Harmoney Corp Ltd

HMY.AX

A research platform of MST Financial

30 August 2023

Scalability driving profitability

Material revenue and profit growth delivered in FY23.

- Cash NPAT growth to $4.7m (up from $0.2m pcp).
- Revenue growth to $107m (up from $73m pcp).
- Stellare 2.0 launched to accelerate operating leverage.

Sustainable top and bottom-line growth in FY23: Harmoney's FY23 results delivered 28% loan book growth (to $744m), a 47% growth in revenues (to $107m) and a significant growth in Cash NPAT to $4.7m (up from $0.2m in FY22).

Stellare 2.0 to unlock new growth avenues: Harmoney's August 2023 launch of its next-generation lending platform (Stellare 2.0) provides a basis for the execution of managements announced strategic growth priorities – a renewed focus on market share capture of the $143B Australian personal loan market with a decreasing marginal cost of originations owing to an increasing proportion of return customers which have near zero acquisition expenses, and the development of new credit products to increase available users and customer lifetime value.

Diversified funding and headroom for scale ambitions: Harmoney have expanded total facilities to over $1.2B including unused capacity of $330m, with its August 2023 announced fifth "Big-4 Bank" warehouse adding $140m, including a new global mezzanine funder, and the settlement of its inaugural New Zealand securitisation adding NZ$200m.

Investment Thesis

Targeting >20% Cash ROE run-rate by FY25: Harmoney reported an 8.4% Cash ROE in its FY23 results, on the back of a record $4.7m cash NPAT. Inside we analyse the key drivers of Harmoney's FY23 result and outlook as Harmoney progresses towards guidance of 20% Cash ROE in FY25.

Exceptional performance unfairly discounted: Harmoney has defied sector sentiment in FY23 maintaining profitable growth on a cash basis, operating with a 9.6% NIM and demonstrating premium asset quality with impairments of just 3.6% in FY23 and 90+ day arrears of 0.58%, a fraction of the 1.4% Equifax Australian personal loan average.

Valuation

Undemanding valuation, even less when excluding cash. At the current share price, we estimate HMY is trading on a Cash PE of just 9.3x FY23A, and P/B of just 0.82x. Our general residual income model produces a valuation of $2.50 using an 11.5% cost of equity, representing a 474% upside.

Risks

Being a finance company, Harmoney has a range of risks applicable including macroeconomic conditions, liquidity and funding risks, credit risk, fraud, cybersecurity, asset-liability mismatch and compliance risks. With New Zealand having entered recession, and speculation that Australian might, the market appears to be predominantly concerned with a deterioration in credit quality.

Equities Research Australia

Financials

Glen Wellham, Senior Analyst
glen.wellham@mstaccess.com.au

Harmoney's purpose is to help people achieve their goals through financial products that are fair, friendly, and simple to use.

Harmoney is an online direct personal lender that operates across Australia and New Zealand providing customers with unsecured personal loans, and secured and unsecured auto loans, that are easy to access, competitively priced (using risk-adjusted interest rates) and accessed 100% online.

Harmoney's proprietary digital lending platform, Stellare™, facilitates its personalised loan product with applications processed and loans typically funded within 24 hours of acceptance by the customer. Stellare™ applies a customer's individual circumstance to its data-driven, machine learning credit scorecard to deliver automated credit decisioning and accurate risk-based pricing.

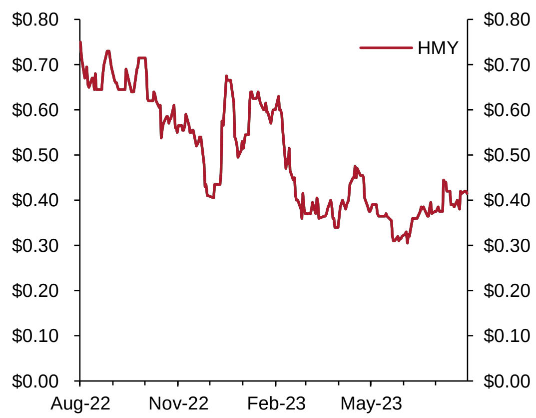
https://www.harmoney.com.au/

Valuation	A$2.50 *(previously $3.17)*
Current price	A0.44
Market cap	A$44.20m
Unrestricted cash on hand	$27.5m

Upcoming Catalysts / Next News

Late October 2023	1Q23 Result
15 November 2023	Annual General Meeting

Share Price ($A)



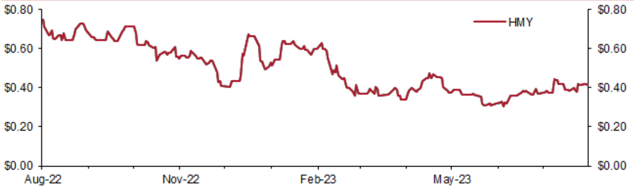
Source: FactSet, MST Access

HARMONEY CORP LIMITED — HMY-AX

Year end 30 June, A$

MARKET DATA		
Price	A$	$0.44
Valuation	A$	$2.50
52 week low - high	A$	1.20 - 0.75
Market capitalisation	A$m	44.2
Shares on issue (basic)	m	101.6
Options / rights (currently antidilutive)	m	0.0
Other equity	m	0.0
Shares on issue (fuly diluted)	m	101.6

12-MONTH SHARE PRICE PERFORMANCE (A$)



INVESTMENT FUNDAMENTALS		FY22A	FY23A	FY24E	FY25E	FY26E
EPS - diluted reported	cps	-18.6	-6.7	-8.1	-2.2	4.4
EPS - diluted cash	**cps**	**0.2**	**4.7**	**4.4**	**10.1**	**14.8**
EPS growth	%	-101%	2593%	-5%	128%	47%
Reported PE	x	-2.3	-6.5	-5.4	-19.4	9.8
Cash PE	x	251.6	9.3	9.9	4.3	2.9
DPS	cps	0.0	0.0	0.0	0.0	0.0
Franking	%	n.a.	n.a.	n.a.	n.a.	n.a.
Dividend yield	%	0%	0%	0%	0%	0%
Payout rato	%	0%	0%	0%	0%	0%
Operating cash flow per share	cps	353.6	23.6	7.1	16.2	24.9
Free cash flow to equity per share	cps	-992.1	-14.0	0.3	7.4	13.4
FCF yield	%	-2281%	-32%	1%	17%	31%
Enterprise value	$m	27.7	36.5	40.9	38.5	30.1
EV/Total Income	x	0.4	0.3	0.3	0.2	0.1
EV/Net lending income	x	0.9	1.0	1.2	0.9	0.6
EV/Net operating margin	x	3.2	1.6	1.9	1.2	0.7
NAV per share	A$	0.59	0.53	0.45	0.43	0.47
NTA per share	A$	0.42	0.33	0.23	0.17	0.17
Price / NAV	x	0.74	0.82	0.97	1.02	0.92
Price / NTA	x	1.04	1.31	1.93	2.60	2.54

KEY RATIOS		FY22A	FY23A	FY24E	FY25E	FY26E
NTA/Net Receivables	%	7.6%	5.1%	3.9%	3.6%	3.8%
Proforma ROE - reported	%	-29.0%	-12.0%	-16.5%	-5.1%	9.9%
Proforma ROE - cash	%	0.3%	8.4%	9.0%	23.0%	33.1%
Net corporate debt	**A$m**	**-16.5**	**-7.7**	**-3.3**	**-5.7**	**-14.0**
Gross debt / equity	x	929%	1303%	1993%	2611%	2852%
Leverage (net debt / invested capital)	x	-39%	-17%	-8%	-15%	-42%

DUPONT ANALYSIS		FY22A	FY23A	FY24E	FY25E	FY26E
Net Profit Margin	%	-26%	-7%	-6%	-1%	2%
Asset Turnover	x	15%	15%	15%	16%	16%
Return on Assets	%	-4%	-1%	-1%	0%	0%
Financial Leverage	x	769%	1259%	1782%	2462%	2903%
Return on Equity	%	-29%	-13%	-17%	-5%	10%

HALF YEARLY DATA		2H22A	1H23A	2H23A	1H24E	2H24E
Total income	A$m	40.6	50.1	57.0	62.6	71.2
Net lending income	A$m	10.0	17.5	17.4	15.5	17.8
Net operating margin	A$m	-0.6	11.0	11.6	9.7	11.9
Reported NPAT	A$m	-14.0	-3.4	-4.2	-4.8	-3.4
Cash NPAT	A$m	0.3	2.3	2.4	1.0	3.5
EPS - diluted cash	**cps**	**0.3**	**2.3**	**2.3**	**0.9**	**3.5**
EPS - diluted reported	cps	-13.8	-3.3	-4.1	-4.8	-3.3
DPS	cps	0.0	0.0	0.0	0.0	0.0

KEY PERFORMANCE INDICATORS		FY22A	FY23A	FY24E	FY25E	FY26E
Group originations	A$m	442.5	426.2	419.2	508.1	570.9
Warehouse funded % of book (average)	%	79%	96%	100%	100%	100%
Gross loan receivables	A$m	581.0	744.0	947.6	1,181.2	1,414.1
Average gross loan receivables (AGR)	A$m	432.5	683.1	841.7	1,064.7	1,297.5
Growth in AGR	%	117%	58%	23%	26%	22%
Interest income / AGR	%	15.9%	15.5%	15.9%	16.0%	16.0%
Interest expense / AGR	%	-4.2%	-5.8%	-6.7%	-6.7%	-6.7%
Net interest margin	%	11.8%	9.6%	9.2%	9.3%	9.3%
Incurred credit losses / AGR	%	2.45%	3.6%	4.11%	4.19%	4.22%
Net lending margin / AGR	%	8.40%	5.1%	3.96%	4.06%	4.21%
Cost to income ratio	%	37%	26%	22%	19%	17%
New business expenses / total costs	%	52.3%	22.7%	21.8%	3.4%	-27.8%

PROFIT AND LOSS		FY22A	FY23A	FY24E	FY25E	FY26E
Interest income	A$m	68.9	105.5	133.8	170.3	207.5
Fee income	A$m	3.9	1.5	0.0	0.0	0.0
Other income	A$m	0.0	0.0	0.0	0.0	0.0
Total income	**A$m**	**72.8**	**107.1**	**133.8**	**170.3**	**207.5**
Interest expense	A$m	-18.1	-39.8	-56.1	-70.8	-86.7
Incurred credit losses	A$m	-10.6	-24.6	-34.6	-44.7	-54.7
Risk Adjusted Income	**A$m**	**44.1**	**42.7**	**43.1**	**54.8**	**66.1**
Movement in ECL provision	A$m	-14.9	-7.8	-9.8	-11.5	-11.5
Net lending income	**A$m**	**29.2**	**34.9**	**33.3**	**43.3**	**54.6**
Marketing expenses	A$m	-20.7	-12.3	-11.7	-12.1	-12.4
Net operating margin	**A$m**	**8.5**	**22.6**	**21.6**	**31.2**	**42.2**
Personnel expenses	A$m	-9.8	-11.0	-11.8	-13.5	-14.7
Share based payments	A$m	-2.7	-1.9	0.0	0.0	0.0
Customer servicing expenses	A$m	-5.2	-6.2	-6.3	-6.8	-7.2
Technology expenses	A$m	-4.2	-4.8	-4.9	-5.2	-5.7
General and administrative expenses	A$m	-4.0	-3.7	-3.8	-4.4	-4.8
Depreciation and amortisation expenses	A$m	-1.3	-2.5	-2.9	-3.1	-3.4
Profit before income tax	**A$m**	**-18.8**	**-7.6**	**-8.1**	**-1.8**	**6.4**
Income tax expense	A$m	0.0	0.0	-0.1	-0.5	-1.8
Reported NPAT	**A$m**	**-18.8**	**-7.6**	**-8.2**	**-2.3**	**4.5**
Adjustments	A$m	3.2	12.3	12.7	12.5	10.5
Cash NPAT	**A$m**	**1.9**	**4.7**	**4.5**	**10.2**	**15.1**
Weighted average diluted shares	m	1.4	101.6	101.6	101.6	101.6

BALANCE SHEET		FY22A	FY23A	FY24E	FY25E	FY26E
Unrestricted cash	A$m	31.2	27.5	23.1	25.5	33.9
Finance receivables	A$m	551.4	708.9	900.8	1,123	1,344
Property, plant and equipment	A$m	0.4	3.7	4.6	5.9	7.8
Goodwill and other intangibles	A$m	8.5	11.6	14.3	18.4	24.3
Other assets	A$m	43.3	34.1	41.4	30.2	30.0
Total Assets	**A$m**	**634.9**	**785.7**	**984.1**	**1,203**	**1,440**
Trade and other liabilities	A$m	6.4	9.9	9.9	9.9	9.9
Borrowings - receivables funding	A$m	549.5	700.7	907.8	1,130	1,363
Borrowings - corporate debt	A$m	14.7	19.8	19.8	19.8	19.8
Provisions	A$m	5.2	1.5	1.0	0.0	0.0
Total Liabilities	**A$m**	**575.8**	**732.0**	**938.6**	**1,160**	**1,393**
Net assets	**A$m**	**59.1**	**53.8**	**45.6**	**43.3**	**47.8**
Net tangible assets	**A$m**	**42.3**	**33.7**	**22.9**	**17.0**	**17.4**
Invested capital	**A$m**	**42.6**	**46.1**	**42.3**	**37.6**	**33.7**
Tangible invested capital	**A$m**	**25.8**	**26.0**	**19.6**	**11.3**	**3.3**
Contributed equity	A$m	123.3	124.0	124.0	124.0	124.0
Treasury shares	A$m	0.0	0.0	0.0	0.0	0.0
Reserves	A$m	7.4	8.9	8.9	8.9	8.9
Retained earnings/accumulated losses	A$m	-71.5	-79.1	-87.3	-89.6	-85.1
Non-controlling interests	A$m	0.0	0.0	0.0	0.0	0.0
Total equity	**A$m**	**59.1**	**53.8**	**45.6**	**43.3**	**47.8**
Basic shares on issue	m	101.0	101.6	101.6	101.6	101.6

CASH FLOW		FY22A	FY23A	FY24E	FY25E	FY26E
Operating						
Net operating cashflow	**A$m**	**5.0**	**23.9**	**7.2**	**16.4**	**25.3**
Investment						
Capital expenditure	A$m	-6.3	-5.0	-6.4	-8.5	-11.3
Acquisitions and divestments	A$m	-312.6	-181.6	-203.6	-233.7	-232.9
Net investment cashflow	**A$m**	**-318.9**	**-186.7**	**-210.0**	**-242.2**	**-244.2**
Financing						
Equity	A$m	0.0	0.0	0.0	0.0	0.0
Debt	A$m	300.8	149.0	203.6	233.7	232.9
Leases	A$m	-0.8	-0.5	-0.4	-0.4	-0.4
Net financing cashflow	**A$m**	**300.0**	**148.5**	**203.1**	**233.2**	**232.5**
Net cash flow	**A$m**	**-13.9**	**-14.2**	**0.3**	**7.5**	**13.6**
Free cash flow to equity	A$m	-13.9	-14.2	0.3	7.5	13.6

Source: HMY reports, MST Access estimates

FY23 Results Analysis and Outlook

Risk Adjusted Income

(RAI) = Revenue - Funding – Credit Losses

Income

As of 30 June 2023, Harmoney's loan portfolio was $744m up $163m (or 28% on pcp), driven by $426m in originations during the period. This was a 4% reduction in origination volumes on the prior year, led by a deliberate moderation in growth expenses to focus on delivering profitability, including a 41% reduction on marketing costs (customer acquisitions costs) on the prior year.

Interest income for FY23 was $105.5m (up 53.5% on pcp) driven by growth in the average loan book, however tempered by a marginally lower average interest of 15.5% (was 15.9%). However, management have highlighted a 15.7% average portfolio interest for June 2023, following interest rate increases on new lending.

Management have also pointed to reduced levels of early repayments compared to the prior year, with reducing mortgage refinancing activity due to rising interest rates.

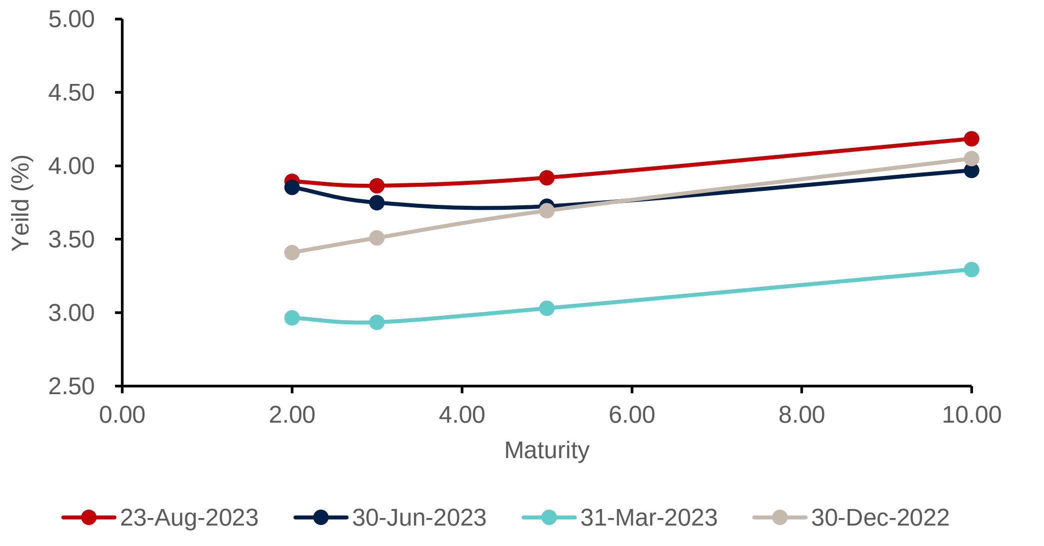
Funding Costs

Harmoney's FY23 interest costs were $39.8, up a significant 120% on pcp, due to loan book growth and a material shift in interest rates from abnormal lows experienced in FY22.

During the period RBA and RBNZ increased official cash rates by 3.25% and 3.50% respectively, with Harmoney's average funding rate increasing to 6.0%, up from 4.5% in FY22. Harmoney's hedging strategies have softened effects of the underlying cost of fund increases in FY23, however as these positions expire management expect the average cost of funds to stabilise close to 7% in the near term.

Interest rate expectations have changed rapidly in the past few months, however based upon the market data and statements by Harmoney, interest rate expectations are stabilising. In recent weeks, the inversion of the Australian government bond yield curve, representing a fall in risk-free rate expectations in the short term, has lessened in intensity. Although the expectations of significant short term rate cuts have diminished, this should still be positive for Harmoney's average funding costs moving forward, as it signals a potential crest or plateau in the RBA's current monetary policy tightening cycle.

Figure 1: Australian Government Bond Yeilds (%)



Source: RBA Capital Market Yields – Daily F2

Credit Quality

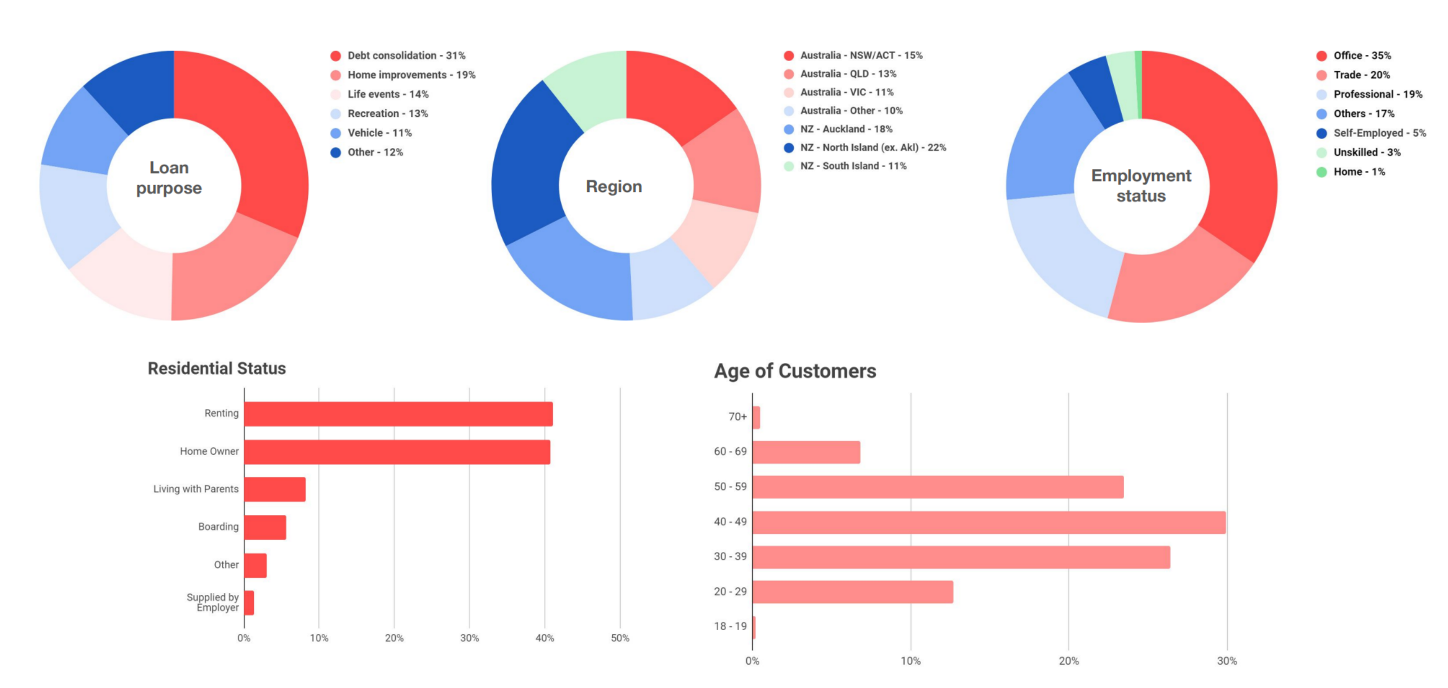
As Harmoney's secured product line (car loans) has only recently been launched earlier this year, most of their book is still unsecured loans, which typically have both higher lending rates and a higher cost of wholesale funding associated with operations due to the absence of collateral for recovery in the event of default, which increases the overall risk. As such Harmoney's realised credit losses are slightly higher than some its peers given its loan book is heavily skewed towards unsecured lending, however this is offset and accounted for in the risk adjusted lending rates, delivering a risk adjusted income margin of 6%

The FY23 results reported 90+ day arrears of 0.58% and an increase in incurred credit losses to 3.6% of the average loan portfolio (FY22: 2.5%) due to "seasoning" of the loan book following rapid prior year growth. Management commentary suggests personal loans reach peak distress 12-18 months into the term. The FY23 figures remain with managements 3-4% target range.

Management have also highlighted the diversification of Harmoney's loan book provides resilience to macroeconomic disruptions, given its broad exposure to economically secure customers, including approximately:

- 40% owning their own home.
- 74% either employed in an office, trade, or professional capacity.

Figure 2: Diversification of Harmoney's 30 June 2023 Loan Book



Source: RBA Capital Market Yields – Daily F2

Harmoney has maintained a stable provision rate of 4.9% of loan book from FY22 to FY23, resulting in a FY23 movements of provisions of $7.8m due to growth in the loan book. (This is excluded from the calculation of Cash NPAT, which only recognised realised credit losses incurred in the period). Due to a forecast continued loan book expansion the coming periods, movements in provisions are expected to be a significant drag on statutory profitability.

Net Operating Income

(NOI) = RAI – Acquisition Costs

Acquisition Costs

In a testament to the strength of Harmoney's consumer direct model, Harmoney's customer acquisition expense to origination ratio improved from 4.7% in FY22 to 2.9% in FY23 following a deliberate moderation in acquisition expenses, with exceptional growth from existing (repeat) customers with repeat customer originations growing 9% on pcp.

Under Harmoney's consumer-direct model its acquisition costs largely comprise online advertising to prospective customers. These costs are expensed up front in the period that they are incurred, not amortised over the life of the loan. Due to the consumer-direct (non-broker intermediated) relationship, when these existing customers return for a subsequent loan this is at near zero origination cost to Harmoney, resulting in an annuity style income stream from Harmoney's up front acquisition cost.

Due to characteristics of the consumer direct model, Harmoney recognises the acquisition expense of acquiring the 'lifetime value' of an annuity style income stream, as originations to returning existing customers have a near zero acquisition cost.

In comparison to broker or dealer led models where acquisition costs are typically amortised over the life of each loan (i.e. commissions), Harmoney's customer acquisition expense to origination ratio is expected to continue to improve as the proportion of loans to existing customers continues to increase.

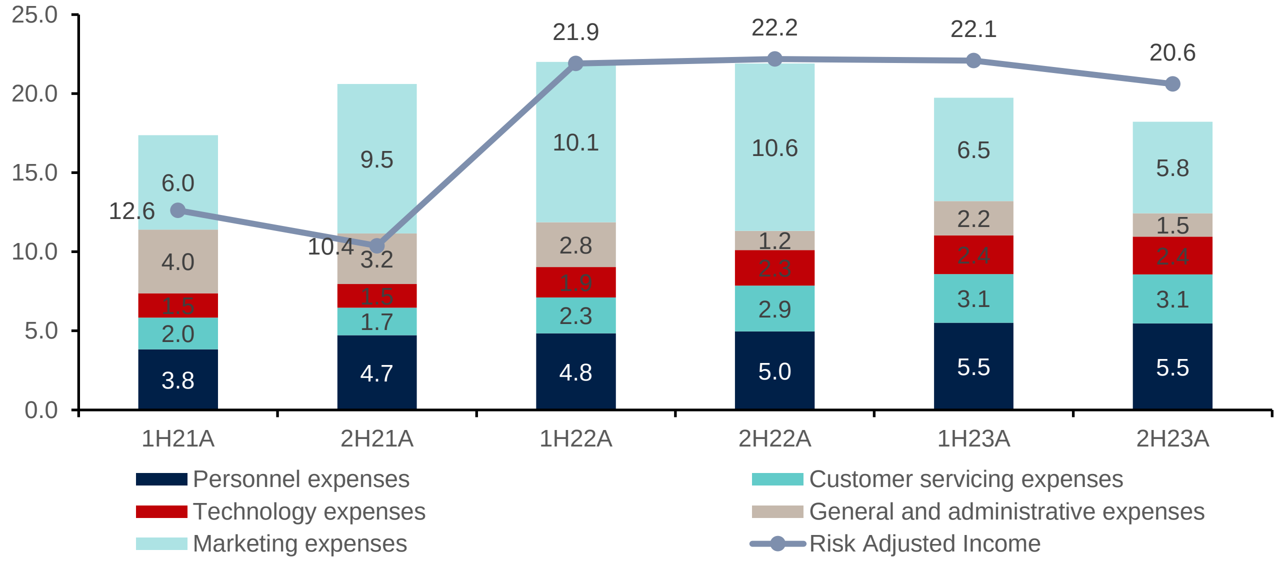
The launch of Stellare 2.0 is expected to continue to improve marketing efficiency in FY24.

Operating Costs

In a demonstration of operating leverage afforded by the consumer-direct model and efficacy of its proprietary Stellare platform, a 900bp improvement in its cost-to-income ratio to 28% in FY23, down from 37% on the prior year. This figure includes all operating costs which bridge Net Operating Income and Statutory NPAT.

Personal expenses were higher in 2H23 driven by additional investment in development capabilities as well as inflationary pressures on salaries driving an increase in cash expenses, however still maintained a considerable buffer afforded by Harmoney's emerging operating leverage.

Figure 3: Cash Expenses (A$m)



Source: RBA Capital Market Yields – Daily F2

Cash ROE

Cash NPAT / Average Shareholder Equity

Cash NPAT and Cash ROE

When assessing high growth lenders such as Harmoney, Cash NPAT can be a superior measure to statutory NPAT as it adjusts out the AASB 9 requirement to expense estimated future period credit losses. Under AASB 9 a growing loan book drives an increased provision expense, ahead of actual credit losses or increased income from that loan book growth. Cash NPAT can be used to derive profit-based comparisons such as Cash Return on Equity and Cash P/E.

We calculate Cash NPAT as Reported NPAT, adding back:

- Movement in ECL Provision
- Share based Payment expense.
- Depreciation and Amortisation

Harmoney's Cash NPAT of $4.7m in FY23, delivered an 8.4% Cash ROE which is remarkably higher than FY22's 0.3%. Management has provided guidance of an expected 20% Cash ROE run rate by FY25, supported by the launch of Stellare 2.0 to both:

- Grow revenues through continued execution on Australian expansion plans and new credit product development to increase available users and customer lifetime value.
- Continue to improve cost-to-income ratio through the operating leverage afforded at scale.

Earnings changes

Following Harmoney's FY23 results, we make the following changes to our earnings estimates.

Figure 4: MST Access General Residual Income Model ("GRIM") valuation of Harmoney Corp Limited

		FY23E			FY24E			FY25E			FY26E		
		Expected	Actuals	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg
Interest income	A$m	106.9	105.5	-1%	135.0	133.8	-1%	164.4	170.3	4%	200.2	207.5	4%
Total income	**A$m**	**107.5**	**107.1**	**0%**	**135.0**	**133.8**	**-1%**	**164.4**	**170.3**	**4%**	**200.2**	**207.5**	**4%**
Interest expense	A$m	-39.8	-39.8	0%	-54.8	-56.1	-2%	-63.3	-70.8	-12%	-77.6	-86.7	-12%
Net lending income	A$m	36.7	34.9	-5%	38.6	33.3	-14%	51.8	43.3	-17%	60.2	54.6	-9%
Net operating margin	**A$m**	**19.1**	**22.6**	**18%**	**20.0**	**21.6**	**8%**	**32.7**	**31.2**	**-5%**	**39.6**	**42.2**	**6%**
Profit before income tax	A$m	-4.5	-7.6	-69%	-5.7	-8.1	-44%	5.6	-1.8	-132%	10.8	6.4	-41%
Reported NPAT	A$m	-4.5	-7.6	-69%	-4.0	-8.2	-104%	4.0	-2.3	-158%	7.7	4.5	-41%
Cash NPAT	**A$m**	**4.7**	**4.7**	**1%**	**5.6**	**4.5**	**-20%**	**14.0**	**10.2**	**-27%**	**27.4**	**15.1**	**-45%**
EPS diluted reported	cps	-4.4	-6.7	-51%	-4.0	-8.1	-104%	3.9	-2.2	-158%	7.6	4.4	-41%
EPS proforma diluted cash	**cps**	**4.6**	**4.7**	**1%**	**5.5**	**4.4**	**-20%**	**13.8**	**10.1**	**-27%**	**26.9**	**14.8**	**-45%**
DPS	cps	0.0	0.0	n.a.	0.0	0.0	n.a.	0.0	0.0	n.a.	0.0	0.0	n.a.

Source: Company reports, MST Access estimates

These changes are primarily due to:

- the incorporation of FY23 results into our model;
- revisions to our loan book growth assumptions and operating expenses given management execution and scale ambitions provided in results commentary, and;
- revisions to our funding costs assumptions given market stabilisation in the expected cost of funds and management guidance.

Changes may appear large due to a small denominator, with Harmony transitioning from being loss making to being profitable on in the near future.

Full details of our earnings estimates appear in the financial summary on page 2.

Valuation

We use a blend of valuation approaches to estimate Harmoney valuation, considering:

- peer multiples and growth rates,
- intrinsic valuation scenarios of its potential future growth profiles

Other equity market considerations such as short sales; any likely forthcoming changes in index inclusion; depth of stock research coverage; composition of and change in the mix of investors (such as founders, board and staff, domestic institutions, foreign institutions, and retail investors) are not incorporated in our valuation; however investors should consider such factors if they seek to develop a price target for the company.

Many analysts use some form of residual income or value-added valuation approach, due to the complexities and uncertainties involved in forecasting cashflow, in part due to regulatory capital requirements. Some of the advantages of this approach are that:

- the bulk of the valuation is generally recognized upfront, in the net asset value providing greater certainty around a large component of the valuation;
- uses profit, rather than cashflow, forecasts.

The derivation of our book value per share and cash EPS used in this valuation method can be found in our balance sheet and income statement respectively.

General Residual Income Model ("GRIM")

We use a two-stage model, using our explicit forecasts over the next five years, followed by a terminal value, to which we add current net assets per share. We continue to assume a risk free rate of 4.0%, an equity risk premium of 5.0% and estimate HMY's equity beta to be 1.5. Based on these, our estimate of HMY's cost of equity to 11.5% and our terminal growth rate assumption is 3.0%.

This produces a general residual income model valuation of A$2.50 per share, down from our previously valuation A$3.17 due to discount roll forward and earnings changes. We note the current valuation still represents a significant upside to the current share price, at 474%.

Figure 5: MST Access General Residual Income Model ("GRIM") valuation of Harmoney Corp Limited

Current date		29-Aug-23										
Last balance date		30-Jun-23										
		Jun-23	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26	Dec-26	Jun-27	Dec-27	Jun-28
Book value per share	A$	0.53	0.48	0.45	0.43	0.43	0.44	0.44	0.47	0.52	0.59	0.73
Equity charge	A$		-0.03	-0.03	-0.03	-0.02	-0.02	-0.03	-0.03	-0.03	-0.03	-0.03
Cash EPS	A$	0.02	0.01	0.03	0.05	0.05	0.07	0.07	0.08	0.10	0.12	0.16
Residual income	A$		**-0.02**	**0.01**	**0.02**	**0.03**	**0.04**	**0.04**	**0.06**	**0.08**	**0.09**	**0.12**
Discounted cash flow	A$	**0.00**	**-0.02**	**0.01**	**0.02**	**0.02**	**0.03**	**0.03**	**0.04**	**0.05**	**0.06**	**0.07**

Sum of discount streams	A$	0.31	**CAPM**	
Future value into perpetuity	A$	2.5	Risk free rate	4.00%
NPV of terminal value	A$	1.66	Equity beta	1.5
add net assets	A$	0.53	Equity risk premium	5.00%
Residual income value per share	**A$**	**2.50**	Cost of equity	11.5%
P/B multiple implied by GRIM valuation	x	4.7	Terminal growth	3.0%
Upside/downside	%	474%		

Source: Company reports, MST Access estimates

Theoretical book multiple valuation

With Harmoney's medium term ROE target of 20%, we can use this to ascertain what theoretical book multiple the company would trade at if it achieves this target (which we think is probable).

One key shortcoming with this method is that it requires an assumed dividend payout ratio, as the theoretical multiple calculation can become undefined if no dividend payout ratio is assumed. For the purposes of this valuation, we assume a 50% dividend payout ratio, despite Harmoney currently seeking to retain all its earnings to support future growth.

This method suggests that with a 11.5% cost of equity, 20% ROE and 50% retained earnings, the appropriate theoretical book multiple that Harmoney should trade on is 6.67x, which applied to its current book value of 53cps would suggest a valuation of $3.53.

Figure 6: Theoretical book multiple valuation for Harmoney

HMY theoretical book multiple valuation		
Target cash ROE	%	20.0%
Cost of equity	%	11.5%
Dividend pay out ratio	%	50%
Theoretical book multiple	**x**	**6.67**
Current book value per share	A$	0.53
Implied valuation	**A$**	**3.53**
Implied upside	%	828.6%

Source: Company reports, MST Access estimates

Updated Investment Thesis

Harmoney is a leading 100% online direct personal lender that operates across Australia and New Zealand, which continues to display strong growth and earnings momentum. The company is profitable on a cash basis and generates operating cashflows, and these should grow as its business grows.

A combination of superior technology, direct business model, and effective marketing strategies gives Harmoney a clear edge over its peers, as well enabling it to achieve strong credit quality for its loan book. Harmoney's highly automated Stellare™ technology ensures the businesses expenses are largely fixed, thus delivering strong operational leverage. Stellare's™ risk selection was strong from the outset and has continued to improve over time. Harmoney is well-positioned in the cross-section of distribution and scalability, with a direct model and high scalability. Banks pulling back from the personal lending industry provides smaller alternative lenders (like Harmoney) an opportunity to capture large market share.

Harmoney uses multiple funding sources and has now largely transitioned to warehouse and ABS funding. The company's already attractive NIMs will be further enhanced by this transition, with the company reporting a NIM near 10% for FY23.

Risks and sensitivities

We elaborate on Harmoney's risks and sensitivities in our initiation report. In summary, they can be categorised under strategic, financial and operational risks summarised as:

Strategic

Harmoney operates in a dynamic and changing market, which sees competitors providing new and innovative offerings in a bid to capture market share.

Furthermore, there is a significant number of regulatory requirements, and could suffer from adverse changes to the requirements, including in Australia:

- Anti-money laundering and counter terrorist financing requirements administered by Austrac;
- Privacy requirements administered by the Privacy Commissioner;
- Financial Service licencing and Credit licencing administered by the Australian Securities and Investments Commission (ASIC);
- Australian Consumer Law and unfair contract terms contained in the Corporations Act administered by the Australian Competition and Consumer Commission (ACCC);
- Taxation legislation administered by the Australian Taxation Office (ATO);
- Accounting standards required under the Corporations Act administered by the Australian Accounting Standards Board (AASB) and ASIC;
- Design and distribution obligations, several of which will be governed by contract law.

Financial

Being a finance company, Harmoney has a range of risks and sensitivities applicable to most companies in the financial sector. These include:

- Macroeconomic conditions
- Liquidity and funding risks
- Credit risk
- Fraud
- Compliance risks

Operational

Most companies, including Harmoney, have a range of operational risks. These include:

- Governance
- Key personnel
- Information technology

- Cybersecurity and data protection
- Force majeure events
- Litigation, claims and disputes

Company Description

Harmoney is the largest 100% consumer-direct money platform in Australia and New Zealand. The Company provides customers with unsecured personal loans, and secured and unsecured auto loans, that are easy to access, competitively priced (using risk-adjusted interest rates) and accessed 100% online. By effectively combining superior data, superior technology, and superior marketing, Harmoney creates direct relationships with consumers, at scale.

It's direct-to-consumer automated loan approval system is underpinned by Harmoney's scalable Stellare™ proprietary technology platform. Stellare™ efficiently facilitates its personalised loan product with applications processed and loans typically funded within 24 hours of acceptance by the customer. The 100% consumer-direct aspect of Harmoney's business model allows the Company to gain access to deep data from consumers. The Stellare™ technology utilises deep consumer data and applies customer's individual circumstances to its machine learning credit scorecard to deliver automated credit decisioning and accurate risk-based pricing. Harmoney have continually improved their credit scoring technology, with the latest Stellare™ Libra algorithms delivering high performance.

A large percentage of Harmoney's originations come from existing or past customers. The minimal cost of marketing to its existing customer base proved a stable source of quality originations through COVID for the business and remain intrinsic to the business going forward.

Harmoney is funded by a number of sources including three of the big 4 Australian banks as well as issuing ABS.

Harmoney hold an Australian Credit Licence (ACL) which allows the company to conduct business as a consumer lender in Australia. Despite the Company ceasing retail peer-to-peer loans in New Zealand, they maintain their FMCA licence in relation to the run-off portfolio. Harmoney also hold an Australian Financial Services Licence (AFSL), which is regulated by ASIC.

Methodology & Disclosures

MST Access is a registered business name of MST Financial Services Pty Ltd (ACN 617 475 180 "MST Financial") which is a limited liability company incorporated in Australia on 10 April 2017 and holds an Australian Financial Services Licence (Number: 500 557). This research is issued in Australia through MST Access which is the research division of MST Financial. The research and any access to it, is intended only for "wholesale clients" within the meaning of the Corporations Act 2001 of Australia. Any advice given by MST Access is general advice only and does not take into account your personal circumstances, needs or objectives. You should, before acting on this advice, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If our advice relates to the acquisition, or possible acquisition, of a financial product you should read any relevant Product Disclosure Statement or like instrument.

This report has been commissioned by Harmoney Corp. Limited and prepared and issued by Glen Wellham of MST Access in consideration of a fee payable by Harmoney Corp. Limited. MST Access receives fees from the company referred to in this document, for research services and other financial services or advice we may provide to that company.

MST Financial also provides equity capital markets ("ECM") and corporate advisory services through its capital markets division, MST Capital Markets ("MST Capital"). MST Capital provides these services to a range of companies including clients of the MST Access service. As such, MST Capital may in future provide ECM and/or corporate advisory services to the company that is the subject of this research report and, accordingly, may receive fees from the company for providing such services. However, MST Financial has measures in place to ensure the independence of its research division is maintained, including information barriers between its Capital Markets and Research teams. In addition, neither MST Access, not any of its research analysts, receive any financial benefit that is based on the revenues generated by MST Capital Markets or any other division of MST Financial.

The analyst has received assistance from the company in preparing this document. The company has provided the analyst with communication with senior management and information on the company and industry. As part of due diligence, the analyst has independently and critically reviewed the assistance and information provided by the company to form the opinions expressed in the report. Diligent care has been taken by the analyst to maintain an honest and fair objectivity in writing this report and making the recommendation. Where MST Access has been commissioned to prepare content and receives fees for its preparation, please note that NO part of the fee, compensation or employee remuneration paid will either directly or indirectly impact the content provided.

Accuracy of content: All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report and have not sought for this information to be independently certified. Opinions contained in this report represent those of MST Access at the time of publication. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results and estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations.

Exclusion of liability: To the fullest extent allowed by law, MST Access shall not be liable for any direct, indirect or consequential losses, loss of profits, damages, costs or expenses incurred or suffered by you arising out or in connection with the access to, use of or reliance on any information contained in this report. No guarantees or warranties regarding accuracy, completeness or fitness for purpose are provided by MST Access, and under no circumstances will any of MST Financials' officers, representatives, associates or agents be liable for any loss or damage, whether direct, incidental or consequential, caused by reliance on or use of the content.

General Advice Warning

MST Access Research may not be construed as personal advice or recommendation. MST encourages investors to seek independent financial advice regarding the suitability of investments for their individual circumstances and recommends that investments be independently evaluated. Investments involve risks and the value of any investment or income may go down as well as up. Investors may not get back the full amount invested. Past performance is not indicative of future performance. Estimates of future performance are based on assumptions that may not be realised. If provided, and unless otherwise stated, the closing price provided is that of the primary exchange for the issuer's securities or investments. The information contained within MST Access Research is published solely for information purposes and is not a solicitation or offer to buy or sell any financial instrument or participate in any trading or investment strategy. Analysis contained within MST Access Research publications is based upon publicly available information and may include numerous assumptions. Investors should be aware that different assumptions can and do result in materially different results.

MST Access Research is distributed only as may be permitted by law. It is not intended for distribution or use by any person or entity located in a jurisdiction where distribution, publication, availability or use would be prohibited. MST makes no claim that MST Access Research content may be lawfully viewed or accessed outside of Australia. Access to MST Access Research content may not be legal for certain persons and in certain jurisdictions. If you access this service or content from outside of Australia, you are responsible for compliance with the laws of your jurisdiction and/or the jurisdiction of the third party receiving such content. MST Access Research is provided to our clients through our proprietary research portal and distributed electronically by MST to its MST Access clients. Some MST Access Research products may also be made available to its clients via third party vendors or distributed through alternative electronic means as a convenience. Such alternative distribution methods are at MST's discretion.

Access & Use

Any access to or use of MST Access Research is subject to the Terms and Conditions of MST Access Research. By accessing or using MST Access Research you hereby agree to be bound by our Terms and Conditions and hereby consent to MST collecting and using your personal data (including cookies) in accordance with our Privacy Policy, including for the purpose of a) setting your preferences and b) collecting readership data so we may deliver an improved and personalised service to you. If you do not agree to our Terms and Conditions and/or if you do not wish to consent to MST's use of your personal data, please do not access this service.