Impax Asset Management Group

Delivering a sustainable future

4 December, 2017

Impax reported outstanding FY17 results and positive start to FY18. Momentum is being driven by organic growth and the proposed combination with US-based Pax World Management LLC, set to complete in Q1 2018. The latter only indirectly affected the FY17 result but is included in our proforma FY18e, and we will update our forecasts, and consider the sensitivities for the enlarged business after the transaction closes. The underlying outlook remains compelling: record 61% growth in assets under management or advice (AUM) in FY17 included **c £2.1bn of net inflows** and **£0.65bn from fund performance**. Total year-end AUM was **£7.3bn (FY16: £4.5bn)**, or £10.3bn including Pax.

FY17 results: AUM, fee income and operating profit growth

Strong growth in fee income and operating margins - revenue and adjusted operating profit (excluding non-recurring items) up 55% and 121% respectively - followed further outperformance by Impax's principal listed equity strategies (each has outperformed the global benchmark over one, three and five years) and a positive start by the new renewable energy private equity fund. Net inflows well spread by geographic source, confirm that Impax's direct marketing and distribution partners have traction in key markets across the USA and Europe.

Pax acquisition on track to complete in Q1 of 2018

We set out the potential benefits of the Pax purchase in our 28 September 2017 update. The deal delivers strategic growth on terms that should enhance EPS and dividend cover. Impax will pay up to US$90m via an initial US$52.5m and the balance in 2021 subject to performance. The operations are complementary, with aligned strategies and business cultures, and over a decade of successful partnership.

Valuation

We expect the addition of Pax to enhance EPS from FY19. Impax's recent share price performance means that the share based consideration should be priced above the 110p we'd assumed, so would be less dilutive. Impax's valuation still appears undemanding relative to prospects; well supported by AUM growth, fee income and cash generation; underpinned by further potential from a broadened offer/ distribution and cross sale opportunities. A proposed 2.2p final dividend is above forecast.

Forecasts

Year end 30 September	2014A	2015A	2016A	2017A	2018E[1]
Revenue, £m	20.4	19.7	21.1	32.7	54.6
Op. Profit, £m	5.3	3.1	4.2	7.9	14.5
EPS, p	2.8	3.1	3.6	6.2	8.1
PER	58.9	53.2	45.8	26.6	20.4
EV/NOPAT	36	81	53	22	16
Yield, %	0.8	1.0	1.3	1.8	1.9

Source: Company data, ED estimates (FY18 forecasts are proforma, with a 9-month contribution from Pax)

Company Data

EPIC	IPX
Price	165p
52 week Hi/Lo	172p / 50p
Market cap	£209m
Net cash (30 Sep 2017)	£20.4m

Share Price, p

Source: ADVFN

Description

Impax is a market leading manager of both listed and private equity funds, which invest in ways that take advantage of more environmentally sustainable corporate and economic growth globally.

Aggregate AUM at end October 2017 was £7.6bn.

The group has won many prestigious awards including:

THE QUEEN'S AWARDS FOR ENTERPRISE: SUSTAINABLE DEVELOPMENT 2014

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FY17 results

The strong FY17 performance built on the increasing appeal of consistent core fund performance and arguably more materially, their focus on an area of growing relevance to institutional investors globally. The Pax acquisition, due to complete next February, should build that profile in key markets i.e. extend the US footprint and potentially transform results.

Strong growth in revenues at improved margin

FY17 revenue growth, 55% up y-o-y at £32.7m reflected record net inflows into the group's listed equity funds, plus steady investment performance. Of the £11.6m reported y-o-y revenue growth, £9.6m related to listed equity flows and performance, c 75% of which was driven by net inflows. The year-end revenue run rate, excluding Pax, was £37.6m, equivalent to a 0.52% weighted average run rate revenue margin based on £7.3bn AUM. That compares with a 0.55% FY17 weighted average revenue margin (FY16: 57%). The fall reflects a changed mix of new business, towards lower-fee strategies distributed by intermediaries.

Private Equity revenue was also up, post successful fundraising for the newest fund (Impax New Energy Investors III), which also completed its first investments. Impax has raised over €300m so far. Fundraising will continue for a few more months, so ongoing discussions may add to that sum before it closes.

Summary income statement

Y/e 30 September	2016	2017	%
Assets under management	**£4.5bn**	**£7.3bn**	**+61**
Investment management & advisory fees	£20.6m	£32.5m	
Transaction fees	£0.5m	£0.2m	
Revenue	**£21.1m**	**£32.7m**	**+55**
Operating earnings	£4.2m	£7.9m	+90
Profit before tax	£5.2m	£5.9m	+13
Diluted EPS	3.62p	6.24p	+72
Shareholders' equity	£26.7m	£35.6m	+33
Interim dividend/share	0.5p	0.7p	+40
Final dividend/share (proposed)	1.6p	2.2p	+38

Source: Impax presentation

FY17 revenue growth was driven by significant organic growth. The group reported record inflows across all listed equity strategies, both Impax labelled products and those sold by its distribution partners globally. All principal Listed Equity strategies extended their strong performance record; each has outperformed the global benchmark (MSCI All Country World Index) over one, three and five years.

Record net inflows builds AUM to £7.3bn at year end

AUM was 61% ahead y-o-y at £7.3bn (FY16: £4.5bn), and £7.6bn at end October. The record net inflows of £2.1bn set out below were around four times that achieved in FY16, sourced across a range of strategies and geographies, and included one new material segregated account. Gross inflows for listed equity totalled £2.35bn vs redemptions of c £0.4bn, mainly related to churn within some of the underlying funds managed by the group, which are sold by distribution partners into the retail and institutional markets.

AUM movement by funds

£m	Listed Equity funds	Private Equity funds	Property funds	Total
1 October 2016	**4,195**	**285**	**22**	**4,502**
Net inflows	1,948	155		2,103
Market movement, FX and performance	645	11	-	656
30 September 2017	**6,788**	**451**	**22**	**7,261**
31 October 2017				**7,604**

Source: Impax RNS & website

Operational gearing - 121% growth in adjusted operating profit

The results illustrate the operational gearing inherent in a highly scalable business model. Underlying operating profit, excluding a non-recurring NIC charge (discussed below) was £9.3m (FY16: £4.2m), a 29% operating margin (FY16: 20%), or 31% based upon the period end run rate of £11.6m. A remuneration structure tied to business performance seeks to align the interests of staff and external investors. The strong FY17 resulted in materially higher variable remuneration costs, but underlying operating profit was 121% ahead, more than twice that for headline revenues.

The 47% increase in operating costs to £24.8m (FY16: £16.9m) was mainly due to an increase in profit-related remuneration (cash bonuses, equity awards and related NI) and placement agent fees associated with the current private equity fundraising. There was also a small increase in headcount and investment in the listed equity business operating systems, and other costs in anticipation of anticipated regulatory changes.

Breakdown of revenues by geography

Y/e 30 September, £'000s	2016	2017	%
Revenue			
UK	8,091	11,190	+38.3
RoW	12,976	21,504	+65.7
Ireland	1,711	1,694	-1.0
France	4,022	6,720	+67.1
Luxembourg	2,756	5,554	+101.5
Netherlands	1,566	2,094	+33.7
North America	2,133	4,611	+116.2
Other	788	831	+5.5

Source: Impax presentation

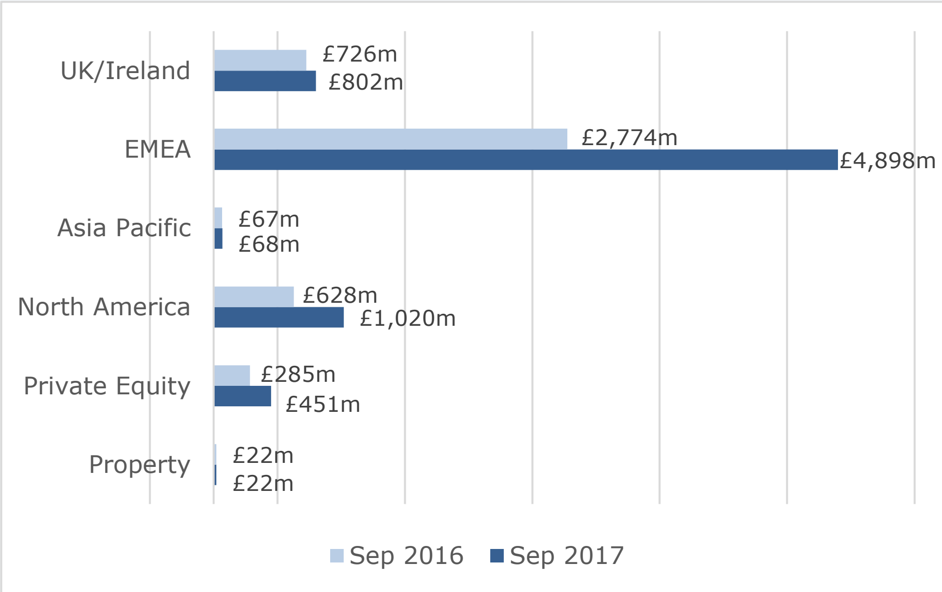
The geographical distribution is set out above. AUM for North America grew 62%, with further commitment to funds sub-advised by Impax on behalf of Pax in the US, and for NEI Investments and Desjardins in Canada, and an extended institutional client base. Impax also reported materially higher inflows via BNP Paribas Asset Management in Asia vs FY16.

European clients were another key source of new business. Growth included major allocations from **ASN Bank Netherlands**, which added £155m, and Impax's Danish distribution partner **Absalon Capital** (£134m more).

There were also strong subscriptions for products managed on behalf of BNP Paribas Asset Management, notably the water (Aqua Fund), sustainable food and agriculture (SMaRT Food Fund) and small cap (Climate Impact Fund).

As the chart below illustrates, the group has successfully extended its geographical reach and created a more balance portfolio, with the UK/Ireland now its 3rd largest source of investment funds:

AUM – Diverse sources of funds



Source: Company

Earnings per Share

Basic earnings per share (EPS) was up 79% at 6.48p (FY16: 3.62p), diluted EPS 72% higher at 6.24p (2016: 3.62p). That growth was broadly driven by operating earnings (equivalent to 4.33p/share), but there were moving parts. Negative adjustments totalled 3.26p/share, a combination of FX/fair value adjustments (net hedge losses on seed investments), acquisition costs and NIC on equity awards. Those were part offset by a positive 2.06p/share PE related tax adjustment. There was also a 0.51p per share dilution, associated with the share price rise over the year.

Headline result includes one-off costs and NI/tax adjustments

Impax reported c £1.0m of exceptional costs related to the Pax acquisition; we have assumed a further £0.5m will be incurred this year. Forex losses of £0.6m principally relate to US dollars purchased ahead of the Pax acquisition. Our FY18 figures incorporate costs related to the planned move to new office accommodation in London, modest additions to team complement to support business growth, and investment ahead of new regulation.

FY17 included a non-recurring, £1.4m increase in provision for NI contributions on employee share schemes. That was a mark-to-market appraisal of the NI cost following the significant rise in Impax's share price during FY17. Another £0.7m charge, assessed on the same basis related to legacy share incentive schemes.

Both were more than offset by adjustments to the corporation tax charge. An underlying £1.1m FY17 tax charge excluding non-recurring items, translated into a £1.8m tax credit, net of a £2.4m tax reclaim post clarification of treatment of historical income from the group private equity business, and a £0.5m CT credit related to mark-to-market equity awards. A further £2.5m CT credit on long-term incentive schemes was taken as a change in equity.

Strong balance sheet and cash generation

The group ended FY17 with a robust balance sheet, reflecting strong cash generation. The Pax acquisition makes efficient use of available resources, but still leaves cash in place for other corporate purposes.

Year-end cash was £20.4m, £4.1m of which is held as a risk buffer. Of the £16.3m balance, defined as 'available cash', the Pax acquisition will consume £8.0m and transaction costs another £1.5m. Assuming £0.9m is set aside for fitout of new premises and £1.0m for working capital, there is still £6.0m unallocated cash, net of option exercise premium/NIC.

Impax also secured two new debt facilities (total US$26m) from Royal Bank of Scotland in relation to the acquisition and general corporate purposes; a US$13m three-year term loan (LIBOR plus 2.9%) and a US$13 million five-year revolving credit (LIBOR plus 3.3%).

Summary balance sheet

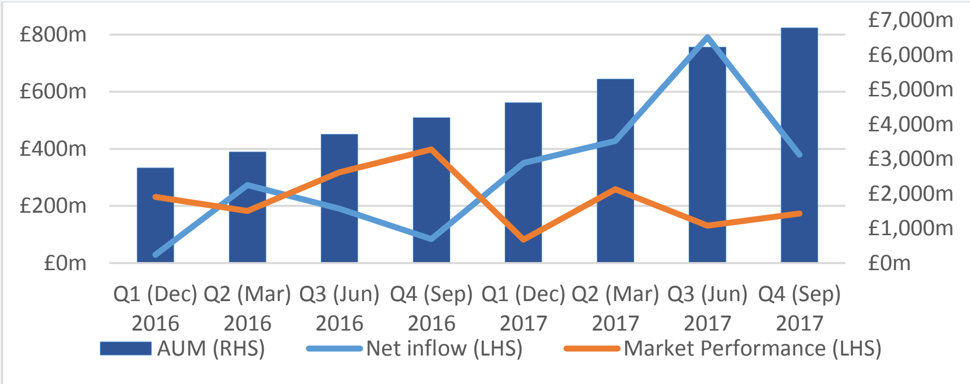
Y/e 30 September £'000s	**2016**	**2017**	**%**
Goodwill and intangibles	1,742	1,698	
Other non-current assets	122	464	
Deferred tax asset	0	1,947	
	1,864	**4,109**	
Cash and cash equivalents	15,695	20,712	+32
Current asset investments	12,811	13,010	
Other current assets	7,309	14,452	
Total assets	37,679	52,283	
Current liabilities	(9,998)	(16,308)	
Non-current liabilities	(936)	(331)	
Net assets	**26,745**	**35,644**	**+33**

Source: Impax presentation

Outlook – buoyed by organic growth and Pax acquisition

The shares have risen sharply, driven by record results in recent years and evidence that the group's funds and strategy have achieved substantial traction with key clients in target markets globally:

Impax AM - AUM growth, new investment and fund performance



Source: Company

Impax announced its proposed acquisition of Pax World Management LLC on 18 September. It set out what we believe is the sound strategic rationale to combine the two entities, to create the leading investment manager focused on the transition to a more sustainable global economy.

We examined that deal and the expected earnings enhancement from FY19 in detail in our last note. We shall publish with updated and extended (to FY19) forecasts when the transaction completes, anticipated before the end of Q1 2018.

The prospects for a highly scalable, operationally geared business to convert further organic growth in AUM into profit and cash will, we expect, continue to underpin the share price and rating.

FINANCIALS

P&L					
Y/e 30 September £'000s	**2014**	**2015**	**2016**	**2017**	**Proforma 2018e**
Revenue	**20,359**	**19,726**	**21,067**	**32,694**	**54,592**
Operating costs excluding legacy LT incentive schemes	(15,039)	(16,616)	(16,915)	(24,809)	(40,090)
Operating profit	**5,320**	**3,110**	**4,152**	**7,885**	**14,502**
Operating margin	26%	16%	20%	24%	27%
Credits/(charges) related to legacy LT incentive schemes	(539)	1,285	27	(653)	0
Exceptional acquisition costs				(999)	(500)
Fair value gain/(loss) on investments	(1,460)	615	989	(605)	0
Investment income	207	228	319	464	320
Finance cost					(678)
Change in third-party interest in consolidated funds	7	(101)	(288)	(239)	0
Profit before taxation	**3,535**	**5,137**	**5,199**	**5,853**	**13,644**
Taxation	(279)	(1,504)	(1,022)	1,814	(3,002)
Profit after tax	**3,256**	**3,633**	**4,177**	**7,667**	**10,642**
Profit attributable to owners of the company					10,212
Non-controlling interests					430
Profit after tax					**10,642**
Earnings per share					
Shares in issue (basic) k	117,314	115,133	111,794	111,251	116,439
Shares in issue (diluted) k	117,733	115,909	114,399	115,396	120,584
Basic EPS, p	**2.78**	**3.16**	**3.62**	**6.48**	**8.37**
Diluted EPS, p	**2.77**	**3.13**	**3.65**	**6.24**	**8.09**
Interim dividend	0.00	0.40	0.50	0.70	0.85
Final dividend	0.00	1.20	1.60	2.20	2.25
Dividends per share, p	**1.40**	**1.60**	**2.10**	**2.90**	**3.10**
Dividend cover	**1.98x**	**1.96x**	**1.74x**	**2.15x**	**2.61x**

Source: Company historic data, ED estimates

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