

Source: Eikon Thomson Reuters

Market data

EPIC/TKR	CLIG
Price (p)	385.5
12m High (p)	398.5
12m Low (p)	285.0
Shares (m)	26.9
Mkt Cap (£m)	103.7
EV (£m)	93.5
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	9.2%
Hargreave Hale	4.9%
Slater Investments	3.3%
Polar Capital	3.0%

Next event

13 th Oct 2016	Ex-div date
17 th Oct 2016	AGM
31 st Oct 2016	Final dividend paid
17 th Jan 2017	Q2 Trading update

Analysts

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City of London Investment Group**Reaping the benefit of favourable markets**

City of London issued a trading statement for the first quarter of the 2017 financial year. With only a month having passed since the year end results were announced, much of the operational information is as expected but there has been further significant benefit from exchange rate movements. Funds under management at the quarter end were \$4.3bn, up from \$4.0bn at the end of June but down a little from the previous announcement. The increase was pretty much in line with the movement in the MSCI Emerging Markets Index.

- ▶ **Operations:** Although the markets have moved strongly in City of London's favour this year, it has continued its excellent cost control. Fixed costs remain at around £0.9m per month. Estimated post-tax profit for the first quarter is £2.3m, including £0.1m of unrealised gains.
- ▶ **New business:** There was no news on new business in the statement. The company reiterated that the impact of Brexit operationally is likely to be very limited, with significant financial benefits from the weakness of sterling against the US Dollar, which is reflected in the better than expected profits.
- ▶ **Valuation:** The prospective P/E of 10.1 times is at a significant discount to the peer group. The yield of 6.5% is very attractive and should at the very least provide support for the shares in the current volatile markets. At current market levels we'd expect dividend cover to be restored in 2017.
- ▶ **Risks:** To date, City of London has not experienced the sort of outflows that some other emerging market fund managers have, aided by its good performance and strong client servicing. Further EM volatility may increase the risk of such outflows however.
- ▶ **Investment summary:** City of London has continued to show robust performance in challenging market conditions. The valuation remains reasonable. At current FUM and exchange rates, dividend cover will be more than restored in FY2017 adding to investors comfort.

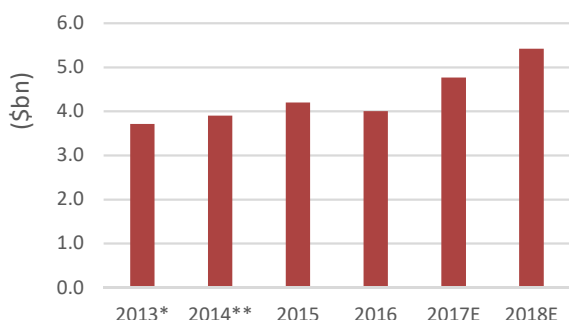
Financial summary and valuation

Year end Jun (£m)	2013*	2014*	2015	2016	2017E	2018E
FUM (\$bn)	3.71	3.90	4.20	4.00	4.77	5.42
Revenue (£m)	29.36	24.22	25.36	24.41	31.34	35.09
Statutory PTP	6.27	5.20	6.61	5.85	9.51	10.75
Statutory EPS (p)	24.9	20.7	26.4	23.3	38.2	43.2
Dividend (p)	24.0	24.0	24.0	24.0	25.0	26.0
P/E (x)	15.5	18.6	14.6	16.5	10.1	8.9
Yield	6.2%	6.2%	6.2%	6.2%	6.5%	6.7%

Source: Hardman & Co Research

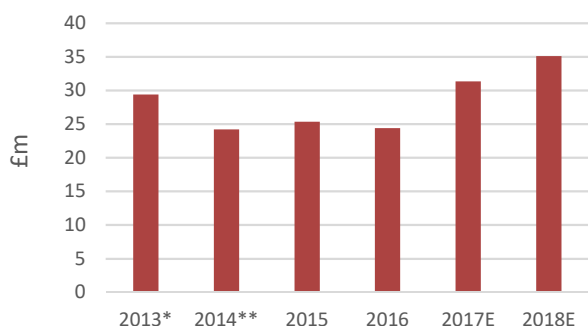
* 2013 and 2014 had May year ends. 2014 had 13 months in financial year.

Funds under Management



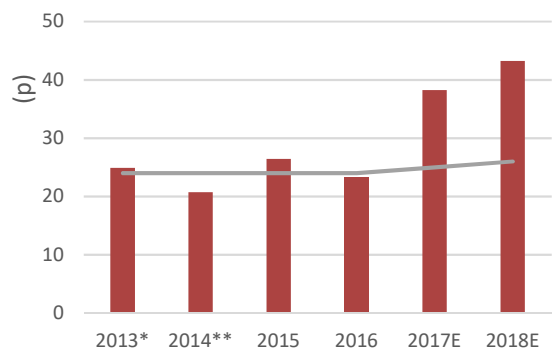
- ▶ Net inflows from 2014
- ▶ Market weakness in 2016 substantially offset by new business flows
- ▶ Assumed steady new business flows and market growth of 5% pa in 2017 and 2018

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
- ▶ Dividend shortfall in 2014 and 2016 covered from reserves
- ▶ If market remains at current levels then we would expect dividend to be covered and increased in 2017

Source: Company data; Hardman & Co Research

Estimate Changes

With the statement largely being in line with our expectations, there have been only small adjustments to our estimates for operational reasons. The slight adjustment to FUM has had a slight negative effect on our estimates.

The main adjustment has again come from the ongoing weakness of sterling and overall this has given upgrades of 17% to our 2017E and 10% to our 2018E. For the moment we have left our dividend forecasts unchanged, but if sterling continues to at this level then there may be scope for larger increases than we have forecast. We note that the cover is assessed over a five-year period, so we would expect any increases to lag profit growth in the short term.

We note that the profit figure quoted by City of London incorporates a 30% profit share for staff. There is a resolution for the AGM to raise this to 35% and we understand that, if passed, this will take effect from January.

Corporate News

Investors should recall that the CEO, Barry Olliff, has set out an intention to sell 500,000 shares at 400p as part of the structured reduction in his holding. With the share price approaching that level, this sale may take place in the near future.

Financials

Summary Financials						
	2013*	2014**	June Year End 2015	2016	2017E	2018E
FUM (\$bn)	3.71	3.90	4.20	4.00	4.77	5.42
P&L (£m)						
Revenue	29.36	24.22	25.36	24.41	31.34	35.09
Expenses	21.01	17.22	16.63	16.66	18.60	20.58
Operating Profit	8.36	7.00	8.73	7.76	12.74	14.51
PBT	8.86	7.24	8.93	7.97	12.86	14.53
Earnings	6.27	5.20	6.61	5.85	9.51	10.75
eps (p)	24.9	20.7	26.4	23.3	38.2	43.2
dps (p)	24.0	24.0	24.0	24.0	25.0	26.0
Key Metrics						
	2013*	2014**	2015	2016	2017E	2018E
Growth (%)						
FUM		5.0	7.7	-4.8	19.2	13.6
Revenue		-17.5	4.7	-3.7	28.4	12.0
Operating Profit		-16.3	24.7	-11.1	64.2	13.9
EPS		-16.9	27.5	-11.7	64.1	13.0
DPS		0.0	0.0	0.0	4.2	4.0
Operating Margins (%)						
Net FUM fee margin	0.92	0.88	0.86	0.86	0.85	0.84
Operating Margin	28.5	28.9	34.4	31.8	40.6	41.4
Tax Rate	29.3	28.2	26.0	26.5	26.0	26.0
Dividend cover	1.0	0.9	1.1	1.0	1.5	1.7
eps Sensitivity						
					2017E	2018E
No net new business						
eps (p)					37.1	37.9
% change					-2.9	-12.3
0% market growth (was 5% pa from Sept 2016)						
eps (p)					37.4	39.5
% change					-2.1	-8.7

Source: City of London Investment Group, Hardman & Co Research

* May year end

** 13-month year as year end change.

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(Disclaimer Version 2 – Effective from August 2015)

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