EQUITY RESEARCH – COMMISSIONED RESEARCH
Research report prepared by DNB Markets, a division of DNB Bank ASA
Financials
Q4 results review
This report was completed and disseminated at 6:43 CET on 04 February 2021

4 February 2021

ESG insight

VEF

One 'unicorn' down, two to go

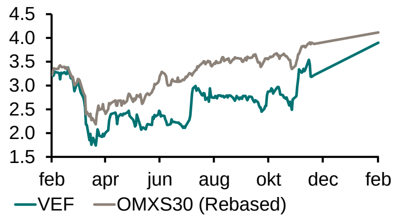
The Covid-19 pandemic is accelerating fintech momentum in emerging markets, where VEF's tech-enabling leaders are gaining significant advantage over incumbent banks with high fees and unsophisticated products. We see VEF as a unique, multifaceted story, and forecast ~20% NAV growth in 2021, driven mainly by Konfio; with a lot of sector liquidity and industry deals, we do not rule out portfolio exits. We have raised our fair value to SEK3.9–5.1 (3.2–4.4).

Portfolio highlights in Q4. 1) VEF's NAV rose 16% QOQ in Q4 (6% in local currencies), driven mainly by a recent USD255m funding round in Creditas valuing VEF's portfolio gem at USD1.8bn (in line with our Q3 2020 value); 2) having raised SEK522m through a directed share issue, VEF's net cash is USD54m, which should allow it to commit ~USD20m to its existing portfolio while letting management leverage the VEF brand to secure future deal flow in frontier markets, where we expect smaller ticket investments in Pakistan, India, and Mexico will be prioritised; and 3) we expect its portfolio holdings to maintain 2–3x YOY revenue growth in 2021, where we see Konfio, Juspay, Nibo, and TransferGo as potential NAV catalysts.

Creditas has started to provide quarterly trading statements. We believe this increased transparency should expand the investment community's appetite for its growth prospects while taking another step towards readiness for an equity offering, in our view. For 2020, despite pandemic headwinds, Creditas grew: 1) its credit portfolio by ~85% YOY, to BRL1.3bn (~USD230m); 2) new loan origination by ~70% YOY, to BRL900m (USD166m); 3) revenues by ~88% YOY, to BRL336m (~USD62m); while 4) delivering a contribution margin of 52.8% (down 4.4%-points YOY), and lowering its net loss by 8% YOY, to BRL186m (~USD34m). We believe the stand-alone Q4 report was also encouraging with 55–85% YOY topline growth while lowering the net loss by 18%, proving the attractiveness of the business model as revenues scale up. We are still in the early stages of penetrating the huge untapped secured lending market in Brazil and Mexico, and we believe the recent USD255m funding should allow Creditas to emerge as an asset-light leader with a potential equity offering acting as a catalyst for VEF in 2022–2023e.

Fair value raised to SEK3.9–5.1 (3.2–4.4) based on four equally weighted valuation methodologies. In our own valuation assessment of VEF's portfolio by 2022e, we calculate potential NAV growth of 20%+. The stock is tradingin line with reported NAV but 16% below our estimated NAV (versus its five-year average of 18% below and sector peers at 8% above). We like that VEF offers unique venture capital (VC) exposure to the wealth catch-up from financial inclusion in emerging markets through VC, to which institutional capital is increasingly attracted in search of alternative sources of return (funding to Latin America-based fintechs has shown a 64% CAGR since 2016). On our conservative forecasts, we see a potential revenue pool of USD22bn for VEF's holdings, which lends unique growth prospects from fintech adoption and serving the underbanked.

VEFLsdb versus OMXS30 (12m)



Source: Factset

SUMMARY	
Share price (SEK)	3.90
Tickers	VEFLSDB SS
CAPITAL STRUCTURE	
No. of shares (m)	829.3
No. of shares fully dil. (m)	834.1
Market cap. (SEKm)	3,234
NIBD adj end-2021e (USDm)	-54
Enterprise value adj (USDm)	330
Free float (%)	101

Source: Company, DNB Markets (estimates)

NEXT EVENT	
Q1 2021	28/04/2021

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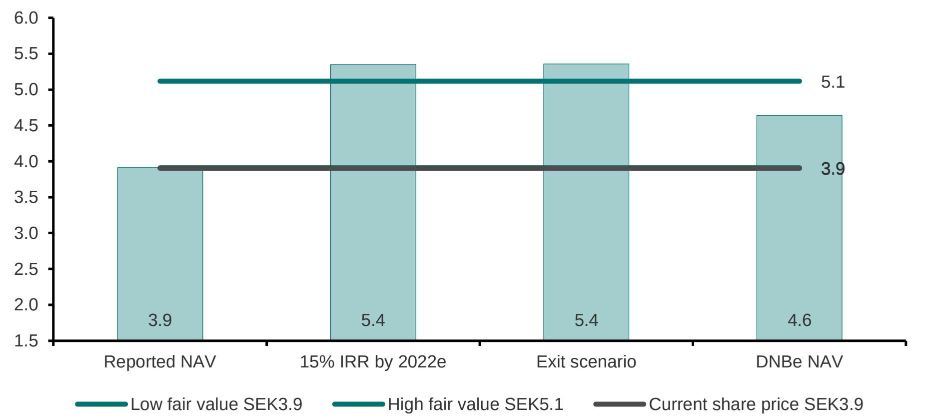
ANALYSTS
Joachim Gunell

Overview

Valuation (SEK)



Source: DNB Markets

Valuation methodology

- Our SEK3.9–5.1/share fair value continues to be based on: 1) reported NAV; 2) a target IRR of 20% by end-2022e for its holdings (versus its 30% IRR target); 3) a multiple on invested capital of 4x and 20% cost of capital using an exit period six years from its initial investment; and 4) our 2022e NAV based on its respective holdings' peer multiples.
- We apply a 0% discount to NAV (previously 10%) target in our valuation scenarios. VEF is currently trading in-line with its NAV (versus its five-year average discount of 18%).

Source: DNB Markets

Downside risks to our fair value

- Low disclosure of early-stage private assets (financial, KPIs, cash-burn etc.) adds valuation uncertainty.
- As VC valuations correlate, albeit with a time lag to public markets, it could trigger a change to the narrative and risk assessed for high-growth loss-making VC investments with little fundamental valuation support if public valuations deteriorate, resulting in private investment impairments, etc.
- Additional capital needs to fulfil its current funding pipeline in combination with new investments.
- Emerging markets carry greater risks in terms of politics, financial stability, and FX (USD versus BRL, MXN, RUB, EUR, and ZAR). Still, VEF's main exposure is to USD/SEK as it invests and reports in USD, but the NAV/share and share price are in SEK, where a weakening of USD (and stronger SEK) should have a negative impact. Accordingly, VEF's benefits from a weak SEK and strong USD.
- Failure to retain key persons in the management team and board of directors to secure the best deal flow.

Source: DNB Markets

DNB Markets estimates

- VEF has a track record of generating substantial shareholder value (NAV IRR of 32% since 2015) and is building traction in the investment community from recent successful portfolio exits (Tinkoff Bank exited at 65% IRR, iyzico at 57% IRR in 2019).
- With a solid net cash position of USD54m (12% of GAV), we believe it has firepower to support its portfolio in future funding rounds.
- Creditas and Konfio hold the largest short-term potential to unlock value and move the needle for VEF's NAV (today composing 56% of its NAV) which on a stand-alone basis could boost VEF's NAV by 20%+ by 2022e, according to our analysis.
- VEF is clearly not a low-risk holding, but lends access to VC in some novel fintech markets. The Latin American-tilted portfolio holds leading versions of proven western business models such as Klarna, Tink, Lendo, Betterment, Fortnox, etc., providing potential exposure to wealth catch-up from financial inclusion in emerging markets.

Source: DNB Markets

Upside risks to our fair value

- Value crystallisation from portfolio exits at attractive terms. We believe VEF strives for 30% IRRs and returns of invested capital of 3–5x.
- New funding rounds (and potentially IPOs in the medium term) in its existing portfolio winners could drive positive NAV revisions from valuation uplifts, which should increase investor appetite, as seen historically.
  - Financing rounds generally take place every 18 months.
  - Short-term potential NAV catalysts: Konfio, TransferGo, Juspay, and Nibo, in our view.
- VEF is improving its communication and documentation of how its fintech investments can generate a positive social impact by increasing accessibility and affordability of financial services in under-served segments, which could increase ESG investor appetite.
- We believe VEF will continue to make share buybacks when it the stock is trading at 20–25%+ below NAV.

Source: DNB Markets

ESG overview

Sustainability assessment

	Positive	Negative
Conclusions	■ The capital VEF injects into fintech investments can generate a positive social impact by increasing accessibility and affordability of financial services, especially for under-served segments (low- and middle-income, and SMEs) that are ignored by traditional banks. ■ Other key ESG considerations from its portfolio holdings relate to responsible lending and debt prevention, increased client transparency and fair advice. Also, there is a layer of energy efficiency from its digital distribution models.	■ Domiciles in Bermuda and Cyprus (considered tax havens) could hurt its governance rating. Granularity in how it presents and discloses ESG considerations have until late been relatively poor. ■ VEF's holdings increase access to credit for under-served segments, which we believe acts as a substitute for traditional lending in segments which would otherwise resort to informal or expensive lending. Still, a change in consumer behaviour with rapidly growing consumer debts in emerging markets could reduce financial stability.
Actions being taken by company	■ With sizeable minority stakes of 10–20% and board representation, VEF has the ability to influence its holdings' directions. Its fintech portfolio is an indirect enabler of almost all the UN's SDGs by 2030, but a direct enabler of SDG 1, 2, 4, 5, 8, and 10, with increased financial inclusion and literacy through less-expensive financial services.	■ As VEF is increasingly communicating and providing documentation regarding how it leverages finance as a force of good in emerging markets, we believe its ESG assessment should improve over time. Also, we do not rule out that it could change to a more modern and ESG-compatible governance structure.
Key ESG drivers		
Short-term	■ Good examples where VEF's holdings' offer to remove barriers for financial inclusion are: ■ JUMO's mobile money marketplace gives the low-income population and SMEs in Africa and Asia access to financial services (who are otherwise excluded from the financial system). ■ Creditas and Konfio help to materially lower borrowing costs in markets that have some of the highest interest rates in the world. ■ Xerpa allows employees to withdraw portions of their salary before payday in Brazil, where tens of millions Brazilians resort to predatory credits to meet their cash needs till the next pay cycle. ■ TransferGo dramatically reduces the remittance transaction costs for blue-collar workers sending money cross-border to families back home.	■ The evolution in borrowing behaviour and large-scale adoption of consumer loans could increase credit losses, lessen consumer protection and comprise financial stability risks in VEF's markets. ■ VEF's parent company domicile is Bermuda (considered a tax haven), while the holding company is registered in Cyprus (corporate tax rate 12.5%), having copied the historical Vostok Nafta structures in its split from VNV in 2015. As corporate tax responsibility and disclosure are increasingly becoming a leading governance consideration, it could hurt its ESG assessment, in our view. ■ Our interpretation is that VEF's management is aware of this from a governance perspective, and we do not rule out that it could change to a more modern and ESG-compatible governance structure in the coming years.
Long-term	■ VEF has the greatest impact on ESG considerations by being an active and responsible owner. Our analysis suggests VEF is increasingly developing its own ESG competence (from investment screening to board decision-making), and we expect it to place high expectations on its portfolio holdings to drive such trends, mainly focusing on the social aspects of financial inclusion of the underbanked population in emerging markets at lower cost.	■ The key to VEF's success is the networks of its skilled management in order to identify successful fintech entrepreneurs and source the best investment ideas. Its future success could depend on its ability to retain and attract new talent. Thus, it is important to have compensation guidelines in line with VC/PE fund benchmarks. VEF's board of directors has a discretionary mandate to pay extraordinary bonuses to key employees upon substantial shareholder value creation (exits, etc.)

Source: DNB Markets

NAV overview

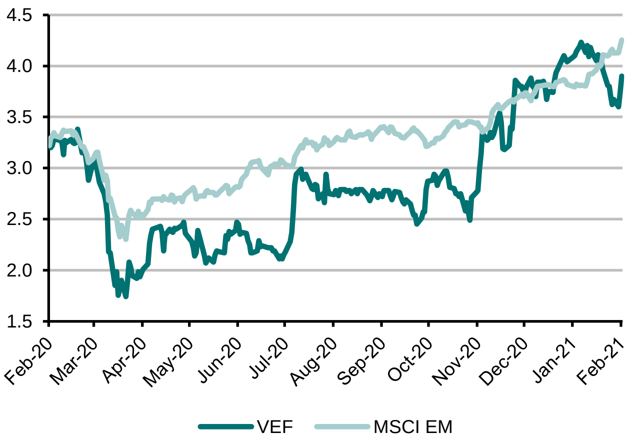
Figure 1: VEF NAV overview

Share price (SEK)	3.9	**NAV/share (DNB)**	3.9	**DNB discount to NAV**	0.3%
DNB fair value (low)	3.9	**NAV/share (rep)**	4.6	**Rep. discount to NAV**	15.9%
DNB fair value (high)	5.4			**DNB discount target**	0.0%

Investment portfolio	**DNB rec.**	**Rep. MV (USDm)**	**DNB value (USDm)**	**Rep. MV (SEKm)**	**DNB value (SEKm)**	**Value (SEK/share)**	**Weight (%) of NAV**	**% of cap/votes**
Creditas	NO COV	169	188	1,421	1,582	1.7	44%	9.8
Konfio	NO COV	49	90	408	755	0.5	12%	11.0
REVO Technology	NO COV	11	11	93	93	0.1	3%	23.0
JUMO	NO COV	10	10	80	80	0.1	2%	6.8
TransferGo	NO COV	29	35	241	297	0.3	7%	15.4
Guiabolso	NO COV	5	12	46	101	0.1	1%	10.9
Xerpa	NO COV	6	6	48	48	0.1	1%	16.0
Nibo	NO COV	14	24	114	203	0.1	4%	20.1
Magnetis	NO COV	8	13	70	113	0.1	2%	17.5
FinanZero	NO COV	10	10	84	84	0.1	3%	18.0
Finja	NO COV	7	7	57	57	0.1	2%	22.8
Juspay	NO COV	17	17	146	146	0.2	4%	9.9
Liquidity management		48	48	405	405	0.5	12%	
Total unlisted		**382**	**471**	**3,213**	**3,964**	**3.9**	**98%**	
Other								
Cash and equivalents		6	6	50	50	0.1	2%	
Other net liabilities		0	0	0	0	0.0	0%	
Other assets/liabilities		0	0	0	0	0.0	0%	
Summary NAV								
Total assets		442	531	3,718	4,468	4.5		
Current net cash		-54	-54	-455	-455	-0.5		
Gearing		-12.2%	-10.2%	-12.2%	-10.2%	0.0		
Net asset value		**388**	**477**	**3,263**	**4,013**	**3.9**		

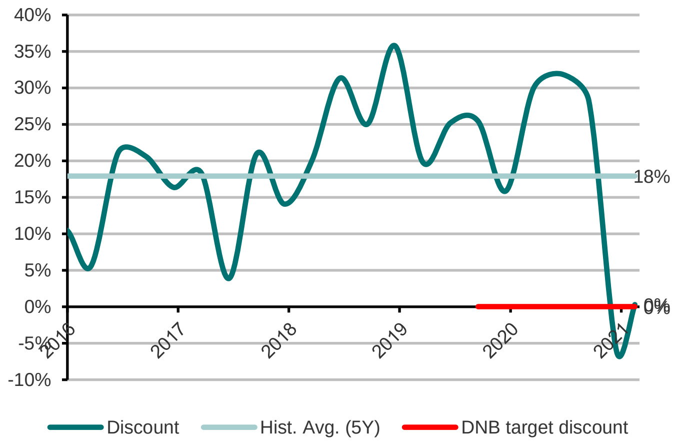
Source: DNB Markets (forecasts), company (historical data)

Figure 2: VEF share price (SEK) versus MSCI EM index



Source: Bloomberg

Figure 3: VEF discount to NAV



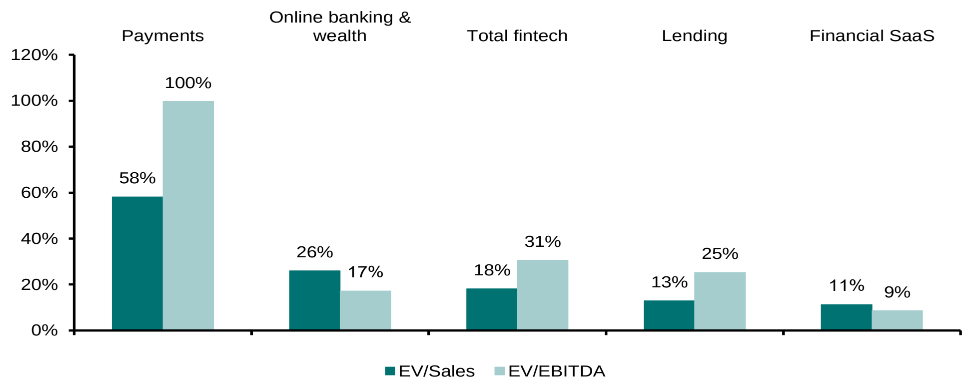
Source: DNB Markets

Figure 4: Additional information

Other data	2017	2018	2019	Current	Owners	% of cap	% of votes	5Y track record	
Market cap	1,409	1,138	1,927	3,234	Ruane, Cunniff & Goldfarb	21.3	21.3	Ann. TSR	21.6%
NAV	1,635	1,806	2,325	3,263	Libra Fund	21.0	21.0	NAV CAGR	32.5%
NAV growth		11%	29%	40%	Wellington	12.9	12.9		
Net cash	75	40	44	54	Swedbank Robur	8.7	8.7		
Gearing	-4.8%	-2.3%	-1.9%	-16.2%	Fidelity (FMR)	6.5	6.5		
DPS	0.00	0.00	0.00	0.00	Fidelity (FIL)	3.2	3.2		
Dividend yield	0.0%	0.0%	0.0%	0.0%					
Management costs	35	49	54	50	Number of shares (m)				
to NAV	2.16%	2.72%	2.34%	1.55%	VEF		834.1		
Analyst: Joachim Gunell (+468 597 91 201, joachim.gunell@dnb.se)					**Total**		**834.1**		

Source: DNB Markets (portfolio views), company (historical data), Holdings (owner data)

Figure 5: Fintech multiples expansion since 31 December 2019



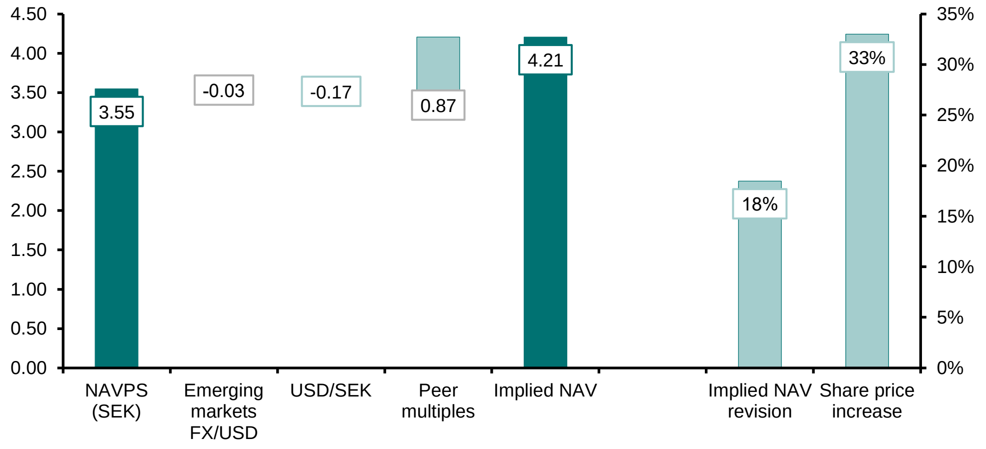
Source: Bloomberg (underlying data), DNB Markets (further calculations)

Figure 6: DNB NAV based on peer group multiples

	Current NAV (USDm)	NAV growth (USDm)	DNBe 2022e (USDm)
Creditas	169	19	188
Konfio	49	41	90
REVO	11	0	11
JUMO	10	0	10
TransferGo	29	7	35
Guiabolso	5	7	12
Xerpa	6	0	6
Nibo	14	11	24
Magnetis	8	5	13
FinanZero	10	0	10
Finja	7	0	7
Juspay	17	0	17
Total	**334**	**89**	**423**
Other assets/liabilities			0
Current net cash			54
Operating expenses until 2021e			-17
Target NAV			**460**
Target discount to NAV			0%
Implied fair equity value			460
Number of shares (m)			834
Implied fair value (USD/share)			0.6
Implied fair value (SEK/share)			**4.6**
Current share price (SEK/share)			**3.9**
Implied fair value potential			*19%*

Source: DNB Markets

Figure 7: VEF sensitivity analysis (FX and peer multiples) versus Q4 2019



Source: DNB Markets

Figure 8: NAV change QOQ versus Q3 (USD)

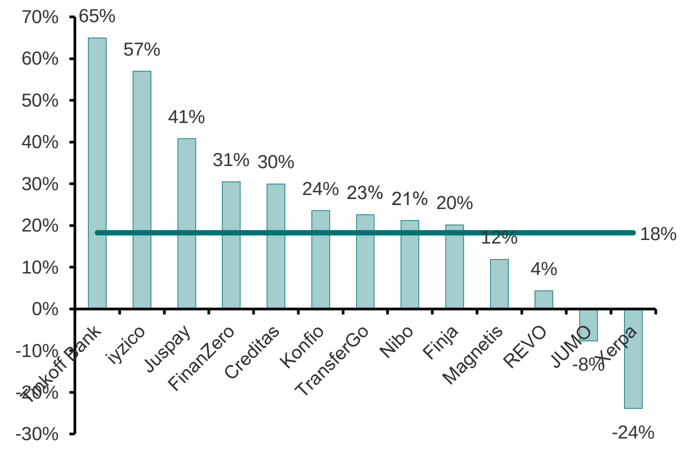
Source: Vostok Emerging Finance

Figure 9: VEF NAV overview

NAV overview (USDm)	Q1'18	Q2'18	Q3'18	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20	Q3'20	Q4'20
Creditas	25.0	25.0	25.0	25.0	25.0	73.2	73.2	73.2	50.4	80.7	102.1	169.0
Konfio		15.0	15.0	15.0	15.0	25.0	41.6	41.6	32.4	28.1	40.3	48.5
Juspay									13.0	13.0	13.0	17.4
JUMO	12.7	13.4	16.4	16.4	16.4	16.4	16.4	16.9	9.0	7.5	8.6	9.5
REVO Group	14.2	14.0	17.2	14.6	18.0	18.4	19.2	16.2	9.7	10.2	11.6	11.1
TransferGo	7.1	13.0	13.0	12.8	12.6	12.8	12.3	12.6	13.5	21.4	25.2	28.6
Guiabolso	30.0	30.0	19.6	15.3	11.0	10.9	10.4	11.5	9.8	9.6	8.7	5.4
Nibo	3.3	3.3	3.8	5.0	8.6	10.0	8.5	10.6	7.0	11.3	13.1	13.6
Xerpa							8.5	8.5	4.5	4.5	4.9	5.8
Magnetis	3.0	3.0	3.7	5.8	6.3	6.5	8.1	8.1	5.7	6.6	7.7	8.3
Finanzero	5.4	5.0	5.1	5.0	4.9	7.8	7.3	7.7	5.4	7.6	9.0	9.9
Finja	1.2	1.2	3.3	3.3	3.3	3.3	3.4	3.4	2.3	2.5	4.2	6.7
Tinkoff Bank	71.4	62.2	48.8	7.9								
iyzico	9.0	17.6	19.0	25.9	26.1	33.9	33.9					
Invested	**182.2**	**202.7**	**189.9**	**152.0**	**147.1**	**218.2**	**242.8**	**210.4**	**162.7**	**203.0**	**248.2**	**334.0**
Invested % of GAV	*86%*	*92%*	*92%*	*75%*	*72%*	*90%*	*95%*	*84%*	*87%*	*91%*	*92%*	*86%*
Liquidity management	23.5	9.5	9.4	44.9	45.4	13.1	6.5	34.5	20.8	18.0	18.0	48.2
Cash	6.6	8.5	6.6	5.5	11.2	12.1	5.2	5.6	3.2	2.5	2.1	4.2
Cash and liquid investments	**30.1**	**18.1**	**16.0**	**50.4**	**56.6**	**25.2**	**11.7**	**40.1**	**24.0**	**20.6**	**20.2**	**52.4**
Cash % of GAV	*14%*	*8%*	*8%*	*25%*	*28%*	*10%*	*5%*	*16%*	*13%*	*9%*	*8%*	*14%*
Other net liabilities	-0.5	-0.6	-0.9	-1.0	-0.7	-4.7	-5.5	-1.0	-0.3	-0.4	-0.2	1.7
Net asset value	**212**	**220**	**205**	**201**	**203**	**239**	**249**	**249**	**186**	**223**	**268**	**388**
NOSH (fully diluted)	671.7	674.0	663.7	663.0	662.8	661.8	659.4	665.4	663.4	663.7	663.4	834.1
NAV/share (USD)	0.32	0.33	0.31	0.30	0.31	0.36	0.38	0.37	0.28	0.34	0.40	0.47
NAV/share (SEK)	2.56	2.83	2.76	2.75	2.81	3.41	3.62	3.60	2.83	3.13	3.63	3.81
VEF share price (SEK)	2.14	2.01	2.05	1.75	2.28	2.50	2.76	2.94	1.99	2.14	2.57	4.04
Market cap (SEKm)	1,437	1,355	1,361	1,160	1,511	1,655	1,820	1,956	1,317	1,420	1,705	3,370
Discount to NAV	16%	29%	26%	36%	19%	27%	24%	18%	30%	32%	29%	-6%
NAV growth (YOY)	40%	38%	10%	1%	-4%	8%	21%	24%	-8%	-6%	8%	56%
NAV growth (QOQ)	7%	4%	-7%	-2%	1%	18%	4%	0%	-25%	20%	20%	45%
Net investments	-2	-18	-7	-1	6	-34	-13	46	0	0	0	-9
Gearing (net debt/GAV)	-14%	-8%	-8%	-25%	-28%	-12%	-7%	-16%	-13%	-9%	-8%	-13%
Management costs	-1.3	-1.5	-1.4	-1.3	-0.8	-2.3	-1.3	-1.2	-0.5	-1.4	-0.9	-3.3
Management costs/NAV (LTM)	2.32%	2.45%	2.89%	2.74%	2.45%	2.41%	2.30%	2.26%	2.87%	1.99%	1.48%	1.55%
USD/SEK	8.1	8.7	8.9	9.0	9.2	9.4	9.6	9.6	10.1	9.3	9.0	8.2

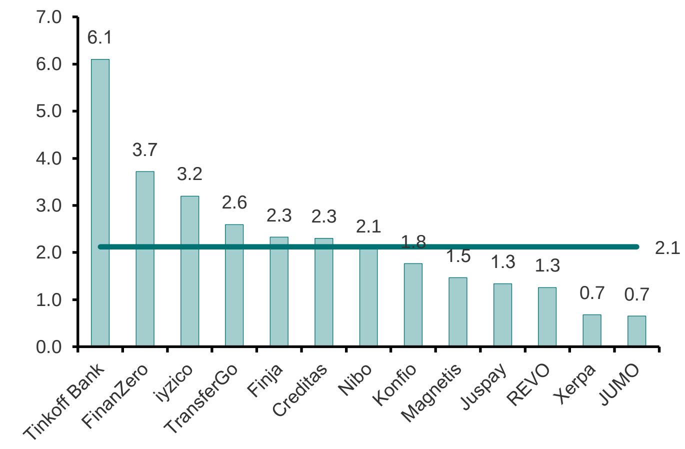
Source: DNB Markets (forecasts), company (historical data)

Figure 10: Portfolio IRRs



Source: DNB Markets

Figure 11: Portfolio CoC multiples



Source: DNB Markets

Summary of positives

Secular growth opportunity from emerging market fintech evolution

We believe the receptiveness and market opportunity for fintech is particularly appealing in VEF's emerging markets (with Latin America composing ~80%), due to a large underbanked population (allowing for scalability), and tech-savvy young population (more likely to adopt fintech solutions). In our view, emerging markets may benefit disproportionally from fintech innovation by leapfrogging traditional banking services. With growing smartphone and Internet access (acting as key delivery mechanisms), the door for financial inclusion opens up, while incumbent banks have long neglected the growing lower-, middle-income and SMEs, spurning innovation for high-margin retail banking products. This makes the oligopolistic banking markets' profit pools (wide interest-rate margins, high lending rates, transaction costs, etc.) rather vulnerable for fintech entrants that can lower spreads/fees, improve transparency, foster financial inclusion and operate with a leaner cost structure, in our view.

Brazil is one of the most interesting structural fintech opportunities, in our view…

With the portfolio maturing, we note potential value catalysts

Our analysis suggests that VEF's portfolio holds the emerging market versions of proven western fintech models such as Klarna, Tink, Lendo, Betterment, and Fortnox, etc., which taps into a potential addressable market opportunity of USD22bn (~SEK190bn), in our high-level breakdown of its sub-sector segments in: 1) lending; 2) payments; and 3) other fintech (accounting SaaS, wealth management, digital banks, mobile wallets, comparison websites, personal finance management, etc.). Our analysis suggests consumer lending companies Creditas and Konfio hold the largest short-term potential to unlock value and move the needle for VEF's NAV (today composing 56% of its NAV) by 20%+ by 2022e. In addition, its early stage holdings (Juspay, TransferGo, Nibo, Magnetis, FinanZero, and Finja) could drive material NAV growth long-term (3–5 years+), if they maintain their current 3–5x top-line CAGRs.

…and VEF owns the emerging market versions of Klarna, Tink, Lendo, Betterment, and Fortnox, tapping into an addressable market of over USD22bn…

VEF's venture capital portfolio offers scarcity value…

According to Blackrock's 2020 institutional rebalancing survey, institutional capital has been pouring into private illiquid investments in search of alternative sources of return. With few publicly listed fintechs in emerging markets, it remains challenging for investors to gain access to this theme. With a portfolio of 12 emerging market fintech holdings, diversified by geography, business model, and stage of development, we note that VEF offers exposure to the wealth catch-up from financial inclusion in EMs. With USD54m in net cash (12% of GAV), it appears well-capitalised to support its holdings in future funding rounds, and adding new investments, in our view.

…lending investors' scarce access to VC fintech in emerging markets

…and a solid exit track record, which is key to the narrative

Exits at attractive returns is key to the investment story in VEF, and it is building traction, having started to realise substantial values in 2019 it had built since inception in 2015 through successful exits (Tinkoff Bank at 65% IRR, iyzico at 57% IRR). While it could prove hard to match the first generation of successful exits, management remains focused on building the next wave of value creation. In our view, VEF is well-positioned to crystallise further shareholder value, and its NAV IRR of 32% since 2015 validates its track record.

Management has a track record of creating substantial value through exits and high returns on invested capital (average of 4.7x from two exits)

EM and fintech experience across management and board of directors

VEF was relatively early in 2015 to chase the fintech opportunity in emerging markets, before it became a target market for global investors with larger international funds. In addition, its heritage from Vostok New Ventures (and previously Vostok Nafta) means it enjoys a strong reputation and brand among emerging market entrepreneurs. While the organisational set-up is quite small and reflects a rather concentrated portfolio, VEF can leverage the combined breadth of its management's and board's network, and extensive emerging market and financial services experience, to identify and source the best investment ideas in its regions.

Management and board with extensive emerging market and financial services backgrounds

Summary of negatives

Rare VC exposure, but the risk profile is high

There are inherent risks fintech VC investing in emerging markets, in our view. Given the early-stage nature of VEF's portfolio, it can provide almost no financial disclosure and operational KPIs of its holdings, as well as for competitive reasons. To us, this limits financial forecast visibility, cash burn, etc., which increases valuation uncertainty as investors seldom have the time for the deep-dive required to fully appreciate VEF. Risks related to audit and regulation are higher in the fintech space, we believe. Moreover, VC investing means high illiquidity risk (once you are in, you could be in for good), and while we do not expect a lack of potential interest for high-quality assets (such as Creditas and Konfio), VEF may not be able to exit its investments according to plan. As VEF invests primarily in equity, there is also risk that there will be no recoveries in the event of bankruptcy of individual portfolio holdings.

VEF is clearly not a low-risk investment, due to the very nature of the early-stage VC businesses in which it invests

Lofty VC valuations after more than a decade-long fintech market boom

The private-market orchestra has been playing for a decade, as the VC market is strongly correlated to the stock market, albeit with a slight lag leading to sustained imbalances after a correction. Following a protracted stock market boom for over a decade until 2020, risk appetite has increased, with record capital allocated to private VC markets (potential over-crowding from institutions allocations and investors such as Softbank), resulting in high investment activity and lowered investment standards (difficult to maintain a disciplined investment approach), leaving fintech valuations stretched. Unlike the 2000 IT bubble, many of the fintech unicorns have revenues, but in most cases earnings are still far in the distance. If stock market conditions deteriorate, valuations contract, and private investments get impaired, it should in our view trigger a change to the narrative regarding the risk of VC investments, especially for emerging markets, which could hamper VEF's exit opportunities.

VC fintech valuations are sky-high, which could reverse if stock market conditions deteriorate, hampering VEF's exit opportunities

High funding need of its portfolio holdings

As VEF's network of new deal opportunities expands and its current portfolio matures, it has grown its rate of investments, in number and average deal size (USD10m–20m). VEF has funded new investment through rights issues (SEK522m in 2020, and USD69m in 2015), but as it has been able to make two cash realisations from portfolio exits (USD152m to date), balancing net investments, its FCF burn averaged USD0m in 2018–2019. It is currently well-capitalised, with a net cash position of USD54m, suggesting room to support its holdings in the current pipeline of financing rounds. Should it choose to have a more opportune pipeline or in the absence of major realisations, it would imply a need for further financing (either through equity as seen historically or bonds, as seen with its older sibling VNV).

Further funding could be needed if it chooses to be more opportune, but for now it has a strong balance sheet

There are inherent risks from investing in emerging markets

The appeal of emerging markets is clear in terms of their greater potential growth rate, and for VEF a structural wealth catch-up, but they also face greater risks to political and financial stability, while lacking the corporate governance structure of developed markets. 2018–2019 were banner years for Brazilian fintech equities, with the IPOs of Stone, PagSeguro, and XP. Still, Brazil's deep recession in 2015–2016 and the current political turmoil across many Latin American countries are examples of the macroeconomic volatility presented by emerging markets. We also believe that adverse FX effects (stronger USD versus BRL, MXN, RUB, EUR, and ZAR) could have an impact on VEF's results, as we do not believe VEF engages in any hedging. Also, as it invests and reports in USD, while its share price is in SEK, a weaker USD (and stronger SEK) should have a negative impact, in our view.

Emerging markets carry greater political, default, and FX risks

Key-person risk

VEF's holdings are start-ups growing at 3–5x per year in many cases, where the entrepreneurs behind the business models are often a dominant force. Such fast growth and dependence on entrepreneurs adds execution and key-person risks, in our view. Moreover, the key to VEF's success is the professional networks of its skilled management and board of directors in order to identify successful fintech entrepreneurs and source the best investment ideas. Its future success could depend on its ability to retain these persons, making it important to have compensation guidelines in line with VC/PE fund benchmarks for key persons, in our view.

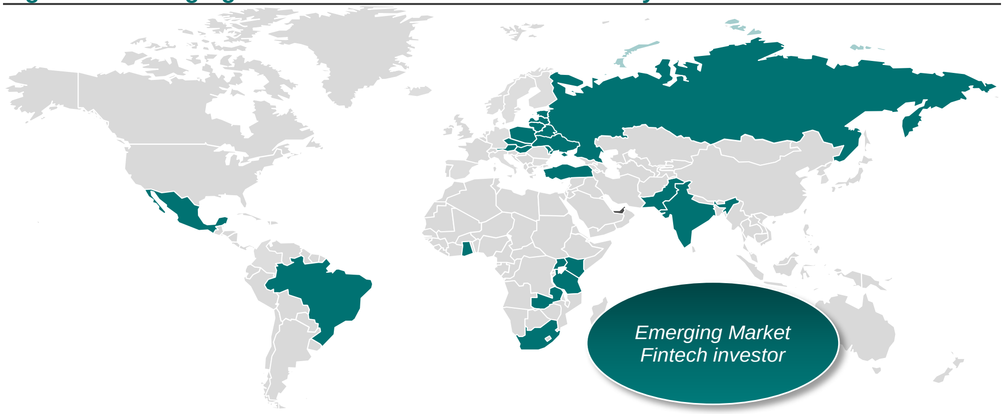
Vital to retain key persons in the management team and board of directors in order to secure the best deal flow

Company overview

Having been spun-out of Vostok New Ventures in 2015, Vostok Emerging Finance (VEF) is a Swedish investment company entirely dedicated to invest in growth stage (VC) private fintech companies operating in scale emerging markets. Its target markets (mainly in Latin America) are in pole position to benefit from fintech adoption, as their large populations are largely 'unbanked' today, whereas penetration of technology (smartphone and internet access being key delivery mechanisms) is reaching a critical mass, while the current oligopolistic financial market structures mean that disruptive consumer-oriented technology can lower the cost of financial services, which are among the highest in the world, and drive financial inclusion.

VEF is an investment company lending investors unique access to VC fintech in emerging markets

Figure 12: Emerging market fintech investor with a heavy Latin America focus



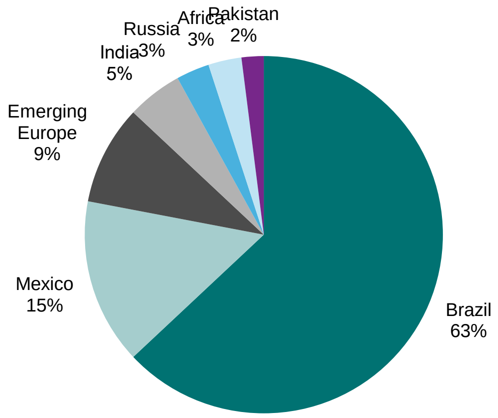
Source: DNB Markets

VEF often takes 10–20% ownership stakes and focuses on backing the entrepreneurs behind the business models, targeting the wealth catch across all lines of fintech sub-sectors including payments, credit, mobile money and financial marketplaces, etc. Today it has a portfolio of 12 holdings diversified by geography, business model, and stage of development, and enjoys a strong brand among emerging market fintech entrepreneurs, which we attribute to:

An active owner with board representation in each of its holdings, striving to find and support the best entrepreneurs behind the business model in each market

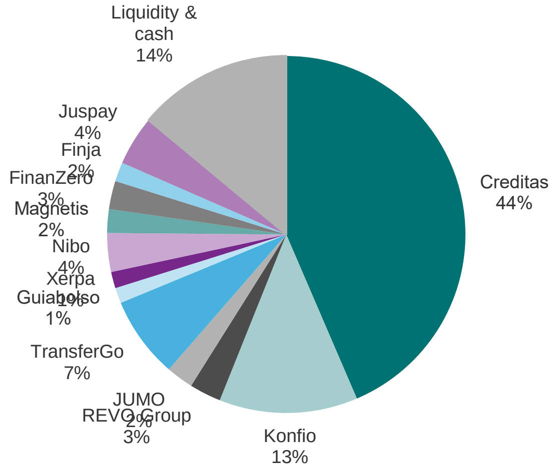
- Being a listed investment company, VEF has access to permanent capital, which means entrepreneurs will not have to worry that it will force an exit before time. (VEF partnered with Tinkoff Bank for almost 14 years).
- With its deep sector expertise and network in emerging markets throughout the world (versus local VCs), it can compare business models, traction, economics, valuation, etc.
- VEF is comfortable with taking a long-term view in the often-volatile world of emerging markets, and can aid its holdings through deep experience of capital-raising processes.

Figure 13: Geographical split ex cash (2020)



Source: Vostok Emerging Finance

Figure 14: Portfolio split (2020)



Source: 2345234

Figure 15: Vostok Emerging Finance portfolio overview

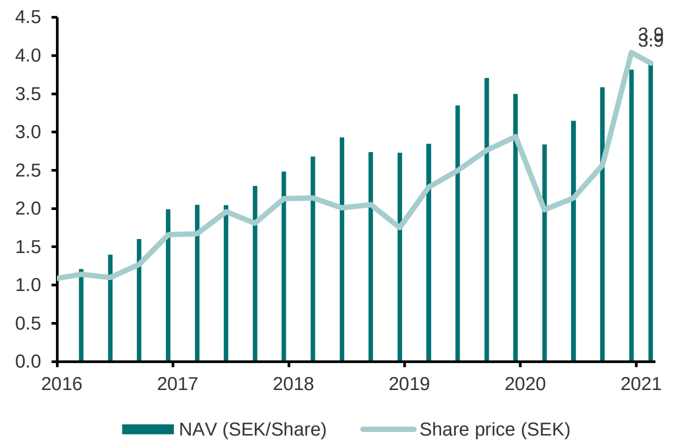
Company	Geography	Business type	% of VEF's portfolio	Ownership	VEF's investment (USDm)	Fair value (USDm)	IRR	CoC return	Investment date
creditas		Secured lending platform	44%	9.8%	73.4	169.0	30%	2.3	Dec-17
konfio		SME lending	13%	11.0%	27.5	48.5	24%	1.8	Jun-18
JUSPAY		Payments	5%	9.9%	13.0	17.4	41%	1.3	Mar-20
JUMO	Pan-Africa, Asia	Mobile money marketplace	3%	6.8%	14.6	9.5	-8%	0.7	Oct-15
peBC+		Payments & consumer credit	3%	23.0%	6.7	11.1	4%	1.3	Sep-15
transferGo		Cross-border remittances	7%	15.4%	11.0	28.6	23%	2.6	Jun-16
Guiabolso		Personal finance management	1%	10.9%	30.0	5.4	-40%	0.2	Oct-17
nibo		Accounting Saas	4%	20.1%	6.5	13.6	21%	2.1	Apr-17
XERPA		HR & payroll platform	2%	16.0%	8.5	5.8	-24%	0.7	Sep-19
magnetis		Digital investment advisor	2%	17.5%	5.7	8.3	12%	1.5	Sep-17
FinanZero		Consumer credit marketplace	3%	18.0%	2.7	9.0	31%	3.7	Mar-16
FINJA		Mobile wallet	2%	22.8%	3.2	6.7	20%	2.3	Jul-16

Source: DNB Markets

VEF aims to be stage-agnostic in its investments, but we note that it tends to enter its holdings in series B–C financing rounds (new investments typically in the range of USD10m–20m), where there is a funding gap between local VCs and global investors. Over the past four years, there is a track record of successful exits (Tinkoff Bank exited at 65% IRR, iyzico at 57% IRR) that have generated a 29% share price IRR since Q4 2015 (NAV IRR of 32%), suggesting that VEF can rightly claim that it is building substantial shareholder value.

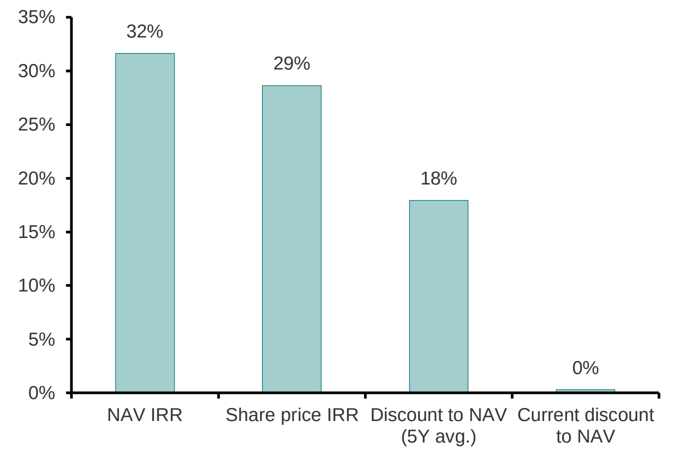
Recent portfolio exits highlight the value creation potential from its early-stage portfolio, having achieved a NAV IRR of 30%+ from Q4 2015

Figure 16: VEF – NAV and share price (SEK)



Source: VEF (underlying data), DNB Markets (further calculations)

Figure 17: VEF performance and IRR (2015–YTD 2020)



Source: VEF (underlying data), DNB Markets (further calculations)

Figure 18: DNB Markets' breakdown of selected Vostok Emerging Finance's key fintech segments

		Scope of the opportunity	*Estimated revenue pool*	*VEF holding*	*Western comparables*
Credit	***Consumer loans*** *(Brazil)*	The large Brazilian incumbent banks hold 80%+ of the outstanding loans in the system and Brazilian consumers pay among the highest interest rates in the world (high-priced unsecured loans with an average APR of 230%). Fintech has the potential to gain market share from reducing the information asymmetry, bridge the gap between savers and borrowers, and reduce the Brazilian consumer debt burden.	SEK60bn (~USD6bn) Based on a market share of 5% of the USD125bn addressable market for high APR products such as credit cards, overdrafts, and personal loans.	creditas *Secured lending* FinanZero *Consumer loan marketplace* ***54% of NAV***	LendingClub SoFi lendingtree Lendo
Credit	***SME lending*** *(Mexico)*	The small business community in Mexico is vast yet underserved by larger banks (7 million SMEs that comprises 35%+ of all outstanding loans to a value of USD50bn). In addition, we note that Mexican SME output to GDP is above 50%, suggesting there is a large financing gap, in our view. For fintechs, there is an opportunity to strenghten SME access to financing by providing convenience and affordability to customers who are creditworthy.	SEK50bn (~USD5bn) We identify an USD50bn total market opportunity within Mexican SME credits and assume a penetration rate of 10%.	konfio *Digital SME lending* ***15% of NAV***	ondeck prospa CAPITAL FLOAT
Payments	***Mobile payments platform*** *(India)*	India has one of the most advanced and complex electronic payment infrastructures globally, resulting in friction and challenges for merchants and banks in the country. There is a growing need for mobile payment platforms for online merchants to solve the challenges to improve customer conversion rates.	SEK15bn (~USD2bn) We assume digital payments processed through online gateways to be a USD80bn market growing at a 100% CAGR until 2025e and apply a 7.5bp fee	JUSPAY *Payment gateway* ***5% of NAV***	stripe adyen PayPal amazon pay
Payments	***Merchant payments*** *(Russia)*	While Point-of-sale financing options that can allow for consumers to spread their cost or consumption habits over time are widely available in developed economies, they are only now becoming the norm in emerging markets like Russia. Moreover, technological developments (particularly smartphones and online commerce) have created an entry point for fintechs.	SEK15bn (~USD1.5bn) Assuming a 5% market share of the Russian e-commerce payments market valued at ~USD30bn	peBc+ *Merchant payments & consumer credit* ***3% of NAV***	Klarna. affirm AIMIA INSPIRING LOYALTY
Payments	***Remittances*** *(EU)*	Blue-collar workers are the most consistent and regular remittances customers in the world. Still, traditional bank networks are local, expensive, slow, and often inconvenient. Fintech innovation has the potential to lower costs associated with transferring money across borders (a key source of income for many low emerging markets) and reduce transfer times.	SEK6bn (~USD0.6bn) We apply a 1% fee on the annual European remittance flows to low- and middle-income regions of USD60bn	transferGo *Cross Border Remittances* ***9% of NAV***	TransferWise azimo worldremit
Other Fintech	***Digital investment advisory*** *(Brazil)*	Saving has traditionally been constrained to the wealthy population but digital wealth management could be a way to reach financial inclusion, especially for the younger and more tech savvy population. Robo-advisors can provide savers with tailored user-friendly and dynamically allocated investment options at lower fees than static funds sold by incumbent banks.	SEK2bn (~USD0.2bn) We estimate that Brazilian robo-advisors can penetrate ~5% of the mutual funds AUM and apply a management fee of 0.5%	magnetis *Digital investment advisor* ***2% of NAV***	wealthfront Betterment ELLEVEST
Other Fintech	***Personal finance management*** *(Brazil)*	As it is difficult to access financial information in combination with complicated financial profiles, Brazilian bank clients have limited tools to monitor and manage a complete view of their income and spending habits. Fintech solutions can help simplify clients' financial profiles by aggregation technology and help them gain a better oversight of their indebtedness and reduce interest costs.	SEK8bn (~USD0.8n) Based on a 10% market share of the ~USD8bn current account fees generated by Brazilian banks	Guiabolso *Personal finance management* ***2% of NAV***	credit karma intuit mint tink muse
Other Fintech	***Accounting SaaS*** *(Brazil)*	The Brazilian accounting and tax environment is complex and there are over 400,000 individual accountant professionals servicing 10+ million SMEs that are legally required to have an accountant. There is a opportunity to leverage innovative technology solutions and provide a full suite of cost-effective administrative solutions and financial products to underserved SMEs.	SEK30bn (~USD3bn) We multiply BRL109 for Nibo's monthly pricing plan to an addressable market of 10+ million Brazilian SMEs	nibo *Accounting SaaS* ***4% of NAV***	xero intuit FORTNOX

Source: DNB Markets

Important Information

Company:	VEF
Coverage by Analyst:	Joachim Gunell
Date:	03-2-2021

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