

FinLab

Seizing opportunities, ready for challenges

FinLab's recent focus was on existing portfolio holdings and selective investments in blockchain projects through the EOS VC Fund. Although some of its fintech companies have seen improved performance in the COVID-19 crisis, the outlook remains uncertain. That said, FinLab is ready to support its holdings with liquidity, which should be backed by its healthy cash position and recurring fee income streams. Despite the broad market sell-off, Heliad's (one of FinLab's holdings) share price has increased 8% since end-December 2019, potentially driven by positive stock catalysts at its largest investment, flatex, an online broker.

Strong write-ups and stable income from investments

In FY19, FinLab's diluted EPS reached €7.33, up from €3.14 the previous year. This was backed by higher write-ups of its unlisted holdings (€37.8m vs €12.5m in FY18), largely driven by the revaluation of its stake in Deposit Solutions. Total income from investments remained broadly stable at €4.6m as the lack of dividends and performance fees from Heliad Equity Partners was compensated for by other income streams, including the management fee from the EOS VC Funds launched in March 2018. The overall result improved to €36.6m from a loss of €3.7m in FY18, affected by a 16% share price decline of Heliad Equity Partners in the period.

Active management in COVID-19 pandemic

FinLab highlighted that it is well positioned in the current COVID-19 crisis and some of its fintech companies have even benefitted from the current market trends (eg nextmarkets and Vaultoro). Management acknowledges the outlook is uncertain and that some of its fintech companies may need to realign their business models or refinance. However, it remains committed to supporting its companies with required liquidity. We believe the portfolio performance should continue to be supported by FinLab's active approach towards its holdings, management expertise and access to broad investor network. Meanwhile, FinLab also continues investing in blockchain projects through its EOS VC Fund.

Valuation: Discount to NAV widened markedly

FinLab's NAV total return was c 33% in 2019, with the discount to NAV widening to 45% at end-December 2019 from 24% a year earlier. Taking into account a c 4% share price drop since end-December 2019, FinLab is trading at a 47% discount to its last reported NAV. Heliad is trading at a discount of c 39% to its end-December 2019 NAV after its shares appreciated 8% since end-December 2019.

Historical financials

Year end	Total Income (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/16	4.9	14.0	2.98	0.00	4.8	N/A
12/17	4.4	14.5	2.85	0.00	5.0	N/A
12/18	4.7	17.1	3.14	0.00	4.5	N/A
12/19	4.6	4.3	7.33	0.00	1.9	N/A

Source: FinLab accounts

Financials

9 April 2020

Price €14.3
Market cap €76m

Share price graph



Share details

Code A7A
Listing Deutsche Börse Scale
Shares in issue 5.3m
Last reported net cash at end- 2019 €6.8m

Business description

FinLab is an incubator and builder of fintech companies based in Germany. It also has holdings in two relatively mature asset management businesses, Heliad and Patriarch, which gives it stable cash flows and a strong balance sheet. In March 2018, FinLab expanded its asset management portfolio with EOS VC Fund. It has 10 fintech investments.

Bull

- Strong balance sheet and stable cash flows.
- Exposure to various fintech segments.
- FinLab may benefit from positioning of some of its fintech companies after the COVID-19 outbreak.

Bear

- Uncertainties over the impact of COVID-19 on some of its holdings.
- Small free float and low liquidity.
- Fintech investments are inherently high risk and the portfolio is relatively concentrated.

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Write-up of Deposit Solutions drives FY19 results

In FY19, FinLab more than doubled its diluted EPS to €7.33 from €3.14 in FY18. Revenues related to services provided to subsidiaries and equity interest declined 26% y-o-y to €1.4m, affected by the lower performance fee from Heliad Management. At the same time, income from investments increased by a notable 19% y-o-y to €2.7m, backed by income streams from its asset management companies (Heliad Management, Patriarch and EOS VC Fund). This was despite the fact that FinLab did not receive a dividend from Heliad Equity Partners in FY19 (vs €0.9m in FY18). EBIT reached €2.2m (vs €0.8m in FY18) as operating expenses reduced by €1.5m to €2.4m on the back of the lower personnel expenses.

On top of that, the financial result improved to €38.1m from €16.3m, of which €37.8m was attributable to write-ups of its unlisted holdings. We estimate that this has largely resulted from the revaluation of FinLab's stake in Deposit Solutions, its largest portfolio holding, which made up 48% of its NAV at end-FY19 as per our calculations. This followed a funding round that Deposit Solutions completed with Deutsche Bank in September 2019, when the bank acquired a c 4.9% stake in the company. This transaction increased the valuation of Deposit Solutions to more than €1.0bn compared to €500m in its previous financing in August 2018. We described the recent transaction in more detail in [our flash note](#). Other write-ups in the period included Kapilendo and Iconic Holding, which we described in [our previous note](#). In the period, FinLab did not conduct any exits and thus did not record any notable income from the sales of securities, in contrast to the previous year when it realised income from its partial exit from Deposit Solutions. At present, FinLab intends to retain its 7.2% stake in the company.

In FY19, net income was €39.5m (vs €16.9m in FY18) while overall result reached €36.6m (loss of €3.7m in FY18), backed by a decline in revaluation reserves of €2.9m vs €20.6m in FY18 related to the weak share price performance of Heliad.

Exhibit 1: FY19 financial highlights			
€000s, unless otherwise stated	FY19	FY18	change y-o-y
Revenue	1,443	1,945	(25.8%)
Income from investments	2,678	2,250	19.0%
Other operating income	499	495	0.8%
Total income	4,620	4,690	(1.5%)
Personnel expenses	(892)	(2,439)	(63.4%)
Non-personnel expenses	(1,542)	(1,462)	5.5%
EBIT	2,186	789	177.1%
Financial result, of which:	38,082	16,294	133.7%
Income from the sale of securities and financial assets	318	10,144	(96.9%)
Retirement of securities and financial assets	(149)	(6,340)	(97.6%)
Write-ups and write-downs of securities and financial assets	37,800	12,462	N/M
Interest and similar income	152	35	N/M
Interest and similar expenses	(38)	(6)	N/M
EBT	40,268	17,083	135.7%
Taxes on income	(744)	(167)	N/M
Net result for the period	39,525	16,916	133.6%
EPS (€)	7.33	3.14	133.8%
Overall result (including change in revaluation reserve)	36,636	(3,669)	N/M

Source: FinLab accounts

In FY19, NAV per share increased by €6.68 to €27.12. As before, we estimate that at least €7.6 of this growth was related to revaluation of FinLab's stake in Deposit Solutions (see above), partly offset by a 14% decline in Heliad's share price in FY19. Consequently, NAV total return was 33% in FY19 and 26% pa since FinLab's establishment at end-2014.

It is worth noting that stock market volatility has a limited impact on FinLab's NAV as its only listed investment is Heliad (c 13% of its NAV at end-FY19) and the fintech companies are revalued on

completion of new financing rounds, which we acknowledge could be more difficult to execute in the current market conditions. That said, Heliad's share price increased 8% since end-FY19, which compares with a 22% drop for the DAX index. We believe this was assisted by a 19% share price appreciation of its major investment, online broker flatex, which represented c 63% of its NAV at end-FY19 (vs 56% at end-FY18) as per our estimates. Notably, in April 2020, flatex announced that its Q120 pre-tax profit significantly exceeded the FY19 figure, driven by a 130% y-o-y growth in the number of transactions amid high market volatility.

In FY19, Heliad recorded net income of €11.3m, compared with net loss of €56.6m in FY18. This was supported by net gains from the fair value assessment of €13.9m. We believe the main contributor was again flatex, whose share price increased c 43% in FY19. Importantly, Heliad will not recommend a dividend pay-out from its FY19 earnings.

Committed to supporting existing holdings

Management highlights that FinLab is well positioned in the COVID-19 pandemic, with the current market situation creating new opportunities for some of its fintech holdings. This has been already reflected in the performance of **nextmarkets**, an online broker, which has recorded significant growth in customers and turnover in recent weeks. Also, Bar9, a subsidiary of **Vaultoro** (a platform to trade physical gold for bitcoins), has doubled its gold trading volumes over the same period after gold traders closed the physical stores and online trading channels. In response to the COVID-19 pandemic, **Kapilendo**, a digital banking partner for small and medium enterprises (SMEs) and FinLab's third-largest portfolio holding, has initiated cooperation with financial advisers to provide liquidity to SMEs through promotional loans.

At the same time, FinLab acknowledges that uncertainty remains high and it cannot rule out that some of its portfolio holdings will need to adapt/revise their business models or refinance. However, it underlines that it is ready to supply its fintech holdings with additional liquidity, if necessary. At end-FY19, FinLab held €6.8m in cash (vs €13.4m at end-FY18) and total short-term assets of around €11m. In 2020, FinLab plans to develop existing holdings and selectively invest into blockchain projects through its asset management business, EOS VC Fund (see more below). The company has revealed that it will soon close two deals from the blockchain space, backed by, among others, a renowned company from the automotive sector.

We believe FinLab's active investment approach, management expertise and extensive network of investors and business partners are essential in the current market environment. On top of that, its largest holdings have been able to significantly scale up operations over recent years. **Deposit Solutions** connects banks from 20 European countries and has mediated €20bn+ in deposits from over 30m depositors through various channels. It employs over 300 people and is backed by renowned financial investors.

Authada became a certified service provider for the eID function in March 2019 and can now expand its identification services to unregulated markets, including e-commerce, e-health, e-betting, and e-mobility. We believe this creates a significant growth opportunity in as far as its offering has been limited to markets that are legally required to collect identity data (ie, financial, insurance and telecommunication sectors). We consider Authada a potential beneficiary of the coronavirus-induced lockdown and social distancing, which should drive digital solutions. Authada's major client wins since our last update note include VisualVest, a German digital wealth management company, and IDnow, a provider of identity-verification-as-a-service in Europe. Moreover, the AUTHADA app has run on iPhones since September 2019 while in November 2019, the company launched its identification solution in the trading app of nextmarkets. The latter presents FinLab's ability to create synergies across its portfolio. Finally, **Kapilendo** continues its transformation into a digital banking partner for SMEs. Interestingly, it listed the first digital security approved by the German banking authority at the end of 2019, raising €2.4m in the form of subordinated debt for the issuer.

Meanwhile, **EOS VC Fund** has continued deploying funds to projects focused on development of the EOS.IO platform (a blockchain protocol powered by the native cryptocurrency EOS). Its recent seven-digit euro investments were Agora Innovation, a Frankfurt-based blockchain start-up focused on blockchain, distributed ledger technology (DLT) and digital assets, as well as CAPTRACE, which offers custodian services secured by third-generation DLT. We appreciate FinLab's efforts to support projects focused on the use of DLT technology in financial services. This is in line with an important market trend that we examined in our recent report, [Blockchain adoption: Implications for the financial services sector](#).

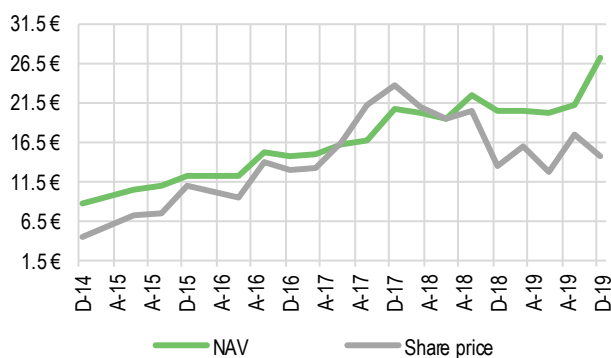
Valuation

FinLab's development is driven by its ability to grow its NAV. Earnings in any given year can be volatile and depend on the timing of revaluations and exits, which are reflected in the income statement on recognition.

During FY19, the company's NAV per share increased c 33% to €27.12, largely driven by the write-up of Deposit Solutions. Over the same period, the share price increased c 9%, which translated into a 45% discount to NAV at end-December 2019 (vs a discount of 24% at end-December 2018). Since end-December 2019, the discount has widened to c 47% after the share price declined by c 4% amid the broader market sell-off. Heliad Equity Partners comprised c 12.5% of FinLab's NAV at end-December 2019 and at that date, it traded at a c 44% discount to its end-December (last reported) NAV per share of €7.39. Although it is common for investment companies to trade at a discount, it is instructive to consider the impact on FinLab's NAV if Heliad's assets were reflected at NAV (especially given its majority represents the listed shares in flatex). If the discount was removed, FinLab's NAV (at end-December 2019) would increase to €29.86 per share and the current share price would represent a discount to the last reported NAV of c 52%.

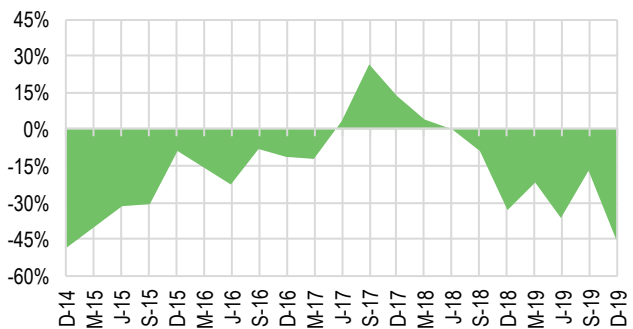
If we reflect the share price movements of major listed holdings within Heliad's portfolio (flatex, MagForce and Elumeo) since end-December 2019 and subsequently remove Heliad's discount to its end December NAV (ie, apply par value), Finlab's discount is 53%. This is largely a function of the 19% appreciation in the flatex share price since end-December 2019.

Exhibit 2: FinLab's share price and NAV performance



Source: FinLab, Edison Investment Research

Exhibit 3: FinLab's discount/premium to NAV



Source: FinLab, Edison Investment Research

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