Change in performance fees accounting

Presentation Transcript
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Christopher Hunt

Good afternoon and thank you for joining us today. As you'll have read in the announcement this morning, over the last five years, ICG has doubled its fee earning AUM. And within that we have grown our equity-like strategies by three times. These strategies have higher performance fee potential. And in order to make this component of the revenue more visible and to remove certain elements of management judgement , today we are announcing a change to the way we recognise performance fees in our financial statements. These changes will be implemented at our H1 results, which we will announce on the 18th of November.

I'm joined by our CFO, David Bicarregui, who will give an overview of the changes we are putting in place and we will then take questions. The slides are available on our website along with the accompanying announcement. As a reminder, and unless otherwise stated, all financial information discussed today is based on alternative performance measures, which excludes the consolidation of some of our fund structures required under IFRS. You can submit questions verbally or through the online platform. Details are available on the portal. And with that, I'll hand over to David.

David Bicarregui

Thank you Chris, and good afternoon everyone. I'd like to start with a bit of context. Over the last decade, we have grown organically to become a global player in a number of investment strategies where we believe there are significant runway of growth, such as structured capital, private equity secondaries, private debt, and real assets. Over the last five years, our fee earning AUM has doubled. And as a result of mix shift and growing in higher fee strategies, our weighted average management fee rate has grown from 86 basis points in FY20 to 97 basis points in FY25. So we are managing more of our client's capital in higher return, higher fee strategies. This deliberate strategic decision about where to orientate our growth has positive implications for the future trajectory of management fees and for performance fees.

We have three revenue streams. Management fees represents the majority of our fee income and are occurring in nature, visible and long-term. Performance fees are small but increasingly valuable revenue stream for us. Over the last five years, they've represented 12% of our total fee income on average. And the fair value movements in the balance sheet investment portfolio, which over the last five years have averaged 13%. Today we are a very fee centric business, with management fees accounting for the large majority of our revenue line. So zooming in on performance fees and to recap on how our performance fee model works, on the left hand side of the slide, we set out an illustrative representation of what performance fee pool would look like for an $8 billion fund generating a gross MOIC of 2.0x. As you can see, ICG will be entitled to $280 million of performance fees, which will be received in cash over the life of the fund.

The accounting for this therefore has three components, which we disclose in our full year and our half year results. The cash received, in this case $280 million in total, which is not impacted by today's change. These are sometimes referred to as realised performance fees. Secondly, the revenue recognition, which over the life of the fund will equal the cash received, but the timing will differ. The timing is the P&L component impacted by the changes announced today. And finally, the balance sheet asset of recognised but unrealized performance fees, which will also be impacted by the adjustments today. These three components as reported in fully results FY25 are set out on the right hand side of this page. Going forward, we will continue to disclose all three metrics at a group level.

Performance fees have been an important contributor to our top line. Over the last five years, the cumulative P&L has been almost £300 million and we have received £210 million in cash. As of the 31st of March, 2025, we had a balance sheet asset of £108 million. As discussed at the beginning of the presentation, we have deliberately shifted the composition of our business and our fee earning AUM, moving towards higher return, higher fee strategies as part of our approach to diversifying the business. Our equity-like strategies, which have higher performance fee potential, have grown three times in absolute terms and now represent over half our fee earning AUM compared to a third in March of 2020. Put another way, given the higher management fees these strategies earn along with their higher performance fee potential, the shape of our fee earning AUM today has significantly more embedded value for shareholders than it did five years ago. So looking ahead, based on our waterfront of products today, we expect this trajectory to continue.

The changes we're making today make the value of our performance fees more visible. The main change revolves around timing of when we start recognising performance fees for a fund and how we will accrue that as the fund matures. Going forward, we will now recognise performance fees for a fund when the subsequent vintage holds the first close and the investment period of the current vintage ends. So taking a practical example, Europe mid-market, you will see Europe mid-market II recognising performance fees once its investment period ends and Europe mid-market III holds the first close. We will accrue this on a linear basis, assuming a twelve-year fund life, compared to 10 years before. The valuation for the purpose of calculating the carry will continue to be based on the fund's current NAV. These changes combined also reduce the management judgement required in the P&L.

On this page, we have set out a modelled example. And the team can talk you through this in more detail offline if helpful. There are therefore three factors that feed into the performance fee recognised in any given year. Firstly, a binary gate of whether the investment period at the prior fund has ended and the subsequent vintage has held a first close. The passage of time, as the fund moves towards the end of its life, and the development of the fund's NAV. Using the model from a few pages back of an $8 billion fund generating two times MOIC resulting in a potential carry pool to ICG of $280 million. For simplicity, we've assumed the fund has 10 assets in its portfolio, all of equal size, and has the same value creation linearly deployed and linearly realised. As you can see, the P&L recognition starts in year four, which is when we assume the following vintage has had a first close and the current vintage ends its investment period.

At that point, we take the fund's MOIC, 1.5x in year four, best fees and expenses and reduce ICG share by the time factor. In future years as the fund accretes value, as it does, for example, between years six and seven when the MOIC increases from 1.9 to two times, the P&L recognition reflects both the passage of time and the value increase. If there's no value accretion, such as in year 10, the P&L is just the passage of time, in this case 1/12th of $280 million, which is $23 million. A couple of things I'd flag here. Firstly, cash and P&L are the same at the end of the fund's life. And secondly, nowhere do you actually see the full value of the performance fees to ICG at any time in point in the P&L, cash flow or balance sheet because it's over a period of time and the linear movements are small relative to the total.

If we then apply this to one of our funds, here we show Europe VI, we can see how the new and old approaches differ in terms of recognition. Of course, cash is unchanged. Given the practical example, the current approach for Europe VI is based on the previous assumption of 10 years fund life compared to 12 years now, which in practise means the difference between the two initial recognition points, A and B, is relatively small on this chart, that in fact be larger if Europe VI were discounted over the 12 years. But you can see the new approach would likely have resulted in smoother recognition and would've converged to cash quicker.

So to recap on these changes and then looking ahead, there'll be no impact to the timing or amount of cash received. We expect a one-off recognition in our upcoming half year results of between 65 and £75 million to reflect the changes outlined today. This is largely a result of starting to recognise full performance fees for Europe VIII, strategic equity III and IV, mid-market I and infrastructure Europe I. For the half year, we expect total performance fees to be in the range of 90 to £95 million.

We are also increasing our medium term guidance for performance fees and FMC operating margin performance fees are now expected to be in the range of 10 to 20% of total fee income compared to 10 to 15% previously. And as a mechanical consequence of that change, the FMC operating margin is now expected to be in excess of 54% compared to 52% previously. In summary, as a result of our deliberate shift to high return strategies over the last decade, there is significant potential value to shareholders from performance fees. The changes today serve to help underline that value and make it more visible in our reported financials.