EDISON

VEF

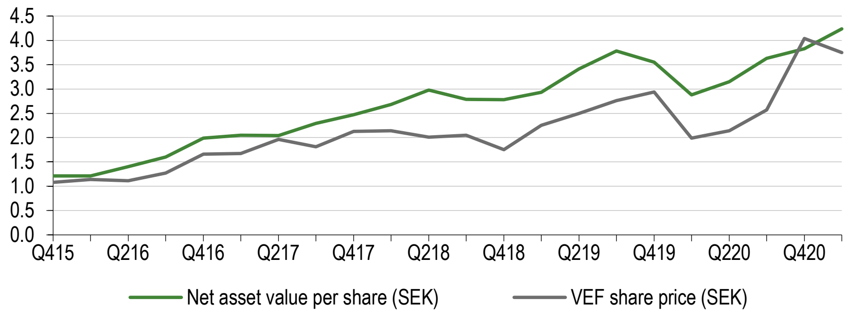
Q121 update

NAV momentum

Investment companies

VEF's Q121 NAV per share was up 17% since our initiation in November 2020. The NAV uplift is a result of positive operating trends and successful capital raising of its invested companies, the highlight being Creditas, a Brazilian online secured lending platform, which accounts for 42% of Q121 NAV. In its Q121 results, VEF also highlighted Konfio, a Mexican unsecured SME lender that is its second largest investment, growing at a good pace and with lower costs than anticipated. VEF had a US$61m rights issue in December, providing money for further growth. VEF trades at a 14% discount to NAV and could offer an attractive entry point for growth-oriented investors that cannot easily get direct exposure to the emerging market fintech asset class.

Quarterly performance showing strong momentum



Source: VEF, Refinitiv

Why invest in emerging fintech now?

The emerging fintech sector continues to be a hot investment space as financial services are becoming increasingly digitalised and emerging markets in general offer a better growth profile than more developed countries, although with higher risks such as greater currency volatility. Continued strong investor appetite from new entrants and incumbents should help exit prices on VEF's investments.

The analyst's view

VEF offers diversified access to well-managed private companies with disruptive business models at an early to mid-growth stage. Although its two most recent investments in 2021 have been small stakes, VEF is typically an active investor with board seats on all its portfolio companies. Its track record is good, although short, with two profitable exits of 66% ROI in 2019. Management of VEF's largest holding Creditas (42% NAV) is working towards an IPO, which if successful would significantly improve VEF's NAV transparency and could crystallise additional value.

Valuation: Trading at a 14% discount to NAV

VEF is trading at a 14% discount to Q121 NAV. Underlying assets are valued under a mark to model approach (normally on a revenue multiple) or on a recent transaction basis. According to the company, the portfolio is on an FY20 revenue multiple of 24x, but revenue tripled in the two years to FY20 and we believe strong momentum should continue thanks to economic recovery and digitalisation trends.

10 June 2021

Price	**SEK3.64**
Market cap	**SEK3,018m**
AUM	**US$403m**
	SEK8.5/US$
NAV per share	SEK4.24
Discount to NAV	14%
Shares in issue	829.3m
Free float	100%
Code	VEFL
Primary exchange	Nasdaq First North (Stockholm)
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(8.3)	(3.5)	54.2
Rel (local)	(10.0)	(12.7)	10.7
52-week high/low	SEK4.23	SEK2.11	

Business description

VEF (formerly Vostok Emerging Finance) is an investment company taking equity positions in early stage fintech companies in a broad range of financial services in emerging and frontier markets where financial services are underpenetrated and populations are jumping straight to digitalisation.

Next events

Q221 results	July 2021

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Edison profile page

VEF is a research client of Edison Investment Research Limited

Q121: Momentum, funding and investments

Since our initiation in November 2020, VEF's net asset value (NAV) per share has risen by 16.8%, split into 5.5% in Q420 and 10.7% in Q121. Total NAV rose from US$268m to US$403m; this includes a successful US$61m rights issue concluded in December 2020.

Brazilian online secured lending platform Creditas (VEF stake: 9.8%) accounted for about half of this NAV increase. Creditas raised US$255m in a funding round in December 2020 in which VEF took up its rights. This increased VEF's stake value by 66% to US$169m. Creditas accounts for 42% of VEF's NAV and 47% of the investment portfolio ex-cash. Creditas management is steering the company towards an IPO, which, if successful, would increase the transparency of the value of the company in VEF's portfolio. Creditas has been growing strongly in its three core lending lines (auto, home and payroll) and is expanding into Mexico. Revenues were up 50% y-o-y in Q120.

Konfio, a Mexican unsecured SME business lender, is VEF's second largest investment (15% of VEF's NAV) and has been the other big driver in VEF's NAV uplift in the last two quarters. The value of the Konfio stake increased by about 50% from US$40.3m in Q320 to US$60.1m in Q121. Konfio has resumed its strong growth in Q420 with better than expected asset quality according to VEF. It is also broadening its product range to include credit as a service and has acquired an enterprise resource planning (ERP) company.

The other NAV highlights in Q120 were the c 30% increase in NAV of FinanZero (a Brazilian digital loan brokering platform) and Jumo (an African lending platform). Both companies have been doing well, and FinanZero had another successful round of financing (VEF invested US$1.5m in the rights issue, for an 18% stake), which set the higher valuation mark. FinanZero and Jumo combined make up 8% of VEF's investment portfolio.

On the negative side, Guiabolso continues to be revalued downwards. It is now focusing on third-party products, which is less ambitious than the initial hopes and plans of a higher profit margin business model offering its own products. It now represents 3% of NAV and its performance is unlikely to be needle-moving for VEF in either direction.

VEF has disclosed that Revo in Russia is currently profitable and that Jumo is close to achieving profitability. All the remaining companies, including Creditas, are still losing money as they are scaling up. VEF has not disclosed any portfolio EBITDA or revenue numbers.

As we detail later in the portfolio section on page 6, nine of the 14 invested companies are valued on a mark to model basis, and the rest are valued on a recent transaction basis, either from purchases or recent funding rounds.

In terms of revenue, figures for Q121 are not available, but we understand that the portfolio revenue grew 62% in US dollar terms in FY20 and tripled over two years to c US$151m.

Two new investments

VEF made two investments in Q121 in new companies: Rupeek in India and Minu in Mexico. In a departure from its usual approach, these were small stakes (1.4% and 1.2%) and did not involve any representation on the board.

Rupeek is a fast-growing asset-backed lending platform focused on gold-secured loans. VEF expects it to broaden its asset-backed offering and potentially to become a second Creditas.

Minu is a an 'employee financial wellness' company and the leading pay on demand lender in Mexico. For a set fee, it allows employees instant access to their earned wages. The payroll deductions are automated and so require little administrative cost to the companies. Minu currently has almost 100 clients including Telefonica, Scotiabank and Rappi. VEF had already invested in this earned wage advance model through Xerpa in Brazil. It sees this as a hook product that can lead to cross selling other financial products.

Emerging fintech opportunity

Technology is increasingly having an impact on financial services at many levels, ranging from electronic payments, online commerce platforms, digital customer service to niche areas such as wealth management. Customers are increasing their digital adoption of financial services, incumbents are increasingly getting involved, while many governments and regulators are taking note and supporting this trend.

The technology advantage can arise from various angles including better collection and usage of customer data, superior service delivery and higher automatization. It can result in lower costs to customers and also greater customer reach, an important topic in emerging markets. The recent lockdown seems to have only increased the move to greater digitalisation. Accenture estimates that in Europe, 33% of all new financial services revenue since 2005 has been captured by fintech companies.

KPMG estimates that investment activity (venture capital, private equity and M&A) in global fintech rose from $18.8bn in 2013 to $168bn in 2019, and despite the pandemic there was still $105.3bn invested in 2020 with 2,861 deals, with a strong rebound in the second half of the year.

According to the FinTech Almanac, fintech activity in South America (VEF's current largest geographic weighting) increased from $434m in 2015 to $1.8bn in 2019.

Emerging markets provide another lever for future growth. This stems not just from the economic and demographic growth outlook being better, but also a more significant amount of both retail and business clients that are underserved or poorly served. Clients are moving directly to digital platforms and bypassing bricks and mortar banking. This is particularly true in the relatively poorer emerging markets such as India, Pakistan and Africa, where the level of financial integration is still comparatively low. According to the World Bank, in 2017 the percentage of the population with a bank account was 21% in Pakistan and 31% in Africa compared to 96% in the EU.

Fintech investment activity has been growing strongly in emerging markets as a result, especially in Latin America. The value of fintech deals and financing in Latin America increased from just $44m in 2013 to about $2bn by 2019. According to Statistica, of this $2bn, 70% was in Brazil and 21% in Mexico.

Fund profile: An active, emerging fintech

VEF (formerly Vostok Emerging Finance) was launched in November 2015 and its headquarters are now in Sweden. Its Swedish depository receipts (SDRs) are listed on the Nasdaq First North exchange in Stockholm. Each SDR is equivalent to one ordinary share and has the same voting rights with no restrictions. As part of its focus on environmental, social, and corporate governance (ESG), VEF decided to change its domicile from offshore in Bermuda to Sweden in Q121. VEF sees many of its portfolio companies as driving financial inclusion and fairness and being 'at the front line of sustainable finance'.

VEF's investment targets are early to mid-stage modern financial services companies in emerging and frontier markets. The company looks for innovative early stage companies capable of challenging incumbent companies with new thinking and modern technology solutions. It also looks for entrepreneurs and teams with good track records, viable concepts and strategies and clear, scalable business models that can deliver high rates of growth.

VEF invests in the whole spectrum of financial services. The portfolio includes firms in consumer credit, payment solutions, money transfer, personal finance, asset management and various types of financial marketplace.

There is a strong preference for larger emerging markets where single-country scalability can provide greater returns. The investments have therefore been in large markets such as Brazil, Mexico, India, Russia, Turkey, Pakistan and Africa, which provide the opportunity to scale up. Brazil is a particular focus for VEF due to a strong online connected customer base, expensive incumbent financial services and the ability for VEF to make value creating deals.

Although VEF's mandate gives it more flexibility, it typically aims for a 10–25% minority equity stake. Where appropriate, the team seeks board appointments where it can add value by knowledge, corporate governance investment profile and networks for capital raising and partnerships. However, as mentioned, VEF's last two investments, Rupeek and Minu, have been smaller stakes of 1.4% and 1.2%, respectively. The average investment duration is expected to be five to seven years, but ultimately this is determined by exit opportunities including unsolicited bids. The permanent capital structure of a closed-end fund gives VEF flexibility in managing its holdings (eg not forcing it to sell due to investor redemptions) and therefore boosting its internal rate of return (IRR). There is no regular dividend target, with the focus being on capital appreciation.

Capital structure and fees

Although VEF can use leverage, it currently operates without any debt and with no management fees. The operating expenses in 2020 were 0.9% of the investment portfolio's NAV (including cash) if we exclude incentive programme expenses. This is down from 1.6% in 2019. If we include the incentive programme, the total operating expenses rise to 1.5% of the portfolio NAV in FY20 (2.25% in FY19).

VEF's long-term incentive plans (LTIPs) initially had a three-year vesting period, but VEF decided to change the LTIP starting in 2020 (the LTIP 2020) to a five-year plan. The final reward depends on the portfolio's NAV growth. Achieving NAV three-year CAGR targets of 10%, 15% and 20%+ results in participants correspondingly receiving 2x, 5x or 10x the number of purchased shares for the base payment. With the five-year plan, the programme is proportionally higher in the first year (2020) and then decreases on a linear basis until maturity. So the pay-out on the LTIP 2020 is 10x, 15x and 35x the number of purchased shares. For under 10% NAV CAGR there is no pay-out.

Exhibit 1 shows the dilution impact of the various levels of incentive scheme pay out in the two LTIPs. If VEF were to hit the 20%+ NAV CAGR, there would be an estimated dilution of 7%.

Exhibit 1: VEF Incentive plan possible dilution

	10% NAV CAGR	15% NAV CAGR	20%+ NAV CAGR
LTIP 2019 – 3-year plan	0.37%	0.94%	1.87%
LTIP 2020 – 5-year plan	1.40%	2.90%	5.00%
Total dilution	**1.77%**	**3.84%**	**6.87%**

Source: VEF

The fund manager: VEF

The manager's view

Management believes VEF's companies are set up to function in the high political and economic volatility of emerging and frontier markets, which could also make them more resilient to the impact of COVID-19. The resilience comes from management teams being more accustomed to macro volatility and the secular growth opportunity that helps VEF ride out the negative shocks. VEF's management also sees the pandemic as having accelerated the trends to greater digitalisation of banking services.

VEF believes that Konfio was perhaps its 'most impressive holding in 2020, especially given the space/country it operates in and the natural macro/credit headwinds that came with COVID-19.' It saw Konfio pass the asset quality stress test in good shape during 2020 and Konfio was able to be 'first out of the blocks in terms of credit growth in 4Q20, which is delivering better quality clients' at lower cost of risk and with a 'broader range of financial services' than before. VEF believes that Konfio may be its next Creditas in terms of breakout value creation and plans 'to back Konfio harder on its path to being the number one digital financial services provider for SMEs in Mexico'.

In addition to Konfio, management also highlights its two Indian investments, Juspay and Rupeek, as having 'a lot of value creation potential' in 2021.

Management is seeing IPO and M&A activity in emerging fintech at elevated levels again following the peak of the pandemic concerns. Investors are excited by the upside from the growth prospects and the disruptive potential of emerging fintech companies. This is good news for business activity and for outsider interest in VEF's investments. However, this also means discipline must be exercised in doing new deals. While it sees 'deal flow as healthy as ever', it is not in a position of great need to invest and can wait for the right deals. In Q121, VEF's number of leads and qualified leads regarding possible deals more than double than in the similar period in Q120.

The portfolio

At the end of Q121, VEF's portfolio consisted of 14 equity investments with a fair value of US$359m and US$45m in cash and liquidity investments ($41m). There is no debt and less than US$1m in liabilities for a company NAV of US$403m. The total amount invested on the current assets is US$212m, excluding the liquidity management cash.

Nine of the companies are valued according to model, ratified by KMPG, and five are currently valued on recent cash raising transactions or purchase price. The latter are Creditas, FinanZero, Finja, Rupeek and mino.

Companies can be split geographically or by sub sector. Of the 14 companies, 13 can be grouped into three areas of primary activity (Nibo is the outlier, being an accounting software services company):

- **Payments and remittances companies**: Juspay, Jumo, Revo, TransferGO and Finja operate in this segment, which naturally lends itself to the global digitalisation trend.
- **Digital lending**: Creditas (which is an asset light company), Konfio and Rupeek produce and sell their own lending products in this segment. Xerpa and Minu are earned wage loan advancement companies and can also be grouped in this category.
- **Finance management and marketplace:** in this segment, the money is made by selling commissions rather than underwriting risk. FinanZero is a loan marketplace that tries to find the best deal for customers from its many partners. Guiabolso offers personal finance management tools and wider products for sale. Magnetis brings wealth management services to more people at lower cost by using robo-advisers.

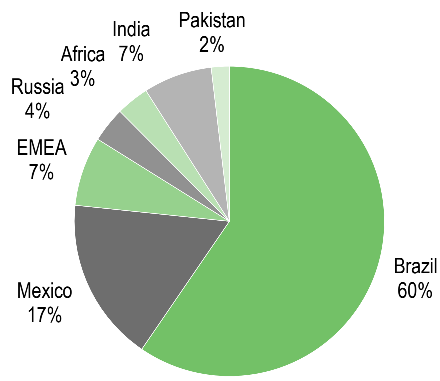
Although the core of each company is its technology, they have different value drivers and competitive challenges. So, even though there is some country concentration in Brazil, the catalysts for performance are not always the same. Some companies may be more exposed to the credit cycles, others to the financial markets, and others such as Nibo are more resistant to the economic cycle.

Exhibit 2: VEF Investment portfolio with NAV quarterly progression

Fair value (US$000s) Company	Location	Invest. Date	FY19	Q120	Q220	Q320	Q420	Q121	Y-o-y (%) Q121	Y-o-y (%) ex-invest* Q121	Q-o-q (%) Q121	Q-o-q (%) ex-invest* Q121
Creditas	Brazil	Dec-17	73,246	50,352	80,713	102,078	169,023	169,023	236%	186%	0%	0%
Konfío	Mexico	Jun-18	41,579	32,359	28,081	40,279	48,504	60,982	88%	88%	26%	26%
TransferGo	EMEA	Jun-16	12,555	13,548	21,428	25,167	28,634	25,942	91%	76%	-9%	-9%
Juspay	India	Mar-20	0	13,000	13,000	13,066	17,372	18,714	44%	44%	8%	8%
Nibo	Brazil	Apr-17	10,619	7,035	11,290	13,000	13,610	13,152	87%	70%	-3%	-3%
REVO Group	Russia	Sep-15	16,244	9,710	10,222	11,585	11,083	13,145	35%	66%	19%	19%
FinanZero	Africa	Mar-16	7,728	5,430	7,576	8,747	9,933	13,055	140%	113%	31%	16%
JUMO	Brazil	Oct-15	16,875	8,994	7,497	8,551	9,540	12,307	37%	37%	29%	29%
Magnetis	Brazil	Sep-17	8,108	5,669	6,616	7,695	8,330	8,922	57%	57%	7%	7%
Rupeek	India	Mar-21						7,000	N/A	N/A	N/A	N/A
Finja	Pakistan	Jul-16	3,389	2,339	2,457	4,181	6,748	6,748	188%	167%	0%	0%
Xerpa	Brazil	Sep-19	8,500	4,511	4,544	4,931	5,758	4,947	10%	10%	-14%	-14%
Guiabolso	Brazil	Oct-17	11,545	9,761	9,601	8,956	5,417	4,848	-50%	-50%	-11%	-11%
Minu	Mexico	Feb-21						450	N/A	N/A	N/A	N/A
Liquidity investments			34,521	20,849	18,047	18,033	48,205	40,678	95%	1%	-16%	0%
Investment portfolio			**244,908**	**183,558**	**221,073**	**266,269**	**382,157**	**399,912**	**118%**	**88%**	**5%**	**4%**
Cash and cash equivalents			5,562	3,150	2,545	2,141	4,224	4,055				
Total investment portfolio			**250,470**	**186,708**	**223,618**	**268,410**	**386,381**	**403,967**	**116%**	**87%**	**5%**	**5%**
Other net assets/ liabilities			(1,031)	(280)	(382)	(236)	1,685	(569)				
Total Net Asset Value			**249,439**	**186,428**	**223,236**	**268,174**	**388,066**	**403,398**	**116%**	**87%**	**4%**	**4%**

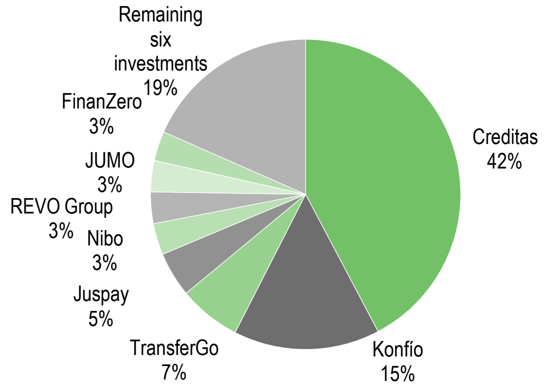
Source: VEF. Note: *Net new investments removed from year-on-year performance for better like-for-like valuation comparison.

Exhibit 3: Q121 portfolio geographic breakdown



Source: VEF

Exhibit 4: Q121 investment portfolio ex-cash position



Source: VEF

Focus on Creditas (9.8% stake)

Creditas is a Brazilian online platform offering secured loans, with about 35% backed by homes (home equity loans) and about 50% by vehicles and 15% in payroll deducted loans (payments are deducted from wages at source), a common loan product in Brazil. In May 2021, Creditas invested BRL95m (US$18m) in local electric motorcycle start-up Voltz. Creditas's CEO expects that in five to 10 years only 20% of motorcycles will use traditional combustion engines and they want to be part of this growing trend towards greener energy sources. Creditas has become a relevant minority investor in Voltz, but the size of the stake has not been yet disclosed.

The home loans business opportunity arises from the fact that unsecured consumer loans are quite expensive in Brazil (average personal unsecured credit was 87% in March 2021, up from a trough of 70% in September 2020 according to central bank figures).

There is considerable unlocked equity value in Brazilian housing. In 2019, the Brazilian central bank was estimating that the market for home equity loans could be as much as BRL500bn. At the end of 2020, the amount of loans in this segment was still under BRL15bn, which suggests that there is more room to grow. Traditionally, property in Brazil could only have one loan attached to it, but this has now changed, allowing for this segment to grow.

Creditas has been capitalising on (1) the fact that the larger banks, although present in this niche, have not been overly focused on it, partly because it cannibalises the much higher-margin unsecured personal credit and (2) technology that can be used to deliver the loans quickly and conveniently.

Caixa Econômica Federal (a specialised government-owned mortgage lender) is the largest lender in the home equity niche, and this is followed by Santander and Itaú, two large private banks. We estimate that Creditas has been able to build up a c 3% market share and it hopes to increase it further. Bari Bank and Banco Inter are among the smaller players that also focus on this area.

Rate competition in home equity

While we see this asset class growing strongly in the future, it is of course very likely that there will be some margin erosion from increased competition.

Currently Creditas's starting lending rates advertised on the website are 10.7% (quoted as 0.085% per month; in Brazil rates are usually quoted on a monthly basis, a hangover from the old high inflation years) plus IPCA consumer inflation index (currently 6.8%) for a total rate of 17.5%. With upfront fees, the rate goes above 20%. Mortgages and home equity loans are not the same product but as a reality check we note that the average mortgage rate in Brazil is 7.9% as of March 2021 (central bank data) in the regular non-special regime market.

Creditas runs an asset-light model and it securitises its portfolio and sells it to institutional investors. The funding rate is 6.75% on top of the IPCA. We would estimate that Creditas makes about a 5–6% interest rate spread on home equity loans, which is attractive enough in our view.

However, we note that the more established banks have a funding advantage due to their retail deposits as well as superior economies of scale. Not only can these banks under-price Creditas, but they have the greater flexibility in the structuring interest rate on loans (ie not necessarily tied to the IPCA index, which some clients might not like).

In the auto loan asset backed segment, Creditas's lending rates start at 14.7% plus fees, although it is currently doing a promotion where they start at 9.9%. However, we believe the average all-in lending rates are closer to 30%. As a reference, the average auto loan rate in Brazil was 20.6% according to the central bank in March 2021. However, as with the case of home equity loans, a loan for car purchase is not the same as a quick, convenient loan backed by your vehicle.

Exhibit 5: Creditas selected performance metrics

	2018	2019	2020	FY20 y-o-y %	Q121	Q121 y-o-y %
Total Origination (BRLm)	235	531	900	69%	421	57%
Gross Revenues (BRLm)	68.9	176	336	91%	124	55%
Gross Revenues (US$m)	18.9	45.6	62.7*	37%	23.2*	
Net Income (BRLm)	(28.5)	(109)	(192)		(65)	
Net Income (US$m)	(7.8)	(28.1)	(35.8)*		(12.1)*	
Loan book (BRLm)	256	679	1,255	84%	1,545	73%
Net margin	(41%)	(62%)	(57%)		(52%)	

Source: Creditas, Edison Investment Research. Note: *At a BRL5.36/US$ rate.

Exhibit 5 shows some of the available numbers from Creditas. Despite the significant headwind of the COVID-19 pandemic in 2020, revenue nearly doubled, origination rose by 69% and the loan book grew 84%. The revenue growth number in US dollars was lower (at 37% based on our calculations) because of the depreciation of Brazilian real against the US dollar during the pandemic. It is possible that some of this weakness may be regained as the pandemic ends.

In the first quarter of 2021, revenue continued to grow at a strong pace despite the pandemic still raging on in Brazil. Revenue was up 55% y-o-y and 20% q-o-q, and origination was up 57% y-o-y and 34 y-o-y.

Creditas is still gaining scale, and currently its client acquisition costs and investments lead it to still be losing money (net margin was -52% in Q121). Asset backed loans, especially when they involve a home, are not necessarily cheap to produce in Brazil, particularly with regulation and bureaucracy. We would estimate that Creditas's client acquisitions costs are probably running as high as 15% of loans and so Creditas might need to at least triple its loan book before it becomes profitable, or cut back its investments. However, this situation is not unusual for a fintech that is ambitiously scaling up and clearly Creditas management is thinking big.

Economy rebound expected with inflation to decline

Brazilian GDP contracted by 4.1% in 2020. The latest central bank collected consensus data show 3.2% and 2.3% forecast increases for 2021 and 2022. The incredible Brazilian real devaluation was a key driver in inflation spiking. The IPCA went from 1.8% in May 2020 to 6.8% in April 2021. The central bank policy rate has increased from a record low of 1.9% in 2020 to the current 3.4%, while the 10-year bond rate has moved from 6.8% to 9.5%. The good news is that collected consensus estimates show that inflation is expected to be only 5.1% at the end of 2021 and 3.6% at the end of 2022.

While the economic outlook in Brazil is not quite as rosy as before the pandemic, structurally the business opportunity for Creditas to grow remains in place.

New investment: Rupeek (1.4% stake)

Rupeek is an online doorstep lender providing loans backed by gold. Although 80% of Indians have bank accounts, more than 90% of Indians do not have access to formal credit. According to the Reserve Bank of India, 95% of household savings are in some form of asset and not as bank deposits. Gold is very popular and the World Gold Council estimated that in 2019 Indian households have stocked up 25,000 tonnes of gold worth US$15tn. It estimates that the gold loan book in India is currently US$150bn.

Rupeek's loan rates tend to be lower than pawnbrokers and the lending is more convenient. The company is growing 15% month-on-month and lends c US$800m annually according to Rupeek's CEO. VEF's stake purchase price valued the company at US$500m. Rupeek's aim is to expand into other types of asset backed lending, much as Creditas has done in Brazil.

New investment: Minu (1.2% stake)

VEF has known Minu management for some time and view this relatively small investment (only US$450k) as a step in the door that might lead to more significant investments in the future. Minu is a Mexican earned wage advancement lender, much like Xerpa as we have mentioned earlier in this note. Minu is the market leader in Mexico in this segment. It charges a US$2 flat fee per transaction. It has more than 100 large companies as clients including Telefonica, Scotiabank, Rappi, Manpower and Cap Gemini. In 2020, the number of transactions increased by 18x according to VEF.

Performance

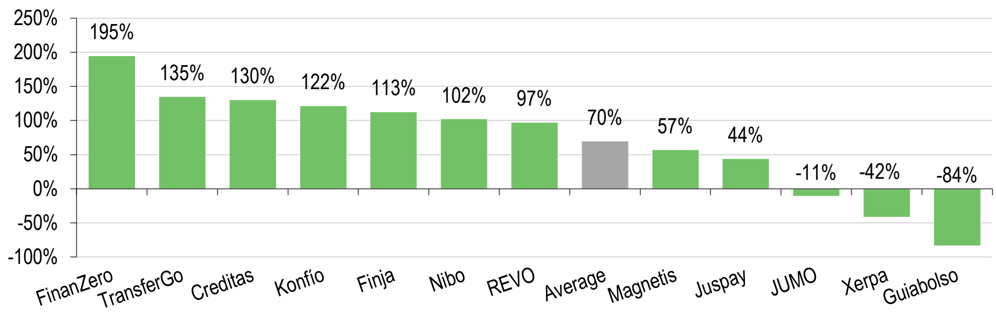
NAV has quadrupled since inception in 2015

When we initiated on VEF, its NAV had tripled since its inception in July 2015 on a Swedish krona basis. Now about seven months later, Q121 NAV has quadrupled since inception. The return has been 58% over the last three years, with a 47% increase in the last 12 months. As shown in Exhibit 9, VEF share price has generally outperformed the world, emerging markets and emerging market financials indices from MSCI. Only the MSCI emerging market tech index has kept pace and outperformed VEF over the years; however, the difference is small: a 6% outperformance over the last three years and 3% over five years.

Although VEF's share price return has generally outperformed the it has underperformed on a 6 months basis. This is because share price overshot the NAV in Q420 and then there was a share price correction and once more the share started to trade at a discount to NAV. The NAV momentum itself as aforementioned has been strong.

VEF's significant increase in NAV was driven by the success of its first two exits, Tinkoff and Iyzico, and by its two largest current investments, Creditas and Konfio. Exhibit 6 shows VEF's current valuations versus invested money in the various portfolio companies. VEF valuations are above the invested value in nine of its 13 investments with an average 70% book gain over investment.

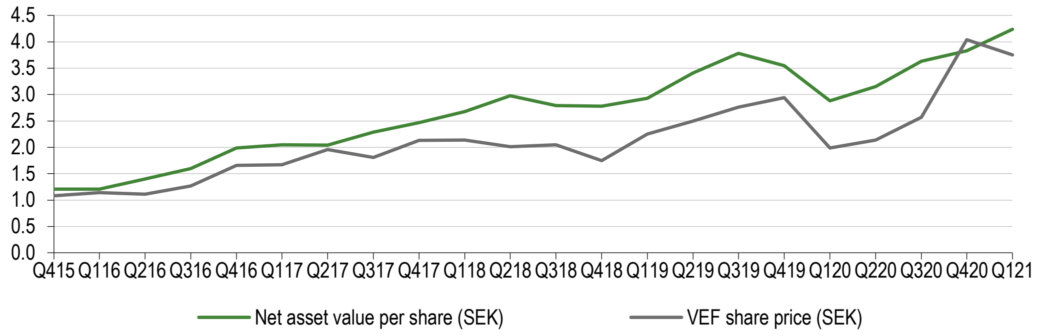
Exhibit 6: Portfolio book value vs net investment (%), Q121



Source: VEF

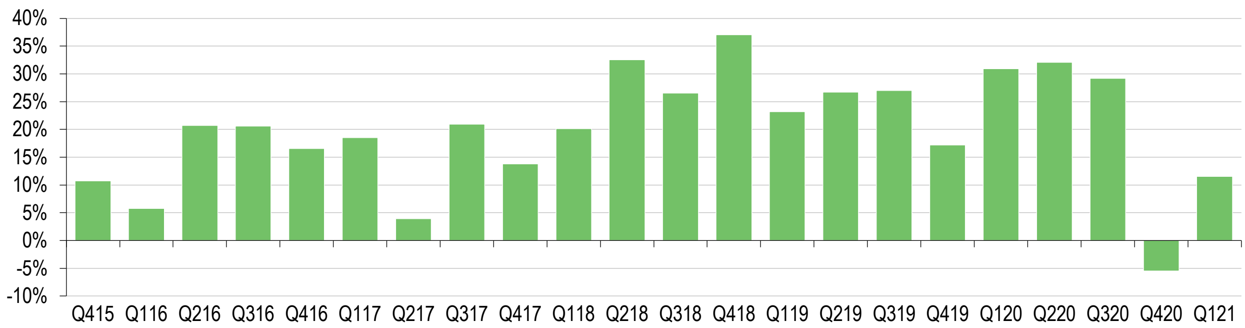
Since the NAV is only released quarterly and with a lag, the discount to NAV tends to be somewhat volatile, reflecting expectations of NAV progression. In Q420, the share price at the end of the year was actually above the disclosed year-end NAV. As of 8 June it is trading at a 14% discount to Q121 NAV.

Exhibit 7: VEF price and NAV (quarterly)



Source: Refinitiv, VEF

Exhibit 8: VEF quarterly discount to NAV



Source: Refinitiv, VEF

Exhibit 9: VEF total return performance relative to indices

(%)	1 month	3 months	6 months	1 year	3 years	5 years	SI
Price relative to MSCI Emerging Markets	(0.2)	1.4	(8.7)	19.2	64.3	160.7	167.5
Price relative to MSCI World	(0.5)	(6.1)	(11.1)	27.4	44.7	154.0	149.7
Price relative to MSCI EM Banks	(3.5)	(5.7)	(11.6)	27.8	86.6	189.3	200.3
Price relative to MSCI EM Consumer finance	0.1	0.7	(7.1)	(36.7)	75.5	178.5	143.0
Price relative to MSCI EM Tech	4.3	5.3	(16.4)	(18.2)	(5.5)	(2.8)	(10.7)

Source: Refinitiv. Note: SI is since inception (July 2015).

Peer group comparison

Exhibit 10 compares VEF with Augmentum, a fintech closed-end fund peer. We also show some open-ended peers even though the capital structure is different. Even when compared to Augmentum, VEF is still relatively unique. Augmentum focuses on UK and European fintech, as opposed to VEF's emerging markets focus.

On an NAV basis, VEF has outperformed peers in our sample over five and three years and was second only to BGF FinTech E2 over the last 12 months. We note VEF's ongoing costs are below its one closed-end peer at 0.84% and 1.55% of NAV in 2020 excluding and including incentive bonus scheme costs, respectively. In our view, the type of fintech investments that VEF pursues, which are almost akin to private equity, are more profitably (and safely) carried out using a permanent capital structure.

VEF's current gearing is zero, unlike Augmentum, which has gearing of 91%. We note that Augmentum did recently pay a dividend and is trading at a significant premium to NAV, which might be understated (the one-year performance has been very modest).

Exhibit 10: Selected peer group at 8 June 2021*

% unless stated	Fund size ($m)	One year NAV TR (cumulat.)	Three year NAV TR (cumulat.)	Five year NAV TR (cumulat.)	Latest discount (cum fair)	Ongoing expense (ex-perform)	Perform. fee	Latest net gearing	12-month yield
VEF	**404.0**	**47.1**	**58.2**	**250.1**	**(11.6)**	**0.84****	**Yes**	**0.0**	**0.0**
Closed end peer:									
Augmentum Fintech Ord	218.7	2.8	20.5		30.6	1.9	Yes	91	0.0
Open-ended peers:									
AXA Framlington FinTech Z GBP Acc	87.9	20.1	51.0	125.1		0.87	No		0.1
BGF FinTech E2 EUR	485.3	43.0				2.30	No		
Jupiter Financial Innovt D GBP Acc	73.8	22.9	35.1	109.3		0.95	No		
Robeco FinTech I EUR	1,278.2	22.3	52.1			0.93	No		
Robeco New World Financial Equities I €	1,790.7	28.4	35.5			0.93	No		
Wellington FinTech N GBP Unhedged	623.4	15.7				1.10	No		

Source: Morningstar, Edison Investment Research. Notes: TR = total return. *Performance to 30 May 2021; **FY20 operating expenses without including the incentive programme. The figure is 1.55% with the incentive bonus scheme.

Valuation scenarios show upside

VEF is currently trading on an FY20 NAV/revenue multiple of about 24x. This figure is pushed upwards by Creditas, which is on 27x. This may look like a high revenue multiple but the company, as mentioned, has been growing strongly to justify this type of multiple. Furthermore, we also note that the pandemic led to a steep devaluation of the Brazilian real, which lost a third of its value against the US dollar in 2020. The Russian ruble and the Mexican peso also lost significant ground. As pandemic fears subside, it is conceivable that some of this devaluation will reverse.

S&P Capital IQ and Morgan Partners estimate that the average trailing revenue multiple on developed market fintech mergers and acquisition deals in recent years was 7–9x for the data and analytics, banking technology and payments segments. VEF is trading at a premium to these ratios, but its ratios are coming down quickly as it continues to deliver on revenue growth. We estimate that the underlying revenue growth was 84% in 2019 and 62% in 2020, with the second year affected by the COVID-19 pandemic. Exhibit 11 shows VEF's estimated portfolio NAV to sales revenue figures assuming growth of 50%, 100% and 150% pa. By 2023, under these assumptions the ratios would be 1.6x to 7.3x.

Exhibit 11: NAV valuation to revenue multiples with different revenue growth assumptions

	FY18	FY19	FY20	FY21e	FY22e	FY23e
Portfolio aggregate:						
150% revenue CAGR 2019–22e	73.0	39.6	24.5	9.8	3.9	1.6
100% revenue CAGR 2019–22e	56.8	29.8	24.5	12.3	6.1	3.1
50% revenue CAGR 2019–22e	73.0	39.6	24.5	16.3	10.9	7.3
Creditas (42% of portfolio NAV):						
150% revenue CAGR 2019–22e	136.3	53.4	27.2	10.9	4.3	1.7
100% revenue CAGR 2019–22e	136.3	53.4	27.2	13.6	6.8	3.4
50% revenue CAGR 2019–22e	136.3	53.4	27.2	18.1	12.1	8.1

Source: VEF, Edison Investment Research. Note: We calculate the NAV of the companies based on the fair value calculations implied by VEF's stakes in the companies.

As we mentioned in our initiation, the key drivers for the valuation are delivering on growth, successful funding, value-creating new deals and profitable exit sales. The Creditas funding round in December was a recent significant success and a case in point. An IPO for Creditas would be very helpful for VEF's valuation, since a big portion of its NAV would be listed.

Sensitivities

Valuation transparency and risks: VEF follows private equity valuation guidelines and benchmarks against peers. However, there is still higher valuation risk than for listed, liquid assets, for which more operational information and metrics are published and accessible. The ongoing COVID-19 pandemic exacerbates these risks, although we note VEF did adjust the valuation of many of its investments. Furthermore, fintech has been attracting significant investor attention for some years and this has affected valuations.

Emerging and frontier risks: there is greater variability in both macro and political risk in emerging and frontier markets.

Competitive risks: many early and mid-stage tech companies end up disappointing investors and falling short of expectations. While growth opportunities do exist and are exciting, at the same it is a competitive market and market shares, profit margins and winning business models are in flux and subject to variation.

Corporate governance risk is higher in smaller, earlier-stage companies and particularly in emerging markets. We note that VEF mitigates this risk by often taking seats on the board of the companies it invests in.

Underlying companies may need cash: with the exception of Revo and Jumo, VEF has indicated that its companies are currently all loss-making and this tends to be common for fintech companies at this stage of growth. However, some companies may need more funding to grow. Further rounds of finance often lead to higher valuations so can be a good thing (as was the case of Creditas recently). But they can be detrimental if the prospects for a company have dimmed and investors or new cash are hard to find.

We also note that VEF's shares trade on Nasdaq First North in Stockholm, which is a trading platform but not a fully regulated market.

Exhibit 12: Financial summary

US$000s; year end 31 December	2018	2019	2020	Q121
INCOME STATEMENT				
Financial assets revaluations	6,213	53,452	84,672	16,304
Dividend and coupon income	3,022	501	391	97
Other income	0	0	72	0
Total operating profit	9,235	53,953	85,135	16,401
Operating expenses	(3,763)	(3,869	(3,255)	(922)
Employee incentive programme	(1,763)	(1,737)	(2,743)	(123
Total operating expenses	(5,526)	(5,606)	(5,999)	(1,045)
Operating result	3,703	48,347	79,136	15,356
Net interest income	16	73	2	63
FX income	(193)	160	389	(143)
Net financial items	(177)	233	391	(80)
Profit before tax	3,532	48,580	79,528	15,276
Taxation	(79)	(51)	(74)	(5)
Net income	3,453	48,529	79,454	15,271
EPS (US$)	0.01	0.07	0.11	0.02
Diluted EPS (US$)	0.01	0.07	0.11	0.02
BALANCE SHEET	**2018**	**2019**	**2020**	**Q121**
Tangible non(current assets	146	275	211	197
Equity financial assets	152,002	210,387	333,952	359,234
Liquid financial assets	44,896	34,521	48,205	40,678
Other financial assets	18	11	0	0
Total financial non-current assets	196,916	244,919	382,157	399,912
Cash and cash equivalents	5,479	5,562	4,224	4,055
Other current assets	0	0	0	196
Total Assets	202,665	250,944	388,940	404,000
Interest(bearing liabilities	0	0	0	0
Long(term liabilities	0	118	70	0
Other current liabilities	163	211	192	170
Tax expenses	0	53	85	46
Accrued expenses	1,080	1,123	527	716
Total liabilities	1,243	1,505	874	932
Shareholders' Equity	201,422	249,439	388,066	403,398
CASH FLOW STATEMENT	**2018**	**2019**	**2020**	**Q121**
Result before tax	3,532	48,581	79,528	15,276
Result from financial assets at FV through P&L	(6,213)	(53,202)	(84,672)	(16,304)
Other non(cash adjustments	(711)	509	350	134
Operating cash flow	(3,392)	(4,112)	(4,794)	(894)
Investments in financial assets	(80,616)	(48,819)	(97,093)	(8,951)
Sales of financial assets	79,337	54,013	41,500	7,500
Repayment of convertible	0	0	851	2,176
Dividend and coupon income	3,022	501	391	97
Net interest income	16	73	2	63
Tax paid	(59)	(30)	(74)	0
Net Investment portfolio cash flow	1,700	5,738	(54,423)	885
Investments in office equipment	(154)	46	0	0
New share issue	0	0	58,601	0
Repayment of lease liabilities	0	0	(72)	0
Buy(back of own shares	(2,327)	(1,586)	(641)	0
Proceeds from new share issue through employee options	0	0	298	0
Other investment & financing activities	(2,481	(1,540)	58,186	0
Change in cash and cash equivalents	(4,173)	86	(1,031)	(9)
Cash and cash equivalents at beginning of the period	9,804	5,479	5,562	4,224
Exchange gains/losses on cash and cash equivalents	(152)	(3)	(307)	(159)
Cash and cash equivalents at end of the period	5,479	5,562	4,224	4,055

Source: VEF accounts

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