

Record

Another performance fee to bolster FY19

Record's Q319 trading update showed a 6.5% decline in AUME, reflecting a combination of outflows, market weakness and foreign exchange moves. This leads to a 10% reduction in our FY20e earnings. For the current year the negative effect is more than offset by crystallisation of a further performance fee, which is a reminder of the potential for positive earnings surprises in subsequent periods, where we assume none. Following further price weakness, the valuation appears cautious.

Year end	Revenue (£m)	PBT (£m)	EPS* (p)	DPS** (p)	P/E (x)	Yield (%)
03/17	23.0	7.9	2.90	2.00	10.6	6.5
03/18	23.8	7.3	2.98	2.30	10.3	7.5
03/19e	24.7	7.5	3.02	2.30	10.2	7.5
03/20e	21.4	5.1	2.08	2.32	14.7	7.6

Note: *EPS are diluted and **DPS excludes special dividends.

Markets trim AUME but performance fee to boost EPS

Record's Q319 trading update for the period to end December showed assets under management equivalent (AUME) down 6.5% in the quarter to \$57.8bn, or 4.2% lower in sterling terms. While below the assumption made in our estimates following H119, this was broadly unsurprising in the context of weakness in equity markets and the previously announced mandate terminations in passive hedging (\$2.5bn). In the event, not all the \$2.5bn has left yet, but will do shortly and there was a (relatively) small additional outflow of \$0.5bn in passive hedging. FX moves and mandate scaling, where volatility targets apply, trimmed a further \$0.9bn from the total AUME. Positively, there was an inflow in the currency for return area and another performance fee was earned in the quarter (£1.3m, relating to performance over a six-month period), giving total performance fees of £2.35m for 9M19.

Outlook

The group is still seeing a good level of interest in its services diversified by customer, product and geography. The environment of political and economic uncertainties globally remains conducive to Record's discussions with potential clients. The performance fee earned in the quarter underlines the point that the enhanced hedging and other mandates capable of earning performance fees have the potential to offset the lower management fees they carry and to counter the competitive pressures that remain a feature of the market. Our EPS estimate for the current year is increased by 12%, reflecting the additional performance fee, and for FY20 the lower AUME starting point results in a 10% reduction (with no performance fees assumed).

Valuation

The shares trade on prospective earnings multiples that are below or just above a comparator group of UK fund managers, while the dividend yield is 7.5% (before the special dividend), which appears cautious for a differentiated and well-capitalised business (capital buffer over the regulatory requirement of c £14m).

Q319 trading update

Financial services

22 January 2019

Price 30.70p
Market cap £61m

Net cash (£m) at end-September 2018	22.8
Shares in issue	199.1m
Free float	32%
Code	REC
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	2.0	4.0	(27.1)
Rel (local)	(2.3)	5.2	(19.3)
52-week high/low	51.10p 29.50p		

Business description

Record is a specialist independent currency manager that provides 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

Q419 trading update	17 April 2019
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Changes in AUME and investment performance

As noted, markets had a negative impact on AUME during Record's third quarter. Exhibit 1 makes clear that there is particularly a high level of equity market exposure in dynamic hedging. In addition to the hedging products, some multi-product mandates are also linked to equity and other markets. Equity markets were notably weak in the period with the MSCI World index, as an example, down 13.4% in the period.

Exhibit 1: Underlying asset class exposure of dynamic and passive hedging AUME (H119)

	% AUME		Revenue
	Dynamic	Passive	Est % of total
Equity	95	27	46
Fixed income	0	41	29
Other	5	32	24
	100	100	100

Source: Record, Edison Investment Research

Exhibit 2 analyses both AUME level and the net flows by period. Here we can see that market moves had a negative impact of \$2bn, equivalent to 3.2% of opening AUME. Foreign exchange and scaling effects in volatility-based mandates had a further 1.5% adverse effect. Turning to flows, there was a \$1.3bn outflow in passive hedging, of which \$0.8bn related to the \$2.5bn mandate terminations announced in the Q219 update. There was an additional outflow of \$0.5bn, which at 1% of AUME is within the normal ebb and flow of mandates. The remaining mandates within the \$2.5bn are likely to leave shortly. Otherwise, there has been a \$0.3bn inflow in currency for return.

Exhibit 2: AUME changes

\$bn	Q318	Q418	Q119	Q219	Q319	Q119	Q219	Q319	9M19
	AUME					Net flows			
Dynamic hedging	4.5	4.3	4.3	4.4	3.9	0.4	0.0	0.0	0.4
Passive hedging	54.3	53.0	52	51.7	48.4	(0.4)	(0.6)	(1.3)	(2.3)
Currency for return	1.7	1.6	2.3	2.4	2.4	0.6	0.0	0.3	0.9
Multi-product	3.1	3.0	3.0	3.0	2.9	0.0	0.0	0.0	0.0
Cash and futures	0.3	0.3	0.3	0.3	0.2	0.0	0.0	(0.1)	(0.1)
Total	63.9	62.2	61.9	61.8	57.8	0.6	(0.6)	(1.1)	(1.1)
Markets						1.2	0.1	(2.0)	(0.7)
FX and scaling for volatility targeting mandates						(2.1)	0.4	(0.9)	(2.6)
Total change						(0.3)	(0.1)	(4.0)	(4.4)

Source: Record, Edison Investment Research

Client numbers are virtually unchanged at 65 versus 66 previously, but within this five have left and four have been added. Only two more will leave with the departure of the remaining element of the \$2.5bn of terminations.

On investment performance in the currency for return strategies, Record reports a marked turnaround in emerging markets, which generated a positive return of 2.42% in the quarter giving an annualised performance (ungeared) of +1.76% since inception (30 November 2009). The multi-strategy product performance was also positive at +0.77% in the quarter.

Estimate changes

Estimate changes for revenue, pre-tax profit and EPS are shown in Exhibit 3. The key drivers of the changes are the additional performance fee crystallised in Q319 and the new, lower starting base for AUME following the update. There is a small positive sterling/dollar currency translation effect compared with our previous estimates. Other assumptions, in particular fee margins, are unchanged. As noted earlier, we do not assume performance fees will be earned in future periods

and only include AUME flows already announced. We do allow for some market growth in the underlying assets for hedging (+2% pa).

Exhibit 3: Estimate changes

	Revenue (£m)			PBT (£m)			EPS (p)			DPS (p)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
03/19e	23.7	24.7	4%	6.7	7.5	12%	2.69	3.02	12%	2.30	2.30	0%
03/20e	22.4	21.4	-4%	5.7	5.1	-10%	2.31	2.08	-10%	2.32	2.32	0%

Source: Record, Edison Investment Research. Note: Dividend excludes any special payment.

Valuation

Exhibit 4 shows the recent share performance for Record and the group of UK asset managers that we use for valuation comparison. While Record is differentiated by its currency management specialisation, its fees are generally based on AUME and, as noted above, this means that there is a sensitivity to equity and other markets, as for the asset managers. Most of the asset managers have been affected by weakness in equity markets and pressures on fee margins while the Record share price has been weaker than the average for the asset managers over the periods shown, probably reflecting the neutral then negative AUME flows and negative foreign exchange effects it has experienced.

Exhibit 4: Recent share price performance (%)

	One month	Three months	One year	Ytd	From 12-month high
Ashmore	4.3	6.9	-10.9	3.2	-14.6
City of London Investment Group	-0.3	-1.6	-13.7	-0.4	-17.4
Impax Asset Management	-9.8	-25.3	-3.2	-10.4	-34.2
Jupiter	9.9	-7.3	-44.1	7.7	-46.3
Liontrust	0.9	-9.8	1.6	-0.5	-17.0
Man Group	14.0	3.4	-31.1	10.5	-32.9
Polar Capital	3.6	-19.5	-8.0	1.0	-35.4
Schroders	10.8	-7.2	-28.7	8.1	-30.2
Average	4.2	-7.5	-17.3	2.4	-28.5
Record	-1.5	-15.1	-29.5	-4.5	-43.6

Source: Refinitiv, Edison Investment Research. Priced as at 18.01.19

As shown in Exhibit 5 (the table shows multiples on a calendarised basis), the combination of price weakness and estimate changes leaves Record on below and slightly above average P/E multiples for CY18 and CY19 and on a below average EV/EBITDA (CY19). The yield (before special dividend) is 7.5%. Including last year's special dividend would give a yield of over 9%.

Exhibit 5: Comparing valuation with UK fund managers

	Price (p)	Market cap (£m)	P/E 2018e (x)	P/E 2019e (x)	EV/EBITDA 2019e (x)	Dividend yield (%)
Ashmore	377	2,712	16.7	15.1	8.9	4.4
City of London Investment Group	379	102	10.2	10.9	7.8	7.1
Impax Asset Management	185	243	15.5	14.6	10.3	2.2
Jupiter	318	1,455	10.1	11.7	7.2	5.4
Liontrust	579	295	12.9	12.3	8.5	3.6
Man Group	147	2,281	12.5	9.9	7.2	5.4
Polar Capital	477	449	10.6	10.8	6.5	5.9
Schroders	2,642	7,167	12.1	12.3	10.4	4.3
Average			12.6	12.2	8.3	4.8
Record	30	60	10.0	12.9	7.8	7.7

Source: Refinitiv, Edison Investment Research. Note: P/Es and EV/EBITDA on a calendar year basis. REC dividend yield excludes special dividend (0.5p) and including this the FY18 dividend was 2.8p. Priced as at 18.01.19

Exhibit 6: Financial summary

Year end 31 March	£000s	2015	2016	2017	2018	2019e	2020e
PROFIT & LOSS							
Revenue (underlying)		20,865	21,246	22,952	23,834	24,665	21,416
Revenue		21,057	21,134	22,952	23,834	24,665	21,416
Operating expenses		(13,521)	(14,344)	(15,365)	(16,735)	(17,094)	(16,386)
Other income/(expense)		0	0	157	173	(138)	0
Operating Profit (before amort. and except.)		7,536	6,790	7,744	7,272	7,433	5,030
Finance income		146	143	112	56	92	91
Profit Before Tax		7,682	6,933	7,856	7,328	7,525	5,121
Taxation		(1,708)	(1,523)	(1,540)	(1,182)	(1,505)	(973)
Minority interests		(192)	131	0	0	0	0
Attributable profit		5,782	5,541	6,316	6,146	6,020	4,148
Normalised revenue (underlying)		20,865	21,246	22,952	23,834	24,665	21,416
Operating expenses (excl. dep'n and amortisation)		(13,206)	(14,023)	(15,023)	(16,430)	(16,809)	(16,101)
EBITDA		7,659	7,223	7,929	7,404	7,856	5,315
Depreciation and amortisation		(315)	(321)	(342)	(305)	(285)	(285)
Other income/(expense)		0	0	157	173	(138)	0
Normalised Operating profits		7,344	6,902	7,744	7,272	7,433	5,030
Finance income		146	143	112	56	92	91
Profit Before Tax (norm)		7,490	7,045	7,856	7,328	7,525	5,121
Normalised revenue/AuME (excl. perf fees) bps		6.2	6.0	5.2	5.1	4.8	4.7
Normalised operating margin (%)		35.2	32.5	33.7	30.5	30.1	23.5
Average Number of Shares Outstanding (m)		218.4	217.9	218.0	206.5	199.1	199.1
Basic EPS (p)		2.66	2.55	2.91	3.03	3.07	2.11
EPS - normalised (p)		2.65	2.54	2.90	2.98	3.02	2.08
Dividend per share (p)		1.65	1.65	2.00	2.30	2.30	2.32
Special dividend per share (p)		0.00	0.00	0.91	0.50	0.77	0.00
Total dividend (p)		1.65	1.65	2.91	2.80	3.07	2.32
BALANCE SHEET							
Fixed Assets		3,273	423	1,228	2,339	2,212	2,217
Intangible Assets		504	299	245	228	363	448
Tangible Assets		129	81	881	910	740	660
Investments		2,567	0	0	1,115	1,075	1,075
Deferred tax assets		73	43	102	86	34	34
Current Assets		37,053	40,541	44,247	29,737	31,735	29,346
Debtors		6,324	5,695	6,972	6,775	8,036	7,174
Cash		12,010	21,720	19,120	12,498	13,717	12,190
Money market instruments		18,100	13,020	18,102	10,198	9,804	9,804
Other		619	106	53	266	178	178
Current Liabilities		(4,522)	(3,256)	(8,644)	(5,525)	(7,035)	(6,633)
Creditors		(2,949)	(2,372)	(3,013)	(2,630)	(3,749)	(3,347)
Financial liabilities		0	0	(4,779)	(2,467)	(2,361)	(2,361)
Other		(1,573)	(884)	(852)	(428)	(925)	(925)
Net Assets		35,804	37,708	36,831	26,551	26,913	24,930
Minority interests		3,876	4,019	0	0	0	0
Net assets attributable to ordinary shareholders		31,928	33,689	36,831	26,551	26,913	24,930
No of shares at year end		217.5	217.2	221.4	199.1	199.1	199.1
NAV per share p		14.7	15.5	16.6	13.3	13.5	12.5
CASH FLOW							
Operating Cash Flow		6,472	5,509	7,107	2,746	6,631	4,802
Capex		(128)	(29)	(899)	(236)	(50)	(140)
Cash flow from investing activities		0	(39)	(189)	(82)	(200)	(150)
Dividends		(3,266)	(3,750)	(3,592)	(6,810)	(5,541)	(6,131)
Other financing activities		(2,571)	7,737	(5,163)	(2,386)	106	91
Other		0	282	136	146	274	0
Net Cash Flow		507	9,710	(2,600)	(6,622)	1,219	(1,528)
Opening cash/(net debt)		11,503	12,010	21,720	19,120	12,498	13,717
Other		0	0	0	0	0	0
Closing net (debt)/cash		12,010	21,720	19,120	12,498	13,717	12,190
Closing net debt/(cash) inc money market instruments		30,110	34,740	37,222	22,696	23,521	21,994
AUME							
Opening (\$bn)		51.9	55.4	52.9	58.2	62.2	60.5
Net new money flows		2.9	(1.4)	3.1	(1.2)	(2.8)	0.0
Market/other		0.6	(1.1)	2.2	5.2	1.1	1.1
Closing (\$bn)		55.4	52.9	58.2	62.2	60.5	61.6

Source: Record accounts, Edison Investment Research

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