



26 April 2021

Financial Services



Source: Refinitiv

Market data

EPIC/TKR	CLIG
Price (p)	540.0
12m High (p)	556.0
12m Low (p)	390.0
Shares (m)	50.7
Mkt Cap (£m)	273.7
EV (£m)	256.1
Country of listing	UK
Market	LSE

Description

City of London is an investment manager, primarily using closed-ended funds to invest in emerging and other markets.

Company information

CEO	Tom Griffith
CFO	Deepranjan Agrawal
Chairman	Barry Aling
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	www.clig.com

Key shareholders

George Karpus	31.5%
Hargreaves Lansdown	6.3%
Aberforth Partners	5.1%
Interactive Investor	3.6%
Barry Olliff	2.5%
Directors & staff	11.9%

Diary

30 June	Year-end
13 July	Pre-close trading update

Analyst

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CITY OF LONDON INVESTMENT GROUP

Another quarter of steady progress

City of London has announced its trading update for 3Q'21. It has been a quarter of steady progress. Markets were supportive, albeit to a lesser degree than in the previous couple of quarters, with the MSCI EM Net TR Index increasing 2.3% and the MSCI ACWI ex US up 3.5%. Performance was also strong across all product areas, driven by good NAV performance, and partially offset by net outflows across each area. FUM increased in all strategies other than Opportunistic Value and total FUM ticked up from \$10.98bn to \$11.06bn. City of London retains an active pipeline across all areas.

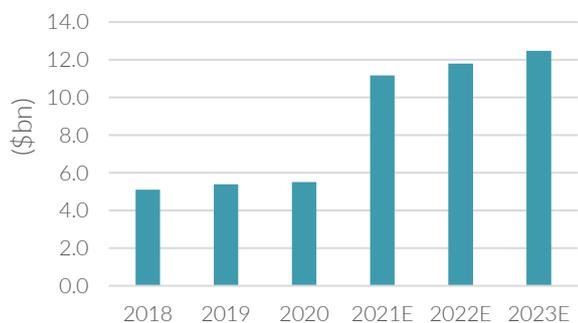
- **Operations:** Revenue rates and expenses remain in line with the previous figures, giving a monthly run-rate for operating profit, pre profit share, of £3.3m. Progress has also been made in harmonising the financial and IT infrastructure in CLIM and KIM.
- **Estimates:** With financial progress largely in line with our expectations, we have only made small changes to our earnings estimates. The net outflows and exchange rate movements have led to small downgrades, with our 2021E EPS reduced by 0.6%, our 2022E EPS by 1.6% and 2023E EPS decreased by 1.5%.
- **Valuation:** Despite the recent good performance, the 2022E P/E of 13.1x remains at a discount to the peer group. The 2022E yield of 6.7% is attractive, in our view, and should, at the very least, provide support for the shares in the current markets.
- **Risks:** Although City of London has reduced its relative emerging markets exposure, it is still 47% of assets. It has proved to be more robust than some other fund managers, aided by its good performance and strong client servicing. Market volatility remains a risk, although increasing diversification is also mitigating this.
- **Investment summary:** Having shown robust performance in challenging market conditions, City of London is now reaping the benefits in a more supportive environment. The valuation remains reasonable. After a special dividend in FY'19, a dividend increase in FY'20, and with the EPS boost from Karpus in 2021, the prospects for future dividend increases look very good.

Financial summary and valuation

Year-end Jun (£m)	2018	2019*	2020	2021E	2022E	2023E
FUM (\$bn)	5.11	5.39	5.50	11.18	11.80	12.48
Revenue	33.93	31.93	33.26	54.21	64.01	67.39
Statutory PTP	12.79	11.40	9.41	21.69	28.14	30.26
Statutory EPS (p)	39.5	34.9	30.3	36.1	41.2	44.5
Underlying EPS (p)	39.5	34.9	38.0	46.8	50.0	53.3
DPS (p)	27.0	27.0	30.0	33.0	36.0	39.0
Special dividend (p)		13.5				
P/E (x)	13.7	15.5	17.8	14.9	13.1	12.1
Dividend yield	5.0%	7.5%	5.6%	6.1%	6.7%	7.2%

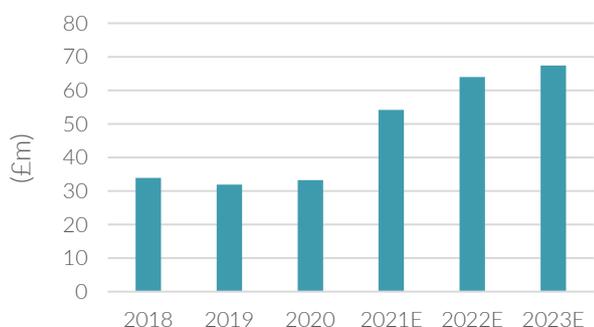
*2019 figures include a special dividend of 13.5p; Source: Hardman & Co Research

Funds under management (FUM)



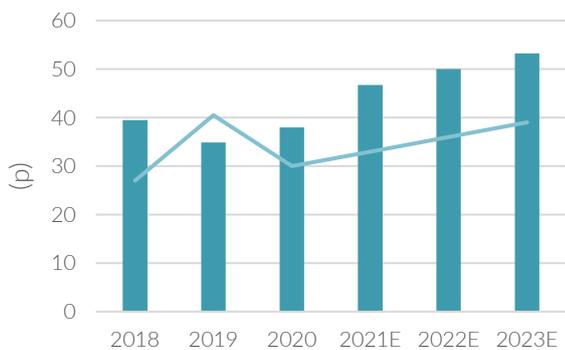
- ▶ Net inflows since 2014
- ▶ Addition of Karpus in 2021 added \$3.58bn
- ▶ Market recovery since spring 2020 has more than offset sharp market fall
- ▶ Assumed steady new business flows and equity market growth of 5% p.a.

Revenue



- ▶ Revenue linked strongly to FUM
- ▶ Ongoing slow decrease in revenue margins from new business
- ▶ Karpus's revenue margin higher than City of London's
- ▶ 2020 growth affected by volatile markets

Underlying EPS (bar) and DPS (line)



- ▶ Profitability historically maintained by cost flexibility
- ▶ Exceptional transaction costs reduce statutory 2020 and 2021E EPS
- ▶ Special dividend of 13.5p in 2019
- ▶ Dividend increased in 2020 and for 2021 interim; we believe our forecasts for 2022 and 2023 are conservative

Source: Company data, Hardman & Co Research

Commentary

Funds

Funds under management (FUM)				
(\$m)	Mar'21	Dec'20	Net flows	Other movements
Emerging Markets	5,250	5,196	-127	181
International	1,734	1,700	-57	91
Opportunistic Value	233	306	-85	12
Other/REIT	25	27	-2	0
CLIM total	7,242	7,229	-271	284
KIM total	3,815	3,749	-7	73
Total	11,057	10,936	-278	357

Source: Hardman & Co Research

While market movements this quarter were less dramatic than we saw in 2020, they still brought a positive contribution to FUM, which was augmented across the board by strong investment performance. City of London attributes most of the outperformance to good NAV performance.

This was offset by net outflows in all strategies, which City of London attributes mostly to rebalancing. Given the strong equity market performance since last spring, this shouldn't be a surprise. Opportunistic Value did see a client loss due to a consultant change.

The only news on new business is that there is an active pipeline across all of its major products.

CLIG FUM progress since FY'18



Source: Company data, Hardman & Co Research
Step change at Sep'20 due to Karpus transaction

Operations

The operational figures are exactly in line with historical figures and our forecasts. There is no change to revenue rates, which continues at 73bps for CLIM and 77bps for KIM. The run-rate for monthly operating profit, pre profit share, is currently £3.3m.

City of London has made progress in bringing together the finance and IT infrastructure of CLIM and KIM. While not expected to bring any cost benefits, this is an important step in integrating the two companies.

Dividends

Earlier in April, City of London intimated that it had a technical infringement of the dividend rules. While it has always had adequate consolidated reserves at a group level to pay dividends as required, these had not always been paid upwards from the operating subsidiaries at the right time. Although technically there could be claims against shareholders and directors at the time of these distributions, in practice, the payments were as intended and agreed.

There will be a general meeting to remediate the position. This will have no effect on any dividends paid, but will put all parties back to the position had the technical requirements been fulfilled at the time.

Estimate updates

With the statement largely being in line with our expectations, there are only small adjustments to our forecasts. Unfortunately, the outflows were stronger than expected and there has been a further weakening of the US dollar relative to sterling, which has led to slight downgrades. Our 2021E EPS decreases 0.6%, from 47.1p to 46.8p. The 2022E EPS is reduced by 1.6% to 50.0p and the 2023E EPS by 1.5% to 53.3p.

Financials

Summary financials						
Year-end Jun	2018	2019*	2020	2021E	2022E	2023E
FUM (\$bn)	5.11	5.39	5.50	11.18	11.80	12.48
P&L (£m)						
Revenue	33.93	31.93	33.26	54.21	64.01	67.39
Expenses	21.40	21.43	21.66	31.19	35.89	37.14
Operating profit	12.53	10.50	11.60	23.02	28.12	30.24
Statutory PTP	12.79	11.40	9.41	21.69	28.14	30.26
Earnings	10.06	9.05	7.37	15.62	20.34	21.96
Statutory EPS (p)	39.5	34.9	30.3	36.1	41.2	44.5
Underlying EPS (p)	39.5	34.9	38.0	46.8	50.0	53.3
DPS (p)	27.0	40.5	30.0	33.0	36.0	39.0
Key metrics						
	2018	2019*	2020	2021E	2022E	2023E
Growth (%)						
FUM		5.5	2.1	103.1	5.6	5.8
Revenue		-5.9	4.2	63.0	18.1	5.3
Operating profit		-16.2	10.4	98.5	22.1	7.6
Underlying EPS		-11.6	8.9	23.0	6.9	6.5
DPS (excl. special div.)		0.0	11.1	10.0	9.1	8.3
Operating margins (%)						
Net FUM fee margin	0.80	0.76	0.75	0.75	0.75	0.74
Operating margin	36.9	32.9	34.9	42.5	43.9	44.9
Tax rate	21.4	20.6	21.7	23.0	24.0	24.0
Dividend cover (x, excl. special div.)	1.5	0.9	1.0	1.1	1.1	1.1
Rolling 5-year cover (x, excl. special div.)	1.2	1.3	1.2	1.3	1.2	1.1
Rolling u/l 5-year cover (x, excl. special div.)			1.2	1.3	1.3	1.3
Underlying EPS sensitivity						
				2021E	2022E	2023E
No net new business						
EPS (p)				46.7	49.6	52.0
change				0.0%	-0.7%	-2.3%
0% market growth (was 5% p.a.)						
EPS (p)				46.7	47.9	48.3
change				-0.2%	-4.1%	-9.3%

*2019 figures include a special dividend of 13.5p; Source: Company data, Hardman & Co Research
£1=\$1.38

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