

NICHOLAS FINANCIAL INC  
Form 10-Q  
February 09, 2017  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, DC 20549**

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**FOR THE QUARTERLY PERIOD ENDED December 31, 2016**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.**

**Commission file number: 0-26680**

**NICHOLAS FINANCIAL, INC.**

**(Exact Name of Registrant as Specified in its Charter)**

**British Columbia, Canada**  
**(State or Other Jurisdiction of**

**8736-3354**  
**(I.R.S. Employer**

**Incorporation or Organization)**

**Identification No.)**

**2454 McMullen Booth Road, Building C**

**Clearwater, Florida**  
**(Address of Principal Executive Offices)**

**33759**  
**(Zip Code)**

**(727) 726-0763**

**(Registrant's telephone number, including area code)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 and 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter periods that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) Yes No

As of February 1, 2017, 12,495,089 shares, no par value, of the Registrant were outstanding (of which 4,713,804 shares were held by the Registrant's principal operating subsidiary and pursuant to applicable law, not entitled to vote and 7,781,285 shares were entitled to vote).

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Nicholas Financial, Inc. and Subsidiaries

Consolidated Balance Sheets

(In thousands)

	<b>December 31, 2016 (Unaudited)</b>	<b>March 31, 2016</b>
<b>Assets</b>		
Cash	\$ 3,664	\$ 1,849
Finance receivables, net	321,757	311,837
Assets held for resale	2,976	2,148
Income taxes receivable		593
Prepaid expenses and other assets	632	977
Property and equipment, net	1,580	1,290
Deferred income taxes	7,232	6,615
<b>Total assets</b>	<b>\$ 337,841</b>	<b>\$ 325,309</b>
<b>Liabilities and shareholders equity</b>		
Line of credit	\$ 214,340	\$ 211,000
Drafts payable	1,687	1,499
Interest rate swap agreements	21	205
Accounts payable and accrued expenses	7,391	5,839
Income taxes payable	605	
Deferred revenues	4,003	3,917
<b>Total liabilities</b>	<b>228,047</b>	<b>222,460</b>
<b>Shareholders equity</b>		
Preferred stock, no par: 5,000 shares authorized; none issued		
Common stock, no par: 50,000 shares authorized; 12,492 and 12,466 shares issued, respectively; and 7,778 and 7,752 shares outstanding, respectively	33,753	33,287
Treasury stock: 4,714 common shares, at cost	(70,459)	(70,459)
Retained earnings	146,500	140,021
<b>Total shareholders equity</b>	<b>109,794</b>	<b>102,849</b>
<b>Total liabilities and shareholders equity</b>	<b>\$ 337,841</b>	<b>\$ 325,309</b>

*See accompanying notes.*

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## Nicholas Financial, Inc. and Subsidiaries

## Consolidated Statements of Income

(Unaudited)

(In thousands, except per share amounts)

	Three months ended December 31,		Nine months ended December 31,	
	2016	2015	2016	2015
Interest and fee income on finance receivables	\$ 22,044	\$ 22,757	\$ 67,606	\$ 67,469
Expenses:				
Marketing	369	384	1,100	1,140
Salaries and employee benefits	5,041	5,539	16,363	16,623
Professional Fees	386	306	1,004	1,131
Administrative	2,546	2,324	7,748	7,176
Provision for credit losses	8,796	7,599	23,966	18,766
Depreciation	142	120	413	334
Interest expense	2,258	2,311	6,745	6,750
Change in fair value of interest rate swap agreements	(81)	(251)	(184)	(128)
	19,457	18,332	57,155	51,792
Operating income before income taxes	2,587	4,425	10,451	15,677
Income tax expense	981	1,698	3,972	6,024
Net income	\$ 1,606	\$ 2,727	\$ 6,479	\$ 9,653
Earnings per share:				
Basic	\$ 0.21	\$ 0.36	\$ 0.83	\$ 1.27
Diluted	\$ 0.21	\$ 0.35	\$ 0.83	\$ 1.24

*See accompanying notes.*

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## Nicholas Financial, Inc. and Subsidiaries

## Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Nine months ended	
	December 31,	
	2016	2015
<b>Cash flows from operating activities</b>		
Net income	\$ 6,479	\$ 9,653
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	413	334
Gain on sale of property and equipment	(13)	(12)
Provision for credit losses	23,966	18,766
Amortization of dealer discounts	(9,830)	(9,886)
Deferred income taxes	(626)	(296)
Share-based compensation	474	416
Change in fair value of interest rate swap agreements	(184)	(128)
Changes in operating assets and liabilities:		
Prepaid expenses and other assets	345	396
Accounts payable and accrued expenses	1,552	(2,202)
Income taxes payable and receivable	1,198	(306)
Deferred revenues	86	657
Net cash provided by operating activities	23,860	17,392
<b>Cash flows from investing activities</b>		
Purchase and origination of finance receivables	(118,276)	(131,416)
Principal payments received	94,220	101,126
Increase in assets held for resale	(828)	(185)
Purchase of property and equipment	(728)	(878)
Proceeds from sale of property and equipment	38	48
Net cash used in investing activities	(25,574)	(31,305)
<b>Cash flows from financing activities</b>		
Increase on line of credit	3,340	14,000
Change in drafts payable	188	(476)
Payment of debt costs		(25)
Expenses related to prior purchase of treasury shares		(50)
Proceeds from exercise of stock options	1	76
Excess tax benefits from share-based compensation		6

Net cash provided by financing activities	<b>3,529</b>	13,531
Net increase (decrease) in cash	<b>1,815</b>	(382)
Cash, beginning of period	<b>1,849</b>	3,388
Cash, end of period	<b>\$ 3,664</b>	\$ 3,006
<b>Supplemental Disclosure of noncash investing and financing activities:</b>		
Tax deficiency from share awards	<b>\$ (9)</b>	\$

*See accompanying notes.*

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Nicholas Financial, Inc. and Subsidiaries

Notes to the Consolidated Financial Statements

(Unaudited)

**1. Basis of Presentation**

The accompanying consolidated balance sheet as of March 31, 2016, which has been derived from audited financial statements, and the accompanying unaudited interim consolidated financial statements of Nicholas Financial, Inc. (including its subsidiaries, the Company) have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q pursuant to the Securities and Exchange Act of 1934, as amended in Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete consolidated financial statements, although the Company believes that the disclosures made are adequate to ensure the information is not misleading. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for interim periods are not necessarily indicative of the results that may be expected for the year ending March 31, 2017. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and accompanying notes thereto included in the Company's Annual Report on Form 10-K for the year ended March 31, 2016 as filed with the Securities and Exchange Commission on June 14, 2016. The March 31, 2016 consolidated balance sheet included herein has been derived from the March 31, 2016 audited consolidated balance sheet included in the aforementioned Form 10-K.

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for credit losses on finance receivables and the fair value of interest rate swap agreements.

**2. Revenue Recognition**

Finance receivables consist of automobile finance installment contracts (Contracts) and direct consumer loans (Direct Loans). Interest income on finance receivables is recognized using the interest method. Accrual of interest income on finance receivables is suspended when a loan enters bankruptcy status, is contractually delinquent for 61 days or more or the collateral is repossessed, whichever is earlier. Chapter 13 bankruptcy accounts are accounted for under the cost-recovery method. Interest income on Chapter 13 bankruptcy accounts does not resume until all principal amounts are recovered (see Note 4).

A dealer discount represents the difference between the finance receivable, net of unearned interest, of a Contract, and the amount of money the Company actually pays for the Contract. The discount negotiated by the Company is a function of the lender, the wholesale value of the vehicle and competition in any given market. In making decisions regarding the purchase of a particular Contract the Company considers the following factors related to the borrower: place and length of residence; current and prior job status; history in making installment payments for automobiles; current income; and credit history. In addition, the Company examines its prior experience with Contracts purchased from the dealer from which the Company is purchasing the Contract, and the value of the automobile in relation to the purchase price and the term of the Contract. The entire amount of discount is amortized as an adjustment to yield

using the interest method over the life of the loan. The average dealer discount associated with new volume for the three months ended December 31, 2016 and 2015 was 6.87% and 7.59%, respectively in relation to the total amount financed. The average dealer discount associated with new volume for the nine months ended December 31, 2016 and 2015 was 7.00% and 7.56%, respectively.

The amount of future unearned income is computed as the product of the Contract rate, the Contract term and the Contract amount.

Deferred revenues consist primarily of commissions received from the sale of ancillary products. These products include automobile warranties, roadside assistance programs, accident and health insurance, credit life insurance, involuntary unemployment insurance coverage, and forced placed automobile insurance. These commissions are amortized over the life of the contract using the interest method.

The Company's net costs for originating Direct Loans are deferred and recognized as an adjustment to the yield and are amortized over the life of the loan using the interest method.

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## Nicholas Financial, Inc. and Subsidiaries

## Notes to the Consolidated Financial Statements (Continued)

(Unaudited)

**3. Earnings Per Share**

The Company has granted stock compensation awards with nonforfeitable dividend rights which are considered participating securities. As such, earnings per share is calculated using the two-class method. Basic earnings per share is calculated by dividing net income allocated to common shareholders by the weighted average number of common shares outstanding during the period, which excludes the participating securities. Diluted earnings per share includes the dilutive effect of additional potential common shares from stock compensation awards. Earnings per share have been computed based on the following weighted average number of common shares outstanding:

	Three months ended December 31, (In thousands, except per share amounts)		Nine months ended December 31, (In thousands, except per share amounts)	
	2016	2015	2016	2015
<b>Numerator:</b>				
Net income per consolidated statements of income	\$ 1,606	\$ 2,727	\$ 6,479	\$ 9,653
Less: Allocation of earnings to participating securities	(22)		(76)	
Net income allocated to common stock	1,584	\$ 2,727	6,403	\$ 9,653
<b>Basic earnings per share computation:</b>				
Net income allocated to common stock	\$ 1,584	\$ 2,727	\$ 6,403	\$ 9,653
Weighted average common shares outstanding, including shares considered participating securities	7,697	7,623	7,763	7,620
Less: Weighted average participating securities outstanding	(107)		(91)	
Weighted average shares of common stock	7,590	7,623	7,672	7,620
Basic earnings per share	\$ 0.21	0.36	\$ 0.83	1.27
<b>Diluted earnings per share computation:</b>				
Net income allocated to common stock	\$ 1,584	\$ 2,727	\$ 6,403	\$ 9,653
Undistributed earnings re-allocated to participating securities				

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Numerator for diluted earnings per share	\$ <b>1,584</b>	\$ 2,727	\$ <b>6,403</b>	\$ 9,653
Weighted average common shares outstanding for basic earnings per share	<b>7,590</b>	7,623	<b>7,672</b>	7,620
Incremental shares from stock options	<b>60</b>	148		