# Pioneer Credit Ltd AUD40m 90 day BBSW+[5.25]% [22] March 2022 secured and subordinated notes

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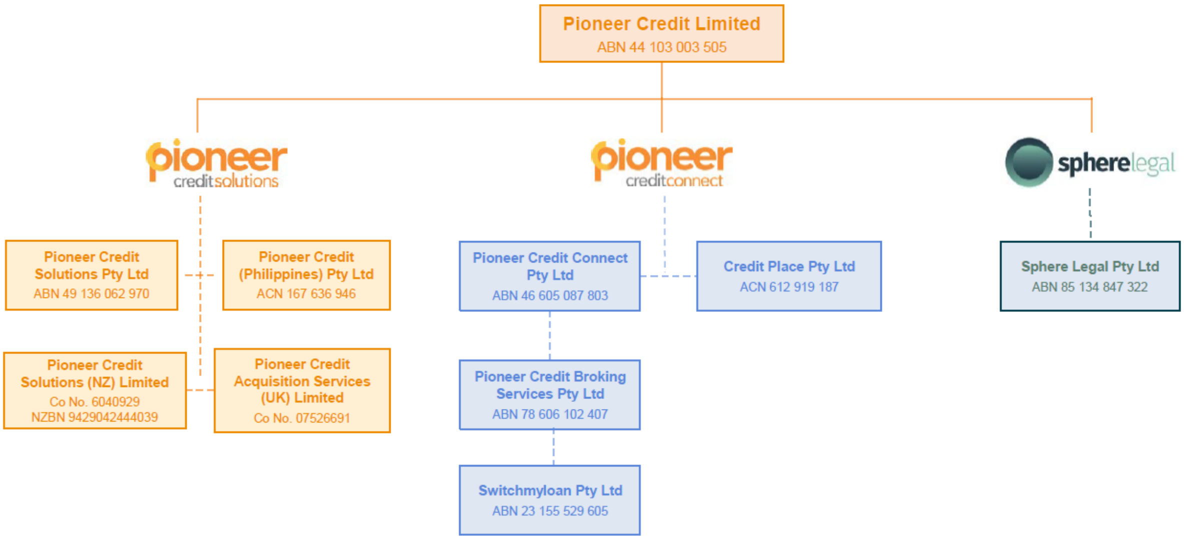
## Issuer outline

Pioneer Credit Limited (Pioneer) is an ASX–listed financial services provider (ASX: PNC) with 180,000 customers across Australia and New Zealand. Pioneer specialises in acquiring and servicing unsecured retail debt portfolios (Purchased Debt Portfolios or PDP) as well as introducing brokered personal credit and loan products.




Source: Company reports

Pioneer's primary business, Pioneer Credit Solutions (Solutions), involves the acquisition and servicing of unsecured consumer retail debt portfolios. These portfolios consist of people with financial obligations to Pioneer and are primarily comprised of personal loans and credit card accounts that are generally more than 180 days overdue. Portfolios are acquired at a discount to their face value and Pioneer works with customers to facilitate payment of the account over time. Through this process, customers progress towards financial recovery and evolve to become "new consumers". This business accounted for materially all of Pioneer's customer payments revenue in FY17. There are currently over 40,000 eligible customers within the Solutions business. Over 65% of these customers have paid more than 75% of their debt including interest. Of these customers approximately half are under 35 years old.

Pioneer Credit Connect (Connect) was launched in late 2016 as the brand for 'emerging prime' credit consumers in Australia, helping customers access appropriate financial products to reach their goals. The foundation of the Connect business is centred on extending Pioneer's relationship with customers beyond their initial account; providing customers with education and products to strengthen their financial health; and attracting new customers to Pioneer.

Connect provides a range of financial products to its customers who are in a position to broaden their financial capacity as well as new to Pioneer customers who have similar characteristics. The two core products offered through Connect are home loans under a traditional broking model or via the direct-to-lender business 'SwitchMyLoan'; and white-labelled personal loans, in partnership with Goldfields Money Limited (Goldfields Money; ASX: GMY).

In November 2016, CreditPlace was launched and provides a platform for customers to understand their financial health. CreditPlace already engages with 'emerging prime' target customers, providing them with their credit score (in partnership with Experian Australia Credit Services and Equifax Inc) free of charge and an explanation of what that score means. This platform empowers customers in making financial decisions and also underpins Connect's customer engagement strategy.

Pioneer is headquartered in Perth, Western Australia with representative offices in Sydney, Melbourne, Brisbane and Manila, in the Philippines. Pioneer has over 500 employees.

Pioneer's near term growth strategy is centred on increasing market share and responding to high yield PDP opportunities. Additionally, over FY18 Pioneer will focus on growing the Connect business by expanding its financial product offering and increasing engagement with new customers.

*Please refer to the Investment Memorandum (IM) and company website for full details on the company and transaction.*

**LTM financials as at 31 December 2017**
Revenue: AUD68.5m
EBITDA: AUD47.1m
Net interest expense: AUD2.6m
PDP valuation: AUD197.6m
Total assets: AUD214.8m
Total debt: AUD101.5m
Gearing (debt/loan book value): 51.4%
Net debt/EBITDA: 2.04x
EBITDA/interest expense: 18.1x

## ISIN
[TBA]

## Trading information
Minimum: AUD50,000
Denominations: AUD1,000
Wholesale clients only

## Coupon
Coupon type: Floating

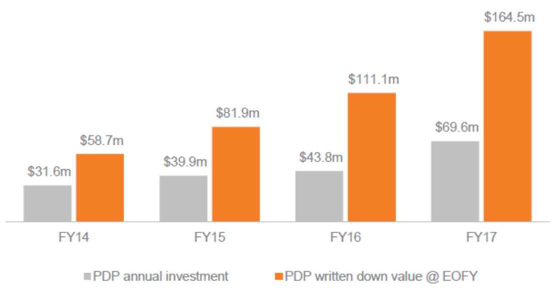
Rate: 90day BSW+5.25%
Payment frequency: Quarterly

### Important dates
Issue date: [22] March 2018
Maturity date: [22] March 2022
Optional redemption date: [22] March 2021 @ 101% of par

### Structure
Type/rank: Subordinated secured notes
Domicile: AUS
Currency: AUD
Amount issued/Outstanding: AUD[40]m/AUD[40]m
Issuer credit ratings: NR
Issue credit ratings: NR
AU Withholding Tax Exempt: Yes

### Strengths
- **Only high-quality portfolios acquired:** Pioneer Solutions primarily acquires Tier 1, high-quality debt portfolios from major banks and financial institutions in Australia and New Zealand. Pioneer has relationships with major originators and sits on all big four Australian bank debt sale panels. Pioneer currently has Forward Flow Agreements (FFAs) with three major Australian banks. Pioneer develops these relationships by actively differentiating itself in the PDP market. This is achieved by providing purchase certainty for vendors through strict investment discipline, delivering price points that underpin a reputation-based, customer centric servicing standard and demonstrating a strong track record of compliance.
  Pioneer seeks to only purchase portfolios that it understands well and has the competency and experience to conduct due diligence on, price appropriately and then recover an amount that is at least in line with its expectations at the time of purchase. Pioneer has not and does not acquire accounts from telecommunication providers, utilities or government agencies. Pioneer does not invest in any form of "payday lending" including small amount credit contracts (SACC) and medium account credit contracts (MACC). Pioneer's investment policy stipulates that it will not invest in any form of payday lending.
- **Value based framework:** Pioneer's customer-centric strategy leads to improved credit standing of customers, helps maximise likelihood of repayment and fosters loyalty. Equally, Pioneer believes this philosophy is looked on favourably by vendor partners due to its high quality outcomes and additional benefits that flow to the brands of not only Pioneer but its partners. This assists Pioneer to achieve market-leading PDP acquisition pricing and utilisation, and also bolsters its ability to provide alternative financial products to customers through Pioneer Connect.
- **Diversified customer base:** Since listing on the ASX in May 2014, Pioneer has successfully broadened its vendor mix to include 19 partners. Pioneer's customer base is geographically distributed across Australia (representative of the national population) and New Zealand. This helps limit concentrations of credit risk in the portfolio as a result of regional economic pressures.
- **Strong regulatory outcomes:** Pioneer's position in the market is unique, having never had a negative outcome with the Ombudsman, never having had a reportable systemic issue and never having had to provide a regulatory enforceable undertaking.

- **Growth in personal lending from niche borrower base:** While Pioneer's Connect business is in infancy, Pioneer's customer centric business model means it has access to a niche set of customers. Historically, Pioneer's customers have had the ability to manage and repay their obligations in full. Utilising this track record, strong credit risk analytics and CreditPlace insights, Pioneer is able to identify 'emerging prime' customers. 'Emerging Prime' is a term used by Pioneer to describe customers who are showing evidence of rehabilitation from the life event which caused their initial default. Evidence may include a strong payment history with Pioneer, stable employment, improving credit scores and evidence of serviceability. Importantly it is the customer's credit score trajectory which indicates that they will become prime borrowers even though at present they may be below major banks' scorecard cut-offs or policy. Pioneer calls the program to rehabilitate these customers the Pathway to Prime, which includes free credit scores, financial literacy education and a budgeting app (Pioneer Path) to assist in achieving financial goals.
- **Competitive advantage:** Pioneer's premium data analytics facilitates selection of lower risk portfolios, which are considered 'Tier 1' customer portfolios.
- **Rigorous credit assessment:** Pioneer adopts rigorous credit assessment and risk frameworks within its Connect business. Connect's lending criteria dictates that approved applicants meet legislative requirements and fulfil minimum serviceability requirements. Customers must pass the application process which includes a clear recent bureau history, income validation, responsible lending criteria and assessment by the underwriters. Connect's overall credit risk is managed to acceptable levels as dictated by the RAS (Risk Appetite Statement). Additionally, credit risk is managed by leveraging all available data at origination to make the best possible decision, adopting a 'low and grow' strategy to conservatively assigning new loan amount with good behaviour, taking security where possible and performing ongoing delinquency management and hardship leveraging internal core customer management capability.
- **Conservative PDP valuations with strong return on investments:** Pioneer's cautious and sophisticated PDP valuation approach includes a 9% downward calibration of gross forecasts and a 20.1% discount rate to present value the portfolio. On average, Pioneer pays less than 20c per $1 to acquire customer portfolios. The liquidation profile of portfolios is up to 10 years, however Pioneer receives 1.4x invested capital back within the first two years of portfolio acquisition, with up to 4x return realised by year 10. Pioneer continuously develops and improves its valuation models.


Source: Company reports

**Strong earnings performance and expected growth:** Pioneer's 1HFY18 PDP liquidations (revenue from PDPs) were AUD46.1m, net revenue was AUD36.8m, and EBITDA was $24.3m, up 60% on the prior comparative half year period. Pioneer has maintained consistent growth in PDPs by investing in portfolios with strong liquidation profiles at attractive price points. Pioneer has secured portfolio investments of AUD80m for FY18.

## Risks

- **Availability and pricing of debt portfolios:** In order to continue its profitable growth, Pioneer needs to be able to purchase debt portfolios at appropriate prices and manage the accounts comprising the portfolio to maximise recovery on those accounts. The availability of debt portfolios at appropriate prices is affected by a number of factors, including macroeconomic and operating conditions, some of which are outside Pioneer's control. Furthermore, increased competition in the PDP market could result in competitors offering higher prices for debt portfolios, which could result in lower margins for Pioneer, if Pioneer has to increase its portfolio acquisition costs.
- **Purchase of debt portfolios:** When Pioneer acquires debt portfolios from its vendor partners, it assumes the risk that the accounts within the portfolios will not be repaid in full or at all. However, a number of steps are undertaken by Pioneer before proceeding with an acquisition, in order to minimise this risk, including purchasing debt portfolios comprising of accounts Pioneer considers its core competencies (personal loans and credit cards) and purchasing accounts from reputable financial institutions, predominantly the major Australian banks.
- **Existing debt portfolios and recovery of accounts:** Pioneer purchases debt portfolios which often consist of a substantial number of accounts without contact details and for which the seller of the portfolio has made numerous attempts to collect. Such accounts may subsequently be deemed uncollectable and written off. Pioneer's strategy for maximising its customer payments over time is to minimise discounts offered for early payment and encourage customers who cannot meet the payment schedule under their existing loan agreement to enter into a new arrangement, known as a payment arrangement. Therefore, it may take a significant amount of time to recover on accounts and there is no guarantee that Pioneer will recover any or all of the accounts comprising a debt portfolio.
- **Inability to purchase new portfolios:** If the value of Pioneer's debt portfolios deteriorates, or Pioneer is unable to collect sufficient amounts on its portfolios, it may not be able to take advantage of opportunities for further portfolio purchases as they arise. Ultimately, all portfolios have a finite life and must be replaced with new portfolios.
- **Changes to macroeconomic factors:** Changes in macroeconomic factors such as an increase in interest rates and cost of living may impact on recovery of accounts. In addition, Pioneer may not be able to identify macroeconomic trends or make changes in its purchasing strategies in a timely manner.
- **Growth in personal lending:** Pioneer has established a personal lending business through Connect. Its ability to profitably scale this business is reliant on successfully attracting potential customers, applying an appropriate risk assessment framework to accurately determine a customer's credit risk and increasing personal loan sales, amongst other things. Failure to expand this business and achieve economies of scale may adversely impact Pioneer's ability to grow future profitability.
- **Defaults in personal loans:** The success of Connect depends on its ability to accurately assess a customer's ability to repay their debts in accordance with an agreed repayment schedule and within a certain period of time. As Connect is a lending business, Pioneer is at risk of borrowers failing to repay their loans. While loans are targeted at appropriate customers, loans are generally unsecured and subject to the capacity of the individual customer to repay them. Pioneer manages its credit risk in a

number of ways, including through strict customer screening and credit assessment processes.

- **Staffing:** Pioneer's success depends on identifying, hiring, training and retaining skilled personnel and senior management. Pioneer needs to retain its existing trained workforce and attract new personnel as it grows. Competition for such personnel is keen and there can be no assurance that Pioneer will always be successful in attracting and retaining such personnel. Pioneer is substantially reliant on the expertise and abilities of its key personnel in overseeing the day to day operations of its business. There can be no assurance given that there will be no detrimental impact on Pioneer if one or more of these employees cease their relationship with Pioneer.
- **Loss of key relationships:** A significant decrease in the volume of debt portfolios available for purchase from any significant vendor partner on acceptable terms would force Pioneer to seek alternative sources of portfolios to purchase. In addition to the factors that impact the supply of debt portfolios generally, vendor partners with whom Pioneer has strategic relationships may not continue to sell debt portfolios to Pioneer on desirable terms or in acceptable quantities, and Pioneer may not be able to replace such portfolios with portfolios from other debt vendors. The loss of a significant key relationship, or the loss of a number of key relationships at the same time, could prevent or restrict Pioneer's ability to purchase debt portfolios at current or forecast levels. This could impact profitability materially.
- **Regulatory and legislative risks:** Pioneer operates in an industry with a strict legal and regulatory framework. Any failure by Pioneer to comply with its ACL and applicable laws and regulations relating to the purchase of debt portfolios, collection on the accounts it acquires, the broader consumer credit industry and NCCP matters could result in the suspension, termination or impairment of Pioneer's ACL or the termination of certain FFAs and therefore could adversely affect Pioneer's reputation, its business and/or result in substantial losses. Changes in the regulatory environment relating to the credit industry generally could have an effect on Pioneer's future business, operations and financial performance
- **Noteholders are subordinated:** The payment obligations of the Issuer and the Guarantors under the Notes and Guarantee rank after, and are subordinated to, it's Senior Liabilities. Please refer to the IM for further details on Intercreditor Arrangements. We would expect recovery in an event of default to be low.
- **The market for these Notes may not be liquid:** If liquidity is low, there is a risk that, if you wish to sell your Notes prior to the Maturity Date, you may not be able to do so at a price acceptable to you, or at all. There is also a risk that the market price will become more volatile in general.

## Other risks

- Call risk: n/a
- Duration risk: n/a

## Summary

The Pioneer subordinated secured notes suit investors looking for a floating rate exposure to a growing financial services business in a niche market segment.

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