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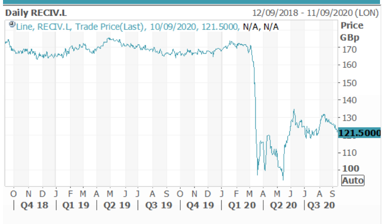
Diversified Financial Services



Source: Refinitiv

Market data

EPIC/TKR	**RECI**
Price (p)	**121.5**
12m High (p)	175.5
12m Low (p)	94.4
Shares (m)	229.3
Mkt Cap (£m)	278
NAV p/sh (p)	145.8
Discount to NAV	17%
Market	Premium Equity Closed-Ended Inv. Funds

Description

Real Estate Credit Investments (RECI) is a closed-ended investment company that aims to deliver a stable quarterly dividend via a levered exposure to real estate credit investments, primarily in the UK and France.

Company information

Chairman	Bob Cowdell
NED	Susie Farnon
NED	John Hallam
NED	Graham Harrison
Inv. Mgr.	Cheyne Capital
Head of Team	Ravi Stickney
Main contact	Richard Lang
	+44 207 968 7328
	www.recreditinvest.com

Key shareholders (31/03/20)

Close Bros	8.55%
AXA SA	8.50%
Premier Miton	8.09%
Bank Leumi	7.82%
Fidelity	7.59%
Canaccord Genuity Group	7.36%
Smith and Williamson	6.84%

Diary

Early Oct	Sep Factsheet
Nov (tbc)	Interim results to Sep'20

Analysts

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REAL ESTATE CREDIT INVESTMENTS

Improving returns on new opportunities

RECI released its *quarterly investor update* on 17 August and factsheet on *8 September*. This note updates investors with the key developments in both these documents. The key messages are i) robust performance of existing portfolio through COVID-19, ii) full interest and capital repayments expected on bond portfolio, iii) strong volume in investment pipeline, iv) lower-risk business is being added, v) pricing on new business 2%-5% above pre-COVID-19 levels like-for-like, vi) low gearing, and vii) stable dividends. All this appears anomalous with the 17% discount to NAV.

- **Current portfolio:** Realised losses have been 1% of NAV, reflecting Cheyne's strong credit assessment and security. Some borrowers have extended facilities (at an appropriate interest cost) but, also, there have been early repayments. We understand all borrowers are paying in full and on time on their (revised) terms.
- **New business:** Against these realised losses, new business pricing has widened and terms have improved. The extra value of new business to be added is likely to exceed realised losses, implying that the overall value of the company should have risen. This may be valued by investors as stable returns reduce uncertainty.
- **Valuation:** RECI trades at a large discount to NAV, in line with its secured lending peers. Its dividend yield, at 9.9%, is the highest of its immediate peers and above wider peer averages. RECI showed its confidence with an accelerated dividend declaration (3p, unchanged on prior quarter) and "stable" dividends going forward.
- **Risks:** Any lender is exposed to the credit cycle and individual loans going wrong. Security is currently hard to value and to crystallise. We believe RECI has appropriate policies to reduce the probability of default and the loss in the event of default. Some assets are illiquid, and Repos financing has a short duration.
- **Investment summary:** RECI generates an above-average dividend yield from well-managed credit assets. Management has confirmed no change to dividend policy, showing its confidence in its sustainability. Bond pricing includes a discount, reflecting uncertainty, which should unwind when conditions normalise. Market-wide credit risk is currently above-average, but RECI's strong liquidity and debt restructuring expertise should allow it time to manage problem accounts. Borrowers have, to date, injected further equity into deals.

Financial summary and valuation

Year-end Mar (£m)	2016	2017	2018	2019	2020	2021E	2022E
Interest income	17.7	15.3	18.4	22.3	26.4	32.1	37.6
Operating income	15.1	15.7	20.6	25.3	-10.4	36.3	42.1
Management fee	-2.0	-2.0	-2.6	-3.0	-4.1	-4.4	-4.6
Performance fee	-0.2	-0.1	-0.3	-0.7	1.0	0.0	0.0
Operating expenses	-3.1	-3.2	-3.7	-4.8	-5.6	-5.4	-5.6
Total comp. income	8.5	9.1	14.9	19.2	-17.4	30.2	35.8
EPS (p)	11.7	12.4	13.0	13.1	-8.7	13.7	13.3
NAV per share (p)	163.2	163.2	164.0	165.1	147.0	148.2	151.1
S/P premium to NAV	-26%	-26%	-26%	-26%	-17%	-18%	-20%
Debt to equity	35%	29%	34%	40%	29%	14%	11%
Dividend (p)	11.6	11.1	12.0	12.0	12.0	12.0	12.0
Dividend yield	9.5%	9.1%	9.9%	9.9%	9.9%	9.9%	9.9%

Source: Hardman & Co Research

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COVID-19

August update – key issues

Unprecedented fiscal and monetary stimulus

RECI noted the dramatic impact of the unprecedented fiscal and monetary stimulus measures across the UK and Europe. This has created an unprecedented amount of money raised for corporate bond opportunities, with record inflows to corporate credit funds and a rapid reduction in stress in bank funding. These, in turn, have seen a material reduction in yields for corporate bonds – particularly high yield bonds. Indeed, junk bonds have rallied by more than 20% from their trough, to leave them broadly unchanged on the year, even though they have material energy exposure.

Impacted many debt markets, but not real estate lending, where spreads remain wide because of limited supply of finance

However, in contrast to the significant reduction in yields for the wider fixed income markets, the yields for European real estate debt markets remain persistently wide. We believe this is driven by three factors: i) for banks, historical losses mean this is an area treated with extreme caution, and so this area will be the last they return to aggressively; ii) all funders have typically been focused on managing their existing books, devoting more resource to negotiations with borrowers than chasing new business; iii) non-bank lenders have not been raising equity/have had their own debt financing constrained, and so have not been chasing new business. We expect these factors to slowly unwind but, for the moment, they present excellent opportunities for those lenders with capacity.

Company's recent response to crisis

Since the May update, the company has made the following comments:

"Successfully engage with its sponsors/ borrowers towards further de-risking its investment book"

- "RECI's borrowers are mainly large, well-capitalised and experienced in dealing with periods of stress. Where necessary, RECI has sought a de-risking of its position (typically via additional equity capital injections) in exchange for the allowance of time and framework to address the ongoing crisis. At present, none of the loan book is in material default. We are comfortable that the investment book is capable of withstanding a long-term recession brought about by the pandemic. We have no concerns with the credit quality of the remaining book.
- We also are pleased with the continuing timely receipt of interest and repayments on loans:
  - Loan three (in the Top 10) partially repaid its balance ahead of schedule, realising £8.3m of cash.
  - A further four positions are now expected to repay (in full or in part) over the remainder of 2020, providing a further cash inflow in excess of £40m to the Company.

"Significantly improve its resilience and flexibility to both defend against uncertainty and to capitalise quickly on opportunities that arise"

- To this end, the net leverage of the Company today is 5.4% of NAV.
- The cash balance has risen to £53m as at 31 July 2020.

"Identify a new pipeline of investments, at significantly improved risk & return parameters, that will work towards improving the income profile of the Company"

- Cheyne Capital has generated a large new pipeline (post May 2020) spanning more than 15 deals, which are mainly focused on senior lending at rates that are 2%-5% higher than those in its February pipeline, giving an IRR of 10%+
- Of these, seven deals (six senior, one mezzanine) are due to close in this coming quarter. These deals are underwritten to an LTC of around 60% and returns that are more than 10% in each instance. The total commitments across these

deals in closing is £305m. RECI is eligible to participate in these deals alongside Cheyne Capital.

"Improve investor communication"

- Improve our investor communication and enhanced transparency in our reporting, with the detailed review of the loans in the book at our last report, and worked on closing the gap between the NAV and share price, which has shown some success."

Hardman & Co comment: focus on management's comment, "no concerns with the credit quality of the remaining book", backed by actual cash receipts

Hardman & Co comment: The measures taken are what we would expect – a detailed interaction with existing clients to establish their risk profile, and stress-testing their cashflow assumptions and actively managing liquidity. The discount to NAV, we believe, indicates investor concerns about credit quality, which clearly are not consistent with management's expectations. The statement, "we have no concerns with the credit quality of the remaining book", made after detailed discussions with borrowers and backed by actual cashflows from repayments, may help allay some of these concerns.

Full repayments expected on bonds

Full repayment expected on bonds, with extra interest to compensate where re-scheduling has occurred

Throughout the crisis, RECI has advised that it expects to receive full repayment on both interest and principal on its exposure to bonds. There has been considerable sentiment-driven mark-to-market volatility, which RECI's NAV captures, but, over time, full repayment is expected. We understand this does not mean that all repayments will be made as originally contracted but, where bond terms have been amended (e.g. extended), interest is due on these, re-scheduling at an appropriate level for the risk, and this extra interest is expected to be paid.

Mix of business improving returns

Improved new business pricing

We understand that new business is 2%-5% above pre-COVID-19 levels for like-for-like risk.

Further 10% of lower-margin historical business expected to be repaid by end-2020. Weighted average life of loans just 1 year.

The aggregate return will be impacted by changes in the existing book. There will be drawing under existing commitments (£5.4m drawn in 1QFY'21) but, relative to new commitments, these low-spread drawdowns are expected to be modest. They may also be impacted by repayments, and the weighted average life of loans is just 1 year. We understand that, following the quarter end, the third largest position, a mixed-use development asset in London, started repaying ahead of schedule, realising £8.3m of proceeds to RECI. Additionally, a further four positions are now expected to repay (in full or in part) over the remainder of 2020, providing RECI with a further cash inflow in excess of £40m. It is worth noting that, since 2012, all realisations have achieved or exceeded expected returns, and this is expected from the above deals.

Low gearing

Net leverage was reduced from 13.3% of equity at end-March to 6.4% at end-August. RECI's current facilities are in Repos where monetary stimulus saw stress rapidly removed, and we understand that there is a strong potential supply from the existing financer and others. To take advantage of this line, RECI would need to invest in bonds (rather than non-repos-able loans), and we understand that the pipeline for bond acquisition is strong. Additionally, it is looking to extend the duration of its Repos from three months to six months.

In the past, RECI has also talked about alternative debt financing, including both on- and off-balance sheet options. We also understand that RECI is in advanced discussions to get long-term, non-recourse financing secured against specific loan assets. By way of example, in its July Factsheet, RECI noted the successful financing of the loan to the Paris prime residential/retail asset (portfolio position 1).

Confidence in liquidity shown by continued dividend payments and FX hedging

We note that, in March, RECI maintained its FX hedges (net cash outflow for margin calls £9m) and paid a dividend (cash outflow £7m). The facts that both are discretionary and that RECI chose to continue the payments are indicative of the confidence it has in own liquidity.

Stable dividends

RECI declared its first interim dividend of 3.0p per share for the year ended 31 March 2021, which was paid on 30 July 2020. Importantly, this was nearly 1.3x covered, with a total NAV return of 3.8p in 1QFY'21.

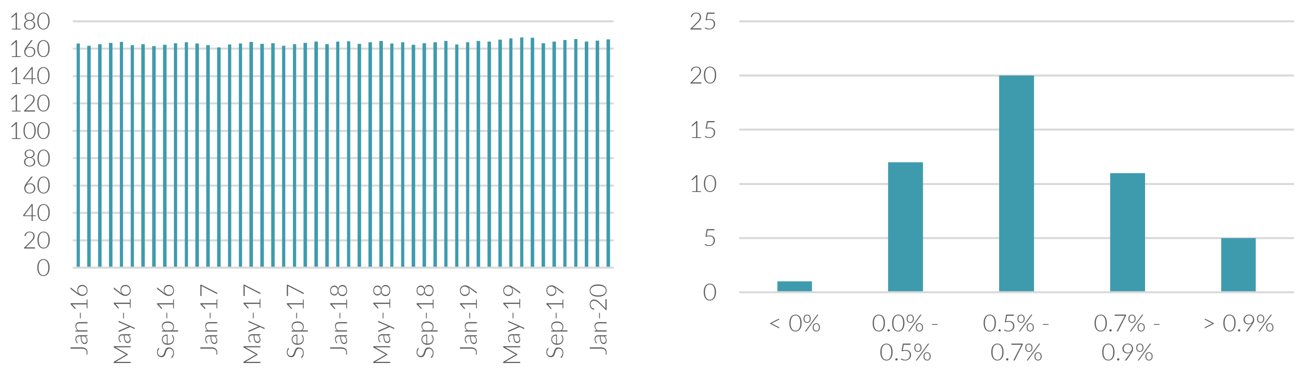
The company also confirmed that there would be no change to its dividend policy for the current financial year ending 31 March 2021, and that it intended to continue to pay a stable quarterly dividend.

Previous resilience of the portfolio

Portfolio returns driven by predictable cashflow, supporting incredibly stable NAV

As can be seen in the updated charts below, consistency of performance has continued to be delivered, with sustained stability in NAV (left-hand chart), and two thirds of the monthly performance since January 2016 has been between 0.5% and 0.9% (all five of the past five months have been in the most frequent 0.5%-0.7% monthly NAV accretion bucket). RECI has continued to pay a 3p quarterly dividend, as it has every quarter since 3Q'17.

Monthly NAV (p, LHS) and number of months, Jan'16–Feb'20, by monthly return (RHS), both dividend-adjusted



Source: RECI Factsheets, Hardman & Co Research

Resilience does not come about by accident. Reflects culture, benefit of hard security, diversification, resource committed to ongoing monitoring and market knowledge.

We covered the reasons why RECI has delivered such a performance in our initiation report. As a brief summary:

- The manager's (Cheyne's) lending culture is hugely important.
- There is clear independence between risk-sanctioning and deal-origination.
- The Board is strong, independent and experienced.
- Property security reduces both the probability of default and the loss in the event of default. The weighted average LTV across the whole portfolio is 63%. Under 5% of loans are at 80%+ LTV.
- The portfolio is diversified (now 53 positions). Italy now represents 4.9% of the portfolio, down from 7.1% six months ago.

- Positions appear to be closely monitored once committed.
- Cheyne gives i) economies of scale, ii) specialist credit and structuring skills, iii) access to new deal flow, and iv) market knowledge and relationships.
- The mix of bonds and loans is likely to provide greater liquidity than a book of loans alone.

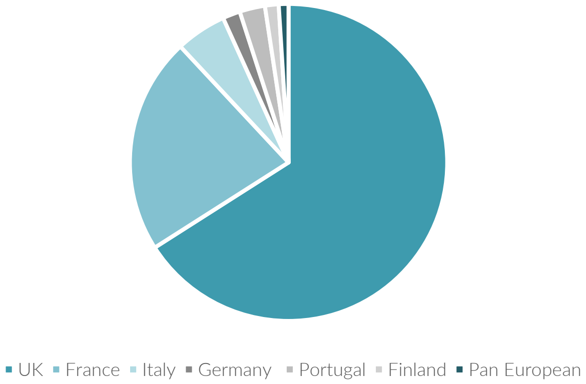
Latest portfolio

Key messages of good diversity, strong asset backing, balanced geographical mix and robust yields all remain unchanged

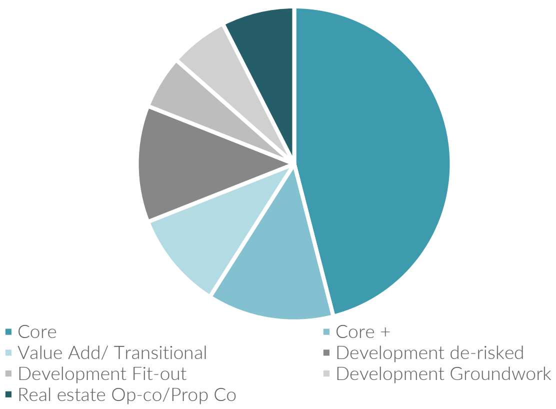
The overall key messages of good diversity, strong asset backing, a balanced geographical mix and robust yields all remain unchanged. The bond portfolio risk has reduced. The August portfolio key statistics are:

- The number of positions is 49, with 23 loans and 26 bonds. The top 10 are £290m of commitments (£208m drawn), and represent 87% of NAV.
- The weighted yield is 10.8% (February 2020 8.6%), with an improving weighted LTV (63.1% against February's 64.7%). Of note, the average unlevered yield on the bond portfolio is 10.1%, against a low of 3.2% in February 2020.
- The loan book average life has been gently declining (now 1.0 years, February 1.3 years), while the life of bonds is 3.6 years (February 1.4 years). The latter reflects restructuring, as well as new positions.
- The UK remains the main exposure.

Portfolio concentration by geography (%)



Portfolio concentration by asset type (%)



Source: RECI August Factsheet, Hardman & Co Research

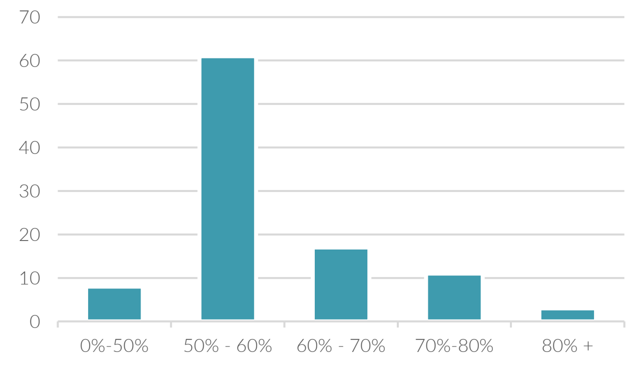
Loan portfolio

The key statistics for the loan portfolio are given below.

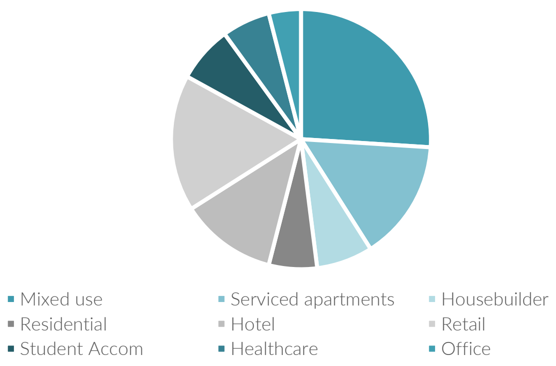
Loan portfolio	End-Aug'19	End-Feb'20	End-Aug'20
Number of assets	17	25	23
Drawn value (£m)	163.7	311.8	281.2
Undrawn commitments (£m)	60.1	62.7	58.9
Weighted average yield	9.2%	8.3%	10.1%
Weighted average LTV	66%	66%	65%
Weighted average life (years)	1.6	1.3	1.0

Source: RECI Factsheets, Hardman & Co Research

Loan book LTV breakdown (%)



Loan book sector breakdown (%)



Source: RECI August Factsheet, Hardman & Co Research

Investors should note that RECI re-categorised some self-originated bonds into loans in 2020 to improve the transparency of self-originated bonds against third-party bonds. This has seen growth in retail loans to around a sixth of the loan book, having been around 5% at end-February. There is no change in RECI's exposure – just a classification issue.

Public market bond portfolio

Bonds invested are typically senior-secured (first-lien) credits, with conservative LTV collateralised by core and core+ assets owned by large institutional borrowers. RECI actively trades its bond book for relative value, and also for the efficient management of liquidity in the company overall. Since earlier in the year, risk has been reduced through lower LTVs, while the yield has been improved.

Bond portfolio

	End-Aug'19	End-Feb'20	End-Aug'20
Number of assets	33	28	26
Fair value (£m)	168.2	99.2	61.5
Weighted average unlevered yield	6.1%	3.2%	7.0%
Weighted average levered yield	8.3%	8.5%	11.3%
Weighted average LTV	61.8%	60.4%	53.3%
Weighted average life (years)	2.4	1.4	3.6

Note: There has been a reclassification of some self-originated bonds into loans
Source: RECI Factsheets, Hardman & Co Research

Top 10 exposures

The top 10 positions are detailed below. Eight of the top 10 are senior loans, one is a senior bond, and one is a mezzanine loan (number 8). The lower risk profile of senior loans is evidenced by the fact there were no writedowns of senior positions in March.

Top 10 commitments (end-Aug'20)	Commitment (£m)	LTV (%)	Manager commentary
Paris prime resi/retail building	48.9	67	Income-producing prime central Paris retail and residential (for rent).
UK mixed-use portfolio	38.0	58	Income-producing granular UK portfolio (mainly residential for rent and sale, offices, light industrial).
London mixed-use development	34.8	45	Completion reached on time in Jun'20. Ongoing partial repayments from sales income. Full repayment anticipated ahead of maturity date.
Lisbon aparthotel	34.6	63	Development in progress. Expected completion early 2022.
London mixed-use development	27.2	64	Substantially complete (delivery scheduled for Dec'20), partially pre-let.
Cambridge serviced apartments	25.4	65	Development in progress. Expected completion 4Q'21.
UK care homes	23.2	73	Stable, income-producing UK care homes. This exposure is a bond.
UK student housing*	22.4	78	Stable income-producing UK student accommodation assets.
London office to residential	20.0	36	Development completed. Residential pre-sales at 20%. Commercial accommodation fully let.
Office development in Bagnolet, Paris suburbs	15.0	59	Construction works in progress. Expected completion 4Q'22.

**Mezzanine loans; Source: RECI Factsheets, Hardman & Co Research*

We detailed in the section, *Nature of borrowers*, in our initiation report, RECI's comments on most of these exposures. In terms of additional comment:

- **Paris prime residential/retail building:** This property is on one of Paris's premier roads (Avenue Montaigne), where RECI expects market values to be robust. It is partially subject to renovation and some delays before it becomes fully income-generating, but the documentation includes a make-good clause to ensure that the IRR is maintained. As noted above, RECI successfully raised external finance secured on this loan. We note that the backer is a high-net-worth family, which should be in a position to inject further equity as required.

- **UK/London mixed-use portfolio:** We note the quality of the borrower (large corporate), the low LTV for senior secured facilities and the mature state of assets.

- **Lisbon aparthotel:** We note that only a small part of the £35m commitment has currently been drawn. The residual amounts are likely to be taken only as the business plan progresses, with the amounts drawn down measured against "project monitor" reports. The potential cash calls have been fully built into projections in RECI's liquidity modelling.

- **London mixed-use development:** We note that the backer is private equity (PE), with capacity to make further equity injections, as required, and that the development is close to completion.

- **Cambridge serviced apartments:** The development is still at an early stage (so limited drawdown to date), with material borrower equity already injected. Delays to completion may be expected, but we understand that there are make-good clauses in the contract. We would expect Cambridge to be a relatively resilient location.

- **UK care homes:** It is currently unclear what the long-term financial dynamics for care homes will be in the UK. It is probable that costs will be higher, with a greater focus on hygiene, and the appetite over the next few years for families to put elderly relatives into a home, given the recent death rates, is unknown. Additionally, there is the risk of litigation. There have been multiple press comments on care companies fearing bankruptcy (e.g. BBC). For RECI's specific exposure, we note RECI's comments about dependency on local authority payments, good-quality reviews and occupancy remaining over 90%.

- **UK student housing:** We note that the LTV is quite high (78%), and it is also a mezzanine loan. We believe there are uncertainties, both positive and negative, in the near term. Of note, it is unclear how many foreign students will be coming to the UK, how much rent will be paid when students are absent from college, whether students will take gap years and, as happened post the Global Financial Crisis (GFC), how many people will take up further education if there a fewer jobs available. We note that the quoted Unite (ticker UTG) has seen its share price fall from 1,342p in mid-February 2020 to a low of 634p in mid-March, before recovering to 961p currently. We also note the outlook comment, in its end-July interim results, with reservations for the 2020/21 academic year at 84% (2019/20: 93%). It is targeting 90% occupancy for 2020/21, resulting in a 10%-20% anticipated reduction in rental income compared with 2019/20. We believe the Russell Group university exposure is likely to be below-average risk for the sector. Management has also commented that its discussions with the borrower have included mitigating action, such as offering the accommodation on short-term lets, should there be a shortfall of foreign students. We understand that the borrower intends, and is currently able, to put in cash to ensure that the loan can be kept current through to the next academic year, if required.

- **London office to residential:** The low LTV should give some protection here.

- **Office development in Paris suburb:** This is a new entry in the top 10, and so we have given more detail below than for the other exposure:

  - Office investments in the Paris suburbs may well show more resilience than the central business district (CBD). Both start from a low supply. However, the demand may very well change for ever, due to COVID-19. Occupiers will always seek connectivity, but this may now shift to a mix of public and private conveyance. Suburbs give attractive, relatively low-rise space, helping social distancing for lifts, etc. Despite available supply being at its lowest level, take-up for office space in the inner suburbs of Paris is – or rather, recently was – close to last year's level (190,000 sq. m. between the beginning of 2020 and mid-March 2020, compared with just over 200,000 sq. m. in 1Q'19).

  - Rents have risen, but not ahead of retail prices, and the market had indeed come slightly "off the boil" later in 2019. France has been one of the strongest-growing European markets, but office take-up Europe-wide was already falling and, in 1Q'20, was ca.30% lower compared with 1Q'19. Paris-wide, office supply peaked at 4.05m sq. m. late in 2014. Despite a rise in 1Q'20 to 3.0m sq. m., the supply is still below the levels of 2017, let alone the 2014 peak. Between 2001 and 2002, Paris office rents fell 14% from their all-time high to €510/sq. m. at the end of 2002. CBD rents have risen since then, but only in line with inflation, at most. At the start of 2020, they were up 15% compared with the 2001 peak, and up 30% versus the 2004 trough, the low point for the century.

  - In conclusion, the outlook for office rents is unclear, and they are at or near a peak. However, the peak is not overly accentuated, and voids and new supply are low. Well-connected suburbs may well outperform, but the outlook is for rents to fall – we estimate – by 15% to 20% in CBD – maybe less in the stronger suburbs. It is visible that there is a floor, and that the starting point was of very low supply, all of which help and all of which give time to adjust.

Valuation

Absolute

Realised losses 2p

Since the end of February, the NAV has fallen from 166.8p to its current level of 145.8p, with 6p due to dividends, and realised losses of just 2.1p. Unrealised losses account for the majority of the balance and are primarily mark-to-market on bonds, where full interest and principal recovery are expected in due course. Despite its recovery over recent months, RECI's share price has fallen by 45.3p (from 166.8p on 29 February to 121.5p now). This equates to more than 20x the realised loss. This suggests that either investors do not believe the current NAV or that they expect future losses, which have not yet been captured by the NAV assessment. We believe that the share price recovery reflects increasing investor confidence that neither are fair. Over time, further delivery of returns may be expected to reverse any residual unjustified sentiment fall.

Current NAV likely to be realistic

We have, in previous reports, considered how the NAV is assessed (e.g. see pages 23-24 of our initiation report, *7%+ yield from well-secured property debt portfolio,* published on 28 August 2019). The critical issues are how conservative the culture of the organisation is and what independent checks and controls are in place to review the process. As we noted in that report, RECI's approach to both appears in line with best practice. We have discussed throughout this report RECI's risk exposures, controls, collection processes and recovery potential.

Discount equivalent to a fifth loss on every one of top 10 positions – unlikely given credit assessment and security

To put the discount into perspective, it (£45m) represents a near fifth loss on the committed, not even drawn amount, for every one of the top 10 exposures. We consider that such a loss rate would be extremely high, given security cover, and we would not expect all of the top 10 exposures to simultaneously default.

Yield

Company indicating stable 12p annual dividend

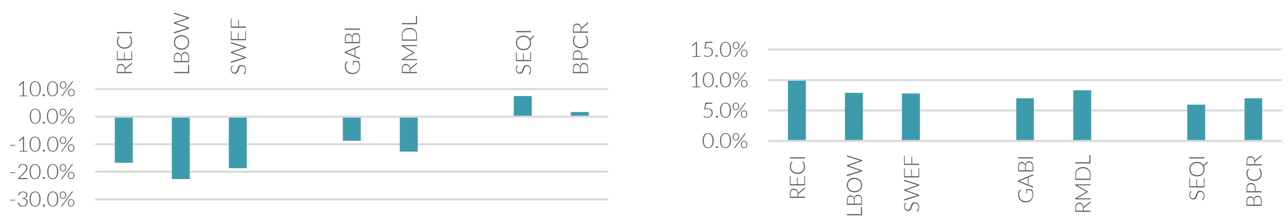
In its *15 May announcement,* RECI brought forward the date of the declaration of the fourth interim dividend, declaring a 3p payment (in line with previous quarters). The Board confirmed that there would be no change to its dividend policy for the current financial year ending 31 March 2021, and that the company intended to continue to pay a stable quarterly dividend, i.e. 12p p.a., and a yield of 9.6%, in line with the current level. This shows great confidence in its portfolio, cash generation and liquidity.

Relative

NAV discount now one of lowest among peers. Dividend yield highest.

RECI comparisons with a close and broad peer group are given below. The NAV discount is now one of the lowest in the close peer group, albeit much higher than the wider peers. The dividend yield is the highest. For investors who view the risk controls and procedures in RECI as being robust, such a valuation appears anomalous.

Premium/discount to NAV (% LHS) and dividend yield for RECI and selected peers (RHS, %)



Source: Latest Factsheets, priced at close 11 September 2020, Hardman & Co Research

Financials

Our profit and loss forecasts have seen a material change since our last report. As noted below, we have materially reduced both Repos financing and equity issuance, which, combined with writedowns, mean the balance sheet is much smaller. At this stage, we have not materially increased the yield, but this is a trend we expect to see on re-investment.

Profit and loss

Year-end Mar (£m)	2015	2016	2017	2018	2019	2020	2021E	2022E
Interest income bonds	6.4	4.7	2.6	5.4	6.9	11.5	9.3	3.3
Interest income loans	9.5	12.9	12.5	12.8	15.2	14.9	22.7	34.3
Other interest income	0.0	0.1	0.2	0.2	0.2	0.1	0.1	0.1
Interest income	**15.8**	**17.7**	**15.3**	**18.4**	**22.3**	**26.4**	**32.1**	**37.6**
Net (losses)/gains on investments	-0.1	4.7	4.6	2.8	-0.1	-35.9	4.3	4.5
Net losses on options	3.2	-1.6	-2.4	-0.9	0.0	0.0	0.0	0.0
Net gains on foreign exchange instruments	2.6	-5.6	-1.8	0.2	3.1	0.0	0.0	0.0
Total net gains on fin. assets at FV through P&L	5.7	-2.6	0.5	2.2	3.0	-36.8	4.3	4.5
Operating income	**21.6**	**15.1**	**15.7**	**20.6**	**25.3**	**-10.4**	**36.3**	**42.1**
Management fee	0.0	-2.0	-2.0	-2.6	-3.0	-4.1	-4.4	-4.6
Performance fee	0.0	-0.2	-0.1	-0.3	-0.7	1.0	0.0	0.0
Other operating expenses	-4.2	-0.9	-1.1	-0.8	-1.1	-2.4	-1.0	-1.0
Operating expenses	-4.2	-3.1	-3.2	-3.7	-4.8	-5.6	-5.4	-5.6
Profit before finance costs	**17.3**	**12.0**	**12.5**	**16.8**	**20.4**	**-15.9**	**31.0**	**36.5**
Finance costs	-3.5	-3.5	-3.4	-1.9	-1.2	-1.5	-0.7	-0.7
Net profit	**13.8**	**8.5**	**9.1**	**14.9**	**19.2**	**-17.4**	**30.2**	**35.8**

Note: 2020 estimated, as awaiting annual results. Source: RECI Report and Accounts, Hardman & Co Research

Hardman & Co adjusted profit & loss

Year-end Mar (£m)	2015	2016	2017	2018	2019	2020	2021E	2022E
Statutory profit	13.8	8.5	9.1	14.9	19.2	-17.4	30.2	35.8
Capital gains & FX movements	5.7	-2.6	0.5	2.2	3.0	-36.8	4.3	4.5
Profit excluding capital gains & FX mvmts.	**8.1**	**11.1**	**8.6**	**12.8**	**16.3**	**19.4**	**26.0**	**31.3**
Adjustment to performance fee	0.0	0.2	0.1	0.3	0.1	0.5	-0.3	-1.3
Adjusted profit	**8.1**	**11.3**	**8.7**	**13.1**	**16.3**	**19.8**	**25.7**	**30.0**
Cost of dividend	13.8	8.5	9.1	14.9	19.2	-25.1	-27.5	-28.7
Statutory cover	5.7	-2.6	0.5	2.2	3.0	-0.7	1.1	1.2
Excluding capital gains cover	8.1	11.1	8.6	12.8	16.3	0.8	0.9	1.0

Source: RECI Report and Accounts, Hardman & Co Research

Our balance sheet forecasts have seen a material change since our last report. We have reduced bonds and the associated Repos financing materially, and we do not assume that RECI will rebuild these exposures in the next two years. In contrast, we do expect further loan growth. This is partially financed by new equity issues (£10m 1Q'21 and £50m through FY'22). We do not believe RECI will undertake such issues at a discount to NAV value. We would hope that the current level of uncertainty/lack of visibility may have reduced significantly over the next year, allowing the first tentative steps for an equity issuance.

Balance sheet								
@ 31 Mar (£m)	2015	2016	2017	2018	2019	2020	2021E	2022E
Bonds	59.4	39.6	49.8	97.3	163.1	237.6	50.0	50.0
Loans	87.1	113.2	109.3	148.1	139.4	137.6	325.2	375.2
Financial assets at FV through P&L	**146.5**	**152.8**	**159.0**	**245.4**	**302.5**	**375.2**	**375.2**	**425.2**
Cash and cash equivalents	8.1	5.3	24.9	7.2	38.6	27.0	-2.4	30.0
Cash collateral at broker	0.0	0.0	0.0	2.4	1.4	25.0	25.0	25.0
Derivatives	4.8	3.2	0.9	0.2	0.7	0.0	0.0	0.0
Other assets	3.5	2.5	4.4	4.9	12.0	14.6	14.6	14.6
Receivable for investments sold	0.0	0.0	0.0	48.1	0.0	0.0	0.0	0.0
Total current assets	16.4	11.0	30.2	62.8	52.7	66.6	37.2	69.6
Total assets	162.9	163.8	189.3	308.2	355.2	441.8	412.3	494.7
Current liabilities								
Derivatives	0.5	0.5	0.0	0.0	0.0	6.2	6.2	6.2
Financing	0.0	0.0	0.0	78.3	100.1	97.0	50.0	50.0
Cash collateral due to broker	0.0	0.0	0.4	0.0	0.1	0.0	0.0	0.0
Preference shares	41.7	41.8	41.9	0.0	0.0	0.0	0.0	0.0
Other liabilities	2.6	2.7	2.7	1.3	1.7	1.5	1.5	1.5
Total liabilities	44.8	45.0	45.0	79.6	102.0	104.6	57.7	57.7
Net assets	**118.1**	**118.8**	**144.3**	**228.5**	**253.2**	**337.2**	**354.7**	**437.1**
NAV per share (p)	**162.3**	**163.2**	**163.2**	**164.0**	**165.1**	**147.0**	**148.2**	**151.1**

Source: RECI Report and Accounts, Hardman & Co Research

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