International Personal Finance plc
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Conference call transcript

Speaker key

JH John Harnett, CEO
DB David Broadbent, Finance Director
GR Gerard Ryan, CEO (Designate)

JH Good morning. I've got Dave Broadbent with me and also Gerard Ryan who's going to take over from me as CEO at the end of March. You'll hear a few words from him a little later on. I'm going to give you a bit of an overview on trading and outlook. Dave will talk a little bit about the balance sheet and capital structure and then we'll ask Gerard to say a few words just about his background and his early impressions of the business and then we'll open up for questions.

So I'll start then on trading. I thought 2011 was a good performance. We knew at the beginning of the year that we'd need to produce some strong growth if we were to offset the impact of high early settlement rebates and higher funding costs and we did that. And I think that performance was encouraging when you compare it alongside a reduction in impairment as a percentage of revenue. So we saw improved credit quality alongside strong growth, which is not always an easy combination.

I think there was some strong operating performances, [we were] particularly pleased with Poland, Hungary and Romania, but also pleased within the second half of the year [when] we saw a much better performance in Mexico - we really do feel that we've turned the corner there and tackled and sorted out a number of the basic issues. There's still some way to go in Mexico but it feels now that it's on an improving trend.

In terms of outlook, 2011 was a good year but we did see slowing growth in the second half, alongside reducing consumer confidence. It's encouraging that at the beginning of 2012 we've seen an uptake in consumer confidence in all of the European markets and alongside that we've been seeing stronger growth. And I think that gives us some degree of comfort as we set out this year to face some headwinds from increased early settlement costs of around £10 million to £15 million and, in terms of reporting, some adverse foreign exchange rates in translating our overseas profits, which as we've said in January were around 17% adverse. So we've got some mountains to climb this year but we did that in 2011 and I'm sure we can do that again this year.

Let me just hand over to Dave to talk about capital structure, balance sheet.

DB Yes, morning everybody, Dave Broadbent here. Just a couple of words. So good cash generation in the business this year - all of the growth and all the returns to investors have been self-funded. We've got, as you know, a very strong balance sheet with a high equity ratio in the business that finished last year at 58.5% and lower gearing of 0.8 times.

As John intimated and we've told you previously, we've looked at our target capital structure for the business and following lots of detailed analysis and stress testing and bearing in mind the uncertain outlook for the global economy in the debt capital markets, we've decided that maintaining a strong equity base is the right thing for the business at this point in time and we set our target capital ratio for around 55%. So that means that we recognise there is a small element of surplus capital in the business at the moment but we don't have any present intention to return that to shareholders or change to a different policy at this stage.

JH Okay and now perhaps before can take questions I can ask Gerard to give a quick overview of his background and some of his early impressions of the business.

GR Thanks John. Good morning, everybody, Gerard Ryan here. I joined the business about five weeks ago and John and I are doing a handover up to 31st March. From a background point of view, finance training is my background but I've spent the last 20 plus years in consumer finance businesses around Europe, initially about a dozen years in London, then four years in Edinburgh with GE followed by another four years with GE Money in Czech and Slovak Republics and then I moved down to Guarantee Bank in Turkey for a year and then with Citigroup in London for the past four years. So I've covered many of the markets that IPF currently operate in, which I think will be a big bonus.

I spent the first four weeks out of my five actually travelling the market. John’s doing all the heavy lifting with the year-end and it’s giving me an opportunity to go out and spend time with the local businesses in country, and so I've particularly spent time with the management teams and then with the frontend of the business, particularly with what we call our development managers and our agents. I've also done a lot of calls to customers with agents, so standard sales calls, collections calls and arrears calls, so that I get a real picture for how it works on the ground with a view to having a good in-depth knowledge of the business before John hands over to me officially at the end of March.

One of the reasons I joined the business was the growth agenda that the chairman and the board outlined to me during our discussions and I'm very happy to say that everything I've seen during the past five weeks supports what I was told. I would say that I'm very optimistic from what I've seen in terms of the opportunities that are in front of us in our existing markets and potentially in other markets but there is no need for us to rush at that at the moment. But certainly our existing businesses have lots of room to grow and that's what I'll be focusing on over the coming weeks and months.

JH Thanks, Gerard. I think that completes our formal part of this, so let's now take questions and we can hand back to the operator.

Delegate 1 Good afternoon, chaps. Could you say something about the FX hedging? Last month when you fixed some in, you did I think 70% of the projected targets for the year. That's a little bit less than usual and I appreciate that it's probably because rates at that stage were against you. What do you plan on doing with the rest, just letting it play out or do you plan on having a second go at some more hedging?

DB You're right, we've covered about 70%; that would be similar to what we'd normally do in the January with a view to topping up around the half year. Obviously one of the key things we take to account is how far into the year you are, so at the half year we'll have a really good read in terms of what we expect [at] the full year and therefore we'd look to take that hedging percentage up. So we might do it before July, but at the moment our intention will be to top it up around then just after the half year.

Delegate 1 Okay, that's fine. And the second question I have, just before I get off, is on Czech/Slovakia; that seems to have been the area in Europe that perhaps is just a tad quiet. I'm just wondering, could you give us a bit of a heads-up on what's happening there?

JH I think if you looked at the growth in credit issued and receivables, Czech/Slovakia was much like Poland. The difference really was that its customer growth was light of where we thought it should be. We were looking for something more like 7% and we got 4%, so that was disappointing. I think we've had a situation in the country where agents and, to some extent, managers have been focusing on lending to existing customers rather than growing by increasing new customers. To be frank, that's a lower risk option and they've been pretty successful at getting the growth they'd want through issuing more to existing customers, but I don't think that's a good long-term strategy.

And so we did quite a lot of work last year in trying to shift the focus of those agents so I think we've got to do some more and be more active at encouraging them to shift and bring new customers on. It is never easy because new customers do represent higher risk and there's no way round that, but I think we've just got to increase the ambition in the field to try and push more growth forward. It's probably worth saying though that Czech/ Slovakia is our most profitable market per customer by some way so growth of existing customers is quite attractive as well.

Delegate 1 Okay, that's fine. Thanks very much, John and all the best for the future.

JH Thank you.

Delegate 2 Right, well I just had a couple of things quickly. One is, I was hoping you guys could elaborate a little bit more on the results from your capital structure conversations internally. I see the 55% which is a pretty significant step up from where you've articulated this ratio on a target basis and it would be helpful, and I don't know if you have any intention of doing so, but it would be great for us as investors to hear a little bit more about what sort of criteria were behind that decision.

I don't know if there were specific analyses you used or if it was more of a qualitative discussion around the risk environment and what could be done vis-à-vis the balance sheets from a debt funding perspective, etc. So that's question number one, just is there more meat on the bone in terms of what you guys can do to talk about how you got to that figure?

DB Yes. I think the short answer is a combination of both qualitative analysis and discussion. So the central piece of work that we did was applying a series of stress tests, the financial projections of the business, to see how it would stand up under another recession. And that involved looking at some rising impairments and a reduction in revenues across a range of markets or specific markets falling into difficulty, and then seeing how the balance sheet faired under that and, in particular, how we faired against our bank covenants during that process.

And the indications following that detailed work was that the right ratios should be around 55%. And then obviously we discussed those results as a board and said does that feel right. Basically the board were all of the same mind that given where the world is at the moment in terms of the economic outlook and also some uncertainty about debt capital markets, that that was a sensible place to be in the current circumstances, but obviously it is something that we would have to revisit in future periods as the business progressed and as the external environment changes.

Delegate 2 One way to interpret that is that because you are already a bit above that target and now we're embarking on 2012 when presumably you'll grow the capital base again, one way to interpret it would be to say, well, 55% is a level and everything above that in theory, based on this new methodology, should be returned to shareholders in some way. Is that the way to think about it or next year at this time we're going to be talking about 60% or something being a new target?

DB No, I don't think you'll see a progressive ratcheting up of the target. I think your underlying thesis is a good one but obviously our first objective will be to spend that surplus capital by growing customers and growing credit issued to customers first and foremost. That would be absolutely our preference.

Delegate 2 Fair enough. Next question briefly would be, can you elaborate a little bit more on the decision to, at least for the time being, forego entering into a new market? I know that this has been something that you guys have been focused on as a firm for some time. Certainly things are a little bit cold in Europe, to say the least, but at the same time opportunities are created in such environments and, as we just learned, you have plenty of excess capital by many definitions. So I'd be curious to know how you guys think about that and what is the driver behind saying not right now?

JH	Let me start this off and then hand over to Gerard. A lot of work has been done and there is still some ongoing in terms of researching new markets. New market entry really is a core part of the growth strategy but this is something which we'll look to in the future, so maybe I'll just hand this over to Gerard to give you his input into this.

GR	Hi yes, I think it is a core part of what we do. Clearly we haven't done it now for a little bit of time but it is something that is on our agenda. And it's really a question of timing so it's not if we'll ever do it; it's more a question of when we will do it. The fact that we do have the capital available wouldn't push me to rush into it. I think it's more a question of getting the timing right and picking the right country. Now, our team have done a lot of research across a lot of markets; they've focused on two in particularly, which are Spain and Bulgaria. As yet, that research isn't complete and I'm waiting for the details to come in, which I think will be another couple or maybe three weeks. We'll go through that then as a team and we'll assess it. But I think it's more a question of when rather than if and we're just not rushing it at the moment, given what I would call just the level of uncertainty that you see in particularly around Europe at the moment.

Delegate 2 Let me reframe the question slightly. What do you personally need to see before you're comfortable giving the green light to something like this beyond just the internal analysis of course?

GR	Well I guess what I'm looking for is just to be happy that we have the right target markers and the right conditions. So for instance the right target market wouldn't be a market where we can't raise local funding, so that would rule out a certain number of countries. The right target market will be one where there isn't hyper inflation. It's a question of just finding the right target, having adequate research that tells us that we understand the market from a cultural point of view as well as a business point of view.

I spent, as I said, four of the last five weeks going around the countries and I have met the cadre of managers who are ready to step up and be a country manager and I'm quite comfortable that we have the right level of resources in country. So from that perspective I don't see that as a constraint. So again I would just reiterate, it's a question of timing and picking the markers that we feel comfortable with at the right time.

JH	And just something I've told you before, but it's clearly important that during the period of pilot we have stability broadly in the economic situation, so we can look at how our customers pay, how well we're retaining, etc. So it probably wouldn't make a lot of sense to start a pilot when things were uncertain. But there is a feeling I think that Europe is beginning to show improvement and it may be that helps us make some progress.

Delegate 2 Can I slide in one quick question, just to finalise here?

JH	Yes, sure.

Delegate 2 You guys called out in some detail the changes, I guess not changes, but the situation in Poland with these early [settlement] rebates in the discussions you're having with some of the regulators there. Can you just clarify that a little bit? To the extent that your appeal is unsuccessful, what might we be on the hook for and how does what Poland is telling you differ from what the CCD directives imply? I'm struggling a little bit to understand what the details here are.

JH I'm trying to keep this really simple. The Polish Consumer Office a while back approached not just us but a number of lenders about rebating and suggested that under the law existing then that we should be giving more generous rebates. And that debate's been going on for some time. What they were asking for is much less generous than that which the Consumer Credit Directive requires and the judgement isn't retrospective in the sense that it will only attach to loan agreements outstanding at the time the decision is finalised.

So as time has gone on, it's become less and less important because the rebates under the Consumer Credit Directive are much more generous. The more business written under the Consumer Credit Directive, the less we have to worry about the ruling from the Consumer Protection Office. If we lost the Consumer Protection Office case on appeal, we think it would cost us about an additional £3 million and that's encapsulated within our guidance that the impact for 2012 for early settlement rebates could be somewhere between £10 million and £15 million higher than in 2011. So if we win that case, as we think we might, then it's a lot more likely to be closer to £10 million than £15 million.

Delegate 2 Oh, I've got it, so that is in that number. I see.

JH It is in that number, yes. It's slightly complicated and, because the passage of time is moving on, it may disappear completely.

Delegate 2 Got it. Okay, that's very helpful, thanks for that. Sorry to monopolise the conversation here...

JH That's no problem. We've got plenty of time.

Delegate 2 Thanks guys.

JH Okay, well thanks for being on the call. We're going to be in the US in a couple of weeks' time. Many of you I will see there; look forward to that. But thanks for today and look forward to seeing you soon. Bye.