of IFRS 9 results in a reduction in the net loan book as at 24 February 2018 of between 4% and 6%.

Despite the adjustments required to receivables and net assets, it is important to note that IFRS 9 only changes the timing of profits made on a loan. The Group's underwriting and scorecards will be unaffected by the change in accounting, the ultimate profitability of a loan is the same under both IAS 39 and IFRS 9 and more fundamentally the cash flows and capital generation over the life of a loan remain unchanged. The Group's bank covenants are unaffected by IFRS 9, as they are based on accounting standards in place at the time they were set.

Cash Flow

The simplified cash flow statement below demonstrates the healthy levels of cash generated by the business prior to re-investment in the loan book asset of £22.9m (FY17: £15.7m).

It also shows how loan book growth in FY18 was primarily through the organic territory builds £11.6m (FY17: £7.6m) whereas last year's growth was a mix of organic growth and acquisitions.

Summary cash flow

£'m	FY18	FY17
Cash from operations excluding investment in loan book	**22.9**	15.7
Cash from funding	**6.0**	1.0
Total cash sources	**28.9**	16.7
Increase in net loan book	**(11.6)**	(1.9)
Acquisitions	**–**	(5.7)
Capital expenditure	**(2.0)**	(1.2)
Corporation tax	**(4.6)**	(4.1)
Interest paid	**(1.4)**	(0.9)
Dividends paid	**(8.4)**	(2.7)
Total cash uses	**(28.0)**	(16.5)
Cash movement	**0.9**	0.2

Andy Thomson
Chief Financial Officer
26 April 2018