Management report

As is traditional, in our year-end investor letter, we look back on 2018, key actions and learnings, as well as our outlook for 2019 and current thinking and positioning. In summary, 2018 saw just one portfolio addition (Konfio), as we continue to raise the investment bar. In early 2019 we completed our first successful exit (Tinkoff), which allowed us to build a very welcome strong capital position as we head into 2019. Creditas and iyzico stepped up as VEF size portfolio standout names, while Guiabolso NAV reduction over the period partly reflects longer-term nature of its revised strategy.

Reflecting on 2018

From a top-down perspective, 2018 was a very different year to 2017 as we moved from a uniformly positive macro, political and markets tailwind into one of the most volatile years, on all fronts, in recent history. For VEF and its portfolio companies this mainly manifested itself through periodic confidence-sapping election windows and weaker/volatile local currencies across the board.

With just three fairly benign macro years behind the company (although a much longer cycle hardened careers at team level before this), it was great to see how our portfolio companies reacted, or to be clear, didn't react, to the top down noise. We always work off the thesis that we are investing in structural growth stories, which are not immune to the short-term macro, but should grow through the cycle as individuals and companies continuously shift their financial services custom to fintech. When we look at our portfolio companies key metrics growth ranging from 50–200% YoY in 2018, and north of that in some of the earlier stage cases, our portfolio has shown much macro resilience to date.

Furthermore, 2018 was a year where we only made one new investment. This follows five investments in 2017 and three in 2016. Effectively, we continue to raise the investment bar in line with a growing risk environment. Our investment into Konfio, a Mexican SME lender, in mid-2018 was the only one that hit that high bar, and their delivery and performance since investing has only confirmed our confidence in that decision. We also spent a lot of time and fresh capital supporting our current portfolio companies (TransferGo, JUMO, REVO, Magnetis, Finja and FinanZero) to make sure they are in a strong capital place to both manage through any local headwinds, but also have the capital in place to further drive their growth.

From an investment perspective, what has tended to work best for us to date is focused single-country plays with exceptionally strong leadership teams. Effectively a focused team of professionals, in a single scale market, coming to the office every day executing along one specific line of business. Within this, we would point to portfolio standouts of Creditas and iyzico but also Magnetis and more recently Konfio.

Finally, we continued to sell down our position in Tinkoff Bank in 2018 and accelerated this trend through the fourth quarter. We ended the year with just 0.5 mln shares in Tinkoff, or USD 8 mln at current market prices. In the early part of 2019, we completed the exit of our Tinkoff position, completing our first portfolio exit, a clear milestone for the company. We entered into Tinkoff at USD 2.98 a share, a USD 19 mln holding. Over the course of our exit of the position we have taken USD 108 mln (average exit price USD 17) off the table, plus an additional USD 9 mln in dividends. An IRR of 65% and 6x cash on cash returns. First big exit for VEF, done. Tinkoff, we salute you.

4Q18 and 2018 performance review

In Q4 2018, total USD NAV of VEF fell 1.7% QoQ to USD 201.46 mln, while rising 1.4% YoY. NAV per share fell 0.5% QoQ to SEK 2.78, up 12.4% YoY.

Over the year Tinkoff Bank was the main driver of NAV in both directions (up for 9M18 and off in Q4) as its share price went from USD 19 on Jan 1 2018, peaking at USD 23.8 in September before ending the year at USD 15.4. Within the majority private portfolio, iyzico was a clear positive force while Guiabolso weighed on proceedings through Q4 and FY18. In general, for those positions valued by mark to model, local currency weighed on all through 2018 while comparison listed company multiples were generally a positive force in 1H18 before weighing into 2H18.

Outlook for 2019

Given our deliberate cash build-up through 2H18, we enter 2019 in a very strong position as this is a great window for the long-term structural investor, like VEF, to be liquid. With the global economy and markets struggling, these are market conditions that should see a continued pricing power shift to the buyer. It is the kind of environment where we will continue to be very selective with transactions, but are very much readied for the opportunities as they arise. Pipeline is not the issue, and hasn't been for some time, it is the right deals at the right time and price we crave and only look to do.

Furthermore, as in the recent past, we look seriously at our own stock as an investment opportunity in this window. With the discount to NAV widened to c. 30%+, a NAV we see upside in over time, some of the best use of our capital can be buying more of our own portfolio at a discount, creating value for our long-term shareholders at the same time.

To quote Warren Buffet, "The best use of cash, if there is not another good use for it in business, if the stock is under-priced is a repurchase," and "Anytime you can buy stock for less than it's worth, it's advantageous to the continuing shareholders". There is always a balance in these things and it is a function of clear capital allocation with the constant goal of creating value for shareholders. We weigh up current portfolio and pipeline needs, coupled with logical buffers for the business, but buybacks are very much on our mind.

Concluding remarks

We start 2019 with a strong portfolio, a strong cash cushion/firepower and feeling as well placed in the EM Fintech ecosystem as we ever have. Confident that our actions and NAV will be reflected in our share price, we continue to actively engage the market to drive that sooner as opposed to later. We re-iterate that delivering shareholder value through a focused approached to increasing our NAV per share and reducing traded discount to market value remain our core focus. We take a long-term view on our company, investments and indeed life, which is necessary when investing in the space that we do. Hence we are ready to react and act in any environment with these supporting mindsets.

February 2019,
David Nangle