CUSPCAPITAL

An introduction to *Venture Capital*

Ruhr-Universität Bochum

June 2, 2022

Cusp Capital –
VC for companies on the cusp of global relevance

→ As a team we started in 2009 and were repeatedly ranked as one of the Top 10 backers of European unicorns by GP Bullhound in their annual Titans of Tech reports.

→ In 2021, we have started Cusp Capital and raised an independent early-stage VC fund.

→ We follow a thesis driven investment approach.

→ We work with entrepreneurs in scaling their businesses by supporting to shape their strategic narrative and operational excellence.

→ With Cusp Capital, we have partnered with 9 companies so far – more to come.

We invested *crossed in many category defining categories over the last 12 years.*

Investments in European champions

zalando	Invested in Series A	DAX 30
Klarna.	Invested in Series C	Private with € 38bn last valuation
Delivery Hero	Invested in Seed	DAX 30
WESTWING	Invested in Series B	Public
GFG Global Fashion Group	Invested in Seed	Public
scalable .CAPITAL	Invested in Series A	Private with € 1.4bn last valuation
sumup	Invested in Seed	Private with € 4.5bn valuation
dataArtisans	Invested in Series A	Acquired by Alibaba
Stylight	Invested in Seed	Acquired by Pro7Sat1
eKomi	Invested in Seed	Sold shares to PE
Wunderlist	Invested in Seed	Acquired by Microsoft
Lazada	Invested in Series A	Acquired by Alibaba

01 Intro Cusp Capital

A new generation of companies changing *the way millions of people live or enabling other businesses to master this change.*

SIDES

Thousands of restaurants are changing to delivery first – SIDES provides the software backbone for their operations.

Name	SIDES	**Founded**	2014
Location	Berlin, Germany	**Invested**	2021

CarbonCloud

The food industry wants to transform itself to carbon net zero – CarbonCloud provides the necessary software to model the change.

Name	CarbonCloud	**Founded**	2018
Location	Gothenburg, Sweden	**Invested**	2021

audvice

Podcasts have become part of consumers' daily routines – audvice is the microcast platform to share knowledge in enterprises.

Name	audvice	**Founded**	2018
Location	Salzburg, Austria	**Invested**	2021

LIBEEN

Millions of Europeans are excluded from homeownership – Libeen makes their dream of owning a home reality.

Name	Libeen	**Founded**	2019
Location	Madrid, Spain	**Invested**	2021

Hivebuy

The rise of eCommerce empowers every employee to procure - Hivebuy helps companies to manage approvals, budgets, and more.

Name	Hivebuy	**Founded**	2021
Location	Berlin, Germany	**Invested**	2021

Fixably

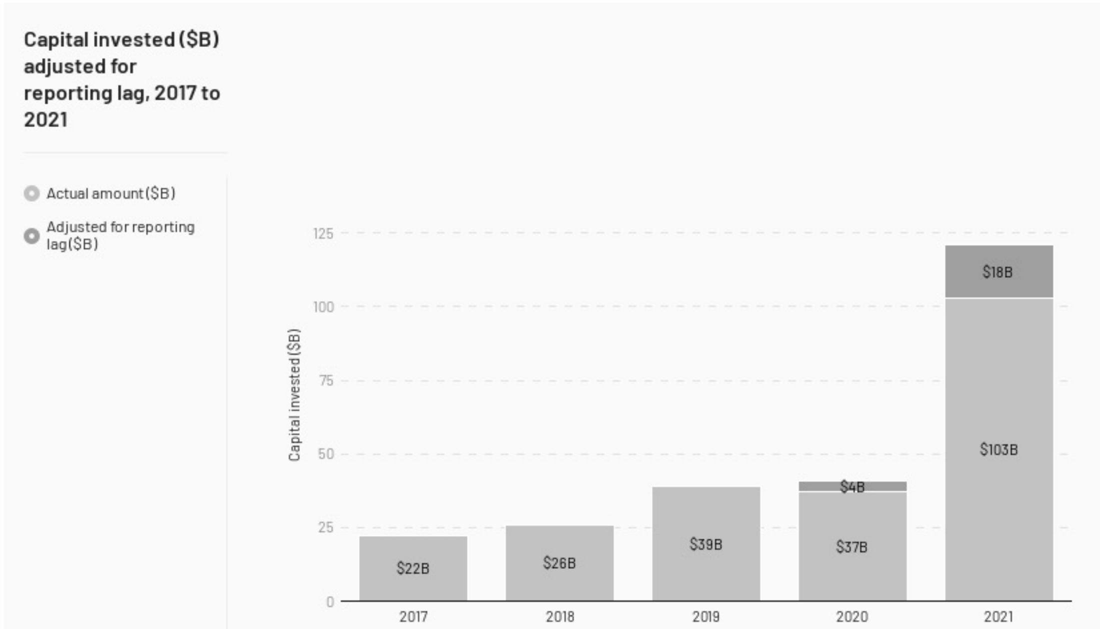
The electronics industry is embracing repair – Fixably provides the Industry Specific Operating System for its service providers.

Name	Fixably	**Founded**	2015
Location	Helsinki, Finland	**Invested**	2022

02 Venture capital – a small asset class with high impact

Venture capital is a growing asset class …

The European technology ecosystem reached $100B of capital invested in a single year for the first time in 2021.



Source: State of European tech

02 Venture capital – a small asset class with high impact

… but still tiny compared to other asset classes.

Allianz third-party portfolio of asset allocation

		As of 31 December 2021	As of 31 December 2020	Delta
Third-party assets under management	**€ bn**	**1,966**	**1,712**	**14.9%**
Business units' share				
PIMCO	%	76.8	78.1	(1.3) %-p
AllianzGI	%	23.2	21.9	1.3 %-p
Asset classes split				
Fixed income	%	75.4	78.3	(3.0) %-p
Equities	%	10.4	9.5	0.9 %-p
Multi-assets	%	10.5	9.4	1.1 %-p
Alternatives	%	3.7	2.7	1.0 %-p
Investment vehicle split[1]				
Mutual funds	%	58.5	57.9	0.5 %-p
Separate accounts	%	41.5	42.1	(0.5) %-p
Regional allocation[2]				
America	%	55.5	54.8	0.8 %-p
Europe	%	32.4	32.8	(0.4) %-p
Asia Pacific	%	12.1	12.4	(0.4) %-p

VC is part of the Alternatives asset allocation

Hedge Funds

Buyout funds

Real estate

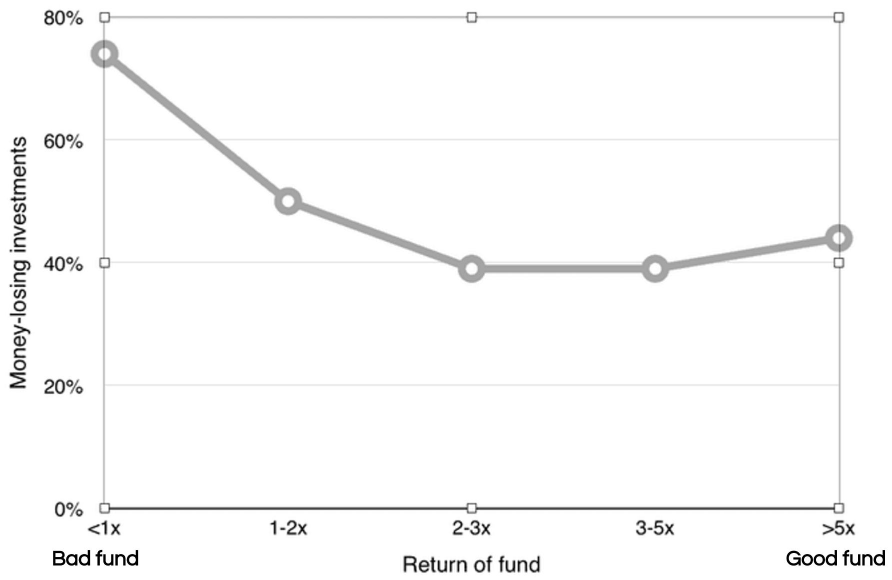
Infrastructure

Venture Capital

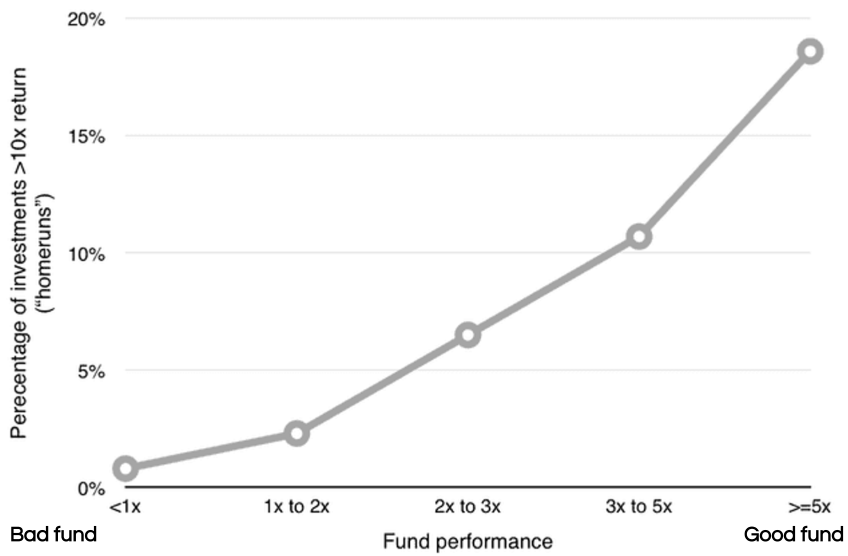
Some of the world’s most successful companies have been funded by venture capital in their early days.

Venture capital is defined by asymmetric returns – *a high probability of default with an (almost) unlimited upside.*

> 40% of investments of a typical VC
loose money



Returns are driven by
home runs



Source: Chris Dixon (a16z), Performance Data and the 'Babe Ruth' Effect in Venture Capital.

To achieve a 3x return on the fund, *every investment needs to have home run potential.*

The Babe Ruth Effect

Frequency vs. magnitude

"Building a portfolio that can deliver superior performance requires that you evaluate each investment using expected value analysis.

What is striking is that the leading thinkers across varied fields—including horse betting, casino gambling, and investing—all emphasize the same point.

We call it the Babe Ruth effect: even though Ruth struck out a lot, he was one of baseball's greatest hitters."

Summary: *In the VC fund model non-profitable investments are overcompensated by fund returners.*

Example of a fund model for a € 100m VC fund

Company	Investment	Money Multiple	Exit proceeds
1	10	0,0x	0
2	10	0,0x	0
3	10	0,0x	0
4	10	1,0x	10
5	10	1,0x	10
6	10	1,5x	15
7	10	1,5x	15
8	10	1,5x	15
9	10	11,5x	115
10	10	12,0x	120
Total	**100**	**3,0x**	**300**

Metrics

Loss ratio:	*30%*
Fund returner:	*20%*
DPI:	*3x*

This example follows the assumption that investments are equally distributed among companies. In reality the fund manager also has to manage allocations of follow-on financings etc. In doing so, opportunity costs need to be considered.

Investment decisions are guided by the goal to *hit home runs*

Market size	Team	Product (market fit)
The TAM narrative	*The ambition & execution*	*The metrics*

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Success in a small market will not lead to outsized returns

The ”so what” question in Venture Capital

- „The team is great and the product is superb, but *so what* if the market is not big enough?”
- “Companies can succeed in great markets with mediocre teams but *great teams will always lose to bad markets”*

But what is the market? The addressable market narrative

- How would you estimate the market size for Uber?

Addressable market narrative – *the case of* Uber

The taxi market narrative by Aswath Damodaran: *Uber is not worth USD 17bn*

Uber: Intrinsic valuation - June 8, 2014 (in US $)

Stable Growth (after year 10)
Expected growth rate = 2.50%
Cost of capital = 8%
Return on capital= 25%
Reinvestment Rate= 2.5%/25% = 10%

Terminal Value$_{10}$= 793/(.08-025) = $14,418

Term yr
EBIT (1-t) $881
- Reinv 88
FCFF $793

Global taxi market is $100 billlion currently, expected to grow 6% a year for next ten years.

Uber will keep 20% of the gross cab receipts as its revenues

Uber's market share of this market will increase to 10% over the next 10 years.

Uber's operating expenses will amount to 60% of its revenues. (Operating margin=40%)

Uber will pay a tax rate of 30% on its income, increasing to 40% over the next 10 years

Uber will generate $5 in incremental revenues for every dollar of incremental capital.

	1	2	3	4	5	6	7	8	9	10
Overall market	$106,000	$112,360	$119,102	$126,248	$133,823	$141,852	$150,363	$159,385	$168,948	$179,085
Share of market (gross)	3.63%	5.22%	6.41%	7.31%	7.98%	8.49%	8.87%	9.15%	9.36%	10.00%
Revenues as percent of gross	20.00%	20.00%	20.00%	20.00%	20.00%	20.00%	20.00%	20.00%	20.00%	20.00%
Annual Revenue	$769	$1,173	$1,528	$1,846	$2,137	$2,408	$2,666	$2,916	$3,163	$3,582
Operating margin	7.00%	10.67%	14.33%	18.00%	21.67%	25.33%	29.00%	32.67%	36.33%	40.00%
Operating Income	$54	$125	$219	$332	$463	$610	$773	$953	$1,149	$1,433
Effective tax rate	31%	32%	33%	34%	35%	36%	37%	38%	39%	40%
- Taxes	$17	$40	$72	$113	$162	$220	$286	$362	$448	$573
After-tax operating income	$37	$85	$147	$219	$301	$390	$487	$591	$701	$860
Sales/Capital Ratio	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00
- Reinvestment	$94	$81	$71	$64	$58	$54	$52	$50	$49	$84
Free Cash Flow to the Firm	-$57	$4	$76	$156	$243	$336	$435	$541	$652	$776

Based on the investment of $1.2 billion made by investors, the imputed value for Uber's operating assets, in June 2014 ,was $17 billion.

Discount back the cash flows (including terminal value) at the cumulated cost of capital.

Value of operating assets = $6,595

Adust for probability of failure (10%)
Expected value = $6,595 (.9) = $5,895

Cost of capital for first 5 years = Top decile of US companies = 12%

Cost of capital declines from 12% to 8% from years 6 to 10.

Source: Aswath Damodaran, https://aswathdamodaran.blogspot.com/2014/06/a-disruptive-cab-ride-to-riches-uber.html

Addressable market narrative – *the case of* Uber

The car ownership alternative narrative by Bill Gurly: *25 times higher than Damadoran's original estimate*

"Sizing the market for a disruptor based on an incumbent's market is like sizing the car industry off how many horses there were in 1910"

Car alternative

New use cases

Higher demand through better prices & services

The Taxi market

Source: Bill Gurley, https://abovethecrowd.com/2014/07/11/how-to-miss-by-a-mile-an-alternative-look-at-ubers-potential-market-size/

Investment decisions are guided by the goal to *hit home runs*

Market size

The TAM narrative

Team

The ambition & execution

Product (market fit)

The metrics

To win, founders need to have high ambitions, execute under pressure & inspire others – *this takes a special character*

Examples of outstanding entrepreneurs (you might have not heard about)

shopify

- *Born in Koblenz*
- *Freelance software developer*
- *Built an e-commerce shop for snowboards*
- *CEO of a USD 45bn company*

Spotify

- *Started to develop websites at age 13*
- *Managed a team of 15 by the age of 18*
- *Founded several companies*
- *CEO of a USD 21bn company*

UiPath

- *Born in Romania*
- *Worked for Microsoft in Seattle, U.S.*
- *Returned to Romania to build the UiPath*
- *CEO of a USD 9bn company*

Your personal ambition test

What would you do?

You have founded a company 3 years ago. The journey so far has been tough but you see great developments over the last year. The opportunity is huge and you are excited that things are finally moving in the right direction.

A competitor comes along and offers you € 50m for your company. Sell or not sell?

Investment decisions are guided by the goal to *hit home runs*

Market size	Team	Product (market fit)
The TAM narrative	*The ambition & execution*	*The references & metrics*

Being in a good market with a product that can satisfy this market – *product market fit*

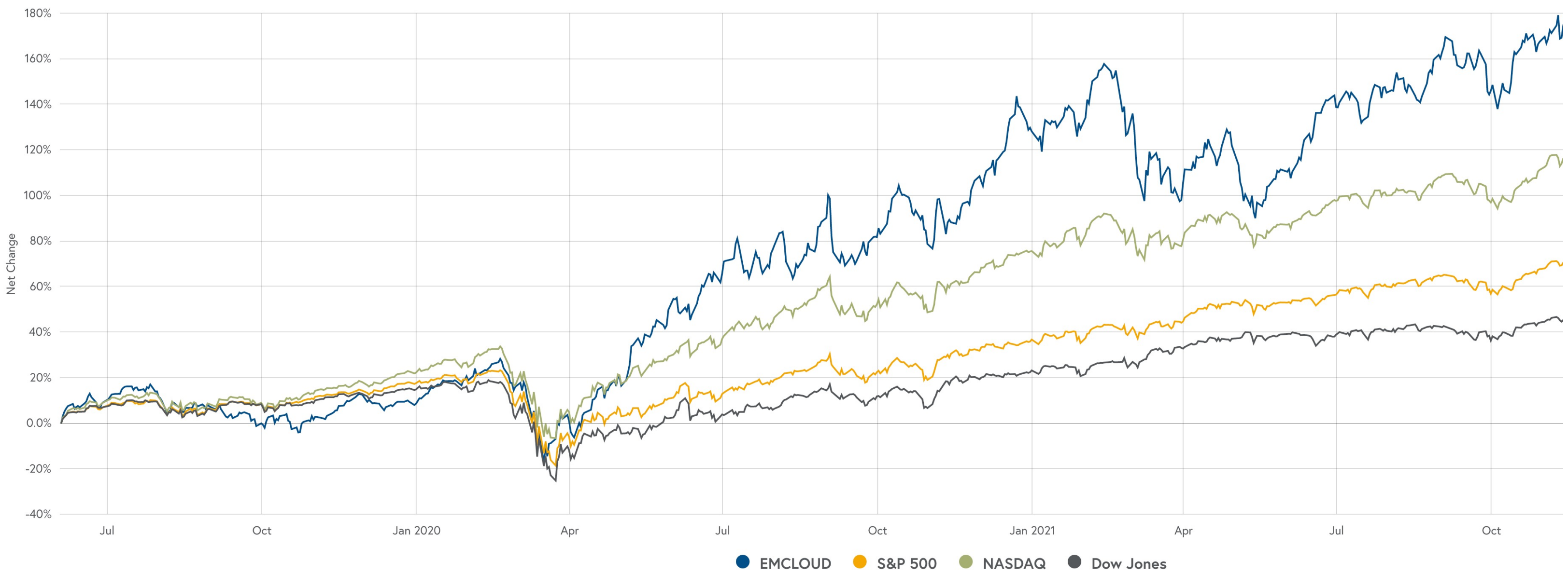
What do industry experts / customers think about the product?

- Expert calls
- Customer calls

Are relevant metrics pointing to product market fit and growth?

- User / customer growth
- Recurring revenue growth
- Net revenue retention
- Churn of customers
- ...

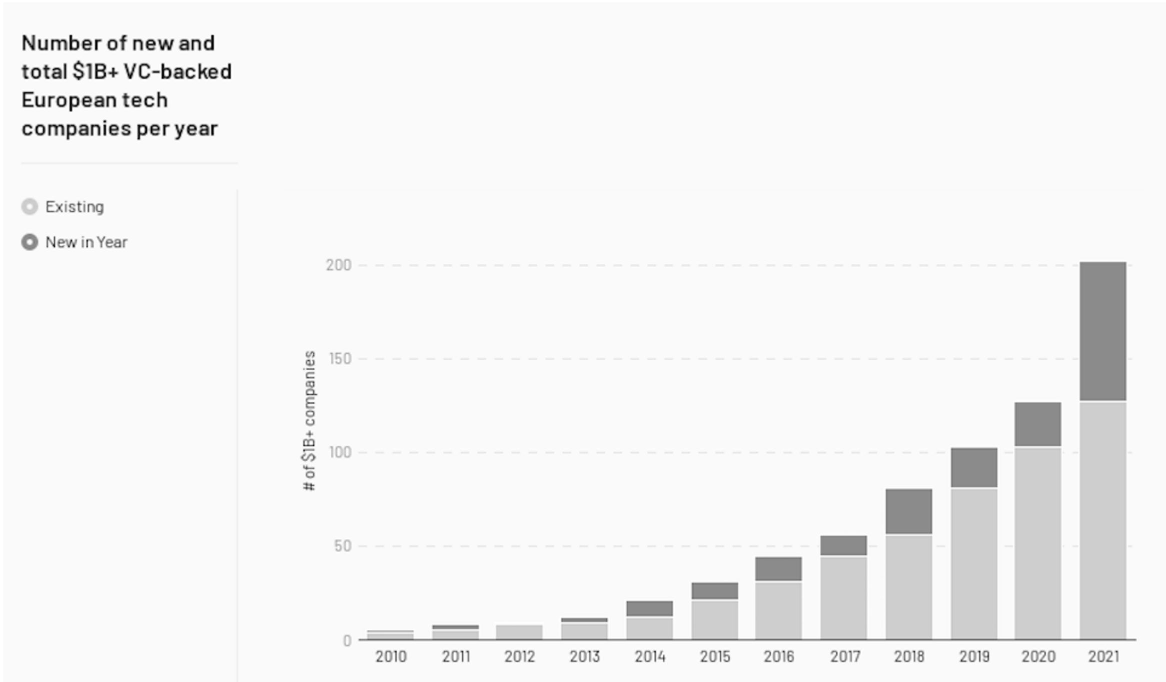
Funding volumes & valuation boomed over the last 3 years – *irrational exuberance?*



For complete index information including methodology, visit NASDAQ.

Funding volumes & valuation boomed over the last 3 years – *irrational exuberance?*

In 2021, more companies than ever before reached unicorn status.

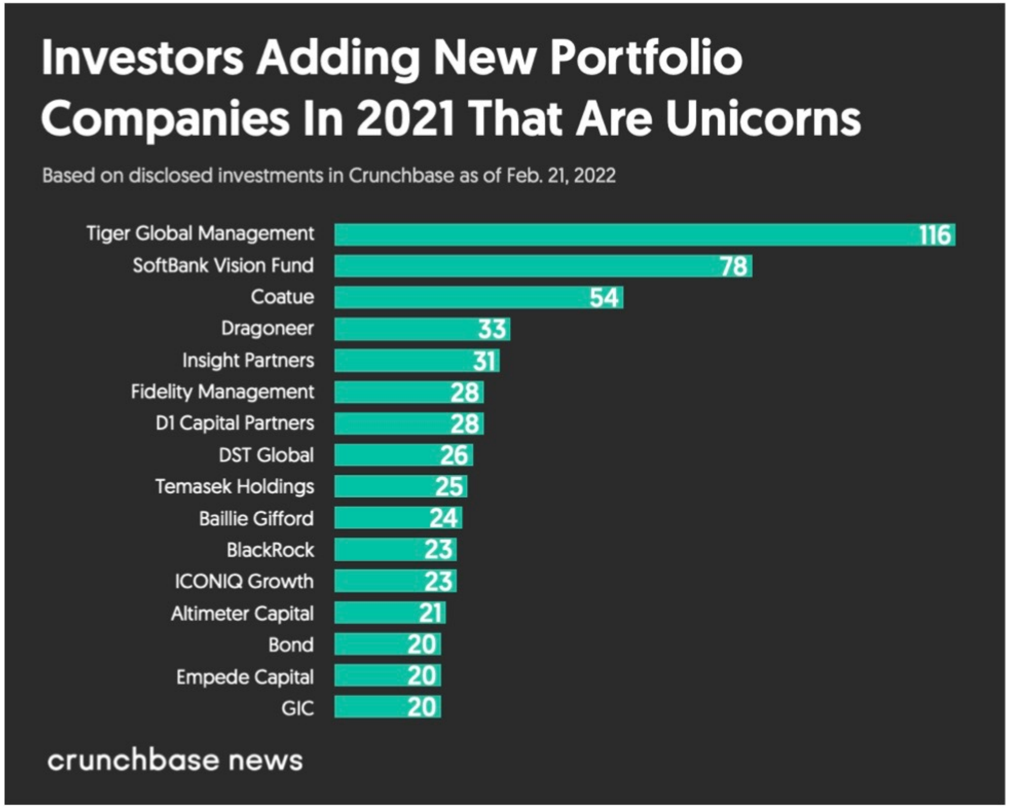


Source: State of European tech

Funding volumes & valuation boomed over the last 3 years – *irrational exuberance?*

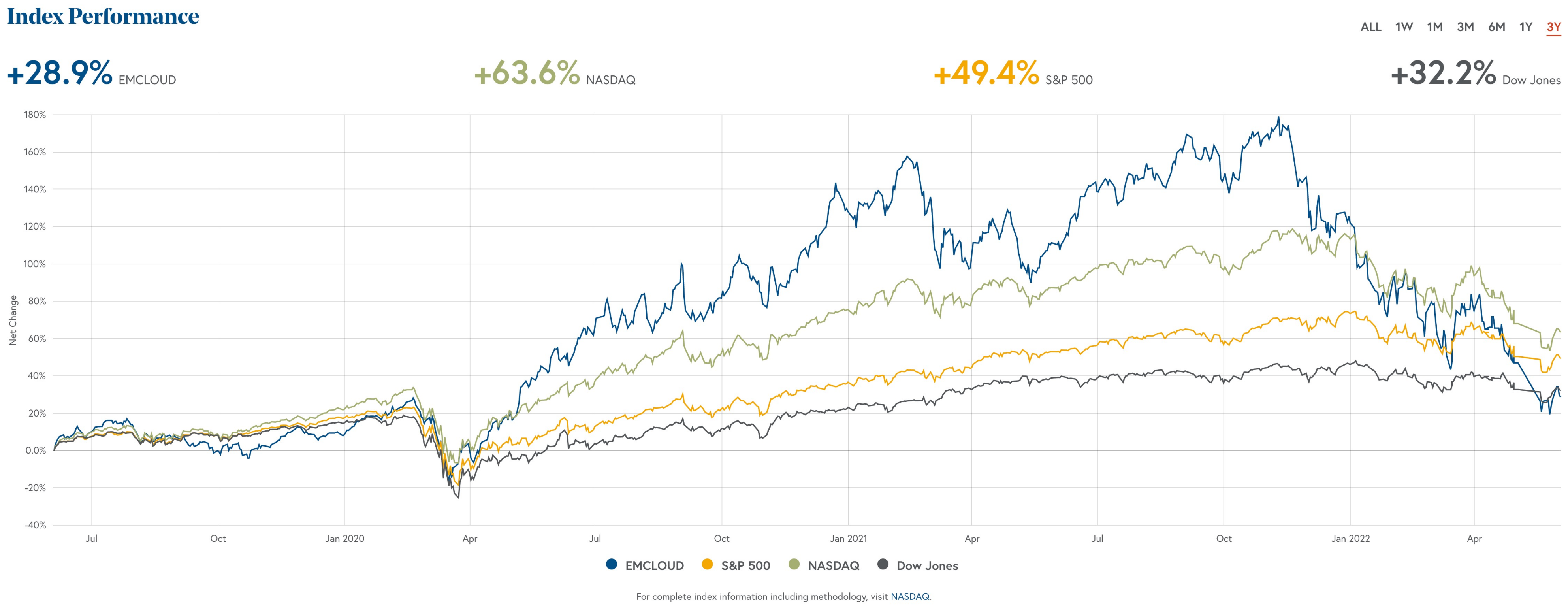
TIGERGLOBAL

- Hedge Fund turned VC based
- Invest out of a USD 12.7bn VC fund
- Have done almost one deal per day in 2021 across the globe

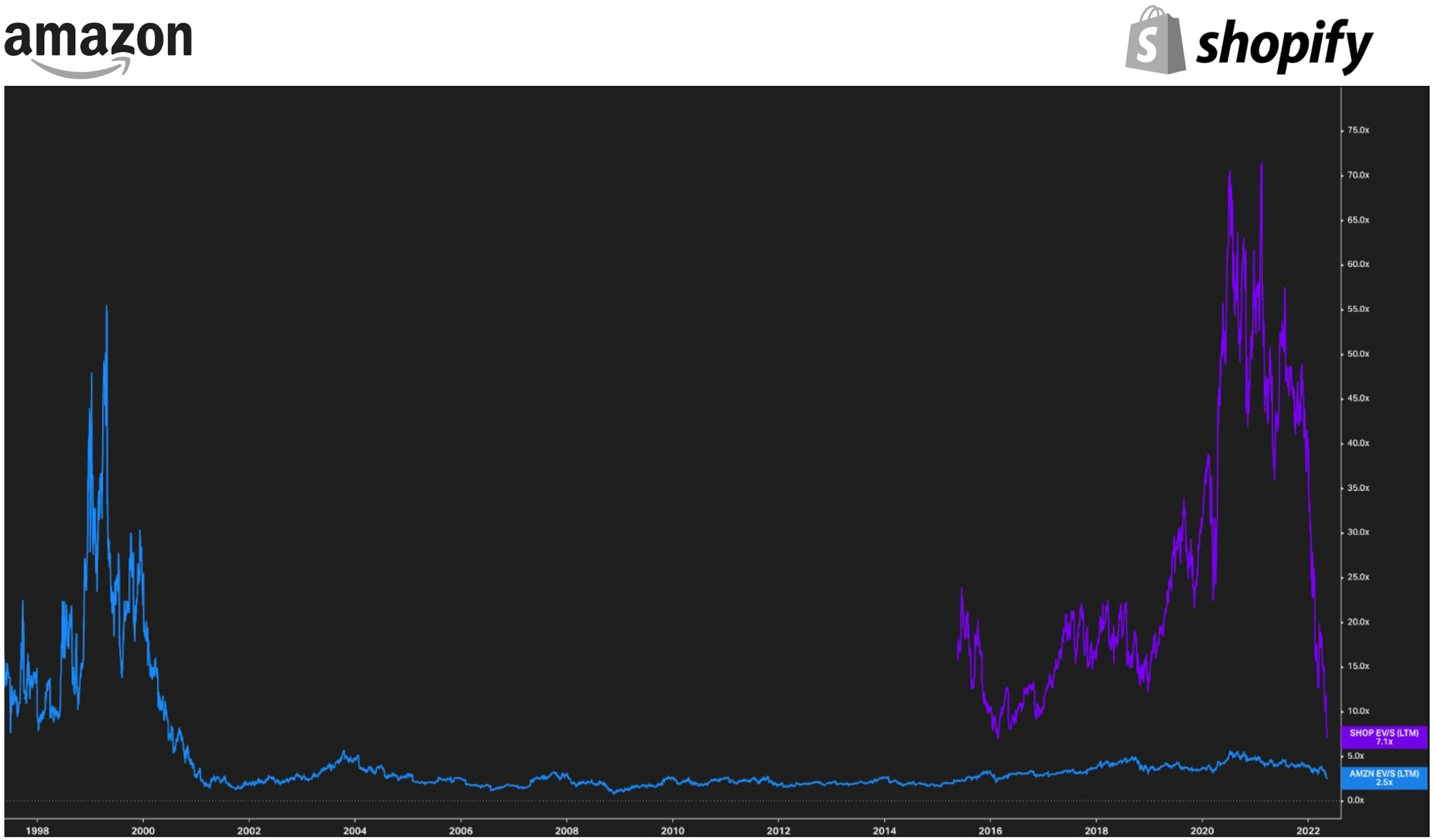


04 The current market environment & case studies

Driven by inflation, increasing interest rates & economic uncertainty we are in a tech bear market– *the drought?*



Driven by inflation, increasing interest rates & economic uncertainty we are in an epic tech bear market– *the drought?*



EV/Sales

Dot-com crash

Today

Driven by inflation, increasing interest rates & economic uncertainty we are in an epic tech bear market– *the drought?*

TIGERGLOBAL

Tiger Global hit by $17bn losses in tech rout

Hedge fund suffers 'breathtaking' drop as speculative stocks sink from pandemic peaks

CNBC DISRUPTOR 50

Klarna to lay off 10% of its workforce as souring economy hits buy now, pay later space

PUBLISHED MON, MAY 23 2022•1:16 PM EDT | UPDATED WED, MAY 25 2022•10:22 AM EDT

TECH

Sequoia coaches start-ups to cut costs or face a 'death spiral' amid stock market slump, bleak economic backdrop

PUBLISHED THU, MAY 26 2022•11:14 AM EDT | UPDATED THU, MAY 26 2022•1:21 PM EDT

The upside of a downturn– *time to build*

Progress in technology *continues throughout market cycles.*

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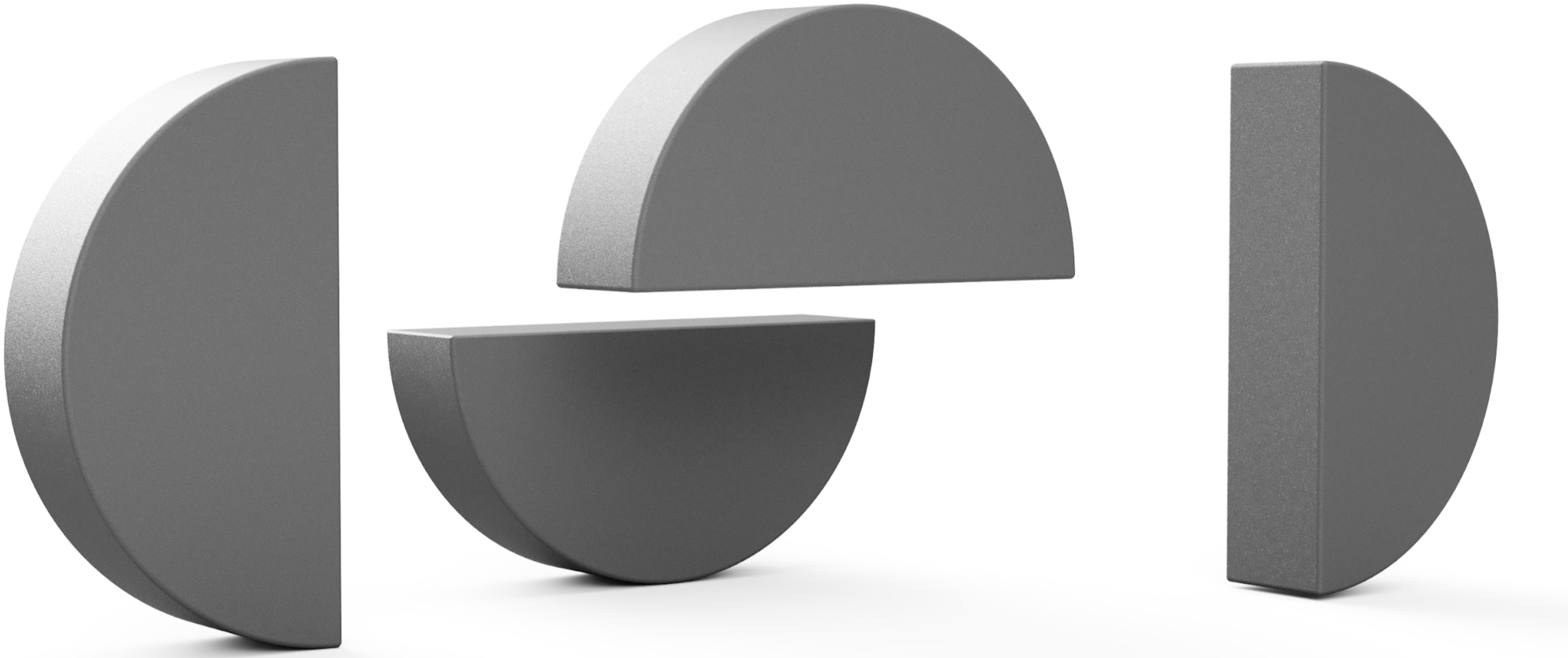

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