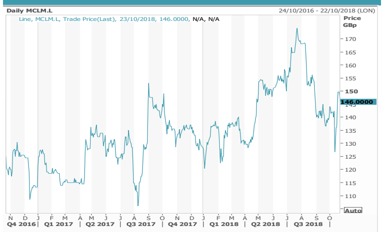
HARDMAN & CO.

23 October 2018

MORSES CLUB PLC

Sustainable growth from focus on quality

Financials



Source: Eikon Thomson Reuters

Market data

EPIC/TKR	**MCL**
Price (p)	149.75p
12m High (p)	174.0
12m Low (p)	123.0
Shares (m)	129.5
Mkt Cap (£m)	193.9
EV (£m)	173.5
Free Float*	60%
Market	AIM

**As defined by AIM Rule 26*

Description

Morses Club (MCL) is number two in UK home credit. It is growing this business organically and by acquisition, and is developing a range of related products, where it has a competitive advantage.

Company information

CEO	Paul Smith
CFO	Andy Thomson
Non-ex. Ch.	Stephen Karle

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Key shareholders

Hay Wain	36.82%
Woodford Inv. Mgt.	9.33%
Miton Asset Mgt.	9.03%
Artemis Inv. Mgt.	6.95%
JO Hambro	6.74%
Majedie Asset Mgt.	5.34%
Blackrock	4.15%
Legal and General	3.22%

Diary

End Feb / early March	Trading statement

Analyst

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The 4 October results confirmed steady growth, controlled risk and delivery in line with expectations. Double-digit underlying revenue and earnings growth was generated from stable customer numbers, and achieved more efficiently with fewer agents. The Provident Financial opportunity is now embedded and management can focus on new growth initiatives. We reviewed MCL's focus on quality in our 19 July 2018 note, *Quality Street*, highlighting how conservatism runs throughout MCL's lending, accounting, agents, customer selection and new product development. Our absolute valuation range is now 179p to 223p.

- **1HFY'19 results:** We believe investors should focus on like-for-like KPIs, not the statutory accounting numbers. On an LFL basis, revenue was up 12%, the net loan book +8%, adjusted PBT +14%, and adjusted EPS +14%. The cost income ratio improved from 59.6% to 58.5%. Impairments were 21.9% of revenue (21.6%).
- **Outlook:** We have made only modest (upward) revisions to estimates. With the former Provident Financial agents, managers and customers significantly embedded, management can now focus on expanding new product areas (online loans, the customer portal, and Morses Club Card), and home collect acquisitions.
- **Valuation:** We detailed a range of valuation approaches and sensitivities in our note, Bringing home collect into the 21st century, published 2 February 2017, and do so again in the section below. The range in absolute valuation methodologies is now 179p to 223p. Peer measures range from 144p to 201p.
- **Risks:** Credit risk is high (albeit inflated by accounting rules) but MCL adopts the right approach to affordability and credit assessment. Regulatory risk is a factor, although high customer satisfaction suggests a limited need for change. MCL was the first major HCC company to receive full FCA authorisation.
- **Investment summary:** MCL is operating in an attractive market, and it has a dual-fold strategy that should deliver an improved performance from existing businesses and new growth options. MCL conservatively manages risk and compliance, especially in new areas. The agent network is the competitive advantage over remote lenders. The valuation appears an anomaly, and we forecast a 5.3% February 2019 dividend yield, with cover of 1.7x (adj. earnings).

Financial summary and valuation

Year-end Feb (£m)	2015	2016	2017	2018	2019E*	2020E*
Reported revenue	89.9	90.6	99.6	116.6	119.3	129.8
Total impairments	-22.9	-18.8	-24.3	-30.4	-26.0	-29.9
Total costs	-51.4	-53.4	-56.7	-65.6	-69.8	-73.9
EBITDA	16.5	19.3	19.9	22.1	24.8	27.9
Adjusted PBT	13.0	16.8	17.7	19.2	21.8	24.6
Statutory PBT	58.5	10.4	11.2	16.1	18.6	21.7
Statutory EPS (p)	46.5	6.1	6.6	10.1	11.7	13.7
Adj. EPS (p)	8.1	10.2	10.8	11.7	13.4	15.2
P/adj. earnings (x)	18.5	14.6	13.9	12.8	11.1	9.8
P/BV (x)	2.0	3.5	3.2	2.9	2.8	2.6
P/tangible book	2.3	4.3	3.8	3.3	3.2	2.9
Dividend yield	n/m	n/m	4.3%	4.7%	5.3%	6.0%

*Source: Hardman & Co Research * IFRS9 basis*

1HFY'19 results

Key messages

1HFY'19 delivery of quality growth

1HFY'19 is a continuation of the messages from FY'18, with management delivering on its promises to sustainably grow the business for the long term, and with a clear focus on adding quality agents and customers. In particular, we note the following.

Core business profits up on stable customer and falling agent numbers

- The core business has delivered good profit growth from increasingly serving high-quality customers. Profits are up more than 10% as stable customer numbers are served by fewer agents. Credit quality remains within the target range.

Focus on new product lines and potential acquisitions in home collect

- MCL, having rightly prioritised resources to deliver the unique opportunity in its core business in 2017/early 2018, can now focus again on other growth initiatives. It appears likely that acquisition of home collect businesses will resume in the near future. Morses Club Card continues to grow and delivery on the advanced customer portal is progressing. The pace of investment in Dot Dot Loans has been kept very modest and it will now focus on larger and longer-term loans than originally planned.

Some further benefit from PFG opportunity but largely embedded now

- The Provident Financial (PFG) fall-out has enhanced the agent, manager and customer franchise, generating revenue and profit streams that should recur over many years. Operationally, the new agents and managers have now been integrated and incremental benefits from here are expected to be less material.

Financial highlights

With the distortions from the transition to IFRS9 accounting, we believe investors should focus on the pro forma IFRS9 numbers and our comments are on this basis.

Net loans +8%, revenue +12%. Quality of customers much improved.

- Revenue rose 12% to £57.5m (48% of our previous FY'19 forecast). Total credit issued increased 5% to £86.1m, with the net loan book growing 8%. Top tier customers accounted for 69% of loan balances, (1HFY'18: 70%, 1HFY'17: 65%). Over the year, there was a 1% fall in customer numbers to 230k (although it was up 1k on the 229k at end-February, despite the usual seasonality).

Impairments as % of revenue broadly stable and within target range, despite growth

- Impairments as a percentage of revenue for the period were 21.9% (1HFY'18: 21.5%). On the old IAS 39 basis, this was 26.6% (FY'18: 26.1%, 1HFY'18: 26.6%) keeping within the target range of 22-27% (management is expected to issue a new guidance range on the IFRS9 basis with the full-year results). A growing business is likely to see higher impairments to revenue, and we note that MCL is applying historical experience assumptions to new lending in its new territory builds. Accounting requirements also inflate the charge relative to cash losses and, again, the effect increases with a growing book. There is no sign of underlying credit strain.

Agent commission risen slightly; expect temporary commissions to fall

- Agent commissions were £12.8m (1HFY'18: £11.2m) representing 22.3% of revenue (1HFY'18: 21.8%) while temporary commissions fell from £1.9m to £1.3m. The latter may be expected to fall to ca.£0.5m once the PFG agents are fully operational.

Efficiency improvement despite higher compliance and marketing

- Administration costs as a percentage of income declined to 58.5%, a 2% efficiency improvement on the 59.6% reported for 1HFY'18. Management reports that a number of small increases across areas such as compliance and marketing have partially offset greater efficiencies in operational delivery.

Adjusted profits up 14%

► Adjusted profit before tax increased 14% to £10.5m. Excluding temporary agent costs and the Dot Dot investments, underlying PBT grew 7% from £11.4m to £12.2m. Reported profit before tax was £10.0m (1HFY'18: £7.2m). Adjusted EPS was 6.6p, up 16%. Basic EPS was up 61% to 6.3p.

Dividend up 18%

► The dividend was 2.6p, up 18% reflecting management confidence as well as the strong earnings growth. We forecast a 5.3% yield, 1.7x covered by earnings.

Company KPIs and targets

We detail below the key KPIs outlined by the company, and a couple of additional measures. The trends are virtually all positive.

Company KPIs and targets

KPI	2015	2016	2017	2018	1HFY'18*	1HFY'19*	Comment
Adjusted profit before tax (£m)	13.0	16.8	17.7	19.2	9.2	10.5	Up 14%
Adjusted EPS (p)	8.1	10.2	10.8	11.7	5.7	6.6	Up 14%
Admin. cost income ratio	36.5%	36.8%	33.1%	32.2%	59.6%	58.5%	Fallen despite compliance
Return on equity	21.5%	27.9%	27.2%	26.5%	N/A	25.4%	Despite low gearing
Tangible equity/avg. recs.	N/M	85.3%	93.5%	92.6%	N/A	87.6%	Cash generation strong
Number of customers ('000s)	198	199	216	229	233	230	Focus on quality
Number of agents	1,893	1,839	1,826	2,030	2,124	1,942	Efficiency improved
Credit issued (£m)	112.0	122.2	144.1	174.4	82.3	86.1	Grown on stable customer nos.
Impairment/revenue	25.5%	20.8%	24.4%	26.1%	21.5%	21.9%	Reflects growth
Period-end receivables (£m)	55.6	56.8	61.2	72.8	62.8	68.0	Higher quality customers.

*Source: MCL, Hardman & Co Research *IFRS9 basis*

Impact on estimates

Modest upward revision to estimates, primarily to IFRS 9 adjustments

Our FY'19 estimates are largely unchanged. For FY'20, we include £3m of acquired revenue. We have reviewed how the PFG agent capacity will be utilised. Compared with prior forecasts, we have now assumed they will, to a greater extent, service customers from vacant rounds rather than expanding the customer base. This change in our assumption sees lower receivables, customer numbers, revenues and costs and is more consistent with management's focus on efficiently managing a quality book.

Estimate changes

	2019E			2020E		
Year-end Feb	Old	New	% change	Old	New	% change
Profit and loss (£m)						
Reported revenue	119.0	119.3	0%	133.0	129.8	-2%
Total impairments	-26.6	-26.0	-2%	-29.1	-29.9	3%
Total costs (inc. temp. comm.)	-69.2	-69.8	1%	-75.6	-73.9	-2%
EBITDA	24.9	24.8	0%	30.1	27.9	-7%
Adjusted pre-tax	21.4	21.8	2%	26.4	24.6	-7%
Statutory pre-tax	18.2	18.6	2%	23.6	21.7	-8%
Statutory EPS (p)	11.4	11.7	2%	14.8	13.7	-8%
Adjusted EPS (p)	13.2	13.4	2%	16.3	15.2	-7%
Dividend (p)	7.7	8.0	4%	8.5	9.0	6%
Balance sheet (£m)						
Amounts receivable	74.0	74.0	0%	79.0	76.8	-3%
Borrowings	16.0	14.0	-13%	16.0	10.0	-38%
Equity	67.6	68.8	2%	76.2	75.3	-1%

Source: Hardman & Co Research

Strategy and outlook

Core business growth

Former PFG agents, managers and customers largely embedded. Temporary commissions should fall away.

In FY'18, MCL reported more than 600 agent and manager hires and a gross 463 (1HFY'18: 411) territory builds, adding ca.22% to its agent network following the self-inflicted woes at Provident Financial (PFG). There were incremental temporary commissions paid and some build-out of infrastructure (noting MCL already had some spare capacity). The agents and managers have now been integrated, although we believe MCL showed its usual risk conservativism, and this led to some agents taking a little longer to get to their full rate of customer numbers. Territory build subsidies in 2H'19 might be a little above the usual level, (Hardman estimates £1.0m vs. usual rate of £0.5m), as MCL will want to keep performing agents on board, and the delay in reaching targeted numbers reflects MCL's risk appetite and not the competence of the agent.

Some opportunity for further efficiency improvement

What was visible in these results is that having onboarded large numbers of agents last year, MCL is now taking the opportunity to improve their efficiency. A stable number of customers is being served by an agent network nearly 10% smaller. MCL highlights that customers per manager is now 793, a 38% growth since the IPO. This efficiency improvement has been delivered through better technology but also a higher quality of agent. Looking forward, the incremental benefits to revenue and costs on 1HFY'19 numbers appear likely to be more modest; although, as noted above, we expect temporary agent commissions to fall from their 1HFY'19 level of £1.3m to ca.£0.5m per six months.

Stable market but some share gains from technology advantage and re-commencement of consolidation. Management advise of much greater seller interest and it is in advanced due diligence in some cases.

The market for home collect is believed to have been broadly stable for some time and MCL growth is likely to come from market share gains. In FY'18 and 1HFY'19, MCL made no loan book acquisitions. The market had slowed in FY'17, and it is likely that some smaller players will be waiting to see the fall-out from PFG before deciding to sell. They could reasonably be expecting more business and so a higher value. MCL management was more focused on effectively managing the short-term opportunity from the released PFG agents. There has also been some uncertainty over what regulatory changes may be enforced, and the degree to which being a larger player would generate significant relative benefits. With these results, management advised that it had seen a spike up in potential interest from sellers with a number of potential acquisitions in discussions. As with MCL, the PFG opportunity for sellers is now visible, MCL management has the resources to exploit this growth and, while the regulatory changes are not finalised, there is a probability that they will play to MCL's business model strengths.

Likely to be more than 30 potential targets in MCL's sweet spot

With just a 14% market share, acquisition opportunities for MCL could be material. While there are in excess of 400 regulated home collect businesses, we do not think it would be efficient for MCL to target the smaller players. We believe there are approximately 20 businesses with loan books in the range of £0.5m-£4m and a further 12 in the range £4m-£20m.

Funding put in place

We note MCL's funding headroom (assuming peak December utilisation) is likely to be ca.£15m and even at that level debt would still be only at about 2/3rds of equity against peers whose debt is multiples of equity. In our view, increasing facilities would not present a problem should some of the larger businesses become available.

New product areas

Online Lending

Platform put in place. Initial lesson from pilot stage has led to focus on longer-term, larger loans than originally planned.

Online lending activities were accelerated with the Shelby Ltd acquisition in January 2017, although, in FY'18, management was focused on the core home collect opportunity. The low-cost, low-risk soft launch (branded Dot Dot Loans in March 2017) saw activity primarily around building the right IT infrastructure, linkages and risk models. Experience to date has led to less appetite for short-term (i.e. three-month) loans, where there has been limited customer loyalty and broker introduction fees often make lending uneconomic. Accordingly, MCL is now focusing on loans averaging ca.£2,500, with a duration of ca.2 years and at established market APR's for these products. The key considerations in targeting this space are:

Less competition in this space

- Limited competition. In the remote, non-standard market, the scale and duration of its loans, places MCL between card providers and guarantor loans and with few competitors. This market opportunity is consistent with our view and the analysis provided by peers (e.g. slide 26 NSF competitive landscape view).

Online product to quality customers at low delivery cost. Different model to Everyday Loans.

- MCL will be offering an online service only. While having a small overlap with the lower end of Everyday Loans (ELL) product range, MCL will not be competing through a branch network and the economics of its model are somewhat different. MCL will be targeting high quality customers, delivered by low cost channels and accepting that, as a remote lender, it will incur higher like-for-like impairments than a branch lender. We therefore expect the ELL overlap to be modest.

MCL has competitive advantages in terms of funding, credit infrastructure, brand recognition and regulator relationships

- MCL has a number of competitive advantages in this part of the market over many potential peers:
    - Long-term committed funding to achieve growth ambitions.
    - Established credit assessment, management and collection infra-structure. There will be differences in credit between this market and home collect lending (e.g. for this level of debt, we would expect a higher dependence on earned income over welfare income) but MCL has the processes to manage it.
    - Brand recognition (particularly among former home collect customers whose finances have improved to the level of being able to afford larger, longer-term loans).
    - Established relationship with the regulator. MCL will need a variation in its regulatory permissions to do this longer-term lending. Having been an established player, this process is likely to be accelerated relative to a new entrant.

MCL will proceed with usual caution and modest start-up losses expected

MCL is cautious in its approach and will not bet the bank on launching online lending. As we noted on p9 of our report Quality street, published on 19 July 2018, MCL's start-up investment has been tiny compared with operations like 118 1118 Money, Likely Loans or Satsuma (combined losses £131m 2013-16). By comparison, MCL saw a loss of £0.8m in FY'18 and a further £0.4m in 1HFY'19.

Morses Club Cards

Steady growth and loan balances now £13m

We note that Morses Club Cards in issue have risen steadily (ca.5k every six months to 27k 1HFY'19 from 21k in FY'18 vs. 11k in FY'17, and the gross loan book is now £13.1m (ca.10% of receivables). MCL believes the incremental data on spending will prove a valuable asset and that having a product that is popular with younger customers is a good acquisition and retention tool.

Customer portal

Looking at range of products to sell to customer base and likely to involve partners who have the product but not the customer base

With regard to the customer portal and associated IT infrastructure, MCL has reported that it is likely to see a full product launch later this year. The test launch in January 2018 has seen customer take up of ca.10% when the portal product range is extremely limited. As the product range increases, we would expect an acceleration in the take-up rate. There was commentary about products offering discounts, reward schemes, banking services and price comparisons using the extensive data likely to be available through the customer portal. Appropriate customer approvals to use their information have been incorporated, and management advises that products such as insurance, utilities and mobile comparisons will be provided by third parties. With these results, we sensed the initial experience leads MCL management to conclude that there is a real financial opportunity from credit-related products provided by MCL (previously management had advised that it viewed the portal as being primarily a customer acquisition and retention tool). We expect the strategy to further evolve with experience through the pilot exercise.

Financials

Profit & Loss

Profit and Loss						
Year-end February (£m)	**2015**	**2016**	**2017**	**2018**	**2019E ***	**2020E ***
Existing operations	22.5	84.7	96.2	116.6	126.0	132.3
IFR9 income effect	0	0	0	0	-6.8	-5.5
Acquisitions during period	67.4	5.8	3.3	0	0.1	3.0
Total revenue	89.9	90.6	99.6	116.6	119.3	129.8
Impairment charge	-22.9	-18.8	-24.3	-30.4	-32.8	-35.4
IFRS9 impairments, net effect					6.8	5.5
Ongoing agent commission	-17.7	-18.5	-21.2	-23.6	-26.7	-29.0
Temporary agent commissions		-0.7	-1.2	-4.4	-2.3	-1.0
Gross profit	49.3	52.6	52.9	58.2	64.3	69.9
Administration expenses pre-excep. and intang. amortis.	-32.8	-33.3	-33.0	-36.1	-39.5	-42.0
Depreciation (incl. goodwill impairment, amortis. of IT)	-0.9	-0.9	-1.3	-1.5	-1.3	-1.9
Operating profit pre-excep. and amortisation	15.6	18.4	18.6	20.6	23.5	26.0
Adjusted financing costs	-2.6	-1.6	-0.9	-1.5	-1.7	-1.4
Adjusted profit before tax	13.0	16.8	17.7	19.2	21.8	24.6
Income tax	-2.7	-3.5	-3.7	-4.0	-4.4	-4.9
Adjusted post-tax profit	10.3	13.3	14.0	15.2	17.4	19.7
Impairments as % revenue (exc. IFRS9 from both)	-25.5%	-20.8%	-24.4%	-26.1%	-26.2%	-26.0%
Impairments as % revenue, IFRS9 basis					-21.8%	-23.0%
Agent costs as % revenue	-19.7%	-20.4%	-21.3%	-20.2%	-22.4%	-22.3%
Admin. costs as % revenue	-36.5%	-36.8%	-33.1%	-31.0%	-33.1%	-32.4%
Total costs as % revenue	-56.2%	-57.2%	-54.4%	-51.2%	-55.5%	-54.7%
Finance costs as % average debt	N/M	N/M	9.5%	11.7%	11.5%	11.7%
Revenue yield (revenue as % average receivables)	N/M	164%	170%	175%	163%	173%
Number of clients	198,171	198,727	216,000	229,000	232,000	235,000
Number of agents	1,893	1,839	1,826	2,030	1,900	1,900
Adj. profit per client	66	84	82	84	94	105
Receivables per agent	29,310	30,903	33,531	35,876	38,926	40,427

*Source: MCL, Hardman & Co Research * IFRS 9 basis*

Impact of discounting

Management has previously highlighted that the accounting requirement to gross up income and then provide against it (in situations where the customer has missed a payment but is still expected to repay) distorts the balance sheet and profit and loss. As can be noted in the table below, with a growing book, the distortion increases. As illustrated in the table below, the impact under IFRS 9 is higher than under IAS39.

Underlying asset value							
£m	**Feb 16**	**Aug 16**	**Feb 17**	**Aug 17**	**Feb 18**	**Aug 17 *****	**Aug 18 *****
Gross balances*	117.6	114.3	122.9	127.8	137.7	127.8	135.7
Gross cash projection**	87.8	86.6	93.9	99.1	110.2	99.1	108.3
Impact of discounting	-31.0	-30.4	-32.7	-34.0	-37.4	-36.4	-40.3
IFRS bal. sheet value	56.8	56.2	61.2	65.1	72.8	62.7	68.0
Discounting impact as % gross	26.3	26.5	26.6	26.6	27.1	28.5	29.8
Marginal impact on P/L of discounting		0.6	-2.3	-1.3	-3.4		-3.9

*Source: Hardman & Co Research * cash amount contractually due, ** cash actually expected to be received *** IFRS9 basis*

Balance sheet

Balance sheet						
@ end-February (£000)	2015	2016	2017	2018	2019E *	2020E *
Non-current						
Goodwill	294	1,326	2,834	2,834	3,334	4,000
Intangible assets	10,391	9,052	7,058	5,520	4,328	3,504
Property, plant and equipment	936	1,182	763	822	647	794
Amounts receivable from customers	1,507	679	395	265	200	100
Deferred tax	0	0	0	0	927	927
Total non-current assets	13,128	12,239	11,050	9,441	9,436	9,325
Current assets						
Receivables	53,976	56,152	60,833	72,563	73,760	76,711
Trade/other receivables	26,216	1,554	2,019	2,039	1,554	1,554
Cash and cash equivalents	8,650	3,755	3,985	4,868	5,756	6,406
Total current assets	88,842	61,461	66,837	79,470	81,070	84,671
Total assets	101,970	73,700	77,887	88,911	90,506	93,995
Current liabilities						
Trade and other payables	-3,274	-7,452	-5,892	-6,695	-7,695	-8,695
Total current liabilities	-3,274	-7,452	-5,892	-6,695	-7,695	-8,695
Net current (liabilities)/assets	85,568	54,009	60,945	72,775	73,375	75,976
Non-current liabilities						
Financial liabilities – borrowings	0	-9,000	-10,000	-15,552	-14,000	-10,000
Deferred tax	-2,614	-1,879	-617	-144	0	0
Total non-current liabilities	-2,614	-10,879	-10,617	-15,696	-14,000	-10,000
Total liabilities	-5,888	-18,331	-16,509	-22,391	-21,695	-18,695
Net assets	96,082	55,369	61,378	66,520	68,811	75,300

*Source: MCL, Hardman & Co Research * IFRS9 basis*

Cashflow

Cashflow statement						
Year-end February (£000)	2015	2016	2017	2018	2019E *	2020E *
Profit (loss) before tax	58,565	10,374	11,219	16,133	18,634	21,740
Depreciation	596	736	544	563	575	453
Impairment of goodwill	56	42	0	0	0	0
Amortisation of intangibles	8,574	5,683	4,412	2,950	2,630	2,890
Share-based payment expenses	0	0	126	431	431	431
Gain on acquisitions	-51,961	-32	0	0	0	0
Loss on disposal of plant, property and equipment	40	146	134	0	0	0
(Increase)/decrease in debtors	-14,803	27,532	-1,918	-11,604	-1,675	1,225
Dividend in Specie to Perpignon	0	-31,129	0	0	0	0
Increase/decrease in creditors	4,768	2,548	-1,640	1,846	1,000	1,500
Interest paid	1	647	927	1,456	1,700	1,400
Taxation paid	-800	-1,737	-4,078	-4,536	-4,865	-5,250
Net cash inflow/(outflow) from op. activities	5,036	14,810	9,726	7,239	18,430	24,388
Cashflows from investing activities						
Purchase of intangibles	-416	-2,523	-1,029	-1,412	-1,531	-2,082
Purchase of property, plant and equipment	-343	-1,152	-125	-622	-400	-600
Disposal of assets	0	501	0	0	0	0
Purchase of subsidiaries	0	-7,383	-5,695	0	-2,000	-4,000
Cash acquired on acquisitions	5,120	0	0	0	0	0
Net cash outflow from investing activities	4,361	-10,558	-6,849	-2,034	-3,931	-6,682
Cashflows from financing activities						
Net borrowing	0	9,000	1,000	6,000	-1,552	-4,000
Interest paid	-1	-647	-927	-1,904	-1,700	-1,400
Dividends	-2,000	-17,500	-2,720	-8,418	-10,360	-11,655
Net cash inflow from financing activities	-2,001	-9,147	-2,647	-4,322	-13,612	-17,055
Net increase in cash and cash equivalents	7,396	-4,895	230	883	887	651
Opening cash and cash equivalents	1,253	8,650	3,755	3,985	4,868	5,756
Closing cash and cash equivalents	8,650	3,755	3,985	4,868	5,756	6,406

*Source: MCL, Hardman & Co Research * IFRS 9 basis*

Valuation

Average valuation upside on absolute measures 34%

We detailed all the assumptions used in our valuation methodologies in our note, Bringing home collect into the 21st century, [published on 2 February 2017]. Post these changes, our absolute valuation techniques now imply an average of 201p. The peer valuations have a range of 143.9p to 201.4p and an average of 172.6p.

Summary of different valuation techniques

	Implied price (p)	Upside (%)
Gordon Growth Model (GGM)	222.7	49%
Dividend Disc. Model (DDM)	178.9	19%
Average absolute measures	200.8	34%
Peer 2017 P/E	143.9	-4%
Peer 2017 yield	201.4	34%
Average peers	172.6	15%

Source: Hardman & Co Research

GGM

We have advanced our base year to February 2020, which sees an uplift of ca.20p per share.

GGM and sensitivities

	Base	+1% ROE	+1% COE	+0.5% G
Return on equity (%)	25	26	25	25
Cost of equity (%)	11	11	12	11
Growth (%)	5.5	5.5	5.5	6
Price/book value (x)	3.5	3.7	3.0	3.8
Premium for near-term outperformance (%)	20%	20%	20%	20%
Adjusted price/book value (x)	4.3	4.5	3.6	4.6
Book value 2020E (£m)	67.8	67.8	67.8	67.8
Valuation (£m)	288.4	303.2	244.1	309.2
Valuation per share (p)	222.7	234.2	188.5	238.7
Variance (per share)		11.4	-34.3	16.0

Source: Hardman & Co Research

Broad peer comparisons

MCL is trading at a material discount to peers on a price earnings and yield basis. The share price volatility of peers such as PFG has seen sharp changes in these measures.

Peer valuation comparisons

	Share price (p)	Market cap (£m)	2018 PE (x)	2018 yield (%)
MCL (Feb'19)	**149.75**	**194**	**11.1**	**5.3%**
NSF (Dec)	64.2	200	15.8	3.8%
PFG (Dec)	533	1,350	10.3	1.8%
S&U (Jan'19)	2080	250	8.6	5.8%
H&T	272	102	9.1	4.1%
Ramsdens (Mar'18)	164	51	9.7	4.3%
Amigo	218	1,038	n/a	n/a
Average peers			10.7	4.0%
MCL price at peer average			143.9	201.4

Source: Hardman & Co Research

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(Disclaimer Version 8 – Effective from August 2018)

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