3 Reasons to Reconsider IGM Financial Inc.

Description

The speculation in recent years has been that Canada's regulatory bodies would outlaw the deferred sales charge (DSC) purchase option for mutual funds—a form of financial advisor compensation that's been condemned by many in the financial planning community.

Well, if the move made by Investors Group is any indication, they won't need to. Industry participants will do it for them.

Investors Group, a subsidiary of **IGM Financial Inc.** (TSX:IGM), announced on Monday that it will discontinue selling DSC funds as of January 1, 2017. In addition to dropping the controversial fee structure, Investors Group is reducing the annual fees on no-load (NL) funds between four and 10 basis points. That might not seem like a lot, but on $11.4 billion in assets under management that adds up to a little more than $9 million annually.

This is a big step for IGM and one reason to reconsider its stock.

Historically, Investors Group funds have been considered some of the most expensive in the country. In 2011 financial planner Ted Rechtshaffen highlighted the problems he had with their funds in an op-ed in the *Globe and Mail*. Among them were poor performance, high fees, and a majority of its funds are sold DSC.

Back in July 2012 it started the process by cutting mutual fund fees between five and 40 basis points on two-thirds of its product offerings. In mid-June it announced fee cuts (effective November 1) on four of its equity mandates that ranged between 15 and 25 basis points annually. Yesterday, IGM addressed both the DSC issue and touched on the fees question.

At the time of the 2012 fee reductions, analysts pointed out that this necessary strategic move would result in a short-term hit to IGM's earnings.

"IGM was an outlier in terms of MERs and the fee reduction will bring it back within a competitive range, albeit at the higher end," stated CIBC analyst Paul Holden in the *Financial Post* at the time. "We view this as a necessary move to stay relevant in an increasingly competitive industry. Lower fees should help sales, but we will wait to see by how much."

Fast-forward to today, and it's obvious IGM continues to remake its mutual fund business, so it remains a relevant player in the Canadian financial services industry. This move to me is a statement by the company that it no longer wants to retain clients under duress (seven-year DSC schedules), but rather through great products at reasonable prices.

Cynics probably aren't buying it. I am. This is a big deal.

The second reason to reconsider IGM stock is its yield. Currently providing investors with 6.3%, the company is essentially paying you to wait for them to revamp its business to the extent it can grow again.

Fool.ca contributor Nelson Smith believes that's best achieved by cutting its dividend and using the proceeds to invest in a lower-cost alternative, whether that's cutting management fees further still or acquiring some sort of digital advisory service that can keep fees low through technology.

At the end of the day IGM generates about $500 million in free cash flow. That's down from its high of $850 million in 2010. Back then it was paying a dividend of $2.05 per share for a 74% payout ratio. Today, it's up to $2.25 per share with a 77% payout ratio.

A better solution would be to curtail its share repurchases—it's spent $367 million over the past two years.

First, cutting dividends in today's low-rate environment is not looked upon favourably by investors; second, the C-suite generally mishandles share repurchases, often buying at market tops rather than market bottoms.

IGM Financial hasn't cut its dividend in the last decade. I don't believe it's about to start.

And the final reason to buy is, the future is here.

In May, IGM announced it would take a 10% interest in Personal Capital Corporation, a U.S.-based robo-advisor founded by Bill Harris, the former CEO of both **Intuit Inc.** and **PayPal Holdings Inc**. Initially investing $50 million, by the end of 12 months it will have spent another $25 million for an additional 5% interest, bringing its total equity ownership to 15%.

We've seen this before.

IGM's parent, **Power Financial Corp.** (TSX:PWF) originally put $10 million into Toronto robo-advisor Wealth Simple in April 2015. It added another $20 million in early 2016 to bring its ownership position to 60.4%.

Power Financial holds interests in digital advisory services on both sides of the border. Look for further integration of the two businesses sooner rather than later.

This is very good news.

CATEGORY

1. Investing

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1. TSX:IGM (IGM Financial Inc.)

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