



Financials



Source: Refinitiv

Market data

EPIC/TKR	BUR
Price (p)	590.0
12m High (p)	1,870.0
12m Low (p)	585.0
Shares (m)	218.6
Mkt Cap (£m)	1,290
Total assets (\$m)	2,249
Free Float*	90%
Market	AIM

*As defined by AIM Rule 26

Description

Burford Capital is a leading global finance and professional services firm focusing on law. Its businesses include litigation finance and risk management, asset recovery, and a wide range of legal finance and advisory activities.

Company information

CEO	Christopher Bogart
CIO	Jonathan Molot
CFO	Jim Kilman
Chairman	Sir Peter Middleton

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www.burfordcapital.com

Key shareholders

Directors	8.7%
Invesco	9.5%
Morgan Stanley	6.1%
Coltrane Asset Mgt.	5.2%
Mithaq Capital	5.1%

Diary

24 Mar	Full-year results
13 May	AGM

Analyst

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BURFORD CAPITAL

Mixture of strong and weak activity in 2019

Burford recently released its first-ever trading statement, covering cash activity in 2019. Group-wide commitments set a new record of \$1.57bn, a 24% increase. Overall deployments were almost flat compared with 2018, at £1.07bn. In both, the Sovereign Wealth Fund (SWF) and fund arrangements increased their share. It was, however, a quiet second half for realisations on-balance sheet in the core litigation finance business. 2019 profits will be lower than in 2018, with Burford indicating that net realised gains will be ca.\$20m-\$30m lower than in 2018 and net unrealised gains ca.\$50m-\$70m lower.

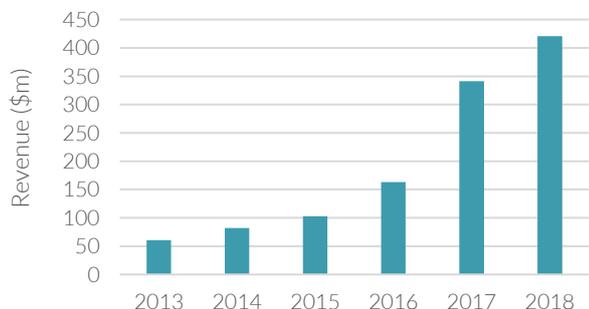
- ▶ **Returns:** While on-balance sheet net realised gains were lower in 2019 than in 2018, the cumulative RoIC since inception ticked up slightly to 93% on \$1.2bn of realisations (85% on \$1bn in 2018). The aggregate IRR also increased from 30% to 31%.
- ▶ **Cash:** Group-wide cash generation increased 23% over 2019 to \$997m. The majority of this increase was driven by post-settlement finance, which is shorter duration. The year-end cash balance of \$192m was slightly up from \$171m at the half year, but down on the \$277m a year ago.
- ▶ **Risks:** The investment portfolio is highly diversified, with exposure to more than 1,100 claims. However, it retains some very large investments, which means revenue could be volatile, particularly in the smaller divisions. The Petersen case shows that this volatility is not simply a negative.
- ▶ **Investment summary:** Burford has already demonstrated an impressive ability to deliver good returns in a growing market, while investing its capital base. As the invested capital continues to grow, we anticipate that the litigation investment business will continue to produce strong earnings growth.

Financial summary and valuation

Year-end Dec (\$m)	2013	2014	2015	2016	2017	2018
Revenue	60.7	82.0	103.0	163.4	341.2	420.7
Operating profit	42.5	60.7	77.2	124.4	285.1	353.0
Reported net income	2.6	45.4	64.5	108.3	249.3	317.4
Underlying net income	40.1	53.0	64.5	114.2	264.8	327.8
Underlying RoE	11.7%	12.1%	16.0%	22.1%	35.9%	30.1%
Underlying EPS (\$)	0.20	0.26	0.32	0.55	1.27	1.50
Statutory EPS (\$)	0.01	0.22	0.32	0.53	1.20	1.51
DPS (\$)	0.05	0.07	0.08	0.09	0.11	0.13
Dividend yield	0.2%	0.3%	0.4%	0.4%	0.5%	0.6%
NAV per share (\$)	1.72	1.87	2.12	2.22	3.19	5.50
P/E (underlying, x)	42.1	31.9	26.2	15.1	6.5	5.5
Price/NAV (x)	4.8	4.4	3.9	3.7	2.6	1.5

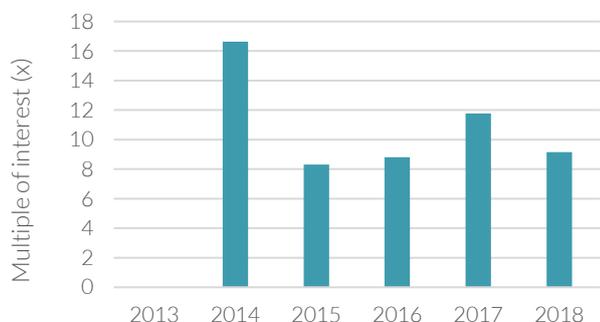
Source: Hardman & Co Research

Revenue



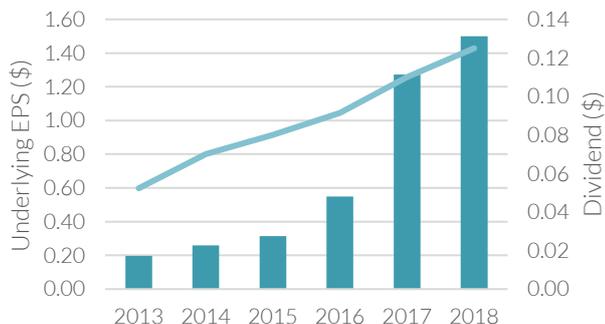
- ▶ Long-term growth has correlated strongly with the pace of investment and conclusions
- ▶ Accelerated investment from 2017 has boosted revenues
- ▶ 2017, 1H'18 and 1H'19 figures were boosted by sales from the Petersen case and the results of the Teinver claim
- ▶ New SWF arrangement will deliver a higher proportion of the returns on capital deployed, but has lowered Burford's capital deployment needs

Interest cover



- ▶ Retail bond issues in 2014, 2016, 2017 and 2018
- ▶ Cash needs and debt issuance are dependent on the rate of investment and the proceeds from realisations
- ▶ Interest cover is very strong, and Burford has ample capacity to issue further debt

EPS (bar) and DPS (line)



- ▶ 2017, 1H'18 and 1H'19 figures were boosted by sales from the Petersen case and the results of the Teinver claim
- ▶ Growth in the pace of investment has driven returns
- ▶ Some large, single claims have brought volatility, although this has been to the upside, as well as the downside

Source: Company data, Hardman & Co Research

Trading update

Burford's first-ever trading statement supplied information on its 2019 cash performance. The disclosure has differences from previous statements, which means that, while 2018 comparisons are provided, we do not have figures from earlier years for greater context. There are many positive aspects, with record commitments and robust cash generation. However, the second half appears to have been quieter than previous periods, and 2019 profits will be down on the 2018 figures.

Much of the change is clearer if split between Burford's balance sheet, investments funded by the Sovereign Wealth Fund (SWF, or BOF-C – as Burford denotes it) and Burford's funds.

Commitments and deployments

The total commitments of \$1,573m represent an increase of 24% over the 2018 figure of \$1,273m. Burford does note that some caution is required when looking at fund figures, as warehousing due to the SWF and BOF funding arrangement can lead to double-counting. On-balance sheet commitments were almost flat YoY at \$728m.

The core litigation finance business was strong, with a 30% increase (25% ex the holding of Petersen in BOF – see below), with the bulk of the growth allocated to the SWF arrangement. Burford's own balance sheet showed a 5% increase to \$429m. Burford cites an increase in corporate monetisation transactions as a source of growth.

Complex strategies showed a small decline, as the spare capacity from a year ago was filled, and new commitments can only be made by recycling the capital from realisations. Asset recovery, which is entirely on-balance sheet, saw a 44% increase in commitments to \$89m. Post-settlement finance, which only goes through a fund, saw a 78% increase to \$299m.

Deployments were more or less flat overall, at \$1,074m, with increased amounts in post-settlement finance offsetting decreases elsewhere. Despite the increased commitments, core litigation saw a 9% decrease, although the former should support deployments going forward. Burford highlighted that less than half of deployments came from the balance sheet, compared with 63% previously. It is worth reminding investors that Burford receives a significantly higher proportion of profits on SWF co-investments than the proportion of capital committed.

Returns and cash proceeds

Group-wide cash generation increased by 23% to \$997m. The bulk of this increase came in the funds, with on-balance sheet cash proceeds declining a couple of percent. On-balance sheet core litigation finance appears to have been somewhat quiet, with \$197m of cash generated, half of which was from the sale of 10% of the Petersen claim. The funds showed an increase in this area, which more than offset this.

Both complex strategies and post-settlement finance posted increases. The former likely reflects the full deployment of the available funds. The post-settlement business is inherently shorter duration and links directly to the increased deployments in the new fund. Asset recovery showed a decline; given the small number of cases involved, this line is expected to remain volatile. No information was given about the insurance operation.

Investment management fees rose 25% to \$20m. No information has been supplied about performance fees but, given the increased FUM in 2019, it seems likely that the bulk of the increase is from management fees.

Returns

Burford's cumulative return statistics for the core litigation investments on the balance sheet improved a little over 2019, with the RoIC increasing to 93% from 85% a year earlier and the IRR moving from 30% to 31%. With the Petersen sale being over half the cash balance sheet returns and being stellar on both metrics, it is likely the other investments produced more pedestrian returns in aggregate. This year's cash returns increased the aggregate by almost 20%.

Burford highlights that 2019 saw a very low level of realised losses of \$6m. This compares with \$21m in 2018 and is the lowest level of realised losses that Burford has ever experienced, which, given the rapid portfolio growth since its early years, is genuinely notable. It suggests that Burford's observation about this being a quiet year, rather than a bad one, is correct, although we note that no comment has been made about unresolved investments.

Cash balances

The cash on the balance sheet has increased since the half year, but has reduced from a year earlier. Cash and cash management investments totalled \$192m, compared with \$171m six months earlier and \$277m at the end of 2018.

Over the year, on-balance sheet cash proceeds exceeded deployments by \$35m, but expenses and interest costs would have had to be funded too (\$66.8m and \$38.5m, respectively, in 2018).

From the conference call, we note that the desire to raise further debt funding remains in place. The timing and potential size remain uncertain, although the indication was that a US Dollar issue would be preferred. Some options would require the release of the annual results.

Profits

Although the valuation process is not complete, Burford expects its net realised gains to be ca.\$20m-\$30m lower than in 2018 and net unrealised gains to be approximately \$50m-\$70m lower. It thus expects profits to be lower in 2019 than in 2018.

The 2018 accounts gave net realised gains of \$155.1m, and fair-value movement was \$232.1m. With the 1H'19 figures at \$124.8m (\$139.5m before elimination of third-party funds) and \$134.7m (\$152.9m), respectively, it can be seen that activity in 2H'19 does seem to have been particularly quiet.

Burford's management has consistently stated that it has no control over the timing of investment realisations (something Muddy Waters failed to grasp in its latest note), and it is likely that, at some point, there will be a quieter period. It would seem that this happened in 2019, particularly in the second half. The low loss rate does suggest that this was simply a period in which there was less realisation activity than in earlier years.

Management highlighted that January 2020 saw much higher activity than usual. There have been litigation successes, which, if upheld and paid, would bring \$150m in group cash profits and \$100m to the balance sheet. These appear to be a mixture of judgments and settlements, with the latter likely to give quicker realisations.

This also supports Burford's assertion that 2019 was simply a slow period. The January activity would have given a materially higher 2019 profit figure had it happened a month earlier, although we note that the fair-value adjustment on these investments would be lower than the headline profit figures.

Un-muddying the waters

There were signs that, having made a substantial profit out of its short attack last summer, based on poorly substantiated accusations, Muddy Waters had largely moved on to other matters. However, it has published a brief report based on the trading statement.

Muddy Waters seems to believe, despite Burford's consistent statements to the contrary, that the group has some control over timing of realisations, which does not help the former's credibility. It is not clear that Burford is "under significant pressure to show it could monetize cases", other than the continual, ongoing desire to be successful. Muddy Waters perhaps overstates its influence on management.

As noted above, the second half was very quiet, and Muddy Waters was correct on this point. Its highlighting of this later in the report on using realised gains appears to simply reiterate the same point in a different way.

On the 2019 Petersen sale, Burford appears to be constrained by purchase agreements from being absolutely clear on what happened. The Hardman & Co understanding is as follows: the Limited Partnerships (LPs) in Burford's funds expect to be offered other opportunities when available, and, when Burford was considering the Petersen sale, they had the chance to participate. The LPs decided as a group to participate, with the decision made by the LP committee for BOF (which is independent of Burford).

In the table of investments to 30 June 2019, it can be seen that 191144 is a North American energy investment for \$30m. This is the only investment in the first half that was allocated to BOF, but not SWF.

As has been often repeated, the purchasers on the other side were institutional investors with the capacity to commit millions of pounds to a single case, and they should be seen as sophisticated. The investment was also oversubscribed. Both these factors suggest that the price was acceptable to the "market". Burford influenced the price in that the transaction would have taken place only if it had been acceptable to it as well. There is no evidence of wrong-doing here. Ideally, Burford could have been clearer with the market, although the sale agreements appear to have prevented that.

The call to disclose the mark-to-market on Petersen is simply noise. To do this would risk influencing the case, and so is clearly not in Burford's interest. The issues about potential repayment seem to be noise as well, as Burford's disclosures last September discussed. The Argentinian government has been getting consistent support from its press, and it seems likely that there will be much more speculation to come before this case is finally resolved. However, we continue to note that this is a single case and, even if the odds are in Burford's favour, a wide range of outcomes, both positive and negative, remain possible.

The point on cash appears unfounded. As outlined above, combining the figures from the trading statement and 2018 expenses gives a rough match for where the latest cash figure is. There is no mystery to resolve.

Its final point about the Perry Ellis case seems overblown. While complex strategies may be lower-risk, they are not "no risk". The failure of one case does not invalidate the strategy in an area that seems to be nicely profitable. It also misses a point that, in many complex strategy matters, there is a return of principal, even if the litigation is unsuccessful.

Disclosure

Burford has committed to significant changes in the presentation of the 2019 results, and some of this will be brought to the 2018 results too, so that comparisons can be made. We look forward to the new information.

Financials

Summary financials						
Year-end Dec (\$m)	2013	2014	2015	2016	2017	2018
Revenue	60.7	82.0	103.0	163.4	341.2	420.7
Expenses	18.1	21.3	25.8	39.0	52.3	66.8
Operating profit	42.5	60.7	77.2	124.4	285.1	353.0
Finance costs	0.0	3.7	9.3	14.1	24.3	38.5
Exceptional items	-40.4	-9.7	0.0	-5.9	-3.8	0.0
Reported pre-tax profit	2.1	47.3	67.9	104.1	249.2	305.0
Reported taxation	0.5	-0.7	-2.2	4.8	0.1	12.5
Minorities	0.1	1.2	1.2	0.6	0.0	0.0
Underlying net income	40.1	53.0	64.5	114.2	264.8	327.8
Statutory net income	2.6	45.4	64.5	108.3	249.3	317.4
Underlying basic EPS (\$)	0.20	0.26	0.32	0.55	1.27	1.50
Statutory basic EPS (\$)	0.01	0.22	0.32	0.53	1.20	1.51
DPS (\$)	0.05	0.07	0.08	0.09	0.11	0.13
Balance sheet (@31 Dec)						
Total equity	351.5	382.7	433.1	462.2	664.5	1,202.7
Invested capital	173.6	207.5	252.9	394.3	631.4	902.0
Fair value balance	214.9	266.8	334.2	559.7	982.2	1,480.2
Total assets	376.1	533.2	608.7	968.2	1,318.0	2,127.3
NAV per share (\$)	1.72	1.87	2.12	2.22	3.19	5.50
Underlying RoE	11.7%	12.1%	16.0%	22.1%	35.9%	30.1%

Source: Hardman & Co Research
£1=\$1.25

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The full detail is on page 26 of the full directive, which can be accessed here: <http://ec.europa.eu/finance/docs/level-2-measures/mifid-delegated-regulation-2016-2031.pdf>

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