morsesclub

2021 Interim Results

Paul Smith – CEO
Andy Thomson – Interim CFO

18 December 2020

Highlights

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H1 2021 has been a significant catalyst towards our vision of becoming a more complete financial services provider

Group

Resilient response to Covid-19, quickly leveraging existing technology and expertise

Financially robust with no staff furloughed or government assistance sought

HCC

Q3 HCC lending running at 69% of FY20 levels, with collections at 76%

Very positive customer response to cashless lending and remote collections model

Digital

Transition of banking and credit platforms onto two new providers to enhance offering to customers

Digital sales and collections significantly improved with sales currently 30% ahead of FY20

Better positioned to take advantage of opportunities in the growing and fragmented non-standard finance credit market

Strategic Roadmap

H1 21 – Rapid Response to Covid-19

Digital focus and capabilities enabled Morses Club to react quickly and effectively to changing customer needs during Covid-19 pandemic

- March – UK Government implements Covid-19 restrictions
- March – all staff begin to work from home. Currently 90% employees satisfied working from home
- April – Extension of RCF to end November 2021
- April – Launch of remote lending product
- July – 109k customers signed up to customer portal
- July – Re-commencement of lending to new HCC customers
- July – Complete realignment of property strategy leading to exit from c. 94 field offices. 20 leases remain with full exit planned in 2021
- August – Strategic contract agreed with Modulr for U Account

No staff furloughed and no government assistance sought

Continued re-engineering of online businesses

Growing levels of lending and encouraging uplift in demand for longer-term digital lending products evident

Increased digitalisation, moving towards a more comprehensive financial services offering morsesclub

Strategic Roadmap

H2 2021 → **FY22**

- Appointment of Graeme Campbell as CFO
- Launch of improved mobile App for U Account
- Launch of Loan management platform – launchpad for next phase of digital strategy
- Transfer of U Account operating platform to Modulr
- Positive response to digital Refer-a-Friend scheme launched in September, prior year referral scheme – 37,000 new customers
- Customer payment performance in October 2020 was 96% of last year
- £43.3m HCC sales executed digitally in 8 months to October 2020
- c.65% lending now completed digitally
- Enabling of virtually paperless loan documentation process
- Further affordability developments planned to keep pace with regulation and TCF principles
- 78% cash collections now made remotely
- 124,000 customers registered on digital customer portal as at December
- 1,451 sales completed via digital Refer-a-Friend, with 32% conversion rate (Dec)
- Banking and credit offering due to be launched in H2
- Break-even of Digital division forecast during FY22

Group-wide project set up to continue re-engineering of business to support digital transformation - Flexible Future

Key stats (HCC)

	Customers signed up to online customer portal	Loans delivered digitally	Customer satisfaction	Cash collected remotely
Pre-Covid-19	**78,000**	**17%**	**97%**	**39%**
Current	**124,000**	**65%**	**97%**	**78%**

Financial Review

Financial Highlights

Results impacted by Covid-19, both in terms of the opening loan book as highlighted in our post balance sheet events FY20 announcement and supressed trading due to weak customer demand, operational transformation and lower risk appetite in this unprecedented crisis

	Group	HCC	Digital
Credit issued (£m)	**60.2** (HY20: 91.0)	**51.1** (HY20: 85.5)	**9.1** (HY20: 5.5)
Adjusted profit before tax (£m)	**2.3** (HY20: 9.6)	**6.8** (HY20: 13.1)	**(4.5)** (HY20: (3.5))
Statutory profit before tax (£m)	**0.8** (HY20: 6.7)	**5.6** (HY20: 11.7)	**(4.8)** (HY20: (5.0))
Customer numbers (000's)	**205** (HY20: 276)	**170** (HY20: 224)	**35** (HY20: 52)
Net loan book(£m)	**55.6** (HY20: 72.2)	**50.4** (HY20: 68.2)	**5.2** (HY20: 4.0)

Interim Dividend proposed of 1.0p (HY20: 2.6p)

Income Statement – HCC

£'m unless otherwise stated

	H1 FY21	H1 FY20	Move
Customer numbers ('000's)	170	224	(54)
Period end receivables	50.4	68.2	(17.8)
Average receivables	61.5	69.9	(8.4)
Revenue	44.2	59.4	(15.2)
Impairment	(8.3)	(10.9)	2.6
Agent commission & other cost of sales	(10.3)	(14.4)	4.1
Gross profit	25.6	34.1	**(8.5)**
Admin expenses	(16.2)	(18.1)	1.9
Depreciation	(1.9)	(1.7)	(0.2)
Normalised operating profit	7.5	14.3	(6.8)
Financing costs	(0.7)	(1.2)	0.5
Adjusted PBT	**6.8**	**13.1**	**(6.3)**
Covid impact identified in PBSE	4.3	-	4.3
Normalised adjusted PBT	**11.1**	**13.1**	**(2.0)**
Impairment/revenue %	18.8%	18.4%	(0.4%)
Agent commission/revenue %	23.3%	24.2%	0.9%
Admin (inc Depr) exp/revenue %	41.0%	33.3%	(7.6%)

Commentary

- Reduced credit issued:
  - £51.1m v £82.2m last year over 26 weeks and £85.5m last year over 27 weeks reported
  - Due to the time taken to be able to sell remotely and weak customer demand
- As a result revenue fell by (25.6%)
- Impairment remained close to last year at 18.8% versus 18.4% as the additional cost of write-off was offset by favourable discounting impact under IFRS9 as loan book shrank
- Savings in Admin and Depreciation costs of £1.7m
- Reduced financing costs reflecting reduction in loan book

Income Statement – Digital

£'m unless otherwise stated

	H1 FY21	H1 FY20	Move
Customer numbers ('000's)	35	52	(17)
Period end receivables	5.2	4.0	1.2
Average receivables	5.4	1.7	3.7
Revenue	6.0	6.9	(0.9)
Impairment	(3.5)	(1.6)	(1.9)
Agent commission & other cost of sales	(0.3)	(0.4)	0.1
Gross profit	2.2	4.9	**(2.7)**
Admin expenses	(5.9)	(7.6)	1.7
Depreciation	(0.2)	(0.5)	0.3
Normalised operating profit	(3.9)	(3.2)	(0.7)
Financing costs	(0.6)	(0.3)	(0.3)
Adjusted PBT	**(4.5)**	**(3.5)**	**(1.0)**
Covid impact identified in PBSE	0.9	-	0.9
Normalised adjusted PBT	**(3.6)**	**(3.5)**	**(0.1)**
Impairment/revenue %	58.3%	23.2%	(35.1%)
Other cost of sales/revenue %	5.0%	5.8%	0.8%
Admin (inc Depr) exp/revenue %	101.7%	117.4%	15.7%

Commentary

- Credit issued increased by 65% to £9.1m from £5.5m last year
- Period end net receivables increased by 30% to £5.2m from £4.0m last year
- Customer numbers were flat as the 17k headline reduction was due to tightening the classification of a live customer in Dot Dot Loans
- Last year revenue included the collect out of the acquired CURO Transatlantic Limited book – also explains why last year's impairment was abnormally low
- £2.0m cost reduction despite a full period of U Money (last year 2 months only)
- Whilst the normalised loss before tax is the same as last year, this is due to a number of one-off favourable impacts. The overall trajectory is positive
- Expected impairment range for Digital lending of 45%-55%, in line with business plan

Post balance sheet event – impact of Covid-19 (FY20)

£'m

Amounts recognised in H1 FY21 compared to FY20 PBSE reported

- The table below summarises the actual impacts of Covid-19 on the closing loan book as at February 2020 that were recognised in the first half year accounts compared to the indications the company gave in their FY20 accounts
- It should be noted that the increased write off in HCC (£4.9m of the £5.8m expected credit losses) was largely offset by the reduction in discounting cash flows under IFRS9 as the loan book shrank significantly during the period. This means that the actual impairment charge was broadly in line with last year (18.8% v 18.4%)

	Incurred	PBSE	Variance
Increased expected credit losses	5.8	5.8	0.0
Loss of forward flow income	0.6	0.3	(0.3)
Extended loan lives	0.6	0.8	0.2
Total	7.0	6.9	(0.1)
Less: IFRS9 provision recognised in FY20	(1.7)	(1.7)	0.0
Net post balance sheet event	5.3	5.2	(0.1)

Balance Sheet

£'m

	Aug-20	Aug-19
Non current assets		
Goodwill	13.0	13.3
Acquisition intangibles	0.6	0.8
Software and licences	8.3	6.6
Plant and equipment	0.8	0.8
Right of use asset (IFRS16)	2.1	3.6
Deferred tax	0.7	0.9
Total fixed assets	25.5	26.0
Current assets		
Trade receivables inc>12 mths	55.6	72.2
Cash and cash equivalents	6.5	7.5
Other current assets	7.8	4.1
Total current assets	69.9	83.8
Total assets	**95.4**	**109.8**
Liabilities		
Loan facility	(14.0)	(23.0)
Lease liabilities (IFRS16)	(2.3)	(3.5)
Trade and other liabilities	(7.3)	(13.0)
Total liabilities	(23.6)	(39.5)
Net assets	**71.8**	**70.3**
Net tangible assets inc software	58.2	56.2
Trade receivables/net assets	77.4%	102.7%

Commentary

- Small increase in total equity reflecting small statutory profit and no dividends in the period
- Continued investment in our technology platforms reflected in software and licences
- Period end net loan book £55.6m, down 23% compared to last year reflecting temporary loss of lending capability, weak demand and reduced risk appetite
- Loan facility drawn significantly reduced to £14m from £23m at the end of August last year reflecting cash generated from loan book reduction
- Trade and other liabilities in Aug-19 included (£3.9m) of deferred consideration and a corporation tax liability of (£1.4m) which is a £1.5m asset in Aug-20
- Current debt facility extended one month to end of December 2021. Renegotiation period will commence well before this date

Cash Flow

£'m

	H1 FY21	H1 FY20
Cash from operations ex invest in loan book	4.9	18.4
Cash from funding	-	8.5
Decrease in net loan book	16.6	0.7
Total Cash Sources	21.5	27.6
Repayment of funding	(20.0)	-
Acquisitions	0.0	(14.0)
Purchase of intangibles	(2.9)	(2.6)
Capital expenditure	(0.3)	(0.9)
Principal paid under lease liabilities	(0.8)	(0.7)
Corporation tax	(1.2)	(1.8)
Interest paid and arrangement fee	(1.6)	(1.3)
Dividends paid	0.0	(6.7)
Total Cash Uses	(26.8)	(28.0)
Cash Movement	**(5.3)**	**(0.4)**

Commentary

- Operational cash flows much reduced but still positive reflecting the profit in the period
- Significant positive cash flows due to reduction in the size of the loan book
- This enabled a significant reduction of the loan balances of £20.0m, reducing the year end debt position of £34.0m down to £14.0m
- No dividends were paid in the period, however the previously reported 1.0p final dividend for FY20 to be paid in February 2021 subject to shareholder approval
- A further interim dividend is proposed of 1.0p to be paid in April 2021

Summary and Outlook

Summary and Outlook

Continued progress made in H1 2021 with further milestones targeted in H2 2021 to fulfil vision of becoming a more complete financial services provider

- Rapid response to Covid-19, assisted by clear strategy and ongoing digitalisation, ensured effective operational procedures and robust financial position
- Realignment of property and working practices, with staff continuing to work from home
- Decline in HCC customer numbers and loan book but improving collections and digital engagement
- Digital sales and collections significantly improved, with credit issued 65% ahead of HY20 and breakeven forecast during FY22
- Re-engineering of business to support digital transformation, with new App and operating system for U Account, along with launch of loan management platform
- Proven demand for additional products in a large and underserved market
- Banking and credit offering to launch in H2 2021
- Current economic situation makes short-term outlook difficult to predict, but contracting credit supply expected to present opportunities
- Interim dividend of 1.0p proposed demonstrating Board confidence

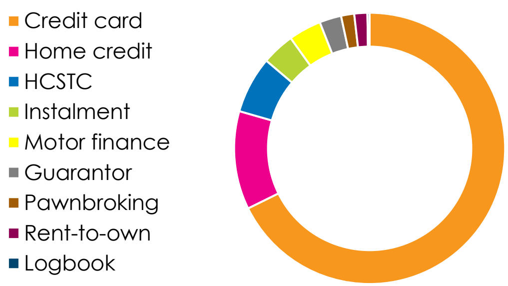
Appendices

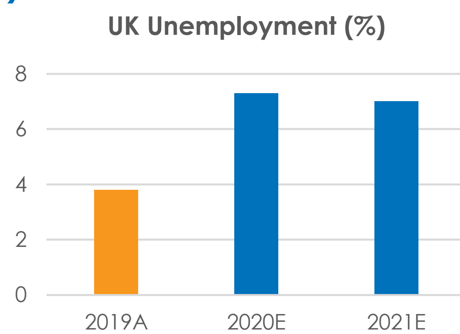
Reconciliation of adjusted profit before tax to statutory profit before tax

£'m (unless otherwise stated)	26-week period ended 29 August 2020	27-week period ended 31 August 2019	Increase / (decrease)
Statutory Profit Before Tax	**0.8**	**6.7**	**(88.1%)**
Amortisation of acquired intangibles[2]	0.2	0.5	**(60.0%)**
Gain arising on acquisitions	-	(0.6)	**n/a**
Non-recurring costs[3]	1.3	3.0	**(43.3%)**
Adjusted Profit Before Tax[1]	**2.3**	**9.6**	**(76.4%)**
Tax on Adjusted Profit Before Tax	(0.4)	(1.9)	**(78.1%)**
Adjusted Profit After Tax	**1.8**	**7.7**	**(75.9%)**
Adjusted EPS[1]	**0.6**	**5.9**	**(90.4%)**
Adjusted Return on Assets[1]	9.9%	24.0%	**(58.8%)**
Adjusted Return on Equity[1]	13.4%	28.4%	**(52.8%)**

The Non-Standard Credit Market

New lending by non-prime segment (2018)[5]





9m people have no savings at all[6] and 7m people have savings of less than £100[7]

10-12m customers have difficulty accessing credit from mainstream financial institutions

£10.7bn total loan receivables across UK non-prime consumer credit[2]

Non-Standard Credit Market expected to grow as supply contracts

Economic conditions likely to push some prime borrowers into non-standard market. Currently circa **2m** people move between standard and non-standard markets due to credit scores[2]

3 million consumers use high cost credit (excluding overdrafts) including rent-to-own, catalogue credit, store cards and HCC[2]

Gross loan receivables for the largest active firms up by **41%** in two years to 2017/18, and net receivables (after impairments) up **32%**

The availability of unsecured consumer credit fell for a **12th** successive quarter in the fourth quarter of 2019[5]

Lenders also further tightened their lending standards for unsecured consumer credit for a **13th** successive quarter[5]

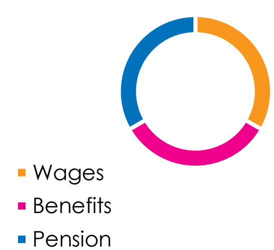
Reduced number of non-standard credit market providers presents opportunities for **market share gains** in online lending and wider market

Economic impact of Covid-19 anticipated to **increase customer numbers** within sub-prime market

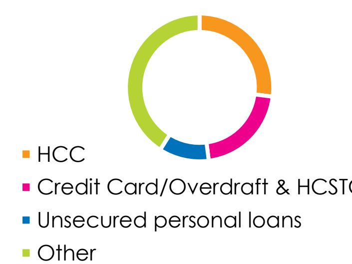
HCC

£1.1bn market | **1.6m users[3]**

Typical HCC customer income sources



Typical HCC customer personal debt



(1) High Cost Credit Review ANNEX 1 - July 2017
(2) Source: Company accounts, Apex insights analysis, FCA market statistics
(3) FCA High Cost Credit Review Technical Annex 1: CRA data analysis of UK personal debt – July 2017
(4) FS17/2: High-cost credit and review of the high-cost short-term credit price cap
(5) Apex Insight - Non-Prime Consumer Credit: UK Market Insight Report - September 2019
(6) Scottish Widows Savings Report 2014
(7) BBC - Millions have less than £100 in savings, study finds
(8) ONS data and HM Treasury forecasts for the UK economy (October 2020)

Strategy: Meeting customer demand for additional products

Feedback from HCC customers:

Up to **65%** of customers **interested in Morses Club current account**

Up to **72%** interested in **using account for money transfers**

Up to **63%** interested in **credit limit current account**

Up to **79%** of customers **aware of portal**

Up to **73%** interested in **having income paid into account**

Up to **32%** of customers **have a credit card**

Up to **73%** interested in **having bills paid from account**

Up to **43%** **use their card for emergency cash**, with up to 36% using it for cash withdrawals

Up to **73%** interested in **setting up direct debits from account**

For HCC customers, **27%** of their credit need is met by HCC; a further **21%** is met by credit card, overdraft and HCSTC, and **11%** in 'other' unsecured personal loans – our multi-product offering means that we can now support an incremental **32%** of their debt requirements

morsesclub putting you first		Dot Dot loans / LOANS
Not working / benefits / part time and casual	Income Source	Full-time / salaried / 15-20% self-employed
Below national average (£10-15k)	Income Levels	Around national average (£20-30k)
Rented accommodation / social housing	Housing	Renters / c.20% mortgages
35-64 years >80%; 18-34 years 100%	People with bank account by age	25-44 years 100%; 35-54 years 100%
Limited or no savings	Savings	Some savings for specific goals

	Morses Club	Shelby Finance			
			U.MONEY		
Brand	morsesclub putting you first	Dot Dot Loans	LOANS	E DRAFT	U ACCOUNT
Market	Short term	Short term	Long term	Revolving	Current Account
Duration	22 – 53 weeks	3 – 12 months	18 – 48 months	Revolving	N/A

Strategy: Targeting a large and underserved market

Underserved 20.2 million adults

Struggling
- 10.2m adults
- Working age
- Reliant on benefits
- Underserved / excluded

Fintechs struggling with dormancy and fraud

Pockit
0.4 million customers

SUITS ME.
0.6 million customers

Squeezed
- 10.1m adults
- Working age
- Lower income
- Underserved / excluded

There is space in our target market

U ACCOUNT

cashplus
>2 million customers

thinkmoney
0.1 million customers

Mainstream 31.7 million adults

Millennials
- 11.2m adults
- Working age
- Mixed income range
- Tech savvy

Established fintechs in this market – becoming saturated

monzo
>13 million customers

Revolut
>10 million customers

STARLING BANK
>1 million customers

Other
- 20.5m adults

High street banks still have the mainstream majority

HSBC

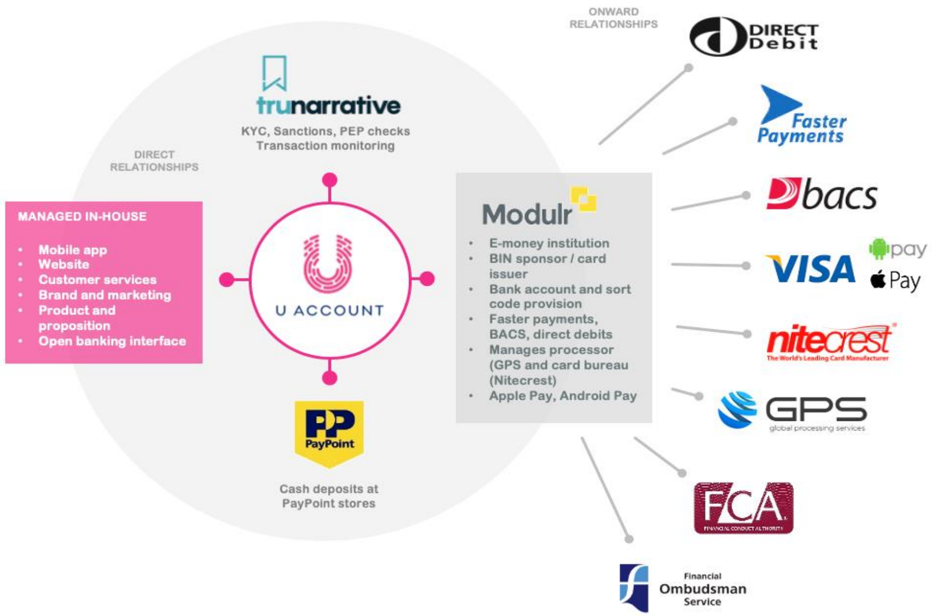
BARCLAYS

LLOYDS BANK

RBS

Strategy: Creating a competitive offering

Partnering to improve upon competing products



Strategy

- Customer needs at the heart of Morses Club's technology strategy
- Continued transformation of working practices - technology and service central to Agent model
- Create innovative, robust, compliant, secure and scalable digital products
- Expand service proposition linked to service model to build share of customer wallet

Near-term deliverables

- Launch of rebranded credit suite for U Account customers at end H2 FY21 including revolving credit product and longer-term loans
- New loan management platform will integrate linked banking and credit products – H2 FY21
- U Account product to be offered to selected HCC customers
- Increased penetration of customer portal by development of wider financial services – pull marketing, rather than push
- Launch of new products and services via Portal to help customers manage their budget and access wider financial services