Numis Corporation

H120 results

Busy and adapting to new circumstances

Financial services

Numis has adapted well to the rapid change in operating requirements, substantial market volatility and changes in the nature of its transaction pipeline. The near-term trading environment seems positive in the circumstances with recapitalisation fund-raisings for clients and good levels of institutional activity buoying performance. The outlook beyond this is less clear but the strength of the Numis franchise and balance sheet is encouraging for the longer term.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/17	130.1	38.3	25.9	12.0	10.8	4.3
09/18	136.0	31.6	23.0	12.0	12.2	4.3
09/19	111.6	12.4	8.1	12.0	34.5	4.3
09/20 mid-scenario**	125.3	16.9	12.0	12.0	23.4	4.3

Note: *PBT and EPS are on a reported basis and EPS is fully diluted. **Figures shown are for a mid-point in a range of scenarios: see Exhibit 7

H120 results: Equities strength drives revenue

H120 revenue was 13% up y-o-y to £63.1m, slightly ahead of the c 10% indicated in the March period-end trading update. The Investment Banking business had a limited window for activity following the general election and before the onset of COVID-19. As a result its revenues were down 5%. In contrast the Equities business recorded revenues up 55% within which Institutional revenue was up 19% and profitability on the trading book was strong compared with a weak H119 (£6.5m against £0.4m). There was a 13% or £1.9m write-down on the investment portfolio. This, with somewhat higher costs than we had allowed (the compensation ratio was 58.6% versus 54.2% for H119 and 57.8%, FY19), left pre-tax profit at £7.3m versus £7.1m for H119. Basic EPS was 6.0p versus 5.4p. The interim dividend is maintained at 5.5p reflecting a commitment to a stable dividend. The balance sheet remains strong with cash up from £84.2m at the year end to £95.3m and a significant excess of capital for regulatory purposes.

Background and outlook

Given the uncertainty created by the pandemic we continue to set out illustrative scenarios for FY20 revenues, profits and earnings per share rather than a point estimate. On the equities side of the business, trading volumes remain at a high level but there could be a quiet period following the currently elevated volatility. Similarly, investment banking is currently trading well but could suffer a pause at some point between recapitalisation activity and a revival in other types of corporate transaction.

Valuation

The shares trade on a book multiple of over 2x which, on our ROE/COE model, would be consistent with an assumed sustainable return on equity (ROE) of 17%. This therefore appears to discount part of a potential profit recovery but can be viewed in the context of a five-year historical average ROE of 18% and the investment in staff undertaken in 2018 to underpin future growth.

15 May 2020

Price	**280p**
Market cap	**£297m**

Net cash end March 2020 (£m)	95.3
Shares in issue	106.3m
Free float	75%
Code	NUM
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	10	(3.5)	5.0
Rel (local)	11.6	26.5	32.2
52-week high/low		306p	167p

Business description

Numis Corporation is one of the UK's leading independent investment banking groups, offering a full range of research, execution, equity capital markets, corporate broking and advisory services. It employs c 285 staff in offices in London and New York, and at the end of March 2019 had 209 corporate clients.

Next events

FY20 trading update	September 2020

Analysts

Andrew Mitchell +44 (0)20 3681 2500

Martyn King +44 (0)20 3077 5745

financials@edisongroup.com

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H120 results

An analysis of the profit and loss figures for the last three half year periods is given in Exhibit 1. Key points from the H120 results included the following, with changes against H119 unless stated:

- Overall **revenue** increased by 13%, within which Investment banking was down 5%, the result of a relatively difficult background for both capital markets and advisory activities where IPOs, M&A and other corporate transactions were muted. Corporate retainers, a more stable source of revenue, were up even though the number of corporate clients fell (209 versus 214) reflecting normal attrition and Numis proactively rotating the client base towards companies expected to be active (the average market capitalisation of new clients was five times that of those lost). Within Equities the change in profitability was accentuated by the £3m loss incurred in relation to the Kier rights issue in H119. Institutional income benefited from increased activity following the general election and recent market volatility.
- Total administrative **costs** increased by 14% including a 23% increase in staff costs driven primarily by variable compensation and there was a small reduction in other costs. The compensation/revenue ratio was 58.6% versus 54.2% (and 57.8% FY19) and remains within the target range of 50–60%.
- Operating profit before other operating income was up 12% to £9.1m with the margin nearly maintained at 14.5%.
- There was a 13% or £1.9m write-down, shown as other operating income, on the (mainly private) **investment portfolio** leaving its value at £13m.
- After this write-down **pre-tax profit** was up 2% at £7.3m and diluted **EPS**, after a lower tax charge, increased 11% to 5.5p.
- The group maintained its commitment to a stable **dividend** across market cycles, announcing an unchanged interim payment of 5.5p.

Exhibit 1: P&L analysis

Year-end September (£m unless stated)	H119	H219	H120	Change H120/H119 (%)
Net trading gains	0.4	3.6	6.5	N/A
Institutional income	16.5	16.8	19.7	19.2
Equities	**16.9**	**20.5**	**26.2**	**55.5**
Corporate retainers	6.4	6.9	6.8	6.0
Advisory	7.5	5.0	7.2	(4.2)
Capital markets	24.9	23.5	22.8	(8.1)
Investment banking	**38.8**	**35.5**	**36.9**	**(5.0)**
Total revenue	**55.7**	**55.9**	**63.1**	**13.3**
Other operating income	(1.4)	(0.8)	(1.9)	33.3
Total income	**54.3**	**55.1**	**61.2**	**12.8**
Staff costs	(30.2)	(34.3)	(37.0)	22.5
Non-staff costs	(17.4)	(15.6)	(17.0)	(2.3)
Total administrative expenses	**(47.6)**	**(49.9)**	**(54.0)**	**13.5**
Operating profit / loss	**6.7**	**5.2**	**7.2**	**8.0**
Finance income/expense	0.4	0.1	0.0	(92.8)
Pre-tax profit	**7.1**	**5.3**	**7.3**	**2.1**
Tax	(1.4)	(1.7)	(1.0)	(28.2)
Effective tax rate (%)	19.6	32.2	13.8	
Attributable profit	**5.7**	**3.6**	**6.3**	**9.5**
Diluted EPS (p)	5.0	3.1	5.5	11.2
Dividend (p)	5.5	6.5	5.5	0.0
Operating profit before other income	8.1	6.0	9.1	12.4
Operating margin before other income (%)	14.6	10.7	14.5	

Source: Numis, Edison Investment Research

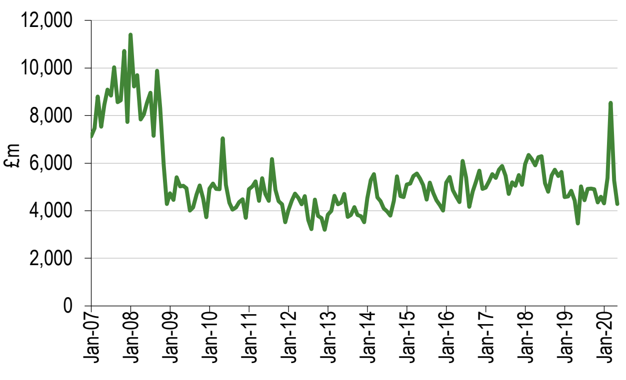
The end-March headcount was modestly higher at 285 (+2% y-o-y) with hiring focused on junior investment banking staff, we assume to support key hires made as part of Numis's earlier investment in staff. Remote working has not disrupted the business and the company has not furloughed staff or accessed any government support schemes.

Background and outlook

We start with charts showing the level of London Stock Exchange trading activity and UK equity indices. Exhibit 2 shows that trading activity rose to levels seen in the global financial crisis, as the impact of the pandemic began to become evident, but has subsequently subsided. Given the uncertainty over how the epidemic and its economic ramifications will develop, further periods of elevated volatility and activity are possible.

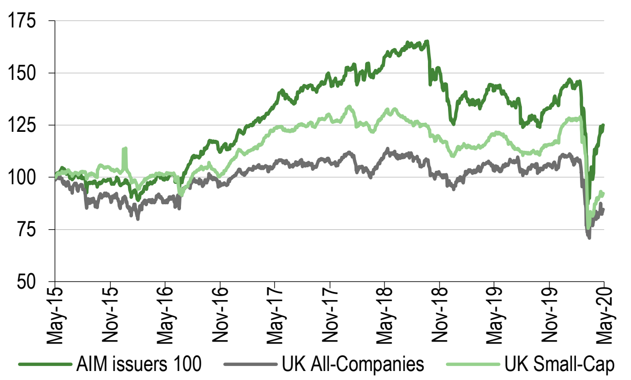
Exhibit 3 records the dramatic fall and bounce back in UK equity indices that has been seen in recent weeks. On a five-year view, AIM issuers (CBOE Alternative UK 100) and All-Companies indices are down c 22% from their peak levels, while the CBOE Small Companies index is down 28%.

Exhibit 2: LSE order book, average daily value traded



Source: London Stock Exchange (Main Market)

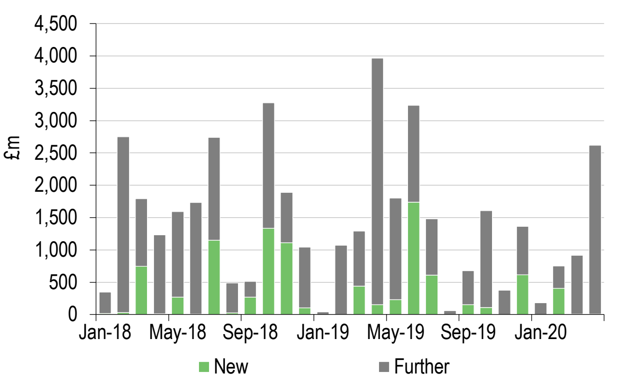
Exhibit 3: UK equity indices



Source: Refinitiv, CBOE indices

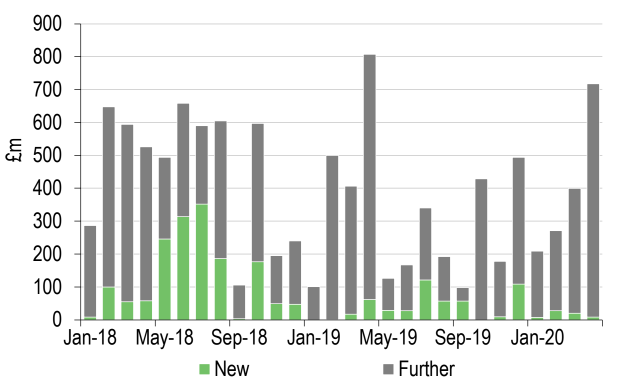
The next two charts look at trends in equity issuance on the London Stock Exchange Main and AIM markets. Money raised was relatively subdued last year, particularly on AIM. Both markets have seen a marked increase in further issuance in March and April as companies have issued equity to recapitalise their balance sheets in order to be able to deal with the consequences of the pandemic.

Exhibit 4: Main Market money raised, new and further



Source: London Stock Exchange

Exhibit 5: AIM money raised, new and further



Source: London Stock Exchange

Such recapitalisations are a continuing feature of the equity market and Numis investment banking staff are fully occupied in providing clients with advice and executing transactions. Exhibit 6 shows the fund-raising transactions the company has been involved in since the end of H120.

Exhibit 6: Fund-raising transactions since end March

Company	Date	Numis's role	Transaction	Money raised (£m)
Asos	14-Apr	Joint global coordinator	Placing	247
Abcam	17-Apr	Joint corporate broker	Placing	110
The Gym Group	21-Apr	Joint book runner	Placing	41
Foxtons	22-Apr	Sole book runner	Placing	22
Hyve	07-May	Sponsor, Financial Adviser, Corporate Broker, Joint Global Coordinator, Joint Bookrunner & Joint Underwriter	Rights issue	127
Polypipe	12-May	Joint global coordinator and joint corporate broker	Placing	120
Keywords Studios	14-May	Financial Adviser, NOMAD, Broker, Joint Bookrunner	Placing	100
Scapa	14-May	Nominated Adviser, Joint Bookrunner and Joint Broker	Placing	33

Source: London Stock Exchange, Numis, Edison Investment Research

Management indicates these transactions and maintained average deal fees have contributed to an improvement in the performance of the investment banking business since the half year end. Numis also reports that the pipeline of recapitalisation transactions has continued to grow, which has partly offset a decline in M&A, private transaction and IPO opportunities where the outlook is described as challenging. This switch in emphasis within investment banking seems likely to persist for the balance of the financial year given the difficult economic background that is unfolding. The equities activities have seen a continued strong performance into the second half with institutional activity remaining at a higher level and trading seeing profitability maintained despite a reduction in trading book positions to contain risk.

As we note earlier, there could be a pause in both equities and investment banking businesses between the current phase of activity and the resumption of a more normal period of transactions as the crisis eases. Nevertheless, the strength of the Numis franchise and its balance sheet position mean that it should be well-placed to navigate such market fluctuations and take advantage of new opportunities as they emerge.

Financials

In line with our previous note in April, we are showing a range of potential outcomes in place of a point forecast for FY20. Our scenario analysis is set out in Exhibit 7. Compared with our previous scenarios the main change is the inclusion of the £1.9m write-down on the investment portfolio reported in the first half, which results in lower profit and earnings outcomes in each scenario.

Exhibit 7: Illustrative scenario analysis for FY20

£m unless stated	Lower	Mid	Higher
Revenue	109.0	125.3	135.0
Other operating income (investment portfolio)	-1.9	-1.9	-1.9
Total income	**107.1**	**123.4**	**133.1**
Non staff costs	(34.0)	(34.0)	(34.0)
Staff costs	(65.0)	(72.6)	(74.6)
Operating profit	**8.1**	**16.8**	**24.5**
Net finance income	0.1	0.1	0.1
Pre-tax profit	**8.2**	**16.9**	**24.6**
Tax	(1.6)	(3.2)	(4.7)
Net profit	**6.6**	**13.7**	**19.9**
EPS (p)	5.8	12.0	17.5
DPS (p)	12.0	12.0	12.0
Return on equity	5%	10%	14%
Total cost/revenue	91%	85%	80%
Total staff cost/revenue	60%	58%	55%

Source: Edison Investment Research

Further details of the middle scenario are shown in the financial summary (Exhibit 8).

The move to a new London office at 40 Gresham Street has been affected by COVID-19, which has delayed construction work. The lease had been expected to begin near the end of FY20 with relocation expected to take place in H221. The lease is now expected to begin in H121 but with relocation still taking place in H221. The 50,000 square foot office will be c 60% larger than the existing one, providing capacity for growth over the term of the 15-year lease. Including the effect of implementation of IFRS 16, Numis expects this will increase ongoing costs by approximately £3m per annum. In addition to this there will be fitout costs, which we estimate could be in the region of £7–9m (based on a Cushman and Wakefield cost report). These costs will be amortised over the lease term (c £0.6m pa) and in cash terms would be broadly balanced by the benefit of a three-year rent-free period (we estimate c £9m in total).

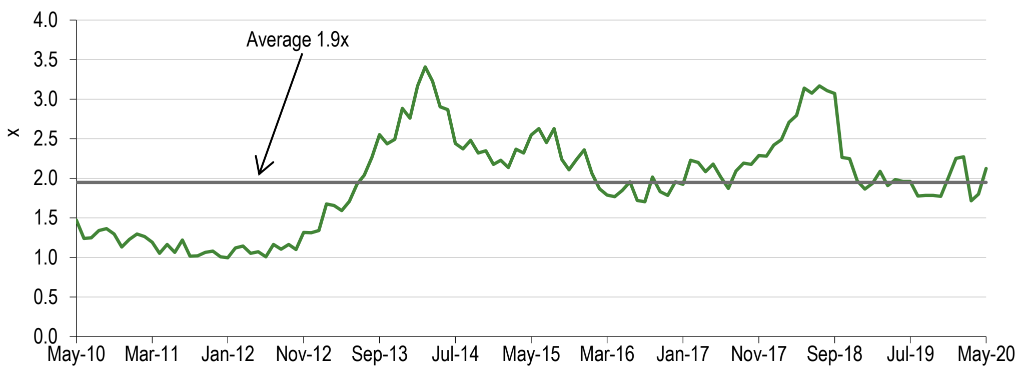
Numis remains financially strong with no debt drawn and end-March cash and cash equivalents of £95.3m compared with £84.2m at the September year end. The combination of cash and a rolling credit facility provides the group with committed liquidity of £130m available. The group also continues to have significant excess capital for regulatory purposes.

Looking at the half-year cash flow there was a net cash inflow from operations of £24m of which £13m was provided by a reduction in trading investments, while other working capital movements were broadly neutral with profit and non-cash accruals making up the balance. Share repurchases and the dividend payment absorbed just over £12m and, with other smaller items accounting for another £1m, in total there was a net cash inflow of £11m.

Valuation

With the substantial uncertainties surrounding estimates for both Numis and its peers we focus on price to book value as a valuation measure at this point. Exhibit 8 shows that this stands at 2.2x modestly above the 10-year average of 1.9x. This follows a sharp dip below the average when the share price fell with the equity market in the initial reaction as the scale of the pandemic began to become clear.

Exhibit 8: 10-year history of the price to book value ratio for Numis



Source: Refinitiv, Edison Investment Research

Using an ROE/COE valuation model to infer the ROE assumption required to match the 280p share price at time of writing gives a value of 17% (based on the H120 NAV of 129p and assuming a cost of equity of 10% and growth of 4%). Our scenarios show ROEs between 5% and 14% for FY20, but on a medium-term view, with a return to more favourable market conditions and as benefits from the investment in staff made in FY18 are realised, a return in line with or above the FY15–19 historical average of 18% still does not appear an unrealistic aspiration for subsequent years.

Exhibit 9: Financial summary

£'000s	2015	2016	2017	2018	2019	Mid scenario 2020e
Year end 30 September						
PROFIT & LOSS						
Revenue	97,985	112,335	130,095	136,047	111,610	125,291
Administrative expenses (excl. amortisation and depreciation)	(65,018)	(76,120)	(83,626)	(94,603)	(85,432)	(93,343)
Share based payment	(4,104)	(6,229)	(10,454)	(10,583)	(10,914)	(10,250)
EBITDA	28,863	29,986	36,015	30,861	15,264	21,698
Depreciation	(882)	(1,126)	(1,226)	(1,113)	(1,124)	(2,894)
Amortisation	(111)	(125)	(89)	(49)	(44)	(95)
Operating Profit	27,870	28,735	34,700	29,699	14,096	18,709
Net finance income	190	37	188	212	550	60
Other operating income	(1,978)	3,759	3,431	1,733	(2,210)	(1,904)
Profit before tax	26,082	32,531	38,319	31,644	12,436	16,865
Tax	(4,533)	(6,132)	(7,942)	(4,967)	(3,110)	(3,204)
Profit after tax (FRS 3)	21,549	26,399	30,377	26,677	9,326	13,661
Average diluted number of shares outstanding (m)	117.6	118.0	117.2	115.8	114.9	114.0
EPS - basic (p)	19.5	23.5	27.4	25.1	8.8	13.0
EPS - diluted (p)	18.3	22.4	25.9	23.0	8.1	12.0
Dividend per share (p)	11.50	12.00	12.00	12.00	12.00	12.00
NAV per share (p)	102.0	113.5	125.0	135.0	131.7	129.3
ROE (%)	19%	22%	23%	19%	6.6%	9.9%
EBITDA margin (%)	29.5%	26.7%	27.7%	22.7%	13.7%	17.3%
Operating margin (before GW and except.) (%)	28.4%	25.6%	26.7%	21.8%	12.6%	14.9%
BALANCE SHEET						
Fixed assets	6,724	5,522	6,147	8,215	6,832	9,671
Current assets	279,114	312,462	407,850	533,033	326,641	378,541
Total assets	285,838	317,984	413,997	541,248	333,473	388,212
Current liabilities	(170,319)	(188,895)	(280,371)	(398,112)	(195,319)	(248,940)
Long term liabilities	0	(12)	0	0	0	(2,736)
Net assets	115,519	129,077	133,626	143,136	138,154	136,536
CASH FLOW						
Operating cash flow	6,467	48,735	43,369	45,830	(2,748)	36,251
Net cash from investing activities	(3,632)	84	(198)	(1,014)	(77)	151
Net cash from (used in) financing	(17,510)	(19,580)	(36,359)	(29,035)	(24,646)	(26,967)
Net cash flow	(14,675)	29,239	6,812	15,781	(27,471)	11,159
Opening net (cash)/debt	(74,518)	(59,591)	(89,002)	(95,852)	(111,673)	(84,202)
FX effect	(252)	172	38	40	0	0
Closing net (cash)/debt	(59,591)	(89,002)	(95,852)	(111,673)	(84,202)	(95,361)

Source: Company data, Edison Investment Research

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