

23 March 2011

## MCB Finance Group

Year End	Net revenue (€m)	PBT* (€m)	EPS* (c)	DPS (c)	P/E (x)**	Yield (%)
12/09	15.7	(0.6)	(6.1)	0.0	N/A	N/A
12/10	11.8	0.5	1.3	0.0	21.9	N/A
12/11e	14.6	1.6	6.8	0.0	4.2	N/A
12/12e	17.1	2.1	9.6	0.0	3.0	N/A

Note: \*PBT and EPS are on a pro-forma company basis. \*\* Converted at €1.163/£.

### Investment summary: Storm to following wind

Having survived the credit crunch and remained profitable throughout in all countries except Latvia, MCB Finance Group's (MCB) loan offering in the Fenno-Baltic region now has the potential for material growth. The IMF forecasts real 2011 GDP growth of c 3%, the product is underpenetrated in Latvia and Lithuania, and MCB can further grow with wider geographic, product and retailer distribution. The stock is not risk free, but if investors gain confidence in estimates, the share re-rating is likely to be sharp. Delivery on our conservative numbers will be enough.

#### 2008/09: The perfect storm

MCB faced the perfect storm in 2008/09. The business faced major challenges as most of the economies in which it operates entered deep recessions and credit costs rocketed. To manage risk, lending was severely curtailed, reducing income. To its credit, ex-central costs, MCB remained profitable in all countries except Latvia, where the duration of lending, over-confidence in models and some weaknesses in modelling techniques saw impairments soar. MCB is a single-bank financed lender and this also raised funding concerns. Sentiment collapsed against all non-prime lenders, Baltic exposure and lenders reliant on statistical modelling of risk.

#### 2010: The turn into a following wind

2010 was a turning point. It saw the group return to profit with impairments falling by around two-thirds. With stronger economic growth, MCB can return to lending (2010 credit issued down 10% on 2009) and generate revenue growth as well as seeing credit continue to improve. Post-Latvian losses, credit-scoring techniques have been enhanced with much more data input into models and tighter over-riding rules applied. Funding has been renewed. The Maxima distribution agreement has been widened to Latvia and Estonia; we believe new countries will follow in due course.

#### Valuation: Confidence in estimates will see major re-rating

On a 2011 P/E of 4x, it is clear that the market does not believe consensus estimates or is not fully aware of the MCB story. Our forecasts have 2011 credit issued at just over double H210 levels and should be conservative (H210 was up over 20% on H209). Delivery on anything close to that is likely to see the shares re-rate. Our DCF methodology implies a price of 50.6p and Gordon's growth methodology 52.2p.

Price **24.5p**  
Market Cap **£4m**

#### Share price graph



#### Share details

Code MCRB  
Listing AIM  
Sector Financials  
Shares in issue 17.39m

#### Price

52 week High 62.5p Low 10.5p

#### Balance Sheet as at 31 December 2010

Debt/Equity (%) 68%  
NAV per share (c) 46  
Net borrowings (€m) 3.25

#### Business

MCB Finance Group is a leading online provider of short- and medium-term loans to customers in Finland, Estonia, Latvia and Lithuania using the Credit24 brand.

#### Valuation

	2010	2011e	2012e
P/E relative	180%	40%	31%
P/CF	N/A	N/A	N/A
EV/Sales	0.7	0.6	0.6
ROE	2.5%	13%	15%

#### Revenues by geography

UK	Europe	US	Other
0%	100%	0%	0%

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## Investment summary: Storm to following wind

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### Company description: Fenno-Baltic, direct, non-standard lender

MCB is a leading online provider of monthly-repayment, short- and medium-term loans to customers in Finland, Estonia, Latvia and Lithuania using the Credit24 brand. Distribution is through the internet (95% 2010 credit issued) and a partnership with Maxima (c 5%). In 2010 the partnership was solely in Lithuania but was extended to Latvia and Estonia in February 2011. The business model is automated and centralised and so low cost. Credit is assessed centrally using credit score-cards, with data input from both internal and external sources. The average loan is small (€350), ranging from €50 to €2,000 (latter only for existing customers). They are short duration (average five months), with a range of two weeks to 24 months. The customer is typically a mid- to low-income earner with an instant cash need, ie the non-standard market. There are opportunities from economic growth, better product penetration, market share gains, new geographies and new countries. Impairments remain key and managing credit using statistical techniques introduces great sensitivity to customer behaviour and modelling accuracy.

### Valuation: Confidence in estimates will see major re-rating

On our numbers, a DCF model indicates a value of 50.6p and our Gordon's growth model (GGM) indicates 52.2p. Every 1% growth or 1% on COE is worth 2.0-2.5p on the DCF and 5.0-6.0p on the GGM. Our forecasts leave room for upgrades, subject to macro-economic factors and company performance. This would see further valuation upside. We believe the share price trading so far below these measures indicates investors do not believe estimates, let alone management targets, or that they are unaware of the MCB story; it has been under-followed in the past. Delivery on earnings, and the widened communication channels, should address both issues.

### Sensitivities

MCB is sensitive to the economic cycle with both credit cost and revenue (through the appetite to lend) affected. However, the business model is likely to prove much more robust than investor sentiment towards the economies, and despite deep recessions across the Baltics, we note the company only lost money in Latvia. After the 2008/09 economic collapse most forecasters are now predicting average growth of around 3% across MCB's countries which creates favourable conditions for a return to lending and growth. Other sensitivities include:

- **Funding and liquidity:** MCB currently funds itself from a single bank provider.
- **Tax rates:** Specifically the tax deductibility of credit losses.
- **Regulatory issues:** MCB is not a bank but subject to consumer protection rules.
- **Competition:** The main competition is from specialist private lending companies.
- **Currency:** It is unlikely the currency pegs in the Baltics will be changed, but a new country could introduce this risk.

### Financials: Steady growth after the storm

Unsurprisingly, we have based our estimates on consensus economic forecasts (moderate real GDP growth 2011/12, gently falling unemployment), combined with an accelerated appetite to lend by the company especially in Latvia. Some investors will no doubt view this central case as overly optimistic and some will see it as overly pessimistic. We generate growth in the balance sheet of c 24% pa, but as we have also assumed a greater willingness to lend longer term, the churn rate

falls and revenue growth is slower than balance sheet growth. The growth in 12mth+ trade receivables indicates that the appetite to lend longer has already begun. Credit impairments, as a proportion of credit issued, improves further. Geographically we have not assumed any new countries although such a development is highly likely over the next two years. We have not currently assumed any share options will be exercised, as they are well out of the money (most exercise prices in range 41-50p, c 8% dilution if all options fully exercised).

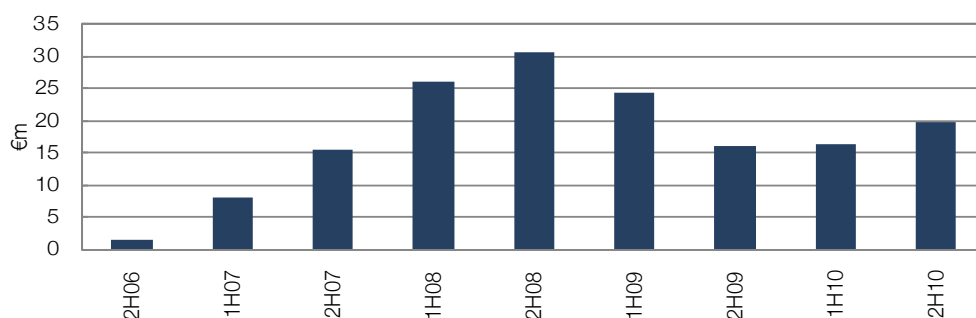
## Company description: Specialist lender in the Fenno-Baltics

### Non-standard, small-denomination, short-duration personal lender

MCB is a leading online provider of monthly-repayment short- and medium-term loans to customers in Finland, Estonia, Latvia and Lithuania using the Credit24 brand. The business started in 2006 and expanded rapidly until the credit crunch; in 2010 it started to expand again.

Distribution is through the internet and a partnership with Maxima, the largest household goods, food and general retailer in the Baltics. The non-exclusive partnership will see Credit24 loans available at the 57 largest Lithuanian stores, 19 in Latvia and seven in Estonia.

#### Exhibit 1: Principal lent



Source: MCB Finance

The business model is highly automated and centralised. Customers use the internet to apply for loans. Credit is assessed centrally using credit score-cards with internal and external data input. The average loan is small and short duration. Around 70% of business is repeat lending to existing customers. The customer is typically a mid- to low-income earner with an instant cash need, ie, the non-standard market.

### Geographically in the Fenno-Baltic region

#### Exhibit 2: Geographic split in 2010

Country	Population m	Principal lent €m	Revenue €m	PBT €m	Impairment - % revenue	Profit % revenue
Finland	5.3	21.3	5.5	2.0	21.9	35.7
Estonia	1.3	5.5	2.3	0.5	20.1	21.7
Latvia	2.3	0.5	0.6	(0.4)	76.5	(74.0)
Lithuania	3.3	8.7	3.4	0.7	20.6	21.1
Central	n/m	0.0	N/A	(2.2)	N/A	N/A
<b>Group</b>	<b>12.2</b>	<b>36.0</b>	<b>11.8</b>	<b>0.6</b>	<b>23.8</b>	<b>4.9</b>

Source: MCB

As can be seen in Exhibit 2 above, Finland is the most important county for MCB, accounting for around a third of revenue, and two-thirds of the country profit and credit issued. Lithuania and Estonia are next, with Latvia by some margin the smallest unit, not least because of the material

losses reported in that country in 2009. This exhibit also shows the consistency across the three main countries, with impairment being around 20% of revenue against a historic figure nearly four times as high in Latvia (most recent lending is much more in line with the other countries).

Normal monthly repayments are collected by invoicing the customer (not direct debit), with the vast majority using internet banking to settle the account. Customer behaviour is such that this billing approach means near-term delinquency is higher than direct collection methods, but it is preferred by customers who value the flexibility it provides. Late payments are pursued by mobile calls/text message on the first day, then with further texts, letters and calls. When an account is over 30 days in arrears, MCB uses external debt collection agencies, believing the specialists in this sphere to be more efficient than an in-house collection team, and provides the service at a variable cost.

### MCB's business churns rapidly

With a current average duration of five months, MCB's business is very much about churn not just the balance sheet. The churn varies between countries with the most rapid turnover in Finland, where external data sources are more limited and so there is less appetite to lend longer term. Historically, it was slowest in Lithuania and Latvia, where there was a competitive market for longer-term loans and more external information is available. Latvia is distorted by the intentional slow down in lending to manage credit risk in 2009 and a competitive environment which has seen massive changes since (allowing much more shorter-term lending and the re-launch of lending in H210).

**Exhibit 3: Churn rates (credit issued/end net receivables)**

	2008	2009	2010	2011e	2012e
Finland	3.4	3.4	3.4	3.3	3.3
Estonia	3.3	3.4	2.9	2.9	2.8
Latvia	2.0	1.8	2.0	2.3	2.3
Lithuania	2.5	3.2	2.4	2.4	2.4
<b>Group</b>	<b>2.8</b>	<b>3.2</b>	<b>3.0</b>	<b>2.9</b>	<b>2.9</b>

Source: MCB, Edison Investment Research

Investors must recognise that having a business with rapid churn heavily distorts some traditional measures. For example, Finnish revenue was 26% of 2010 credit issued against 88% of 2010 end-net receivables. Credit measures are distorted (see Exhibit 4) with the real impairment in Finland, Estonia and Lithuania around 6-8% of credit issued, not the 19-72% reported on end balance sheet numbers. Investors should focus on credit issued rather than the balance sheet measures.

**Exhibit 4: Profitability to balance sheet ratios**

	2008	2009	2010	2011e	2012e		2009	2010	2011e	2012e		2008	2009	2010	2011e	2012e
<b>Revenue as % credit issued</b>						<b>Impairment as % credit issued</b>					<b>Profit as % credit issued</b>					
Finland	22%	27%	26%	26%	26%	Finland	(9%)	(6%)	(6%)	(5%)	Finland	7%	8%	9%	10%	9%
Estonia	24%	45%	42%	42%	42%	Estonia	(22%)	(8%)	(8%)	(8%)	Estonia	5%	3%	9%	10%	10%
Latvia	25%	110%	108%	71%	60%	Latvia	(104%)	(83%)	(20%)	(16%)	Latvia	2%	(33%)	(80%)	6%	8%
Lithuania	22%	41%	39%	40%	39%	Lithuania	(17%)	(8%)	(8%)	(7%)	Lithuania	4%	7%	8%	9%	9%
<b>Revenue as % end net receivables</b>						<b>Impairment as % end net receivables</b>					<b>Profit as % net end receivables</b>					
Finland	74%	90%	88%	88%	86%	Finland	(30%)	(19%)	(19%)	(17%)	Finland	25%	26%	31%	32%	31%
Estonia	78%	153%	124%	122%	118%	Estonia	(58%)	(66%)	(61%)	(59%)	Estonia	18%	9%	27%	29%	27%
Latvia	50%	200%	212%	167%	136%	Latvia	(189%)	(163%)	(47%)	(36%)	Latvia	3%	(60%)	(157%)	13%	18%
Lithuania	55%	129%	93%	94%	91%	Lithuania	(53%)	(19%)	(18%)	(16%)	Lithuania	11%	21%	20%	21%	21%

Source: MCB, Edison Investment Research

### Strategy: Leverage infrastructure when economic conditions allow

Having spent five years building the business, managing it through economic crisis and continually refining processes and procedures, MCB can expand in organic lending, new geographies, enhanced distribution channels and, potentially, new products. The vast majority of this can be accommodated on the existing, scalable platforms.

## Revenue streams

MCB charges a fee for each loan, which is priced at the average cost of providing the loan. MCB charges competitive interest rates over the life of the loan. Fees are also charged for early redemption, late payments, reminder letters, etc. Under IAS accounting, all these income streams are amortised over the loan. As can be seen in Exhibit 4, revenue as a percentage of credit issued ranges from high 20s to mid 40s (Latvia being an exception), so for a €350 average loan, the customer pays back in total c €440 in Finland and c €490 in Estonia and Lithuania.

## UK listing

The board decided to raise €5m with an AIM listing in 2007, choosing the UK because the rigour and requirements of UK market were perceived to enhance the Estonian holding company's reputation and credibility. A secondary issue followed in 2008.

## Management

The board is heavily skewed to entrepreneurs involved in venture capital, especially in technology. Consequently, we believe that its skill base is strong in managing new business and marketing to cross-border, mass market customer bases exploiting the latest technologies. Short-term cash loans are a relatively new product, having only really started in 2005. The MCB team is more experienced than average, having been in the market from the start, and, after weathering the storm of 2008/9, they have seen credit-scoring models stress-tested. Supplementing this hard-won internal expertise, the company uses external advisers extensively. However, we believe some investors would be more comfortable if the board also included someone with wider and longer credit experience perhaps covering a couple of economic cycles.

We note that directors have been strong buyers of the shares. Their interests are aligned to shareholders.

## Growth opportunities

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**In addition to economic growth and improving product penetration, MCB has company-specific growth from new geographies, new distribution agreements, and new products. Growth from existing markets and entering new geographies appears to us the most likely.**

## Economic growth

As can be seen from the IMF forecasts in Exhibit 5, GDP fell massively across MCB countries in 2009. This is expected to be replaced by moderate growth for 2011. The expectation remains for growth well below the boom years of 2006/07, but is enough to expect unemployment to fall across the region. Investors will no doubt have their own views about the accuracy of these forecasts, but assuming they are correct, credit risk should improve along with the economy and also allow for greater revenue opportunities.

**Exhibit 5: Economic forecasts (%)**

Country			Real	GDP	Unemployment				
	2006	2007	2008	2009	2010e	2011e	2009	2010	2011
Finland	4.9	4.2	1.0	(8.0)	2.4	2.0	8.3	8.8	8.7
Estonia	10.0	7.2	(3.6)	(13.9)	1.8	3.5	13.8	17.5	16.4
Latvia	12.2	10.0	(4.6)	(18.0)	(1.0)	3.3	17.3	19.8	17.5
Lithuania	7.8	8.9	3.9	(14.8)	1.3	3.1	13.7	18.0	16.0

Source: IMF, Table 2.3, p94 World Economic Outlook, October 2010, IMF European regional outlook 2009 Table 1

## Improving penetration in existing countries

MCB's below-prime, short-term lending is a relatively new product in Fenno-Baltic region. The company believes it could be attractive to 20-30% of the population from time to time, although clearly not all would be borrowing at the same time. If this assumption is correct, the potential market is significant most notably in Latvia and Lithuania. MCB can incrementally take market share.

## New geographies

MCB pays MC Global a licence fee for the perpetual, exclusive and irrevocable right to use the Credit 24 brand across a number of countries in addition to those mentioned above. The list includes Czech Republic, Slovakia, Hungary, Poland, Romania, Slovenia, Croatia, Serbia, Macedonia, Montenegro, Bosnia, Albania, Kosovo, Bulgaria, Moldova, Ukraine and Belarus. We would expect MCB to expand into one of these countries next, more probably in Central Europe rather than the Balkans. Incremental costs should be modest, primarily marketing, as the infrastructure is already in place and local fixed costs minor. The rapid growth seen by the company in 2008 was partially due to geographic expansion. We have not built any new geographies into our forecasts for, though such growth is likely, the visibility of the effect on estimates is too poor at this stage.

## Expand distribution lines

As outlined above, MCB has a distribution agreement with Maxima which currently generates around 20-25% of the Lithuanian credit issued (c 5% group). This is being expanded across Estonia and Latvia. MCB is also re-launching its lending through the Latvian post office. With a well-recognised brand in Credit24, MCB makes an attractive partner for retailers wanting to offer their customers on-the-spot finance (typically the funds are in the customer's account within 15 minutes).

## New products

We believe management is looking at expanding into product areas which are closely aligned to the existing business. In particular small scale, short-term point of sale finance has many characteristics which are similar to the internet, low cost model of MCB.

## Credit

In addition to economic risk, credit losses will also be driven by whether good or bad lending decisions are made. Most credit officers are taught the "canons of lending", sometimes shortened to CAMPARI and ICE. MCB is an online lender, a common delivery channel in the Fenno-Baltic region, and adopts the standard statistical modelling typical to this type of business.

**Exhibit 6: Canons of lending**

CANON		MCB Approach
Character	Can customer be trusted	Statistical modelling
Ability	Is customer financially aware	Statistical modelling
Means	What are customer means	Statistical modelling
Purpose	What is loan wanted for	Market analysis not customer specific
Amount	Is amount appropriate	Smaller loans for newer customers
Repayment	How will repayment be made	Shorter loans for newer customers, statistical modelling
Insurance	Any security taken	Not applicable to unsecured lending
<b>&amp;</b>		
Interest	What rate should be charged	MCB does not currently use risk adjusted pricing
Charges	Any extra fees	Including new loan fees / early redemption charges etc
Extras	Any other sources of revenue	Possible but hard on direct approach

Source: Edison Investment Research

**MCB's approach**

The most important is character and whether the customer will actually make a repayment when they have the ability to. Some lenders, such as Provident Financial or International Personal Finance, use agents who live in the community in which they are lending, and who know the customers, often on a very personal basis. This can be especially useful where the borrower (often the matriarch) may not be the main earner in the household. The weakness of that approach is that it opens the agent to personal bias, the risk of which increases the closer the agent is to the borrower. One major advantage of statistical modelling, including behavioural analysis, and the MCB approach is that it reduces the risk of bias. Such modelling also means that loan applications are processed automatically thus reducing administration expenses.

The statistical models MCB uses have a wide range of inputs. In the Baltic countries this includes market-wide central databases, utility company and tax authority data, although in Finland the latter two are not available. All customers have a bank account (penetration rates are very high across the region), which provides both a means of confirming customer identity and an inherent credit check. The former is important to limiting identity-theft fraud losses. In addition to this third-party data, MCB has been developing its own dataset off its own clients' behaviour. The analyses try to identify behavioural patterns as well as trends across the database. There is clearly no competitive advantage in the external data, although being one of the largest players in the market creates a better internal database than peers.

MCB's experience, ex-Latvia, has been for c 15% of accounts to move into over 30-day delinquency. To put this into perspective, this is only modestly above the level Barclays reported that in its mainly prime card books (one month + arrears of 3.4% in the UK and 4.6% in the US) and more than compensated for by revenue. When an account is 30 days in arrears, MCB uses external debt collectors and typically recovers 50-70% of the principal outstanding. The expected loss is thus c 6-7% of credit issued or 25-30% impairment loss as percentage of revenue (the same as International Personal Finance's target range of loss).

MCB actively manages risk. New customers are offered smaller loans over a shorter duration and every new customer in the Baltics receives a call both to welcome them to the business and verify their application. Once a repayment record is established, MCB will lend larger sums over longer periods. It will not lend to customers with negative credit histories – its customers may be non-

standard but they are not bad credits. MCB does not automatically re-finance or extend delinquent loans; it only does so as part of an active negotiation with customers in arrears. Management information means credit performances across the portfolio are monitored daily, allowing for any problem concentrations to be rapidly addressed. The automated model also trades a certain degree of risk against the cost, potential impact on revenue, and complexity of requiring too much input from customers.

Statistical modelling has its weaknesses. Dozens of PhD mathematicians, a hundred years of internal data and excellent external data did not save HSBC Finance Corporation (mainly Household) from massive losses in 2007. Modelling is reliant on historic data, which creates incremental risks: These are mitigated by MCB as follows: 1) Inaccurate data. MCB uses a wide range of customer, internal and external data (the sources are detailed above). 2) Inaccurate modelling, especially with changes of customer behaviour. MCB limits this risk with short-duration loans, although in extreme situations, it may choose to limit lending to establish new credit scores and this may affect revenue. In normal conditions, MCB is continually reviewing and upgrading its credit scoring system, without having a dramatic impact on income. 3) Over-confidence. We believe that, ahead of the credit crisis, many lenders in the US relied excessively on what computer modelling told them. MCB seems to be taking a cautious approach to credit, but this remains an area to monitor.

While we may believe that investors would be more comfortable if MCB enquired deeper into the purpose of the loan (the risk on debt consolidation is different from, say, emergency car repairs), we recognise that extending the application form risks alienating new clients and undermining revenue. Customers may not accurately respond as MCB cannot verify their answers. Similarly risk-adjusted pricing creates opportunities for revenue optimisation but increases the cost and complexity of the offering.

### **What went wrong in Latvia and what has changed as a result?**

Latvia generated a markedly different financial performance and was the only country to report a loss through the crisis (2009 loss €868k, 2010 loss €421k). The 2009 loss was driven by impairments (94.5% of revenue, 104% credit issued), while 2010 was more about slowing lending in the uncertain environment and reducing revenue (credit issued: 2010 €0.5m, 2009 €2.9m; revenue 2010 €0.5m, 2009 €2.6m).

We believe part of the Latvian losses arose because it had the weakest economy (18% reduction in real GDP in 2009 see Exhibit 5), although we note the other Baltic countries were not far behind. An additional factor causing bad debts was the longer average duration of lending (see Exhibit 3 on churn). We believe this was partly competition driven, and partly because there was an over-confidence in the modelling, driven by the relatively large amounts of external data available in that country. The latter may have led to the manual rules being too relaxed. We note the issues were country specific, that recoveries have been more than the total amount lent (and so losses related to lost revenue not principal) and that all the other countries remained profitable.

The Latvian losses should now be history and we believe investors should look to the valuable lessons that have been learned from the manageable cumulative losses (€1.2m, or just over 20% of one year's group administration expenses). The models today are markedly different from the past. There is much more external data, a longer internal track record and more behavioural analysis used in the calculations. In addition to better input and algorithms, there is greater

precedence given to over-riding rules (such as the maximum loan size a new borrower can take, acceptable duration etc). The initial results from the re-launch of lending in Latvia are encouraging and group-wide credit is the lowest proportion of revenue since the company was founded.

We believe the lessons learned in Latvia will be especially important as MCB moves to new countries, where the roll-out is likely to be more controlled than it may otherwise have been (so not dissimilar to the piloting approach IPF uses to explore new geographies).

## Sensitivities

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MCB is sensitive to the economic cycle with both credit cost and revenue (through the appetite to lend) affected. We believe though that the business model is likely to prove more robust than investor sentiment towards the economies, and we note the company only lost money in Latvia. After the deep recession of 2008/09 most forecasters are now predicting average growth of around 3% across MCB's countries, which creates favourable conditions for a return to lending and growth. Other sensitivities include:

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## Macroeconomic growth

Unexpected unemployment/under-employment is the biggest source of credit loss and MCB is exposed to this. If the expected growth in Fenno-Baltic region is not delivered, results will be below forecasts. There is similar upside if growth is above forecast. We believe investor reaction to macro-economic news, and so the share price, is likely to be much more volatile than the business results themselves. MCB faces the same sensitivity and reaction as Provident Financial and IPF.

## Funding and liquidity

MCB has historically been financed by a one-year facility from one bank (Rietumu Bank) rolled over annually. Rietumu is one of the Baltics' largest corporate banks and had an end-2010 capital adequacy ratio of 17.3% and a liquidity ratio of 58%, both around twice regulatory requirements. Rietumu is in a position to continue the facility, and it was recently extended to 31 March 2012 at an increased level of €12m (from €10m). Rietumu has the right to exercise options (at 45p) which, if done, would roll the facility over to March 2013. We believe MCB will widen and diversify its funding sources over time, and we believe investors will welcome such a move.

## Tax rates and geographic split of profits

Forecasting MCB's earnings will always be complicated by where it generates its profits and the tax rates in that country, prior-year negotiations and taxable losses carried forward. We note:

- Profits in Finland, Lithuania and Estonia cannot be offset against the losses in Latvia.
- In Lithuania most bad debts are not immediately allowable for tax purposes, so the tax charge for that country is very high in 2009 when credit losses were high.
- In Latvia not all bad debts are allowable for tax purposes.

Overall we believe a blended group tax rate of c 30% is not unreasonable, but it will be volatile.

## Currency risk

All the countries are either using euros, are pegged to the euro or float in a tight band: Finland (euro), Latvian lats (floats around 1% of LVL0.702804/€, planned for euro in 2014), Lithuanian litas pegged at LTL3.4528/€, planned for euro on 1 January 2014) and Estonian (euro from 2011). If any of these pegs/fixed floats were broken, or a new country entered, there could be a risk, although MCB has a clause requiring customers to repay in euros. In addition, MCB shares are quoted in sterling, and so some valuation comparisons and investors are rate sensitive.

## Regulation

MCB is not a bank (no retail deposits), so it falls under consumer protection and disclosure regulations in each country, as well as data protection, eg the new Lithuanian maximum APR (250%) whose effect we do not expect to be material. This limits compliance costs and means that MCB and its competitors do not have material government regulation and intervention.

## Competition

MCB's direct competitors are small private companies, not big institutions. In some markets such as Latvia there was historically competitive pressure for longer average loans, which we believe was a factor in Latvia reporting a loss in 2009. Pressure to lend long-term in Latvia has gone, but there is intense competition in all markets which management believes is addressed by a good product range, service and brand.

## Related parties

MCB discloses related party transactions (note 19 of 2009 Annual Report and Accounts). Out of group administration expenses of c €5m, MCB paid over €250k to MC Global (owned by the founder of MCB and still a 46% shareholder, although not on the board) for the perpetual, exclusive and irrevocable right to use the Credit 24 brand. In addition, there are services where the company advises that the staff ownership in the related entities is small, and all transactions are at market rates.

## Valuation

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Given the global economic uncertainties, we believe it is appropriate to be conservative in our forecasts, especially beyond 2011. We believe management's assessment will generate higher earnings than we are forecasting, and that this would naturally be reflected in a (materially) higher valuation. Over time, assuming market conditions stabilise, we believe we have left room to upgrade our estimates and so the valuation.

On our numbers, a DCF model indicates a value of 50.6p and our Gordon's growth model (GGM) indicates 52.2p. Every 1% growth or 1% on COE is worth 2.0-2.5p on the DCF and 5-6p on the GGM. We believe the share price trading so far below these measures indicates investors do not believe estimates, let alone management targets, or that they are unaware of the MCB story because it has been under-followed in the past. Delivery on earnings and the widened communication channels management have opened should address both issues.

## Peer group comparisons

None of the direct competitors in the Fenno-Baltic region are directly quoted. International Personal Finance (2011e consensus P/E 10.7x) is the closest comparator, although its operations are more

central Europe and Mexico and it is an agent-distribution model. As a UK-listed name, MCB could also be compared with Provident Financial (2011e 11.3x), S&U (10x) and Cash Converters (7.0x, dual listing in Australia and UK), although the underlying businesses are different. MCB is trading at c two-thirds of book value, while IPF is at 2.6x book and Provident Financial 4.1x.

## Discounted cash flow model 50.6p

Our DCF model assumptions are company-specific, forecast to 2012, 8% compound growth for 10 years and a 10x multiple applied for the terminal cash flow. Discounting these cash flows by 15% per year generates a value of 50.6p, of which just 24% is in the terminal value.

## Gordon's growth model 52.2p

Assuming long-term RoE of 20% (2012 forecast 15% and conservatively below the level seen by PFG [c 30%]/IPF [c 22%]), growth of 8% and a 15% CoE generates a P/BV value of 1.7x. Applying this to the end 2010 BV per share (46.2c) indicates 79c, which we then discount by 20% to reflect the fact that near-term returns are below long-term, sustainable returns; value 63c (converting at €1.163/£ = 52.2p).

## Financials

We have used consensus economic forecasts and an accelerated appetite to lend especially in Latvia and forecast balance sheet growth of 24% in 2011, but with slightly longer lending, revenue growth is a little less. Our numbers are conservative with credit issued being just over double the H210 amount (H210 was over 20% above both H110 and H209). Credit quality improves modestly. Geographically, we have not assumed any new countries, which would accelerate top-line growth though initially dilutive to earnings. With all the share options currently well out of the money, we have not assumed they will be exercised (c 8% EPS dilution if they all were).

### Exhibit 7: Profit and loss (€'000s)

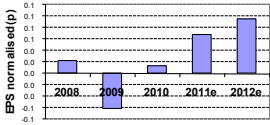
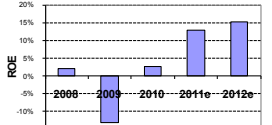
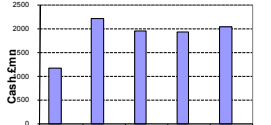
€'000s	2007	2008	2009	2010	2011e	2012e
Year end 31 December						
<b>PROFIT &amp; LOSS</b>						
<b>Revenue (net of financing cost)</b>	<b>3,818</b>	<b>12,071</b>	<b>14,346</b>	<b>11,058</b>	<b>13,475</b>	<b>15,825</b>
Cost of Sales (exc amortisation and depreciation)	(5,423)	(7,777)	(7,135)	(7,662)	(8,816)	(10,163)
Credit losses	(1,387)	(4,030)	(7,764)	(2,805)	(3,050)	(3,350)
<b>EBITDA</b>	<b>(2,991)</b>	<b>264</b>	<b>(553)</b>	<b>591</b>	<b>1,609</b>	<b>2,112</b>
Depreciation	(11)	(38)	(45)	(21)	(23)	(26)
Amortisation	(74)	(16)	(20)	(36)	(36)	(36)
<b>Operating profit (pre exceptional)</b>	<b>(3,076)</b>	<b>209</b>	<b>(619)</b>	<b>534</b>	<b>1,550</b>	<b>2,050</b>
<b>Profit Before Tax (FRS 3)</b>	<b>(3,076)</b>	<b>209</b>	<b>(619)</b>	<b>534</b>	<b>1,550</b>	<b>2,050</b>
<b>Profit Before Tax (pro forma)</b>	<b>(2,743)</b>	<b>487</b>	<b>(634)</b>	<b>577</b>	<b>1,675</b>	<b>2,275</b>
Tax	(82)	(422)	(343)	(500)	(600)	0
<b>Profit After Tax (FRS 3)</b>	<b>(3,076)</b>	<b>127</b>	<b>(1,041)</b>	<b>191</b>	<b>1,050</b>	<b>1,450</b>
<b>Profit After Tax (pro forma)</b>	<b>(2,743)</b>	<b>405</b>	<b>(1,056)</b>	<b>234</b>	<b>1,175</b>	<b>1,675</b>
Average Number of Shares Outstanding (m)	17.4	17.4	17.4	17.4	17.4	17.4
<b>EPS - normalised (c)</b>	<b>(15.77)</b>	<b>2.33</b>	<b>(6.07)</b>	<b>1.34</b>	<b>6.76</b>	<b>9.63</b>
<b>EPS - FRS3 (c)</b>	<b>(17.7)</b>	<b>0.73</b>	<b>(5.98)</b>	<b>1.10</b>	<b>6.04</b>	<b>8.34</b>
Dividend per share (c)	0.00	0.00	0.00	0.00	0.00	0.00
EBITDA Margin (%)	(78.3%)	2.2%	(3.9%)	5.3%	11.9%	13.5%
Operating Margin (before GW and except.) (%)	(80.6%)	1.7%	(4.3%)	4.8%	11.5%	13.1%

Source: MCB, Edison Investment Research

### Exhibit 8: Balance sheet (€'000s)

	2007	2008	2009	2010	2011e	2012e
<b>Fixed Assets</b>	<b>829</b>	<b>984</b>	<b>828</b>	<b>1,318</b>	<b>848</b>	<b>851</b>
<b>Current Assets</b>	<b>8,694</b>	<b>22,081</b>	<b>15,179</b>	<b>13,826</b>	<b>16,650</b>	<b>19,900</b>
<b>Total Assets</b>	<b>9,523</b>	<b>23,065</b>	<b>16,007</b>	<b>15,144</b>	<b>17,497</b>	<b>20,751</b>
<b>Current Liabilities</b>	<b>(6,258)</b>	<b>(2,493)</b>	<b>(8,541)</b>	<b>(7,444)</b>	<b>(8,747)</b>	<b>(10,551)</b>
Long term Liabilities	0	(12,050)	0	0	0	0
<b>Net Assets</b>	<b>3,265</b>	<b>8,523</b>	<b>7,467</b>	<b>7,700</b>	<b>8,750</b>	<b>10,200</b>
<b>CASH FLOW</b>						
<b>Operating Cash Flow</b>	<b>(8,303)</b>	<b>(11,680)</b>	<b>6,665</b>	<b>1,084</b>	<b>(1,336)</b>	<b>(1,256)</b>
Net cash from investing activities	(105)	(98)	(23)	(89)	(25)	(25)
Net cash from (used in) financing	8,640	12,435	(5,590)	(1,260)	(100)	(1,300)
<b>Net Cash Flow</b>	<b>233</b>	<b>657</b>	<b>1,052</b>	<b>(265)</b>	<b>(1,461)</b>	<b>(2,581)</b>
Opening cash	274	506	1,163	2,214	1,950	750
<b>Closing net (debt)/cash</b>	<b>506</b>	<b>1,163</b>	<b>2,214</b>	<b>1,950</b>	<b>750</b>	<b>500</b>

Source: MCB, Edison Investment Research

Growth	Profitability	Balance sheet strength	Sensitivities evaluation	
			Litigation/regulatory	◐
			GDP growth / unemployment	●
			Currency	○
			Stock overhang	○
			Interest rates	◐
			Oil/commodity prices	○

Growth metrics	%	Profitability metrics	%	Balance sheet metrics	Company details
EPS CAGR 08-12e	43	Impairment as % rev	25	Gearing 2010	68%
EPS CAGR 10-12e	168	Cost as % revenue	70	Interest cover 2010	1.8x
EBITDA CAGR 08-12e	30	ROE 10	2.5%	CA/CL 2010	1.9x
EBITDA CAGR 10-12e	66	Gross margin 10	2	Stock turn 2010	n/m
Rev CAGR 08-12e	7	EBITDA margin 10	11	Debtor days 2010	n/m
Rev CAGR 10-12e	21	Gr mgn / Op mgn 10	6.9	Creditor days 2010	32
				Address:	
				Lootsa 8 Tallinn 11415 Estonia	
				Phone	+358 9 4259 7644
				www.mcbfinance.com	

Principal shareholders (31.12.2010)	%	Management team
MC Global Limited	45.9	<b>CEO: Rami Ryhänen</b>
IIU Nominees Limited	10.7	Mr Ryhänen has been CEO since MCB's inception in 2005. Previously he was CEO of Jippii Mobile Entertainment Oy, CEO of Small Planet Limited and customer relationship director of Sonera Oyj. Mr Ryhänen has an MBA from the Institute for International Management Centers.
Orient Equity Partners (subsequently raised to 9.6%)	8.5	
Henry Nilert (FD)	7.0	
Europanel AB	4.3	
P Lorange	3.8	
Hansa Eastern European Equity Fund	3.1	<b>CFO: Henry Nilert</b>
		Mr Nilert joined the company as CFO in March 2006 before which he was a partner of Crystal Capital Partners LLP, a private equity advisory firm based in London. Previously he co-founded iobox, a wireless software company. Mr Nilert worked in investment banking in London, New York and Helsinki.
Forthcoming announcements/catalysts	Date *	Chairman: Dr Anton Mayr
AGM	Mid May	Dr Mayr is the founder and managing director of Stratos Ventures Inc, a US venture development company and of its Finnish early stage venture capital fund. He was a founder of an early-stage research-focused biomedical company and was an investment manager at Citicorp Venture Capital. He holds doctorate in law from Salzburg, an LLM from McGeorge School of Law and an MBA from Columbia Business School.
Trading update	End June	
Interim results	Early September	
<i>Note: * = estimated</i>		
Companies named in this report		
International Personal Finance, Provident Financial, S&U, Cash Converters, Barclays		

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