

Mossberg's Investor Digest

Best Idea Profile

Virtus Investment Partners (Nasdaq: VRTS)

DESCRIPTION:

Headquartered in Hartford Connecticut, Virtus Investment Partners is an investment management firm with approximately \$21 billion under management. The company manages money for individuals and institutions through a group of affiliated and unaffiliated managers with multiple independent investment strategies. Virtus was spun out of The Phoenix Companies (NYSE: PNX) on December 31, 2008.

KEY INVESTMENT CONSIDERATION:

Removal of corporate burden will aid in restoring margins to nominal industry levels – Because it was part of a larger corporation, Virtus' corporate burden was excessive and not indicative of the profitability levels that can be produced based on its book of business. The company is in the process of right-sizing its operations and reducing the corporate burden it inherited from The Phoenix Companies. For example, the company has reduced its annual corporate office rent expense from \$2.8 MM to \$0.8 MM; human resources expense from \$3.0 MM to \$0.7 MM; and communications expenses from \$1.3 MM to \$0.4 MM.

Good business with great returns - With normalized industry EBITDA margins in the 20% to 40% range, the money management business is highly profitable, requires limited capital and delivers strong returns.

Opportunity for the best managers to take market share – Given the turmoil in capital markets investors are firing their long-time money managers and hiring new ones. Unlike the good times of a bull market, this means market share is up for grabs and those managers with the best records will take share. About a third of the funds managed by Virtus' affiliates have Morningstar ratings of 4 and 5 stars and the majority of the funds are 3 stars.

Sizable deferred tax loss carry forward could be a hidden asset. – The company has a deferred tax asset of \$115 million that represents Virtus' share of the tax loss carry forward of its former parent. The company has recorded a valuation allowance of \$108 million against the tax asset, because according to the accountants, the valuation has to be "objectively verified". At the time of the spin out it was challenging to "objectively verify" the company's future growth and profitability. If management is successful in restoring growth and profitability, it's possible the valuation allowance could be removed. This means the company's tax bill will be substantially reduced in the coming years.

VALUATION:

Virtus was spun out of its former parent in a taxable transaction, which is fairly atypical and puts selling pressure on the stock for those shareholders who need to sell part or all of their shares to meet the tax obligation. Since the beginning of the year, approximately 90% of the float has traded, which means it is likely that this tax affected selling is complete and there will be less artificial downward pressure on the shares. Before the company was spun out from The Phoenix Companies, Virtus sold a 23% equity stake for \$45 million to Harris Bankcorp, which would imply a valuation over \$30 per share. For Harris to complete a transaction in October of 2008 (one of the most uncertain times in the history of global financial markets) and pay a price that is more than 2x today's levels implies a large vote of confidence from Harris. Longer term, Harris, which is owned by BMO Financial Group, is a likely acquirer of Virtus. Historically money management firms trade at a ratio of approximately 2.5% of enterprise value to assets under management. VRTS trades at just 0.57%. As the company right-sizes its operating expenses and proves its ability to deliver industry margin levels, a return to historical valuations equates to a valuation multiple of 4x current levels.

(Nasdaq: VRTS)

Investment Data (as of 5/22/09)

Recent Price	\$15.15
52-Week Range	3.78 - 15.92
Fiscal Year End	December
Dividend	N/A
Yield	N/A
Shares Outstanding	5.8 MM
Average Trading Volume (3 mos)	68,000
Market Capitalization	88 MM
Convertible Preferred Stock	46 MM
Cash	27 MM
Long Term Debt	12 MM
Enterprise Value (EV)	119 MM
LT Debt/ Equity	0.5
Tangible BV/ Share	N/A
TTM Revenue	153 MM
P/ Revenue	0.6x
TTM EPS	n/a
P/ EPS	n/a

We attempt to provide subscribers with reasoned opinions based on our analysis of publicly available information from sources believed to be reliable, but make no representations as to its accuracy or completeness. Best Idea profiles are not based upon individual needs of subscribers nor are they an offer to buy or sell securities. Additional disclosures can be found under the Disclosures portion of the Mossberg's Investor Digest website.