

Harmony

Tuning up the Efficiency in 1H24

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Harmony (HMY) reported a resilient 1H24 result, with operational efficiency gains the key positive. Rising interest rates and a weak macro environment weighed on performance in 1H24 relative to 1H23, reflected in: (1) a -60 bp contraction in net interest margin (NIM) to 9.2%, (2) a +110 bp rise in incurred credit losses to 4.2%, and (3) slowing loan book growth of +8%. Nevertheless, HMY delivered its fourth consecutive half-year cash profit (A\$0.5m) and, critically, a -4% sequential decline in the cost-to-income ratio to 24%. FY24 guidance implies a challenging 2H24, but continued operational efficiency gains and the successful launch of Stellare® 2.0 into the Australian market should insulate HMY somewhat, and position it well for a potential turn in the interest rate cycle. We make minor amendments to our earnings forecasts, with lower costs driving a small +2cps increase to our spot valuation from A\$1.27 to A\$1.29.

ASX Code	HMY	Financials: Jun/	23A	24E	25E	26E	Valuation (x)	23A	24E	25E	26E
Share price	A\$0.53	Rev (A\$m)	105.5	124.0	135.4	156.1	PE	n/a	n/a	25.9	6.4
Spot Valuation	A\$1.29 (from 1.27)	NPAT* (A\$m)	0.2	(3.2)	2.1	8.3	EV/EBIT	n/a	n/a	n/a	n/a
Risk rating	High	EPS* (Ac)	0.2	(3.1)	2.0	8.2	EV/EBITDA	n/a	n/a	n/a	n/a
Issued shares	102.0m	DPS (Ac)	0.0	0.0	0.0	0.0	Price / NTA	0.5	0.5	0.5	0.5
Market cap	A\$53.5m	Imputation (%)	0	0	0	0	Cash div yld (%)	0.0	0.0	0.0	0.0
Avg daily turnover	37.0k (A\$16k)	*Based on normalised profits					Gross div yld (%)	0.0	0.0	0.0	0.0

What's changed?

- **Earnings:** Normalised NPAT estimates rise +5%, +6%, and +1% in FY24/FY25/FY26 respectively on better cost control
- **Spot valuation:** Rises +2cps to A\$1.29.

1H24 result and FY24 outlook

HMY reported a 1H24 cash profit of A\$0.5m or an -A\$1.1m loss on our preferred 'normalised profit' measure, in-line with our expectations and a solid outcome given the challenging operating backdrop that saw net lending margins fall -40 bp to 5.0%. HMY also provided FY24 outlook commentary, saying it expects: (1) 'continued loan book growth', (2) NIM of 9%, and (3) positive cash NPAT. Guidance for FY24 is consistent with our expectations for +2% loan book growth, 9% NIM, and a cash profit of A\$0.9m.

Impressive cost-to-income progress

The key positive from HMY's 1H24 result was the continued decline in the cost-to-income ratio, which has now fallen from 69.1% in 1H21 to 23.9% in 1H24. Despite +8% loan book growth and +20% revenue growth versus 1H23, operating expenses rose by just +0.4% from 1H23 to 1H24, demonstrating the scalability of HMY's tech-driven lending platform. We continue to be encouraged by HMY's progress in generating operational efficiencies and expect a continuation of the downward trend in cost-to-income in future periods. Further reductions in the cost-to-income ratio should drive operational leverage and provide a tailwind for earnings growth.

Stellare® 2.0 in market

HMY has launched its proprietary Stellare® 2.0 lending platform into the Australian market. HMY expects Stellare® 2.0 to improve customer conversion rates through its advanced credit assessment capabilities, via harnessing machine learning algorithms to offer a more nuanced and accurate analysis of borrowers' creditworthiness. More efficient risk matching to individual customer profiles should increase the likelihood of loan acceptance. HMY provided several constructive performance metrics for Stellare® 2.0, including: (1) 25x more code releases per week than Stellare® 1.0, (2) a -12% technology cost-saving run rate versus 1H24, (3) 100% of customers receiving an instant credit decision, and (4) 18x quicker funds delivery from the beginning of a loan application.

Harmoney Corporation Ltd. (HMY)
Market Data (A\$)

Priced as at 23 Feb 2024	0.53
52 week high / low	0.65 / 0.31
Market capitalisation (A\$m)	54.0

Key WACC assumptions

Risk free rate	5.00%
Equity beta	1.40
WACC	11.7%
Terminal growth	2.0%

Profit and Loss Account (A\$m)	2022A	2023A	2024E	2025E	2026E
Interest income	68.9	105.5	124.0	135.4	156.1
Net interest income	50.8	65.7	68.6	74.6	86.4
Other income	3.9	1.5	0.3	0.3	0.3
Net operating income	54.7	67.2	68.8	74.8	86.6
Operating expenses	(54.5)	(62.5)	(67.6)	(67.6)	(72.0)
Associate income	0	0	0	0	0
Tax	0	0	(0.4)	(0.5)	(1.2)
Minority interests	0	0	0	0	0
Normalised NPAT	(3.9)	0.2	(3.2)	2.1	8.3
Abnormals/other	(14.9)	(7.8)	(0.6)	(5.6)	(5.9)
Reported NPAT	(18.8)	(7.6)	(3.8)	(3.5)	2.5
Normalised EPS (cps)	(3.9)	0.2	(3.1)	2.0	8.2
DPS (cps)	0	0	0	0	0

Growth Rates	2022A	2023A	2024E	2025E	2026E
Revenue (%)	96.1	53.1	17.5	9.2	15.3
EBITDA (%)	n/a	n/a	n/a	n/a	n/a
EBIT (%)	n/a	n/a	n/a	n/a	n/a
Normalised NPAT (%)	n/a	n/a	n/a	n/a	>100
Normalised EPS (%)	n/a	n/a	n/a	n/a	>100
Ordinary DPS (%)	n/a	n/a	n/a	n/a	n/a

Cash Flow (A\$m)	2022A	2023A	2024E	2025E	2026E
EBITDA	n/a	n/a	n/a	n/a	n/a
Working capital change	n/a	n/a	n/a	n/a	n/a
Interest & tax paid	n/a	n/a	n/a	n/a	n/a
Other	n/a	n/a	n/a	n/a	n/a
Operating cash flow	n/a	n/a	n/a	n/a	n/a
Capital expenditure	n/a	n/a	n/a	n/a	n/a
(Acquisitions)/divestments	n/a	n/a	n/a	n/a	n/a
Other	n/a	n/a	n/a	n/a	n/a
Funding available/(required)	n/a	n/a	n/a	n/a	n/a
Dividends paid	n/a	n/a	n/a	n/a	n/a
Equity raised/(returned)	n/a	n/a	n/a	n/a	n/a
(Increase)/decrease in net debt	n/a	n/a	n/a	n/a	n/a

Balance Sheet (A\$m)	2022A	2023A	2024E	2025E	2026E
Working capital	56.8	43.5	34.7	29.5	31.2
Receivables	553.1	710.8	722.0	833.1	949.9
Intangibles	8.5	11.6	13.5	15.4	17.0
Right of use asset	0.2	3.4	3.5	3.0	2.5
Other assets	16.1	16.1	16.1	16.1	16.1
Total funds employed	634.9	785.7	790.2	897.5	1,017.2
Deposits	n/a	n/a	n/a	n/a	n/a
Other borrowings	570.4	726.9	732.4	840.5	961.4
Other liabilities	5.4	5.0	3.5	3.0	2.5
Shareholder's funds	59.1	53.8	54.2	54.1	53.4
Minority interests	0	0	0	0	0
Total funding sources	634.9	785.7	790.2	897.5	1,017.2

* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend** Information on Forsyth Barr's Carbon and ESG (CESG) ratings can be found at www.forsythbarr.co.nz/corporate-news-events/cesg-report

Spot valuation (A\$)

DCF	1.29
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DCF valuation summary (A\$m)

Total firm value	141
(Net debt)/cash	0
Less: Capitalised operating leases	(9)
Value of equity	132

Valuation Ratios	2022A	2023A	2024E	2025E	2026E
EV/Sales (x)	n/a	n/a	n/a	n/a	n/a
EV/EBITDA (x)	n/a	n/a	n/a	n/a	n/a
EV/EBIT (x)	n/a	n/a	n/a	n/a	n/a
PE (x)	n/a	>100x	n/a	26.2	6.5
Price/NTA (x)	0.5	0.5	0.5	0.5	0.5
Free cash flow yield (%)	n/a	n/a	n/a	n/a	n/a
Adj. free cash flow yield (%)	0.8	29.1	48.5	58.3	76.8
Gross dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0

Capital Structure	2022A	2023A	2024E	2025E	2026E
Interest cover EBIT (x)	>100x	>100x	>100x	>100x	>100x
Interest cover EBITDA (x)	>100x	>100x	>100x	>100x	>100x
Net debt/ND+E (%)	n/a	n/a	n/a	n/a	n/a
Net debt/EBITDA (x)	n/a	n/a	n/a	n/a	n/a

Key Ratios	2022A	2023A	2024E	2025E	2026E
Return on assets (%)	-0.6	0.0	-0.4	0.2	0.8
Return on equity (%)	-3.2	0.2	-2.5	1.7	6.7
Return on funds employed (%)	0.0	0.0	0.0	0.0	0.0
EBITDA margin (%)	n/a	n/a	n/a	n/a	n/a
EBIT margin (%)	n/a	n/a	n/a	n/a	n/a
Capex to sales (%)	n/a	n/a	n/a	n/a	n/a
Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a
Imputation (%)	0	0	0	0	0
Pay-out ratio (%)	0	0	0	0	0

Segment Performance	2022A	2023A	2024E	2025E	2026E
Group Reported NPAT	(18.8)	(7.6)	(3.8)	(3.5)	2.5
Movement in credit provision	14.9	7.8	0.6	5.6	5.9
Share based expenses	2.7	1.9	0.5	1.0	1.1
D&A expenses	1.3	2.5	3.4	3.6	4.0
Group Cash NPAT	0.2	4.7	0.8	6.7	13.4
Group Loan book (\$m)	581.0	744.0	757.3	873.7	996.0
NIM (%)	11.8%	9.6%	9.1%	9.1%	9.2%
Equity ratio (%)	9.3%	6.8%	6.9%	6.0%	5.2%

Australia:	2022A	2023A	2024E	2025E	2026E
Loan book (period end, \$m)	274.1	381.6	393.1	491.3	594.5
Number of originations (#)	12,571	12,597	10,924	13,655	16,522
Total Income (\$m)	25.8	52.7	62.5	72.9	90.0
NIM (%)	12.2%	10.3%	9.3%	9.4%	9.5%
AU Cash NPAT (\$m)	(1.5)	5.8	4.6	9.6	15.8
New Zealand:	2022A	2023A	2024E	2025E	2026E
Loan book (period end, \$m)	306.8	362.4	364.2	382.4	401.5
Number of originations (#)	14,161	13,605	10,085	10,589	11,118
Total Income (\$m)	47.0	54.3	61.7	62.7	66.4
NIM (%)	11.5%	9.0%	8.9%	8.8%	8.9%
NZ Cash NPAT (\$m)	(7.9)	(11.7)	(3.8)	(2.9)	(2.4)

Earnings revisions

We leave our forecasts essentially unchanged outside of minor compositional tweaks to operating expenses. HMY's 1H24 result and outlook commentary were consistent with our expectations of slowing growth and suppressed margins in FY24. We retain our view that FY24 will represent a cash earnings trough for HMY before expansion in FY25 and FY26.

Figure 1. Earnings revisions

A\$m	FY24E			FY25E			FY26E		
	Old	New	Change	Old	New	Change	Old	New	Change
Interest income	123.2	124.0	+1%	135.4	135.4	+0%	156.1	156.1	+0%
Other income	1.0	0.3	-75%	0.3	0.3	-17%	0.3	0.3	-17%
Total Income	124.2	124.2	-0%	135.7	135.6	-0%	156.4	156.4	-0%
Interest expense	(55.4)	(55.4)	+0%	(60.8)	(60.8)	+0%	(69.8)	(69.8)	+0%
Impairment expense	(32.1)	(32.1)	+0%	(35.5)	(35.5)	+0%	(38.6)	(38.6)	+0%
Customer acquisition expense	(10.7)	(10.8)	+2%	(11.0)	(11.2)	+2%	(11.3)	(11.5)	+2%
Other operating expenses	(26.1)	(25.8)	-1%	(27.9)	(27.6)	-1%	(29.2)	(28.9)	-1%
Depreciation and amortisation expenses	(3.4)	(3.4)	+0%	(3.6)	(3.6)	+0%	(4.0)	(4.0)	+0%
Income tax benefit/(expense)	(0.5)	(0.4)	n/a	(0.6)	(0.5)	n/a	(1.2)	(1.2)	n/a
Reported NPAT	(3.9)	(3.8)	+3%	(3.7)	(3.5)	+5%	2.4	2.5	+4%
Movement in expected credit loss provision	0.6	0.6	+0%	5.6	5.6	+0%	5.9	5.9	+0%
Normalised NPAT	(3.3)	(3.2)	+5%	1.9	2.1	+6%	8.2	8.3	+1%
Share based payment expenses	0.7	0.5	-33%	1.3	1.0	-20%	1.3	1.1	-20%
Depreciation and amortisation expenses	3.4	3.4	+0%	3.6	3.6	+0%	4.0	4.0	+0%
Cash NPAT	0.9	0.8	-10%	6.8	6.7	-2%	13.5	13.4	-1%

Source: Company, Forsyth Barr analysis

1H24 results analysis – key points

- **Loan book:** Grew +2% sequentially/or +8% versus the prior comparable period (pcp) to A\$756m on lower loan originations.
- **Net interest margin (NIM):** Contracted -20 bp sequentially, or -60 bp versus pcp to 9.2%. NIM is still within management's target range of 9% to 10%, but HMY was unable to pass through the full +70 bp increase in funding costs in 1H24.
- **Incurred losses:** Rose +20 bp sequentially/or +110 bp versus pcp to 4.2%. Incurred losses are now above management's target range of 3% to 4%. Lower originations increased the seasoning of HMY's loan book, causing a higher proportion of borrowers to enter the 'peak hazard' loss period.
- **Net lending margin (NLM):** Fell -40 bp sequentially/or down -150 bp versus pcp to 5.0%.
- **Cost-to-income ratio:** Declined -4% sequentially/or down -5% versus pcp to 24%.

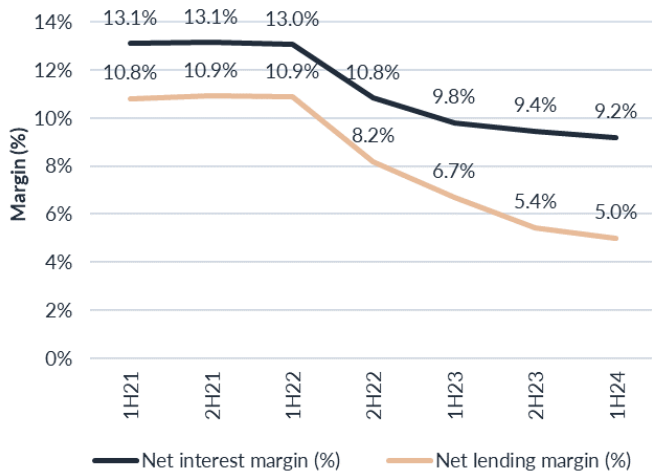
Figure 2. 1H24 results analysis

A\$m	1H23	1H24	Change	1H24	Deviation	Comments
	Actual	Actual	%	FB	%	
Interest income	49.5	60.3	+22%	59.9	+1%	Some book growth and book rolling onto higher rates
Other income	0.5	0.1	-87%	0.8	-91%	Peer-to-peer lending concluded
Total Income	50.1	60.4	+21%	60.6	-0%	
Interest expense	(18.0)	(26.0)	+45%	(26.6)	-2%	Impact of rising interest rates, partially offset by hedging
Impairment expense	(14.6)	(15.1)	+3%	(15.0)	+1%	Higher incurred losses, lower ECL provision movement
Customer acquisition expense	(6.5)	(5.4)	-17%	(5.5)	-1%	Reflects focus on profitability at this point in the cycle
Other operating expenses	(13.2)	(12.9)	-2%	(13.2)	+2%	Lower personnel and G&A expenses
Depreciation and amortisation expenses	(1.1)	(1.5)	+34%	(1.7)	-11%	
Income tax benefit / (expense)	-	-	n/a	(0.2)	n/a	
Reported NPAT	(3.4)	(0.6)	n/a	(1.6)	n/a	1H24 helped by positive ECL provision movement
Movement in expected credit loss provision	4.6	(0.5)	n/a	0.3	n/a	Benefit from movement in expected loss rate from 4.9% to 4.8%
Normalised NPAT	1.2	(1.1)	n/a	(1.3)	-14%	
Share based payment expenses	0.0	0.1	n/a	0.4	-71%	
Depreciation and amortisation expenses	1.1	1.5	+34%	1.7	-11%	
Cash NPAT	2.3	0.5	-78%	0.7	-27%	Fourth consecutive HY cash profit

Source: Company, Forsyth Barr analysis

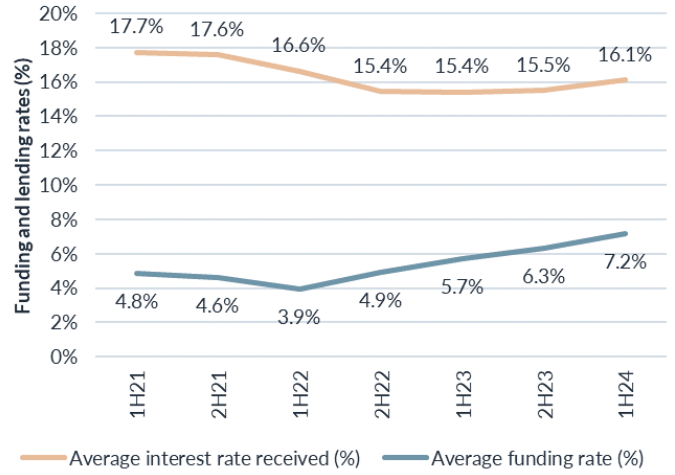
Key charts

Figure 3. HMY – NIM and NLM margins



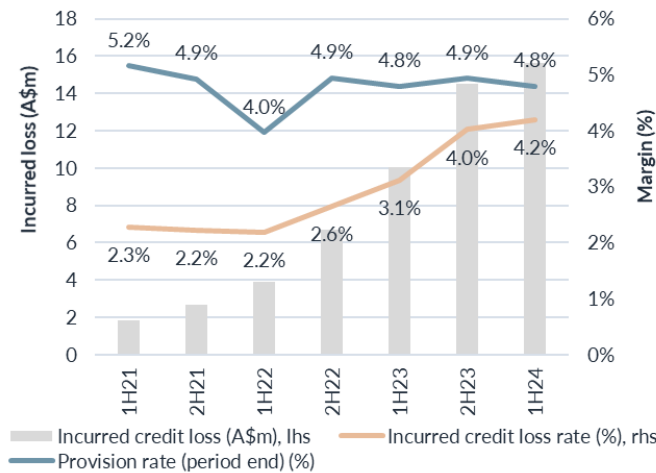
Source: Company, Forsyth Barr analysis

Figure 4. HMY – Average funding and lending rates



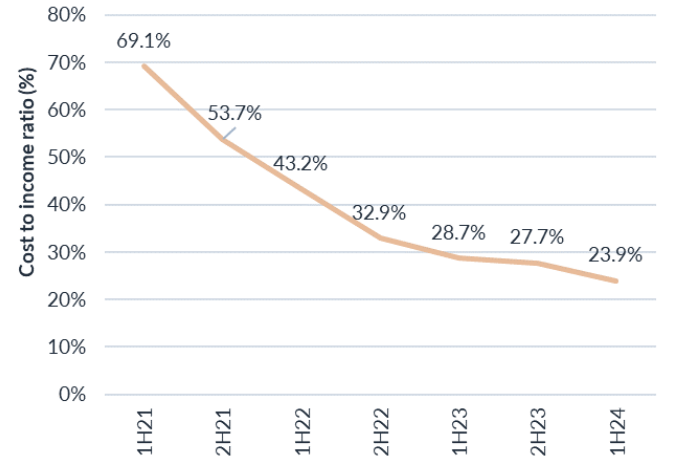
Source: Company, Forsyth Barr analysis

Figure 5. HMY – Incurred loss and provisioning rate



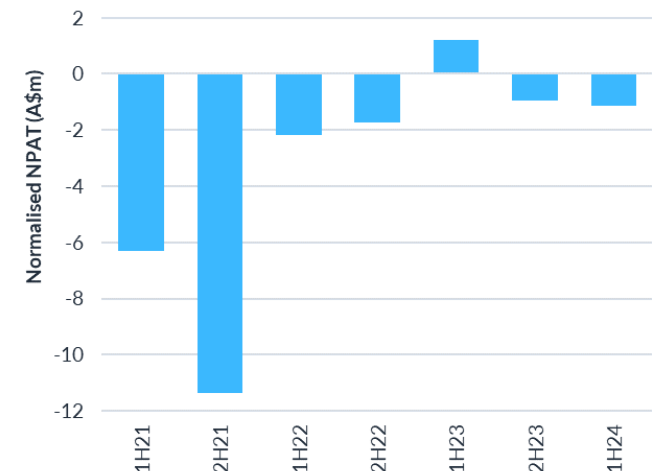
Source: Company, Forsyth Barr analysis

Figure 6. HMY – Cost-to-income ratio



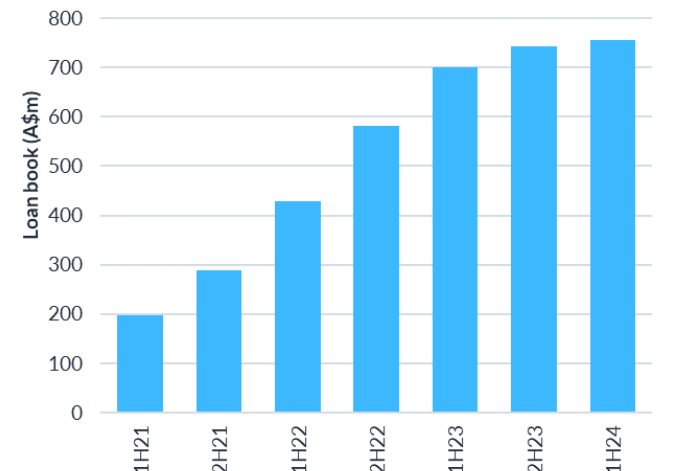
Source: Company, Forsyth Barr analysis

Figure 7. HMY – Normalised NPAT



Source: Company, Forsyth Barr analysis

Figure 8. HMY – Loan book



Source: Company, Forsyth Barr analysis

Figure 9. Price performance (A\$)



Source: Forsyth Barr analysis

Figure 10. Substantial shareholders

Shareholder	Latest Holding
Heartland Group Holdings	10.1%
Lookman Family Trust	9.0%
Kirwood Capital	8.7%

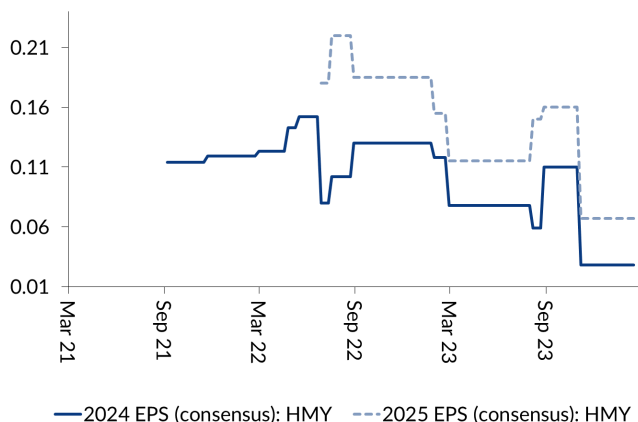
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 11. International valuation comparisons

Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2025E	
				2024E	2025E	2024E	2025E	2024E	2025E		
<i>(metrics re-weighted to reflect HMV's balance date - June)</i>											
Harmony	HMV AU	A\$0.53	A\$54	<0x	25.9x	n/a	n/a	n/a	n/a	0.0%	
Humm Group	HUM AU	A\$0.69	A\$351	13.0x	9.1x	59.2x	51.6x	>75x	>75x	3.6%	
Moneyme	MME AU	A\$0.09	A\$73	2.6x	2.2x	45.3x	28.9x	45.6x	28.9x	n/a	
Plenti Group	PLT AU	A\$0.69	A\$120	<0x	>50x	>75x	>75x	<0x	>75x	0.0%	
Solvar	SVR AU	A\$1.24	A\$259	9.6x	8.2x	7.3x	6.7x	7.5x	6.8x	9.9%	
Latitude Group Holdings	LFS AU	A\$1.17	A\$1,211	36.6x	11.8x	73.6x	40.0x	>75x	68.3x	5.8%	
Wisr	WZR AU	A\$0.03	A\$45	16.5x	5.5x	>75x	>75x	n/a	n/a	n/a	
Anz Group Holdings	ANZ AU	A\$28.30	A\$85,113	12.7x	13.0x	n/a	n/a	n/a	n/a	5.7%	
Commonwealth Bank Of Austral	CBA AU	A\$116.23	A\$194,645	20.2x	20.9x	n/a	n/a	n/a	n/a	3.9%	
National Australia Bank	NAB AU	A\$32.90	A\$102,320	14.6x	14.8x	n/a	n/a	n/a	n/a	5.1%	
Westpac Banking Corp	WBC AU	A\$24.58	A\$85,984	13.0x	13.4x	n/a	n/a	n/a	n/a	5.8%	
Compco Average:				15.4x	11.0x	46.3x	31.8x	26.5x	34.7x	5.0%	
EV = Mkt cap+net debt+lease liabilities+min interests-investments				HMV Relative:		n/a	136%	n/a	n/a	n/a	-100%

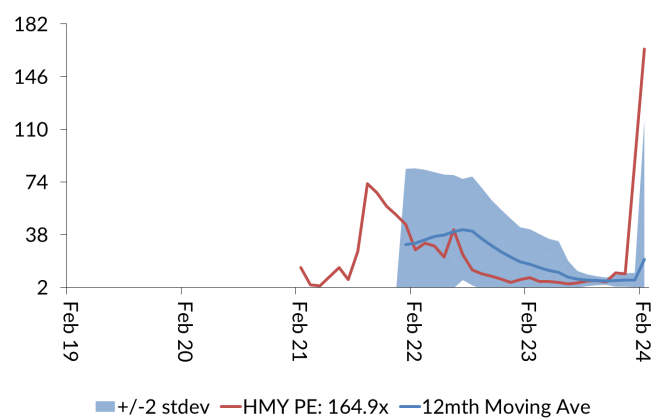
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (HMV) companies fiscal year end

Figure 12. Consensus EPS momentum (A\$)



Source: Forsyth Barr analysis

Figure 13. One year forward PE (x)



Source: Forsyth Barr analysis

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