Share

FY16 results

Poised for delivery

Financial services

Share plc's FY16 result was modestly ahead of our expectation and it is making progress in its work to enhance its customer proposition and servicing through significant investment in IT. The results of this should become more evident in the current year and help continue the growth in assets under administration (AUA), potentially helped by further acquisitions of books of accounts and corporate partnerships. As a platform with relatively stable costs once the IT renewal has been completed, increasing scale should feed through to geared profit improvement. Our central valuation of 29p is maintained.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/15	14.1	0.6	0.40	0.74	68.0	2.7
12/16	14.6	0.0	0.00	0.25	N/A	0.9
12/17e	16.5	0.3	0.12	0.30	215.2	1.1
12/18e	17.5	0.7	0.36	0.50	73.3	1.8

Note: *PBT and EPS are normalised, excluding exceptional items and share-based payments.

FY16 results

AUA increased by 32% to £3.7bn in 2016, reflecting both market strength (the FTSE All Share Index was up 12%), transfers in, organic growth and the benefit of book acquisitions and partnerships. Revenue was up by 4% but this includes interest income where lower rates depressed the contribution further, and fee and commission income alone were up 8%. Reported pre-tax profit was £1m (vs £0.9m in FY15), including a £2.1m profit on the sale of London Stock Exchange shares. There was a marginal normalised profit after tax (vs £0.6m) reflecting investment costs. Following the adoption of a new dividend policy based on earnings and cash generation a dividend of 0.25p was declared (vs 0.74p in FY15), slightly ahead of our estimate.

Outlook: More positive trends

Following a particularly poor market background for retail investment activity in H215 and the H116 uncertainty ahead of the Brexit referendum, activity levels have picked up, an improvement that has been sustained into the current year. This year should also benefit from full inclusion of accounts acquired during 2016 and the initiation of services for Computershare, together with the services to be provided to an as yet unnamed wealth manager. IT investment should also see more tangible benefits with the launch of a new version of the Share app, which will include dealing and other functionality, as well as improvements to the website to ease customer use. We now forecast an underlying profit rather than loss for 2017, while tempering our expectation for 2018 to allow more fully for the costs of investments.

Valuation: Unchanged

Our DCF assumptions take into account near-term depressed profits and a return to significant profitability over the medium term as operational gearing comes into play. Our central valuation of 29p is unchanged (see page 7).

15 March 2017

Price	**27.10p**
Market cap	**£39m**

Net cash (£m) at 31 December 2016	11.4
Shares in issue	143.7m
Free float	31%
Code	SHRE
Primary exchange	LSE
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(0.9)	(0.9)	(2.7)
Rel (local)	(2.9)	(7.0)	(17.3)
52-week high/low		29p	27p

Business description

Share plc's main subsidiary is The Share Centre, which is a self-select retail stockbroker that also offers share services for corporates and employees. It has a relatively high proportion of income from fees.

Next events

Q1 trading update	April 2017
AGM	June 2017

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Edison profile page

Share is a research client of Edison Investment Research Limited

Customer-focused retail stockbroker

The Share Centre, Share's main business, was launched in 1991 to provide execution-only stockbroking services to individual investors. In addition to share dealing accounts, The Share Centre also offers accounts for ISAs, SIPPs and investment clubs. It has c 250,000 customer accounts and £3.7bn of AUA. Customers are signed up individually and through corporate partnerships such as those with Henderson for investment trust ISA accounts, Barclays (certificated and investment club dealing services), Computershare (certificated and corporate sponsored nominee dealing) and Invesco Perpetual (ISA accounts). Revenue is generated from three sources: account fees, trading commissions and interest income, split 46.4%, 48.2% and 5.4% respectively for 2016. Share's account fee structure is differentiated from many peers by being fixed per account rather than based on the value of AUA. Transaction commissions are either charged at 1% with a minimum of £7.50 or, for those who deal frequently or in large sizes, on a flat £7.50 per bargain basis with a £20 quarterly fee (a 30% discount is offered to holders of 500 or more shares in Share plc). This means that the accounts frequently rank favourably in comparisons of providers (depending on portfolio size and frequency of trading).

FY16 results

Share's FY16 results were ahead of our estimates with revenues 2% above our forecast, while a small underlying net profit rather than a loss was recorded. Progress is being made in the programme of IT investment aimed at improving the customer proposition and servicing, enabling Share to scale the business and respond to market changes in a timely manner. See Exhibit 1 for details of the profit and loss for the full-year and half-year periods. The main points are highlighted below:

- **AUA** increased by 32% to £3.7bn, reflecting market strength (FTSE All Share +12%) and net flows. Segregated customer deposits stood at £296m compared with £176m at end 2015.
- The three in-house **fund of funds,** while still small, now manage £70m compared with £50m and are seen as providing an easy entry point for investors into the world of equity investing.
- The level of dealing activity spiked after the Brexit vote and remained at a higher level, allowing full-year total **revenues** to increase by 4% after a reduction in the first half. Interest income was pressured further by lower rates, and fee and commission revenue alone increased by 8%.
- Overall **costs** (nearly £16m) were up 6.8%, including an increase in staff costs of 8% partly reflecting an increase in staff numbers from 169 to 185 as IT capabilities and in-house marketing have been strengthened. Amortisation cost increased sharply (still only £0.1m), reflecting capitalised investment in systems development.
- Reported **pre-tax profit** was £1.0m versus £0.9m, including a one-off gain of £2.1m on the partial sale of shares in the London Stock Exchange. There was a small underlying profit in 2016 compared with a profit of £0.58m (excludes one-off items, among which is the FSCS levy of £0.272m versus £0.478m).
- Underlying, basic, diluted **EPS** was 0.0p compared with 0.4p for 2015. Reported earnings per share were 0.5p (unchanged).
- A **dividend** per share of 0.25p was announced compared with 0.74p reflecting the new policy adopted during the year under which payments will be based on earnings and cash generated.
- The **balance sheet** remains strong with year-end net cash of £11.4m (£11.7m FY15).

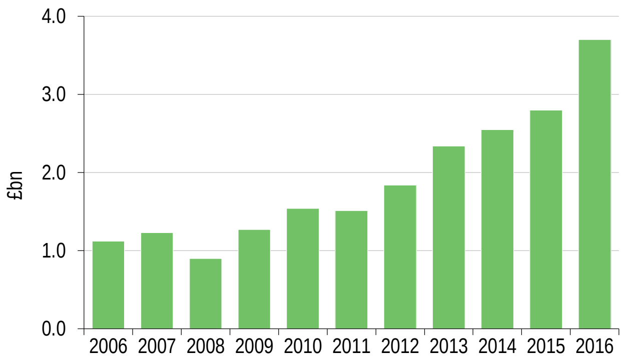
Exhibit 1: Results summary: H216 and FY16

Year-end 31 December	H115	H215	H116	H216	H216 vs H215 %	2015	2016	2016 vs 2105 %
£000 except where stated								
Account fees	3,199	3,201	3,271	3,513	9.7	6,400	6,784	6.0
Dealing Commissions	3,426	2,974	3,443	3,597	20.9	6,400	7,040	10.0
Interest and other income	743	507	510	276	(45.6)	1,250	786	(37.1)
Revenue	7,368	6,682	7,224	7,386	10.5	14,050	14,610	4.0
Total costs	(7,451)	(7,493)	(7,892)	(8,064)	7.6	(14,944)	(15,956)	6.8
Operating profit	(83)	(811)	(668)	(678)	(16.4)	(894)	(1,346)	50.6
Investment revenues	223	53	230	18	(66.0)	276	248	(10.1)
Other losses and gains	2	1,477	628	1,491	0.9	1,479	2,119	43.3
Pre-tax profit	142	719	190	831	15.6	861	1,021	18.6
Normalised pre tax	608	(24)	110	(156)		584	(46)	
Tax	(33)	(163)	(56)	(228)		(196)	(284)	
Post-tax profit	109	556	134	603	8.5	665	737	10.8
Normalised EPS (p)						0.40	0.00	
Dividend (p)						0.74	0.25	(73.0)

Source: Share plc, Edison Investment Research

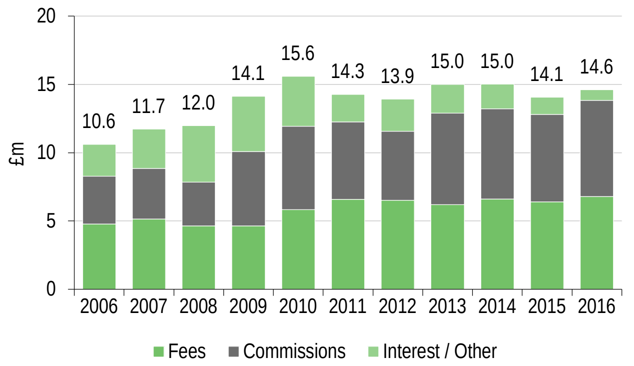
As noted above, AUA rose strongly, accelerating the longer-term trend illustrated in Exhibit 2, helped by market strength, transfers-in from other providers and the benefit of additions through partnership or acquisition such as those agreed with Barclays and Hendersons.

Exhibit 2: Share plc AUA



Source: Share plc

Exhibit 3: Share plc revenue analysis over time



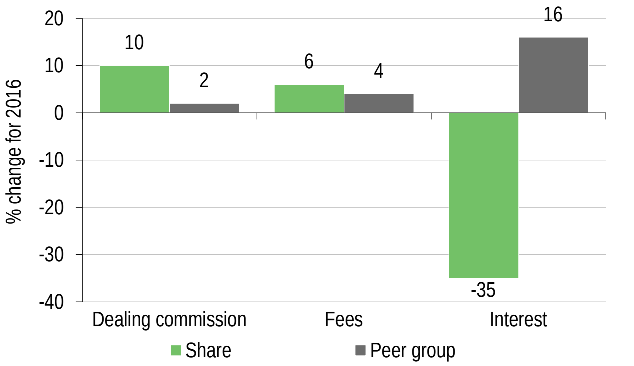
Source: Share plc

Exhibit 3 shows an analysis of Share's revenue over a similar timescale with a key feature being the way in which overall revenue has been broadly maintained in the face of two changes: the first being the adoption in 2013 of a flat fee structure that did not attempt to replace trail commission or to continue a model based on a percentage of assets; and the second, the dramatic contraction in interest income on customer cash balances reflecting central bank measures to guard against deflation. Interest income in 2016 accounted for 5.4% of revenue compared with 14.0% in 2013.

Share notes that last year its level of interest fell sharply while that of its peers increased (Exhibit 4). The company believes that some of its peers may use relatively higher risk counterparties to earn higher returns while those that are part of a bank may benefit from better rates. Share's dealing and fee revenue growth outperformed a ComPeer-collected peer group over the period. (The peer group excludes Hargreaves Lansdown, which does not submit monthly information to ComPeer.) The relative performance of commission income benefited from a new partnership and acquisitions (see below), while fee income was bolstered by strong new account acquisition and a good year for the administration of EIS and Business Property Relief schemes (180 funds, 24 investment managers).

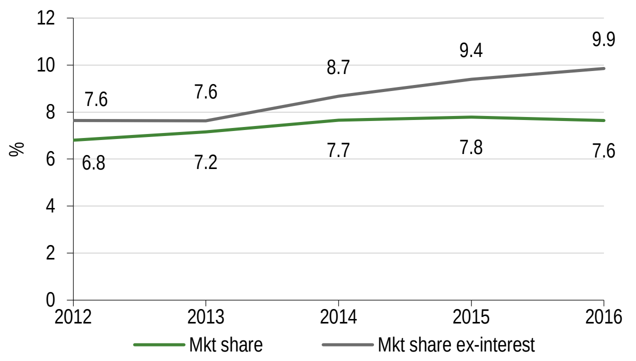
Reflecting these trends there has been a disparity between Share's market share progression with and without interest income (Exhibit 5). For 2016, excluding interest income, Share's revenue market share excluding interest reached a record level of 9.85% compared with 9.39% for 2015. Including interest income, the market share was lower at 7.64% versus 7.79%.

Exhibit 4: Share plc revenue analysis over time



Source: Share plc, ComPeer

Exhibit 5: Share plc market share progress



Source: Share plc, ComPeer

Work on Share's **digital transformation** was a feature of 2016 and remains in progress during the current year with more visible delivery set to become evident. Last year, the company launched its first mobile and tablet app for Apple and Android devices and, critically, is due to add dealing and other functionality later this year. The website is to be enhanced to improve customer usability while work on a new back-office system will be helped by the project that has already been completed to move the database on to new technology.

The central place of IT for Share reflects its concentration on its core retail broking business and strategy of putting customers first. Chairman Gavin Oldham comments that from inception the concentration in the business has been on servicing the customer accounts, not on securing transaction volumes alone. This was in order to establish long-term customer relationships and hence a sustainable business. This is also evident in the flat fee structure, which is in line with the nature of the costs in the business. Prospectively, this could mean that Share is well positioned from a competitive position as year-end statements highlight more clearly the level of fees investors are paying at other providers.

In 2015, Share signed a **partnership agreement** with Barclays Stockbrokers for certificated dealings and an **acquisition** of investment trust ISA accounts from Henderson. In 2016, in a further transaction with Barclays it acquired accounts for investment clubs, corporates and charities. Heads of terms were agreed with Computershare for the provision on a white label basis of certificated dealing and corporate nominee dealing services. Computershare provides registry services to more than 900 corporates in the UK, Ireland and Channel Islands and has 22 corporate nominee clients including Aviva, E.on, Rio Tinto, Standard Chartered and Vodafone. This service is due to be launched shortly and, ahead of this, a deceased estate service was launched in the second half of 2016. Share also announced the acquisition of a book of up to 8,700 (over £200m) ISA accounts from Invesco Perpetual (due to complete in April 2017) and that it is in advanced discussions with a leading wealth manager with development work to provide a streamlined administration service for part of the business already underway.

As part of its focus on the core retail broking business, Share decided to transfer the **Authorised Corporate Director** activity to another party (Treasury Capital Ltd). This is due to complete on 24 March. The business had cash of £0.774m at the year end and we assume that this will effectively stay with Share, although no terms have been disclosed.

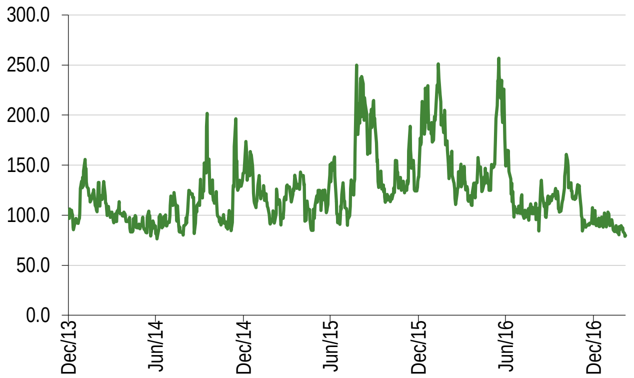
Background and outlook

Exhibits 6 and 7 provide a reminder of the UK equity market background in recent years highlighting fluctuations in the FTSE All-Share Index but strong overall progress despite an uncertain economic and political background. The Volatility Index (sometimes termed a 'fear gauge') has shown a decline since the Brexit vote, creating a calmer background that has encouraged a higher level of retail transactions.

Exhibit 6: FTSE All-Share Index (total return)

Source: Thomson Datastream

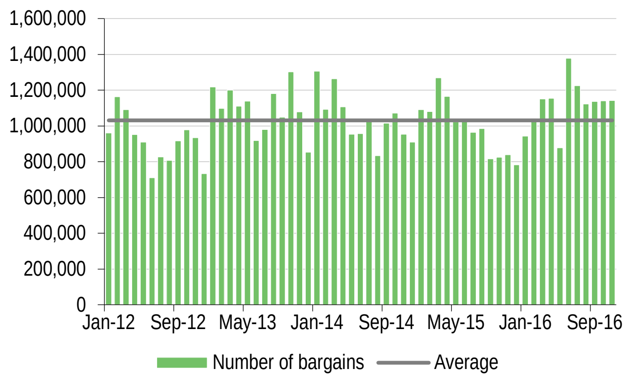
Exhibit 7: FTSE100 Implied Volatility Index



Source: Thomson Datastream

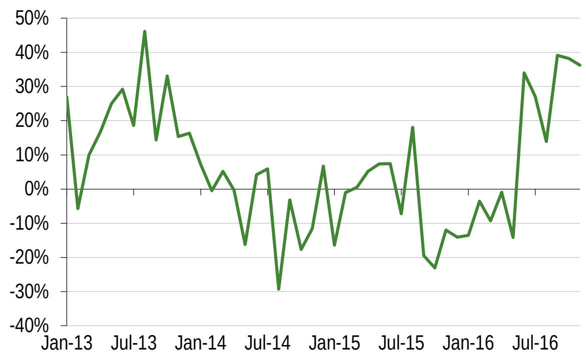
This is shown in Exhibits 8 and 9 with a noticeable pick-up in the level of transactions, even discounting the spike at the time of the Brexit referendum.

Exhibit 8: Retail trading volume (bargains)



Source: ComPeer, London Stock Exchange

Exhibit 9: Retail trading volume (change vs prior year)



Source: ComPeer, London Stock Exchange

Prospectively, global geopolitical uncertainty remains in place and in the UK and Europe there could be fluctuating sentiment towards news from Brexit negotiations. Having said this the UK economy has remained resilient compared with many expectations during 2015 and forecasts have generally been revised upwards. European growth expectations have also strengthened, albeit concerns remain over aspects of the eurozone.

For Share, a key determinant of future performance will be delivery of its digital transformation as this should provide an improved customer experience (Share continues to score well on Trustpilot ratings) and facilitate a scaling of the business through customer transfers in, further partnerships and acquisition of books of accounts. Eventually a move towards the normalisation of interest rates could also be beneficial for revenue. Assuming the current level of customer cash at c £300m, a 25bp improvement in rates received could add £0.75m to revenues that would drop straight through to pre-tax profit.

Financials

We have increased our revenue estimate for the current year (see Exhibit 10) to reflect the strong second half of 2016 and start to the current year, while cautiously leaving our 2018 estimate unchanged. As a result, our underlying profit forecast for 2017 has moved from loss to profit, although in revising our 2018 estimate we have allowed for higher costs resulting from continuation of investment through the current year tempering our profit estimate. Looking further ahead we would expect success in attracting new customers and further acquisitions of books of accounts or partnerships to generate operational leverage given the investment now being undertaken to refresh the technology base.

While the dividend payout was reduced from 0.74p to 0.25p for 2016, we expect the move back into greater profitability to be accompanied by a more rapid increase in dividend than previously expected.

Exhibit 10: Estimate revisions

	Revenue (£m)			PBT (£m)			EPS (p)			Dividend (p)		
	Old	New	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg
2016	14.4	14.6	2%	-0.9	0.0	N/A	-0.49	0.00	N/A	0.20	0.25	25%
2017e	15.7	16.5	5%	-0.2	0.3	N/A	-0.06	0.12	N/A	0.20	0.30	50%
2018e	17.4	17.5	0%	1.1	0.7	-42%	0.68	0.36	-47%	0.30	0.50	67%

Source: Edison Investment Research. Note: For 2016 new column = actual

Looking at Share's cash flow for 2016, the main features were investment in intangibles of nearly £1.2m, reflecting work capitalised on system development. This was more than offset by the sale of shares in the London Stock Exchange, which meant that sales of available for sale investments totalled nearly £2.4m. Combined with a small operating cash inflow resulting from a working capital inflow and the dividend outflow of c £1m, the level of cash was only down modestly from £11.7m in FY15 to £11.4m.

From a regulatory perspective, Share still has a healthy margin above its target level of regulatory capital. Its resources stood at 2.6x the regulatory requirement; this compares with 3.6x for the prior year, partly reflecting a rise in the capital requirement from £5.1m in 2016 to £5.6m, but more importantly the deduction of the increased level of intangibles noted above together with the non-inclusion of the profit on the London Stock Exchange share sale in regulatory capital prior to audit. Prospectively, inclusion of this profit should act to offset the net increase of c £1m we expect in intangibles on the balance sheet in 2017.

Valuation

We have updated our comparative table, which includes selected measures for Share, Alliance Trust Savings (unquoted subsidiary of Alliance Trust) and Hargreaves Lansdown. As before, this underlines the scale of Hargreaves Lansdown with AUA of £70bn in total compared with Alliance Trust Savings at £13bn and Share on £3.7bn. The agreed purchase of TD Direct Investing by Interactive Investor will give that combination AUA of c £18bn. Given the potential benefits of scale, we would expect further consolidation on a medium- to longer-term view crystallising value for seller and buyer depending on the terms and how the industry pricing model evolves.

There is a wide variation in valuation multiples. Perhaps unsurprisingly, Hargreaves Lansdown, as market leader by a large margin with an established record of strong growth and profitability, is the most highly valued across each of the measures. Share is more expensive than Alliance Trust Savings in terms of adjusted value to AUA, but this can be explained by the higher revenue yield earned by Share, while in terms of adjusted value to revenue Share is valued below the other two companies. Increased scale through acquisition or organic growth would be likely to benefit profitability and hence valuation on these metrics.

Exhibit 11: Peer comparison

£m unless stated	Share	Alliance Trust Savings	Hargreaves Lansdown
Market capital	38.9		6,215.6
Surplus capital (assumes cover of twice the regulatory requirement)	5.4		55.2
Adjusted value	33.6	54.0	6,160.4
Revenue	14.6	13.7	369.8
AUA	3,700	13,000	70,000
Market capital/revenue (x)	2.7	N/A	16.8
Market capital/AUA (%)	1.1	N/A	8.9
Adjusted value/revenue (x)	2.3	3.9	16.7
Adjusted value/AUA (%)	0.9	0.4	8.8

Source: Edison, companies' disclosure. Note: valuation of Alliance Trust Savings from H116 results, revenue 2015 and AUA at end September 2016. Hargreaves Lansdown AUA and revenue (annualised) from H117.

To give an absolute indication of value we have also updated our DCF model using the same central assumptions but rolling our forecasts forward a year. Among the assumptions are two years of strong cash flow growth of 60% in 2020 and 2021 (following a return to reported profits of c £0.5m in 2019) and seven years of growth at 5%. We also assume a terminal multiple of 10x and a discount rate of 10%. Exhibit 12 sets out the sensitivity of the value output to changes in the discount rate and 2020-21 growth assumption. Our central valuation of 29p is unchanged.

Exhibit 12: Discounted cash flow valuation sensitivity (pence per share)

	Discount rate				
2020 and 2021 growth	8%	9%	10%	11%	12%
0%	20	20	19	18	18
30%	26	25	23	23	22
60%	32	31	29	28	26
80%	38	36	34	32	30

Source: Edison Investment Research

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Exhibit 13: Financial summary

£000 except where stated	2014	2015	2016	2017e	2018e
Year end 31 December					
PROFIT & LOSS					
Account fees	6,610	6,400	6,784	8,480	9,074
Dealing Commissions	6,610	6,400	7,040	7,533	7,909
Interest and other income	1,800	1,250	786	474	510
Revenue	15,042	14,050	14,610	16,486	17,493
Cost of Sales (excl amortisation and depreciation)	(14,579)	(14,812)	(15,727)	(16,622)	(17,284)
EBITDA	463	(762)	(1,117)	(135)	209
Depreciation	(104)	(111)	(121)	(131)	(150)
Amortisation	(11)	(21)	(108)	(390)	(400)
Operating profit (pre-exceptional)	348	(894)	(1,346)	(656)	(341)
Other	60	1,479	2,119	0	0
Investment revenues	308	276	248	201	198
Profit Before Tax (FRS3)	716	861	1,021	(455)	(142)
Profit Before Tax (norm)	1,615	584	(46)	329	658
Tax	(109)	(196)	(284)	0	0
Profit After Tax (FRS 3)	607	665	737	(455)	(142)
Profit After Tax (norm)	1,416	555	4	172	506
Average Number of Shares Outstanding (m) - excl treasury	143.5	139.2	139.3	140.0	140.0
EPS - normalised (p)	0.99	0.40	0.00	0.12	0.36
EPS - FRS3 (p)	0.42	0.48	0.53	(0.33)	(0.10)
Dividend per share (p)	0.62	0.74	0.25	0.30	0.50
EBITDA Margin (%)	3.1%	(5.4%)	(7.6%)	(0.8%)	1.2%
Normalised operating margin (%)	8.3%	2.2%	(2.0%)	0.8%	2.6%
BALANCE SHEET					
Fixed Assets (mainly Investments)	9,405	8,083	8,341	9,420	9,485
Current Assets	21,316	19,716	23,883	23,376	23,850
Total Assets	30,721	27,799	32,224	32,796	33,335
Current Liabilities	(8,450)	(7,681)	(13,384)	(14,159)	(14,659)
Long term Liabilities	(1,594)	(1,418)	(1,096)	(1,096)	(1,096)
Net Assets	20,677	18,700	17,744	17,541	17,580
CASH FLOW					
Operating Cash Flow	348	(894)	(1,346)	(656)	(341)
Net cash from investing activities	(434)	1,990	483	(1,399)	(417)
Net cash from (used in) financing	(736)	(878)	(1,019)	(350)	(420)
Net Cash Flow	(971)	(992)	(242)	(2,108)	(384)
Opening net (debt)/cash	13,626	12,655	11,663	11,421	9,313
Closing net (debt)/cash	12,655	11,663	11,421	9,313	8,929

Source: Company accounts, Edison Investment Research

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