



MLC Centre  
Level 36, 19 Martin Place  
Sydney NSW 2000 AUSTRALIA

General: +61 2 9235 4888  
Facsimile: +61 2 9235 4800  
Website: [www.magellangroup.com.au](http://www.magellangroup.com.au)  
ABN: 59 108 437 592

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ASX Limited  
ASX Market Announcements Office  
Exchange Centre  
20 Bridge Street  
SYDNEY NSW 2000

**MAGELLAN FINANCIAL GROUP LIMITED  
INTERIM RESULTS BRIEFING  
TELECONFERENCE AND WEBINAR  
CEO AND CFO REMARKS**

MFG's Chief Executive Officer (CEO), Hamish Douglass and Chief Financial Officer (CFO), Kirsten Morton presented the Results for the half year ended 31 December 2017 by teleconference and webinar yesterday.

A copy of the CEO and CFO Remarks from the Interim Results Briefing are attached.

A recording of the teleconference is available at:

<https://www.magellangroup.com.au/shareholder-centre/latest-results/>

For further information, please contact:

Sarah Thorne  
Investor Relations  
Ph (02) 9235-4844

Geoffrey Stirton  
Company Secretary  
Ph (02) 9235-4828

## **Magellan Financial Group**

### **Interim results**

#### **Analyst/investor call – CEO and CFO remarks**

**6 February 2018**

### **Craig Wright, Head of Governance and Advisory**

#### ***Introduction***

- Good afternoon everyone and on behalf of the company, welcome to the Magellan Financial Group interim results conference call for the half year ended 31 December 2017. I'm Craig Wright, Head of Investor Relations at Magellan.
- The company's results will be presented today by the CEO & Chief Investment Officer of Magellan, Mr Hamish Douglass and the Chief Financial Officer, Ms Kirsten Morton.
- As you can see, we've implemented a new format for the interim results and trust this will prove most efficient for those interested in Magellan results.
- An investor presentation has been lodged with the ASX and is available on Magellan's website. We are not planning to step through the presentation on today's call however it is available for further information. A transcript of this call will be made available on ASX within 24 hours.
- Please note that there will be a Q&A session at the end of the call.
- For those of you joining us via the webcast, you can submit a question by typing it directly into the webcast portal.
- For those of you who have joined through the teleconference, the teleconference administrator will advise you at the end of the call how you can ask a question.
- Please note that today's call is being recorded. We may also have the media on the line today.
- Thank you and I will now hand it over to Hamish.

## **Hamish Douglass, CEO and Chief Investment Officer**

### ***Introduction***

- Magellan has had an extremely busy and productive first half.
  - We completed the \$1.57 billion initial public offering of the Magellan Global Trust, the largest closed end fund raising in Australian history;
  - We became the naming rights sponsor for men's Domestic Test Cricket; and
  - Today announced two strategic acquisitions: Frontier Partners in the United States; and Airlie Funds Management.
- We view each of these initiatives as strategically important to the ongoing development of Magellan.
- I would like to start with discussing the strategic initiatives.

### ***Frontier Partners***

- The first is to acquire 100% of the Frontier Partners, a privately owned group of companies based in Chicago. Frontier is a specialist distribution group that assists fund managers penetrate the North American institutional market.
- Frontier has been Magellan's distribution partner in North America since 2011. It has been an outstanding relationship for Magellan and today we have \$12.6 billion in funds under management in North America with some of North America's most prestigious institutional investors including state plans, marquee foundations and family offices and large corporations.
- The key to our success in North America had been our partnership with Frontier and most importantly our relationship with the owner and founder of Frontier, Mr Bill Forsyth.
- I cannot speak more highly of Bill. With the acquisition of Frontier, Bill has agreed to become the Executive Chairman of Magellan's business in North America and lead the development of our North American business. I view this as a coup for Magellan as Bill is one of the highest calibre individuals with whom I have worked. Securing Bill to lead our North American business has been the primary driver of this transaction as we see substantial opportunities for Magellan in the North American market in the years ahead.
- Financially this transaction is also attractive to Magellan. Following the completion of the transaction we will cease paying ongoing success fees to Frontier on our mandates in the United States and will enjoy improved economics on our funds on the Frontier mutual fund platform. Based on the current level of funds under management this will result in an initial benefit of around \$10 million per annum.
- Frontier also owns a registered broker deal and an investment adviser to a mutual fund platform. These capabilities should result in savings in the future as we bring some of these functions effectively in house.

- I believe that this acquisition materially enhances our distribution and management capabilities in the North American market whilst also being financially attractive from day 1.

### ***Airlie Funds Management***

- The second strategic initiative is the acquisition of Airlie Funds Management.
- I could not be more excited about the bringing together of Magellan and Airlie.
- It is my view, and I am sure many people would agree, that John Sevier and Matt Williams are the pre-eminent portfolio management team in Australian equities.
- Our partnership with Airlie has not come about overnight but has evolved from discussions over the past decade.
- I am completely humbled that John Sevier, Matt Williams and David Cooper have chosen to partner with Magellan to further develop the Airlie business. I do not use the word partner lightly, but it is how I really feel. They have decided to exchange their equity in Airlie for equity in Magellan and they have become our partners in every sense.
- John, Matt and David have already built an outstanding business with over \$6 billion in funds under management. We have a tremendous opportunity to further develop the Airlie business into the retail market.
- We are delighted to announce that we intend to launch, in the coming months, the Airlie Industrial Share Fund which will be an Active ETF quoted on the ASX.
- The proposed launch of the Airlie Industrial Share Fund highlights the potential power of the combination of Airlie and Magellan. It will leverage Airlie's pre-eminent expertise in Australian equities and Magellan's operational expertise and distribution strength in the retail and adviser market.
- Our distribution team is incredibly excited.
- Magellan will acquire 100% of Airlie through the issue of shares in Magellan to Airlie's shareholders at the completion of the acquisition, expected to be at the end of February 2018. The acquisition of Airlie will be immediately accretive to our earnings per share.
- Importantly Airlie will continue to operate under the Airlie brand.
- We very much look forward to working with John, Matt and David and welcome the entire Airlie team to Magellan.
- We expect that these transactions together will be modestly accretive to EPS in the first full year and provide an attractive return on capital. This excludes any benefits over time from the soon to be launched Airlie Industrial Share Fund. Total consideration payable in respect of the acquisitions comprises US\$15 million in cash and approximately 4.5 million Magellan shares. This represents approximately 2.6% of Magellan's issued capital. The Magellan shares will be issued post the record date for the interim dividend.

### ***Magellan Global Trust and Cricket Australia Sponsorship***

- The third initiative is the launch of the Magellan Global Trust and Cricket Australia sponsorship.
- The Group remains focused on developing its retail business and executing its self-directed investor strategy and has made some important progress in the past six months.
- The Magellan Global Trust is an important part of our self-directed strategy and raised \$1.57 billion in October 2017 from more than 32,000 investors.
- As at 31 December 2017, the Magellan Global Trust and our three Active ETFs had a combined funds under management of approximately \$2.8 billion with over 50,000 unitholders. We are now building a very accessible platform of ASX quoted product.
- A core focus of our self-directed strategy is to raise awareness of the Magellan brand and our expertise in global investing.
- Our partnership with Cricket Australia, to sponsor the men's domestic test cricket series for 3 years, provides an important platform to raise brand awareness. We also have an option to extend the sponsorship for a further 2 years.
- We are delighted with the first season of our sponsorship with Cricket Australia and believe it has meaningfully moved the needle on general awareness of Magellan and our tagline "Experts in Global Investing".
- Let me give you a few stats:
  - More than 14.5 million people watched the Magellan Ashes series on television on Channel 9.
  - 866,000 people attending the various grounds which was the second highest attendance in history outside a series in the 1930s which was a six test format.
  - There were more than 15 million average daily views on the Cricket.com.au website and Cricket Live App.
- We'd like to confirm our expectation that the Group's marketing expense will increase materially in the 2018 financial year to approximately \$11.0-\$11.5 million. Whilst the step up in expenditure this year is meaningful it is worth noting that our total marketing expense represents approximately 3% of our revenue.
- I also note that building a meaningful retail self-directed business is a real challenge and will take multiple years to gain traction.

### ***Interim Results Highlights***

- I would like to go through some financial highlights for the six months to 31 December 2017:
  - Underlying net profit after tax increased by 25% to \$109.2 million. This excludes the one-off costs of the Magellan Global Trust raising.

- This was driven largely by a 25% increase in average funds under management compared with the previous corresponding period.
- The interim dividend increased by 16% to 44.5 cents. As you know we have revised the dividend policy and are now excluding any performance fee component with the interim dividend and paying out any performance fees as a performance fee dividend with the final dividend.
- Excluding the performance fee component paid last year, the interim dividend increased by 20%. This is in line with the increase in the profit before performance fees of the funds management segment.
- Before handing over to our CFO, Kirsten Morton, I would like to make two other observations:
- Closing of Global Equity Strategy
  - The first is relation to the closing of our Global Equities strategies.
  - We have previously disclosed that we would be closing our Global Equity strategies to new institutional investors on 31 December 2017.
  - As part of this process, clients have reserved additional capacity that they can utilise over the next 12-24 months. I note that St James's Place has reserved capacity that they can utilise over a longer period of time.
  - Whilst we do not wish to disclose the total amount of reserved capacity, it is meaningful, and we would expect solid ongoing institutional inflows into our global equity strategies over the next 24 months as clients utilise all or part of this reserved capacity.
- Retail flows
  - Our retail net inflows, excluding the Magellan Global Trust raising, were materially lower in the past 6 months than in the previous corresponding period.
  - Our monthly average net inflows (excluding the proceeds of the Magellan Global Trust raising) were approximately \$55 million per month over the six months compared with \$207 million per month over the previous corresponding period.
  - This largely reflects lower net inflows into our Global Equity strategies.
  - We believe by far the largest impact has been client switching into the Magellan Global Trust which we anticipated. This should be a one-off impact as advisers adjusted their client portfolios.
  - The net inflows have also been impacted by lower industry net inflows by the advice industry and to some extent by some changes by a very limited number of advice practices. We had two small advice groups that exited our fund, another advice group that changed their portfolio model weightings and a client experiencing structural outflows in the last 6 months. These were not material in

the context of our advice business. Remember we have relationships with over 500 advice groups in Australia and New Zealand.

- I also note we have introduced a new unit class in the Magellan High Conviction Fund with a lower base fee and higher performance fee. The performance of the High Conviction Fund has been exceptional, and we are seeing real interest by advisers in the new unit class.
- I would now like to hand over to Kirsten to run through the financials.

## **Kirsten Morton, Chief Financial Officer**

### ***Financials***

- Thank you, Hamish.
- Magellan had a strong start to the 2018 financial year.
- We reported profit after tax of \$53.5 million which was down from \$87.0 million for the six months to 31 December 2016.
- However, after excluding the one-off offer costs of the Magellan Global Trust, our underlying profit was \$109.2 million, up 25% over the prior corresponding period.
- The net MGG offer costs after tax were \$55.7 million and were funded out of available cash. These costs are not included in the Funds Management segment and therefore do not affect the profitability of the Funds Management business.
- The growth in underlying profitability of the Group reflects a 22% growth in management and services fees driven by a 25% increase in average funds under management.
- Our reported diluted earnings per share was 31.0 cents per share. Excluding the MGG net offer costs, diluted earnings per share increased 25% to 63.4 cents per share.
- As Hamish outlined, the Directors have declared an interim dividend of 44.5 cents per share, up 16% over the prior corresponding period. Excluding the performance fee component from the prior half year's dividend, the interim dividend increased 20%.
- To reiterate our dividend policy, the company pays an Interim and Final Dividend of 75-80% of the Funds Management profit, excluding crystallised performance fees. We will also pay an annual Performance Fee Dividend of 0-100% of the net crystallised performance fees after tax. Any Performance Fee Dividend will be paid alongside the Final Dividend. The payment of dividends by the Group will be subject to available franking credits and corporate, legal and regulatory considerations. The level of payment of Performance Fee Dividends will also be subject to capital needs of the Group.
- Our underlying effective tax rate was 23.5%, broadly in line with the prior corresponding period of 23.0%. This underlying effective tax rate reflects the benefits of the Offshore Banking Unit license.
- Including the MGG offer costs, the reported effective tax rate was 15.4%

- Moving on to the Funds Management business, which is the core operating business of Magellan.
- Revenues of the Funds Management business increased 26% to \$189 million. The growth in revenues reflect:
  - A 25% increase in management fees in line with the increase in average funds under management;
  - An increase in performance fees to \$9.6 million. It is important to note that performance fees fluctuate materially from period to period;
  - A decrease in services fees to \$2.4 million reflecting our amended agreement with MFF Capital Investments.
- Expenses in the Funds Management business grew 27% to \$50.5 million.
- The key drivers of the increase in expenses were two-fold:
  - Employee expenses, which increased by 8% to \$25.4 million. This included a modest amount of redundancy payments as a result of some restructuring of the investment team, which won't occur in the second half; and
  - An increase in our marketing expenses to \$6.7 million.
- For the 2018 financial year, we expect our employee expenses, which are the largest contributor to expenses, to increase at the lower end of the 5-8% guidance.
  - This estimate excludes the impact of additional employee expenses relating to the acquisition of Frontier and Airlie. The estimated impact for the 6 months to 30 June 2018 of these additional employee expenses is approximately \$4.6 million. We are delighted to welcome 25 people who will be joining us from Airlie and Frontier.
- As Hamish has already discussed, our marketing expense for the 2018 financial year is expected to increase to \$11-\$11.5 million, in line with our previous guidance.
- I would also like to note the increase in occupancy expense to \$2.7 million which includes a one-off cost of approximately \$1.3 million in regard to the closure of our New York office. Our distribution team members in the US continue to operate out of Newport Beach.
- Profit before tax of the Funds Management business grew 25% to \$138.5 million and if we exclude performance fees, profit before tax grew 21% to \$129 million.
- The business continues to operate efficiently with the cost to income ratio (excluding performance fees) of 28.1%.
- Now turning to capital management.
- The group continues to maintain a strong balance sheet with Net Tangible Asset per share of \$2.54. This includes the effect of the one-off MGG IPO costs.
- We recently established a small debt facility to aid in overall liquidity management. This facility is sized at \$50 million and is currently undrawn.



- The Group had total net Principal Investments of \$243.5 million. Our Principal Investments includes investments in Magellan's listed and unlisted funds. We intend to allocate any surplus cash generated, after allowing for the payment of dividends, to Principal Investments.
- We aim to earn satisfactory returns for our shareholders and the Board has established a pre-tax return hurdle of 10% per annum over the business cycle for the Principal Investments which to date we have achieved. Over the last 1,3 and 5 years, the pre-tax returns are 16%, 11.5% and 18.8% per annum respectively.
- Since inception from 1 July 2007 and excluding the Group's investment in MFF Capital Investments, the portfolio has returned pre-tax 11.1% per annum.
- With that, I will now turn back to Craig.