# Impax Asset Management

## Poised to thrive in ‘sustainable investing 2.0’

31 May 2023

**Impax’s recent AUM progress during another period of market turmoil looks more impressive than we first thought when publishing our April ‘23 note now that we have more peer data. Over H1-23 (Oct 22 – Mar 23), 12% AUM growth (+£4.4bn to £40.1bn) was the highest among a London-listed peer group. £1.1bn of net inflows translated to a 6-month inflow rate of +3.1% which was also the highest by some distance (peer group median: -2.3%). Investment performance contributed £3.3bn to AUM, one of the highest returns among peers (page 3).**

H1-23 revenue of £88.0m was up 1.4% on the preceding half-year (H2-22: £86.8m) and down 0.3% y-o-y from £88.6m in H1-22, impacted mostly by changes in average AUM over these periods (average AUM in the H1-22 y-o-y comparative period was buoyed to an extent by very strong markets in the last quarter of 2021, while in H2-22 it was depressed after sharp market falls).

Adj. operating costs* increased 11% y-o-y from £54.7m to £60.6m, mostly due to increased staffing levels over the last year and investment in systems and infrastructure to ensure the business remains equipped to support further growth. Hence, adj. operating profit fell 20% y-o-y from £34.0m to £27.3m and adjusted operating margin fell from 38% to 31%.

**The balance sheet of the group remained strong even though cash reserves declined by 8% y-o-y to £61.8m from £67.4m. Impax has no debt. The interim dividend is unchanged at 4.7p.**

### Bullish outlook for Impax as sustainable investing market transitions

We think there is a flight to quality underway as sustainable finance transitions to ‘phase 2.0’ (page 10). Demand remains strong, but those asset managers which ‘jumped on the bandwagon’ with less than credible products are being forced to re-label or re-classify their funds due to increasing investor sophistication and regulatory pressure. Managers will also need to generate superior returns from ‘pure play’ sustainable investments (renewable energy, sustainable water, sustainable agriculture, waste reduction etc), not just by being overweight ‘big tech’ as many have done in the past.

With a 25-year track record; superior sustainability credentials; knowledge, experience, and systems for generating superior returns from pure-play sustainable investments; Impax is poised to thrive.

**Our AUM forecasts remain unchanged, but our near-term profit forecasts reduce with the costs increase, which means our fundamental valuation / share reduces from 1,000p to 900p.**

### Summary financials & forecasts

| Year end 30 Sep | FY20A | FY21A | *H1 22A* | FY22A | *H1 23A* | FY23E | FY24E |
|---|---|---|---|---|---|---|---|
| AUM, £bn | 20.2 | 37.2 | *38.0* | 35.7 | *40.1* | 41.9 | 49.1 |
| Revenue, £m | 87.5 | 143.1 | *88.6* | 175.4 | *88.0* | 178.4 | 203.7 |
| Adjusted Op. Profit*, £m | 23.2 | 55.8 | *34.0* | 67.4 | *27.3* | 55.5 | 69.4 |
| Net profit after tax | 13.7 | 40.2 | *26.6* | 59.5 | *16.8* | 34.9 | 44.9 |
| EPS basic, p | 10.6 | 31.5 | *20.6* | 46.0 | *13.0* | 27.1 | 34.8 |
| EPS adjusted & diluted, p | 14.5 | 34.4 | *21.5* | 42.1 | *17.2* | 33.4 | 39.9 |
| PER | 74.5 | 25.0 | *19.1* | 17.2 | *30.3* | 29.2 | 22.7 |
| Dividend, p | 8.6 | 20.6 | *4.7* | 27.6 | *4.7* | 27.6 | 29.1 |
| Yield | 1.1% | 2.6% | *0.6%* | 3.5% | *0.6%* | 3.5% | 3.7% |
| Net assets, £m | 71.4 | 110.5 | *112.3* | 138.2 | *119.7* | 133.8 | 135.8 |
| Net cash, £m | 38.8 | 74.2 | *72.0* | 110.9 | *67.1* | 107.2 | 114.0 |

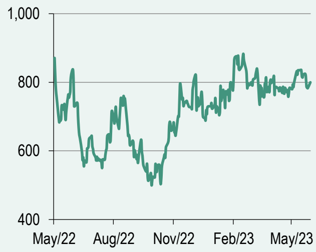
*Source: Group report & accounts and ED estimates* *PER & Yield based on share price of:* ***789p***

** eliminates non-recurring acquisition costs, amort. of intangibles acquired, one-off tax credits & M-T-M of NI on equity awards*

**Company Data**

| | |
|---|---|
| EPIC | IPX |
| Price (last close) | 789p |
| 52 weeks Hi/Lo | 898p/487p |
| Market Cap | £1046m |
| ED Fair Value/share | 900p |
| Proforma net cash | £67m |
| Avg. daily volume | 192k |

**Share Price, p**




*Source: ADVFN*

**Description**

Impax is a specialist asset manager, focused on the growth opportunities arising from the transition to a sustainable economy. Founded in 1998, it offers a range of listed equities, fixed income, systematic, and private markets strategies.

AUM on 31 Mar 2022: £40.1bn

Next Event, Q3 AUM update: Jul 23

THE QUEEN'S AWARDS FOR ENTERPRISE: SUSTAINABLE DEVELOPMENT 2020

SHARES AWARDS 2021 WINNER AIM Company of the Year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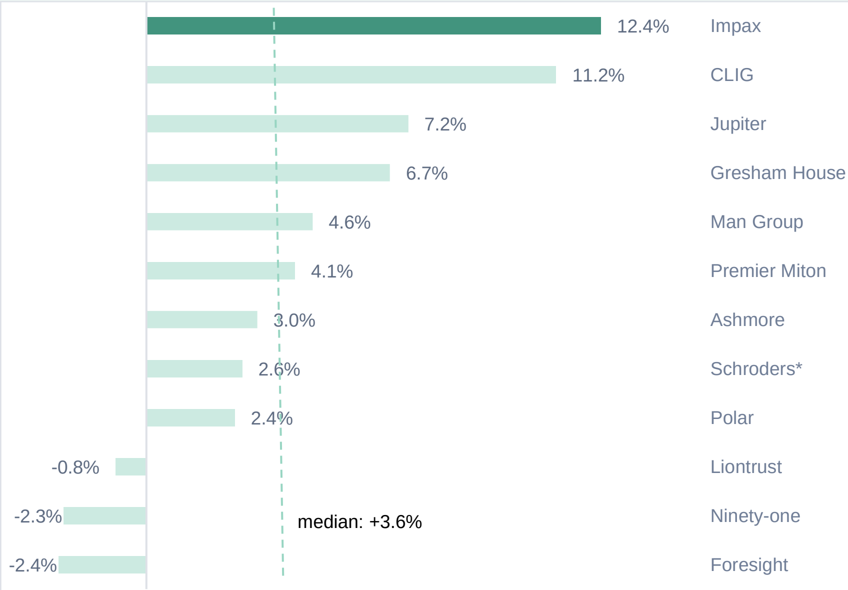
## Impressive AUM growth, net flows & investment returns

AUM grew by £4.4bn (12%) over H1 from £35.7bn on 30 Sep 22 to £40.1bn on 31 Mar 23, with net flows accounting for +£1.1bn of the increase and investment returns +£3.3bn. Impax's AUM growth was the strongest among a peer group of London-listed asset managers.

**AUM growth (excl. acquisitions): 1 Oct 22 – 31 Mar 23**




*Source: Company reports, ED analysis. *Asset management only.*
*Data not available for Abrdn which would usually be in this peer group comparison*

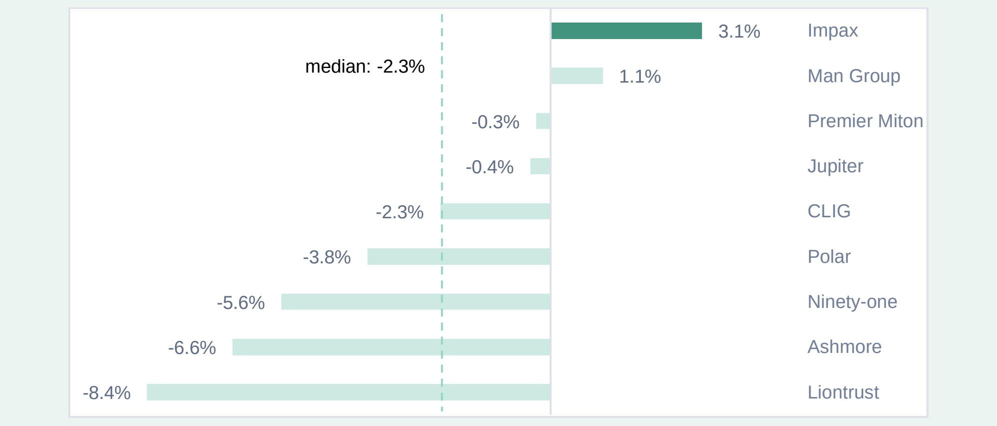
Some notable developments contributing to this growth (or with future potential) include:

- Strong inflows into Sustainability Lens equities strategies, with the US Large Cap strategy seeing net inflows of £751m, including a Japanese pension fund mandate and the launch of a sub-advisory mandate with ABN AMRO. Global Opportunities saw net inflows of £708 million, including subscriptions via distribution relationships St. James's Place in the UK and Formuepleje in Denmark.
- In thematic Environmental Markets equities strategies, Climate and Sustainable Food received good investor interest with inflows of £211 million and £77 million respectively.
- The opening of a new office in Japan, following selection by the Tokyo Metropolitan Government to receive a Green Finance Subsidy. Also, Impax won a significant segregated mandate from a Japanese pension fund during the Period.
- In the US, the Pax World mutual fund range were renamed to Impax Funds. Availability of the Impax Funds was increased on several of the largest wealth management platforms. Impax Funds in the US grew AUM by 14.5% to US$8.2 billion.
- Ireland-based UCITS funds grew by 2.7% to £2.0 billion, and Impax Environmental Markets plc grew total net assets by 6.8%.
- Within Private Markets, Impax successfully exited two Spanish solar PV investments through its third fund. The fourth fund has been fundraising while progressing its investment programme, with eight projects closed and €107.5 million invested by the Period end. In April, the fourth fund also held the third close of its fundraising, taking total capital commitments to €300.3 million by 30 April 2023.
- An actively managed, listed equities UCITS fund investing in Sustainable Infrastructure was launched in November.

**Probably most impressive, however, was the continuation of solid positive flows (+£1.1bn) in an environment characterised by further market turmoil and, no doubt, investor nerves, when most asset managers experienced net outflows.**

In fact, Impax recorded the highest 6-month net inflow rate by some distance compared to peers: +3.1% versus a peer group median of -2.3%.

**Net inflows as % of opening AUM: 1 Oct 22 – 31 Mar 23**

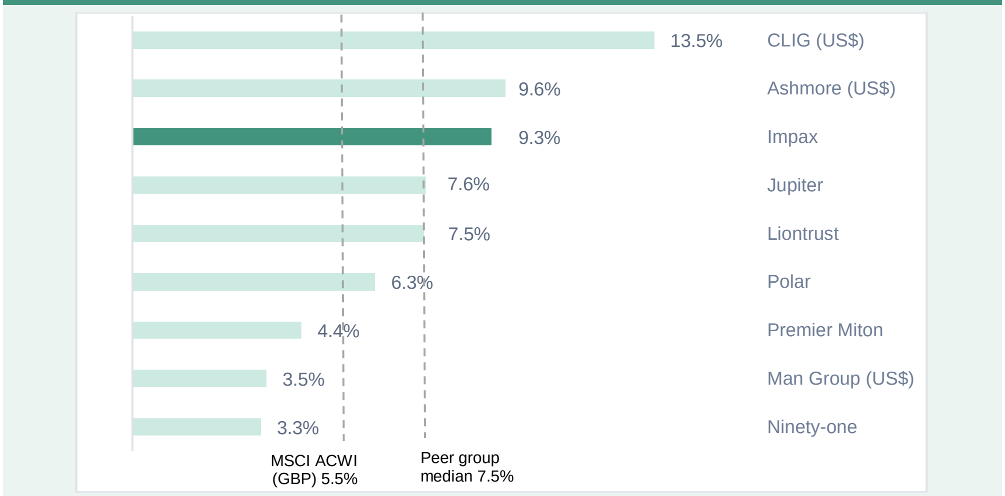



*Source: Company reports, ED analysis*
*Note: Net flow split not available for: Schroders, Foresight, Gresham House, Abrdn*

## Investment performance – group level

Investment performance added £3.3bn to AUM, which was also an impressive performance compared to peers. **Investment return for the half-year was +9.3%, versus a peer group median of +7.5% and the *MSCI ACWI* (GBP) of +5.5%.**

**Investment returns: 1 Oct 22 – 31 Mar 23**




*Source: Company reports, ED analysis*
*Note: Investment return split not available for: Schroders, Foresight, Gresham House, Abrdn*

It is also important to flag the significant impact of currency movements on the above comparisons during the 6-month period under review. Notably, the start of H1 on 1 Oct 22 was very close to the 'mini budget' GBP low. Sterling then appreciated c. 10% relative to the US$ over H1.

**Hence, returns of those asset managers and indexes reporting AUM in GBP (as Impax does) had a significant currency headwind compared to those reporting in US$** (on those investments not denominated in GBP). CLIG and Ashmore, with the highest returns, both report AUM in US$ and would have had a positive currency effect on their returns relative to Impax.

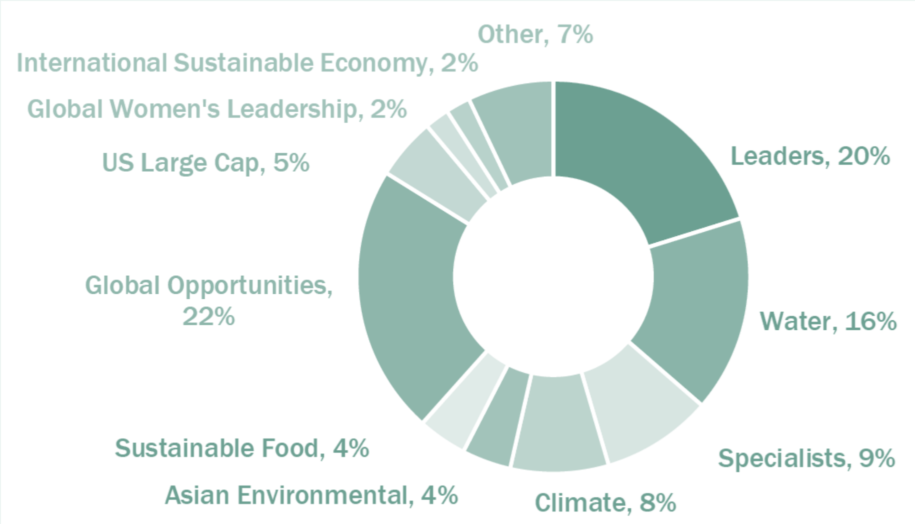
To illustrate the quantum of this impact, we note that the *MSCI ACWI*, measured in GBP, recorded a 5.5% gain in the Oct 22 – Mar 23 period, compared to the 16.9% gain of the same index measured in US$.

## Investment performance – strategy level

Better like-for-like comparisons can be gleaned from strategy-level comparisons to benchmarks, which are not impacted by a currency mismatch. These comparisons are also more relevant to maintaining an attractive proposition for clients and driving further AUM growth.

We remind readers of the AUM split of Impax's investment strategies in the chart below.

**AUM by investment strategy**




*Data as at 31 Mar 23*
*Source: Impax*

We show Impax's investment performance by strategy over multiple time horizons in the tables overleaf (performance shown for largest two strategies which make up around 90% of AUM - Environmental Markets Strategies and Sustainability Lens Strategies).

**We note that Impax has consistently achieved returns above benchmarks,** with above benchmark performance shaded in green, below benchmark in red:

## Environmental Markets Strategies to 31 Mar 2023, % annualised return

**LEADERS:** AUM £ 7,8bn

All-cap global equities strategy investing in companies that are developing innovative solutions to resource challenges in environmental markets, addressing a number of long term macro-economic themes: growing populations, rising living standards, increasing urbanisation, rising consumption, and depletion of limited natural resources. Companies will have >20% of their revenue from sales in environmental markets.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 5.9% | 19.4% | 11.6% |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

**WATER:** AUM £6,2bn

All-cap global equity strategy that invests in stocks of companies operating across the water infrastructure, utilities and treatment sectors

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 5.6% | 21.4% | 13.3% |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

**SPECIALISTS:** AUM £ 3,6bn

Small & mid cap global equities strategy investing in "pure play" companies which have >50% of their revenue from sales in environmental markets. Companies will be developing innovative solutions to resource challenges in environmental markets, addressing a number of long term macro-economic themes: growing populations, rising living standards, increasing urbanisation, rising consumption, and depletion of limited natural resources.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | -1.3% | 21.3% | 12.0% |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

**CLIMATE:** AUM £ 3.1bn

Global equities with demonstrable exposure to products and services enabling mitigation of climate change or adaptation to its consequences.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | -2.7% | 18.8% | 11.9 |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

**ASIAN ENVIRONMENTAL:** AUM £ 1,5bn

Investing regionally in Asia-Pacific companies active in the rapidly growing resource efficiency and environmental markets.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | -1.1% | 14.7% | 7.8% |
| Benchmark – MCSI AC AP Composite | -2.4% | 8.4% | 3.5% |

**SUSTAINABLE FOOD:** AUM £ 1,5bn

Investing in the most innovative companies across the sustainable food value chain.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 0.9% | 14.9% | 7.5% |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

*Source: Impax, ED analysis*
*All numbers show annualised returns. All returns and AUM shown in GBP as of 31 Mar 23.*
*Figures are presented gross of management fees and include the reinvestment of all income.*
*MSCI indices are total net return (net dividend re-invested).*
*MSCI AC AP Composite is a custom-made benchmark made up of 80% MSCI AC Asia Pacific ex Japan and 20% MSCI Japan, rebalanced daily*

## Sustainability Lens Strategies to 31 Mar 2022, % annualised return

**GLOBAL OPPORTUNITIES:** AUM £ 9.0bn

An all-cap global equity strategy that invests in companies possessing sustainable competitive advantages in order to achieve long-term capital growth.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 4.2% | 17.2% | 13.5% |
| Benchmark – MCSI All Country World Index | -1.4% | 15.5% | 9.7% |

**US LARGE CAP:** AUM £2.0bn

A core equity strategy that fully integrates analysis of sustainability risks and opportunities and invests in companies that have strong prospects and attractive valuations.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | -3.0% | 20.0% | 15.8% |
| Benchmark – S&P 500 Index | -1.7% | 18.7% | 14.0% |

**US SMALL CAP:** AUM £0.5bn

A core strategy that fully integrates analysis of ESG risks and opportunities and focuses on high quality companies at reasonable prices. The strategy uses a proprietary sustainability lens and ESG research to better manage sustainability risks and identify opportunities, and it is fossil fuel free.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | -1.4% | 20.0% | 8.6% |
| Benchmark – Russell 2000 Index | -5.9% | 17.6% | 7.4% |

**CORE BOND STRATEGY:** AUM £0.7bn

An investment-grade bond strategy focused on the opportunities and risks arising from the transition to a more sustainable economy.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 1.8% | -1.9% | 3.8% |
| Benchmark – Bloomberg Barclays US Aggregate Index | 1.4% | -2.7% | 3.5% |

**HIGH YIELD BOND STRATEGY:** AUM £0.6bn

A high yield bond strategy leveraging proprietary sustainability tools and research to better identify opportunities and mitigate risks. Focuses on companies with stable profits and manageable debt loads and growing businesses with improving credit profiles.

| Investment period | 1Y | 3Y | 5Y |
|---|---|---|---|
| Impax performance | 1.6% | 4.4% | 5.8% |
| Benchmark – ICE BofA Merrill Lynch US High Yield BB-B (Constrained 2%) Index | 3.3% | 5.4% | 5.9% |

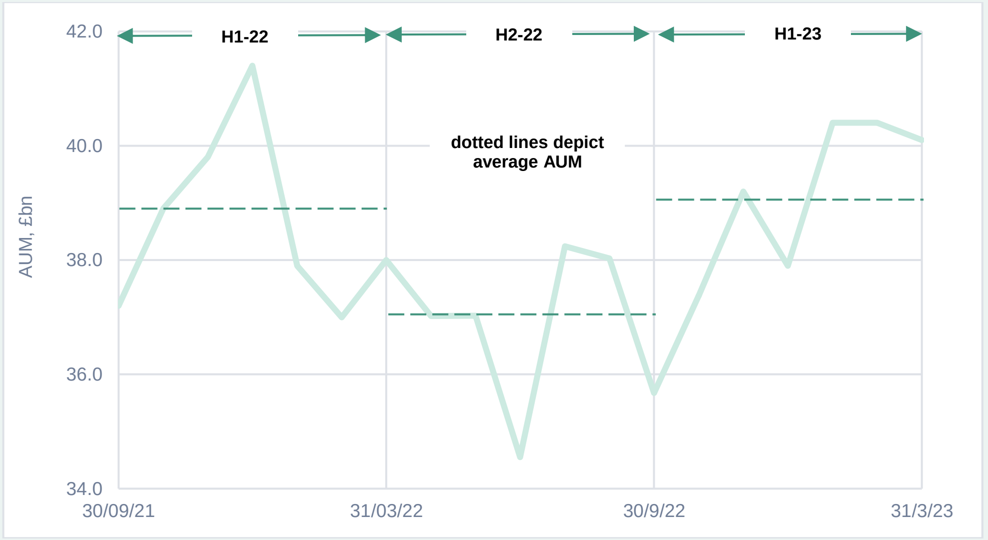
Source: Impax, ED analysis
All numbers show annualised returns. Returns and AUM as at 31 Mar 2023.
Strategy returns are calculated including the dividends re invested, net of withholding taxes , gross of management fee.
MSCI indices are total net return (net dividend re invested).
S&P 500 Index is an unmanaged index of large capitalisation common stocks.
The Russell 2000 Index ("Benchmark") is an unmanaged index and measures the performance of the small cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.
The ICE BofA Merrill Lynch U.S. High Yield BB B (Constrained 2%) index ("Benchmark") tracks the performance of BB and B rated fixed income securities publicly issued in the major domestic or Eurobond markets, with total index allocation to an individual issuer limited to 2%.
Bloomberg Barclays U.S. Aggregate Bond Index represents securities that are U.S. domestic, taxable and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities and asset backed securities.

## H1-23 financials

Because average AUM is the main driver of revenue for Impax, and end-of-period AUM is the main driver of run-rate revenue (although the relationships are not perfectly linear as product mix and in turn fee margin also impacts revenue), It is useful to have a more detailed understanding of AUM development and AUM averages for the period under review and for comparative periods to. This is presented in the chart below.

It should be immediately apparent that Impax's strong net inflows and investment performance over the last six months has resulted in AUM recovering after the sharp market falls during calender-2022, **with average AUM for H1-23 higher than the preceding six-month period, and roughly the same as that of the year-on-year comparator.**

**AUM profile last three half-years, £bn**




*Source: Impax, ED analysis*

### Revenue

**H1-23 revenue of £88.0m was up 1.4% on the preceding half-year (H2-22: £86.8m) and down 0.3% y-o-y from £88.6m in H1-22, impacted by the above changes in average AUM and shifts in product mix** which resulted in the average fee margin decreasing from 46bps to 45bps.

**Run-rate revenue was up 10% over the preceding half-year and 3% y-o-y** (£177m at the end of H1-22; £166m at the end of H2-22; £183m at the end of H1-23), driven mostly by closing AUM levels at the end of each period. [Run rate revenue measures monthly end-of-period revenue (Mar for H1, Sep for H2), extrapolates this for 12 months and adjusts to remove the effects of one-off transactions.]

### Expenses and profitability

Adjusted operating costs increased 11% y-o-y from £54.7m to £60.6m (these costs exclude non-recurring acquisition costs, on-going amortisation of intangibles acquired, one-off tax credits and mark-to-market charges on equity award schemes).

The increase was mostly due to increased staffing levels over the last year to ensure the business is equipped to support further growth. In H1-22, the number of total average staff was 227; in H2-22, 253; and in H2-23, 283. In addition, further investments in systems, infrastructure, risk and compliance were made. Impax has stated that hiring is now expected to slow with the business well equipped to handle an increase in scale.

Adjusted operating profit fell 20% from £34.0m to £27.3m, and adjusted operating margin fell to 31% from 38% in H1-22. However, run-rate annualised adjusted operating profit was £58.0m, up from £54.3m in H2-22 but down from the £65.2m of H1-22. Run rate annualised adjusted operating profit margin closed at 31.8%. Adjusted diluted eps fell 18% to 17.2p (H1 22: 21.1p).

We think that the downtick in margin is temporary (caused by the sharp market and AUM falls during calender-2022 and Impax's investments in growth), and that Impax will return to margin growth as AUM grows (which we believe it will – see section 'AUM growth outlook' on page 10). We think that adjusted operating margins can exceed 35% and head towards 40% over the medium term, if Impax grows its AUM in line with our forecasts.

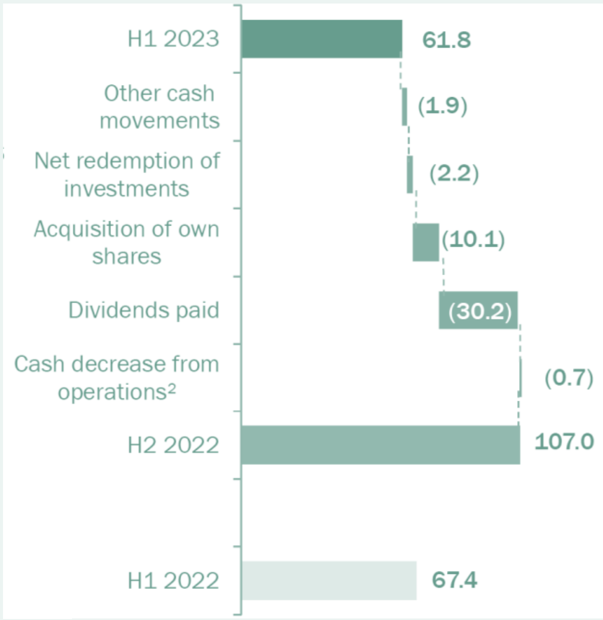
IFRS PBT fell 35% y-o-y from £32.7m in H1 22 to £21.4m in H1 23; PAT fell 37% from £26.6m to £16.8m (with an increased effective tax rate of 22% applied for the period as a result of the increase in the main corporation tax rate in the UK from 19% to 25% from 1 April 2023); and basic EPS fell 37% from 20.6p to 13.0p.

## Balance sheet and cash position both remain robust

**The Balance sheet of the group remained strong even though cash reserves declined 8% y-o-y to £61.8m from £67.4m** (these reserves exclude 3rd-party interest on consolidated funds, and therefore differ slightly from accounting 'net cash' which includes these funds).

We also flag that end-H1 is usually the low-point of the Impax annual cash cycle due to the payment of the prior-year final dividend (£30.2m) and annual staff bonuses being paid during this period. Additionally, Impax spent £10.1m acquiring its own shares (an ongoing practice to minimise dilution from staff awards),

**Cash movements, £m**

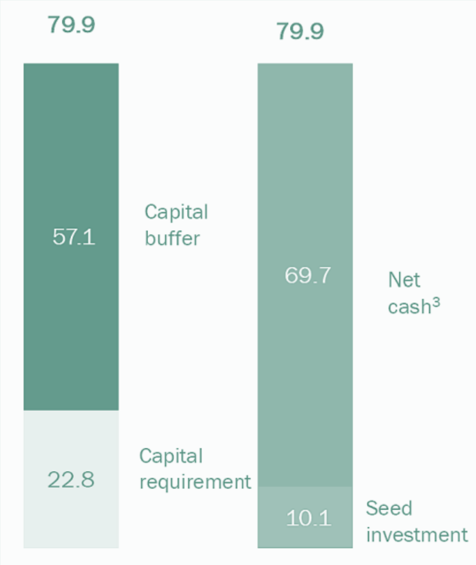



*Source: Impax*
*Excludes third-party interest on consolidated funds and cash held in Research Payment Accounts.*
*[2]Cash generated from operations net of lease payments.*

**Net assets increased by 7% to £119.7m from £112.3m. Impax has no debt.**

The group also provides a capital resources breakdown (see chart below) that takes into account minimum regulatory cash. **This shows Impax having a capital buffer of £57.1m:**

**Capital resources breakdown, £m**




*Source: Impax*
*[3] For capital purposes*

**The interim dividend has remained unchanged at 4.7p**

## AUM growth outlook

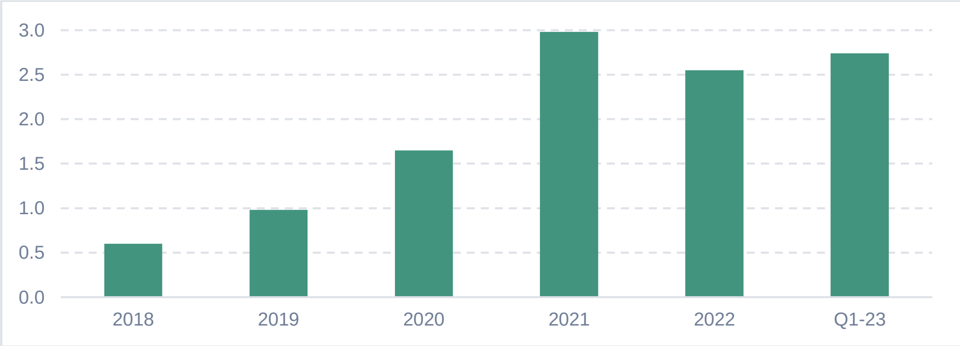
The primary growth drivers for Impax are both the growth of the global sustainable investing market and Impax's share of it. We are bullish on both these drivers and expand on this below.

### Demand for sustainable investments solid amid turmoil of 2022

The sustainable investment market[1] has undergone tremendous growth in recent years because of significant capital flows into funds, market appreciation, and many funds being 're-packaged' as 'ESG' or 'sustainable'. Europe (incl. UK & Switzerland) has captured the bulk of this growth and recently accounted for 84% of global sustainable fund assets. The US accounted for 11% and the rest of the world 5%.

Following a dip in assets during 2022 (due to widespread market falls, not negative net flows – see below), Q1-23 saw a return to growth.

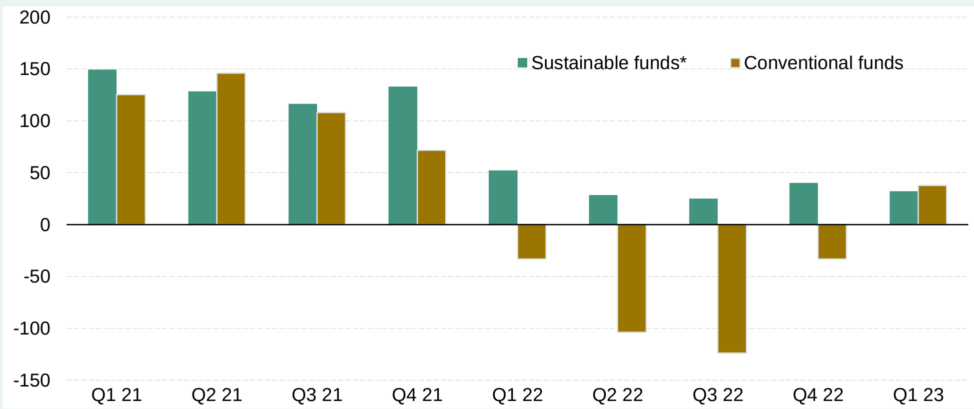
**Global Sustainable Fund Assets, US$trn**




*Source: Morningstar: Global Sustainable Fund Flows: Q1 2023 in Review (and prior reports)*

**In Europe, flows into sustainable funds were far stronger than those into conventional funds during the turmoil of 2022 and remained positive during every quarter, while conventional funds saw outflows during every quarter**. Morningstar wrote: "*sustainability-focused investors—who are typically values-driven and long-term-oriented—are slower to pull money from funds they are invested in*".

**European sustainable* and conventional fund flows, US$bn**




*Source: Morningstar: Global Sustainable Fund Flows: Q1 2023 in Review (and prior reports)*
** Open-end funds & ETFs domiciled in Europe that claim to have a sustainability objective and/or use binding ESG criteria for investment selection. Excludes funds that employ only limited exclusionary screens, such as controversial weapons, tobacco, and thermal coal. Excludes money market funds, feeder funds, and funds of funds.*

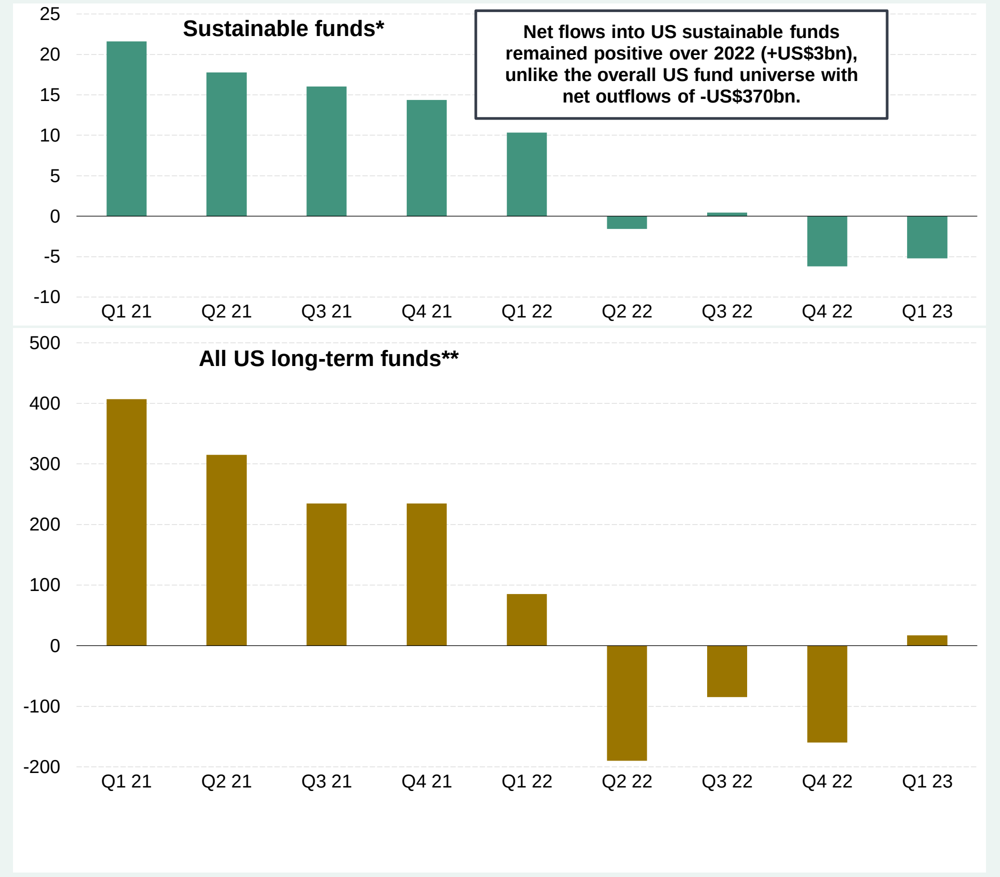
Also, considering that the market share[2] of sustainable funds In Europe stood at 22% at the end of Q1-23, (up from 18% 6-months prior), **there is ample headroom for further growth**.

[1] All market data in this section taken from Morningstar's *Global Sustainable Fund Flows: Q1 2023 in Review* (and prior reports)
[2] *Using the Morningstar definition of a sustainable fund as noted in the above charts*

**In the US, the overall picture for sustainable funds is not as robust as in Europe, but there is still evidence of demand and even more headroom for growth compared to Europe** (the share of sustainable fund assets in the US compared to the overall fund universe is tiny).

During 2022, net flows recorded by sustainable funds were still more resilient than the overall fund universe, although this wasn't the case during Q1-23, when overall demand for sustainable funds was weaker compared to the overall fund universe.

**US Sustainable* and all US Long-term** fund flows, US$bn**




*Source: Morningstar: Global Sustainable Fund Flows: Q1 2023 in Review; U.S. Sustainable Fund Flows: First-Quarter 2023 in Review; Sustainable Funds U.S. Landscape Report, Feb 2023; morningstar.com/articles/1138366/us-fund-flows-january-kicks-off-2023-in-positive-territory; morningstar.com/articles/1102711/june-cements-a-negative-quarter-for-us-fund-flows;*
** Open-end funds and exchange-traded funds that, by prospectus or other regulatory filings, claim to focus on sustainability; impact; or environmental, social, and governance factors, excluding money market funds, feeder funds, and funds of funds..*
*** Long-term U.S. mutual funds and exchange-traded funds excluding money-market funds*

But it is important to flag that **in Q1-23, actively managed sustainable funds in the US (Impax's primary market) recorded positive flows (+US$91m), and that one single passively managed fund, the iShares ESG Aware MSCI USA ETF, had higher outflows (-US$6.5bn) than the overall US sustainable fund market net outflow number (-US$ 5.2bn), indicating that flows would have been positive excluding this fund.** According to Morningstar's *U.S. Sustainable Fund Flows: First-Quarter 2023 in Review* report, the above iShares outflow was due to a reduction in allocation to this fund by a Blackrock model portfolio.

Without doubt, the outlook for sustainable investing in the US is made more uncertain by an ideologically driven political backlash. There are even moves to legislate against ESG investing in some states (Florida and Texas are prominent). But in many East and West coast states such as New York and California, which each have huge amounts of capital for asset managers to target, the demand for sustainable investments remains strong, **and we still see the US as a massive opportunity for Impax.**

It was a mixed picture of sustainable fund flows in other markets during Q1-23, with Canada, Australia and New Zealand (combined), Taiwan, and Malaysia recording net inflows; while Japan, Singapore and Hong Kong saw outflows (data for China not available).

Impax has also expressed positivity regarding market growth prospects and its current pipeline. More specifically, it has flagged a range policy support measures around the world which continue to provide tailwinds for sustainable investing: "*The US' Inflation Reduction Act, the EU's Green Deal Industrial Plan, and similar climate-related measures in China and India, have already attracted capital flows into many areas of the economy in which Impax invests. This includes opportunities around renewables, transformation of the grid, and electric vehicles.*"

## Impax poised to thrive in 'sustainable investing 2.0'

We think 2022 will probably be remembered as the start of a transition in the sustainable investing market. Pre-2022, in a 'sustainable investing 1.0' environment, demand for almost any funds with 'sustainable' or 'ESG' in the name or description was insatiable. And asset managers moved quickly and opportunistically to satisfy this demand. It was also an environment of little or no specific sustainable investing regulation.

Things have changed. In a 'sustainable investing 2.0' environment, investor demand is far more sophisticated and nuanced and aims to seek out the most credible sustainable investing funds, which are also now regulated more robustly, with more regulation to come. We believe Impax, with its 25-year track record, dedicated to sustainable investing, is poised to thrive.

**First, from a product credibility perspective, Impax stands out from those many fund managers which 'jumped on the ESG bandwagon'** to satisfy investor demand, often with little substance behind their products. Without doubt, up until early 2022, many fund managers which launched new ESG or sustainable funds and re-packaged (or even just re-labelled) existing funds as 'ESG' or 'sustainable', did so as a marketing move, rather than a genuine attempt at new product development. The nadir of these less-than-genuine ESG efforts was probably the May 2022 raid by authorities on German asset manager DWS, over accusations of misleading investors about the green credentials of some of their products.

Investor and regulatory pressure have ramped up significantly to clamp down on these practices, which has resulted in a significant reduction of funds claiming to have the highest sustainability credentials.

Indeed, in Europe, in Q4 of 2022, 307 funds were downgraded from 'dark green' Article 9 status (funds which have a sustainable-investment objective) to 'light green' Article 8 status (funds which only promote environmental and/or social characteristics), while only 20 upgraded from 8 to 9. In Q1 of 2023, a further 14 funds downgraded, probably marking the near end of the 'great reclassification'. These moves were most probably driven by ESMA's specification that Article 9 funds should hold only sustainable investments, except for cash and assets used for hedging purposes.

Meanwhile, many funds upgraded from Article 6 (those without a sustainable investing purpose) to Article 8 (light green): 85 in Q4 of 2022 and 263 in Q1 of 2023, indicating that many asset managers still see opportunity to attract assets through sustainable funds (albeit mostly via Article 8 funds). **However, we believe that these 'light green' funds and their like will be at a disadvantage when compared to the credibility of Impax's specialist offerings.**

Impax's strong positioning is also being reinforced by market watchers such as Morningstar which recently chose Impax to be one of eight asset managers (out of 94) categorised as a "Leader" in the incorporation of ESG factors into its investment process.

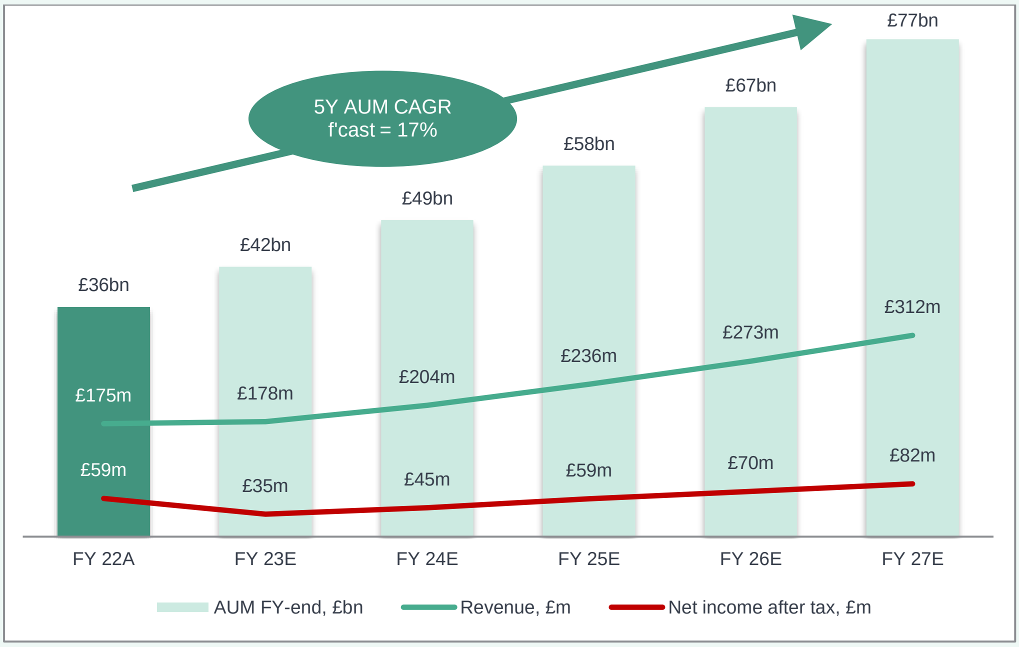
**Secondly, Impax is at an advantage when it comes to generating superior returns from the most credible of sustainable investments.** During the 'sustainable investing 1.0' period, many ESG funds generated strong returns from simplistic strategies that resulted in them being overweight 'big tech' (which performed very well until end-2021). They just avoided 'smokestack' industries or ethically questionable sectors (such as tobacco).

But now, asset managers have to compete in the high-credibility sustainable investing space which is a lot more nuanced. Just because companies do not have obvious smokestacks does not mean they qualify as sustainable investments. For example, large data centres and AI algorithms consume huge amounts of power which means that many tech companies will no longer qualify as sustainable investments. **To compete, asset managers are going to have to generate superior returns from more 'pure play' sustainable investments (renewable energy, sustainable water, sustainable agriculture, waste reduction etc), and few have the knowledge, experience and investing systems of Impax.**

## Valuation headroom

The forecasts used in our fundamental valuation are summarised in the chart below.

**Projections used for fundamental valuation**




*Source: Impax, ED Analysis*
*Note: the reduction in net income in FY23 is partly due to the increase in the rate of UK corporation tax from 19% to 25% in April 2023*

These forecasts are arrived at using the following main assumptions:

- Net inflows of just under £2bn are achieved in FY23 (£1.1bn achieved in H1), increasing to around £7bn per year by FY27 (we remind readers that net flows for FY21 reached £10.7bn).
- Investment performance of +5% per year is achieved.
- Adjusted operating margins improves as the business scales, from the current 31% to around 38% by FY27 (Impax achieved a margin of 39% in FY21).

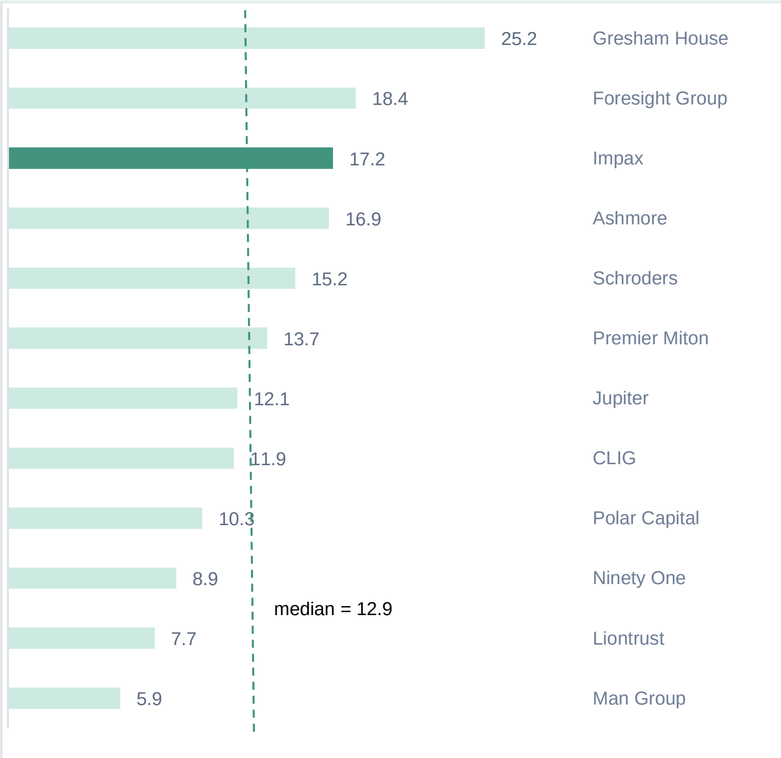
**Using a discounted cash flow methodology, with a discount rate of 13.4% we arrive at a fundamental valuation of 900p, around 14% above the last closing share price.**

We also flag that due to the recent spike in 10-year gilt yields - the risk-free rate used in our DCF calculation - to 4.3%, the above discount rate might be temporarily high if gilt yields reduce. Should this happen, it would have a positive impact on our fundamental valuation.

Additionally, Impax's PE ratio of 17.2, while in the upper range of a peer group, is certainly not excessive given Impax's recent performance compared to peers and its growth prospects.

We also highlight that asset managers' PERs have fallen sharply since the end of the bull market in early-2022. In January 2022, we recorded an asset manager peer group median PER of 31.3 (now just 12.9). We suspect that these PERs may recover quite sharply should markets stage a recovery.

**PE Ratios, UK-listed asset managers**




*Source: ADVFN, Company reports, ED Analysis*
*Data as at 30 May 2023*

# Appendix– historic and forecast Financials

| Consolidated Income Statement + Forecasts | | | | | | | |
|---|---|---|---|---|---|---|---|
| **12 months to end Sept, £m** | **2020A** | **2021A** | ***H1 22 A*** | **2022A** | ***H1 23A*** | **2023E** | **2024E** |
| **Revenue** | **87.5** | **143.1** | ***88.6*** | **175.4** | ***88.0*** | **178.4** | **203.7** |
| | | | | | | | |
| **IFRS Income Statement** | | | | | | | |
| Operating costs | (69.9) | (95.6) | (56.7) | (110.2) | *(63.1)* | (126.7) | (136.9) |
| **Operating profit** | **17.6** | **47.4** | ***32.0*** | **65.2** | ***24.8*** | **51.6** | **66.7** |
| Fair value gain/(loss) on investments | - | - | - | - | - | - | - |
| Non-controlling interest | - | - | - | - | - | - | - |
| Finance cost | (1.9) | (2.0) | *(0.4)* | (0.6) | *(4.9)* | (9.8) | (9.8) |
| Investment income | 1.0 | 0.3 | *1.1* | 8.0 | *1.5* | 2.9 | 2.9 |
| **IFRS profit before tax** | **16.7** | **45.7** | ***32.7*** | **72.6** | ***21.4*** | **44.8** | **59.9** |
| Taxation | (2.9) | (5.5) | *(6.0)* | (13.1) | *(4.6)* | (9.9) | (15.0) |
| **IFRS PAT** | **13.7** | **40.2** | ***26.6*** | **59.5** | ***16.8*** | **34.9** | **44.9** |
| Basic EPS, p | 10.6 | 31.5 | *20.6* | 46.0 | *13.0* | 27.1 | 34.8 |
| Diluted EPS, p | 10.5 | 30.3 | *20.1* | 44.7 | *12.8* | 26.1 | 33.5 |
| | | | | | | | |
| **Adjusted Income Statement** | | | | | | | |
| Adjustments to operating costs: | | | | | | | |
| Acquisition equity incentive scheme awards | 0.1 | 1.6 | *0.7* | 1.3 | *(0.7)* | (0.7) | - |
| Mark to market charge on equity awards | 3.0 | 4.2 | *0.1* | (1.5) | *(0.5)* | (0.5) | - |
| Amortisation of goodwill/intangibles | 2.5 | 2.4 | *1.2* | 2.4 | *(1.3)* | (2.7) | (2.7) |
| Credit from contingent consideration adjustment | - | 0.2 | - | - | - | - | - |
| **Adjusted operating profit** | **23.2** | **55.8** | ***34.0*** | **67.4** | ***27.3*** | **55.5** | **69.4** |
| Fair value gain/(loss) on investments | - | - | - | - | - | - | - |
| Non-controlling interest | - | - | - | - | - | - | - |
| Finance cost | (1.9) | (1.1) | *(0.4)* | (0.6) | *(0.6)* | (1.1) | (1.1) |
| Investment income | 0.9 | 0.2 | *1.1* | 8.0 | *1.5* | 2.9 | 2.9 |
| **Adjusted profit before taxation** | **22.2** | **54.9** | ***34.6*** | **74.8** | ***28.2*** | **57.3** | **71.2** |
| Taxation | (3.5) | (9.3) | *(6.1)* | (12.3) | *(5.7)* | (12.6) | (17.8) |
| **Adjusted PAT** | **18.7** | **45.7** | ***28.6*** | **62.5** | ***22.5*** | **44.7** | **53.4** |
| Adjusted Basic EPS, p | 14.6 | 35.8 | *22.1* | 48.3 | *17.5* | 34.6 | 41.4 |
| Adjusted Diluted EPS, p | 14.5 | 34.4 | *21.5* | 42.1 | *17.2* | 33.4 | 39.9 |
| | | | | | | | |
| **Dividends** | | | | | | | |
| Interim dividend, p | 1.8 | 3.6 | *4.7* | 4.7 | *4.7* | 4.7 | 7.3 |
| Final dividend, p | 6.8 | 17.0 | | 22.9 | | 22.9 | 21.8 |
| **FY dividends per share, p** | **8.6** | **20.6** | | **27.6** | | **27.6** | **29.1** |

*Source: Group report & accounts and ED estimates*

| Consolidated Balance Sheet + Forecasts | | | | | | | |
|---|---|---|---|---|---|---|---|
| **as at end Sept, £m** | **2020A** | **2021A** | ***H1 22A*** | **2022A** | ***H1 23A*** | **2023E** | **2024E** |
| **Assets** | | | | | | | |
| **Non-current assets** | | | | | | | |
| Goodwill | 12.3 | 11.8 | *12.1* | 13.9 | *12.7* | 12.7 | 12.7 |
| Intangible assets | 20.9 | 17.5 | *16.7* | 18.3 | *15.4* | 15.6 | 12.9 |
| Property, plant and equipment | 10.9 | 9.4 | *9.0* | 9.3 | *8.3* | 7.7 | 6.1 |
| Deferred tax assets | 5.5 | 11.9 | *7.3* | 4.8 | *5.3* | 5.3 | 5.3 |
| **Total non-current assets** | **49.5** | **50.6** | ***45.1*** | **46.3** | ***41.7*** | **41.3** | **37.0** |
| **Current assets** | | | | | | | |
| Trade and other receivables | 20.7 | 39.8 | *39.5* | 38.8 | *44.0* | 39.4 | 45.0 |
| Investments | 4.4 | 7.6 | *6.2* | 7.3 | *10.1* | 10.1 | 10.1 |
| Current tax account | 0.2 | 0.1 | *0.6* | 0.2 | *2.4* | 0.2 | 0.2 |
| Cash: money mkt & LT deposits | 18.5 | 38.1 | *40.5* | 58.7 | *20.2* | 20.2 | 20.2 |
| Cash and cash equivalents | 20.2 | 36.2 | *31.6* | 52.2 | *46.9* | 87.1 | 93.8 |
| **Total current assets** | **64.1** | **121.7** | ***118.3*** | **157.1** | ***123.6*** | **157.0** | **169.3** |
| **Total Assets** | **113.6** | **172.4** | ***163.4*** | **203.5** | ***165.3*** | **198.3** | **206.3** |
| | | | | | | | |
| **Equity and Liabilities** | | | | | | | |
| **Equity** | | | | | | | |
| Ordinary shares | 1.3 | 1.3 | *1.3* | 1.3 | *1.3* | 1.3 | 1.3 |
| Share premium incl. merger reserve | 9.3 | 10.8 | *10.8* | 10.8 | *10.8* | 10.8 | 10.8 |
| Exchange translation reserve | 1.4 | 0.4 | *0.4* | 3.1 | *2.6* | 1.9 | 1.9 |
| Hedging reserve | (0.1) | - | *-* | - | *-* | - | - |
| Retained earnings | 59.5 | 98.0 | *99.8* | 123.0 | *105.0* | 119.8 | 121.8 |
| **Total equity** | **71.4** | **110.5** | ***112.3*** | **138.2** | ***119.7*** | **133.8** | **135.8** |
| **Current Liabilities** | | | | | | | |
| Trade and other payables | 28.0 | 50.1 | *41.4* | 53.6 | *35.2* | 54.5 | 62.3 |
| Lease liability | 1.4 | 1.3 | *1.3* | 1.5 | *1.4* | 1.3 | 1.1 |
| Current tax liability | 0.2 | 1.9 | *0.4* | 2.2 | *2.0* | 2.2 | 2.2 |
| **Total current liabilities** | **29.6** | **53.4** | ***43.1*** | **57.3** | ***38.5*** | **58.0** | **65.5** |
| **Non-current Liabilities** | | | | | | | |
| Accruals | - | - | *-* | - | *-* | - | - |
| Lease liabilities | 9.3 | 8.1 | *7.6* | 7.6 | *6.7* | 6.1 | 4.6 |
| Deferred tax liability | 3.3 | 0.4 | *0.4* | 0.4 | *0.4* | 0.4 | 0.4 |
| **Total non-current liabilities** | **12.6** | **8.5** | ***8.0*** | **8.0** | ***7.1*** | **6.4** | **4.9** |
| **Total equity and liabilities** | **113.6** | **172.4** | ***163.4*** | **203.5** | ***165.3*** | **198.3** | **206.3** |

*Source: Group report & accounts and ED estimates*

## Consolidated Cash Flow Statement + Forecasts

| 12 months to end Sept, £'m | 2020A | 2021A | *H1 22A* | 2022A | *H1 23A* | 2023E | 2024E |
|---|---|---|---|---|---|---|---|
| **Profit before taxation** | **16.7** | **45.7** | ***32.7*** | **72.6** | ***21.4*** | **44.8** | **59.9** |
| Adjustment for: | | | | | | | |
| Investment income | (1.0) | (0.3) | *(1.1)* | (8.0) | *(1.5)* | (2.9) | (2.9) |
| Interest expense | 1.9 | 2.0 | *0.4* | 0.6 | *4.9* | 9.8 | 9.8 |
| Depreciation and amortisation | 4.3 | 4.1 | *2.1* | 4.3 | *2.4* | 4.9 | 4.9 |
| Fair value (gains)/losses | - | - | *-* | - | *-* | - | - |
| Non-controlling interests | - | - | *-* | - | *-* | - | - |
| Contingent consideration adjustment | - | - | *-* | - | *-* | - | - |
| Share-based payment charges | 1.8 | 4.9 | *2.6* | 6.2 | *2.6* | 6.2 | 6.2 |
| **Op CF before movement in working capital** | **23.7** | **56.4** | ***36.6*** | **75.6** | ***29.9*** | **62.6** | **77.7** |
| (Increase)/decrease in receivables | (4.0) | (19.0) | *0.3* | 1.0 | *(5.2)* | (0.7) | (5.6) |
| (Decrease)/increase in payables | 4.7 | 22.5 | *(8.7)* | 3.7 | *(18.5)* | 0.9 | 7.7 |
| **Cash generated from operations** | **24.4** | **59.8** | ***28.1*** | **80.3** | ***6.2*** | **62.9** | **79.9** |
| Corporation tax paid | (0.6) | (4.4) | *(4.6)* | (9.0) | *(5.9)* | (9.9) | (15.0) |
| **Net cash generated from operating activities** | **23.8** | **55.4** | ***23.5*** | **71.3** | ***0.3*** | **53.0** | **64.9** |
| **Investing activities** | | | | | | | |
| Deconsolidation of investment fund | - | - | *-* | - | *-* | - | - |
| Investment income received | 0.2 | 0.1 | *0.1* | 0.6 | *1.3* | 2.9 | 2.9 |
| Settlement of investment related hedges | (0.2) | (0.5) | *(0.1)* | 0.1 | *(0.5)* | - | - |
| Net redemptions/(investments) uncons. funds | *1.2* | (2.5) | *1.2* | 0.4 | *(2.2)* | (2.9) | - |
| (Incr)/decr in cash in money market & LT deposit | (3.3) | (19.6) | *(2.4)* | (19.1) | *38.5* | 38.5 | - |
| Purchase of Impax NH shares | - | (0.7) | *-* | - | *-* | - | - |
| Acquisition of PPE and intangible assets | (0.2) | (0.3) | *(0.4)* | (0.8) | *(0.4)* | (0.5) | (0.5) |
| **Net cash used in investing activities** | **(2.2)** | **(23.4)** | ***(1.5)*** | **(18.9)** | ***36.7*** | **38.0** | **2.4** |
| **Financing activities** | | | | | | | |
| Acquisition of non-controlling interest | (0.2) | (0.2) | *(0.1)* | (0.2) | *-* | - | - |
| Repayment of bank debt | - | - | *-* | - | *-* | - | - |
| Interest paid on bank debt | (0.1) | (0.1) | *(0.1)* | (0.1) | *(0.0)* | (9.8) | (9.8) |
| Dividends paid | (7.4) | (13.6) | *(22.5)* | (28.7) | *(30.2)* | (35.9) | (38.9) |
| Acquisition of own shares | (4.2) | - | *(3.9)* | (8.8) | *(10.1)* | (10.1) | (10.1) |
| Payment of lease liabilities | (1.7) | (1.7) | *(0.8)* | (1.7) | *(1.0)* | (1.7) | (1.7) |
| Cash received on exercise of Impax share options | 0.5 | 0.6 | *0.2* | 0.5 | *1.3* | 1.3 | - |
| **Net cash generated from /(used in) financing** | **(13.2)** | **(15.0)** | ***(27.2)*** | **(39.0)** | ***(40.1)*** | **(56.2)** | **(60.6)** |
| | | | | | | | |
| **Net (decr)/incr in cash and cash equivalents** | **8.4** | **16.9** | ***(5.2)*** | **13.4** | ***(3.1)*** | **34.9** | **6.7** |
| Cash and cash equivalents at beginning of year | 11.9 | 20.2 | *36.2* | 36.2 | *52.2* | 52.2 | 87.1 |
| Effect of foreign exchange rate changes | (0.1) | (1.0) | *0.5* | 2.6 | *(2.2)* | - | - |
| **Cash and cash equivalents at end of year** | **20.2** | **36.2** | ***31.5*** | **52.2** | ***46.9*** | **87.1** | **93.8** |

*Source: Group report & accounts and ED estimates*

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