THORN GROUP LTD

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THORN REVENUE UP, ONE-OFF ITEMS IMPACT PROFIT, FINAL DIVIDEND AT 6 CENTS

Highlights – FY16 Results

- Revenue up 3.5% to $304m, underlying profit after tax steady at $30.3m
- Reported profit after tax down 34% to $20.1m
- Three significant one-off items, totalling $11.8m pre-tax ($10.3m after tax), affected reported profit
- Final dividend 6.0c, full year dividend 11.5c (FY15: 11.75c) fully franked
- Thorn Business Finance doubles revenue and earnings
- Outlook focused on growth of Consumer Leasing and Business Finance

Financial services company, Thorn Group Limited (ASX: TGA), has reported higher revenue but lower profit, principally due to three significant one-off items, for the financial year to 31 March 2016.

Revenue increased 3.5 per cent on the previous year from $293.7 million to $304.0 million and profit after tax was 34 per cent lower, decreasing from $30.6 million to $20.1 million.

The underlying strength of Thorn's consumer leasing and commercial finance business divisions, has led directors to pay a final dividend of 6 cents a share, taking the full year dividend to 11.5 cents fully franked, representing a payout ratio of 88 percent on earnings per share of 13.1 cents.

Three significant one-off items affecting results were:

- Closure of the TFS consumer loan division at year end, involving a pre-tax cost of $2.3 million
- Write off of goodwill in receivables management business, NCML, of $6.7 million
- Refund of historic credit balances in the consumer leasing business following closure of legacy IT systems, resulting in a provision of $2.8 million pre tax

Excluding these significant items, profit after tax would have been $30.3 million.

Combined results from Thorn's two principal businesses, consumer leasing and business finance, showed revenue up 5.7 per cent and EBIT up 3.4 per cent, with Thorn Business Finance doubling revenue, EBIT and contribution to combined earnings, up from 11 per cent to 22 per cent.

Operations

Consumer leasing business, Radio Rentals, continues to experience strong demand, but recorded flat revenue at $246m, principally due to tightened credit assessment practices relating to evolving regulatory oversight and 'responsible lending' concepts. A significant technology project has now commenced to improve customer experience and transactional efficiency.

Customer satisfaction levels remain strong, with independent market research showing 97 per cent of customers say Radio Rentals treated them with dignity and respect, 92 per cent consider Radio Rentals affordable and 70 per cent say Radio Rentals was the only way for them to access affordable everyday essential goods.

Earnings were affected by enhanced credit assessment procedures and historic customer credit refunds, resulting in underlying EBIT being 4 per cent lower at $49.7m.

In FY17, Radio Rentals will open two new outlets, one in Victoria and another in Western Australia. In addition, Radio Rentals plans to transition 6 existing 'Full Service Branch' locations to a 'Hub and Spoke' business model which will benefit from access to high footfall shopping centres. This strategy has proven successful in supporting installation growth and will extend Radio Rentals' demographic reach.

Thorn Business Finance (TBF) comprises Thorn Equipment Finance and Thorn Trade & Debtor Finance (formerly Cash Resources Australia), with the latter contributing 45 per cent of the division's combined EBIT, assisted by a lift in invoice purchases.

TBF revenue doubled from $15 million to $30.5 million, mostly due to continued origination growth in Thorn Equipment Finance, which drove a 60 per cent increase in net receivables from $82.4 million to $131.9 million, with EBIT also doubling, to $14.0m. This continues to demonstrate Thorn's ability as a niche provider to meet a growing demand for effective financing solutions for the underserviced small and medium business market.

Performance of receivables management business, NCML, was affected by lower contingent client placements and a new valuation methodology being applied to purchased debt ledgers, resulting in current year EBIT declining from $2.3m to $1.4m. This underpins Thorn's decision to write off goodwill totalling $6.7m from its acquisition of NCML in 2011. In recent months the division has demonstrated early signs of competitive edge and improved new business levels.

A decision to close the consumer finance division and liquidate its $33m receivables book supports Thorn's return on capital strategy, with costs of closure and asset value adjustments of $2.3m to assist the book run-off reducing current year EBIT from a profit of $0.7m to a loss of $1.6m. Capital returned from the book run-off will be reinvested to support the growth of higher returning business divisions.

Receivables, balance sheet

Group receivables, which underpin future revenue and earnings, continue to grow and increased 31 per cent to $379.5m for the year. Gearing, excluding securitised debt, increased from 38.7 per cent to 53.2 per cent to support this growth and align with the strength of Thorn's balance sheet.

Current loan facilities provide an additional $42 million to support further expansion. Diversification of existing funding facilities will be reviewed in FY17 as a prudent measure to ensure the business has access to multiple funding sources to support its growth profile.

Commentary

Managing Director of Thorn Group, Mr James Marshall, said that, while the financial results for FY16 were impacted by three significant one-off events and an evolving regulatory landscape, the group's core businesses of Consumer Leasing and Business Finance had been performing well, which was promising for future growth.

"We are particularly pleased with the performance of the business finance division, doubling revenue and profit in FY16, and contributing significantly to the group's overall result," Mr Marshall said.

"We welcome the Treasury panel's review into consumer leasing and believe the report's recommendations strike the right balance between protecting consumers and supporting low cost providers like Thorn. This may open up opportunities for market consolidation in the fullness of time" Mr Marshall said.

"We believe the increased focus on our two core businesses, coupled with a strategic priority to deliver an above average return on capital, will deliver growing benefits for all our stakeholders in years to come," Mr Marshall said.

People

During the year, Thorn enhanced its management team with Peter Forsberg appointed as Chief Financial Officer, Wendy Yip as Chief Risk Officer, Peter Ryan as General Counsel and Matt Ingram, formerly head of Thorn Business Finance, now Chief Operating Officer, all adding to the strength of Thorn's leadership and risk management capability.

Strategic review

The outcome of a strategic review by Thorn has made it clear the two principal businesses, consumer leasing and business finance, generate attractive and recurring levels of return on capital that warrant further investment. This reflects a combination of the group's skills, infrastructure, marketing and investment in technology to improve customer experience, transactional efficiency and demographic reach.

Thorn's strategic direction over the next few years will be to focus on growing in these two areas, while also applying the group's skill set to receivables management. This will streamline product development and also define potential acquisitions to add to market positioning.

To enhance this focus on areas of highest return, Thorn has exited consumer loans, where high marketing costs and increasing competition had reduced return on capital for this business.

Government review of Small Amount Credit Contracts and Consumer Leasing

Last month, the Government Review Panel released its final report recommending, among other things, caps on consumer lease pricing. In its report, the Panel recognised fundamental differences between leasing and loan products and has recommended a level of pricing caps which will only affect a small percentage of Radio Rentals products, but importantly will not impact the sustainability of Thorn's consumer leasing business.

ASIC Review and contingent liability

In its HY16 report, Thorn flagged a contingent liability in relation to potential inconsistencies in its credit assessment procedures. Thorn has been assisting an investigation which ASIC has been undertaking into Thorn's compliance with the responsible lending obligations pertaining to consumer leases under the National Consumer Credit Protection Act 2009.

ASIC has informed Thorn that it is concerned about possible breaches of Thorn's responsible lending obligations in respect of consumer leases entered into in the period 1 January 2012 to 1 May 2015.

ASIC's investigation is ongoing and Thorn is obtaining advice and considering its position in relation to ASIC's concerns. There are a number of potential outcomes from this engagement with ASIC, one of which is the imposition of penalties, but the outcome is not certain at this stage. Thorn will advise the market further at the appropriate time.

Outlook

Thorn's strategic focus is on its two principal business divisions of consumer leasing and business finance, building on the economics of providing niche financial services efficiently to produce attractive returns on capital.

The consumer leasing industry has been subject to increasing levels of regulation and regulatory scrutiny in FY16 and Thorn, as an industry leader, intends to continue to invest in risk management and responsible lending initiatives to meet these requirements. Developments in these areas may have a short term effect on Thorn. However, strength of consumer sentiment and support for consumer leasing underpin confidence in positioning the business to advance market share and cement Thorn as a leading provider in the sector.

Thorn is confident Business Finance will continue its growth trajectory, with the group also seeking out opportunities to grow this division further.

Thorn will continue to pursue organic growth across the group while reviewing acquisition opportunities that add value and align with the group's overall strategy.

For further information please contact:

James Marshall

Managing Director, Thorn Group Limited

James.marshall@thorn.com.au

Telephone: +61 2 9101 5057 or +61 404 811 254

Ian Westbrook

Hill + Knowlton Strategies

Ian.westbrook@hkstrategies.com

Telephone: +61 2 9286 1225 or +61 407 958 137

ABOUT THORN GROUP LIMITED (ASX: TGA, www.thorn.com.au)

Thorn Group is a diversified financial services company, providing financial solutions to niche consumer and commercial markets. Thorn's operating priorities are diversifying and growing as a business and meeting the needs of customers, employees and investors. Its principal operations are its foundation business, Radio Rentals (RR in South Australia), a leader in the household goods rental market since 1937 and with over 90 outlets nationally, and Thorn Business Finance, a provider of leasing and debt finance to businesses. Thorn employs in excess of 800 people, has been listed on the ASX since 2006, is licensed under the National Consumer Credit Protection Act 2009 and operates a responsible lending policy.