Tatton Asset Management

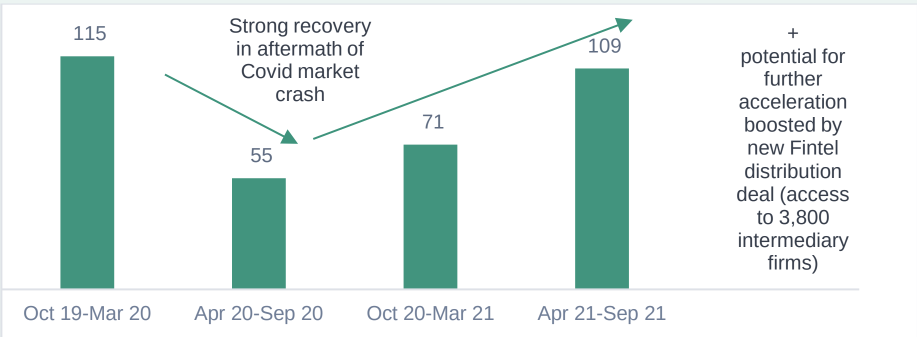
Strong organic growth triggers fair value increase

19 October 2021

AUM reached £10.8bn on 30 Sep 21, an increase of 20% in H1 (31 Mar 21: £9.0bn) and up 38% y-o-y (30 Sep 20: £7.8bn). We knew the acquisition of Verbatim funds had boosted H1 AUM by £650m, but net inflows were also stronger than expected, at £652m (99% up on H1 21: £328m).

Average monthly net inflows have recovered strongly since the Feb-Mar 20 Covid crash (when net inflows dipped across the asset management sector), doubling from £55m (six months to 30 Sep 20) to £109m (six months to Sep 21). Tatton has in fact been **one of the top performers in the sector when it comes to net inflows** (see page 3), and **we see further potential for inflows to accelerate**, especially as the new Fintel distribution deal (announced in Sep 21) - which provides access to an additional 3,800 intermediary firms - gathers momentum.

Average monthly net inflows, £m



Source: Company reports and updates, ED analysis

Market movements and investment performance also provided a boost to AUM, contributing £495m. **Paradigm, the group's IFA support services business, continued to progress steadily**. Mortgage client firms increased from 1,612 to 1,646 during H1 with completions up 30% y-o-y (from £5.0bn in H1 20 to £6.5bn). Consulting member firms increased from 407 to 418 during H1.

Fair value increases

On the back of higher-than-expected total AUM and net inflows, the potential to further boost inflows through the new Fintel distribution deal, and the value-enhancing price paid for the Verbatim funds, **we revise our core value from 410p per share to 560p per share.** Our revenue forecast for FY 22 increases from £26.3m to £28.1m and adjusted operating profit forecast from £12.8m to £13.7m.

Key Financials

Year-end 31 Mar	FY 19A	FY 20A	*H1 21A*	FY 21A	*H1 22E*	FY 22E	FY 23E
AUM end-of-period, £bn	6.1	6.7	*7.8*	9.0	*10.8*	11.4	13.1
Revenue, £m	17.5	21.4	*10.9*	23.4	*13.1*	28.1	31.7
Operating profit (adj), £m	7.3	9.1	*5.0*	11.4	*6.2*	13.7	16.3
Operating margin (adj), %	41.7%	42.5%	*45.6%*	48.8%	*47.2%*	48.8%	51.3%
EPS basic (adj), p	11.0	13.1	*7.0*	16.1	*8.9*	18.8	22.3
Div, p	8.4	9.6	*3.5*	11.0	*4.3*	13.0	15.5
Yield, %	1.7%	1.9%	*0.7%*	2.2%	*0.9%*	2.6%	3.1%
PER*	44.9	37.6	*35.2*	30.6	*27.7*	26.3	22.1
Net assets, £m	15.3	17.8	*20.0*	24.4	*25.0*	28.5	33.7
Net cash, £m	12.2	12.8	*13.3*	16.9	*15.0*	18.8	23.6

Source: Company Historic Data, ED estimates. PER and Yield based on share price of: ***493p***

**PER based on adj basic earnings (particularly relevant in FY21 due to extraordinary share-based pmt charge)*

Company Data

EPIC	TAM
Price (last close)	493p
52 weeks Hi/Lo	562p/250p
Market cap	£290m
ED Fair Value / share	560p
Proforma net cash	£15m
Avg. daily volume	60k

Share Price, p

Source: ADVFN

AUM on 30 Sep 21: £10.8bn

Description

Tatton Asset Management was founded in 2007 and serves smaller, UK-based Independent Financial Advisers via two distinct business units: *investment management* (discretionary fund management or DFM) delivered via WRAP platforms (just under 80% of group revenue), and *adviser support services* - regulatory and compliance consulting and outsourcing, plus mortgage and protection insurance aggregation (just over 20% of group revenue).

Next event: Interim results 17 Nov 21

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Revised assumptions and core value

Our previous valuation assumed that Tatton would attract around £1bn of net inflows per year for the next few years, and market movements would add a further 4% per year to AUM, with Tatton reaching around £15bn AUM by 2025.

Net inflows are currently ahead of this assumption (£652m in H1). In addition, in Sep 21 Tatton signed a five-year strategic distribution partnership with Fintel – a major support services and technology provider to financial intermediaries - which provides access for the distribution of Tatton funds and portfolios to 3,800 Fintel intermediary firms and 6,000 Defaqto users. **This deal has huge potential.**

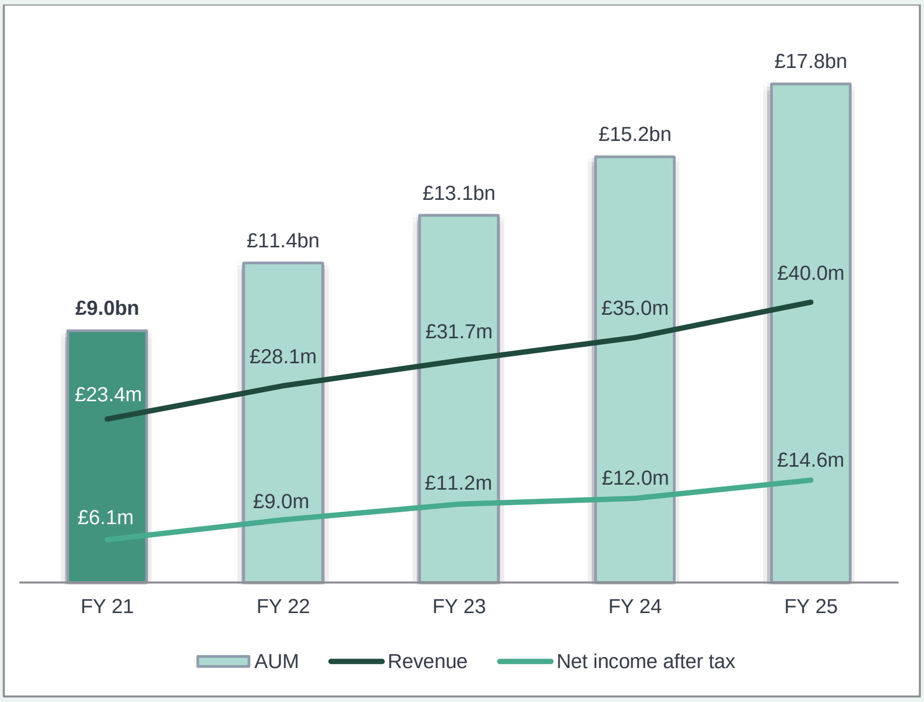
If Tatton makes even modest progress and converts say 500 firms as new clients in the five-year period, we estimate this would boost AUM by around £1.5-2.0bn (average of £3-4m per IFA), with the potential to add even more AUM in that time without winning more clients.

This is because when an IFA enters a relationship with Tatton, it typically moves only a small part of its client's assets to Tatton immediately (firms with less than a one-year relationship with Tatton have an average AUM of around £1.5m) but increases this over time (average AUM per existing IFA is around £10m for direct firms – a direct firm is an IFA that places its AUM with Tatton without being a Paradigm client as well. 'Dual client firms' have an even higher average of around £30m).

As such, we revise our growth forecasts (which are summarised below), and our core value to 560p. We do however remind readers that some volatility in AUM levels is inevitable as asset managers' AUM is correlated to market movements.

In addition, **Tatton is on the hunt for further value-enhancing acquisitions. It has a significant 'war chest' of £15m net cash and a £30m credit facility** (net cash was £16.9m on 31 Mar 21 but has now reduced because of the £2.8m first tranche payment for the Verbatim funds). We think finding reasonably valued or even under-priced opportunities to deploy some of this capital is a realistic expectation, and growth could be boosted even further.

Summary growth projections

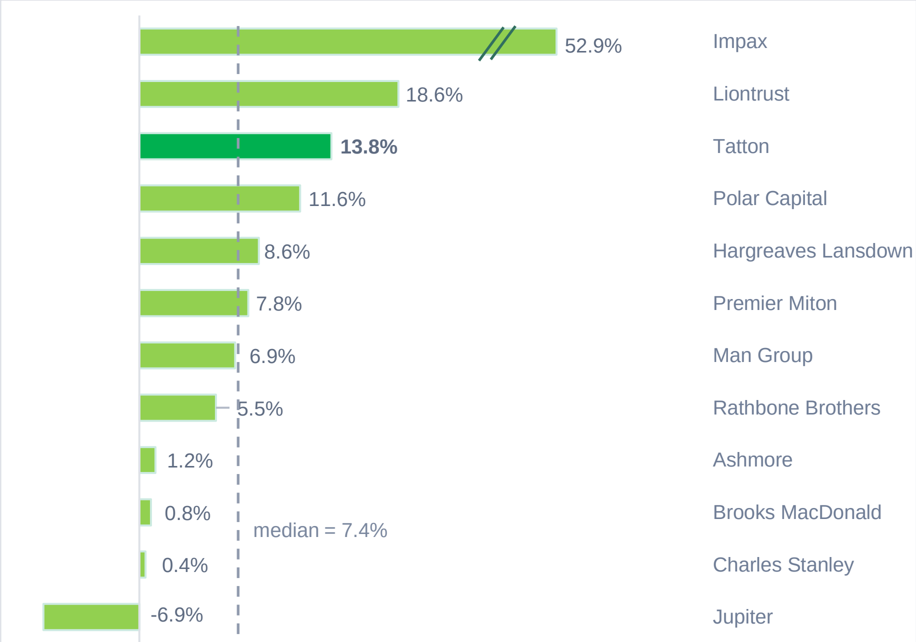


Source: Company Historic Data, ED estimates

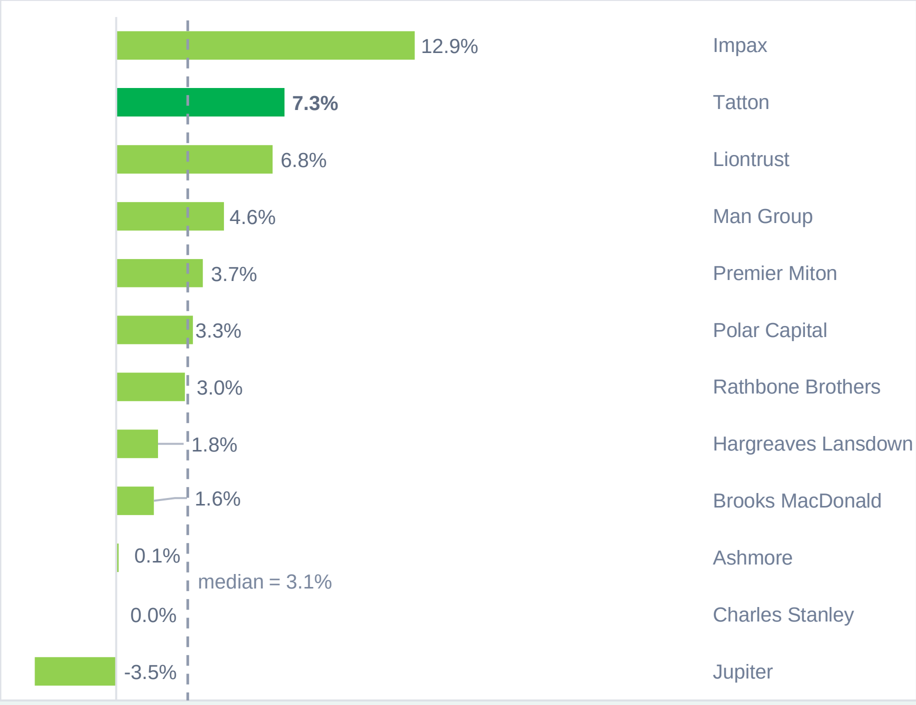
A growth leader compared to peers

It is also worth considering Tatton's recent growth performance (in particular net inflows which is a key value driver for asset managers) compared to peers. While not all asset managers and platforms we track had reported AUM for the period to 30 Sep 21 at the time of writing (St James's Place, Brewin Dolphin, AJ Bell, Quilter, River & Mercantile had not), it is clear that Tatton has been a leader when it comes to attracting assets. The charts below show a peer comparison of inflows for the 12m and 6m periods ending 30 Sep.

Net inflows as % of opening AUM, 12m to 30 Sep 21



Net inflows as % of opening AUM, 6m to 30 Sep 21



Source: Company reports and updates, ED analysis
Data excludes AUM from acquisitions

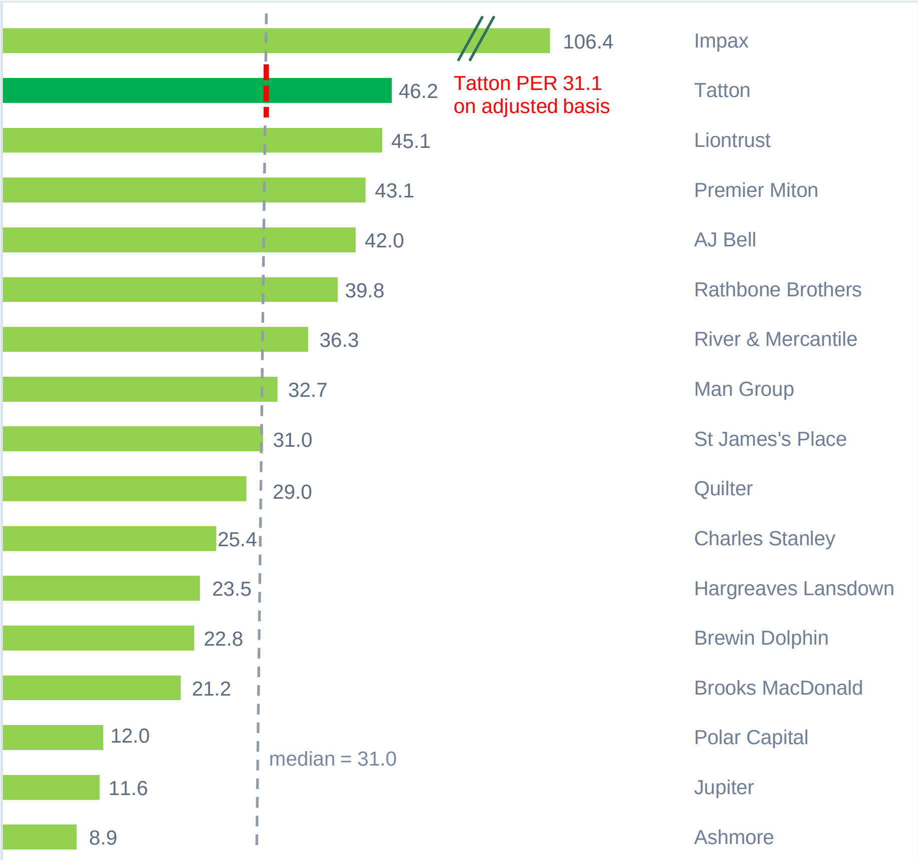
PER not particularly demanding

However, despite its growth leader status and growth opportunities, Tatton does not command a particularly demanding valuation rating compared to other asset managers and platforms.

While its PER using basic (non-adjusted) earnings is indeed in the top quartile of the peer group, we remind readers of Tatton's extraordinary share-based payment charge of £3.7m in FY21 which resulted in depressed basic earnings and inflates its PER (the FY20 charge was particularly high because Tatton did not release this charge in FY20 due to the prevailing uncertainty of the impact of the pandemic at the end of FY20 – this was then subsequently incurred in FY21).

Tatton's PER using adjusted earnings is 31.1, the same level as the peer group median.

PE ratios, UK-listed asset managers and platforms



Source: ADVFN
Data as at 15 Oct 21

We conclude that on a fundamental valuation and peer comparison basis, there is potential for further re-rating of the Tatton share price should it deliver on its growth potential.

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