

# Verisec

Sector: Information Technology

## Impressive growth intact

### Higher base case of SEK 125 per share

For the second quarter in a row Verisec reports impressive growth numbers, exceeding our estimates by a wide margin. Higher sale estimates and exclusion of an anticipated share issue this year motivates a higher base case of **SEK 125 (110) per share**. As the company now has solved the short-term capital need with a financing limit of up to SEK 30 million, we now longer include dilution (8% before this update) from any capital raising.

### 47 percent growth

Sales at SEK 28.2 (19.2) million increased by 47% y/y, compared to estimates of SEK 20.0 million. Growth during the quarter was attributable to Verisecs international markets. In Q1'19 sales increased by 59% (compared to estimates of 4%). We did not believe that the outcome represented a new "normal" level and thus did not extrapolate the growth numbers. Of course, the Q2'19 figures contradicts this conclusion and we have now raised our sale estimates by 17%/20% for '19e/20e.

### EBIT in line with projections

Adjusted for the difference in activated costs (SEK 0.7 million), the EBIT loss (investments in Freja eID burdens profitability) at SEK -7.9 (-8.5) million was in line with estimates. This was driven by a weaker gross margin of 60 (58) % (estimates: 63) and higher other OPEX of SEK -24.9 (-16.3) million (estimates: -19.4), up from SEK -21.1 million in Q1'19. Our sale revisions are somewhat mitigated by higher cost estimates.

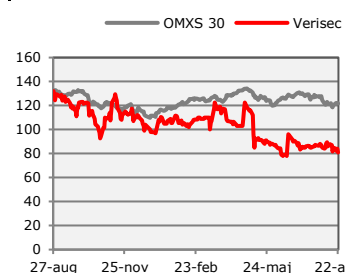
### Freja eID – several new agreements

Regarding Freja eID, Verisec has signed several agreements during the last period, including with Svenska Spel and integrators such as Pulsen Integration AB. Also, in May, Freja eID was established in the Norwegian market. Verisec communicates that the focus on users will increase during the autumn. According to us, this is Verisecs most important task to become a platform company – to aggregate demand (users). As noted earlier, we would like to get a better insight about the users to improve the evaluation of the case. Going forward, the number of users will be the dominant factor in our assessment of the investment case

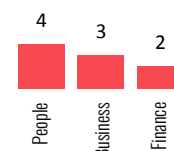
KEY FINANCIALS (SEK)	2017	2018	2019E	2020E	2021E	2022E
Net sales	64	76	105	140	169	211
EBITDA	-14	-22	-19	-1	16	57
EBIT	-22	-28	-32	-16	1	42
EPS (adj.)	-4.8	-6.2	-6.5	-3.2	0.2	6.7
EV/Sales	8.5	5.8	3.3	2.5	2.0	1.6
EV/EBITDA	Neg.	Neg.	Neg.	Neg.	27.9	6.0
EV/EBIT	Neg.	Neg.	Neg.	Neg.	N.M.	8.2
P/E	Neg.	Neg.	Neg.	Neg.	N.M.	12.0

### FAIR VALUE RANGE

BEAR	BASE	BULL
50.0	125.0	350.0



### REDEYE RATING



### KEY STATS

Ticker	VERI.ST
Market	First North
Share Price (SEK)	79.8
Market Cap (MSEK)	389
Net Debt 19E (MSEK)	-43
Free Float	43 %

### ANALYSTS

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## Verisec: Q2'19

Net sales amounted to SEK 28.2 (19.2) million (expected: 20.0) with an operating profit of SEK -7.9 (-8.5) million (expected: -8.7).

Verisec: Estimates vs. Outcome, Q2'19				
(SEKm)	Q2'18	Q2'19e	Outcome	Dev. (Abs.)
<b>Net sales</b>	<b>19.2</b>	<b>20.0</b>	<b>28.2</b>	8.2
<i>growth y/y</i>	55%	4%	47%	
Activated costs	1.4	1.3	2.0	0.7
<b>Total revenue</b>	<b>20.7</b>	<b>21.3</b>	<b>31.7</b>	10.4
COGS	-8.1	-7.4	-11.3	
Personnel costs	-11.5	-12.0	-14.3	
Other OPEX	-8.0	-7.4	-10.6	
<b>EBITDA</b>	<b>-6.9</b>	<b>-5.5</b>	<b>-4.5</b>	1.0
D&A	-1.6	-3.2	-3.4	
<b>EBIT</b>	<b>-8.5</b>	<b>-8.7</b>	<b>-7.9</b>	0.8
Gross-margin	58%	63%	60%	-3.1 pp
EBITDA-margin	neg	neg	neg	
EBIT-margin	neg	neg	neg	

Source: Redeye Research, Verisec

Looking at the revenue distribution the growth is not driven by Sweden (and consequently not by Freja eID). Geographies outside Sweden were the growth drivers during the quarter. Both 'Goods' and 'Services' showed a big uptake, even though 'Services' outperformed.

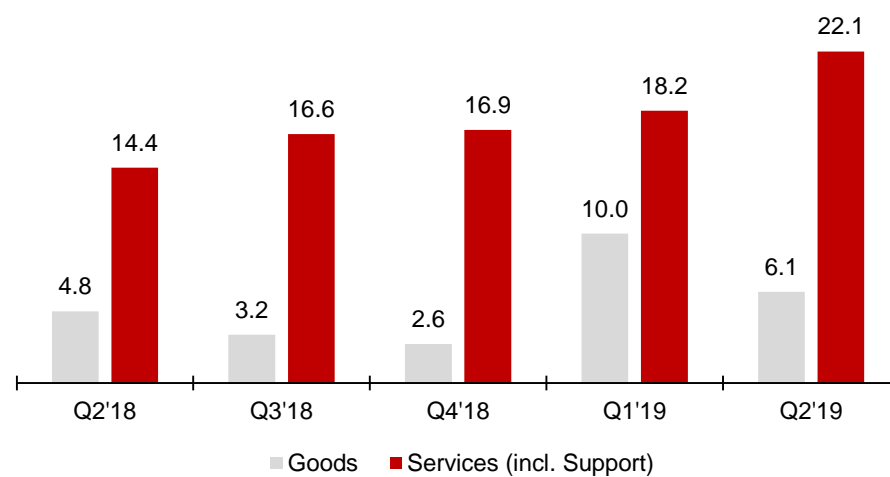
Verisec: Revenue distribution, Q2'18/Q2'19			
(SEKm)	Q2'18	Q2'19	Change
<i>by geography</i>			
Sweden	10.3	10.1	-2%
<i>% of total sales</i>	54%	36%	
Europé (excl. Sweden)	5.3	11.1	111%
<i>% of total sales</i>	27%	39%	
Others	3.6	7.0	94%
<i>% of total sales</i>	19%	25%	
<b>Total sales</b>	<b>19.2</b>	<b>28.2</b>	<b>47%</b>
<i>by product</i>			
Goods	4.8	6.1	27%
<i>% of total sales</i>	25%	22%	
Services (incl. Support)	14.4	22.1	54%
<i>% of total sales</i>	75%	78%	
<b>Total sales</b>	<b>19.2</b>	<b>28.2</b>	<b>47%</b>

Source: Redeye Research, Verisec

Services grew 54% y/y and has also showed a consistent development q/q during the last year which supports future sales. 'Goods' shows a bigger variance due to the nature of the business (irregular and bigger orders skew the numbers). This is due to the long sales cycle, and something that will be evident also in the future, resulting in sales that will fluctuate.

**Verisec: Revenue distribution, Q2'18-Q2'19, SEKm**

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Source: Redeye Research, Verisec

## Financial projections

Following the report, we raise both out sales and cost estimates, resulting in an almost unchanged EBIT. Going forward, the number of users will be the dominant factor in our assessment of the investment case as we believe that power, for “digital goods”, comes from controlling demand (users). The number of users during 2019-2020 will have a big impact on our view of the investment case and thus our valuation.

It is hard to put estimates on the number of users connected to Freja eID in 2019-2020, but one can look at specific clusters of users within the public sector

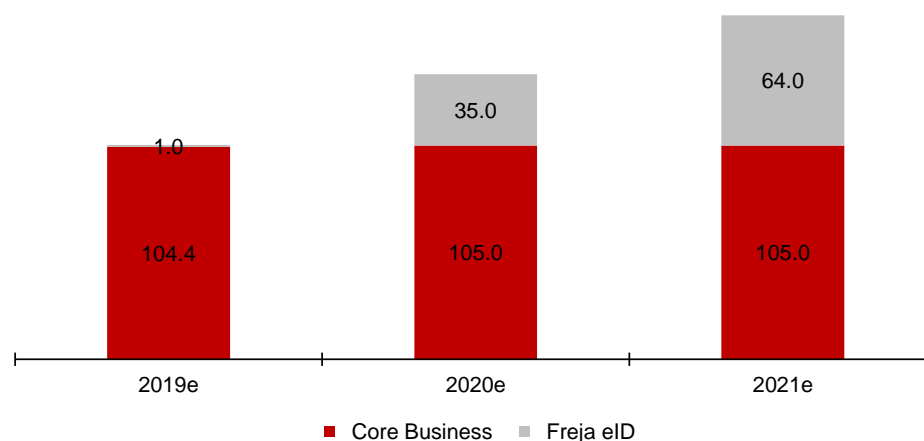
(focus vertical for Verisec) in Sweden. The number of employees in the public sector is around 1.6 million. The number of employees in municipalities and county councils is over 1 million, where 270 000 is within county councils. We think that market penetration of 30 percent of the total employees (that is 300 000 users) in municipalities and county councils should be a realistic and achievable number the coming years.

### Verisec: Estimates changes, '19e-'20e

(SEKm)	2019e	2020e
<b>Net sales (new)</b>	<b>105</b>	<b>140</b>
Net sales (old)	90	117
change (%)	17%	20%
<b>COGS (new)</b>	<b>-40</b>	<b>-43</b>
COGS (old)	-33	-36
change (%)	-21%	-21%
<b>OPEX (new)</b>	<b>-92</b>	<b>-104</b>
OPEX (old)	-78	-88
change (%)	-17%	-18%
<b>EBIT (new)</b>	<b>-32</b>	<b>-16</b>
EBIT (old)	-30	-16
change (%)	-8%	3%

Source: Redeye Research

### Verisec: Sales by business segment, '19e-'21e, SEKm



Source: Redeye Research

## Detailed estimates

Verisec: Estimates '19e-'21e												
(SEKm)	Q1'18	Q2'18	Q3'18	Q4'18	2018	Q1'19	Q2'19	Q3'19e	Q4'19e	2019e	2020e	2021e
<b>Net sales</b>	<b>17.7</b>	<b>19.2</b>	<b>19.8</b>	<b>19.5</b>	<b>76.2</b>	<b>28.1</b>	<b>28.2</b>	<b>25.0</b>	<b>24.0</b>	<b>105.4</b>	<b>140.0</b>	<b>169.0</b>
Core Business	17.7	19.2	19.8	19.5	76.2	28.1	28.2	24.5	23.5	104.4	105.0	105.0
Freja eID	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.5	0.5	1.0	35.0	64.0
Growth YoY (%)	24.9%	54.5%	7.3%	21.9%	24.8%	59%	47%	26%	23%	38%	33%	21%
Activated costs	0.9	1.4	1.3	1.3	4.9	1.0	2.0	1.4	1.4	5.8	6.0	8.0
<b>Total revenue</b>	<b>18.7</b>	<b>20.6</b>	<b>21.1</b>	<b>20.8</b>	<b>81.1</b>	<b>29.2</b>	<b>31.7</b>	<b>26.4</b>	<b>25.4</b>	<b>111.2</b>	<b>146.0</b>	<b>177.0</b>
COGS	-6.6	-8.1	-7.2	-6.4	-28.2	-10.6	-11.3	-9.3	-8.9	-40.1	-43.4	-47.3
Personnel costs	-10.9	-11.5	-10.2	-11.8	-44.4	-13.9	-14.3	-12.0	-14.3	-54.5	-61.6	-67.8
Other OPEX	-8.4	-8.0	-6.1	-7.7	-30.2	-7.2	-10.6	-8.5	-10.8	-37.1	-41.9	-46.1
<b>EBITDA</b>	<b>-7.2</b>	<b>-7.0</b>	<b>-2.4</b>	<b>-5.1</b>	<b>-21.7</b>	<b>-2.6</b>	<b>-4.5</b>	<b>-3.4</b>	<b>-8.6</b>	<b>-20.5</b>	<b>-1.0</b>	<b>15.8</b>
D&A	-1.6	-1.6	-1.7	-1.9	-6.9	-3.1	-3.4	-3.4	-3.5	-13.5	-14.6	-14.7
<b>EBIT</b>	<b>-8.7</b>	<b>-8.5</b>	<b>-4.1</b>	<b>-7.1</b>	<b>-28.5</b>	<b>-5.7</b>	<b>-7.9</b>	<b>-6.8</b>	<b>-12.1</b>	<b>-34.0</b>	<b>-15.5</b>	<b>1.1</b>
Gross-margin	63%	58%	64%	67%	63%	62%	60%	63%	63%	62%	69%	72%
EBITDA-margin	neg	neg	neg	neg	neg	neg	neg	neg	neg	neg	-1%	9%
EBIT-margin	neg	neg	neg	neg	neg	neg	neg	neg	neg	neg	-11%	0.6%

Source: Redeye Research, Verisec

## Valuation

Based on our discount rate of 12.0 percent (used in all scenarios), we have a fair value range of **SEK 50-350 (45-310)** with a base case of **SEK 125 (110) per share**. As the company now has solved the short-term capital need with a financing limit of up to SEK 30 million, we now longer include dilution (8% before this update) from any capital raising this year. In conjunction with higher sale estimates this motivates a higher valuation.

### Bear Case 50.0 SEK

In our bear case scenario, we expect Freja eID to be used as a complement to more dominating standards such as BankID. In this scenario, Freja eID will not become one of the most used electronic identities in Sweden. The landscape within this segment will become more competitive in the near future, and Freja eID will only be used within minor niche segments such as the public sector. Most revenues will, therefore, come from Verisec's core business.

The average growth rate during 2018-2022 is set to 17 percent and profitability is postponed to 2022. The company will be able to maintain a margin at around 14 percent on a maturity level.

### Base Case 125.0 SEK

In base case we expect Freja eID to become a standard in the public sector. Member organizations and niche banks are also expected to offer Freja eID as a complement to BankID. We believe that cost savings and simplified customer processes will attract retail chains and e-commerce players. eIDAS and other regulations will be key future drivers for Freja eID.

If Freja eID succeeds in achieving critical mass, we believe that gambling companies and various payment solutions providers will be potential customers.

For a platform company, EBIT-margins around 40 percent is possible. The economies of scale are evident, providing substantial margins. However, at this early stage, we estimate a margin at around 20 percent on a maturity level. The EBIT margin is expected to turn positive 2021 with an average sales growth of 28 percent during 2018-2022.

### Bull Case 350.0 SEK

In our bull case scenario, the strategic transformation into a platform company becomes successful with higher market penetration in most of the communicated customers segments compared to the base case. We also estimate a higher growth rate for the core business compared to the base case.

The company will be able to maintain a margin at around 35 percent on a maturity level with average margins around 11 percent. Average sales growth is estimated to be 50 percent during 2018-2022 per year.

## Catalysts

### Framework agreement

Framework agreement with a large cluster of municipalities

### A major niche bank

Resurs Bank is already a service provider, other niche banks will highly likely offer Freja eID.

### Big member organization

We see the public sector and member organisations as the most likely customers in 2019. Many potential service providers have millions of users.

## Summary Redeye Rating

The rating consists of three valuation keys, each constituting an overall assessment of several factors that are rated on a scale of 0 to 1 points. The maximum score for a valuation key is 5 points.

### Rating changes in the report

**People: 4**

The allocation of capital by management can be considered value-accretive by observing its track record. Transparency could be increased to some extent in terms of more detailed segment revenues for example. Although, management has historically allowed Verisec to grow with profitability at a pace it can handle. The stable ownership from Marquay Invest (56%) were the CEO and founder Johan Henrikson is a major shareholder has enabled the company to grow profitably and to constantly evolve its products and services.

**Business: 3**

The company has since its inception been able to transform its product offering in line with user convenience trends. However, the competition is intense and there are a number of initiatives that pose a danger to the company in the longer term. Verisec has historically had an impressive profitability record during periods of high growth. The last years the level of profitability has dropped due to its expansion and investments in Freja eID. If the company succeed in its transformation to a platform company (Freja eID) the economies of scale are evident and will enable high margins.

**Financials: 2**

Verisec and its core business have a large proportion of recurring revenue and a relatively diversified allocation of revenue among its customers. Verisec has solved the short-term capital need with a financing limit of up to SEK 30 million. As for now, we are uncertain about the near-term development for Freja eID and its effect on the cash flow. This uncertainty should disappear the coming quarters and a higher score will be motivated if Freja eID scales up sooner than expected (in terms of growth).

INCOME STATEMENT	2017	2018	2019E	2020E	2021E
Net sales	64	76	105	140	169
Total operating costs	-77	-98	-124	-141	-153
EBITDA	-14	-22	-19	-1	16
Depreciation	-4	-6	-3	-3	-3
Amortization	-5	-1	-11	-11	-12
Impairment charges	0	0	0	0	0
EBIT	-22	-28	-32	-16	1
Share in profits	0	0	0	0	0
Net financial items	1	-1	-1	0	0
Exchange rate dif.	0	0	0	0	0
Pre-tax profit	-21	-29	-33	-16	1
Tax	0	0	1	0	0
Net earnings	-21	-30	-32	-16	1

BALANCE SHEET	2017	2018	2019E	2020E	2021E
<b>Assets</b>					
<i>Current assets</i>					
Cash in banks	18	29	48	31	30
Receivables	14	19	26	35	42
Inventories	2	1	2	2	3
Other current assets	16	15	15	15	15
Current assets	50	64	92	84	91
<i>Fixed assets</i>					
Tangible assets	5	6	7	8	9
Associated comp.	0	0	0	0	0
Investments	0	0	0	0	0
Goodwill	0	0	0	0	0
Cap. exp. for dev.	0	0	0	0	0
0 intangible rights	9	14	15	11	7
0 non-current assets	0	0	11	11	11
Total fixed assets	14	20	33	30	27
Deferred tax assets	0	0	0	0	0
Total (assets)	64	85	125	114	118
<b>Liabilities</b>					
<i>Current liabilities</i>					
Short-term debt	0	0	6	6	14
Accounts payable	39	46	68	73	68
0 current liabilities	0	0	0	0	0
Current liabilities	39	46	74	78	81
Long-term debt	0	0	0	0	0
0 long-term liabilities	0	0	7	7	7
Convertibles	0	0	0	0	0
Total Liabilities	39	46	81	85	88
Deferred tax liab	0	0	0	0	0
Provisions	0	0	0	0	0
Shareholders' equity	24	39	45	29	30
Minority interest (BS)	0	0	0	0	0
Minority & equity	24	39	45	29	30
Total liab & SE	64	85	125	114	118

FREE CASH FLOW	2017	2018	2019E	2020E	2021E
Net sales	64	76	105	140	169
Total operating costs	-77	-98	-124	-141	-153
Depreciations total	-9	-7	-13	-14	-15
EBIT	-22	-28	-32	-16	1
Taxes on EBIT	0	0	0	0	0
NOPLAT	-22	-28	-32	-16	1
Depreciation	9	7	13	14	15
Gross cash flow	-14	-22	-19	-1	16
Change in WC	13	3	15	-5	-13
Gross CAPEX	-12	-13	-27	-11	-12
Free cash flow	-13	-32	-31	-17	-9

CAPITAL STRUCTURE	2017	2018	2019E	2020E	2021E
Equity ratio	38%	46%	36%	25%	25%
Debt/equity ratio	0%	0%	12%	19%	46%
Net debt	-18	-29	-43	-25	-17
Capital employed	6	10	2	4	13
Capital turnover rate	1.0	0.9	0.8	1.2	1.4

GROWTH	2017	2018	2019E	2020E	2021E
Sales growth	3%	20%	38%	33%	21%
EPS growth (adj)	19%	29%	6%	-50%	-107%

DCF VALUATION		CASH FLOW, MSEK	
WACC (%)	12.0 %	NPV FCF (2018-2020)	-33
		NPV FCF (2021-2027)	255
		NPV FCF (2028-)	344
		Net Debt	43
		Fair value estimate MSEK	609
Assumptions 2017-2023 (%)			
Average sales growth	21.6 %	Fair value e. per share, SEK	125.0
EBIT margin	6.4 %	Share price, SEK	79.8

PROFITABILITY	2017	2018	2019E	2020E	2021E
ROE	-63%	-93%	-76%	-43%	4%
ROCE	-53%	-90%	-73%	-37%	3%
ROIC	-142%	-455%	-330%	-879%	29%
EBITDA margin	-22%	-28%	-18%	-1%	9%
EBIT margin	-35%	-37%	-31%	-11%	1%
Net margin	-33%	-39%	-30%	-11%	1%

DATA PER SHARE	2017	2018	2019E	2020E	2021E
EPS	Neg.	Neg.	Neg.	Neg.	0.17
EPS adj	Neg.	Neg.	Neg.	Neg.	0.17
Dividend	0.00	0.00	0.00	0.00	0.00
Net debt	-4.10	-6.04	-8.81	-5.18	-3.40
Total shares	4.44	4.79	4.87	4.87	4.87

VALUATION	2017	2018	2019E	2020E	2021E
EV	540.8	440.2	345.9	345.9	345.9
P/E	Neg.	Neg.	Neg.	Neg.	N.M.
P/E diluted	Neg.	Neg.	Neg.	Neg.	N.M.
P/Sales	8.8	6.2	3.7	2.8	2.3
EV/Sales	8.5	5.8	3.3	2.5	2.0
EV/EBITDA	Neg.	Neg.	Neg.	Neg.	21.9
EV/EBIT	Neg.	Neg.	Neg.	Neg.	N.M.
P/BV	22.9	12.1	8.8	13.6	13.2

SHARE PERFORMANCE	GROWTH/YEAR	16/18E	
1 month	-6.9 %	Net sales	28.7 %
3 month	-10.0 %	Operating profit adj	20.7 %
12 month	-39.5 %	EPS, just	16.8 %
Since start of the year	-17.6 %	Equity	35.2 %

SHAREHOLDER STRUCTURE %	CAPITAL	VOTES
Marquay Invest AB	55.5 %	55.5 %
Swedbank Robur Fonder	9.4 %	9.4 %
Handelsbanken Fonder	5.5 %	5.5 %
Svolder AB	5.1 %	5.1 %
AMF Aktiefond Småbolag	3.9 %	3.9 %
Merlinum AB	3.8 %	3.8 %
Kristofer von Beetzen	2.5 %	2.5 %
Arpeggio AB	1.5 %	1.5 %
Avanza Pension	1.1 %	1.1 %
Nordnet Pensionsförsäkring AB	0.9 %	0.9 %

SHARE INFORMATION	
Reuters code	VERI.ST
List	First North
Share price	79.8
Total shares, million	4.9
Market Cap, MSEK	388.8

MANAGEMENT & BOARD	
CEO	Johan Henrikson
CFO	Jakub Missuna
IR	Kristofer von Beetzen
Chairman	Christian Rajter

FINANCIAL INFORMATION	

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## Redeye Rating and Background Definitions

### Company Quality

Company Quality is based on a set of quality checks across three categories; PEOPLE, BUSINESS, FINANCE. These are the building blocks that enable a company to deliver sustained operational outperformance and attractive long-term earnings growth.

Each category is grouped into multiple sub-categories assessed by five checks. These are based on widely accepted and tested investment criteria and used by demonstrably successful investors and investment firms. Each sub-category may also include a complementary check that provides additional information to assist with investment decision-making.

If a check is successful, it is assigned a score of one point; the total successful checks are added to give a score for each sub-category. The overall score for a category is the average of all sub-category scores, based on a scale that ranges from 0 to 5 rounded up to the nearest whole number.

The overall score for each category is then used to generate the size of the bar in the Company Quality graphic.

### People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.

The People rating is based on quantitative scores in seven categories: Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board.

### Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.

The Business rating is based on quantitative scores grouped into five sub-categories: Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks.

### Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.

The Financial rating is based on quantitative scores that are grouped into five separate categories: Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality.

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## Disclaimer

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### Redeye Rating (2019-08-28)

Rating	People	Business	Financials
5p	11	8	1
3p - 4p	49	41	26
0p - 2p	20	31	53
Company N	80	80	80

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### CONFLICT OF INTERESTS

Havan Hanna owns shares in the company: No

Tomas Otterbeck owns shares in the company: No

Redeye performs/have performed services for the Company and receives/have received compensation from the Company in connection with this.