

# Record

## Steady performance and growing recognition

First-half results announced on 18 November held no surprises after a detailed Q217 trading update issued in October. While underlying profits were down modestly year-on-year, this reflected lumpy allocations to a tactical mandate in H116. More importantly, assets under management equivalents (AUME) and client numbers increased and the company reports that the recent prominence of currency volatility has helped to increase interest in a range of Record's products. The current rating of c 12x FY17e earnings appears conservative and the ordinary yield (before any special payment) stands at over 5%.

Year end	Revenue* (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/15	20.9	7.5	2.66	1.65	11.8	5.3
03/16	21.2	7.0	2.55	1.65	12.2	5.3
03/17e	21.7	7.2	2.62	1.65	11.9	5.3
03/18e	23.1	8.1	2.91	1.65	10.7	5.3

Note: \*Revenue, PBT and EPS exclude non-controlling interests relating to seed investments. EPS is normalised fdil. Prospective dividends exclude any special dividends.

## H117 results

Compared with end March 2016, AUME rose 4% to \$55.0bn from \$52.9bn under a new classification approach set out on page 2. Inflows contributed 2.6% to growth and market moves 4.3% partly offset by a 3% negative exchange rate move. Passive hedging mandates now comprise 83% of the total AUME and generate 53% of fee income, covering operating costs before the group profit share scheme. Underlying pretax profit nearly matched H116; a period that benefited from an unusually high allocation to a tactical bespoke mandate. The majority of currency for return strategies performed well, a potentially positive indicator for future flows. We leave our forecasts unchanged having raised them following the Q2 trading update.

## New opportunities

The recent volatility of foreign exchange markets following surprises such as the Brexit vote and the US election have raised awareness of the risks and rewards of currency management among potential clients. In addition, the development of more sophisticated hedging protocols, increasing regulatory pressure on clients and the development of new products mean Record is able to add more value and therefore earn higher fees from some existing clients.

## Valuation: Still undemanding

Record trades at c 12x our FY17e EPS forecast and an EV/EBITDA multiple of c 5.4x. These still rank below the UK-quoted asset manager peer group we use for comparison (see page 4). The board intends to maintain the ordinary dividend at 1.65p per share subject to business conditions, giving a yield of over 5%, but each year will consider distributing earnings not needed to maintain Record's substantial capital buffer. The relatively low free float may be a restraining factor, but continued growth in AUME, sustained performance in the currency for return strategies and any special distribution could be catalysts for a re-rating.

## Half-year results

### Financial services

25 November 2016

**Price** **31.13p**  
**Market cap** **£69m**

Net cash and money market instruments (£m) at 30 September 2016 (excluding cash consolidated from seed funds) 28.8

Shares in issue 221.4m

Free float 32%

Code REC

Primary exchange LSE

Secondary exchange N/A

### Share price performance



% 1m 3m 12m

Abs 14.8 22.1 8.3

Rel (local) 17.2 22.6 0.3

52-week high/low 33.6p 22.1p

### Business description

Record is a specialist, independent currency manager providing a number of products and services, including passive and dynamic hedging, and a range of currency for return strategies, including funds and customised segregated accounts.

### Next events

Q3 trading update 20 January 2017

Financial year end 31 March 2017

Q4 trading update 21 April 2017

Annual results 16 June 2017

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## Half-year results

The half-year results were in line with expectations following the detailed Q2 trading update covered in our last [note](#) of 25 October, and we have not changed our estimates. In this section we summarise the key points and then deal in more detail with the product reclassification (which does not reflect any change in the underlying business).

- **AUME** increased 4% to \$55.0bn at 30 September from \$52.9bn at 31 March, reflecting inflows of \$1.4bn, positive market movements of \$2.3bn and negative FX effects of \$1.6bn.
- **Client numbers** increased to 61 from 58 at the end of March and, on a longer view, have risen from 41 in 2012 and 48 in 2014.
- **Revenue** on a reported basis was £11.1m, vs £10.4m in H116. This included £0.5m of other income from funds in which Record has non-controlling interests. The underlying revenue number of £10.6m in H117 compares well with H116's £10.8m given the prior year period benefited from an unusually high level of revenue from a tactical bespoke mandate. 53% of management fee income now comes from relatively sticky and stable passive hedging mandates and covers all operating expenses before the group profit share.
- **Underlying operating profit** followed a similar pattern at £3.5m vs £3.6m in H116 and was ahead of £3.3m in H216. The **margin** of 33% was unchanged from H116. **Basic EPS** were 1.33p vs 1.36 in H116.
- An unchanged interim **dividend** of 0.825p has been declared, which will be paid on 23 December. Subject to business conditions, the board intends to pay a maintained full year ordinary dividend of 1.65p. As reported at the year-end, the board is of the view that Record now has sufficient capital to give it, and potential clients, confidence in the strength of the balance sheet. The board will therefore consider paying special dividends or other distributions at the end of each financial year to return at least some of the surplus of earnings over the ordinary dividend for that year. Based on our estimated earnings this could allow for an additional payout of up to c 0.95p, giving a potential yield of over 8%.

Exhibit 1 gives performance data for Record's currency for return strategies. All components of the multi-strategy product (emerging market, forward rate bias, and momentum and value) generated a positive performance in the half-year. The forward rate bias strategy benefited from higher-rate currency performance while most lower-rated currencies weakened (the yen was an exception).

### Exhibit 1: Performance

Fund name	Gearing	Half year return	Return SI pa	Volatility SI pa	Inception
FTSE FRB10 Index Fund	1.8	3.97%	1.60%	7.46%	Dec 2010
Emerging Market Currency Fund	1.0	3.16%	0.54%	6.61%	Dec 2010
Index/Composite returns		Half year return	Return SI pa	Volatility SI pa	
FTSE Currency FRB10 GBP excess return		2.16%	2.31%	4.64%	
Currency Value		1.82%	3.39%	3.23%	
Currency Momentum		4.76%	2.68%	3.74%	
Record Multi-Strategy		2.52%	1.56%	2.20%	Aug 2012
Record Multi-Strategy (with FRB10)		3.16%	2.06%	2.42%	Feb 2015

Source: Record plc. Note: SI = since inception.

## Product reclassification

Record manages the impact of foreign exchange rather than the underlying assets and its measure of assets under management is therefore notional, distinguished by the descriptive title, 'assets under management equivalents' (AUME). Management fees are accrued on a daily basis, usually on an agreed percentage of AUME denominated in the client's chosen currency. Record has historically reported AUME and management fees under four product categories: dynamic hedging, passive hedging, currency for return and cash & other. But in practice, some clients set mandates

that combine hedging and return-seeking objectives, with fees for each calculated differently. Previously such mandates were separated into different product lines for reporting purposes; from now on, to reflect the composition of AUME and fees earned more consistently, Record will report a fifth category: 'multi-product'. It should be emphasised that there has been no change in service or product offered and there is no change in how Record operates or earns management fees. AUME in the multi-product category are now based on the chargeable size of those mandates and this results in the \$0.8bn reduction in AUME on the new definition shown in Exhibit 2. Two mandates currently fall into the multi-product category.

**Exhibit 2: AUME reclassification as at 30 September 2016**

	Historic AUME (\$bn)	Reclassification (\$bn)	AUME redefinition (\$bn)	New AUME (\$bn)	Old management fee rate (bps)	New management fee rate (bps)
Dynamic hedging	7.5	(1.8)	0.0	5.7	14	13
Passive hedging	46.0	(0.4)	0.0	45.6	4	4
Currency for return	2.1	(1.2)	0.0	0.9	14	17
Multi-product		3.4	(0.8)	2.6		20
Cash & other	0.2	0.0	0.0	0.2		
<b>Total/fee income (£m)</b>	<b>55.8</b>	<b>(0.0)</b>	<b>(0.8)</b>	<b>55.0</b>	<b>10.6</b>	<b>10.6</b>

Source: Record plc, Edison Investment Research

## Outlook

Currency markets have had a turbulent two years, with three events standing out: the revaluation of the Swiss franc in January 2015, the result of the UK's EU referendum and the election of Donald Trump to the US presidency. The diversity of Record's clients' requirements means that market movement in one particular direction is not necessarily of net benefit or detriment to the mandates it manages overall, but these events have raised the profile of currency management as a matter for potential clients to consider. Management reports that there has been an increase in the number of inquiries and that several discussions either to expand existing mandates or to establish new ones are underway.

Currency markets are also experiencing regulatory change, which increases the compliance burden for some of Record's clients by requiring margin to be posted to support currency hedging positions for example. While this could put off clients, it is also an opportunity for Record to add value by managing collateral. The growing sophistication of passive hedging has also meant that it commands higher fee margins, breaking 4bps on average for the first time in H117. New services such as tenor management have also been developed (optimising the time at which a forward contract is rolled), which can save clients 20-30bps on 20% of their portfolio or 4-6bps across a whole portfolio, a saving equivalent to the cost of a passive hedging mandate.

With volatility likely to continue in currency markets, these developments present opportunities for Record to attract new business and increase returns.

The positive performance of currency for return strategies recorded in Exhibit 1 is encouraging for future inflows. While recent weakness in emerging market currencies has partly reversed the performance in this area, the company indicates it is still in positive territory year to date. The new categorisation of AUME already makes clear an increase from \$0.6bn to \$0.9bn in currency for return between March and September this year.

## Valuation

As a specialist currency manager with an emphasis on hedging mandates, Record is differentiated from other asset managers. While the drivers of assets under management are different, Record's charging model is similar to other asset managers. We therefore compare Record with UK-quoted asset managers in Exhibit 3. It is at the lower end of the range for both P/E and EV/EBITDA, with the latter multiple clearly reflecting the strong cash balance.

**Exhibit 3: Earnings and EBITDA multiple comparisons for UK fund managers**

	Price (p)	Market cap (£m)	P/E ratio (x)	EV/EBITDA (x)
Aberdeen Asset Management	287.8	3,801	14.5	10.5
Ashmore	296.5	2,084	15.9	9.2
City of London Investment Group	354.8	92	12.8	7.5
Henderson	244.2	2,762	16.5	12.1
Impax Asset Management	48.5	62	16.3	10.8
Jupiter	435.6	1,993	14.4	9.9
Liontrust	345.0	156	15.0	8.1
Man Group	124.1	2,079	11.5	6.2
Polar Capital	284.5	257	13.9	8.2
Schroders	2,850.0	7,617	16.3	12.3
<b>Average</b>			<b>14.7</b>	<b>9.5</b>
<b>Record</b>	<b>31.1</b>	<b>69</b>	<b>11.9</b>	<b>5.2</b>

Source: Bloomberg, Edison Investment Research. Note: P/E ratio and EV/EBITDA for calendar 2016e. Prices at close 23 November 2016

Record's shareholders' funds of £35m and money market instruments, cash and equivalents (excluding non-controlling interests) of £28.8m at the half-year point provide ample capital and liquidity headroom, which management considers to be sufficient to give clients confidence in the stability of the business and its ability to withstand potential shocks. As noted earlier, this raises the possibility of special dividends that, on our estimates, could increase the yield on the ordinary dividend of over 5% to more than 8%.

**Exhibit 4: Financial summary**

£000s except where stated	2015	2016	2017e	2018e
Year to March				
<b>PROFIT &amp; LOSS</b>				
Revenue	21,057	21,134	21,656	23,054
Operating expenses	(13,521)	(14,344)	(14,567)	(15,141)
Operating Profit (before amortisation and except.)	7,536	6,790	7,089	7,913
Finance income	146	143	142	146
Profit Before Tax	7,682	6,933	7,230	8,059
Taxation	(1,708)	(1,523)	(1,518)	(1,692)
Minority interests	(192)	131	0	0
Attributable profit	5,782	5,541	5,712	6,367
Normalised revenue (underlying)	20,865	21,246	21,656	23,054
Operating expenses (excluding depreciation and amortisation)	(13,206)	(14,023)	(14,246)	(14,820)
EBITDA	7,659	7,223	7,410	8,234
Depreciation and amortisation	(315)	(321)	(321)	(321)
Normalised Operating profits	7,344	6,902	7,089	7,913
Finance income	146	143	142	146
Profit Before Tax (norm)	7,490	7,045	7,230	8,059
Normalised revenue/AuME (excluding perf fees) bps	6.0	4.7	5.2	5.2
Normalised Operating Margin norm. (%)	35.2	32.5	32.7	34.3
Average Diluted Shares Outstanding (m)	218.4	217.9	218.3	218.5
Basic EPS (p)	2.66	2.55	2.63	2.93
EPS - normalised fully diluted (p)	2.65	2.54	2.62	2.91
Dividend per share - proposed (p)	1.65	1.65	1.65	1.65
<b>BALANCE SHEET</b>				
Fixed Assets	3,273	423	282	141
Intangible Assets	504	299	105	(89)
Tangible Assets	129	81	134	187
Investments	2,567	0	0	0
Deferred tax assets	73	43	43	43
Current Assets	37,053	40,541	42,872	45,947
Debtors	6,324	5,695	5,805	6,180
Cash	12,010	21,720	23,941	26,642
Money market instruments	18,100	13,020	13,020	13,020
Other	619	106	106	106
Current Liabilities	(4,522)	(3,256)	(3,318)	(3,474)
Creditors	(2,949)	(2,372)	(2,418)	(2,574)
Other	(1,573)	(884)	(900)	(900)
Net Assets	35,804	37,708	39,837	42,615
Minority interests	3,876	4,019	4,019	4,019
Net assets attributable to ordinary shareholders	31,928	33,689	35,818	38,596
No of shares at year end	217.5	217.2	217.5	217.5
NAV per share p	14.7	15.5	16.5	17.7
<b>CASH FLOW</b>				
Operating Cash Flow	6,472	5,791	5,843	6,323
Capex	(128)	(29)	(130)	(130)
Cash flow from investing activities	0	(39)	(50)	(50)
Dividends	(3,266)	(3,750)	(3,583)	(3,589)
Other financing activities	(2,571)	7,737	142	146
Other	0	0	0	0
Net Cash Flow	507	9,710	2,221	2,700
Opening cash/(net debt)	11,503	12,010	21,720	23,941
Other	0	0	0	0
Closing net (debt)/cash	12,010	21,720	23,941	26,642
Closing net debt/(cash) inc money market instruments	30,110	34,740	36,961	39,662
Closing AUME (\$bn)	55.4*	52.9	55.0	55.8

Source: Record, Edison Investment Research. Note \*2015 AUME on previous disclosure basis.

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