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Challenging changing environment

Company/ASX Code	Credit Corp Group/CCP
AGM date	Thursday 1 Nov 2018
Time and location	11.00 am Boardroom P/L, Grosvenor Place Level 12, 225 George Street, Sydney, NSW, 2000
Registry	Boardroom
Webcast/teleconference	Yes
Poll or show of hands	Awaiting clarification
Monitor	Sue Erbag, Patricia Beal and Allan Goldin
Pre AGM Meeting?	Meeting with Chair and CFO

Item 1	**Consideration of accounts and reports**
ASA Vote	No vote required

Summary of ASA Position

Governance and Culture

This is the first year ASA is reporting on CCP and from our conversation with the Chair and CFO, overall they were both quite open and communicative about many areas of the business. The Chair was once a member of the ASA and has a good understanding of our objectives. The areas which both were more apprehensive to discuss were details of key management personnel (KMP), citing a need to guard their strategies for motivating KMP, this also flowed through to our request for non-statutory actual remuneration for the CEO. On the positive side, they were open to discussing CCPs strategy for expansion and the operational side of the business. We will continue to stress the importance and value of full transparency on KMP pay, which we believe is in the best interests of shareholders and directors. Overall CCP has put positive measures in place for areas of its remuneration structure but now that it has been elevated higher up the ranking of the ASX, it has more work to do to be aligned with its new peers and is still falling short of ASA recommendations.

Financial performance

CCP is a debt purchasing and lending company, with operations across Australia, New Zealand and the U.S. For financial year 2018 (FY18) CCP reported revenue of $299m (up 12%), statutory net profit after tax of $64.3m (up 17%), earnings per share of 135.1 cents (up 16%), and dividends per share of 67 cents (up 16%). Total shareholder return was 5.8%.

CCP increase in revenues was driven mostly by its growth of ANZ consumer lending and US debt purchasing showing its first profit. Lending contributes to 25% of profits equating to $16.1m and growing strongly (group net profit $64.3m). Debt purchasing is split $120m Australia, $50m US.

CCP entered the US market 6 years ago and its expansion there will result in an increase in headcount from 230 to 400. This increase in staff is expected to support an increase in US debt purchasing from its current level of $50m to $80m per annum (expected net profit $10m). The reasoning for this geographic expansion is primarily the maturing Australian market, of which CCP currently holds approximately 30%. Over the last few years CCP has been able to take advantage of its balance sheet strength and closure of some US debt purchasing competitors and is now starting to win more business and see positive returns on this side of the business.

There is still however further opportunity for expansion in debt purchasing and lending in Australia. The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Royal Commission) has prompted some banks to reduce the size of their personal loan books. This may benefit CCP which purchases personal debt from the banks as well as lending to customers which the Banks may turn away. Return on capital (ROC) will continue to be targeted at 18% for both the US and ANZ.

CCP had strong lending growth for FY18 of 19%, its group lending target is $230m over the next few years (currently $170m).

Car lending is also gathering pace and CCP is looking to grow this area of their business to $100m but is some way off as they need to refine their current model. Car lending is desirable for CCP because of the longer termed revenue it generates in comparison to personal lending which is paid off over the shorter term.

CCP purchased its debt collection competitor NCML in 2016 and believes it can improve the profitability of the business by managing its risk better. CCP has built up a large database of historic and current customers which it uses to understand customer behaviour and manage risk.

CCPs bank funding currently comes through Westpac but moving forward as its funding requirements grow it may seek out alternative lenders.

Key Events

The last year has seen negative sentiment build around the finance industry as the Royal Commission has delved deeper into their practices. Smaller lenders may now see themselves drawn into this, as Labor, the Liberals and Greens push for a senate inquiry into their lending practices.

Credit Corp pulled out of payday lending in February 2016. This move was prompted just 2 years after they entered the sector after CCP came under pressure from ASIC to make the change. Legislation defines these payday lending/small account credit contract (SACC) loans as amounts under $2,000 for terms up to 12 months. The maximum interest that can be charged is equivalent to 48% pa.

Whilst CCP is technically not a payday lender the criteria which separates it from being included in this category, is now at risk of changing. The Chair expressed CCP would welcome an investigation into lending practices as it sees its own practices as superior to that of its competitors. On its personal small loans (under $2000) CCP charges interest at just under 48%. The importance of CCP being excluded from the payday lending category is that payday lenders face higher costs from banks for funding and also face stricter banking covenants. Thus CCP is able to operate at a lower cost than payday lenders. When Labor, supported by the Greens and some Independents announced that if it is elected they would have a Royal Commission into payday lenders, CCP saw its share price drop by 9.2%, reflecting that even though it may not technically be a payday lender, a portion of shareholders and the market still view it as such.

It is of concern that there has not been any board renewal in terms of appointing new directors for more than 4 years.

Summary

(As at FYE)	**2018**	**2017**	**2016**	**2015**
NPAT ($m)	64.3	55.2	45.9	38.4
UPAT ($m)	64.3	55.2	45.9	38.4
Share price ($)	18.07	17.71	12.01	12.17
Dividend (cents)	67	58	50	44
TSR (%)	5.8	48	2.8	44.9
EPS (cents)	135.1	116.8	98.4	83.0
No. of deferred shares vested to CEO	146,266	64,102	66,412	63,942
Date of vesting	Nov-17	Sep-16	Sep-15[1]	Sep-14[2]
CEO total remuneration, actual ($m)	4.3	2.5	2.3	2.2

CCP does not supply the actual remuneration however we sent the above table to the CFO and he has provided some information not previously disclosed in the annual reports (see below).

1) In addition to shares divested, cash payments of $186,335 in respect of the 2009-12 LTI and $332,460 in respect of the 2013-15 LTI occurred in Sep-14, these have been included in the total actual remuneration estimates.

2) In addition to shares vested, a cash payment of $331,595 occurred in respect of the 2013-15 LTI occurred in Sep-15, these have been included in the total actual remuneration estimates.

For 2018 the shares vested during the year were worth $2,945,797 being 146,266 shares vesting on November 1, 2017, Fixed Annual Remuneration of $678,600, Cash STI of $665,000 and other cash of $17,857.

For 2018, the CEO's total actual remuneration was [50.1] times the Australian Full time Adult Average Weekly Total Earnings (based on [November 2017 / May 2018] data from the Australian Bureau of Statistics).

Note - For May 2018, the Full-time adult average weekly total earnings (annualised) was $85,956 (http://www.abs.gov.au/ausstats/abs@.nsf/mf/6302.0, "Full-time adult average weekly total earnings", Trend(a)).

Item 2 (a)	**Re-election of Richard Thomas**

ASA Vote	**Against**

Summary of ASA Position

Richard Thomas has been non-executive director (NED) since 2006 (12 years) and has over 40 years' experience in Finance. Mr Thomas currently holds 12,584 ordinary shares in CCP.

Whilst Mr Thomas is highly qualified and experienced for his role, his re-election does not fit well with ASA requirements. The board overall has half of its NEDs serving for longer than 9 years. The ASX states that after 9 years a board members Independence should be questioned. After 12 years, ASA will no longer classify directors as independent.

Item 2 (b)	**Re-election of Eric Dodd**
ASA Vote	**For**

Summary of ASA Position

Eric Dodd has been non exec director for since 2009 (9 years). He is also Chair of Integrity Insurance Group (Australia) and Chair of First American Title (Australia). He has extensive experience in the Australian Insurance sector having also served as CEO of MBF/BUPA Australia Group. Mr Dodd currently holds 5000 shares in CCP.

Whilst Mr Dodd is highly qualified and experienced for his role, his re-election after 9 years starts to trigger questions over his Independence as per ASX guidelines. Mr Dodd currently falls slightly short of our recommendation for shareholdings equating to 100% of fees. Currently his shareholding valued at $103,800 equates to 86.5% of his fees of $120,000.

Item 3	**Adoption of Remuneration Report**
ASA Vote	**Against**

Summary of ASA Position

Like every annual report there is a remuneration table showing the remuneration paid to each KMP during the year and the breakdown of those payments. Unfortunately the remuneration is for statutory remuneration and doesn't show the take home pay of the KMPs. The remuneration report is detailed and clearly laid out, however it still lacks important information. The short-term incentive (STI) does have performance hurdles but it is paid out solely in cash, ASA advocates an STI split between cash and shares.

The long-term incentive (LTI) it is based over a 3-year performance cycle and the performance rights are allocated and converted into deferred vesting shares at the end of the first 3 years and then continue to be paid out during the following 2 years.

The statutory remuneration report is generally clearly expressed. The CEO's remuneration comprises of $700,000 fixed salary cash, benchmarked against the average salary of CEOs in the same industry of similar sized companies. The STI is paid out in cash annually and the STI target is split between the Group achieving its target net profit after tax (NPAT) and is subject to a minimum return on equity (ROE) of 15 per cent being achieved. The maximum STI payable is 100% of the salary and minimum is 50% of the salary. There are also individual objectives/ Key Performance Indicators (KPIs, including strategic KPIs aligned to milestones in the three-year Strategic Plan). The KPIs are split between targeted NPAT, new loans purchasing targets being met, maintaining the quality of the existing loans portfolio, US operational performance and other strategic expansion opportunities. Details of the exact targets for KPIs and the results achieved are not given.

The LTI as stated above is paid out in performance rights converting to deferred vesting shares achieved against performance hurdles being met. The number of shares issued are calculated based on fair value therefore there is no transparency. The LTI hurdles are split 50% between a target compound annual growth rate (CAGR) of NPAT and 50% total shareholder return (TSR) relative to the ASX 200 (excluding energy and metals shares). The NPAT CAGR hurdle for 2019 is set at 9%. There are clawback clauses in place for underperformance.

However, its remuneration arrangements fall short of some ASA guidelines. Our primary areas of concern are:

- The remuneration structure is too short-term focussed with short term incentives (100% cash) and LTIs performance period being only three years. We believe that short term incentives should be half in cash in year one and half in equity deferred by 1 year, and that the period for long term incentives should be at least four, preferably five years.
- We are opposed to how the number of shares issued as part of the long term equity awards are calculated based on fair value not face value. The use of fair value means the company is not clearly communicating the true value of these awards. As this company, unlike virtually everyone else in the ASX 200, does not have the CEO as an executive director, there is no requirement to vote on his bonus. If we did we would be voting our open proxies against.

Item 4	**Approval to increase the maximum aggregate fee pool for NEDs**
ASA Vote	**For**

Summary of ASA Position

CCP wishes to increase the maximum aggregate pool available for NED fees by $200,000 per annum, from $900,000 per annum to $1,100,000 per annum (including superannuation contributions made by the Company for the benefit of NEDs and any salary sacrifice arrangements on a pre-tax basis). The purpose of this increase is to allow CCP to hire more NEDs with expertise that will support its growth in the U.S. The pool was last increased in 2012.

One of the individuals involved in the preparation of this voting intention has a shareholding in this company.

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