

# Record

Q221 trading update

## AUME growth prompts estimate increases

Record's Q221 trading update confirmed that its new \$8bn dynamic hedging mandate has started and that, prior to this, assets under management equivalent (AUME) expanded by 4% in the quarter. The group continues to work on developing new products and is deploying technology to enhance its ability to deliver these and existing products cost effectively.

Year end	Revenue (£m)	PBT (£m)	EPS* (p)	DPS** (p)	P/E (x)	Yield (%)
03/19	25.0	8.0	3.25	2.30	13.2	5.3
03/20	25.6	7.7	3.26	2.30	13.2	5.3
03/21e	24.9	6.5	2.68	2.30	16.0	5.3
03/22e	28.7	8.9	3.65	2.30	11.8	5.3

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

## Q221 trading update

In September Record announced that it had, subject to contract, won an \$8bn AUME dynamic hedging mandate. This important win is now confirmed and the mandate started at the beginning of Q321 (October) with AUME likely to build over several quarters. In Q221 AUME in dollar terms grew by 4% to \$65.9bn, mainly reflecting exchange rate movements, scaling related to mandate volatility targeting and movements in equity and other markets (total +\$2.4bn). Net client flows were positive at \$0.2bn. Record is continuing to work on product innovation and is making progress in particular on an Impact/ESG bond product (here Record will effectively be managing the underlying exposure and the currency overlay, so similar to a conventional asset management product with fees at an appropriate level). As part of the group's moves to retain talent and ensure succession planning, a joint share ownership plan was launched in September to provide equity-based incentives to key staff below board level. A sale of 4m shares by chairman Neil Record at 37.3p facilitated the launch.

## Estimates raised in response to AUME increase

We have increased our estimates (EPS +13% FY21, +57% FY22) to take into account the moves in AUME outlined above while allowing for the sterling/dollar rate and some average management fee dilution because of the scale of the new dynamic hedging mandate and the move of some passive hedging mandates to a (lower) management fee with the potential for performance fees. There were no performance fees crystallised in Q221 and we have not assumed any in our estimates so this remains a potential source of upside for earnings and dividends.

## Valuation: Below peer multiples

Although the shares have responded strongly to the news of the new dynamic hedging mandate, they still trade on calendar 2020 P/E and EV/EBITDA multiples below the average for a group of UK asset-managers. On our estimates, Record's multiples will fall further as the full benefits of the increased level of AUME flow through.

### Financial services

21 October 2020

Price **43p**

Market cap **£86m**

Net cash (£m) at end March 2020 excluding seed fund cash of £4.3m 18.0

Shares in issue 199.1m

Free float 56%

Code REC

Primary exchange LSE

Secondary exchange N/A

### Share price performance



% 1m 3m 12m

Abs 37.2 22.0 28.1

Rel (local) 38.9 27.4 52.9

52-week high/low 44.5p 26.3p

### 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

H121 results 24 November 2020

Q321 trading update 22 January 2021

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## Changes in AUME and investment performance

Exhibit 1 shows the recent progression of AUME and net flows. Overall AUME in US dollar terms increased by 4% in Q221 and by nearly 13% in H121 to \$65.9bn: the year-on-year increase was 10%. In sterling terms AUME was marginally down from end June at £51.0bn versus £51.2bn. There was a small inflow in Q221 and a small outflow for H121 as a whole although, within this, the mix was favourable in terms of fee rates as there were inflows into Dynamic hedging (recent average fee rate c 15–16bp) and outflows from Passive hedging (average c 3bp).

We calculate that the average AUME in sterling terms for H121 increased by 6.8% when compared with the average for H120, reflecting a combination of positive net inflows, market moves, scaling and foreign exchange movements.

Exhibit 1: AUME changes							
Year-end March	Q220	Q420	Q121	Q221	Q121	Q221	H121
\$bn	AUME			Net flows			
Dynamic hedging	3.2	2.5	2.9	3.2	0.1	0.4	0.5
Passive hedging	50.4	50.3	53.9	55.6	(0.6)	(0.2)	(0.8)
Currency for return	2.9	2.6	3.1	3.4	0.0	0.0	0.0
Multi-product	3.1	3.0	3.2	3.5	0.0	0.0	0.0
Cash and futures	0.3	0.2	0.2	0.2	0.0	0.0	0.0
<b>Total</b>	<b>59.9</b>	<b>58.6</b>	<b>63.3</b>	<b>65.9</b>	<b>(0.5)</b>	<b>0.2</b>	<b>(0.3)</b>
Markets					3.6	0.5	4.1
FX and scaling for mandate volatility targeting					1.6	1.9	3.5
<b>Total change</b>					<b>4.7</b>	<b>2.6</b>	<b>7.3</b>

Source: Record

Q221 investment performance was negative. The Dynamic Macro Currency strategy, which had performed very strongly in the January-March period (+6.92%) and then surrendered some of its gains in April-June as markets bounced (-3.39%), saw more modest erosion in the latest quarter (-0.41%). The more systematic return-seeking strategies were also negative in the quarter and as a result the Multi-Strategy product was down 2.20% in the quarter (but still showing a positive return since inception of 0.33% per annum).

## Estimate changes

Changes in key figures from our estimates are shown in Exhibit 2. The main driver of the changes is the increase in AUME highlighted earlier. Importantly, no additional investment in personnel or systems are required to service the new dynamic hedging mandate and this contributes to the substantial increase in our FY22 earnings estimate. We have assumed the \$8bn is included progressively in AUME over three quarters. The fee rate is consistent with Record's other dynamic hedging mandates, based on the size of allocation. We therefore expect the average fee rate, both for the mandate and for Dynamic hedging as a whole, to decrease as the mandate builds in size. Even so, the relatively high fee rate that applies to dynamic hedging compared with passive hedging, together with the assumption that the only marginal cost attached to the additional revenue is profit-related compensation (set at just over 30%), means there is a substantial impact on group profit as the mandate flows into AUME.

As noted earlier, there is also expected to be some dilution of average management fee in Passive hedging as a number of mandates have chosen to transfer from a management fee only basis to one with a lower management fee but with the potential for performance fees. Retaining these mandates on the alternative fee basis should help moderate the persistent pressure on passive hedging management fee rates, for a period.

No performance fees have been crystallised year to date, but, as a reminder, £2.3m was earned in FY19 and £1.8m in Q320. The £1.8m fee was equivalent to 0.4bp of the average trailing 12-month AUME at that point, which is material when compared with the group average management fee of 4.9bp for FY20. Our estimates do not include any assumed performance fees. By their nature, the timing of performance fees is intermittent and their level uncertain.

On a longer view, performance fees are likely to be a recurring feature for Record enhancing both earnings and dividend payments when they arise. New product introductions could help boost AUME, increase average fee rates in some cases and broaden diversification. IT modernisation has the potential both to enable competitive product offerings and to enhance the degree of operational gearing further as Record increases its focus on growth.

#### Exhibit 2: Estimate changes

	Revenue (£m)			PBT (£m)			EPS (p)			DPS (p)*		
	Old	New	Change	Old	New	Change	Old	New	Change	Old	New	Change
03/21e	23.7	24.9	5%	5.7	6.5	13%	2.37	2.68	13%	2.30	2.30	0%
03/22e	24.0	28.7	20%	5.6	8.9	57%	2.33	3.65	57%	2.30	2.30	0%

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

Our dividend estimates shown above exclude special dividends. The board's policy is to target a dividend at least covered by earnings and to take into account expected increases in costs and regulatory capital requirements. Given the cost and regulatory capital point we do not expect a special payment for FY21, subject to further estimate changes. In view of the increase in AUME a maintained ordinary dividend may still be a plausible assumption for this year. In light of our FY22 earnings estimate (3.65p) we would pencil in a special payment of 0.70p giving a total dividend of 3.0p.

For more detail on our estimates, see Exhibit 4.

## Valuation

An updated version of our comparative valuation table, which puts Record in the context of a group of UK asset managers, is shown in Exhibit 3. 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 3: Comparing valuation with UK fund managers

	Price (p)	Market cap (£m)	P/E 2020e (x)	EV/EBITDA 2020e (x)	Dividend yield (%)
Ashmore	384	2,738	15.4	9.6	4.4
City of London Investment Group	400	203	11.1	N/A	7.5
Impax Asset Management	540	704	36.9	27.7	1.0
Jupiter	232	1,283	10.9	6.3	7.4
Liontrust	1,280	780	20.5	14.6	2.6
Man Group	118	2,245	12.9	8.5	6.9
Polar Capital	524	516	11.8	7.3	6.3
Schroders	2,836	7,484	16.1	11.1	4.0
<b>Average</b>			<b>16.9</b>	<b>12.1</b>	<b>5.0</b>
<b>Record</b>	<b>43.0</b>	<b>85</b>	<b>15.2</b>	<b>10.6</b>	<b>5.3</b>

Source: Refinitiv, Edison Investment Research. Note: P/E and EV/EBITDA on a calendar-year basis. Record's dividend yield excludes the special dividend. Priced at 21 October 2020.

Our table shows calendarised figures for 2020 P/E and EV/EBITDA. Record shares trade on below the peer averages for both measures. The earnings and EBITDA for calendar year 2020 benefit from a quarter of the performance fee earned in FY20 although, more significantly, the three quarters contribution from FY21 only includes a partial benefit from the new dynamic hedging mandate. The dividend yield of 5.3% is slightly above the peer average and there is the potential for this to be enhanced with a special dividend in due course (on our estimate the FY22 yield would be 7.0%).

**Exhibit 4: Financial summary**

£000s	2018	2019	2020	2021e	2022e
<b>March</b>					
<b>PROFIT &amp; LOSS</b>					
Revenue	23,834	24,973	25,563	24,915	28,745
Operating expenses	(16,735)	(17,089)	(17,996)	(18,523)	(19,981)
Other income/(expense)	173	(8)	82	0	0
Operating Profit (before amort. and except.)	7,272	7,876	7,649	6,392	8,764
Finance income	56	113	88	86	86
Profit Before Tax	7,328	7,989	7,737	6,477	8,850
Taxation	(1,182)	(1,559)	(1,365)	(1,231)	(1,682)
Minority interests	0	0	48	40	30
Attributable profit	6,146	6,430	6,420	5,287	7,199
Revenue/AuME (excl. perf fees) bps	5.1	4.9	4.9	4.3	4.9
Operating margin (%)	30.5	31.5	29.9	25.7	30.5
Average Number of Shares Outstanding (m)	206.5	198.1	197.1	197.1	197.1
Basic EPS (p)	3.03	3.27	3.26	2.69	3.66
EPS - diluted (p)	2.98	3.25	3.26	2.68	3.65
Dividend per share (p)	2.30	2.30	2.30	2.30	2.30
Special dividend per share (p)	0.50	0.69	0.41	0.00	0.70
Total dividend (p)	2.80	2.99	2.71	2.30	3.00
<b>BALANCE SHEET</b>					
Non-current assets	2,339	2,161	4,868	4,288	3,698
Intangible Assets	228	288	470	475	475
Tangible Assets	910	761	751	616	476
Investments	1,115	1,112	2,472	2,472	2,472
Other	86	0	1,175	725	275
Current Assets	29,737	31,427	31,149	30,888	33,961
Debtors	6,775	7,562	8,704	8,001	8,991
Cash	12,498	12,966	14,294	14,736	16,819
Money market instruments	10,198	10,735	7,958	7,958	7,958
Other	266	164	193	193	193
Current liabilities	(5,525)	(6,158)	(6,955)	(6,712)	(6,604)
Creditors	(2,630)	(2,736)	(3,009)	(2,766)	(3,108)
Financial liabilities	(2,467)	(2,621)	(2,191)	(2,191)	(2,191)
Other	(428)	(801)	(1,755)	(1,755)	(1,305)
Non-current liabilities	0	(29)	(901)	(451)	(451)
Net Assets	26,551	27,401	28,161	28,013	30,604
Minority interests	0	60	132	92	62
Net assets attributable to ordinary shareholders	26,551	27,341	28,029	27,921	30,542
No of shares at year end	199.1	199.1	199.1	199.1	199.1
NAV per share p	13.3	13.7	14.1	14.0	15.3
<b>CASH FLOW</b>					
Operating Cash Flow	2,746	7,026	6,543	6,491	7,315
Capex	(236)	(72)	(243)	(140)	(140)
Cash flow from other investing activities	7,899	(561)	1,513	(64)	(64)
Dividends	(6,810)	(5,517)	(5,888)	(5,394)	(4,578)
Other financing activities	(10,367)	(613)	(943)	(450)	(450)
Other	146	205	346	0	0
Net Cash Flow	(6,622)	468	1,328	442	2,083
Opening cash/(net debt)	19,120	12,498	12,966	14,294	14,736
Closing net (debt)/cash	12,498	12,966	14,294	14,736	16,819
Closing net (debt)/cash inc money market instruments	22,696	23,701	22,252	22,694	24,777
<b>AUME</b>					
Opening (\$'bn)	58.2	62.2	57.3	58.6	71.4
Net new money flows	(1.2)	(4.5)	4.6	5.0	2.7
Market/other	5.2	(0.4)	(3.3)	7.8	0.4
Closing (\$'bn)	62.2	57.3	58.6	71.4	74.4

Source: Record accounts, Edison Investment Research

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