9 November 2021

Market data

EPIC/TKR	**TISEG**
Price (p)	**1,300**
12m high (p)	1,325
12m low (p)	875
Shares (m)	2.8
Mkt cap (£m)	37
EV (£m)	23
Free float*	100%
Country of listing	Guernsey
Market	TISE

**As defined by AIM Rule 26*

Description

TISE is a regulated exchange specialising in listings. It is looking to expand its business by growing its share of the bond listing market. It has a strong balance sheet, and is highly cash-generative. It is listed in Guernsey.

Company information

CEO	Cees Vermaas
CFO	Andrew Watchman
Chair	Charlie Geffen

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www.tisegroup.com

Key shareholders

Bailiwick Investments Ltd	13.6%
J Moulton	11.5%
M Thistlethwayte	8.9%
S & M Lansdown	8.9%
Carey Olsen Corporate Finance Ltd	8.7%
F Le Poidevin	7.1%

Diary

Mar'22	Final results

Analyst

Jason Streets 020 3693 7075
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THE INTERNATIONAL STOCK EXCHANGE

Global, responsive, competitive

The International Stock Exchange (TISE) is a stock exchange based in Guernsey currently specialising in listings, notably for bonds. It has been growing strongly for six years, and is looking to diversify its core business into related areas. In particular, it is looking to expand its share of securitisation listings, and has just launched a professionals-only market, QIBM. TISE is a high-margin, cash-generative, profitable business with a strong balance sheet. It is well-positioned to adapt to the constantly evolving regulatory environment, in our view.

- **Strategy:** TISE specialises in listings that are sought for technical reasons, typically to ensure tax advantages or lower costs, while still being on a recognised exchange. It does relatively little trading; most of the assets are held to maturity by professional investors. It is well-located and highly efficient.

- **Opportunities:** TISE currently has just a 3% share of bond listings in Europe, and it has revamped its offer with a new market for qualified investors only. It has attracted some important new members in Ireland, and is phasing out membership fees. It is introducing a new trading system to help build liquidity.

- **Valuation:** There are no directly comparable listed companies – other traded exchanges are substantial trading venues. We have used a DCF model with a high 15% discount rate to reflect the current regulatory uncertainties. Our derived central value is £64m, or 2,275p per share.

- **Risks:** TISE's main threat comes from changes to regulations that might make its venue uncompetitive. The risk from rule changes initiated by the UK Treasury seems to be less severe than first anticipated – the definition of who may qualify may prove too narrow or complex to make switching from an overseas listing worthwhile for many issuers. In addition, its reputation for probity is important for attracting listings and approval from various international bodies. Its own shares are illiquid, and typically trade only a few times each quarter.

- **Investment summary:** TISE aims to expand its customer base and build on its growth record. With a strong track record and robust balance sheet, we believe TISE is well-placed to diversify its revenues and continue to trade very profitably.

Financial summary and valuation

Year-end Dec (£000)	2018	2019	2020	2021E	2022E	2023E
Sales	7,323	7,585	8,362	9,560	10,461	11,403
EBITDA	3,362	3,608	3,817	5,008	5,817	6,664
Reported EBIT	3,300	3,574	3,769	4,960	5,769	6,617
Reported PTP	3,358	3,633	3,801	4,985	5,794	6,642
Net income	3,358	3,476	3,622	4,751	5,522	6,330
Underlying EPS (p)	124	123	128	168	196	224
Fully diluted EPS (p)	120	123	128	168	196	224
Net (debt)/cash	11,334	8,375	10,748	13,196	16,033	19,397
Dividend (p)	30	32.5	50	80	100	110
P/E (x)	10.5	10.6	10.1	7.7	6.6	5.8
EV/EBITDA (x)	7.1	7.8	6.8	4.7	3.5	2.6
Yield	2.3%	2.5%	3.8%	6.2%	7.7%	8.5%

Source: Hardman & Co Research

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The International Stock Exchange

Background

The International Stock Exchange (TISE) is a regulated market specialising in listing bond issuances aimed at professional investors. It is uniquely positioned within the European time zone but outside both the UK and the EU. It is an exceptionally convenient offshore location. It is headquartered in Guernsey and has staff operating in Dublin, Guernsey, the Isle of Man, Jersey and London.

Sources of revenue

TISE makes the vast bulk of its current revenues from listing fees, both annual and initial. Unlike the large listed exchanges – Euronext, LSE, Deutsche Boerse – it does not have a large trading business. It is, in essence, a listing venue: companies list bond and specialist vehicles on TISE to fulfil legal obligations rather than specifically to raise capital.

Approximately 90% of the securities listed on the Exchange are Special Purpose Vehicles (SPVs) of one kind or another. They are mostly bonds, and are typically listed for one or more of the three principal reasons entities use an exchange like TISE:

- to benefit from the Quoted Eurobond Exemption (QEE);
- to avoid the onerous obligations set by the EU, such as the Market Abuse Regulation (MAR); and
- to ensure eligibility for inclusion in mutual funds.

Types of listing on TISE as at June 2021

Type of listing	Number	Percentage
Bonds (including 330 high-yield bonds)	3,196	93%
Open-ended investment vehicle	154	4%
Closed-ended investment vehicle	73	2%
Equity	8	0%
Total	3,431	100%

Source: TISE, Hardman & Co Research

The QEE allows listed vehicles to pay interest to their investors without deducting UK withholding tax (WHT). This is especially relevant for high-yielding bonds where the coupon represents a significant part of the expected return.

MAR is an EU-wide regulation that obliges listed vehicles to make various disclosures and prepare reports, which many issuers consider very onerous for what are effectively static vehicles.

Lastly, and most simply, most jurisdictions across the world require mutual funds (or their equivalent) to invest a minimum percentage of their assets in entities listed on a recognised exchange. Therefore, if an issuer wants its securities to appeal to the widest possible pool of investors, it makes all the difference if they are listed.

TISE recognition

TISE is an international exchange recognised by the UK tax authority (HMRC), by the US Securities and Exchange Commission (SEC), the Irish Revenue Commissioners, the Australian Stock Exchange (ASX) and the German financial regulator (BaFin). Crucially, the corporate structure separates the marketing of the business from the regulation of the Exchange. It aims to provide a pragmatic and sensible regulatory environment, with the Exchange's market authority applying global standards of regulation in a proportionate manner that aims to balance the interests of both issuers and investors. It is an Affiliate Member of the International Organisation of Securities Commissions (IOSCO) and an Affiliate Member of the World Federation of Exchanges (WFE), as well as being a member of the Association for Financial Markets in Europe (AFME), the International Capital Markets Association (ICMA) and the United Nations' Sustainable Stock Exchanges (UN SSE) initiative.

Guernsey status

Guernsey is a self-governing dependency of the Crown with its own directly elected legislative assembly, its own administrative, fiscal and legal systems, and its own courts of law. Although Guernsey is not part of the UK, it is part of the British Isles and there are very strong economic, cultural and social links between Guernsey and the UK. Guernsey is not represented in the UK Parliament but the Crown is responsible for the island's defence and for its formal international relations.

Guernsey is also a Designated Territory for the purposes of Section 270 of the UK Financial Services and Markets Act 2000. This allows collective investment schemes to "passport" into the UK. Consequently, a TISE-listed, Guernsey-incorporated open-ended investment company that is regulated under Guernsey's recently revised Class A Rules can be as easily promoted to UK retail investors as if the fund was regulated in the UK.

Technically, Guernsey is deemed to be an offshore financial centre – that is a "country or jurisdiction that provides financial services to non-residents on a scale that is incommensurate with the size and the financing of its domestic economy" – but it is no pariah. It was recognised by the IMF as being in Group 1 in its year 2000 classification, defined as "generally viewed as cooperative, with a high quality of supervision, which largely adhere to international standards". Nor is it one of the 12 jurisdictions on the EU blacklist.

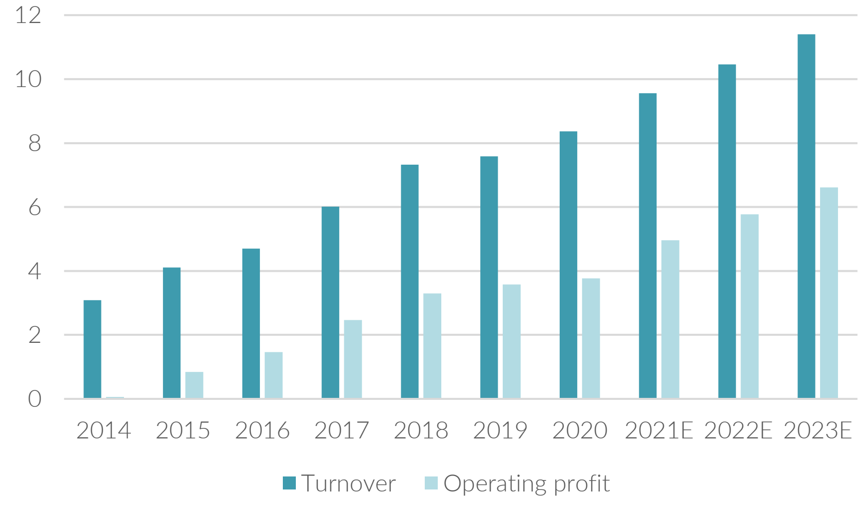
Guernsey is very much a mainstream financial centre, and its customers are a Who's Who of international financial and non-financial firms.

The business

Operating performance

The performance of TISE over the past few years has been impressive. Revenue has grown from £3.1m in 2014 to £8.4m in 2020, a CAGR of 18%, and costs have only grown at 7% p.a., leaving profits to have grown from just above breakeven to £3.8m in 2020. The first half of 2021 continued in the same vein with revenue +16% and profit metrics all up ca.45%.

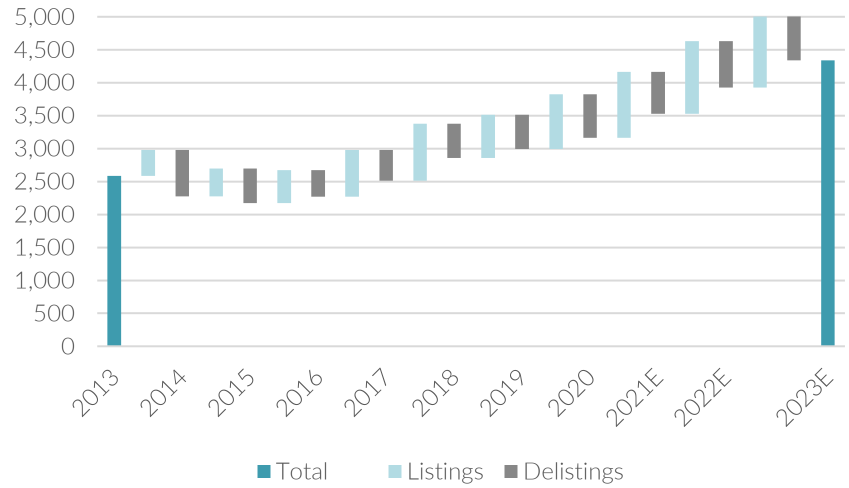
TISE operational performance, 2014-23E (£m)



Source: TISE, Hardman & Co Research

The growth has been driven by an increase in new listings from 393 in 2014 to 831 in 2020, a CAGR of 13%. There was a dip in 2019, which we believe was caused partly by the extension of QEE rules to multilateral trading facilities (MTFs) and to pre-Brexit market hesitancy. There were 507 new listings in the first half of 2021 compared with 390 in the first half in 2020.

Listings on TISE, 2014-2023E

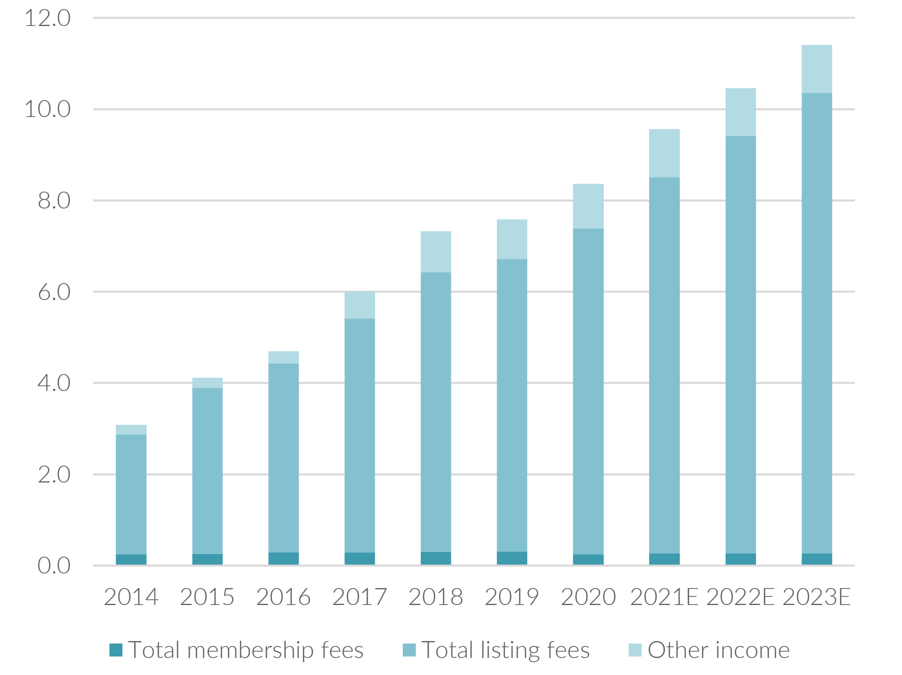


Source: TISE, Hardman & Co Research

The total number of listings has increased from 2,274 in 2014 to 3,162 at the end of 2020 a CAGR of 6% p.a.; and on to 3,431 as at June 2021. Issues are constantly delisting as bonds mature. Currently, ca.20% of listings are cancelled each year.

There are two principal listing fees: the initial listing fee when an issue is first admitted to the Exchange and an annual fee payable while it is still listed. The average initial listing fee was £3,400 in 2020 and the average annual fee was £1,400. In 2014, around half the total listing fees came from initial fees; by 2020, this had dropped to 39%.

TISE income sources, 2014-23E (£m)



Source: Hardman & Co Research

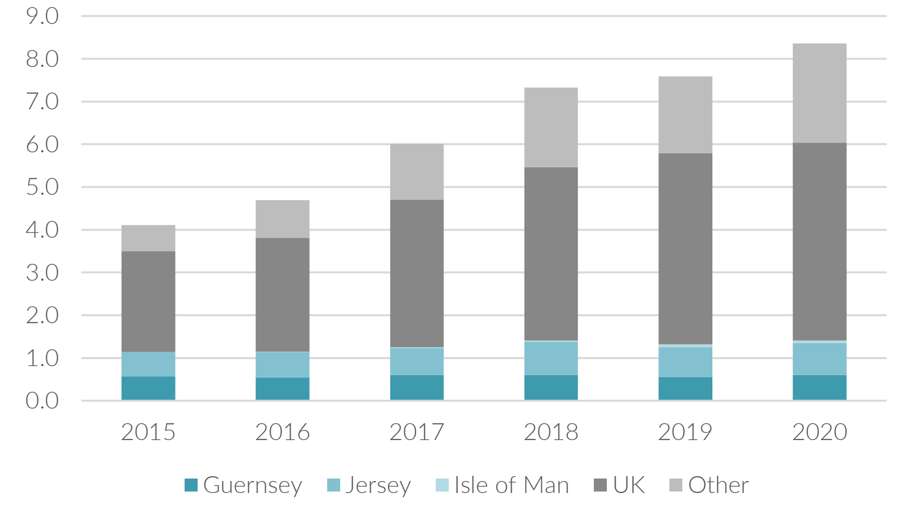
The other source of revenue is from members' fees. The number of members had fallen steadily from 46 in 2014 to 34 in 2020. This has been caused by consolidation among members and the clearing out of inactive sponsors. Members' fees generated just £250k in 2020, so they are a relatively small contributor. In the first half of 2021, the number of members increased for the first time since 2018 as TISE actively courted Dublin law firms involved in securitisation listings. TISE has decided to phase out membership fees over the next three years.

Future listings

For our forecasts, we have assumed 1,000 new listings in 2021, 1,100 in 2022 and 1,200 in 2023. The actual number of listings depends heavily on market conditions. Market activity has remained elevated since the start of the pandemic. With much rebuilding of the economy to do and interest rates set to be lower for longer, we expect activity in capital markets to be sustained. We are also expecting the delisting rate to remain static.

The geographical source of fees is dominated by the UK, which accounted for 55% of total fees in 2020 – a very typical year. It crept up to 58% in the first half of 2021. Guernsey, Jersey and the Isle of Man represented a further 17% and the balance came from Europe and across the world. With the expansion of the business into securitisations, and a concerted marketing effort in Dublin and London, we would expect the Irish-initiated listings to grow as a source of future business.

Geographical source of revenue, 2015-20 (£m)



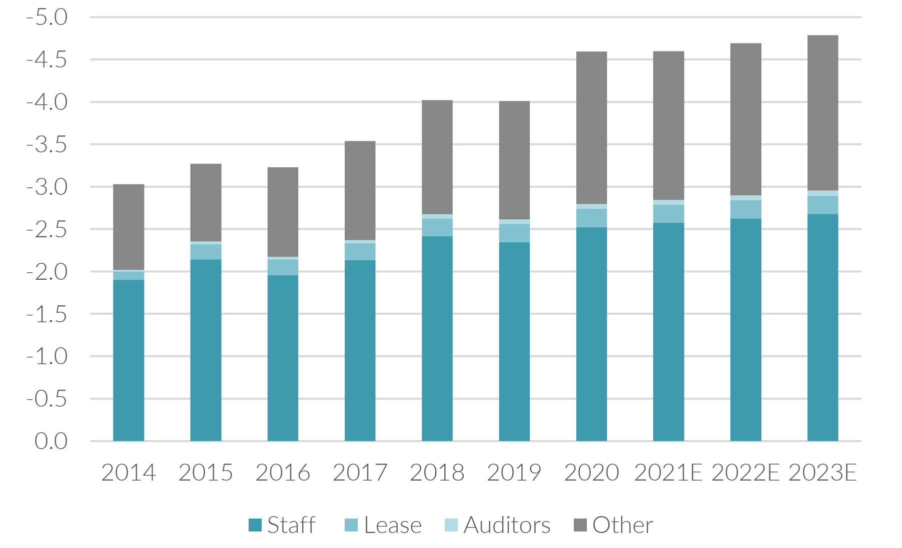
Source: TISE

Costs

The largest chunk of costs is staff, accounting for 55% of total costs. Overall costs account for about 55% of total income and have been consistent at around that level for the past few years. In the first half of 2021, costs were in line with 2H 20 and down on the first half of 2020. We have them growing at 2% a year from 2022E onwards. We are not expecting the shape of costs to change significantly in the future. With operating margins consistently at 45% or higher, this is a very profitable business.

TISE is investing in a new trading system, supplied by Avenir Technology. It is an auction-type system and will be ready in the second half of 2021. It is not expected to cost more than £200k. It has the capability to be upgraded to continuous trading if warranted.

TISE costs, 2014-23E (£m)



Source: Hardman & Co Research

Efficient operations are key to TISE's appeal to potential clients. It already operates a 3+1 system – that is, within three days of receiving an initial listing submission that meets the minimum information requirements, TISE commits to responding with a comments letter. For each subsequent review, it promises to respond within a day. This is best-in-class performance.

It has also introduced the TISE "Passport": a pan-European fast-track listing service available for those bond programmes already approved by a national competent authority within the EEA or UK. TISE will accept a pre-vetted bond programme where it has been "wrapped" with its templated "TISE Passport Letter". The completed TISE Passport Letter and corresponding bond programme together constitute a TISE Passport programme for the purposes of listing final terms on TISE. No fees are payable to complete a TISE Passport; thereafter, it is £800 per bond listed.

Opportunities for growth

TISE is looking at expanding into new products and geographies. Some of the high-growth segments are specialist areas such as insurance-linked securities (ILS) and collateralised loan obligations (CLOs).

Bond expansion

The biggest opportunity lies in the bond markets, and TISE has developed a Qualified Investor Bond Market (QIBM) to expand its presence here. Regulation and technology are revolutionising the bond markets. In particular, in Europe, MiFID II introduced new obligations of transparency in both the issuing and trading of bonds. Bond markets, though, are very different from equity markets. According to data published by the Federation of European Stock Exchanges (FESE), there were 7,214 European companies with listed shares on European Exchanges as of July 2020; while ESMA reported that there were more than 160,000 outstanding corporate bonds available for trading in EEA venues. Very few of these bonds will trade on a daily basis, and most will not trade at all for a month, or even longer. Usually, corporate bonds are active in the secondary market only for the first few days after they are issued and before they settle in the hands of long-term investors who will tend to hold them until maturity. What secondary market activity there is, is usually driven by credit events (such as a change in rating).

Liquidity vs. transparency

In such an illiquid market, improving transparency is very tricky. The market relies on market makers to provide liquidity, but they can't operate efficiently (i.e. profitably) if every trade is visible and their positions effectively become public. One solution is new electronic platforms: exchanges that connect end investors to each other without the need for broker intermediaries, although they are not excluded. One example of such a platform is MarketAxess, a $17bn NASDAQ-listed electronic platform for fixed-income securities. It said at the release of its 1Q 21 results that it saw electronic trading continue to advance in fixed income markets around the world. Nevertheless, the vast majority of trading currently still takes place Over-The-Counter (OTC, 50%) or through Systematic Internalisers (SIs, 26%).

QIBM: professionals-only market

Another trend is the issue of bonds that are only available to "qualified institutional buyers" (QIBs). These private placement bonds (also known as 144As after the relevant SEC rule number) have simpler disclosure requirements on the understanding that they will only be acquired by sophisticated investors. To become a QIB, you must have at least $100m under management.

TISE has developed a bond market for QIBs, QIBM, which can offer listing and trading beyond the typical bond classes – high-yield bonds and private equity-backed transactions – that it offered previously. It can now compete directly with the bond markets in Dublin and Luxembourg for the listing of securitisations, including CLOs, derivative bonds, as well as sovereign and public bonds.

There are just over 800 securities listed on QIBM, which gives it a market share of just 3%. There is ample scope for this to grow.

Earlier in 2021, TISE recruited Anthony Byrne, an experienced operator from Euronext Dublin, as Head of Bond Markets. He will be leading the thrust to become the leading European professional bond market. One early success is the signing of Arthur Cox as a listing agent for QBIM. Arthur Cox is one of Ireland's leading law firms and was approved as an authorised sponsor by the Irish Stock Exchange (now Euronext Dublin) in 2004. Two other prominent Irish law firms have also become listing members: Mason Hayes & Curran and Matheson.

Sustainable finance

There is also a whole new segment of "green" and "sustainable" bond issues, a sub sector of the Environmental Social and Corporate Governance (ESG) market. This is an ill-defined area with no standard rules but is clearly likely to be a popular area for future capital raising as issuers take advantage of asset managers seeking to burnish their environmental credentials.

TISE established a dedicated environmental-focused market segment, TISE GREEN, in 2018 and had its first four "green" bonds admitted to its Official List (a prerequisite) and the segment. In July 2021, the segment was relaunched as TISE Sustainable and now reflects a wider remit – companies with an environmental, social or sustainable purpose, which adhere to ESG standards, can be admitted as opposed to limiting it to just to bonds to fund "green" activities.

TISE is a member of the UN Sustainable Stock Exchanges initiative, reflecting its desire to be part of the sustainable capital markets ecosystem: both in the managing of its own business and in its role as a facilitator of global capital flows.

The TISE Sustainable initiative is an important one but not likely to be the largest driver of new business.

New trading system

TISE has not been renowned for its trading. It has lacked a proper price discovery platform and, without liquidity, it is hard to attract new listings to build its secondary market. Pools of liquidity are highly attractive businesses: once the liquidity is established, it is very hard to move it elsewhere. Liquidity attracts liquidity in a positive feedback loop, in our view.

TISE's new auction-based trading system will go live in 2H 21. It should improve the liquidity of existing listed equities. Also, the higher level of trading should help to attract further issues.

The system is also suitable for both the bond market – there is an increasing demand for secondary trading in long-maturity bonds – and the new private market initiative.

Private markets

Another potential area of expansion is "private markets". The vast majority of companies are not listed. For larger small companies – those worth between say £100m and £2bn – there are really only two sources of equity capital: a public stock exchange or private equity. The former has very strict regulations (especially when it comes to control and governance) typically, and the latter tends to come at the expense of control and can be expensive.

TISE is developing a new, third option for unlisted companies to enjoy some of the benefits associated with a listing or private equity funding, but without strict regulations nor loss of control. The private market will provide a safe and efficient rule-based platform to facilitate secondary market trading between shareholders and sophisticated investors in private company shares. It is aiming to introduce this service in 2022.

Summary

TISE is well-positioned to expand its business. It is a well-recognised and mature exchange. It has worked hard on being user-friendly. Its stance on regulation is that it should be practical – it needs to uphold minimum standards, but it doesn't want to overregulate to deter potential customers. Its reputation – and recognition by HMRC, the SEC and others – is crucial.

Threats

The rules governing securities are both TISE's strength and weakness. Their existence drives issuers to look for regulated exchanges to list on, but they can be changed at any time. For example, the QEE was extended in April 2018 to bonds that were admitted to trading on an MTF operated by an EEA-regulated recognised exchange. An MTF is similar to an exchange but generally without the onerous listing obligations, making it an attractive cheaper option. This inevitably introduced more competition from alternative listing venues.

On the plus side, it was the introduction of MAR in July 2016 that helped drive plenty of business into TISE's hands. MAR requires that policies and procedures are put in place to ensure compliance with its rules; for example, relating to additional disclosure requirements, the preparation of insider lists and reporting of transactions involving persons discharging managerial responsibilities. EU exchanges have incorporated MAR requirements into their listing rules as it is directly applicable in all EU Member States and affects all issuers on EU exchanges.

TISE listings of debt securities are not subject to MAR, but instead are subject to the requirements of TISE's QIBM Listing Rules (the "Listing Rules"). TISE's position is more flexible and recognises that specialist debt securities issued by SPVs/holding companies tend to be purchased and traded by only a limited number of sophisticated or institutional investors.

The EU recently reviewed how MAR was functioning and concluded that it worked well and did not need any significant alterations.

Current regulatory reviews

The UK Government has conducted a review of the tax treatment of asset holding companies in alternative fund structures. Its second consultation period ended in February 2021 and it published its findings in July with the intention of introducing legislation as part of Finance Bill 2021/2022.

Introducing the review, the UK Government said that it was prepared to make legislative changes to bring clear benefits by facilitating the flow of capital, income and gains between investors and underlying investments via UK companies. It was not prepared, however, to make changes that take significant amounts of existing UK taxable income and or gains out of the scope of taxation in a way that is inconsistent with the principles of the UK tax system. It said that *"the regime is intended to only be available to investment arrangements that involve the pooling of investor funds with professional investment managers. The regime is not intended to affect the taxation of profits from trading activities, UK property or intangibles."*

In order to restrict the new, looser, rules solely to legitimate investment vehicles, the definitions and qualifications have to be very tightly drawn. There are still details that need to be clarified and it is not clear that the proposed new regime will be plain sailing. As UK law firm Pinsent Masons commented "*the success of the qualifying asset holding companies (QAHC) regime and the ability of QAHCs to compete with overseas alternatives could potentially still be held back by the general complexity of the UK tax code, with many existing anti-avoidance rules in particular continuing to apply to QAHCs with modifications*". In other words, it may still be simpler to list on a recognised exchange overseas, in e.g. Guernsey, because it is not clear whether a vehicle will qualify under the new rules and the legal advice required might be as costly as any savings achieved. Furthermore, there may be an ongoing requirement to prove that the holding company still qualifies – an unattractive proposition for issuers looking for simple and cheap structures.

Cost of listing

After the first general consultation in March 2020, and introducing the second in December 2020, which was asking for specific measures, HM Treasury said, with respect to QEE: *"… a number of respondents estimated that listing generally costs between £20,000 and £30,000 per instrument. Respondents said that this cost and the administrative requirements involved in listing debt compared unfavourably with jurisdictions where no WHT is charged on interest or where an exemption is automatically available in many circumstances. A few respondents said that where debt was listed to access the QEE, it was most convenient to use a foreign stock exchange such as the International Stock Exchange. They said this was unappealing for funds that would like their structures to be entirely onshore."*

Summary

What looked as though it could only be construed as potentially bad news for TISE may prove to have a more modest effect after all. The issue that the UK Government is trying to resolve is the cost barrier for setting up asset holding companies in the UK and one of those costs are literally TISE's revenues: the cost of listing on an exchange. However, in order to ensure that the regime is not abused, the rules to qualify as a QAHC have to be so strict that it might not be worth many vehicles bothering. There are costs involved in listing on exchanges such as TISE, but, in the grand scheme of things, they are not that material. Also in TISE's favour, the process is well-known by issuers, lawyers, investors, etc. so that it represents a very small hurdle to clear.

REITs

The second aspect of the UK Government consultation that is relevant to TISE concerns the issue of Real Estate investment Trusts (REITs). REITs are specialist property investment vehicles that provide exemption from corporation tax on profits and gains from their UK-qualified property rental businesses. In return, UK REITs are required to distribute at least 90% of their taxable income for each accounting period to investors, where the income is treated as property rental income rather than dividends.

Number of UK-listed REITs

Source: TISE
Note: the 2021 figure is up to end-September

To qualify as a REIT, the company must be listed on a recognised stock exchange. For REITs that want a diverse ownership, liquid trading in their shares and, consequently, using the listing to raise further capital, the London Stock Exchange is ideal. However, for those REITs that are tightly held, long-term investments where trading is very much a secondary consideration, the rules and expense of the LSE are unattractive. TISE has proved to be a very attractive alternative listing venue for these REITs and it now hosts more than 40% of all listed UK REITs, with a further 10 listed in first half of 2021 alone, taking the total to 38, plus a further three since then.

After consultation, the UK Government has decided to remove the listing requirement if at least 99% of the shares are held by institutional investors. The measure will come into effect from 1 April 2022. It is not yet clear whether listed REITs held by institutional investors will seek to delist, and it might well encourage companies to become REITs that would not have under the previous regime. Whether it halts the current flow of illiquid, institutionally held REITs listing on TISE remains to be seen.

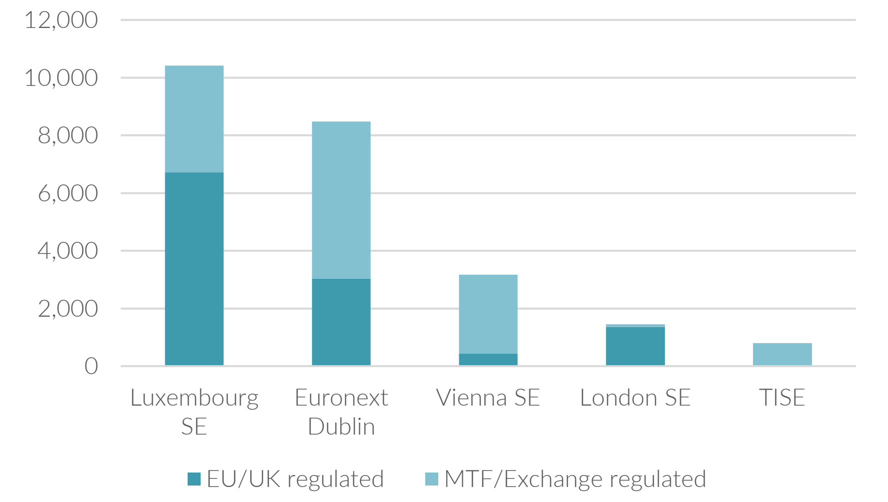
This represents a clear risk to TISE's business. REITs are not a large part of TISEs business, but they have been a growing, and successful one. One response of TISE is the new trading system, which should improve liquidity in the existing REITs and may encourage them to stay and others to join them in the future.

TISE's competitors also face the same regulatory threats and opportunities.

Competitors

TISE's two main competitors are the Luxembourg Exchange and the Dublin-based Global Exchange Market (GEM), which is now owned by Euronext. In 2020, there were more than 24,000 new European bond listings. Luxembourg had the largest share at 43%, followed by Euronext Dublin with 35%, Vienna with 13% and the London Stock Exchange with 6%. TISE's share was just 3%, and it is this that TISE is addressing with the launch of QBIM. It aims to get its share up to 14% within a few years.

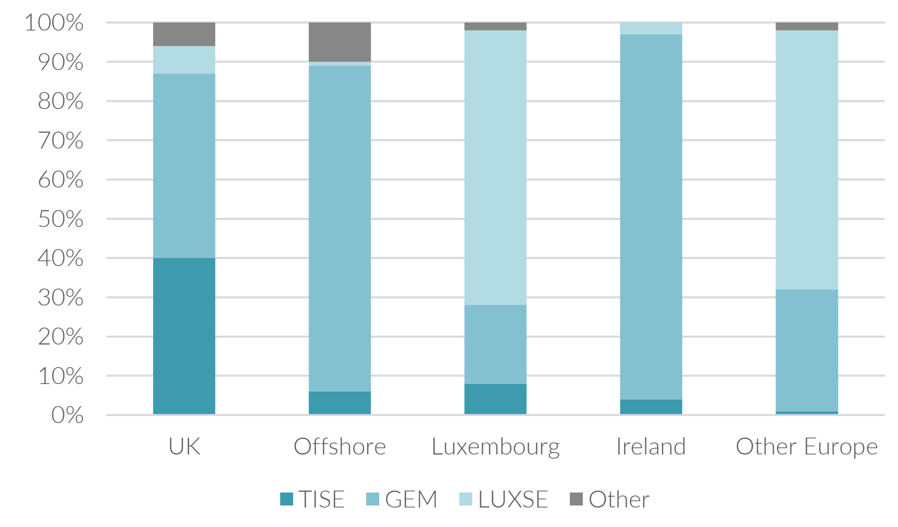
Share of 2020 European bond listings by market



Source: ISMA

Both Dublin and Luxembourg are in the EU and subject to European directives such as MAR. Luxembourg has established a listing-only market called SOL that is exempt from MAR but does not qualify for the Eurobond WHT exemption. Both exchange companies have set out to compete with TISE through streamlining their processes to allow efficient listing. Many of these listings are completely standard exercises and the most important thing is the efficiency with which they can be listed.

Share of corporate debt listings by issuer domicile



Source: Hardman & Co Research

Costs relatively unimportant

Despite the UK Government's motivation to reduce costs for the market participants, cost is not generally seen as that important when companies and their advisers are considering listing locations. This is partly because the cost differentials are not that great and partly because the listing costs are very small compared with all the other costs involved, which is not to say that participants wouldn't prefer not to have to incur the expense of listing.

The geographical congruence of issuers with listing locations is no coincidence. Concentrating everything in one jurisdiction makes everything simpler. Luxembourg and Ireland have grown as financial centres due to their low corporate tax regimes[1]. Ireland is coming under pressure from the EU to raise its corporate tax rate and is being threatened with exclusion from the €750bn Coronavirus Rescue Fund. So, the regulatory threats are spread around not just concentrated on Guernsey.

Although much smaller in size than TISE, two other competitors worth mentioning are Bermuda and Cayman Islands: two more offshore financial centres. Bermuda tends to specialise in insurance vehicles and the Caymans are seen as being rather loosely regulated. Neither is a particularly big player with European issuers, but they are clear competitors in the rest of the world, especially North America.

Reputation

In 2019, when the LF Woodford Equity Income Fund in the UK was struggling with liquidity issues, it sought to list several of its unlisted holdings on TISE to avoid breaching the limit on the proportion of unlisted equities it held in the fund. The purpose of the restriction on unlisted securities is to avoid problems of illiquidity if an open-ended fund is seeing redemptions. The TISE listing solved the listing requirement but not the liquidity issue. The lack of trading in the listed stocks raised questions about the valuation of the stocks within the Woodford portfolio.

TISE raised concerns with The Financial Conduct Authority on several occasions over the valuations and suspended the listings for some weeks. The listings were subsequently cancelled. It is clear that TISE did nothing wrong.

TISE commented in its 2019 annual report that it took "and will continue to take, regulatory action in order to protect the integrity of the market. It has also liaised at the earliest opportunity with other relevant authorities, especially where matters of concern fall outside of its own remit. This is in the best interests of the market and its participants."

We do not believe this will have any impact on TISE's reputation for running a reputable exchange.

[1] Both are in the same Group I IMF category of offshore financial centres as Guernsey. Landlocked Luxembourg proving, along with Switzerland, that "offshore" is a financial concept rather than a geographical descriptor.

Financials

Income statement

The key driver of our revenue forecasts is the number of new listings each year. We have assumed there will be 1,000 in 2021, and then 1,100 and 1,200 in each of the subsequent two years. If TISE is successful in reaching 14% market share, then these numbers will be substantially too low. We have also assumed constant average initial listing fees of £3,500 and annual fees of £1,500. TISE has introduced a new pricing package that includes a lifetime fee option as opposed to paying an initial and then annual fee. It is impossible to know what the take up of this might be.

TISE is also phasing out membership fees over the next three years. The more listings a member does, the quicker it will pay no fees. By 2025, there will be no membership fees. Total membership fees in 2020 were £248,000.

We have costs growing at just 2% after no growth this year. If revenue grows faster than we are modelling, there may be some additional staff costs to include, which might drag the forecast EBIT margin down a touch but overall EBIT would be higher.

Income statement, 2018-23E

Year-end Dec (£000)	2018	2019	2020	2021E	2022E	2023E
Turnover	7,323	7,585	8,362	9,560	10,461	11,403
Admin expenses	-4,023	-4,011	-4,593	-4,600	-4,692	-4,786
Operating profit	3,300	3,574	3,769	4,960	5,769	6,617
Interest income	58	53	23	25	25	25
Fair value gains/losses		6	9			
Profit before tax	3,358	3,633	3,801	4,985	5,794	6,642
Tax		-157	-179	-234	-272	-312
Net income	3,358	3,476	3,622	4,751	5,522	6,330
No. of shares (m)	2.70	2.82	2.82	2.82	2.82	2.82
No. of shares (fully diluted, m)	2.80	2.82	2.82	2.82	2.82	2.82
EPS (p)	124	123	128	168	196	224
EPS (fully diluted, p)	120	123	128	168	196	224
Dividend per share (p)	30.0	32.5	50.0	80	100	110
Special div. per share (p)		200.0				
EBITDA	3,362	3,608	3,817	5,008	5,817	6,664
EBIT margin	*45%*	*47%*	*45%*	*52%*	*55%*	*58%*
Tax rate		*4%*	*5%*	*5%*	*5%*	*5%*
Growth						
Turnover	*22%*	*4%*	*10%*	*14%*	*9%*	*9%*
EBIT	*34%*	*8%*	*5%*	*32%*	*16%*	*15%*
EPS	*33%*	*3%*	*4%*	*31%*	*16%*	*15%*

Source: Hardman & Co Research

Balance sheet

The TISE business is very cash-generative. Between 2014 and the end of 2020, the net cash and investments balance has risen from £3.1m to £10.7m and it has paid out a further £9.4m in dividends – £17m of net cash generated in the past six years. At the end of the first half of 2021, net assets had risen a further 16% to £10.3m.

TISE carries no debt and has ample distributable reserves. Even the £2.9m of creditors is mostly just deferred income – listing fees invoiced but not yet booked as income. Cash and cash equivalents includes £1.5m of regulatory capital.

Financially, this is a very robust business.

Balance sheet, 2018-23E

@ 31 Dec (£000)	2018	2019	2020	2021E	2022E	2023E
Intangible assets	0	0	0	80	80	80
Tangible fixed assets	54	59	67	190	192	194
Total fixed assets	54	59	67	270	272	274
Debtors	977	1,188	974	974	974	974
Investments	8,750	5,273	7,039	7,039	7,039	7,039
Cash, etc.	2,584	3,102	3,709	6,157	8,994	12,358
Total current assets	12,311	9,563	11,722	14,170	17,007	20,371
Creditors due within a year	-2,589	-2,926	-2,880	-3,036	-3,174	-3,314
Net current assets	9,722	6,636	8,842	11,134	13,833	17,057
Provision for other liabilities	-7	-10	-12	-12	-12	-12
Net assets	**9,768**	**6,686**	**8,897**	**11,391**	**14,093**	**17,319**
Called-up share capital	2,799	1,332	1,332	1,332	1,332	1,332
Share-based payments reserve	140	140	140	140	140	140
Retained earnings	6,830	5,215	7,426	9,920	12,621	15,848
Total shareholders' equity	**9,768**	**6,686**	**8,897**	**11,391**	**14,093**	**17,319**

Source: Hardman & Co Research

Cashflow

TISE's income statement is very transparent and converts pretty straightforwardly into cash. In general, there is small increase in negative working capital with the business growth; little in the way of investment in assets; and no large distortion from share-based payments.

The only large, non-operational line is the net acquisitions of investments, which is TISE managing its cash balance.

Cashflow statement, 2018-23E

Year-end Dec (£000)	2018	2019	2020	2021E	2022E	2023E
Profit before tax	3,358	3,633	3,801	4,985	5,794	6,642
Depreciation and amortisation	62	33	48	48	48	48
Share-based payments	52		0			
Interest	-50	-51	-33	-25	-25	-25
Tax paid		-150	-160	-179	-234	-272
Other	2	6	2			
Working capital change	364	120	149	100	100	100
Operating activities	3,788	3,591	3,807	4,929	5,683	6,492
Purchase of assets	-13	-38	-56	-250	-50	-50
Acquisitions of investments (net)	-3,850	3,473	-1,765			
Interest received	50	51	32	25	25	25
Investing activities	-3,813	3,486	-1,789	-225	-25	-25
Issue of equity	318					
Dividends paid	-820	-6,559	-1,411	-2,257	-2,821	-3,103
Financing activities	-503	-6,559	-1,411	-2,257	-2,821	-3,103
Increase in cash	**-527**	**518**	**608**	**2,447**	**2,837**	**3,364**
Cash start	3,111	2,584	3,102	3,709	6,157	8,994
Cash end	2,584	3,102	3,709	6,157	8,994	12,358

Source: Hardman & Co Research

Dividend

TISE's policy is to pay total annual dividends of approximately 50% of the group's net income during the relevant financial year. This dividend is expected to continue to be paid in two instalments in April and October. It may also pay special dividends when appropriate.

Risks

We have discussed at length the possible regulatory changes in the UK that pose potential threats to TISE's attractiveness or need as a location for securities listing. This remains the most pressing and serious threat to TISE's future profitability. TISE is taking the appropriate response to this threat and seeking to diversify the sources of its revenues further.

Any diversification carries risk of the new initiatives failing to reach profitability and losing the investment made in them.

Further changes in regulation in the UK or elsewhere will always provide challenges and opportunities.

Systems risks pose problems for all businesses and TISE is dependent on IT systems for the processing of listing applications. Its new trading system will also introduce security and continuity considerations.

For shareholders of TISE, there is another clear (and slightly ironic) risk, which is that there is very little liquidity in TISE's shares that are listed on its exchange. They trade only occasionally and only in small quantities. Regular returns may be received from dividends, but selling the equity could be difficult. TISE is focused on increasing the profile of the company, and spreading the story beyond the Channel Islands. This should help with liquidity along with the new trading system.

Valuation

As a rule, we tend to like comparable company valuations. There are three listed European stock exchanges; unfortunately, they are not comparable. Size alone makes the comparison tangential at best, but, even more importantly, they are substantial trading revenues, which generate significant revenues but also act as stabilising force for the revenue stream. It is extremely difficult to wrestle away trading from a dominant venue – liquidity attracts liquidity and moving it (without some seismic change) is extremely difficult and consequently very rare.

The Luxembourg Stock Exchange is a private company and not listed and The Irish Stock Exchange was acquired by Euronext. They would have made ideal comparators.

Having said that, TISE has shown that its business produces very stable and growing revenues. Initial and annual listing fees are attractive annuity streams. The average life of a listing on TISE is about six years. In the chart below, we show the number of listings in each year and the number remaining from that year's vintage, as at 1Q 21.

Listing lifetimes

Source: Hardman & Co Research

As a fall back, when no useful comparable companies are trading, we use a DCF model. The normal constraint on a DCF is the unknowable future cashflows. Here, the real concern is not the shape of the future revenue stream but the risk to its sustainability from regulatory interruption. To compensate for this, we have used a 15% central discount rate, notably higher than our usual 10%.

DCF valuation

£m	2018	2019	2020	2021E	2022E	2023E	2024E	2025E
Revenue	7.3	7.6	8.4	9.6	10.5	11.4	11.9	12.3
EBITDA	3.4	3.6	3.8	5.0	5.8	6.7	6.9	7.2
Tax	0.0	-0.2	-0.2	-0.2	-0.3	-0.3	-0.3	-0.3
Net cashflow	3.4	3.5	3.6	4.8	5.5	6.4	6.6	6.9
Discount factor				1.0	1.1	1.3	1.5	1.7
Discounted cashflow				5.0	5.0	5.0	4.5	4.1

Source: Hardman & Co Research

We have taken our forecasts out to 2023. We have a mid-term growth rate with a central assumption of 4% and have then assumed a perpetual growth rate of a nominal 2%. Since capex and depreciation are very low and nearly equivalent, we have used net income as a (very good) proxy for net cashflow.

DCF summation

Value components	£m
2022-25	18.7
2026 onwards	32.3
Total	51.0
plus net cash end-2021	13.2
Equity value	64.2
Equity value per share (p)	2,275

Source: Hardman & Co Research

Our central valuation works out at £64m, or 2,275p per share, based on a current issued share capital of ca.2.8m shares. We have also shown a table with varying growth rates for the two years between our forecast period (to 2023) and our perpetual calculation…

DCF sensitivity table – Valuation

Mid-term growth rate	2%	4%	6%	8%
Discount rate	£m	£m	£m	£m
10%	93	95	98	101
15%	63	64	66	67
20%	49	50	51	52

Source: Hardman & Co Research

…and how these values equate to multiples of 2021E EBITDA…

DCF sensitivity table – EV/EVITDA 2021E

Mid-term growth rate	2%	4%	6%	8%
Discount rate	(x)	(x)	(x)	(x)
10%	15.9	16.4	17.0	17.5
15%	9.9	10.2	10.5	10.8
20%	7.2	7.4	7.6	7.8

Source: Hardman & Co Research

…and 2021E PER.

DCF sensitivity table – PER 2021E

Mid-term growth rate	2%	4%	6%	8%
Discount rate	(x)	(x)	(x)	(x)
10%	19.5	20.1	20.7	21.2
15%	13.2	13.5	13.8	14.1
20%	10.4	10.6	10.8	11.0

Source: Hardman & Co Research

Directors

Charlie Geffen (Non-executive Chair)

Charlie has been Chair since January 2021. He is also a member of the group's Audit Committee, Nominations Committee and Remuneration Committee and was previously Chair of The International Stock Exchange Authority Limited.

Charlie is an English qualified lawyer with more than 30 years' experience advising on a wide range of corporate matters. After a law degree at Leicester, he joined Ashurst and spent 32 years there, including as Head of Private Equity and the past five as Senior Partner. He then joined US law firm Gibson, Dunn & Crutcher and, was Chair of the Corporate Practice in London.

Cees Vermaas (CEO)

Cees has been Chief Executive Officer since November 2020. He is responsible for all aspects of leadership and management of the company.

Cees has more than 20 years' experience within international financial market infrastructure. He has held senior executive positions within several international exchanges, including CEO of CME Europe Ltd, CEO of Euronext Amsterdam and Head of European Cash Markets for NYSE Euronext.

Guy Coltman (Non-executive Director)

Guy joined the board in February 2014 as an independent Non-executive Director.

Guy is an Advocate of the Royal Court of Jersey and qualified as a solicitor in England and Wales. He is a corporate partner of Carey Olsen's Jersey practice.

Gill Morris (Non-executive Director)

Gill is an independent Non-executive Director and was appointed to the board in January 2021.

Gill is a Chartered Accountant and Chartered Tax Adviser, she has more than 35 years' experience working in Australia, London and Guernsey, initially qualifying within the "big four" and then holding several senior leadership positions at Specsavers Optical Group. She is currently a Panel Member of the Guernsey Tax Tribunal.

Stuart Turner (Non-executive Director)

Stuart joined the board in April 2014 as an independent Non-executive Director.

Stuart has extensive IT and change management experience and has spent the past 30 years in the financial markets industry. He is a director of Avenir Limited, which has developed a new and innovative range of post-trade software for securities depositories and share registrars.

Anderson Whamond (Non-executive Director)

Anderson is an independent Non-executive Director and was appointed to the board in March 2017.

Anderson has over 30 years' experience in the banking and financial sector. He is an Executive Director of Fiera Capital (IOM) Limited (formerly Charlemagne Capital (IOM) Limited) and also a director of a number of listed and non-listed investment companies.

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In particular, Article 12(3) of the Directive states: 'The following benefits shall qualify as acceptable minor non-monetary benefits only if they are: (b) 'written material from a third party that is commissioned and paid for by a corporate issuer or potential issuer to promote a new issuance by the company, or where the third party firm is contractually engaged and paid by the issuer to produce such material on an ongoing basis, provided that the relationship is clearly disclosed in the material and that the material is made available at the same time to any investment firms wishing to receive it or to the general public…'

The fact that Hardman & Co is commissioned to write the research is disclosed in the disclaimer, and the research is widely available.

The full detail is on page 26 of the full directive, which can be accessed here: https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2031-EN-F1-1.PDF

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