

The NAGA Group

Software

13 July 2020

Recovering in favourable market conditions

NAGA recorded a heavy EBITDA loss in FY19, affected by adverse market conditions and a significant decline in revenues from services from Naga Development Association (NDAL). Preliminary Q120 figures show solid growth in sales and net income as the company benefited from high market volatility triggered by the COVID-19 pandemic and a lower operating cost base following the completion of group restructuring. The focus is now on expansion outside Europe, which it plans to finance with proceeds from a targeted €5m capital increase announced in June 2020.

FY19 results reflect recent challenges

EBITDA fell to a loss of €9.2m in FY19 (vs EBITDA of €0.3m in FY18) and the net loss was €13.4m (€4.1m in FY18) as lower operating expenses post restructuring (down 26% y-o-y) did not compensate for a significant drop in sales (brokerage sales and revenues from services were down 48% and 75% y-o-y respectively). In FY19, one-offs related to restructuring were €1.1m and it posted a €1.4m write-off of receivables from NDAL. When adjusted for restricted cash, net debt was €3.4m at end 2019 (vs net cash of €2.4m at end 2018). NAGA has received €5m funding from its core shareholder Fosun Fintech Holdings in recent months, including a €3.0m senior loan in November 2019 and a €2m convertible bond issued in January 2020 (both have a two-year maturity). It also secured €4.5m in a pre-placement of a targeted €5m capital increase announced in late June, which is expected to close in July.

Solid ytd performance in a supportive market

Preliminary figures report sales of €7.0m in Q120 (vs €0.6m in Q119) and net profit of €2.1m (net loss of €3.9m). Trading volume reached €47bn between end December 2019 and end May 2020, which already exceeds last year's figure (€41bn). NAGA's full-year guidance assumes significant growth in brokerage sales, coupled with a notable reduction in revenues from services after it decided to postpone works on NAGA Wallet and NAGA Exchange developed by NDAL. Consequently, NAGA expects higher EBITDA and net income in FY20.

Valuation: Improving after a weak performance

NAGA's share price increased to c €2.5 in early July 2020 after trading at all-time lows in H219 (c €0.6–1.0 per share over the period). Positive stock catalysts were solid Q120 results and strong trading figures amid high market volatility during the pandemic. NAGA trades at FY20 EV/sales of 5.3x and FY20 EV/EBITDA of 26.4x.

Consensus estimates

Year end	Revenue* (€m)	EBIT (€m)	PBT (€)	EPS (€)	P/E (x)	Yield (%)
12/18	16.1	(4.8)	(5.0)	(0.10)	N/A	N/A
12/19	6.2	(12.2)	(12.3)	(0.33)	N/A	N/A
12/20e	19.6	3.0	2.9	(0.03)	N/A	N/A
12/21e	23.1	3.9	3.8	0.02	124.0	N/A

Source: NAGA Group, Refinitiv consensus as at 8 July 2020. Note: *Revenue includes brokerage sales and revenues from services as reported by the company.

Price €2.32

Market cap €93m

Share price graph



Share details

Code	N4G
Listing	Deutsche Börse Scale
Shares in issue	40.2m
Last reported net debt at end-2019*	€3.4m

*Adjusted for restricted cash of €2.9m

Business description

The NAGA Group is a fintech start-up in social trading with a flagship product (Naga Trader) and supplementary services. Headquartered in Hamburg, the company's operating subsidiary Naga Markets Ltd. is located in Limassol, Cyprus.

Bull

- The COVID-19 pandemic has driven market volatility, which supports NAGA's performance.
- Completed restructuring may improve results in FY20.
- Ongoing expansion to Asia may boost sales.

Bear

- NAGA has increased its leverage over recent months.
- Sales and earnings are dependent on market conditions historically.
- Business activity in emerging markets poses a greater risk than in developed countries.

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Substantial EBITDA loss and drop in sales in FY19

NAGA's total performance declined to €7.0m in FY19 from €17.7m a year earlier, which was a function of a sharp drop in brokerage sales, revenues from services and activated programming services. Brokerage sales decreased by 48% y-o-y to €4.2m, due to lower market volatility in the period as well as the launch of ESMA regulations in July 2018 (which introduced new leverage restrictions for retail clients trading in CFDs). Revenues from services were down 75% y-o-y to €2.0m and included c€1.4m generated on sales from its advisory services to NDAL, significantly down vs €7.6m a year earlier. NDAL is NAGA's business partner; it raised US\$50m from an initial coin offering (ICO) conducted in December 2018 and is responsible for the development and operations of the NAGA Coin, NAGA Wallet and NAGA Exchange.

We note that NAGA's operating expenses included a €1.4m write-off on receivables from NDAL vs €1.7m in FY18 (the company had €1.4m in trade receivables from NDAL at end 2019). A similar write-off occurred in FY18. As highlighted in our [previous update note](#), we believe this write-off may indicate that these proceeds are now largely exhausted, as they were already spent and/or because some part was held in cryptocurrencies and lost a significant part of its value. We understand that NAGA does not expect any meaningful revenues from services in FY20 because its focus is now on NAGA Trader. At the same time, NAGA highlights that it will continue its cooperation with NDAL on operating NAGA Wallet and NAGA Exchange. However, we understand NAGA will postpone additional development of NAGA Wallet and NAGA Exchange until after 2020.

Exhibit 1: Financial summary

€000s	FY19	FY18	y-o-y change
Revenue	6,224	16,119	(61.4%)
Brokerage revenue	4,222	8,119	(48.0%)
Revenue from services	2,001	8,001	(75.0%)
Activated programming services (commissions)	779	1,595	(51.2%)
Total performance	7,002	17,715	(60.5%)
Other operating income	167	4,719	(96.5%)
Services purchased	0	(2,899)	N/M
R&D expenses	(1,717)	(2,605)	(34.1%)
Brokerage expenses	(1,339)	(1,071)	25.0%
Commission expenses	0	29	N/M
Personnel expenses	(4,589)	(6,819)	(32.7%)
Marketing & advertising expenses	(2,455)	(1,774)	38.4%
Value adjustments on receivables	(1,410)	(1,803)	(21.8%)
Other operating expenses	(4,828)	(5,221)	(7.5%)
EBITDA	(9,167)	270	N/M
D&A	(2,745)	(5,086)	(46.0%)
Amortisation of goodwill	(270)	0	N/M
EBIT	(12,182)	(4,816)	N/M
Financial income	7	18	(61.1%)
Financial costs	(132)	(161)	(18.0%)
Income (loss) before taxes	(12,307)	(4,959)	N/M
Income taxes	(151)	(447)	(66.2%)
Deferred taxes	(919)	1,307	(170.3%)
Net profit/(loss)	(13,377)	(4,100)	N/M

Source: The NAGA Group accounts

In FY19, operating expenses reduced by 26% y-o-y to €16.3m. This was backed by lower personnel costs, largely driven by a reduction in management board salaries (€0.3m in FY19 vs €1.6m in FY18) as well as reduced R&D expenses. These reductions were partly offset by higher marketing costs resulting from the company's decision in 2019 to enter markets outside Europe and minor other operating expenses, which in the previous year were generated in the form of a surcharge on the services purchased from NDAL. Restructuring costs of €1.1m in FY19 mostly comprised a €0.4m severance payment to co-founder and former CEO Yasin Qureshi, who moved from the management board to a newly created advisory board on 30 April 2019, a €0.4m indemnity

payment for the cancellation of an advertising contract with HSV and €0.3m in compensation payments to its employees in Spain, where the company closed its offices in FY19.

Lower operating costs did not compensate for the significant drop in sales and EBITDA declined to a loss of €9.2m versus €0.3m in FY18, while the net loss was €13.4m versus a net loss of €4.1m a year earlier.

NAGA had 25.4k customers at end December 2019 (versus 22.4k at end December 2018) and managed assets of c €17.6m (€15.8m). The average number of active users increased to 5.1k per month in 2019 (4.3k) and trading volume reached €41bn (€36bn).

Capital injections to facilitate growth

Capital base supported by funding from Fosun

The operating cash outflow was €2.4m in FY19 (vs an outflow of €2.9m in FY18) and cash stood at €3.2m at the period end (€3.7m). Of this amount, €2.9m was under restriction of disposal as these funds were deposited as security with liquidity providers. Net debt adjusted for the latter reached €3.4m, compared to net cash of €2.4m at end 2018. Over the period, the company increased its long-term liabilities after it received a €3.0m senior loan in November 2019 from Fosun Fintech Holdings, a subsidiary of the Chinese conglomerate Fosun Group and NAGA's core shareholder with a c 30% stake in the company. The loan has a two-year maturity and an interest rate of 12% per annum. In addition, the company recorded €0.6m in liabilities to shareholders and board members, which are due once NAGA achieves a certain (undisclosed) level of EBITDA. We note that total assets were €119.0m at end 2019 and they mostly included intangible assets (c €109m), of which €95.0m was goodwill from the HBS transaction (see our [update note](#) for more details).

NAGA further increased its leverage post the period end after Fosun Fintech Holdings granted it a €2.0m convertible bond in January 2020. The bond also has a two-year maturity and a coupon of 6% per annum. We estimate that the €5m funding provided by Fosun Fintech Holdings in late FY19 and early FY20 implies an annual interest expense of c €480k. In May 2020, NAGA's liquidity position was supported by the disposal of its stake in easyfolio (a robo advisor offering ETF portfolio strategy products) for c €0.2m. It acquired a c 50% share in the company for €0.5m in 2018 and had increased its stake to 100% in December 2019 for an undisclosed amount.

Targeting €5m proceeds from share issue

In June 2020, NAGA announced it planned to conduct a capital increase with a targeted volume of €5.0m, which it mostly intends to use to finance its international expansion and marketing activities. The company will issue 2m shares at a subscription price of €2.50 per share (versus a closing price of €3.06 per share a day before the announcement). A day following the announcement, NAGA revealed that 91% of existing investors had waived subscription rights, but it had secured the corresponding amount of €4.5m in a pre-placement of 1.8m shares to other German and international investors. Subscription started on 3 July and will finish on 16 July 2020.

Market volatility assists performance post restructuring

By the end of 2019, NAGA had completed the restructuring of the group, which it initiated in April 2019 (please refer to our [update note](#) for more details). In early April 2020, the company released preliminary Q120 figures, reporting a significant year-on-year growth in sales to €7.0m (vs €0.6m in Q119) and net profit at €2.1m (vs a net loss of €3.9m). During the period, trading volume reached €23bn (already more than half of the FY19 volume of €41bn) and the customer base doubled compared with end 2019. The company highlights that high market volatility triggered by the COVID-19 pandemic has had a positive impact on its business so far in 2020. It revealed recently

that the trading volume in April and May 2020 totalled €24bn and it attracted more new clients than in Q120.

For 2020, NAGA guides to a significant growth in brokerage revenues but it does not expect any meaningful revenues from services. The company's guidance assumes a significantly higher EBITDA, supported by lower operating costs due post restructuring, as well as higher net income despite an increase in financial expenses (as discussed above). NAGA expects strong growth in its customer base and trading volume.

The company hopes its growth will be assisted by expansion outside Europe (in FY19 it generated 67.5% of its sales in Europe). Over recent months, the company has opened new offices in Uruguay and Thailand and started operations in China in June 2020. As part of the restructuring, NAGA reduced its management board to two members when Yasin Qureshi left it in April 2019. However, in November 2019 the company appointed Michalis Mylonas as the third board member. He has been CEO of NAGA Markets since 2017 and is now responsible for finance and regulations within the group.

In respect of recent product portfolio developments, the company launched NAGA Stocks in January 2020, which allows European users to trade directly in 400 stocks listed on nine stock exchanges without commission and offers access to 40k financial instruments, including CFDs, FX, ETFs and cryptocurrency. In May 2020, NAGA commenced NAGAPro, a platform for the use of trading influencers, and announced that it will develop its own challenger bank NAGA Pay, which will combine mobile banking, trading, social trading and cryptocurrency trading. Its launch is planned for Q420.

Valuation

NAGA's share price was c €2.5 per share at 8 July 2020, which compares with its IPO price of €2.6 per share and represents a notable growth from the all-time low of c €0.6 per share at the end of 2019.

Given NAGA's short operating history and business focus, blockchain and fintech companies still in the ramp-up phase may be appropriate comparators for valuation purposes. Having said that, we acknowledge that NAGA's lack of profits last year (although it turned profitable in Q120) and turnaround stage limit the value of this comparison. The peer group includes online brokers (eg IG Group, CMC Markets and flatex), which are however more mature and profitable companies. NAGA is trading at an FY20 EV/sales ratio of 5.3x and FY20 EV/EBITDA ratio of 26.4x based on consensus forecasts.

Exhibit 2: NAGA group peer comparison

Company name	Market cap local ccy (m)	Stock exchange	P/E (x)			EV/sales (x)			EV/EBITDA (x)	
			2019	2020e	2021e	2019	2020e	2021e	2019	2020e
IG Group	£3,174	LSE	20.2	13.7	13.7	5.8	4.5	5.1	13.6	9.4
CMC Markets	£986	LSE	11.5	11.2	11.2	3.6	3.2	4.0	8.0	8.5
Alpha FX Group	£281	LSE	24.1	27.5	27.5	6.0	5.7	4.6	13.9	14.6
JOYY Inc	CNY6,729	Nasdaq	22.1	23.8	23.8	N/A	N/A	N/A	N/A	N/A
flatex AG	€826	Deutsche Börse	54.5	24.6	24.6	8.9	5.5	4.2	31.1	14.3
Peer group average			26.5	20.2	20.2	6.0	4.7	4.5	16.7	11.7
Naga Group	€100	Deutsche Börse	N/A	N/A	124.0	16.6	5.3	4.5	N/A	26.4
Premium/(discount)			N/A	N/A	N/M	174%	11%	0%	N/A	126%

Source: Refinitiv data at 8 July 2020, Edison Investment Research

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