

# Record

## Enhancing products and service

H120 results

Record has maintained its commitment to improving service levels and introducing new products to meet client needs. In H120 this included a new strategy within the currency for return area and it is extending its derivative management capabilities to asset classes outside currency. These initiatives may not affect earnings significantly in the near term but are part of a process of innovation and investment that has helped to limit fee margin erosion and provide a stronger base for future client acquisition.

Year end	Revenue (£m)	PBT (£m)	EPS* (p)	DPS** (p)	P/E (x)	Yield (%)
03/18	23.8	7.3	2.98	2.30	13.8	5.6
03/19	25.0	8.0	3.25	2.30	12.6	5.6
03/20e	22.8	6.2	2.52	2.30	16.3	5.6
03/21e	22.8	6.0	2.47	2.30	16.6	5.6

Note: \*EPS is diluted. \*\*DPS excludes special dividends.

## H120 results slightly ahead of expectation

Assets under management equivalent (AUME) had already been reported and in US dollar terms were up 4.6% to \$59.9bn in H120, mainly as a result of net inflows of \$2bn. Average AUME in sterling terms was marginally down on H119 and after small mix and fee margin effects, management fees were down just 3%. There were no performance fees in the period (vs £1m in H119) so revenues were down nearly 10% to £11.4m. Costs were held broadly stable with lower variable compensation offsetting investment in IT and people to support client services and new products. This meant the decline in pre-tax profit from £4.0m in H119 to £3.2m essentially reflected the absence of an equivalent performance fee this year. Diluted EPS was 1.29p versus 1.61p and the interim dividend was maintained at 1.15p. The balance sheet remains strong with no debt and own cash of £17.7m.

## Encouraging outlook

The global backdrop, with continuing sources of geopolitical uncertainty, remains favourable for Record when meeting potential and existing clients. It sees an encouraging range of opportunities across its product range and geographies. The group's track record and position as an independent currency manager allied with its dedication to improving and customising services for clients stand it in good stead to counter competitive pressures and grow the business over the longer term.

## Valuation

Our EPS estimate for the current year is increased by 6%, reflecting the slightly better than expected H1 outcome and higher AUME level. For FY21 these positive effects are neutralised by the recent strengthening in the sterling/US dollar rate. Compared with asset management peers, Record trades on a similar prospective P/E rating and offers a yield premium and the potential for a special dividend if performance fees are earned.

## Financial services

28 November 2019

**Price** 41p  
**Market cap** £82m

Net cash (£m) at end September 2019 excluding seed fund cash of £5.8m 17.7

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 28.8 31.1

Rel (local) 0.5 22.6 23.5

52-week high/low 41.2p 27.3p

## 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

Q320 trading update 17 January 2020

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## Independent specialist currency manager

Founded in 1983 by chairman Neil Record, the company's main activity is providing currency hedging services, acting as an agent for clients, including public and private defined benefit pension schemes and other institutional investors. Record also offers currency for return, multi-product and related services.

The passive hedging product seeks to provide cost-effective reduction of exposure to currency risk for clients' international portfolios. To counter competitive pressures from large banks, Record places strong emphasis on providing a tailored service to meet customer requirements and may include additional services as part of its offering. Its enhanced passive hedging service provides the same risk mitigation but aims to exploit structural inefficiencies in currency markets to deliver an enhanced outcome. Dynamic hedging also targets systematic reduction of currency risk while seeking to modify the level of hedging to allow clients to gain some benefit from weakness in their own currency. Currency for return strategies aim to exploit stable inefficiencies in currency markets and include a number of strategies: forward rate bias, emerging market currencies, momentum, value and, recently introduced, range-trading and dynamic macro currency (see comments below). The multi-product category includes mandates where hedging and return-seeking strategies are combined on a bespoke basis.

### Exhibit 1: Record profile in numbers (H120)

Analysis by strategy						
			AUME (%)	Management fees (%)*	Est. average fee rate (bp)**	
Dynamic hedging			5.3	17.9	15	
Passive hedging			84.1	52.8	3	
Currency for return			4.8	8.6	9	
Multi-product			5.2	20.7	19	
Cash			0.5	N/A	N/A	
Total			100.0	100.0	5	
Value			\$59.9bn	£11.1m		
Client analysis						
Number (by financial year)		Type	% AUME	Concentration	% fees	Longevity (years)
2015	55	Public pension funds	42	Top 10	76	≤1
2016	58	Corporate pension funds	42	Next 10	19	>1 to ≤3
2017	59	Foundations & trusts	11	Balance	5	>3 to≤ 6
2018	60	Other	5			>6 to ≤10
2019	65					>10
H120	70		100		100	
Geographical analysis						
By country		% fees		% AUME	AUME progression (\$bn)	
Switzerland	41	Europe ex-UK		74	2015	55.4
US	26	North America		12	2016	52.9
UK	10	UK		12	2017	58.2
Other	22	RoW		2	2018	62.2
					2019	57.3
	100			100	H120	59.9
Underlying asset class exposure of dynamic and passive hedging AUME (%)						
			Dynamic	Passive	Est. % of hedging fees	
Equity			100	29	47	
Fixed income			0	42	31	
Other			0	29	22	
			100	100	100	

Source: Record, Edison Investment Research. Notes: \*Management fee excluding performance fees. \*\*Fee rate is our own calculation and within each strategy there will be a range of mandate types and fee structures/levels. Rounding may mean some columns do not sum.

We have collated Record's disclosure analysing AUME and management fee exposure in the table above. The first section gives an analysis of AUME, fees and fee rates **by strategy**. This underlines

the importance of hedging services that in total accounted for 70% of revenue in H120. Passive hedging AUME was 84% of the total but the relatively low fee rates that prevail in this area, at c 3bp on average, meant the strategy contributed 53% of management fees.

The **client analysis** shows a progression in the number of clients over the period shown with a net addition of five in the first half of the current year. This count is by legal entity and a commercial relationship includes a number of entities so there can be lumpy movements in the client count. In total, 38% of clients have been with Record for over six years. The institutional nature of the market served (with 84% of AUME from pension funds) means client concentration is quite high with 76% of fees earned from the top 10 clients.

The **geographical analysis** shows the importance of Swiss mandates (mainly for hedging services), which accounted for 41% of fees, whereas Europe ex-UK accounted for 74% of AUME. The base currency exposure of AUME at end-March was 57% in Swiss francs, 16% in euros, 13% in sterling and 11% in US dollars. Between FY15 and H120 AUME increased from \$55.4bn to \$59.9bn with the progression dampened by an outflow of \$4.5bn in FY19, primarily from passive hedging mandates where specific developments, including moving to a unitised structure, played a role in the terminations.

Finally, looking at the underlying **asset class exposure** for the hedging mandates, equity markets account for an estimated 47% of hedging management fees with fixed income 31%. As shown, dynamic hedging mandates were entirely equity related while passive hedging exposure was more balanced, including 42% in fixed income and 29% in other assets.

## Recent AUME changes and first-half results

### AUME

As announced in its October trading update, Record's AUME increased by \$2.6bn (4.6% or 10.6% in sterling terms) during H120 with most of the increase accounted for by net inflows of \$2bn for this period (see Exhibit 2). The main element within this was passive hedging mandates where the net inflow was \$1.6bn. Most of the inflow took place in the second quarter and largely reflected adjustments to existing clients' mandates. Market movements accounted for a positive \$1.3bn change whereas foreign exchange and mandate scaling effects generated a negative move of \$0.7bn. Compared with end-H119, US dollar AUME was 3% lower whereas, based on reported quarter-end figures, we calculate that sterling-denominated average AUME was marginally lower in H120 than in H119 (-0.2%).

**Exhibit 2: AUME changes**

Year-end March	Q219	Q419	Q120	Q220	Q120	Q220	H120
\$bn	AUME	AUME	AUME	AUME	Net flows	Net flows	Net flows
Dynamic hedging	4.3	3.1	3.4	3.2	0.3	(0.1)	0.2
Passive hedging	52.0	48.2	48.9	50.4	0.1	1.5	1.6
Currency for return	2.3	2.7	2.6	2.9	(0.1)	0.3	0.2
Multi-product	3.0	3.0	3.1	3.1	0.0	0.0	0.0
Cash and futures	0.3	0.3	0.3	0.3	0.0	0.0	0.0
<b>Total</b>	<b>61.9</b>	<b>57.3</b>	<b>58.3</b>	<b>59.9</b>	<b>0.3</b>	<b>1.7</b>	<b>2.0</b>
Markets					0.0	1.3	1.3
FX and scaling for mandate volatility targeting					0.7	(1.4)	(0.7)
<b>Total change</b>					<b>1.0</b>	<b>1.6</b>	<b>2.6</b>

Source: Record, Edison Investment Research

### H120 results

The profit and loss for H120 with analysis of changes since H119 and H219 is set out in Exhibit 3. Comments on key areas are below with comparisons between H120 and H119 unless stated.

- Total **management fees** were down 2.5% reflecting a combination of a marginally lower average AUME level (see comments above) and mix changes.
- Within this, dynamic hedging fees fell by 15.2% as average AUME in this area (down c 20% in sterling terms) was reduced by discretionary profit-taking undertaken by Record on behalf of a client in FY19. This reduction has been partially reversed in the current year.
- **Total revenue** was nearly 10% lower as there was no performance fee crystallised in the period compared with H119, which included fees of £1m.
- **Fee margins** on a like-for-like basis were broadly stable and we calculate the average fee margin for the group has been similar over the last three half-year periods, at 4.8bp per year for H120 based on the reported revenue and AUME figures. The effect of the uptake of the enhanced passive hedging product with a c 10% lower management fee and the potential for performance fees on management fee margin has been limited.
- **Costs** were nearly flat with lower variable compensation offsetting investment in people and IT to support continued client service enhancement and new products. Although lower, variable compensation as a percentage of pre-bonus operating profit increased to 31.6% (30%), reflecting the adoption of more flexible profit share rules that take account of individual performance to a greater extent. The variable payment percentage may range between 25% and 35%.
- The containment of costs meant there was only a £0.9m (22%) reduction in **pre-tax profits** essentially reflecting the absence of performance fees.
- The interim **dividend** was unchanged at 1.15p and the group remains committed to its policy of paying out excess earnings subject to capital and investment requirements.

**Exhibit 3: H120 P&L analysis**

£000	H119	H219	H120	Change vs H119	Change vs H219
Dynamic hedging	2,351	2,247	1,994	-15.2%	-11.3%
Passive hedging	5,999	5,611	5,880	-2.0%	4.8%
Currency for return	899	876	958	6.6%	9.4%
Multi-product	2,172	2,153	2,301	5.9%	6.9%
<b>Management fees</b>	<b>11,421</b>	<b>10,887</b>	<b>11,133</b>	<b>-2.5%</b>	<b>2.3%</b>
Performance fees	1,048	1,285	0	-100.0%	-100.0%
Other investment services income	155	177	252	62.6%	42.4%
<b>Total revenue</b>	<b>12,624</b>	<b>12,349</b>	<b>11,385</b>	<b>-9.8%</b>	<b>-7.8%</b>
Cost of sales	-194	-191	-119	-38.7%	-37.7%
<b>Gross profit</b>	<b>12,430</b>	<b>12,158</b>	<b>11,266</b>	<b>-9.4%</b>	<b>-7.3%</b>
Administrative expenses	-8,295	-8,409	-8,232	-0.8%	-2.1%
Other income/expense	-138	130	50	-136.2%	-61.5%
<b>Operating profit</b>	<b>3,997</b>	<b>3,879</b>	<b>3,084</b>	<b>-22.8%</b>	<b>-20.5%</b>
Net finance income	41	72	83	102.4%	15.3%
<b>Profit before tax</b>	<b>4,038</b>	<b>3,951</b>	<b>3,167</b>	<b>-21.6%</b>	<b>-19.8%</b>
Taxation	-822	-737	-652	-20.7%	-11.5%
<b>Profit after tax</b>	<b>3,216</b>	<b>3,214</b>	<b>2,515</b>	<b>-21.8%</b>	<b>-21.7%</b>
<b>Diluted EPS (p)</b>	<b>1.61</b>	<b>1.62</b>	<b>1.29</b>	<b>-19.8%</b>	<b>-20.1%</b>
DPS (p)	1.15	1.84	1.15	0.0%	
Tax rate	20%	19%	21%		

Source: Record, Edison Investment Research

Exhibit 4 shows the performance of currency for return fund, index and composite performance in the half year and since inception. All showed positive returns in the half year with the Multi-Strategy Composite in particular showing a relatively favourable combination of return and volatility since inception, with an information ratio of 0.55 compared with 0.42 for the Deutsche Bank currency index (in US dollar with equal weighting between carry, momentum and value). Record also reported that the long-term performance puts it in the top quartile of its peer group. The product combines carry, emerging market, momentum, value and range trading strands. The addition of a

complementary dynamic macro strategy should help to generate a diversified return. The performance of the Multi-Strategy Fund is still affected by a weak initial period following its launch in 2018 but was positive in H120.

Record has also reported the performance of the enhanced passive hedging programme relative to a fixed tenor benchmark. This showed a half-year return of 0.04% and a since-inception (October 2014) annual return of 0.12%. This is material in the context of Record's average passive hedging management fee margin of 0.03% per year.

**Exhibit 4: Currency for return investment performance to 30 September 2019**

	Gearing	Half-year return	Return SI pa	Volatility SI pa	Inception
<b>Fund</b>					
Record FTSE FRB10 Index Fund	1.8	0.27%	1.70%	6.73%	Dec-10
Record Emerging Market Currency Fund	1.0	3.67%	1.63%	6.33%	Dec-10
Record Currency Multi-Strategy Fund		0.77%	-1.72%	9.33%	Feb-18
<b>Index/composite returns</b>					
FTSE Currency FRB10 GBP excess return		0.02%	2.18%	4.50%	Dec-87
Record Multi-Strategy Composite (4% target volatility)		2.38%	1.52%	2.80%	Jul-12

Source: Record. Note: All GBP base apart from Record Multi-Strategy Composite, which is on a US\$ base and shows excess returns gross of fees.

Record continues with its strategy of product innovation to counter downward pressure on fee rates and, with the results, announced the New York hiring of John Floyd, a seasoned FX market manager who has managed a dynamic macro strategy for 15 years. This strategy is more discretionary than Record's existing, primarily quantitatively driven strategies and is therefore complementary. In particular, it has demonstrated outperformance in periods of heightened risk aversion in markets that have been more challenging for the more systematic approaches.

Another development is to broaden the application of Record's experience and established market relationships in managing derivatives and derivative overlays by offering a service in asset classes outside currency. Record has for some time managed equity and other derivative strategies to generate synthetic returns on cash deposits required to meet hedging cash flow requirements. As a result this offering has not required significant development of systems and capability. Record expects clients to use this service to facilitate tactical positioning without adjusting underlying portfolio positioning so there would not be related AUME and fees will be reported as part of other investment services income, along with fees from the hedging signal agreement with WisdomTree asset management and other services.

## Outlook, estimate changes

Currency volatility between the euro, US dollar and Swiss franc (Exhibit 5) has been subdued in comparison with 2014/16, but continued geopolitical uncertainties provide a favourable backdrop for Record's conversations with existing and potential clients. Together with Record's own work to enhance service levels and develop new products, this has contributed to what the company describe as a good range of new business opportunities diversified by geography and product. The more recent product initiatives and continued measured investment in IT and people should support the prospects for longer-term growth.

As previously, our forecasts do not assume either AUME inflows or outflows beyond those already announced. Similarly, we do not assume any performance fees until these have been crystallised and announced.

**Exhibit 5: Implied volatility for one year at the money options CHF and EUR vs USD**


Source: Bloomberg. Note: CHF = Swiss franc, EUR = euro, USD = US dollar.

The main factors driving changes in our estimates (see below) are the increase in AUME reported for the first half, minor positive adjustments to assumed fee margins based on implied values for H120 and updating the assumed sterling/US dollar exchange rates (significantly negative for FY21) to reflect recent market moves. Further details of our estimates are shown in the financial summary (Exhibit 8).

**Exhibit 6: Estimate changes**

	Revenue (£m)			PBT (£m)			EPS (p)			DPS (p)*		
	Old	New	Change	Old	New	Change	Old	New	Change	Old	New	Change
03/20e	22.2	22.8	2%	5.8	6.2	6%	2.38	2.52	6%	2.32	2.30	-1%
03/21e	23.0	22.8	-1%	6.0	6.0	0%	2.46	2.47	0%	2.34	2.30	-2%

Source: Edison Investment Research. Note: \*Dividend excludes any special payment.

The group figure for net cash and money market instruments managed as cash was similar to the year-end figure at £23.5m (£23.7m). Stripping out the cash held by seed funds (non-controlling interests) gives an own cash figure of £17.7m.

## Valuation

An updated version of our valuation table, which shows Record in the context of a group of UK asset managers, is shown below. Record is differentiated by its role as a specialist currency manager but its fees are primarily based on the size of AUME so, like the asset managers, it is exposed to movements in underlying equity and fixed income markets and flows.

**Exhibit 7: Comparing valuation with UK fund managers**

	Price (p)	Market cap (£m)	P/E 2019e (x)	EV/EBITDA 2019e (x)	Dividend yield (%)
Ashmore	467	3,314	17.8	11.4	3.6
City of London Investment Group	445	118	12.4	10.1	6.1
Impax Asset Management	286	371	26.5	19.0	1.4
Jupiter	375	1,707	13.3	8.9	4.6
Liontrust	918	500	16.8	12.7	2.9
Man Group	147	2,864	11.0	8.3	6.0
Polar Capital	526	507	12.9	7.0	6.3
Schroders	3,289	8,780	16.9	12.2	3.5
<b>Average</b>			<b>16.0</b>	<b>11.2</b>	<b>4.3</b>
<b>Record</b>	<b>41</b>	<b>81</b>	<b>15.1</b>	<b>9.3</b>	<b>5.6</b>

Source: Refinitiv, Edison Investment Research. Note: P/Es and EV/EBITDA on a calendar year basis. Record's dividend yield excludes the special dividend. Priced at 26 November 2019.

Although Record's shares appreciated strongly after the October second-quarter trading update, they previously lagged the asset manager peers and now trade on below the peer average calendar year 2019 P/E and EV/EBITDA ratios. The earnings for calendar year 2019 do benefit



from a proportion of the £1m performance fee earned in FY19 and our FY20 Record earnings estimate does not include any performance fees; for FY20 Record is trading on a P/E of 16.3x, only a modest premium to the peer multiple of 15.6x for the same period. Meanwhile, the dividend yield of 5.6% is a premium to the peer average and there is the potential for this to be enhanced with a special dividend, particularly if performance fees are crystallised.

**Exhibit 8: Financial summary**

Year end March	£'000s	2017	2018	2019	2020e	2021e
<b>PROFIT &amp; LOSS</b>						
Revenue		22,952	23,834	24,973	22,763	22,823
Operating expenses		(15,365)	(16,735)	(17,089)	(16,822)	(17,006)
Other income/(expense)		157	173	(8)	50	0
Operating Profit (before amort. and except.)		7,744	7,272	7,876	5,991	5,818
Finance income		112	56	113	166	165
Profit Before Tax		7,856	7,328	7,989	6,156	5,982
Taxation		(1,540)	(1,182)	(1,559)	(1,231)	(1,137)
Minority interests		0	0	0	55	40
Attributable profit		6,316	6,146	6,430	4,980	4,886
Revenue/AuME (excl. perf fees) bps		5.2	5.1	4.9	4.9	4.8
Operating margin (%)		33.7	30.5	31.5	26.3	25.5
Average Number of Shares Outstanding (m)		218.0	206.5	198.1	197.5	197.5
Basic EPS (p)		2.91	3.03	3.27	2.54	2.49
EPS - diluted (p)		2.90	2.98	3.25	2.52	2.47
Dividend per share (p)		2.00	2.30	2.30	2.30	2.30
Special dividend per share (p)		0.91	0.50	0.69	0.00	0.00
Total dividend (p)		2.91	2.80	2.99	2.30	2.30
<b>BALANCE SHEET</b>						
Non-current assets		1,228	2,339	2,161	3,425	2,806
Intangible Assets		245	228	288	378	418
Tangible Assets		881	910	761	776	681
Investments		0	1,115	1,112	1,152	1,152
Other		102	86	0	1,119	555
Current Assets		44,247	29,737	31,427	30,406	30,747
Debtors		6,972	6,775	7,562	6,674	6,720
Cash		19,120	12,498	12,966	9,740	10,035
Money market instruments		18,102	10,198	10,735	13,860	13,860
Other		53	266	164	132	132
Current liabilities		(8,644)	(5,525)	(6,158)	(6,010)	(6,028)
Creditors		(3,013)	(2,630)	(2,736)	(2,627)	(2,645)
Financial liabilities		(4,779)	(2,467)	(2,621)	(2,721)	(2,721)
Other		(852)	(428)	(801)	(662)	(662)
Non-current liabilities		0	0	(29)	(1,170)	(606)
Net Assets		36,831	26,551	27,401	26,651	26,918
Minority interests		0	0	60	125	85
Net assets attributable to ordinary shareholders		36,831	26,551	27,341	26,526	26,833
No of shares at year end		221.4	199.1	199.1	199.1	199.1
NAV per share p		16.6	13.3	13.7	13.3	13.5
<b>CASH FLOW</b>						
Operating Cash Flow		7,107	2,746	7,026	6,423	5,562
Capex		(899)	(236)	(72)	(250)	(140)
Cash flow from other investing activities		(5,159)	7,899	(561)	(3,149)	15
Dividends		(3,592)	(6,810)	(5,517)	(5,908)	(4,578)
Other financing activities		(193)	(10,367)	(613)	(461)	(564)
Other		136	146	205	120	0
Net Cash Flow		(2,600)	(6,622)	468	(3,226)	294
Opening cash/(net debt)		21,720	19,120	12,498	12,966	9,740
Other		0	0	0	0	0
Closing net (debt)/cash		19,120	12,498	12,966	9,740	10,035
Closing net debt/(cash) inc money market instruments		37,222	22,696	23,701	23,600	23,895
<b>AUME</b>						
Opening (\$'bn)		52.9	58.2	62.2	57.3	59.8
Net new money flows		3.1	(1.2)	(4.5)	2.0	0.0
Market/other		2.2	5.2	(0.4)	0.5	0.6
Closing (\$'bn)		58.2	62.2	57.3	59.8	60.4

Source: Record accounts, Edison Investment Research



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