INVESTMENT AND SOVEREIGN RESEARCH May 2, 2022

Victoria Mutual Investments Limited

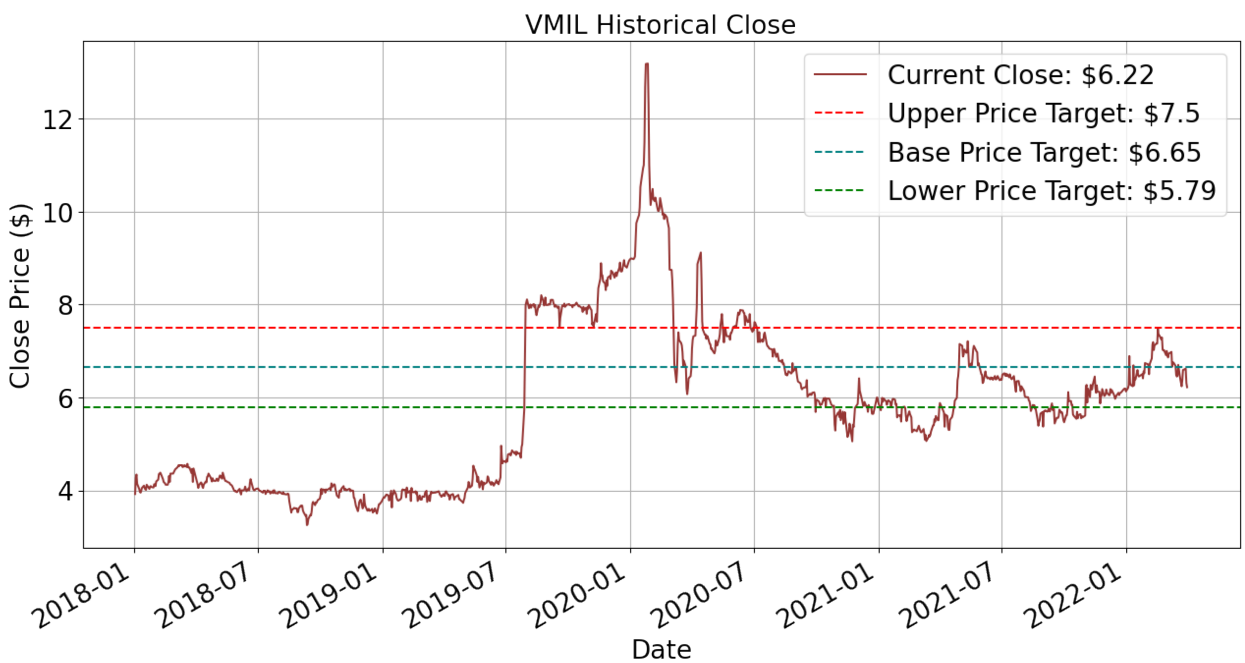
PLEASE SEE IMPORTANT DISCLOSURES & COPYRIGHT INFRINGEMENT IN THE APPENDIX

Executive Summary

Victoria Mutual Investments Limited (VMIL) was incorporated in 1984. The Company has a wholly-owned subsidiary Victoria Mutual Wealth Management Limited (VMWM), which was established in 1994. The primary activities of VMWM are investment brokering, advisory services and money market dealing. Meanwhile, VMIL offers margin loans, insurance premium financing, lease financing, underwriting services, and corporate loans. VMIL was listed on the Jamaica Stock Exchange on December 29, 2017.

At the end of the period under review (FY 2017 to FY 2021), Gain from Investment Activities and Net Fees and Commissions income are the primary sources of revenue, accounting for 38.4% and 41.1%, respectively. Meanwhile, Net Revenue and Profits have increased at a CAGR of 20.3% and 13%, respectively.

VMIL currently trades at approximately 16.8x, its trailing 12-months EPS above the 13.8x harmonic mean of the peer group. Meanwhile, VMIL has relatively low liquidity, exchanging an average daily volume of 102.4 thousand units over the past year, valued at approximately $651.4 thousand. Over the past month, VMIL has had an average bid-ask spread of about 3.5%, indicating a relatively high implicit cost to acquire shares.



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Recent Developments

For the 4th quarter ended December 2021, VMIL recorded a loss of $48.2 million primarily due to an 84.1% decline in gain from investment activities to $64 million. Furthermore, net fees and commission income fell 46.4% to $102.1 million.

Meanwhile, VMIL seeks to raise up to $3 billion via issuing two tranches of bonds. The bonds are unsecured and offer interest rates of 6.5% and 6.75% on JMD for 18 and 24 months. This represents the second debt issuance in 6 months. If fully taken up, this would significantly increase the Company's borrowings from $5.5 billion recorded at the end of FY 2021.

Additionally, the Company is expanding its regional footprint with a confirmed agreement to acquire Republic Funds Barbados Incorporation.

Key Financial Data

	YE 2017	YE 2018	YE 2019	YE 2020	YE 2021	CAGR
BVPS	2.11	1.81	2.85	2.89	2.67	6.09%
EPS	0.29	0.27	0.40	0.29	0.38	6.71%
Dividend Per Share	0.32	0.14	0.19	0.03	0.16	-16.35%
Stock Price	3.24	3.75	9.00	6.00	6.15	17.38%
Main Market Index	288,382	379,791	509,916	395,615	396,156	8.26%
Abridged Income Statement (in Millions)						
Net Interest Income	246.99	250.08	260.38	289.62	390.46	12.13%
Gain on Investment Activities	193.08	213.88	485.90	593.99	776.15	41.60%
Net Fees and Commission Income	500.16	838.27	933.13	925.32	832.09	13.57%
Operating Revenue	966.46	1,306.78	1,682.96	1,875.59	2,023.53	20.29%
Operating Costs	498.63	767.74	881.40	1,240.71	1,197.93	24.50%
Pre-Tax Profits	467.83	539.04	786.23	598.87	792.36	14.08%
Profits	346.30	397.60	598.05	433.59	564.14	12.98%
Corporate advisory services	316.54	614.48	528.34	499.38	304.20	-0.99%
Abridged Balance Sheet (in Millions)						
Investment Securities	11,683.64	13,241.36	16,718.18	16,526.04	20,665.88	15.32%
Earning Assets	15,055.05	17,458.50	20,655.46	23,906.72	24,717.21	13.20%
Total Assets	20,068.45	21,610.20	25,327.70	29,723.68	31,243.15	11.70%
Equity	2,534.02	2,722.42	4,276.83	4,331.47	4,001.20	12.10%
Repo Liabilities	13,164.96	15,454.98	16,999.39	20,312.83	19,649.27	10.53%
Borrowings	506.11	1,410.63	2,410.63	3,042.64	5,521.96	81.74%
Total Liabilities	17,484.43	18,837.78	21,000.87	25,342.20	27,391.95	11.88%
Ratios						**Average**
Efficiency Ratio	-	-	-	-	-	0.00%
Net Profit Margin	35.83%	30.43%	35.54%	23.12%	27.88%	30.56%
Debt/Equity	0.20	0.52	0.56	0.70	1.38	0.67
Financial Leverage	8.86	7.93	6.71	6.40	7.32	7.44
Dividend Yield	0.00%	3.50%	3.26%	0.41%	2.60%	1.95%
Dividend Payout Ratio	109.1%	52.8%	47.7%	10.4%	41.2%	52.24%
P/E	11.17	14.15	22.57	20.76	16.35	17.00
P/B	-	2.07	3.16	2.08	2.31	192.13%
ROE	0.00%	15.13%	17.09%	10.07%	13.54%	11.17%
ROA	0.00%	1.91%	2.55%	1.58%	1.85%	1.58%

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Financial Overview

Income Statement Review (FY 2017 – FY 2021)

Net revenue for VMIL increased 7.9% to $2.02 billion in FY 2021, with two of its three primary revenue sources increasing. The primary revenue sources are Net Interest Income, Gains from Investment Activities and Net Fees & Commissions.

Net Interest Income increased 34.8% in FY 2021 to $390.5 million. It was driven primarily by a 31.4% increase in interest income from investment securities to $833.4 million. Meanwhile, interest expense only increased 17.5% to $767.4 million. The primary contributors to rising costs are associated with repurchase agreements and loans and borrowings, which amounted to $563 million and $196.2 million, respectively.

Gain on investment activities increased by 30.7% in FY 2021 to $776.2 million, but growth slowed below the CAGR of 41.60% over the last five years. The strong performance of the equity portfolio drove a **gain on investment activities in 2021. The equity portfolio recorded an increase of $171.5 million versus a loss of $51.1 million in 2020**. Quoted equities accounted for in the income statement ranging from $340.9 million in FY 2020 to $574.7 million in FY 2021, and the Main Market only increased 0.14% in FY 2021. Therefore the performance of the equity portfolio was impressive.

Net Fee and Commission income fell 10.1% to $832.1 million in FY 2021 due to revenue from Corporate advisory services declining 39.1% in FY 2021 to $304.2 million. This revenue source has been on a steady descent since its peak of $614.5 million in FY 2018. Meanwhile, fees from unit trust funds only increased 6.5% in FY 2021 to $334.9 million to become the primary contributor to net fees and commissions income. However, the growth was well below the CAGR of 56.4% over the period. Furthermore, funds managed on a non-recourse basis only increased 5.76% to $34.71 billion, indicating slowing growth at a critical strategic and stable revenue source.

Ultimately, Net Revenue increased by 20.3%, driven primarily by growth in the Gains from investment activities. Meanwhile, operating costs fell 3.5% in FY 2021 to $1.2 billion due to only provisioning for credit loss of $4.9 million versus $119.3 million in FY 2020, resulting in profit surging 30.1% in FY 2021 to $564.1 million. However, profits still lag the $598.1 million recorded in FY 2019. However, it should be noted that FY 2019 profit was boosted by a write-back of $96 million in credit losses.

Balance Sheet Review (FY 2017 – FY 2021)

Total assets increased 5.1% to $31.2 billion, mainly due to growth in investment securities and loans receivable; however, resale agreements curtailed total assets growth. The primary asset is investment securities, which increased 25.1% in FY 2021, outpacing the 15.3% CAGR for the period under review. The growth in investment securities is primarily due to investment in GOJ securities, which increased by 11.7% to $14.1 billion, and a $1.1 billion investment in a JMD Corporate bond.

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Shareholder equity declined by 7.8% or $330.3 million to $4.05 billion due to a $668.90 million decrease in investment revaluation reserves due to the decline in investment securities held. The primary liability is repo liabilities, which declined 3.3% in FY 2021 to $19.6 billion and currently account for 62.9% of total assets.

The most substantial liability on VMIL's balance sheet is repurchase agreements (repos); at the end of FY 2021, it accounted for $19.6 billion or 62.9% of total assets. Another significant liability is borrowings which surged under the review period, increasing 81.5% in FY 2021 to $5.5 billion. The primary source of borrowings is fixed and variable unsecured bonds valued at $4.2 billion. Of these notes, $2.3 billion fixed at 5.5% is due to mature on January 16, 2023. Meanwhile, $730.6 million fixed at 5.5% is expected to mature in April 2023.

Proceeds from loans in FY 2021 were $2.5 billion, up 295.5% over the same period last year. FY 2021 saw the highest inflow from loans under the review period, far exceeding the $1 billion recorded in FY 2019. Meanwhile, Dividends increased to $232.5 million, up from $45 million in FY 2020 but down from the $285.1 million paid in FY 2019.

Ratios (FY 2017 – FY 2021)

VMIL's efficiency ratio has been trending higher for the period under review, primarily due to growth in expenses outpacing revenue growth. However, FY 2021 saw a marginal improvement in the efficiency ratio to 59%.

Meanwhile, borrowings have surged during the review period resulting in debt to equity swelling 96% to 1.4x. However, financial leverage is 7.3x, well below the peak of 8.9x in FY 2017. Therefore, while financial leverage is up from FY 2020, it remains within the Company's normal range.

Forecast and Valuation

We view VMIL peers as companies operating primarily in the Diversified Financial Services and Capital Markets sector.

We used our projection of VMIL's FY 2021 BVPS and then applied the harmonic P/B multiple of peers (adjusted for historical differences) to arrive at our price target of $6.65. The assumption that investor sentiment towards VMIL's peer group remains relatively stable is fundamental to our price target. Below is a chart illustrating the relationship between VMIL's P/B ratio and its peer group average over the last three years. **We used the 80th and 20th percentile of P/B multiple difference to derive the upper and lower price targets of $7.50 and $5.79, respectively.**

Chart 1 below indicates that VMIL's P/B is trading close to the average P/B premium of 84.4%. The Company's current P/B premium indicates limited upside potential, given that it's close to the historical average.

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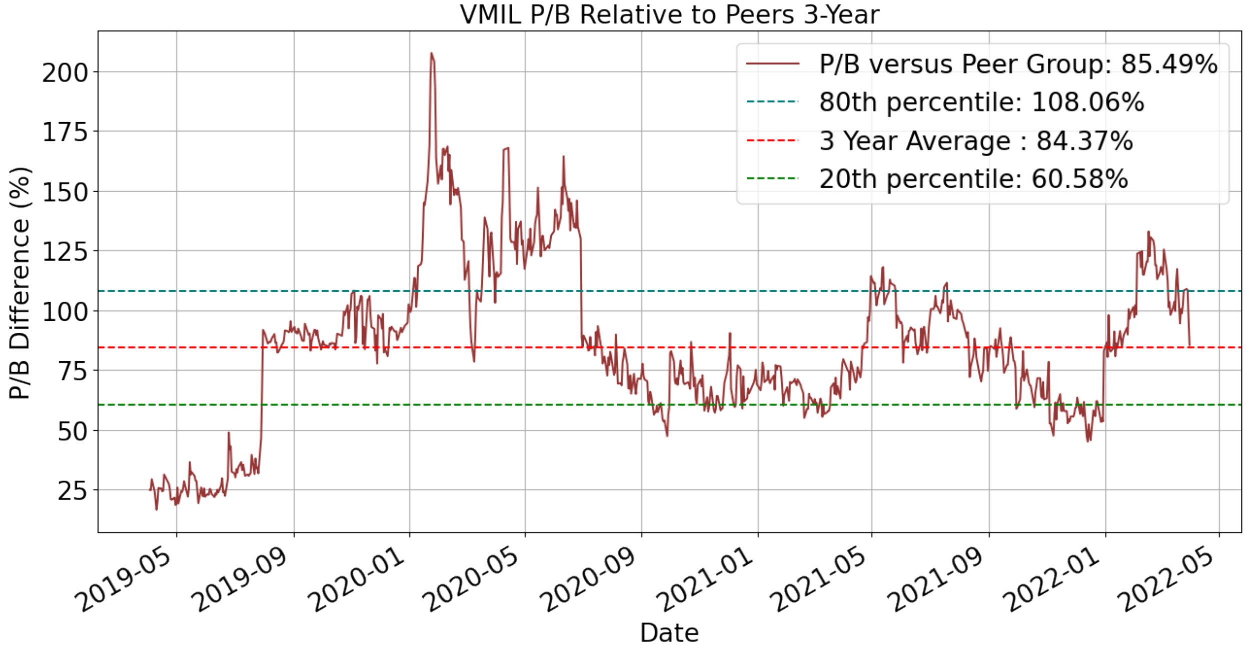
Chart 1.



	Price Target	Implied Upside/(Downside)
Upper	7.50	20.58%
Base	6.65	6.91%
Lower	5.79	-6.91%

Meanwhile, VMIL's P/E and P/B ratios exceed peers except for BIL, but its ROA is below the peer group mean. VMIL's superior ROE relative to peers may explain its relatively high multiples. However, it should be noted that higher levels of financial leverage aid VMIL's superior ROE. In comparison, PROVEN, MIL and BIL had financial leverage of 4.7x, 2.9x and 2.5x, respectively, at the end of their most recent reports.

Consumer Finance & Capital Markets Group					
Ticker	**Market Cap($B)**	**P/E**	**P/B**	**ROA**	**ROE**
BIL	113.53	24.90	3.04	5.14%	12.74%
MIL	8.88	10.77	0.67	2.46%	7.09%
PROVEN	27.19	10.34	1.07	2.18%	10.19%
VMIL	9.33	16.54	2.33	1.85%	13.54%
Mean	39.73	13.78	1.26	2.91%	10.89%

Outlook

In the long term, we have a neutral outlook on VMIL. However, we expect a marginal decline in earnings in the near term. In VMIL's favour, we expect growth to continue for its funds under management on a non-recourse basis, which aids the growth in fee income, a primary stable revenue source of the Company. Additionally, VMIL's acquisitions, such as Republic Funds Barbados, provide a potential avenue for growth.

However, our positive expectations are tempered by assets under management on a non-recourse basis, only increasing by 5.8%. The current growth rate was half the growth seen in FY 2020 and about 25% of the growth in FY 2019. Finally, while the acquisition of Republic Funds Barbados could aid profit growth, we are cautiously optimistic given Carilend's performance.

Meanwhile, in the near term, we expect a decline in gains from investing activities to be the primary driver of earnings decline in FY 2022.

FY	Q1	Q2	Q3	Q4	YE
2022	E 0.04	E 0.09	E 0.19	E 0.03	E 0.36
2021	0.06	0.12	0.23	(0.03)	0.38

Key Risks to Our Price Target

Approximately half of VMIL's investment securities will mature in 5 or more years, and long-term bonds tend to be more sensitive to interest rate changes. Therefore, VMIL's book value could face a material decline in this rising interest rate environment. Additionally, $2.3 billion of fixed-rate notes at 5.5% is set to mature on January 16, 2023; if refinanced, it will likely be at a higher rate, resulting in compressed Net Interest Margins.

Meanwhile, Net Fees and Commission income, a key revenue source, has struggled to grow in recent years and declined in FY 2021. If this revenue source fails to meet our expectations, revenue growth could miss our forecasts.

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Recommendation:

We recommend an **UNDERWEIGHT** rating on VMIL at this point, given that the stock trades moderately below our base price target and has material near-term headwinds. **Our rating considers several factors, including potential growth rate and stock liquidity.**

We expect steady albeit slower growth in the medium to long term. Additionally, we see meaningful headwinds for the Company in the near term. The critical source of revenue growth, Net Fees, and Commission income shows signs of stagnation. Furthermore, VMIL has seen a meaningful increase in operating costs, further limiting earnings growth.

Finally, VMIL's stock is relatively illiquid, trading an average daily value of about $651.4 thousand over the last year. However, the volume traded has been trending up in 2022. **See charts 3 – 4 below for volume and value exchanged annually for the period under review.**

Chart 2.

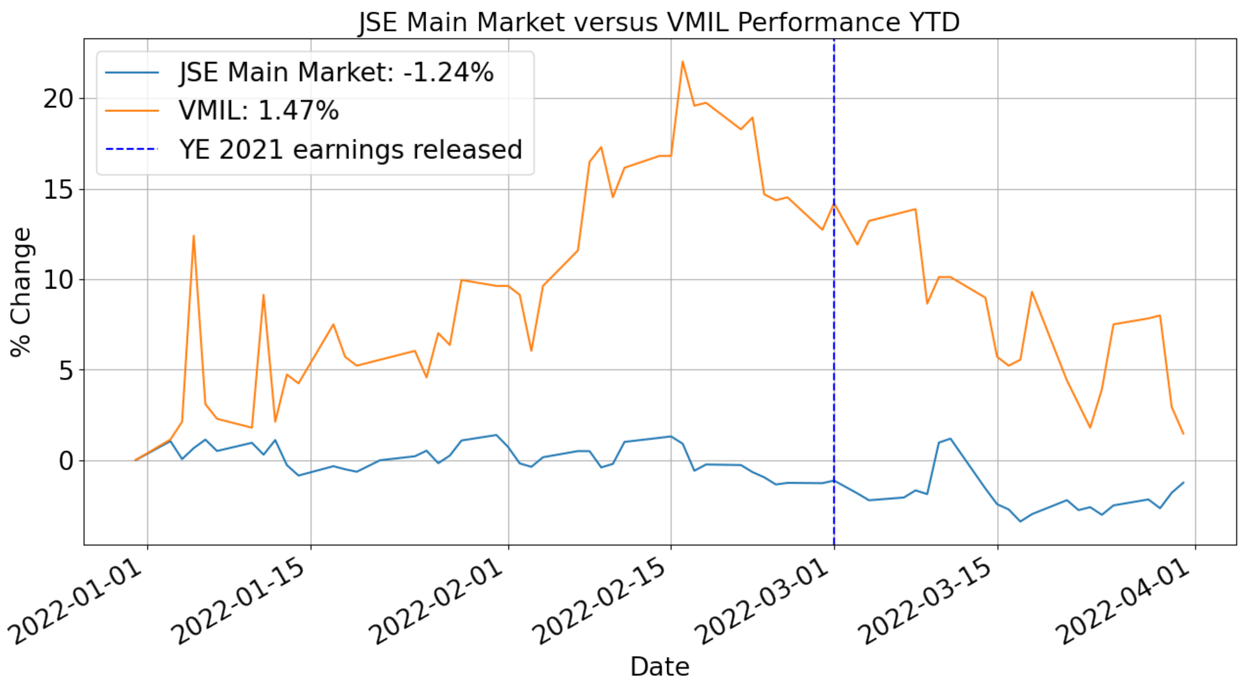


Chart 3.

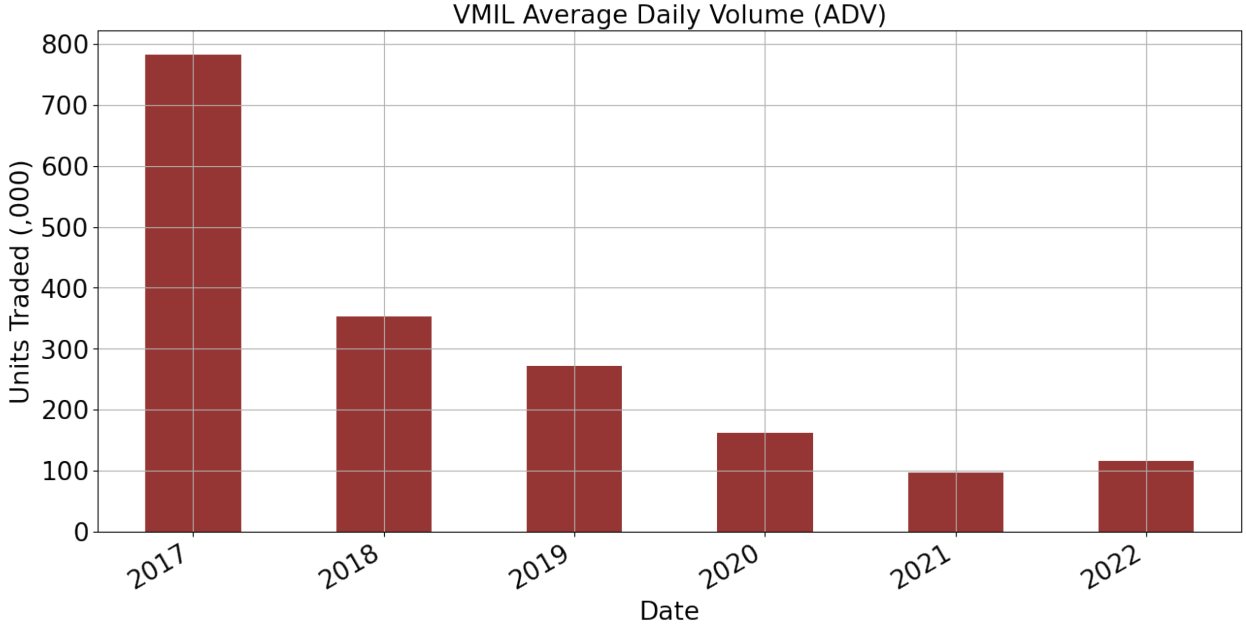
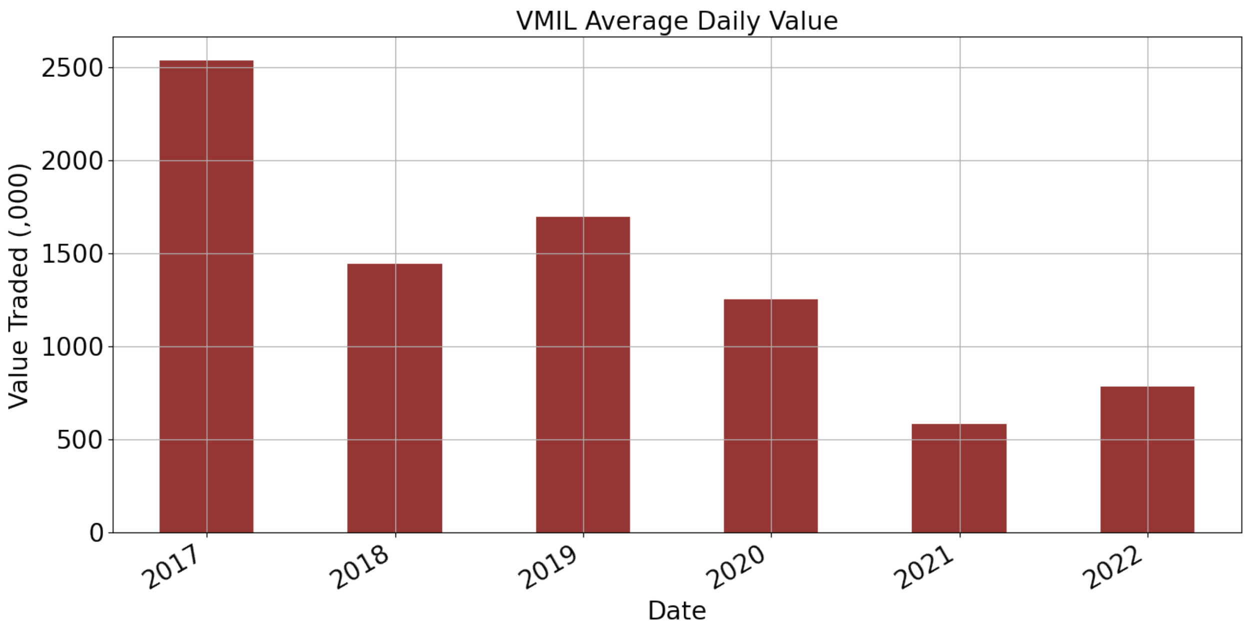


Chart 4.



Source: http://www.jamstockex.com, JMMB Investment & Research, Bloomberg, Various Company Financial Statements.

APPENDIX

IMPORTANT DISCLOSURES

ABSTRACT—As a part of our new Portfolio Strategy we are recommending strict adherence to the following Portfolio Allocation **DEFINITIONS/RECOMMENDATIONS**.

PLEASE NOTE THAT NO INDIVIDUAL ASSET IN YOUR PORTFOLIO SHOULD HAVE A WEIGHTING GREATER THAN 5% UNLESS OTHERWISE RECOMMENDED BY YOUR PORTFOLIO MANAGER OR A SPECIFIC JMMB RESEARCH REPORT. CONSEQUENTLY THE FOLLOWING **DEFINITIONS** ARE PROVIDED FOR CLARITY.

OUTPERFORM/OVERWEIGHT/BUY—EXPOSURE TO THIS ASSET SHOULD BE UP TO 10% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

MARKETPERFORM/HOLD/MARKETWEIGHT—EXPOSURE TO THE ASSET SHOULD BE EQUAL TO 5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB.

UNDERPERFORM/UNDERWEIGHT— ADJUST EXPOSURE IN YOUR PORTFOLIO HELD AT JMMB TO BETWEEN 2.5% AND 4.9% FOR THIS PARTICULAR ASSET

STRONGLY UNDERPERFORM/UNDERWEIGHT—REDUCE EXPOSURE TO THIS ASSET TO BELOW 2.5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

SELL—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO (0%).

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