PARTICIPANTS

Corporate Participants

Jeff Christensen – Vice President-Investor Relations, EZCORP, Inc.
Stuart I. Grimshaw – Chief Executive Officer & Director, EZCORP, Inc.
Mark Ashby – Chief Financial Officer, EZCORP, Inc.

Other Participants

William R. Armstrong – Analyst, C.L. King & Associates, Inc.
Michael Browning Del Grosso – Analyst, Jefferies LLC
Chris Smith – Analyst, GLG Partners
Richard Gregg Hillman – Analyst, First Wilshire Securities Management, Inc.
Eugene Fox – Analyst, Cardinal Capital Management LLC
Todd Meadow – Vice President, Nomura Securities

MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the EZCORP fourth quarter and full year fiscal 2016 earnings conference call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions] As a reminder, this call may be recorded.

I would now like to turn the conference over to Jeff Christensen, Vice President of Investor Relations for EZCORP. Please go ahead, Jeff.

Jeff Christensen, Vice President-Investor Relations

Thank you, and good morning, everyone. Joining me today are Stuart Grimshaw, Chief Executive Officer of EZCORP, and Mark Ashby, Chief Financial Officer of EZCORP. During our prepared remarks, we will be referring to slides which are available for download on our website at investors.ezcorp.com.

Before we begin, I'd like to remind everyone that this conference call contains certain forward-looking statements regarding the company's expected operating and financial performance for future periods. These statements are based on the company's current expectations. Actual results for future periods may differ materially from those expressed or implied by these forward-looking statements due to a number of risks and other factors that are disclosed in our annual, quarterly, and other reports filed with the Securities and Exchange Commission.

Now, I would like to turn the call over to Mr. Stuart Grimshaw. Stuart?

Stuart I. Grimshaw, Chief Executive Officer & Director

Thanks, Jeff, and welcome, everyone. It's a chilly day here in Austin, but we'll go through the financial year that has just completed. It's been quite a long year and there's a bit of stuff to get through, but we've got some pleasing messages which have come out of a year of very hard work.

On slide three, I'll touch on four of the messages that we do want to leave you with. And the first one is we've continued the intense focus on meeting our customers' desire for cash whenever they want it and wherever they want it.

We've got some strong training programs that we've been executing behind this, particularly, the Mystery Shop Program where, on a quarterly basis, we have three phone calls and one video of the interaction our customers have with our staff. That's an important training tool which we continue to utilize and learn from, which is leading to some strong positive metric growth in the Net Promoter Score as well. We continue to invest in that tool as it's bringing the desired results.

The results are actually followed through in the second point that we are capturing market share and we're leading the market in PLO growth in both U.S. and Mexico. Same store PLO growth in the U.S. is up 4% year-on-year, and this is the fourth consecutive quarter of positive growth. And in Mexico, it's up 20% year-on-year, and it's the ninth consecutive double-digit quarter. But importantly, the same quarter last year was a 20% growth as well, so we've comped 20% on 20%, which is an exceptional outcome and shows the focus and the strength of the management team in Mexico.

We have a proven track record of pawn execution with strong operating leverage, and I'll deal with that particularly over the page. But, importantly, in the last, we have a strong liquidity position in which we finished the year. We have about $66 million cash balance at year-end, $50 million in undrawn credit facility, and we anticipate receiving $45.7 million of the $89.9 million notes receivable from the Grupo Finmart sale, and Mark will touch on that a little bit later in the presentation.

So I turn to slide four and what we see here is the strength of the operating leverage in the business. We look at the total revenues up 5%, net revenues up 9%, profit before tax is up a large number. But if you look at the drop in the dollar, we increased our net revenue by $37 million and $20 million of that actually dropped to the bottom line, which means that $0.54 of every dollar in net revenue was finding its way to the bottom line, and that's a very strong leverage factor that we've been able to achieve.

We look down at the metrics below, the pawn loans outstanding we've talked about, the strong PSC growth of 4%, and 22% for U.S. and Mexico respectively. Inventories are up in the U.S. and Mexico. In U.S. particularly, we had a very low inventory balance last year. As many of you'll recall, we actually started moving our aged inventory quite rapidly. And our sales gross profit has been up quite strongly over that period of time.

On to slide five, which is a consistent slide that we've shown, it shows the path of execution, and we have achieved quite a lot in a very short period of time. But, as we look forward, we're looking to how we further invest into the fabric of our pawn businesses. The technology structure and point of sale system, there's a new point of sale system which we will start piloting in the first quarter of next calendar year, so our second quarter financial.

We're investing in the product and customer data analytics. We have a lot of rich data that sits within the business that we're now starting to use and integrate into the point of sale system as well. Still early days, but we're finding that that's providing with some great insights into how the customers behaving and which products are actually starting to move quickly.

We're investing in process analysis and improvements. We don't have as much standardization through the stores as we would like to have, so we've embarked upon a complete analysis of process efficiencies. This is still in its early days, but we can see there will be some easy wins out of the analysis that's already being undertaken.

Store refurbishment program, we haven't actually touched the stores for quite a period of time. That actually makes it somewhat hard for our customers and our staff to interact, so we have to invest into the fabric of those, and that's a three-year program, which we'll be running through. And we're tracking towards the annual corporate expense of $50 million in FY18 as we have always outlined, and I'm sure Mark will touch on that just a little bit later on.

So, with that sort of introduction, I'll now pass it over to Mark Ashby.

Mark Ashby, Chief Financial Officer

Thanks, Stuart. Good morning, everybody. I'll take you through a few financial slides with the focus really on the adjusted results, so with taking into account restructuring, restatement costs from last year that fell into FY16, constant currency impact, and some non-cash impairment charges, and there's a reconciliation of this in the rear of the deck.

As we have a look at the year, some of the points that Stuart's already touched on, we have PLO growth of 6.2%, merchandise gross profit up 17%, and that really did drive the net revenue up 9% to $438.2 million for the full year. The U.S. Pawn segment, and you can see down the bottom, there was good growth in U.S. Pawn segment profit, Mexico Pawn segment profit, and Stuart's touched on some of the drivers of that and the focus in those areas.

As we look at the cost structure, the Q4 costs are really not representative of the run rate. In the quarter, we increased the accrual for store operations incentives as well as corporate incentive and bonus plans. And the annual is probably a bit more meaningful to look at. So, as you look at the annual number, we're now seeing a $2 million per quarter reduction that we'll annualize into next year. So that's an $8 million number coming off that $64 million as we come into FY17.

Overall, the underlying costs, excluding the changes to the STI and the long-term incentive plans, were actually down about $8 million, and they were offset by that amount. So, as you look at the bottom line for the year, we've got a profit before tax of $23 million on an adjusted basis compared to $3 million of last year.

If we look at the next page and look at the annual performance, firstly of the U.S. Pawn business; and these charts are available for the quarter a bit further into the pack as well. Again, just reinforcing the PLO growth, same store up 4%, pawn service charges up 6%, 4% on a same store basis. Looking at average PLO per store, now at an industry leading $288,000. Continued improvement in merchandise margin as we reduced our aged inventory even further, and that will also apply to Mexico. There was a substantial growth in merchandise margin by 300 basis points. Consistent yields in PLO and inventory to last year also supported the growth.

The expense really primarily I've touched on for each of the stores. There's a bonus pool that's been implemented and a strong incentive program for the year, and we've seen the benefits of that. And also, the increase is driven by the cost of new stores that were acquired during the course of the year.

If we turn to the next page, which is page eight, which is the Mexico Pawn, similar types of positive improvement. The PLO same store up 20%. We're really compounding 20%, as Stuart mentioned, last year which is a very strong effort. This drove pawn service charges up some 22% and the monthly yield has been consistent over the year. Similar to the United States, the merchandise margin had a very strong increase, up to 32% from 20% last year, and that really drove improvements in the inventory yield.

Expense increase, really, driven again through store incentives, some new stores that were opened during the year, de novo stores, and an increase in the marketing which we've seen the benefits from growth into the business.

If we turn to page nine, and Stuart touched on this earlier in his presentation, as you're aware, we touched on the – we sold the Grupo Finmart business in September. And as a part of the deal, there is a Notes Receivable to EZCORP and they were created to the tune of $89.8 million. All the committed payments to date have been received of some $6.4 million. And during 2017, we expect $45.7 million worth of cash to come into the business. If you add that incoming liquidity to our opening cash position for the year of $66 million plus the $50 million undrawn debt facility, that gives us a very positive framework to provide investment and support investment back into the business.

One question that does tend to pop up is what's the exchange and exposure, and at the bottom left-hand side, we break out what the denominations are for the notes, and there is very little FX exposure back into the United States.

So, on that note, I'll pass back to Stuart.

Stuart I. Grimshaw, Chief Executive Officer & Director

Thanks, Mark. On slide 10, what we've outlined there is exactly how we're focused on the market leadership position that we are aspiring to. The important thing here is you've seen that 99% of our revenue is actually coming out of pawn operations, so the investments that Mark is talking about is actually going [ph] solidly (11:33) into the pawn business. There are eight items there that we're focused on, and a couple of them I've touched on already.

I think the things that we're really focusing on is around the people, which we look at the incentives, training, coaching and mentoring, we have increased the number of district managers in the field by three to four people. We have greater depth at the district VP level, and that's allowed us to actually have more people in the field looking and training the people on the ground.

The discipline in pawn loan values is quite critical. As we've seen in the past, the discipline actually makes us successful, and we've seen with the new point of sale system coming in that will allow us to have very tight discipline around the pricing that happens at store level.

The store acquisitions and de novo openings, as we've said before, we're looking at the de novo openings in Mexico in particular, and with store acquisitions, we've looked at many potential acquisitions over the last three to six months; a number of them haven't actually met our hurdles, so we have backed away from that. And we will continue to exercise capital discipline should any further store acquisitions come across our desk.

On to slide 11, this is really the summary of where we are. The industry is an attractive one. It's a large industry, it's mature but it's highly fragmented, and with that provides opportunities for us, and we're seeing that through the positive PLO growth that we're achieving. It's a fully collateralized loan portfolio and the recourse to the customer doesn't exist, so it's a very good product for the customer base that we do service.

From an EZCORP perspective, we have now established a very strong track record of execution, as we've talked about; four consecutive quarters of positive PLO growth in the U.S. and nine consecutive quarters of positive PLO growth in Mexico. We have also done what we've said. We said we'd shut the U.S. financial services down, and we did that on time and ahead of budget. We also completed the sale of Grupo Finmart as we had announced to the market on time.

I've talked about the focus on customer leadership and I can't reiterate how much this is driving the results that we are seeing. And we're relentless on ensuring that we are meeting the needs of our customers and the results we're seeing ensure that that does happen.

And the last thing I would say is that we're actually very disciplined. We have improved our liquidity position, we've got strong leverage, and we continue to exercise with caution the way we allocate capital to ensure the returns meet the hurdles that we do have.

So, with that overview, we'll now turn it over to questions.

QUESTION AND ANSWER SECTION

Operator: [Operator instructions] Our first question comes from Bill Armstrong with C.L. King & Associates. Your line is now open.

<Q – Bill Armstrong – C.L. King & Associates, Inc.>: Good morning, gentlemen. Nice quarter. I'd like to talk about the retail margins in the fourth quarter; roughly, flat in the U.S. and up big in Mexico. In Mexico, can you remind us, were margins depressed in any way because of clearance sales last year? And what other drivers might there have been? And then in the U.S., are we kind of at maybe a level of margins that are sort of a steady run rate going forward?

<A – Stuart Grimshaw – EZCORP, Inc.>: Yeah. Thanks, Bill. In Mexico, we actually sold off a lot of our aged inventory in the last quarter particularly, which caused the compression in that margin. And we finished the year with 4% aged inventory. We're down to 3% this year, which means that we could capture some of the margin, so we had a healthier inventory position coming to this year, which is reflected through that Mexican margin. With the U.S., we did offload a fair bit of aged inventory also, but we think the margins – we're pretty much hitting around that level. If we can keep them at 36% to 38% level, we'd be doing pretty well.

<Q – Bill Armstrong – C.L. King & Associates, Inc.>: Okay, got it. And then, on the administrative expenses, obviously, down year-over-year, but they were up versus Q3 on a sequential basis. And I think you mentioned something in your opening comments. I was wondering if you could just expand on what drove that and on what we should kind of look at as we go into the new fiscal year.

<A – Mark Ashby – EZCORP, Inc.>: It's Mark here, Bill. There was a couple of drivers in the fourth quarter, particularly, the bonus impact if you're talking administrative expenses in the stores. If you're talking administrative expenses in what we call corporate in here, you have a similar effect where we increased our accrual quite substantially, but it's actually across the business. So it does tend to be a bit lumpy from that perspective.

Hence, I'm trying to give an indication when we look at the corporate numbers coming forward and then coming down by about $2 million a quarter over the course of the year, so off that $64 million type base. Outside of that, there was, obviously, we took an equity loss on the CCV business of about $5.8 million, I think it was or so, during the last quarter, so that actually reflects in some of the numbers as well.

<Q – Bill Armstrong – C.L. King & Associates, Inc.>: Okay. So if I understand that then we had $64 million in the year just ended, and so would you be targeting around $56 million, in that neighborhood in fiscal 2017? In other words, an $8 million decrease?

<A – Mark Ashby – EZCORP, Inc.>: Yeah, that's the run rate we're expecting at the moment, Bill.

<Q – Bill Armstrong – C.L. King & Associates, Inc.>: Okay, great. Thank you. I'll get back in queue.

<A – Mark Ashby – EZCORP, Inc.>: Pleasure.

Operator: Our next question comes from Mike Del Grosso with Jefferies. Your line is now open.

<Q – Mike Del Grosso – Jefferies LLC>: Good morning. Quick question actually on a similar line on the store OpEx; you mentioned the store efficiency program you're planning on running out, and wanted to ask about kind of the trajectory as we head into next year. Are there any upfront investments associated with that and how do we think about that?

<A – Stuart Grimshaw – EZCORP, Inc.>: Most of the upfront investments will be through the capital expenditure patterns. As I mentioned, the IT install refurbishments will be capital expenditure. We have – there's been a slight increase in staffing levels through the stores, so we're probably more focused on ensuring that the corporate expenses are minimized, while we continue to invest in the front. So we don't want to, I suppose, choke the stores off by pursuing a cost regime.

We're actually in a – we're into here to serve the customers and, in some of our stores, we actually have run the staffing down to a lower level, so we've already increased this. I don't think we're going to see too many more – too much more in a way of increases in store operating expenses, so I'd expect it to be pretty much flat.

<Q – Mike Del Grosso – Jefferies LLC>: Got it. Thank you.

Operator: Our next question comes from Chris Smith with GLG Partners. Your line is now open.

<Q – Chris Smith – GLG Partners>: Hi there. How are you doing?

<A – Stuart Grimshaw – EZCORP, Inc.>: Good morning.

<Q – Chris Smith – GLG Partners>: Just a couple of questions. Good morning. You talked about your sort of healthy liquidity situation right now. Just wondered if you can maybe highlight how you'll be looking to use that cash. Will it be in terms of rolling out new stores? Again, you talked about you've looked at several potentials but not really seen anything that's that attractive. Are you able to give any guidance on the number of stores that you're looking to add this coming year?

<A – Stuart Grimshaw – EZCORP, Inc.>: No, it all depends if the opportunity comes up, and that's the advantage of having liquidity is that we have the opportunity to transact in some form of size if something comes in. But, having been through two years of, I suppose, tougher liquidity conditions, I'm more than happy to actually be in a very liquid position and not transact if something doesn't meet our hurdle.

So, we want to be fairly conservative, Chris. We don't want to just pursue stores for the sake of pursuing stores, which can get us into trouble. And I think we already reiterated many times, we just have to continue to have the discipline that perhaps we haven't had in the past and make sure we have a very liquid balance sheet.

<Q – Chris Smith – GLG Partners>: Okay. So, in terms of sort of cash use, you don't really have anything else in mind in terms of...

<A – Stuart Grimshaw – EZCORP, Inc.>: No.

<Q – Chris Smith – GLG Partners>: ...you're going to remain very much focused now on the pawn business?

<A – Stuart Grimshaw – EZCORP, Inc.>: Yeah, that's correct.

<Q – Chris Smith – GLG Partners>: Okay.

<A – Mark Ashby – EZCORP, Inc.>: It's Mark here. Just in terms of our CapEx spend, coming into the year, we touched on the store refurbishment program, and so we're kicking that off. So in our CapEx expectation over the next three years now, it's probably about $55 million, but about $23 million or so could be in FY16, just depending upon how quickly we kick the refurbishment program off. But that's really up from about $13 million or $14 million in the last year.

<Q – Chris Smith – GLG Partners>: Okay, great. Thanks. Then just a follow-up question. Now, you've sold the Grupo business and the business overall is a lot cleaner, are you able to kind of give any guidance on where you see sort of revenue, EBITDA checking out this year?

<A – Mark Ashby – EZCORP, Inc.>: No. No, we don't give guidance.

<Q – Chris Smith – GLG Partners>: Okay. Okay, no problem. That's all I have. Thank you very much.

<A – Stuart Grimshaw – EZCORP, Inc.>: Thanks, Chris.

Operator: Our next question comes from Gregg Hillman with First Wilshire Securities. Your line is now open.

<Q – Gregg Hillman – First Wilshire Securities Management, Inc.>: Yeah, good morning, gentlemen.

<A – Stuart Grimshaw – EZCORP, Inc.>: Hi, Gregg.

<Q – Gregg Hillman – First Wilshire Securities Management, Inc.>: Hey. Two questions. First of all, based on some of your recent results, do you have reason to change your three-year plan in any ways in terms of expense reductions or other items in your three-year plan? And then, number two, the whole question of the impact of taking away much of the payday loan business on the pawn industry, what's the current state of the industry for states that have already shut down payday loan businesses, for like Maryland, and like the last 25 years? Have you reviewed that evidence and what does that tell us what happened?

<A – Stuart Grimshaw – EZCORP, Inc.>: On the expense reductions, we're actually – they're locked, so we're not going to change those. Once we get to the end of the three years, we'll obviously – we'll probably at the end of two, we'll start reviewing where we head from there, so there are no changes to that.

And the number of states that have actually taken payday out, we actually haven't been with. So, Maryland, we're not there. We're trying to – we're sort of looking at it at the moment. We're watching with interest what's happening with the transition going through at the moment, because we're not quite sure how the industry is going to play out. So I think everyone on both sides, be it pawn or payday, are watching with interest to see what are the first moves around discussions with the CFPB and how the Republicans look at these industries.

<Q – Gregg Hillman – First Wilshire Securities Management, Inc.>: But hasn't this already been played out several times?

<A – Stuart Grimshaw – EZCORP, Inc.>: Yeah, I don't have enough information, Gregg, to be honest to actually answer that with a degree of accuracy.

<Q – Gregg Hillman – First Wilshire Securities Management, Inc.>: Okay. And getting back to the three-year plan, so, basically, the three-year plan is more or less on track and on time and going as you outlined it when you first came?

<A – Stuart Grimshaw – EZCORP, Inc.>: Yeah, that's correct.

<Q – Gregg Hillman – First Wilshire Securities Management, Inc.>: Okay, great. Thanks.

<A – Stuart Grimshaw – EZCORP, Inc.>: Thanks Gregg.

Operator: Our next question comes from Eugene Fox with Cardinal Capital Management. Your line is now open.

<Q – Eugene Fox – Cardinal Capital Management LLC>: So, just two questions. As it relates to this bonus expense, we would have seen that in both the corporate line as well as the operation expenses. Would I assume the order of magnitude would have been similar between the two?

<A – Mark Ashby – EZCORP, Inc.>: No, I think corporate was a bit higher.

<Q – Eugene Fox – Cardinal Capital Management LLC>: Okay. And it would have all been in Q4, but conceptually, we should think about it as spread – it's for performance over the year?

<A – Mark Ashby – EZCORP, Inc.>: Correct.

<Q – Eugene Fox – Cardinal Capital Management LLC>: Got it. Second question. The Cash Converters stock that you took the write-down on, how should we think – how are you thinking about that strategically?

<A – Stuart Grimshaw – EZCORP, Inc.>: We're looking at it with interest. We have a much higher entry price. We think the company has a lot more potential than perhaps where it's reflected in the share price, but it's been going through a bit of a tough time. We'd like to try and see where value can be restored into the stock price and then consider what should be done there. So at the moment, it's pretty much let's see if we can get some of the value back on that stock. It's in a good – it seems to be a pretty good industry, it's got a great brand, and we review it every year as to what's happening, but at the moment it's a watching brief.

<Q – Eugene Fox – Cardinal Capital Management LLC>: Okay. Thank you.

Operator: Our next question comes from Todd Meadow with Nomura. Your line is now open.

<Q – Todd Meadow – Nomura Securities>: Hey, guys. Congratulations on a great quarter and continued execution on your plan. Just wanted to ask a question about the notes receivable. So, at the bottom of slide nine, the footnote, percentage of notes secured, can you provide a little detail around that?

<A – Mark Ashby – EZCORP, Inc.>: Yeah. Some of the notes are actually secured against some of the loan portfolio that Grupo Finmart have, so it's a direct security over those lines.

<Q – Todd Meadow – Nomura Securities>: Got it, and do you--

<A – Mark Ashby – EZCORP, Inc.>: And it's collateralized, is a better way to describe it.

<Q – Todd Meadow – Nomura Securities>: Do you have a reserve account for uncollectability of that at all, or?

<A – Stuart Grimshaw – EZCORP, Inc.>: It's over-collateralized.

<A – Mark Ashby – EZCORP, Inc.>: Yeah.

<A – Stuart Grimshaw – EZCORP, Inc.>: So, it's over-collateralized, so by default, the reserve sits within the over-collateralization.

<Q – Todd Meadow – Nomura Securities>: Okay. I got it. Thank you.

Operator: Thank you. And I'm showing no further questions. I would now like to turn the call back over to Stuart Grimshaw for any further remarks.

Stuart I. Grimshaw, Chief Executive Officer & Director

Thanks very much, and thanks for dialing in, or if you logged into the webcast, thanks for listening to us. Mark Ashby and Jeff Christensen are available for follow-up questions later this day, so this concludes the call and thanks everyone for dialing in. Have a great day.

Operator: Ladies and gentlemen, thank you for participating in today's conference. You may all disconnect. Everyone have a great day.