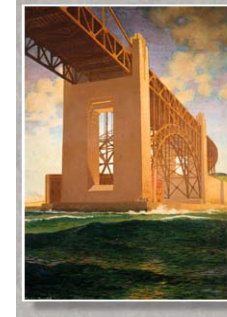


# ALLIANCE VENTURE

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**Investing in emerging  
technology companies  
& supporting their  
global expansion**



**Choosing Innovation projects  
a VC perspective**

**Erling Maartmann-Moe**

[www.allianceventure.com](http://www.allianceventure.com)

# Overview of lecture

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- What is Venture Capital?
- Example portfolio
- Sources of capital
- Process for evaluation
- Investment criteria
- Quantitative measures
- Shares and value creation

# Alliance Venture – Overview

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- Alliance Venture invests in *Norwegian emerging technology* companies at an early stage with a focus on ICT:
  - where we can *add value* with our operational experience and international network
  - by supporting their *international expansion through alliances* with leading technology corporations and international venture capital firms
- Funds under management:

## Alliance Venture IP

- Formed in 2001
- Capital of 83 MNOK
- Fully invested in 9 companies
- 5 exits with good multiples

## Alliance Venture Polaris

- Formed in December 2006
- Capital of 339 MNOK
- Selected by Innovation Norway (IN) as the Oslo-based nationwide seed fund
- Committed capital structure is 51% private funds and 49% loan from IN

# Venture: Webster's dictionary

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Main Entry: <sup>1</sup>ven·ture Pronunciation: \ 'ven(t)-shər\ Function: *verb*

Inflected Form(s): ven·tured; ven·tur·ing \ 'ven(t)-sh(ə-)rɪŋ\

Etymology: Middle English *venteren*, by shortening & alteration from *aventuren*, from *aventure* adventure Date: 15th century *transitive verb*

1 : to expose to hazard : [risk](#) , [gamble](#) <*ventured* a buck or two on the race>

2 : to undertake the risks and dangers of : [brave](#) <*ventured* the stormy sea>

3 : to offer at the risk of rebuff, rejection, or censure <*venture* an opinion> *intransitive verb* : to proceed especially in the face of danger  
— ven·tur·er \ 'ven(t)-sh(ə-)rər\ *noun*

# Alliance Venture Polaris – Portfolio Companies

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Provides a new system for web navigation that automatically generates a menu for any website without any redesign that allows much more efficient and user-friendly way to browse the site. [www.bmenu.com](http://www.bmenu.com)



Aggregator of digital music, signing artists and labels within independent music outside the major record companies, and selling its tracks through leading storefronts like iTunes and Microsoft. Focusing on the Nordic market, but also has operations in China and South Africa. [www.phonofile.com](http://www.phonofile.com)



Develops gas sensors for detection of gases and measurement of gas concentrations in applications such as air control in buildings, detection of combustible gases in explosive areas, patient monitoring and anesthetics systems in hospitals. [www.optosense.com](http://www.optosense.com)



Has developed the PagePlanner publishing software with primary focus on the magazine and catalogue industry. PagePlanner delivers a multi-platform (magazine, mobile, iPad, web) publishing system as SaaS. [www.pageplanner.com](http://www.pageplanner.com)

# Alliance Venture Polaris – Portfolio Companies

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Offers digital cross media communication technology, primarily for audience participation and user submitted content in broadcasting and advertising. The platform works for both traditional TV and webTV, IPTV, mobile TV etc where viewers participate through their mobile phones, the Internet, set-top boxes, Facebook, Twitter etc. [www.never.no](http://www.never.no)



Provider of Integrated Access Devices (IAD). The IAD combines the functionality of the broadband modem and the high speed wireless router, targeting the market for residential devices, offering integrated high speed internet access, Voice over IP (VoIP), IPTV and mobile services in the same unit (Quattro play). [www.pingcom.net](http://www.pingcom.net)



Novelda is a fabless semiconductor company developing single chip realizations of Ultra Wide-Band (UWB) Impulse Radios (IR). Novelda aims to become the world's leading supplier of integrated circuits (IC) to OEMs for UWB-IR-based sensor and wireless communication products.

[www.novelda.no](http://www.novelda.no)



3D perception develops and supplies patented projection technologies and projection related solutions to the simulation, automation and entertainment industries. Products enable geometrical correction of images projected on to curved screens and make it possible to seamlessly combine images from multiple projectors. [www.3d-perception.com](http://www.3d-perception.com)

# Alliance Venture Polaris – Portfolio Companies

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Encap delivers a patented user authentication solution for online banking or enterprise VPN log-in. The solution replaces the access token/electronic code calculator with the user's own mobile phone as the hardware component in the implementation of the two-factor user authentication security mechanism. [www.encap.no](http://www.encap.no)



Integrasco is a leading Internet Word of Mouth analytics firm which helps global brands make sense of the buzz found on blogs, bulletin boards and any other interactive consumer channel, focusing on product buzz in multiple languages. Integrasco is a pioneer in the field of data mining and in possession of comprehensive mining technology. [www.integrasco.com](http://www.integrasco.com)



poLight develops active optical components for the imaging, optical communication and display markets, with the main focus on auto-focus lenses for wafer level cameras for mobile handsets and other portable devices, based on a portfolio of patents. [www.polight.com](http://www.polight.com)

# Alliance Venture exits – international focus

## AV portfolio company

## Description

## Acquiring company



A fabless IP core design company targeting the SoCs (Systems-on-Chips) providers for handheld 3D graphics and multimedia hardware. [www.falanx.com](http://www.falanx.com)  
**SOLD TO ARM IN 2006 for 25 MUSD**  
**AV return: 32 MNOK, 6x multiple and 128% IRR**



Network independent value added voice, data communication, multimedia software and services for next generation telecom networks. [www.net4call.com](http://www.net4call.com)  
**SOLD TO ORACLE IN 2006 for 10 MUSD**  
**AV return: 29 MNOK, 14x multiple and 93% IRR**



Routing, signal processing and optical transport solutions for audio, video and datacom to the broadcast industry. Renamed Nevion. [www.nevion.com](http://www.nevion.com)  
**SOLD TO HERKULES CAPITAL IN 2008 for 200 MNOK**  
**AV return: 16 MNOK; 2x multiple and 20% IRR**



Software company that develops and markets solutions for support automation and self service. [www.tific.com](http://www.tific.com)  
**SOLD TO PLUMCHOICE IN 2011 for 15 MUSD**  
**AV return: 12 MNOK; 1.4x multiple and 7% IRR**



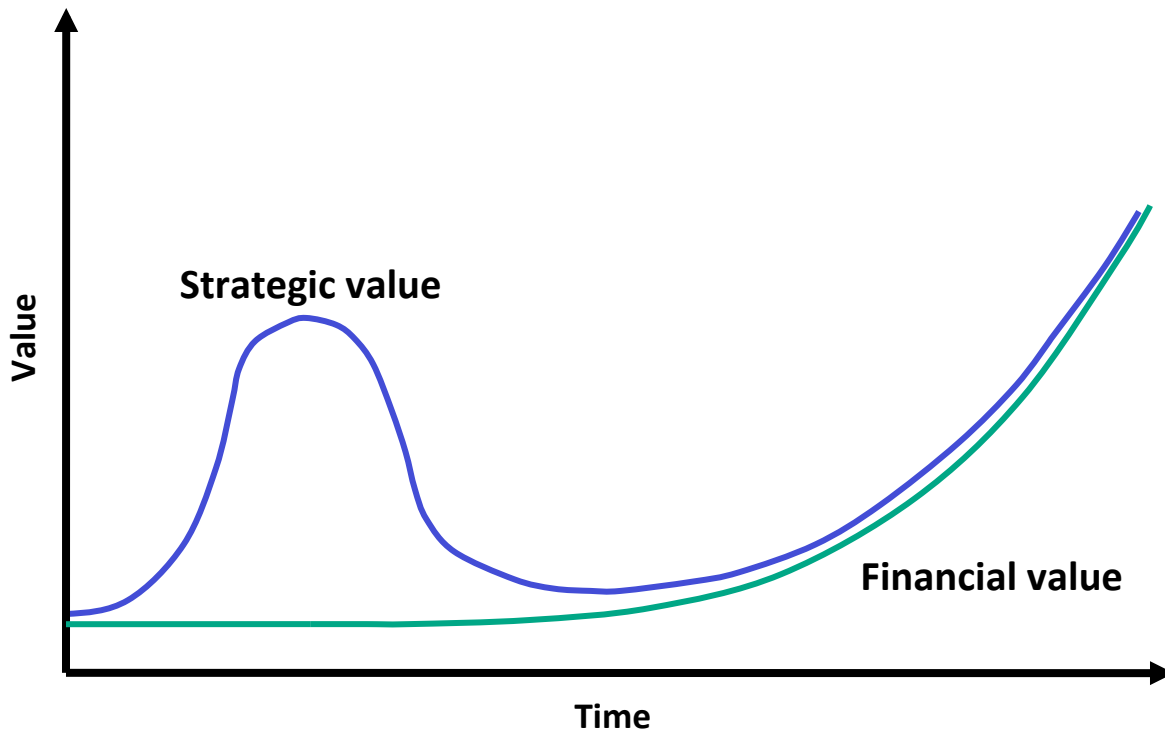
Tailor-made portals and communities for learning in large organizations, hosted as a service. [www.edvantagegroup.com](http://www.edvantagegroup.com)  
**SOLD TO LUMESSE IN 2011 for 22 MUSD**  
**AV return: 20 MNOK; 1.7x multiple and 6% IRR**





# While it takes a long time to develop financial value, strategic value can be realized earlier

## Conceptual model for alternative value development scenarios

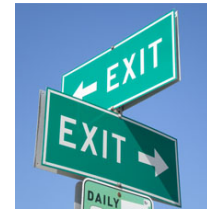


- Developing financial value takes a long time – longer than expected
- The financial value is flat as the cash-flow is negative
- The slow development is related to gaining market acceptance and building distribution
- Meanwhile, unique technology can have substantial value to established industry players with market access

# Guiding AV investment principles and theses

Principle	Details/Logic
<b>Invest on a lean/capital efficient basis</b>	<ul style="list-style-type: none"> <li>• Capital efficiency is seen as key for multiples</li> <li>• Time investment in go-to-market with proof of traction to avoid burning resources</li> </ul>
<b>Seek aligned and capable co-investors</b>	Complimentary skills and different views add value, while increasing robustness in difficult situations
<b>Ride fundamental/macro trends</b>	<ul style="list-style-type: none"> <li>• “Skate where the puck will be” – the right macro trends do a lot of the work</li> <li>• Watch out for hype; understand the fundamentals</li> </ul>
<b>Invest on strategic hypothesis</b>	Define success criteria for investment in terms of strategic hypothesis; compare with expected trends
<b>Seek strategic exits for value/return</b>	Depending on technology and value chain fit, the value is bigger for an industrial player
<b>Serve an underserved tech investment opportunity locally</b>	The number of active Nordic seed and venture funds is significantly reduced; limited competition
<b>The traditional VC value chain is broken; face the consequences</b>	<ul style="list-style-type: none"> <li>• A traditional Series A-C relay is atypical in Europe</li> <li>• Ability to fund all the way is key to avoid wipe-out</li> </ul>

# AV pursue a dual track exit strategy



Track	Key value creation activities & indicators	Value realization logic	Realization / exit route
<b>Strategic</b>	<ul style="list-style-type: none"> <li>• Technology, prototypes and products</li> <li>• IPR</li> <li>• Market proof</li> <li>• Partnerships</li> </ul>	<ul style="list-style-type: none"> <li>• Unique capabilities/offers</li> <li>• Technology driven</li> <li>• Value chain/acquirer fit</li> <li>• Driven by acquirer's value</li> </ul>	<ul style="list-style-type: none"> <li>• Strategic trade sale</li> </ul>
<b>Financial</b>	<ul style="list-style-type: none"> <li>• Building business – revenue, profit, growth</li> <li>• Building organization</li> <li>• Building customer base</li> <li>• Building capabilities and business processes</li> <li>• Distribution</li> </ul>	<ul style="list-style-type: none"> <li>• Standalone business and financial value</li> <li>• Complementary products</li> <li>• Complementary market coverage</li> <li>• Complementary capabilities</li> <li>• Multiple driven</li> </ul>	<ul style="list-style-type: none"> <li>• Trade sale</li> <li>• IPO</li> <li>• PE buy-out</li> </ul>

# Sources of Capital

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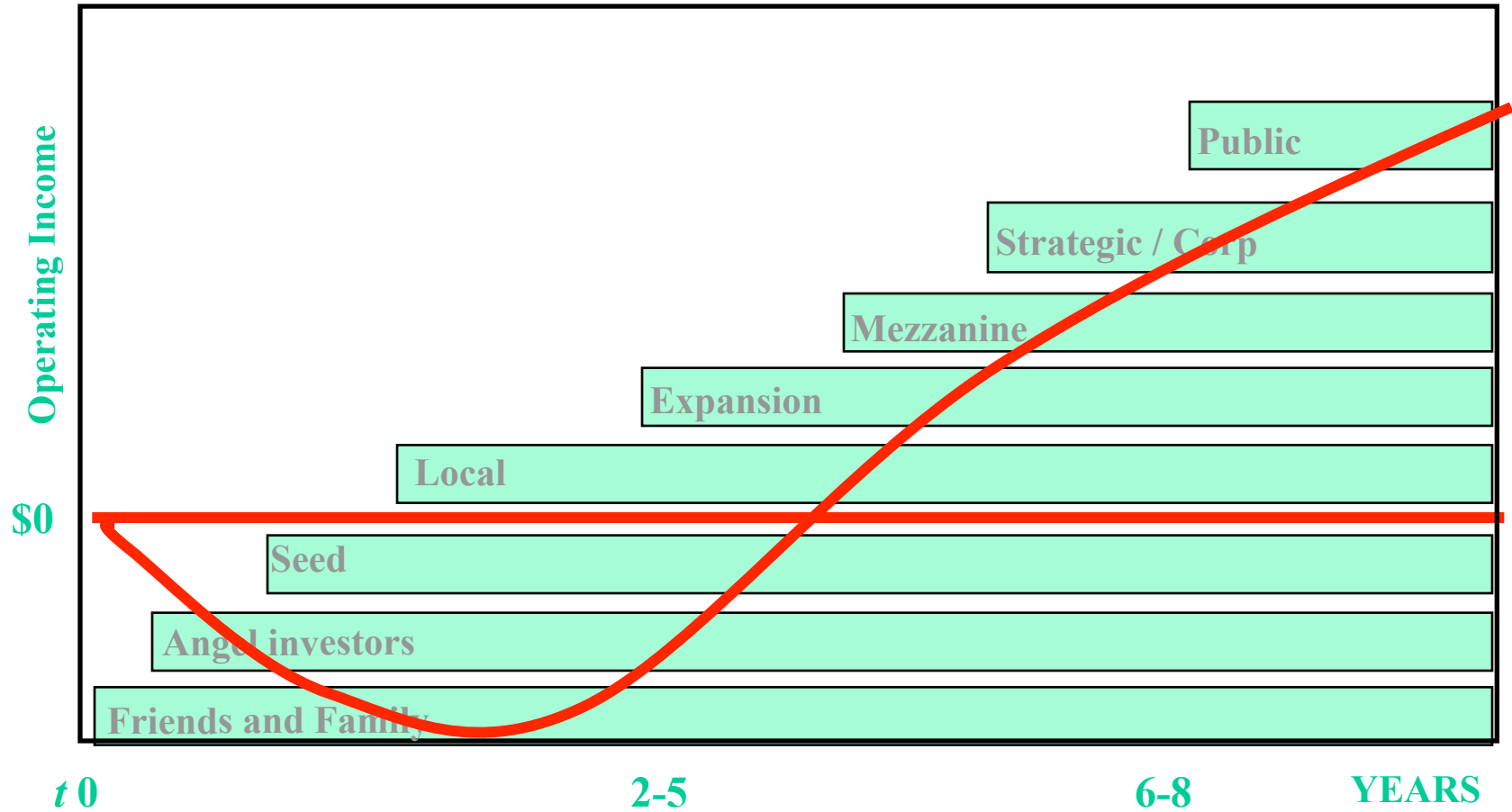
Kilde: Smarter Ventures, FT Prentice Hall, 2003

# Sources of capital - equity

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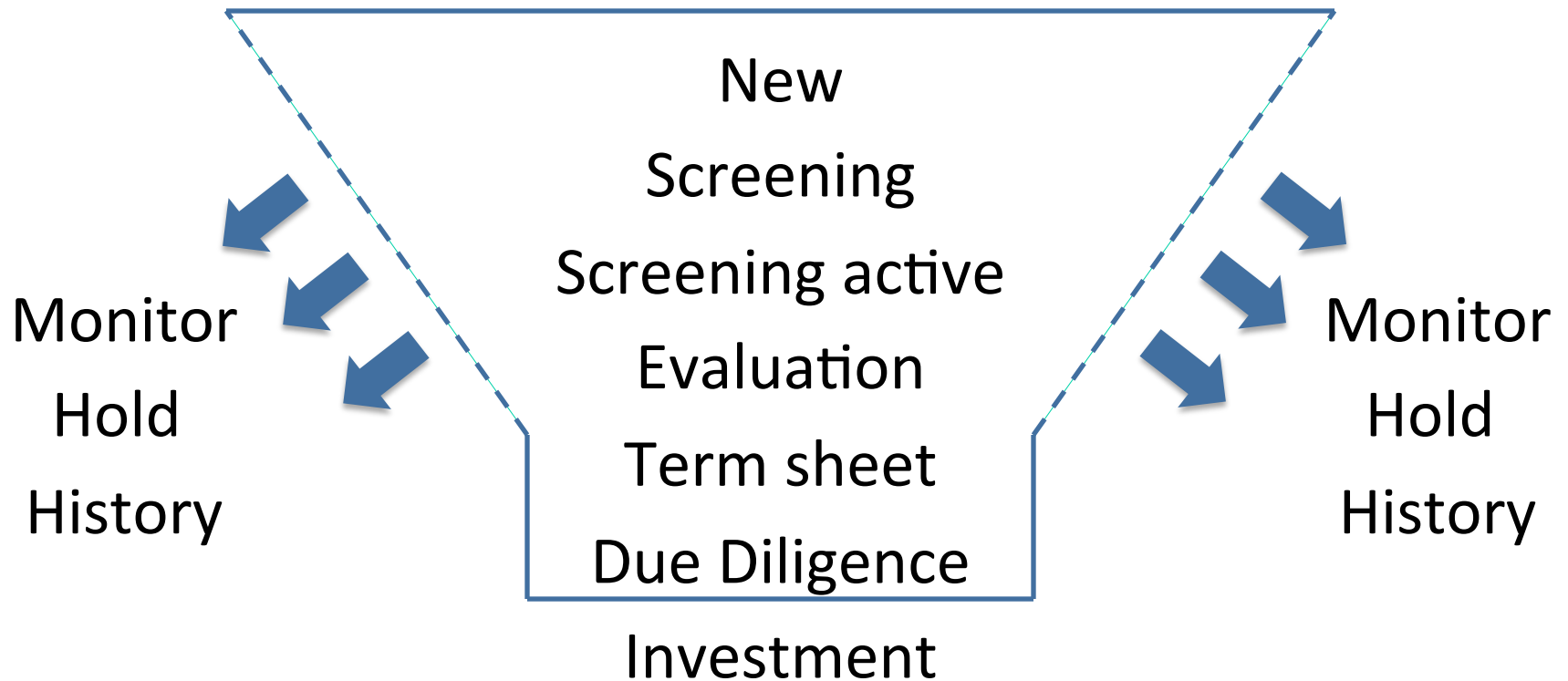
- In general:
  - Equity
  - Loans – generally not available for start-ups
  - Soft funding – important supplement
  - Revenue, profit
- Equity sources for start-ups:
  - Own team
  - "FFF" (friends, fools and family)
  - Rich persons
  - Professional investors / Business Angels
  - Seed Funds
  - Venture Capital Funds
  - Established companies/industrial investors

# Funding stages



# Process for evaluation and decision

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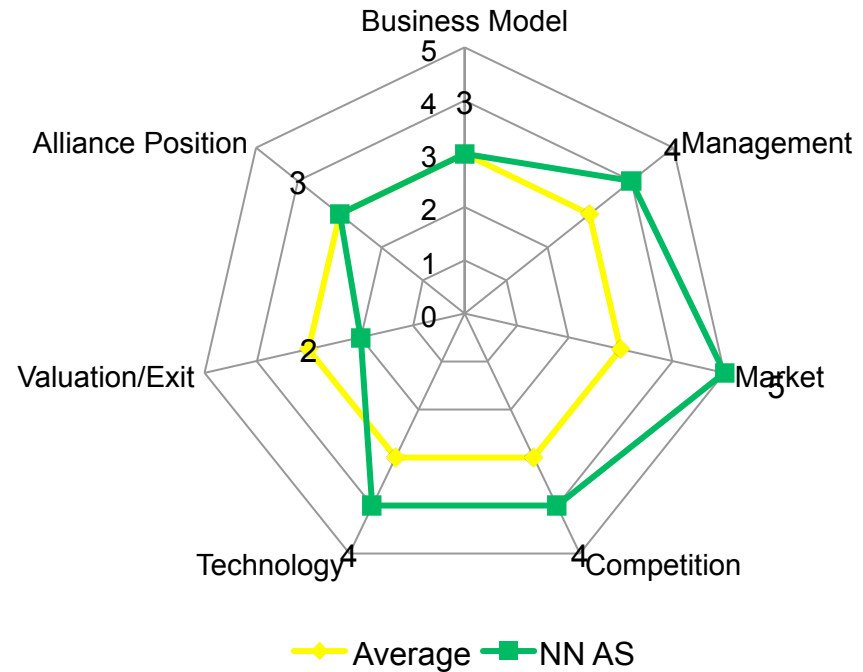


*Supported by tools*

# Dimensions

- Business Model
- Management
- Market
- Competition
- Technology
- Valuation/Exit
- Alliance Position

## Evaluation mapping





# Dimensions – Business Model

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- Business Model
  - Scalability
  - Risk
  - Upside
  - Cash flow/ burn-rate

# Dimensions – Management

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- Management
  - Management strength
  - Technical competence
  - Strength and weaknesses

# Dimensions – Market

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- Market
  - Market potential \_ TAM (Total Adressable Market)
  - International potential
  - Cultural/language independence

# Dimensions – Competition

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- Competition
  - Competitive landscape
  - Competitors
  - Unfair advantage

# Dimensions – Technology

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- Technology
  - Level of technology
  - Products
  - Protection/ patents/ uniqueness

# Dimensions – Valuation/exit

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- Valuation/exit
  - Pricing
  - Alternative exit scenarios and potential

# Dimensions – Alliance Venture position

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- Alliance Venture position
  - Portfolio focus for Alliance
  - Can Alliance contribute?
  - Alliance position
  - Alliance influence

# Portfolio goals Alliance Venture

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- Potential for 5-10 x investment
- Minimum ownership and value potential: 20%, 30 MNOK
- Can the team deliver, should it be strengthened?
- Good working relationship – “coachable”
- Strategic exit potential
- Differentiation/protection (“competitive advantage”)



# Quantitative methods for Choosing Projects

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The difference between the present value of cash inflows and the present value of cash outflows. NPV is used in capital budgeting to analyze the profitability of an investment or project.

NPV analysis is sensitive to the reliability of future cash inflows that an investment or project will yield.

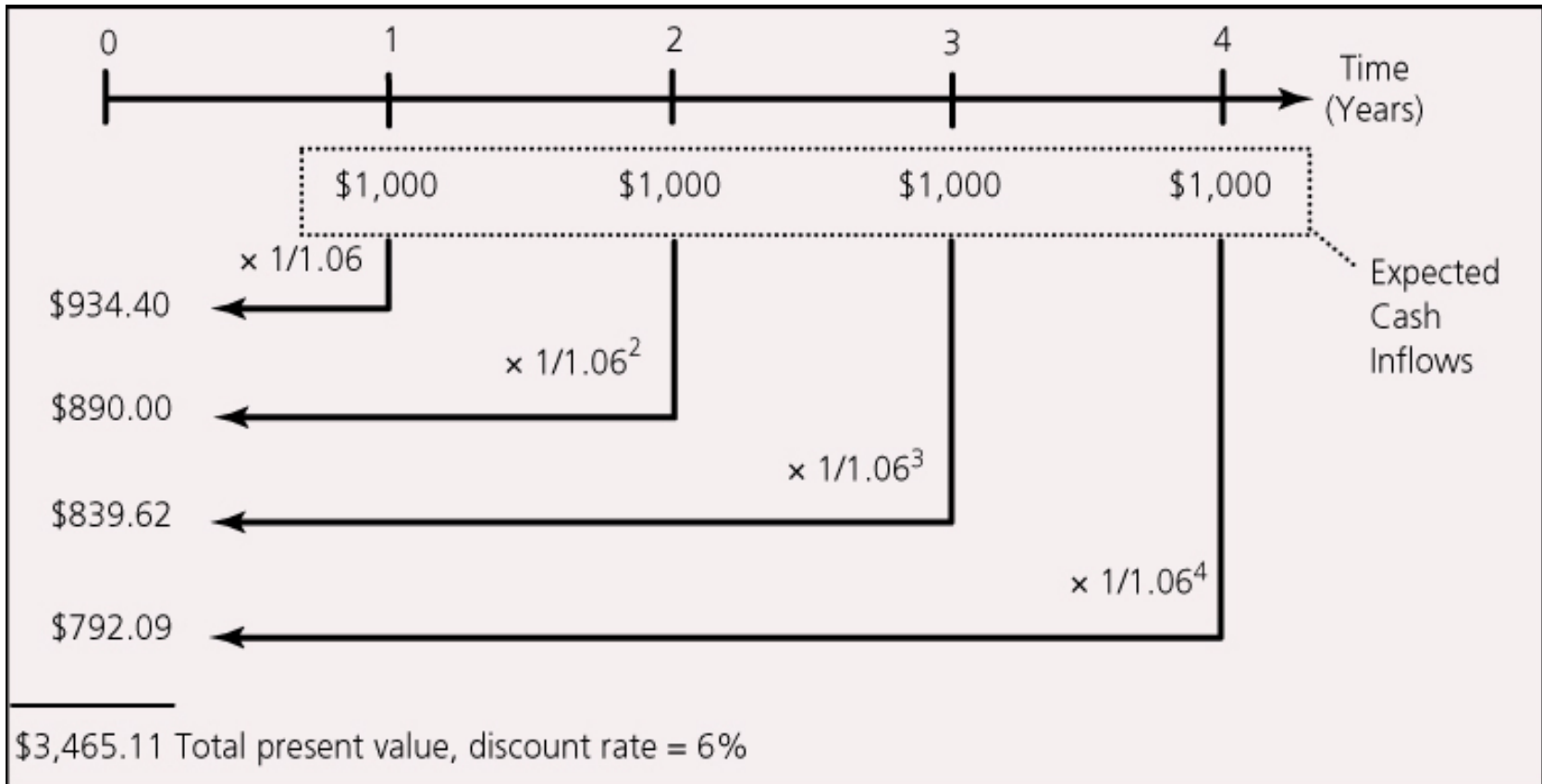
Formula:

$$NPV = \sum_{t=1}^T \frac{C_t}{(1+r)^t} - C_0$$

In addition to the formula, net present value can often be calculated using tables, and spreadsheets such as Microsoft Excel.

[NPV](#)

# Net Present Value (NPV)



# Internal Rate of return (IRR)

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IRR is 'The discount rate that makes the net present value of all cash flows from a particular project equal to zero.

Typically, a VC invests a number of tranches initially, then develops the company over a few years before it is sold, Possibly with an earn-out element.

33% Investment year 1	-4000
Investment year 2	-6000
Investment year 4	-3000
Exit year 7	21000
Earn-out year 8	4000

# Investment process – Term sheet & Due dil

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- Legally non-binding LOI
- Strong commitment to invest...
- ...providing Due diligence process
  - Legal
  - Technical
  - Personnel
  - Financial
  - Patents

# Investment process – Venture terms

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- Term-sheet will outline principles and mechanisms for:
  - Valuation (pre/post)
  - Size of investment
  - Lock-up of key personnel
  - Drag and tag
  - Redemption
  - Liquidation preference
  - Anti-dilution
  - Board representation
  - Conditions for closing

# Investment process - closing

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- Term-sheet will be "translated" into:
- SPA (Share purchase agreement)
- Shareholders agreement

# Shares

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- A unit of ownership interest in a corporation or financial asset.
- Price
  - Nominal value
  - Market price
  - Difference (market price-nominal value) can be used by company for development
- Share issue
  - Pre/post
- Valuation
- Terms, classes, voting rights....

# Example:

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- A company has 10.000 shares
- Nominal value is 10 kr
- Total share capital is 100.000 kr (legal minimum in Norway)
- Investor is offered 20% of company for 200.000 kr.
- Pre-valuation: 800.000
- Post-valuation: 1 mill
- 2.500 new shares are issued at price 80 kr.
- Surplus 70 kr.
- Founders are diluted in %, but the company gets  $2500 * 70kr = 175.000$  for development



# Why VC?

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- Share risk, limit responsibility
- Foundation for raising more/other capital
- Active partner, network
- BUT:
  - Specialized financing
  - High growth companies with international ambitions
  - More important to conquer a market, than to keep control
  - If you accept VC you will be a minority shareholder (but possibly a rich one ;-)

# What does it "cost" to use VC?

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- 90% of companies declining an offer for VC money are bankrupt after 3 years
- Approx. 1/3 of total listed company value in the US are created by VC-backed companies
- VC-backed companies grow faster, get to IPO faster, and have better results
- BUT:
  - Exit
  - Portfolio considerations
  - Does not "throw good money after bad money"

# When should entrepreneurs seek VC financing?

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- Not too early
  - Too strong dilution
- Start of growth phase
  - Product portfolio
  - Paying customers
  - Start of internationalization

# Choosing an innovation project

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- Large potential market, global
- Game-changer/distruptive
- Scalability
- Unfair advantage
- Your team can do it
- Customer-driven development