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HOW WALL STREET FINANCES HIGH-COST CONSUMER LENDERS

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In January 2014, Reinvestment Partners published a report which detailed how Wall Street financiers have supported high-cost consumer finance companies. The report focused on the loans made by major banks to payday lenders, consumer finance companies, buy-here pay-here auto lenders, rent-to-own chains. The emphasis was on activity during recent years. The report illuminated how the involvement of banks was instrumental to the expansion of high-cost consumer finance. It acknowledged that some banks had suspended their involvement, but by chronicling the past, it served to remind the public of the history between banks and this industry.

This shorter report updates the changes that have occurred over the last eighteen months. Banks ask their commercial borrowers to refinance frequently. This reflects the rapid change in the credit-worthiness of the consumer lenders they serve. With each amendment to credit agreements, banks also generate another round of investment banking fees. In this period, almost all of the lenders have had to amend their loans.

Some have also chosen to issue notes. Notes are a type of bond with whose period of repayment lasts for between one and ten years. Unlike a term loan or a line of credit, they can be traded. It is rarely the case that the bondholders are only banks. They are purchased by many kinds of institutions. Buyers can include insurance companies, state pension funds, private investors, mutual funds and others.

But there is some good news. In several cases, some lenders have withdrawn from their relationships. Some banks have drawn the line with payday lenders – saying that they will no longer do business with this industry. But none have agreed to withdraw entirely. Instead, they walk a careful path, financing some high cost lenders while simultaneously proclaiming their hesitancy to work with near neighbors.

Renewed Agreements

World Acceptance

World Acceptance secured a new credit agreement on November 18th, 2014[1]. The lenders were Wells Fargo, Bank of America, Bank of Montreal, Capital One, TD Bank, First Tennessee Bank and Texas Capital Bank. Of note, BB&T did not participate. It had been a lender until then. TD Bank indicated that it would withdraw from the loan on June 15th, 2015. A covenant in the loan ties the loan performance among World's portfolio to the advance rate. If more than eighteen percent of World's loans are more than 60 days late, for example, then the maximum advance rate is 84 percent. Moreover, it required World to alert Wells Fargo (as the AA) of any new enforcement action. World has the ability to borrow up to $680 million under this contract.

In May 2015, World Acceptance announced that its revolving credit line would be reduced from $680 million to $430 million. In tandem with change, World said it would sell $250 million in 5-year notes to make up for the shortfall. But unexpectedly, World announced that it was canceling the sale of notes. TD North has not indicated any change in its plans to withdraw, so a question about World's future capital structure remains unanswered.

The answer came two months later (June 24th, 2015), when World Acceptance announced another amendment (the Ninth Amendment to the Amended and Restated Revolving Credit Agreement) which called for a stair-stepped reduction in their line amount over the next two years. It immediately reduced the line to $600 million and called for subsequent reductions to $500 million in March 2016 and $400 million in March 2017[2].

Wall Street is putting World on a credit diet. To make it worse for the company, the lenders even went so far as to increase the interest rate charged by 100 basis points and stiffened some of the loan covenants. TDNorth followed through on its plan to exit the relationship.

At the end of March 2015, World had $501.2 million in long-term debt.

First Cash Financial

On Feb. 5th, 2014, First Cash entered into a new credit agreement[3]. Wells Fargo was designated as the Administrative Agent and participated as a lender. The Agreement provided First Cash with a revolving credit facility of up to $160 million. The terms included an agreed-upon option for an increase of $50 million. The agreement matures in February 2019. The revolving line bears interest at shorter-term LIBOR rates (1 month) plus 2.5 percent. Currently, 1-month LIBOR rates are trading at approximately 19/100ths of a percent.

[1] http://www.sec.gov/Archives/edgar/data/108385/000010838514000053/exhibit101-112014.htm
[2] http://www.sec.gov/Archives/edgar/data/108385/000010838515000047/exhibit101_62215.htm
[3] http://www.sec.gov/Archives/edgar/data/840489/000084048914000006/fcfs020520148-k.htm

Upon origination, First Cash pulled down $145.87 million to repay a portion of debt outstanding under the existing credit agreement. The other outstanding debt was repaid with cash. There is a covenant which states that FCFS' total borrowing cannot exceed 2.5 times EBITDA.

In the previous agreement, JP Morgan Cash served as the administrative agent and participated as a lender.

In September 2014, First Cash sold $200 million in notes bearing a face value interest rate of 6.75 percent[4]. Moody's considered them at the lowest end of investment grade.

In their most recent fiscal year, the company derived 95 percent of its revenue from pawn lending and the rest from payday loans. It estimates that the annualized yield on its pawn loans is 168 percent[5]. Whereas it once operated national payday lender Cash & Go, during the last several years it has been shuttering its payday operations. It still operates as a Credit Services Organization ("CSO") in Texas. Consumers who access those loans pay 10 percent interest plus a fee of $22 per every $100 advanced. Terms vary from 7 to 180 days. FCFS offers auto title loans in Texas.

EZCorp

In June 2014, EZCorp repaid its credit agreement by issuing $200 million in convertible senior notes[6]. Lenders participating in the loan had been Wells Fargo, Amegy, BOKF (D.B.A. Bank of Texas), U.S. Bank, and Compass (now BBVA)[7]. With the proceeds of the bond issue, EZCorp paid down the entire $119 million outstanding on their $175 million credit line[8]. That loan was due to mature in May 2015.

Additionally, its foreign subsidiary Grupo Finmart owes approximately $92 million in a mix of loans and notes[9].

On July 2nd, 2014, EZCorp announced that it had issued an additional $30 million in notes. Together, this means that the company has $230 million outstanding in 2.125 percent convertible senior notes with the same expiration[10]. The notes mature in 2019. AT the moment, they are trading at a severe discount ($76.78). The yield on those 2.125 coupons is now 9.44 percent.

On July 28th, 2015, EZCorp announced that it would shutter its Financial Services division. This change means that EZCorp will no longer offer payday loans, auto title loans, or consumer installment loans. The company acknowledged that regulatory changes, coupled with their lack of size relative to competitors, made it an unattractive business venture. EZCorp will remain active in pawn lending.

As a result of that decision, lenders to EZCorp will no longer be considered as participants in the commercial capitalization of payday lenders.

[4] http://www.sec.gov/Archives/edgar/data/840489/000084048914000067/fcfs090820148-k.htm
[5] http://ww2.firstcash.com/sites/default/files/20140905_IP.pdf
[6] http://www.sec.gov/Archives/edgar/data/876523/000110465914047802/a14-15880_1ex4d1.htm
[7] http://www.sec.gov/Archives/edgar/data/876523/000095012311049188/d82245exv10w1.htm
[8] http://www.sec.gov/Archives/edgar/data/876523/000110465914047834/a14-15880_28ka.htm
[9] http://www.sec.gov/Archives/edgar/data/876523/000087652315000018/a2015-q110q_12312014.htm#s94DA28A846CD5533A021CE9EAF53D8B1
[10] http://www.sec.gov/Archives/edgar/data/876523/000087652314000070/a8-knotesoverallotment6x14.htm

Enova

Most of Enova's debt is sourced from the sale of notes. On May 30th, 2014, Enova sold $500 million in 9.75 percent senior notes which are due in June 2021[11]. The notes were sold to institutional debt buyers. At the end of March 31st, 2015, the company owed $494.3 million on those notes. The sale of that debt allowed the company to repay a $450 million credit that that it had previously received from Cash America.

On March 25th, 2015, Enova amended its revolving credit facility. In the new agreement, Enova's credit line with Jeffries[12] contracted from $75 million to $65 million[13]. At the same time, lenders increased a different line ("the senior secured indebtedness basket") to a maximum of $20 million or to 2.75 percent of total assets. Enova was spun off from Cash America on November 13th, 2014. At the end of March 2015, the Company said that it was not using the line.

Cash America

Cash America amended its credit agreement (the Sixth Amendment) on December 23rd, 2014[14]. Lenders consisted of Wells Fargo Bank, KeyBank, U.S. Bank, Amegy Bank, First Tennessee Bank, and BOKF (dba Bank of Texas). In the new terms, several loan covenants were altered. When originated, it gave the company the ability to draw up to $280 million. After the spin-off of Enova, the company repaid all of the outstanding debt due on its line of credit.

In 2013, Cash America issued $300 million in senior notes bearing a rate of 5.75 percent. As of June 30th, 2015, the outstanding principal balance was $184.5 million. Those bonds bore an interest rate of 5.75 percent, but because the company is considered attractive to bondholders, they are selling at a premium above par.

In connection to its spin-off of Enova, Cash America reduced its long-term debt from $717.4 million to $196.5 million during the course of 2014.

The company estimates that its pawn loans yield 131 percent interest.

QC Financial

On July 23rd, 2014, QC Financial amended the terms associated with its revolving line of credit[15]. The changes focused on the covenants associated with their loan and reduced the total amount of the credit line. The new agreement gives QC the ability to draw from a $20 million revolving line and another $5 million from a line of credit. Previously, QC had access to $27 million on its revolver and another $32 million in a term loan[16]. QC paid down the term loan over three years, ending in June 2014. On the date of the July 2014 transaction, QC said that it was utilizing $8.5 million of the line.

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[11] http://www.sec.gov/Archives/edgar/data/1529864/000156459015003649/enva-10q_20150331.htm#NOTES_TO_CONSOLIDATED_FINANCIAL_STATEMENt
[12] http://www.sec.gov/Archives/edgar/data/1529864/000119312515105239/d894326dex109.htm
[13] http://www.sec.gov/Archives/edgar/data/1529864/000156459015002145/enva-8k_20150325.htm
[14] http://www.sec.gov/Archives/edgar/data/807884/000115752314004890/a51011072ex10_1.htm
[15] http://www.sec.gov/Archives/edgar/data/1289505/000119312514284427/d765337dex101.htm
[16] http://www.sec.gov/Archives/edgar/data/1289505/000119312511265485/d240569dex101.htm

US Bank led various aspects of the contract. Lenders were U.S. Bank, BOKF (dba Bank of Kansas City), Enterprise Bank & Trust, Pulaski Bank, and United Community Bank. However, long-time partner First Tennessee Bank did not participate in the July 2014 loan.

Community Choice Financial

Over the last five years, Community Choice Financial has gradually increased the degree to which it finances its capital structure from debt.

At the same time, they entered into a four-year $40 million agreement for a revolving line of credit. It bears an interest rate of LIBOR plus 5 percent. At the end of 2014, it was not currently being utilized[17]. But in March 2015, the company refinanced its line of credit. On March 31st, 2015, CCFI reported that it had drawn $26.7 million on that new line.

The company had approximately $188 million in long-term debt at the end of 2010. As of March 31st, it had $420 million outstanding on its senior notes. The interest rate on those notes is 10.75 percent.

Back in July 2012, the company issued another $25 million in senior secured notes at "substantially similar" terms to the first notes. Several of its subsidiaries have also borrowed and have outstanding debt. One subsidiary has a $7 million revolving line of credit. Another subsidiary has a $35 million installment loan. A third has a note outstanding for $1.4 million.

On July 19th, 2015, Moody's Investor Service took the unusual step of downgrading Community Choice's debt to Caa1[18]. As a result, bonds with a face value of $100 are selling for only $40.27. In effect, investors see Community Choice's future ability to pay its debt that they are requiring a yield of 45 percent[19]. Moody's puts the cause on this state of affairs on CCFI's decision to expand its internet business. According to Moody's, this new line of business did not adequately underwrite, and as a result, the quality of receivables on its balance sheet deteriorated. In turn, when CCFI refinanced in credit facility in 2015, it agreed to "disadvantageous terms."

High-Cost Consumer Finance Companies that are No Longer Publicly Traded

DFC Global: In 2014, DFC Global ceased to be a publicly-traded company. As a result, it no longer has to issue reports on its capital structure. DFC Global continues to offer short-term internet consumer loans in the United States. In 2013, the CFPB states that its Military Installment Loan and Education Services ("MILES") program violated the Consumer Financial Protection Act. In 2013, DFC issued $230 million in senior unsecured notes bearing an interest rate of 3.25 percent[20]. At the moment, they have paid down most of the outstanding principal.

Advance America: Advance America is one of the largest payday lenders in the United States. In 2012, they were purchased by a group of private investors. At the time, they were financed by a consortium of nine banks. They enjoyed a $200 million line of credit and a $100 million term loan.

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[17] http://www.sec.gov/Archives/edgar/data/1528061/000110465915023986/a14-26759_110k.htm#Item6_SelectedFinancialData_082958

[18] https://www.moodys.com/research/Moodys-downgrades-Community-Choice-to-Caa1--PR_330445

[19] http://finra-markets.morningstar.com/BondCenter/Results.jsp

[20] http://finra-markets.morningstar.com/BondCenter/BondDetail.jsp?ticker=C599477&symbol=DLLR4048141

Closing

There is plenty of room to be optimistic about the future. Some institutions are moving away from any engagement with payday lenders. Simultaneously, bondholders of notes see their notes as riskier. Many lenders must now pay more to borrow than they had in the past.

Some notable events:

- JPMorgan Chase Bank is no longer a lender to First Cash Financial.
- BB&T parted ways with World Acceptance.
- TDNorth has announced a plan to extricate itself from its share of the loan with World Acceptance by the end of June 2015. Had it not been for a disruption in World's financing plans, this would have been realized. For the time being, TDNorth's intentions appear to remain unchanged. They will exit as soon as World can complete a planned sale of notes.
- First Tennessee Bank did not participate in the amended credit agreement with QC Financial.

Bank of America, JPMorgan Chase, Fifth Third, and Capital One say have indicated that they will no longer finance payday lenders. While such comments have not been issued publicly, the record shows that they are implementing this plan. Nonetheless, Bank of America, Chase, and Capital One are still financiers to World Acceptance. World is not a payday lender, but they are a high-cost consumer finance lender whose loans often exceed 100 percent.

To some extent, the new anxiety among banks is mirrored by bond investors. In most cases, the price of bonds in these firms is now well below the amount at their issuance. Community Choice is the extreme example, where its debt now sells for only 2/5th of its face value. But the same is true of several other lenders. This tells us that Wall Street is gradually becoming more skeptical about this industry.

CAPITAL STRUCTURE OF PAYDAY AND/OR HIGH-COST CONSUMER FINANCE LENDERS

Lender	Receivables (Net of Reserves)	Loans and Lines of Credit	Notes	Yield % on notes	Equity
First Cash	$136.7	$160.0 ($22.4 utilized)	$200	5.30	$448.6
World Acceptance	$742.3	$600.0	$0		$315.6
Cash America	$297.0	$0	$196.5	5.33	$1,133.2
QC Financial	$61.3	$25.0 ($15.4 utilized)	$0		$70.36
Enova	$279.1	$0	$495	13.55	$177.8
Community Choice Financial	$159.7	$40.0 ($26.7 utilized)	$420	45.31	$45.4
DFC Global			$230	5.24	

All dollars in millions

This data is sourced from the most recent annual report from each company. However, given its recent decision to take out a revolving line of credit, the data from Community Choice Financial is from reports issued at the end of March 2015.

CURRENT LOANS OUTSTANDING, BY BANK

Financial Institution	Amount	Relationships
Wells Fargo	$ 240,000,000	2
Bank of America*	$ 155,000,000	1
Bank of Montreal*	$ 130,000,000	1
Jefferies	$ 65,000,000	1
Texas Capital	$ 70,000,000	2
BOKF	$ 45,625,000	2
Capital One*	$ 45,000,000	1
First Tennessee*	$ 40,000,000	1
Amegy	$ 40,000,000	1
US Bank	$ 9,375,000	1
Enterprise Bank & Trust	$ 5,625,000	1
Pulaski Bank	$ 2,500,000	1
United Community Bank	$ 1,875,000	1
Total	*$ 850,000,000*	

*only lending to consumer finance companies – no relationship with payday lenders