**Market data**

EPIC/TKR	BUR
Price (p)	644.5
12m High (p)	660.0
12m Low (p)	206.5
Shares (m)	208.2
Mkt Cap (£m)	1342
Total Assets (\$m)	756.8
Free Float*	86%
Market	AIM

*As defined by AIM Rule 26

Description

Burford Capital is a leading global finance and professional services firm focusing on law. Its businesses include litigation finance, insurance, law firm lending, corporate intelligence and judgement enforcement, bankruptcy litigation funding, advisory and professional services, and a wide range of professional activities.

Company information

CEO	Christopher Bogart
CIO	Jonathan Molot
Chairman	Sir Peter Middleton
	+1 (212) 235-6820
	www.burfordcapital.com

Key shareholders

Directors	14%
Invesco Perpetual	27.8%
Woodford Investments	10.0%
Fidelity Worldwide	8.7%
Aberdeen Asset	4.9%

Next event

14 Mar 2017	Full year results
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Analyst

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Burford Capital

Positive judgement from the secondary market

On 3rd January Burford announced that on 30th December it had sold an interest in the Petersen claim to a third party investor at a price that implied a valuation of more than ten times Burford's investment. The claim has been progressing well and, having passed a significant milestone in 2016, would have been expected to rise in value regardless of any transaction. This is the second secondary market transaction that Burford has completed, each demonstrating a gain over the existing valuation. In this report we discuss the implications for valuations, both for this specific case and for the portfolio as a whole.

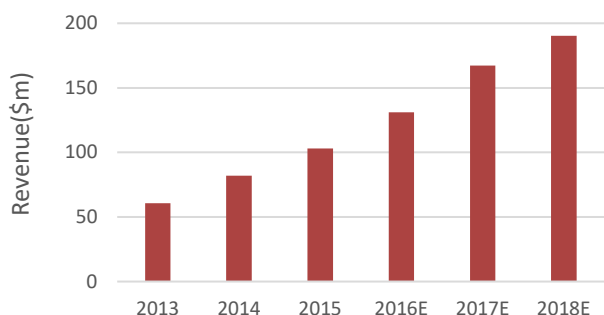
- ▶ **Earnings:** Although the multiple of investment is well ahead of Burford's likely valuation of it, the statement suggests that the actual monetary gain will be small. We have upgraded our expected revenue by \$4m to reflect this gain, giving a 5% upgrade to 2016E.
- ▶ **Balance sheet:** Burford have invested a sum 'of less than \$18m' into the Petersen claim. There may be an effect on the valuation, but this is very hard to quantify. The asset was likely to be revalued upwards anyway, and, as discussed in this report, this is unlikely to reflect the full transaction value.
- ▶ **Valuation:** With the deal enhancing earnings and supported by helpful currency moves, Burford's rating remains good value despite the strong share price performance. The prospective P/E for 2018E is only 15.0 times, while an 18% RoE with strong growth suggests excellent metrics all round.
- ▶ **Risks:** The investment portfolio is fairly diversified, but retains some very large investments, which means revenue may be volatile. As the company matures we would expect that to decrease, but not to disappear. The Petersen case shows that this volatility is not simply a negative.
- ▶ **Investment summary:** Burford has already demonstrated an impressive ability to deliver good returns in a growing market while investing its capital base. As the invested capital continues to grow, the litigation investment business will continue to produce strong earnings growth.

Financial summary and valuation

Year end Dec (\$m)	2013	2014	2015	2016E	2017E	2018E
Revenue	60.7	82.0	103.0	131.0	167.3	190.2
Operating Profit	42.5	60.7	77.2	100.9	125.7	141.8
Reported net income	2.6	45.4	64.5	80.6	99.5	114.8
Underlying net income	40.1	53.0	64.5	80.6	99.5	114.8
Underlying Return on Equity	11.7%	12.1%	16.3%	17.4%	18.6%	18.2%
Underlying EPS (\$)	0.20	0.26	0.32	0.39	0.48	0.55
Statutory EPS (\$)	0.01	0.22	0.32	0.39	0.48	0.55
Dividend per share (\$)	0.05	0.07	0.08	0.09	0.11	0.12
Yield	0.6%	0.8%	1.0%	1.1%	1.3%	1.5%
NAV per share (\$)	1.72	1.87	2.12	2.40	2.79	3.34
P/E (x) (underlying)	41.4	31.4	25.8	20.8	16.8	14.6
Price/NAV (x)	4.7	4.3	3.8	3.4	2.9	2.4

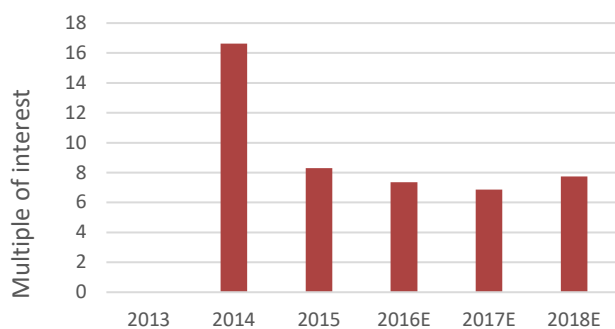
Source: Hardman & Co Research

Revenue



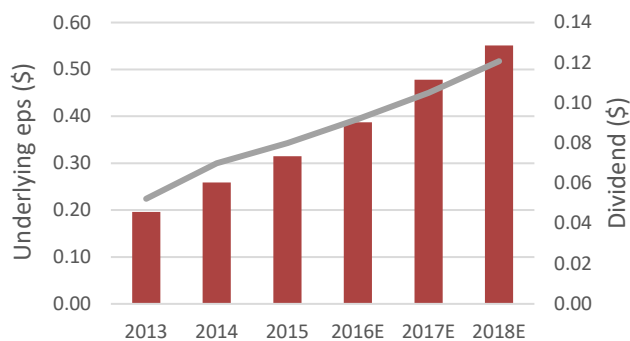
- ▶ Growth depends on pace of investment and conclusions
- ▶ Accelerated investment in 2016 will boost 2017 and 2018 revenue
- ▶ Continued investment in the business underpins the growth
- ▶ Acquisition adds revenue from 2017 onwards

Interest Cover



- ▶ No debt prior to 2014
- ▶ Retail bond issues in 2014 and 2016
- ▶ \$43.75m loan note issued for acquisition
- ▶ 2014 issue was mid-year so only partial accrual of coupon

Eps and dividend



- ▶ Full effect of large single \$100m investment coming through properly in late 2016 and into 2017
- ▶ 2015 boosted by large single gain
- ▶ 2016 results to date showing benefits of a wide range of investments
- ▶ Some large single claims may introduce volatility in the future

Source: Company data; Hardman & Co Research

Background

The valuation of illiquid investments almost inevitably has a degree of opaqueness, and Burford's litigation finance portfolio is no exception. Burford introduces as much objectivity as possible and usually adjusts the value of an investment according to progress through the legal process. This is sensible – for example, very weak cases may well be dismissed very early on (though Burford tends not to invest in these in the first place). The size of any adjustment will depend on the case and the terms of the contract and, inevitably, will have an element of subjectivity.

Burford management believe they are being conservative in their valuations. The evidence to date has supported this and has primarily come from the further gains on the conclusion of investments. For example, over the 30 months since December 2013, gains on realisations have slightly exceeded fair value movements. This would indicate that the full value of realisations is not being anticipated in the valuations.

Ideally there would be a secondary market in litigation finance investments against which valuations could be benchmarked. This seems unlikely on a large scale, not least because the work involved in doing diligence on a case is substantial and financiers have, with good reason, preferred to be discrete about the individual cases they are involved in.

In the first half of last year Burford completed a single secondary market transaction and received an offer to complete a second transaction. The amount involved was small, but did give a gain over the carrying value. The unaccepted offer would also have given a gain had it gone ahead.

Petersen Investment

Unusually for a Burford case, many of the details of this claim have been made public. This case refers to the ownership of YPF, an Argentinian oil company. The Petersen Group held a 25% stake which was expropriated in 2012. Repsol, whose 50% stake was also expropriated, started suing the Argentinian government and a settlement was reached with a payment of approximately \$5bn.

The Petersen Group has been liquidated, and Burford is providing finance to the liquidators to pursue a claim in a New York court. Earlier this year the court denied Argentina and YPF's motions to dismiss the claims, which is very positive. The case is now at an interlocutory appeal as of right.

Burford to date has invested a sum of less than \$18m in the case. The company will be entitled to a gross payment of 70% of any recovery, though have cautioned that expenses in this case are meaningful and that the net recovery will probably be below 60%. It should be clear that this case could, if successful, potentially provide a significant gain to investors. However, like all individual cases, there is a potential binary nature to the outcome and no recovery is assured. The litigation itself has not started yet, and if this goes the distance then it could be some years before it is resolved.

In a secondary market transaction Burford has sold an interest in the Petersen case. The amount of the interest is described as 'immaterial', while noting that the price paid was ten times the amount invested, leading to a transaction size of several million dollars.

The transaction took place on 30th December 2016, so will apply to FY2016. Given the progress in the case in 2016, there would probably have been an uplift to the valuation this year, though Burford have not indicated what that would have been.

Effect on Burford

This very positive for Burford, but it is not clear whether this will have a meaningful effect on the company's finances in the short run. Hardman & Co would make the following observations:

- ▶ The amount involved in the transaction was very small. It seems unlikely that the same valuation could be applied to the whole investment.
- ▶ Burford has still to get the views of their auditors.
- ▶ The secondary market is very limited and to date Burford can only evidence two transactions. In particular, Burford does not *need* to get its capital back quickly and consequently is only likely to transact value enhancing deals.

The latter in particular means that there will be no effect on the valuation of the rest of the portfolio. We think it is unlikely that the secondary market will ever reach the stage that a market based valuation approach will be feasible, but those to date do give some further support to the management's belief that they are being conservative.

The company also cites advantages for risk management and capital efficiency. Given the size of the transactions to date we do not believe that these are significant, but could have the potential to become so if further ones occur.

Summary

Regardless of how the transaction gets reflected in the accounts, this is a positive for investors. They get further confirmation that Burford's valuation process is conservative. Additionally, there is an indication that a third party not only believes in the value of the Petersen case, but also that there remains sufficient further upside to invest.

It does augur well for future gains and further justifies a premium rating for the company.

Financials and Forecast

The sale was described as 'several millions dollars', but also as 'immaterial' to the claim. We have upgraded our revenue figure by \$4m to reflect this additional gain. We have not adjusted our fair value movements, as the gain may be offset significantly by the uplift that would happen anyway and, so, may be incorporated in our expected figures.

We note, as before, that our revenue forecasts largely reflect an expected average based on analysis of Burford's track record. Individual cases are binary in nature and, therefore, impossible to explicitly forecast. Burford has a few large cases, including the Petersen claim, which may have a significant but impossible to forecast impact on the results.

Summary financials						
Year end Dec (\$m)	2013	2014	2015	2016E	2017E	2018E
Revenue	60.7	82.0	103.0	131.0	167.3	190.2
Expenses	18.1	21.3	25.8	30.1	41.6	48.4
Operating Profit	42.5	60.7	77.2	100.9	125.7	141.8
Finance cost	0.0	3.7	9.3	13.7	18.3	18.3
Exceptional items	-40.4	-9.7	0.0	0.0	0.0	0.0
Reported pre-tax	2.1	47.3	67.9	87.6	107.4	123.5
Reported taxation	0.5	-0.7	-2.2	-5.7	-6.7	-7.5
Minorities	0.1	1.2	1.2	0.6	0.0	0.0
Underlying net income	40.1	53.0	64.5	81.2	100.7	116.0
Statutory net income	2.6	45.4	64.5	81.2	100.7	116.0
Underlying Basic EPS (\$)	0.20	0.26	0.32	0.40	0.48	0.56
Statutory Basic EPS (\$)	0.01	0.22	0.32	0.40	0.48	0.56
Dividend (\$)	0.05	0.07	0.08	0.09	0.11	0.12
Balance sheet						
Total equity	351.5	382.7	434.3	499.0	580.0	696.1
Invested Capital	173.6	207.0	239.0	421.4	491.8	565.0
Fair Value Balance	214.9	266.3	319.6	574.4	722.2	881.7
Total Assets	376.1	533.2	594.1	783.3	864.3	936.6
NAV Per share (\$)	1.72	1.87	2.12	2.40	2.79	3.34
Return on Equity	0.8%	12.4%	16.1%	17.5%	18.6%	18.2%

Source: Hardman & Co, £1=\$1.26

Notes

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