

Source: Eikon Thomson Reuters

Market data

EPIC/TKR	CLIG
Price (p)	420.5
12m High (p)	420.5
12m Low (p)	318.5
Shares (m)	26.9
Mkt Cap (£m)	113.2
EV (£m)	102.7
Market	LSE

Description

City of London is an investment manager specializing in using closed end funds to invest in emerging markets.

Company information

CEO	Barry Olliff
CFO	Tracy Rodrigues
Chairman	David Cardale

www.citlon.com

Key shareholders

Directors & staff	20.3%
Blackrock	10.0%
Hargreave Hale	4.9%
Polar Capital	3.3%
Slater Investments	3.0%

Next event

18 Sep 2017	Preliminary results
9 Oct 2017	Q1 trading update
12 Oct 2017	Ex-div date
23 Oct 2017	AGM

Analysts

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City of London Investment Group**Good yield getting better**

City of London has announced a trading statement for FY 2017. Over the year, funds under management grew to \$4.7bn, a 17% increase over a year ago. This lagged the increase in the MSCI Emerging Markets TR Index of 24%. Fund performance was generally good, with only the Frontier assets lagging the benchmark. As indicated in earlier statements, the slower growth in assets was due to redemptions with net outflows over the year of \$306m in Emerging Market, offset slightly by net inflows of c\$26m into Diversification strategies.

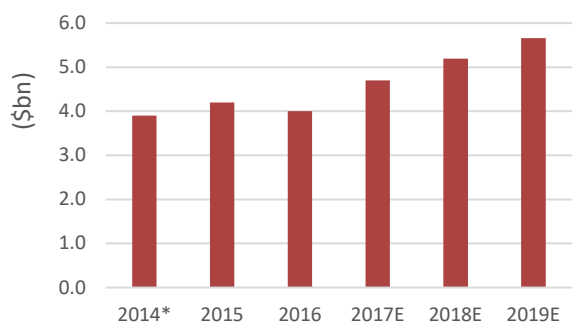
- ▶ **Profits:** City of London expects that pre-tax profits for the year will be £11.6m. Profit after tax will be approximately £9.1m, with the tax paid being reduced by a one-off refund of prior years' US state taxes of £0.4m. Basic eps will be 36.9p and the diluted figure is 36.7p.
- ▶ **Dividend:** The biggest news for many investors will be the increase in the dividend. As per our forecasts, the final dividend has been increased by 1p to 17p, giving a full year total of 25p: this is the first increase since 2012. Cover for the year is a very healthy 1.46 times.
- ▶ **Valuation:** The prospective 2018 P/E of 10.3 times is at a significant discount to the peer group. The current yield of 5.9% is very attractive and should at the very least provide support for the shares in the current volatile markets.
- ▶ **Risks:** Although Emerging Markets can be volatile, City of London has proved to be more robust than some other emerging market fund managers, aided by its good performance and strong client servicing. Further EM volatility may increase the risk of such outflows however.
- ▶ **Investment summary:** Having shown a robust performance in challenging market conditions, City of London is now reaping the benefits in a more supportive environment. The valuation remains reasonable. With dividend cover having returned to a comfortable position, investors can start thinking about future increases.

Financial summary and valuation

Year end Jun (£m)	2014*	2015	2016	2017A/E	2018E	2019E
FUM (\$bn)	3.90	4.20	4.00	4.70	5.19	5.66
Revenue (£m)	24.22	25.36	24.41	31.37	34.14	34.79
Statutory PTP	7.24	8.93	7.97	11.60	13.24	13.62
Statutory EPS (p)	20.7	26.4	23.3	36.9	41.0	42.2
Dividend (p)	24.0	24.0	24.0	25.0	26.0	27.0
P/E (x)	20.3	15.9	18.0	11.4	10.3	10.0
Yield	5.7%	5.7%	5.7%	5.9%	6.2%	6.4%

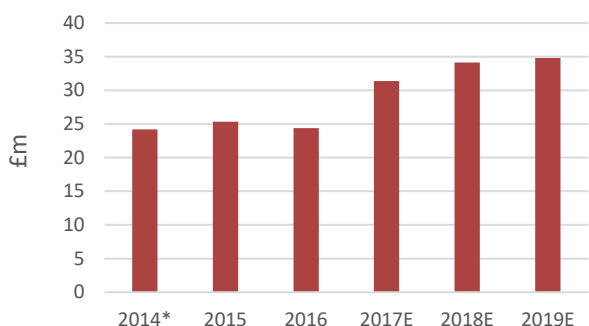
Source: Hardman & Co Research
 * 2014 had 13 months in financial year.

Funds under Management



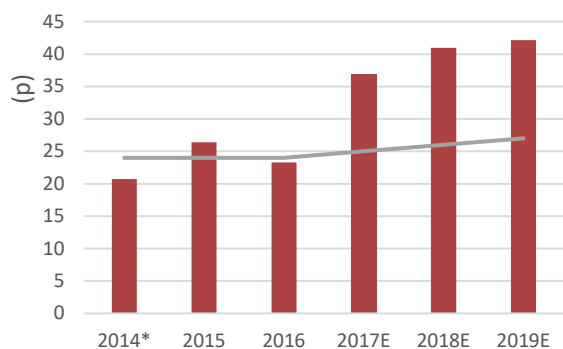
- ▶ Net inflows from 2014
- ▶ Market weakness in 2016 substantially offset by new business flows
- ▶ Assumed steady new business flows and market growth of 5% pa in 2018 and 2019

Revenues



- ▶ Revenues strongly linked to FUM
- ▶ Slight decrease in revenue margins from new business
- ▶ Some currency effects, particularly from strong US Dollar from 2015 to 2017

eps (bar) and dividend (line)



- ▶ Profitability historically maintained by cost flexibility
- ▶ Currency movements lead to step change in 2017
- ▶ Dividend shortfall in 2014 and 2016 covered from reserves
- ▶ Dividend increased in 2017 with cover of 1.46 and we expect steady increases over the next couple of years

Commentary

The pre-tax profit estimate is slightly behind our estimate of £11.8m, with outflows being slightly more than anticipated and expenses being a little higher. City of London's explanation of a rebalancing of gains is understandable given that fund performance for the year has been good and Emerging Markets are also performing well. With all that, we would have expected the asset class to start attracting new money, and are pleased to note that c\$125m of new money has been confirmed for this financial year.

The higher expenses are largely attributed to the fall in sterling vs the US dollar.

The comment about fund performance for the whole year being positive in most asset classes is reassuring, given that the second quarter was clearly tough for the group. Clearly, the second half of the FY has seen a very good performance.

Estimate Updates

The main effect on our estimate updates comes from FUM being higher than we had forecast, with an offset from the movements in exchange rates. The net result is a small upgrade to our earning estimates. Our eps estimates are increased by 3% to 41.0p for 2018E and 42.2p for 2019E.

The dividend increase of 1p matched our estimates. Although dividend cover at 1.46 times is higher than the rolling target of 1.2 times, the lower cover for the last few years meant that any increase was likely to be limited. We have continued to forecast a 1p increase for each of the next two years. If the financial position remains as strong as we expect then a larger increase in 2019 may be possible.

Share sales

As previously indicated, during Q4 the CEO, Barry Olliff, sold 500,000 shares at 400p. He has updated his statement of intentions and will now sell 250,000 shares at incremental price increases of 25p - i.e. he will sell 250,000 at 425p, another 250,000 at 450p. This is part of a plan to reduce his shareholding in an ordered manner as he heads towards retirement.

Financials

Summary Financials						
	2014*	June Year End			2018E	2019E
	2014*	2015	2016	2017A/E	2018E	2019E
FUM (\$bn)	3.90	4.20	4.00	4.70	5.19	5.66
P&L (£m)						
Revenue	24.22	25.36	24.41	31.37	34.14	34.79
Expenses	17.22	16.63	16.66	19.77	20.93	21.20
Operating Profit	7.00	8.73	7.76	11.60	13.21	13.59
PBT	7.24	8.93	7.97	11.60	13.24	13.62
Earnings	5.20	6.61	5.85	9.10	10.20	10.49
eps (p)	20.7	26.4	23.3	36.9	41.0	42.2
dps (p)	24.0	24.0	24.0	25.0	26.0	27.0
Key Metrics						
	2014*	2015	2016	2017A/E	2018E	2019E
Growth (%)						
FUM		7.7	-4.8	17.5	10.5	9.0
Revenue		4.7	-3.7	28.5	8.8	1.9
Operating Profit		24.7	-11.1	49.5	13.9	2.9
EPS		27.5	-11.7	58.4	11.1	2.9
DPS		0.0	0.0	4.2	4.0	3.8
Operating Margins (%)						
Net FUM fee margin	0.88	0.86	0.86	0.85	0.83	0.83
Operating Margin	28.9	34.4	31.8	37.0	38.7	39.1
Tax Rate	28.2	26.0	26.5	26.0	26.0	26.0
Dividend cover	0.9	1.1	1.0	1.5	1.6	1.6
eps Sensitivity						
					2018E	2019E
No net new business						
eps (p)					39.5	40.0
% change					-3.5	-5.0
0% market growth (was 5% pa)						
eps (p)					39.4	39.8
% change					-3.8	-5.6

Source: City of London Investment Group, Hardman & Co Research
* 13-month year as year end change.

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(Disclaimer Version 2 – Effective from August 2015)

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