

Numis Corporation

H119 results

Cost discipline and franchise strength in evidence

In particularly difficult market conditions, Numis's franchise strength and maintenance of the compensation ratio softened the impact of lower investment banking and equities revenue. Earnings per share were still down by two-thirds compared with H118 but, looking ahead, a return to a more favourable environment should allow Numis to deliver attractive returns on equity once more (historical five-year average c 20%).

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/16	112.3	32.5	22.4	12.0	11.7	4.6
09/17	130.1	38.3	25.9	12.0	10.1	4.6
09/18	136.0	31.6	23.0	12.0	11.3	4.6
09/19e	117.6	18.1	12.7	12.0	20.6	4.6

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

H119 results

As foreshadowed in the March update, H119 trading was affected by the uncertain UK political background and equity market volatility. Compared with H118, overall revenues were down 25% within which investment banking was down 24% and Equities 28%. The adverse background did not stop further growth in the franchise with the corporate client count increasing by a net six companies to 214. A reduction in variable compensation allowed the compensation ratio to be held stable at 54%, despite an increase of 14% in the average headcount following last year's investment in hiring to support future growth. Even so, underlying operating profit was 58% lower and pre-tax profit was down 64% to £7.1m. Diluted EPS was 5.0p vs 14.6p, while the interim dividend was unchanged at 5.5p.

Outlook

The timing and nature of an eventual resolution of the Brexit impasse should be a key driver of a revival in earnings for Numis and its peers. While this keeps being deferred it does seem plausible that there is a significant level of deferred corporate activity that will eventually be released as confidence returns. Even without this there is evidence in the first half that Numis's investment in supporting its service delivery is helping limit the impact of reduced activity levels, especially in equity capital markets. The investment should also mean the group is well placed to take opportunities to increase market share over the medium to long term.

Valuation

Our earnings estimate for FY19 has been reduced by 20% reflecting higher non-staff costs and more conservative revenue assumptions for H219. This points to a prospective ROE of 10% for the current year whereas a ROE/COE model suggests the market is discounting a return of c 16% at the current price. Given the historical five-year average of 20%, this still leaves significant upside as the market environment becomes less challenging.

Financial services

9 May 2019

Price 261p
Market cap £278m

Net cash (£m) end March 2019	78.9
Shares in issue	106.0m
Free float	75%
Code	NUM
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	7.0	3.6	(37.1)
Rel (local)	9.0	0.4	(34.4)
52-week high/low	440.0p	221.5p	

Business description

Numis is one of the UK's leading independent corporate advisory and stockbroking groups, offering a full range of research, execution, equity capital markets, corporate broking and advisory services. It employs over 270 staff in offices in London and New York, and at the end of September 2018 had 210 corporate clients.

Next events

FY19 trading update	September 2019
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Key points from H119 results

As noted, group revenue was 25% lower than H118 within which investment banking was down 24% and equities 28% (see Exhibit 1 for details). The first half of last year was a tougher comparative period for investment banking than the second half and, sequentially, its revenues were just ahead of H218, with a pick-up in M&A advisory fees and private capital markets offsetting much-reduced IPO activity. This was a creditable performance in a period in which Numis notes that overall UK equity capital markets activity was approximately 50% lower (H119 versus H218). Average deal fees matched the level for FY18, reflecting deal size and the seniority of roles secured: both potentially positive indicators and linked by Numis to the continuing strengthening of the quality of the client base. During the period the market capitalisation of clients added was above those leaving, with an average for all clients of £836m versus £711m for H118. The 214 corporate clients at end H119, a net increase of six since H118, included six FTSE 100 index and 48 FTSE 250 constituents.

Within equities, institutional commissions were down by 12% reflecting lower trading activity but still robust payments for research with Numis looking for these to be broadly maintained for FY19 as a whole. Trading income (-92%) was affected by the trading background but was particularly impacted by a rare underwriting loss of c £3m (before related corporate fee) associated with the Kier rights issue during the period.

The other operating income line moved from a positive £0.4m contribution to a loss of £1.4m. This arose from a £0.9m write down on unquoted investments and a loss of £0.5m on the one remaining quoted investment. This left total income down 27% compared with the prior-year period.

Exhibit 1: P&L analysis

£m unless stated	H118	H218	H119	Change H119/H118
Net trading gains	4.6	5.0	0.4	-92.1%
Institutional commissions	18.7	19.1	16.5	-11.8%
Equities	23.3	24.2	16.9	-27.5%
Corporate retainers	6.1	6.3	6.4	4.9%
Advisory fees	11.7	5.6	7.5	-35.7%
Placing commissions / capital markets	33.0	25.8	24.9	-24.7%
Investment banking	50.9	37.7	38.8	-23.7%
Total revenue	74.1	61.9	55.7	-24.9%
Other operating income	0.4	1.3	(1.4)	N/A
Total income	74.5	63.2	54.3	-27.2%
Staff costs	(40.0)	(35.4)	(30.2)	-24.4%
Non-staff costs	(14.9)	(16.2)	(17.4)	16.8%
Total administrative expenses	(54.8)	(51.5)	(47.6)	-13.2%
Operating profit / loss	19.7	11.7	6.7	-66.0%
Finance income/expense	(0.2)	0.4	0.4	N/A
Pre-tax profit	19.5	12.1	7.1	-63.6%
Tax	(2.7)	(2.3)	(1.4)	-48.6%
Effective tax rate	13.9%	18.6%	19.6%	41.2%
Attributable profit	16.8	9.9	5.7	-66.0%
Diluted EPS (p)	14.6	8.5	5.0	-66.0%
Dividend (p)	5.5	6.5	5.5	0.0%

Source: Numis, Edison Investment Research

Turning to expenses, the level of staff costs was 24.4% lower as a reduction in variable compensation allowed the compensation ratio to be held stable at 54%, despite an increase of 13.5% in the average headcount following last year's investment in hiring to support future growth. Although further additions may be considered if market conditions provide good opportunities, the group does not expect a material change in staff numbers during the second half.

In contrast, non-staff costs saw increases of 16.8% and 7.5% compared with H118 and H218 respectively. This was driven by a combination of the costs associated with the increase in headcount, including additional data services, an element of one-off data-related fees arising from a periodic audit of usage and continuing spending to strengthen systems supporting regulatory compliance further. Operating profit was 66% lower, 58% on an underlying basis, excluding gains or losses from the investment portfolio. Pre-tax profit was down 64% to £7.1m and diluted EPS was 5.0p vs 14.6p; the interim dividend was unchanged at 5.5p.

Background and outlook

Recent equity market trends are shown in Exhibits 2 and 3. The sharp decline in equity indices in the final quarter of calendar year 2018 and the subsequent recovery and pull back in volatility are clear. The first chart also illustrates the outperformance of the FTSE SmallCap index compared with the All-Share and AIM All-Share indices over the five-year period shown. At the time of writing the All-Share and SmallCap indices were down modestly, whereas the AIM /All-Share was down 12% for Numis's financial year to date. Compared with the final quarter of calendar year 2018 this creates a potentially more positive background for corporate activity once political uncertainty subsides.

Exhibit 2: FTSE AIM, All-Share and Small Cap indices

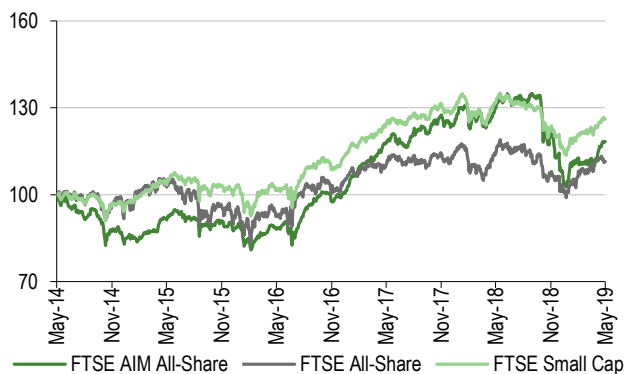
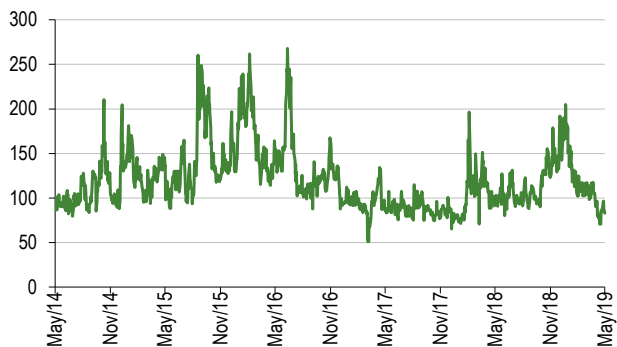
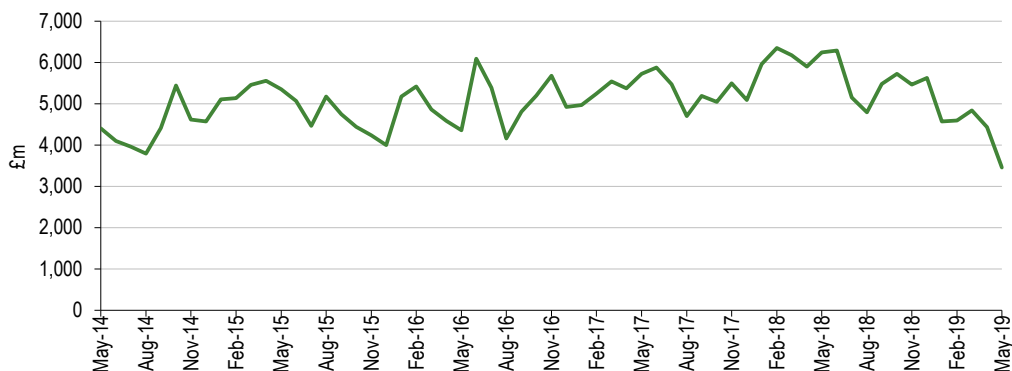


Exhibit 3: FTSE 100 volatility index

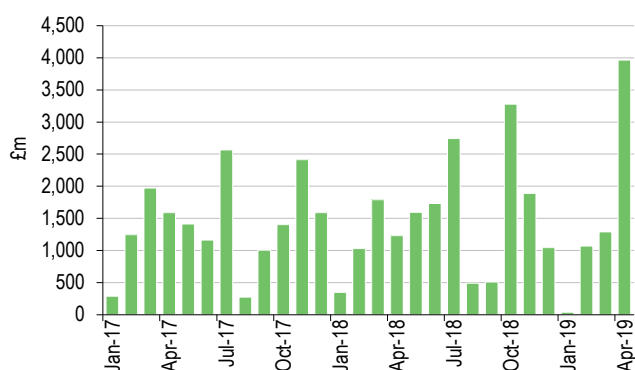


As shown in Exhibit 4, the average daily value traded on the London Stock Exchange order book has been on a downward trend in recent months. A cautionary note for the near term but this could reverse quickly given greater market confidence on the macro outlook and Numis indicated that April trading in equities continued at a similar level to the first half.

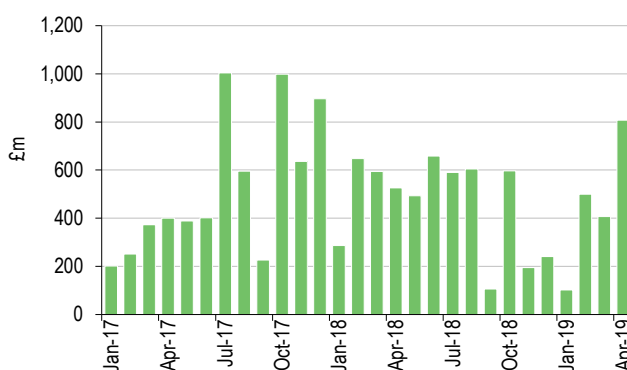
Exhibit 4: London Stock Exchange electronic order book, average daily value traded



The LSE's new and further issuance figures for the main market and AIM (Exhibits 5 and 6) show the very subdued background in Numis's H119 and some revival in activity in April. For the main market much of this value related to a placing by Astra Zeneca (£2.9bn). Numis has reported that it completed a number of transactions in April, although they have been generally lower value fee events. Nevertheless, the pipeline is promising, with a greater number of M&A opportunities offsetting a reduction in the number of IPOs in the pipeline. The breadth of the pipeline has narrowed somewhat so the near-term outcome is even more uncertain than usual, depending on the incidence of specific completed transactions.

Exhibit 5: LSE main market new and further issuance


Source: London Stock Exchange

Exhibit 6: LSE AIM new and further issuance


Source: London Stock Exchange

Greater political certainty remains elusive but we see the prospect a significant revival in activity once it arrives as plausible, and Numis's investment in its franchise leaves it well positioned to take advantage of opportunities as they arise. This should allow it to generate significantly more attractive returns on equity than during the first half (8% annualised compared with the historical five-year average c 20%).

Strategically, the group remains committed to its vision of creating the investment bank of a generation by building the size and quality of its franchise, becoming the leading UK equities platform, developing complementary products/services, maintaining operating/capital disciplines and delivering shareholder returns (for more details see our [January note](#)).

Financials

We have adjusted our estimates to allow for the first-half numbers including a reduction in other income and somewhat higher non-staff expenses than previously. The continued deadlock surrounding Brexit has contributed to slightly more conservative revenue assumptions. Key lines from our estimates for FY19 are summarised in Exhibit 7 below. We look to put in place estimates for FY20 nearer the year end, potentially with the benefit of greater clarity on the UK political outlook.

Exhibit 7: Estimate revisions

	Revenue (£m)			PBT (£m)			EPS (p)			DPS (p)		
	Old	New	Change	Old	New	Change	Old	New	Change	Old	New	Change
09/19e	119.7	117.6	-1.8%	22.3	18.1	-18.9%	15.8	12.7	-20.0%	12.0	12.0	0.0%

Source: Edison Investment Research

The modest reduction in our revenue estimate combined with a small increase in overall costs results in a 16% reduction at the operating profit level, which is amplified by the assumption of a loss rather than profit for other income resulting in 19% and 20% falls in pre-tax profit and EPS estimates respectively. A comparison of our segmental revenue estimates is shown in Exhibit 8 with further detail for the P&L, balance sheet and cash flow shown in the financial summary (Exhibit 10).

Exhibit 8: Revenue analysis

£000s	2018	2019e	Change	Old 2019e	New vs old
Net trading gains	9,594	3,600	-62%	3,500	3%
Institutional income	37,866	34,000	-10%	35,000	-3%
Equities	47,460	37,600	-21%	38,500	-2%
Corporate retainers	12,430	13,000	5%	13,000	0%
Advisory fees	17,335	17,000	-2%	17,200	-1%
Placing commissions/capital markets	58,822	50,000	-15%	51,000	-2%
Investment Banking	88,587	80,000	-10%	81,200	-1%
Total revenue	136,047	117,600	-14%	119,700	-2%

Source: Edison Investment Research

Regulatory capital is significantly higher than required providing stability and flexibility. At the half year end net cash stood at £78.9m (£82.5m H118 and £111.7m FY18) and additional liquidity has been provided by a new £35m credit facility that will further enhance the ability to engage in larger transactions. The facility is committed for three years and the costs associated with it are expected to be offset by the saving generated by Numis becoming a direct clearing member of LCH, a move that itself is enabled by the structure of the new facility.

Valuation

We have updated our peer comparison table in Exhibit 9; this includes UK quoted brokers and a selection of US and European investment banks and advisory firms. The absence of UK peer prospective P/Es and the continuing uncertainty of the political background means this measure is of limited use, although on our reduced estimate Numis trades well above its international peers. In terms of price to book ratio, Numis trades above the UK average but at a similar level to the international companies. We have shown the H119 annualised ROE for Numis of 8.1% but, as noted earlier, the five-year average return was 20%. At 261p a ROE/COE model suggests the market is discounting an ROE of c 16%, still leaving significant upside once trading conditions allow a return to previous levels of ROE.

Exhibit 9: Peer comparison

	Price (local)	Market cap (£m)	Last reported P/E (x)	Current P/E (x)	Yield (%)	ROE (%)	Price to book (x)
UK brokers							
Numis	261	279	11.3	22.0	4.6	8.1	2.0
Arden Partners	23	7	Loss	N/A	0.0	N/A	0.7
Cenkos	62	35	14.8	N/A	7.3	25.3	1.3
Shore Capital	222	48	17.8	N/A	4.5	4.8	0.8
WH Ireland	49	21	Loss	N/A	0.0	N/A	1.4
UK average			14.6	N/A	3.3	12.7	1.2
US, European IB and advisory							
Bank of America	29.8	283,344	11.4	10.4	1.8	10.5	1.1
Evercore	89.8	4,262	10.0	11.0	2.1	69.7	4.7
Goldman Sachs	201.0	73,515	8.0	8.6	1.6	12.3	1.0
Greenhill	18.9	391	N/A	N/A	1.1	29.7	6.2
JP Morgan	112.6	365,304	12.5	11.2	2.2	13.0	1.4
Moelis	35.8	2,138	11.9	14.0	5.2	60.4	5.0
Morgan Stanley	46.5	78,274	9.8	9.3	2.4	11.8	1.1
Stifel Financial	58.7	4,166	11.1	10.2	0.8	14.2	1.4
Credit Suisse	12.8	32,787	11.9	9.6	2.0	6.9	0.7
Deutsche Bank	7.0	14,549	16.1	13.2	1.6	0.3	0.2
UBS	12.3	47,386	9.7	9.9	5.7	5.3	0.9
US, European IB and advisory average			11.2	10.7	2.4	21.3	2.2

Source: Refinitiv. Note: Priced at 8 May 2019, P/Es are for financial years therefore not all same period end.

Exhibit 10: Financial summary

£'000s	2015	2016	2017	2018	2019e
Year end 30 September					
PROFIT & LOSS					
Revenue	97,985	112,335	130,095	136,047	117,600
Administrative expenses (excl. amortisation and depreciation)	(65,018)	(76,120)	(83,626)	(94,603)	(87,284)
Share based payment	(4,104)	(6,229)	(10,454)	(10,583)	(11,000)
EBITDA	28,863	29,986	36,015	30,861	19,316
Depreciation	(882)	(1,126)	(1,226)	(1,113)	(1,100)
Amortisation	(111)	(125)	(89)	(49)	(30)
Operating Profit (before amort. and except.)	27,870	28,735	34,700	29,699	18,186
Net finance income	190	37	188	212	810
Other operating income	(1,978)	3,759	3,431	1,733	(900)
Profit before tax	26,082	32,531	38,319	31,644	18,096
Tax	(4,533)	(6,132)	(7,942)	(4,967)	(3,529)
Profit after tax (FRS 3)	21,549	26,399	30,377	26,677	14,567
Average diluted number of shares outstanding (m)	117.6	118.0	117.2	115.8	114.9
EPS - basic (p)	19.5	23.5	27.4	25.1	13.8
EPS - diluted (p)	18.3	22.4	25.9	23.0	12.7
Dividend per share (p)	11.50	12.00	12.00	12.00	12.00
NAV per share (p)	102.0	113.5	125.0	135.0	133.0
ROE (%)	19%	22%	23%	19%	10.3%
EBITDA margin (%)	29.5%	26.7%	27.7%	22.7%	16.4%
Operating margin (before GW and except.) (%)	28.4%	25.6%	26.7%	21.8%	15.5%
BALANCE SHEET					
Fixed assets	6,724	5,522	6,147	8,215	6,103
Current assets	279,114	312,462	407,850	533,033	373,195
Total assets	285,838	317,984	413,997	541,248	379,298
Current liabilities	(170,319)	(188,895)	(280,371)	(398,112)	(239,378)
Long term liabilities	0	(12)	0	0	0
Net assets	115,519	129,077	133,626	143,136	139,920
CASH FLOW					
Operating cash flow	6,467	48,735	43,369	45,830	(4,283)
Net cash from investing activities	(3,632)	84	(198)	(1,014)	350
Net cash from (used in) financing	(17,510)	(19,580)	(36,359)	(29,035)	(28,959)
Net cash flow	(14,675)	29,239	6,812	15,781	(32,891)
Opening net (cash)/debt	(74,518)	(59,591)	(89,002)	(95,852)	(111,673)
FX effect	(252)	172	38	40	5
Closing net (cash)/debt	(59,591)	(89,002)	(95,852)	(111,673)	(78,787)

Source: Company data, Edison Investment Research

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