Credit Ratings & Research

General Finance Limited

NZBN: 9429038072994

Credit Rating Synopsis

Date: 10/01/2020

Prepared for: General Finance Limited

Report prepared by: Equifax Australasia Credit Ratings Pty Ltd (“Equifax”)

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Job Number: 326007

Currency used in this report: This report is presented in New Zealand Dollars unless otherwise noted

Corporate Scorecard
From Equifax

Contents

1. Executive Summary

General Finance Limited ("GF", "the Company")

GF is Non-Bank Deposit Taking (NBDT) organisation that is licenced and domiciled in New Zealand. The Company offers secured loans and accepts customer deposits. Equifax has affirmed General Finance Limited's 'BB-' credit rating at Sep 2019. The Outlook for the rating is Positive.

GF's credit rating reflects its strong capital and funding position, its acceptable asset quality metrics – mainly conservative Loan to Value Ratios (LVRs), and its specialised market position as a short-term bridging loan specialist. The rating is also supported by the Company's stable profitability and liquidity. Meanwhile, the rating is constrained by GF's small scale, exposure to higher-risk borrowers and moderately high concentration to a few borrowers and depositors. Our outlook for the rating is positive, based on the Company's focus on, and capacity to finance, near-term growth targets.

Strengths

- GF's niche market position as a short-term and bridging loan specialist, catering to a market underserved by many industry competitors, supports its competitive position and profitability. Despite net-interest margins (NIMs) decreasing to 3.28% in the H1FY20 (FY19: 3.42%, FY18: 4.47%) as management focused on asset and deposit growth, NIMs remain healthy and in line with the industry median. GF's NIMs, together with low instances of non-performing loans, support its consistently positive earnings.

- GF's low impaired loan metrics are reflective of its asset quality and conservative lending policies. The Company's conservative LVR – with a maximum permitted LVR of 75% and average loan book LVR of 45.2% at Sep19 (Jun19: 50.2%), reduces the risk of loss upon a credit event's occurrence, while the management's policy to primarily accept general use residential properties as collateral increases our confidence in GF's risk management.

- GF is well funded and capitalised. A capital ratio of 24.8% at Sep19 (Jun19: 28.0%, Mar19: 33.7%) supports the Company's growth plans, while maintaining adequate headroom to regulatory and GF's trust deed minimum capital ratio threshold. Furthermore, the Company's parent – General Capital Ltd, has recently listed on the NZ stock exchange and has injected $1.9m in equity into GF since Mar18. This, together with strong growth in consumer deposits during the preceding 24 months, means that GF is suitably positioned to execute its growth plans.

-GF's positive short-term asset liability duration gap supports is liquidity position. Unlike most industry peers, GF uses longer dated consumer deposits to underwrite shorter duration loans, which supports the Company's capacity to withstand a stressed liquidity scenario. The Company's liquidity is further supported by its internal guidelines to hold a minimum of 10% of total assets in cash/ equivalents. Benefitting from strong deposit growth during the recent months, liquid assets to total assets improved to 23.8% at Sep19 (Mar19: 13.9%)

Weaknesses

- GF's primary reliance on the underlying collateral for the loan, exposes the Company to a higher degree of market risk and credit risk than traditional banks or non-bank financial institutions. The Company underwrites secured short-term interest-only loans to higher-risk borrowers, wherein recurring earnings of the borrower are not the primary source of the loan's principal repayments. As such, any adverse developments in the underlying housing and real estate market segments may potentially expose the Company to an increase in credit and/or liquidity risk, and a reduced collateral cover. However, the Company mitigates this risk by continuing to maintain a conservative average collateral cover on its loan book.

- A weaker growth in loan book compared to the rate of growth in deposits, may supress the Company's earnings. During H1FY20, 74.8% loan book growth (annualised) was significantly lower than the forecast for FY20 (159%) and as deposits grew by 144% (annualised), excess liquidity supressed GF's portfolio yield and NIMs for the period. We note the Company is undertaking measures to balance deposit and loan-book growth, which is likely to counter these risks.

- GF's small scale underlines a high concentration risk in its operations. At Sep19, GF's top-six loans accounted for 125% of total equity (Jun19: 104%), while the largest depositor accounted for 12.4% of total deposits (Jun19: 13.4%). However, management's continued focus on deposit growth and loan book diversification is expected to reduce some of these concentration risks, going forward.

- GF's growth plans and scalability are moderately constrained by its reliance on key executives' expertise. An absence of formal financial and qualitative metrics for loan approval mean GF has a high reliance on its key executives' expertise for loan origination and approval, thereby exposing it to keyperson and business continuity risks. Further, the Company's executive team is small and is expected to require additional operational support to manage and monitor risks for a larger loan book.

The outlook for the rating is positive, and a rating upgrade maybe premised upon a sustainable improvement in scale and franchise coupled with the introduction and implementation of more prescriptive credit and risk management policies.
There may be downward pressure on the rating if either the Company's asset quality, capital ratio or liquidity position materially deteriorate, on an individual or a collective basis.

Risk Rating

BB-

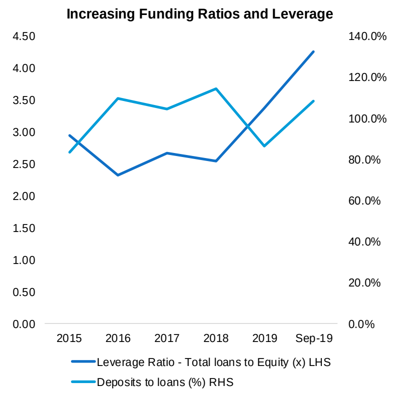
Outlook: Positive

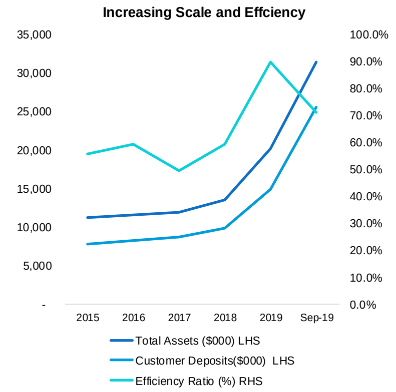
Type: Public, Monitored

Industry Percentiles

Scale:	
Total Assets	25%
Gross loans	25%
Profitability:	
NIM	25%
ROE	42%
ROA	42%
Efficiency Ratio	58%
Capitalisation:	
Leverage (Gross loans to Equity)	75%
Capital Ratio	100%
Capital to Total Assets	67%
Funding and liquidity:	
Deposits to loan ratio	75%
Liquid assets to total assets	92%
Asset Quality:	
Net Charge-offs	100%
Non performing loans	100%
Provision for loan losses	83%

Key Trends





2. Scope of Report

The purpose of this report is to provide a Credit Rating Synopsis on General Finance Limited ("GF", "the Company").

We have complied with our rating services guidelines in order to derive the credit rating on General Finance Limited. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold or sell any securities or make any other investment decisions. The details pertaining to this report are outlined below:

Report Details	
Date of Report	**10 January 2020**
Request Type	**Issuer**
Assessment Type	**Under Ongoing Monitoring**
Rating Initiation	**Issuer based (solicited)**
Rating Distribution	**Public Rating**
Report Distribution	**Unrestricted**
Purchased by	**General Finance Limited**
Report Fee	**Fixed Price**
Ancillary fees	**Nil**
Issuer Name	**General Finance Limited**
Issue Name	**Not Applicable**
Issuer First Time Rated	**No**
Issue First Time Rated	**Not Applicable**
Financial Scope	**Standalone Entity**
Structure	**Limited Company**
Industry	**Financial Services**

This report should be read within the context of Corporate Scorecard's Rating Services Guide. This Report should be taken as a whole and cannot be abridged or excerpted for any reason.

We have conducted this assessment on the basis of the information provided to us by General Finance Limited, publicly available information and from our own enquiries. We have derived a credit rating on the Company based on the understanding that General Finance Limited has no contingent liabilities, cross guarantees or other liabilities to any other entity other than as disclosed to us or as detailed in the financial statements. Our duty does not include auditing the financial statements.

Information Sources	
Financial statements	**Audited Financial Statements for the years ended 31 March 2019, 2018 and 2017.** **Audited Interim Financial Statements for the 6-month period ended 30 September 2019.**
Name of auditor	**Baker Tilly Staples Rodway Auckland**
Other Information Sources	**The Company's response to our Request for Information, AML & CFT Audit report by William Buck Audit (NZ) Limited as at Mar19, the Company website, industry and regulatory websites, management interviews, media articles, adverse searches and internet searches.**
Subject participation	**Yes**
Material financial adjustments	**None**
Limitations of assessment	**None noted**
Outsourced rating activities	**No**
Confidentiality agreement	**No**
Material client	**No**
Rating amended post issuer disclosure	**No**
Potential conflict of interest	**GF is also a user of other Equifax products which are procured on commercial terms.**
Rating methodology	**Financial Institution Rating Criteria**

This report should be read within the context of Equifax's Ratings Services Guide.

APPENDICES

1. Explanation of the Equifax's credit rating

1.1 What is a rating?

Credit ratings provide an Agency's opinion as to the capacity, viability and willingness of an entity, issuer, or counterparty to meet their respective financial commitments. As such, Equifax assigns ratings based on the credit worthiness of an entity, commitment or product, and provides probabilistic assessments of default over the short, medium and long-term.

Credit ratings are a critical measure used extensively in commercial, financial and capital markets to support key business decisions. Equifax's credit ratings are used to support debt and bonding decisions, loan origination and recovery, insurance and warranty, funds management, portfolio management, tendering and procurement, counterparty risk assessments and other commercial contracts.

Equifax provides credit ratings on government and commercial agencies, international conglomerates, infrastructure consortia, financial institutions, publicly listed entities, private corporations and small-to-medium sized enterprises across a range of industry sectors both domestically and internationally. As such, Equifax is also able to provide detailed industry intelligence, benchmarking reports and analysis across a wide range of sectors.

1.2 Equifax's credit rating

Equifax and other credit rating agencies all attempt to measure the probability of an entity being able to honour its financial commitments as and when they fall due. The most recognised credit rating is that based on Bond Rating Equivalents (BRE) used over the past eighty years to determine the proximity of an entity's securities to default (non-payment of interest or principal). The accuracy of this method has been extensively tested and is accepted worldwide.

The Equifax's database contains more than 100,000 financial years of information spanning more than twenty-five years. As such Equifax is in a unique position, having developed a large and empirical data source on entities across various industry sectors with long data histories covering a range of economic conditions and one or more complete business cycles. Equifax has therefore been able to use a variety of quantitative validation tools and comparisons using this information to adequately verify the stability, accuracy and consistency of its rating models.

Equifax's rating models have been designed to assess the proximity of an entity to defaulting on its financial commitments and obligations. Proprietary risk analytics are used to evaluate the multivariate interrelationship of key risk indicators using scientifically based and empirically derived risk metrics. These models evaluate the financial performance, position and profile of an entity in the context of its industry, size and structure. They have been validated on Australian and international data with the assistance of Professor Edward Altman, an internationally recognised leader in the field of credit risk analysis and bankruptcy prediction.

Equifax uses its comprehensive benchmarking database to evaluate the financial position, performance and credit quality of an agency, institution, corporation or entity relative to an industry and its peers. This enables the identification of key sensitivities, trends, cautionary alerts and exception reports based on identified anomalies and/or outliers across key credit indicators of a select benchmarking group.

While there is no single method to discriminate unambiguously between firms that will default and those that will not, Equifax can make probabilistic assessments of default. This requires a large database of actual defaults to enable an assessment of default probabilities and actual default rates from empirical evidence. The Australasian market has a comparatively small number of corporate bond issues and a relatively benign credit climate over recent decades, and as such empirical data on Australian default rates is limited. Therefore, Equifax considers it is more appropriate to apply default probabilities using empirical data from international markets over several economic cycles.

Equifax's default statistics have been derived from nearly twenty years' experience analysing mainly US non-financial, non-utility corporate bond issuers. The analysis covered a relatively large number of companies (approximately 1,000 rated each year) and follows the well-established static pool approach used by Credit Rating Agencies to report their default experience. Static pools were created for bond issuers each year by both notch and grade, and the history of these bond issuers was then analysed over the period. The pools were then combined so that long-term average default experience by duration could be calculated, and both annual and cumulative default experience was calculated from the pools.

Equifax's risk analytics enable analysts to evaluate the most critical and sensitive financial and risk items through the Risk Assessment Platform by analysing key indicators to derive a definitive credit risk score and Bond Rating Equivalent (BRE), providing Probabilities of Default (PoD) over the short-, medium- and long-term horizon.

1.3 Rating Definitions

Credit ratings provide an Agency's opinion as to the capacity, viability and willingness of an entity to meet their respective financial and contractual commitments. As such credit ratings are assigned in accordance with the entity, commitment or product's proximity to default. Equifax adheres to internationally recognised grades and are similar to other agency classifications, providing ratings across twenty-two credit notches from 'D' (in default) to 'AAA' (extremely strong).

Moody's	Fitch	S&P	Rating	Default rates (5 years)	Classification	Risk Level
Aaa	AAA	AAA	AAA	0.17	High Grade	Negligible
Aa1	AA+	AA+	AA+	0.31		
Aa2	AA	AA	AA	0.44		
Aa3	AA-	AA-	AA-	0.55		
A1	A+	A+	A+	0.76	Investment Grade	Very Low
A2	A	A	A	0.81		
A3	A-	A-	A-	1.47		
Baa1	BBB+	BBB+	BBB+	2.08		Low
Baa2	BBB	BBB	BBB	3.19		
Baa3	BBB-	BBB-	BBB-	4.37		
Ba1	BB+	BB+	BB+	7.13	Near Prime	Low to Moderate
Ba2	BB	BB	BB	7.49		
Ba3	BB-	BB-	BB-	10.52		
B1	B+	B+	B+	16.34	Sub Prime	Moderate
B2	B	B	B	22.21		
B3	B-	B-	B-	24.16		High
Caa1	CCC	CCC+	CCC+	28.16	Credit Watch	Very High
Caa2		CCC	CCC	29.90		
Caa3		CCC-	CCC-	39.16		
Ca		CC	CC	52.87	Distressed	Extremely High
		C	C	55.00		
C	D	D	D	100.00		

Equifax assigns ratings based on the credit worthiness of an entity or a specific financial commitment, and provides probabilistic assessments of default over the short, medium and long-term. Every entity or commitment has some probability of default over a period of time, even those assigned with the strongest of ratings. An Investment Grade classification is attributed to credits that exhibit a lower probability of default, while a Sub-Prime classification has a greater expectancy of default.

An Equifax's credit rating may also be assigned additional clarification markers (symbols) to qualify the credit risk assessment. These may include:

Conditional Rating (#)
A Conditional Rating is used where Equifax has rated an entity on the basis of significant risk factors and/or report qualifications, with recommendations providing one or more conditions precedent and/or mitigation action(s) to reduce identified uncertainty and risk.

Provisional Rating (*)
A Provisional Rating is used when the most recent financial figures are based on draft management accounts or are deemed out-of-date. Entities with a provisional rating should be re-evaluated as soon as finalised financial statements become available.

Indicative Rating (^)
An Indicative Rating is used where Equifax is engaged to conduct preliminary analysis only, and as such an official rating assignment would require a more detailed and comprehensive investigation and due diligence assessment prior to the provision of our professional opinion.

1.4 Rating Outlooks

Equifax's forward estimates help ascertain the trajectory of ratings as well as the risks to ratings. Ratings with a positive trajectory are assigned 'Positive Outlooks'. Ratings with a negative trajectory are assigned 'Negative Outlooks'. Where Ratings are expected to remain unchanged, a 'Stable Outlook' assigned.

Rating trajectories are closely related to the outlook for the corporate's earnings. Earnings growth that is within sustainable growth parameters together with an attenuation of earnings volatility provide upward rating pressure and so may warrant the assignment of a Positive Outlook.

Credit Concepts measured

The main credit concepts measured against Australian and New Zealand Standard Industry Classifications (ANZSIC) and specific Peer Groups based on entity size are available in Corporate Scorecard's Rating methodology, which can be found at the below-mentioned links

http://corporatescorecard.com.au/services_credit_ratings.php

http://corporatescorecard.com.au/docs/RatingMethodologyFinancialInstitutionRatingCriteria.pdf

2. Regulatory Disclosures and Disclaimer

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Equifax Credit Ratings also holds an Australian Financial Services License (AFS License no. 341391) which licenses it to provide credit ratings to wholesale clients in Australia.

The credit rating issued by Equifax Credit Ratings reflects our current opinion of the relative credit risk of the institution. This opinion has been formed in accordance with Equifax's published credit ratings methodology - financial institution rating criteria (version 5, 2018).

http://www.corporatescorecard.co.nz/docs/RatingMethodologyFinancialInstitutionRatingCriteria.pdf

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