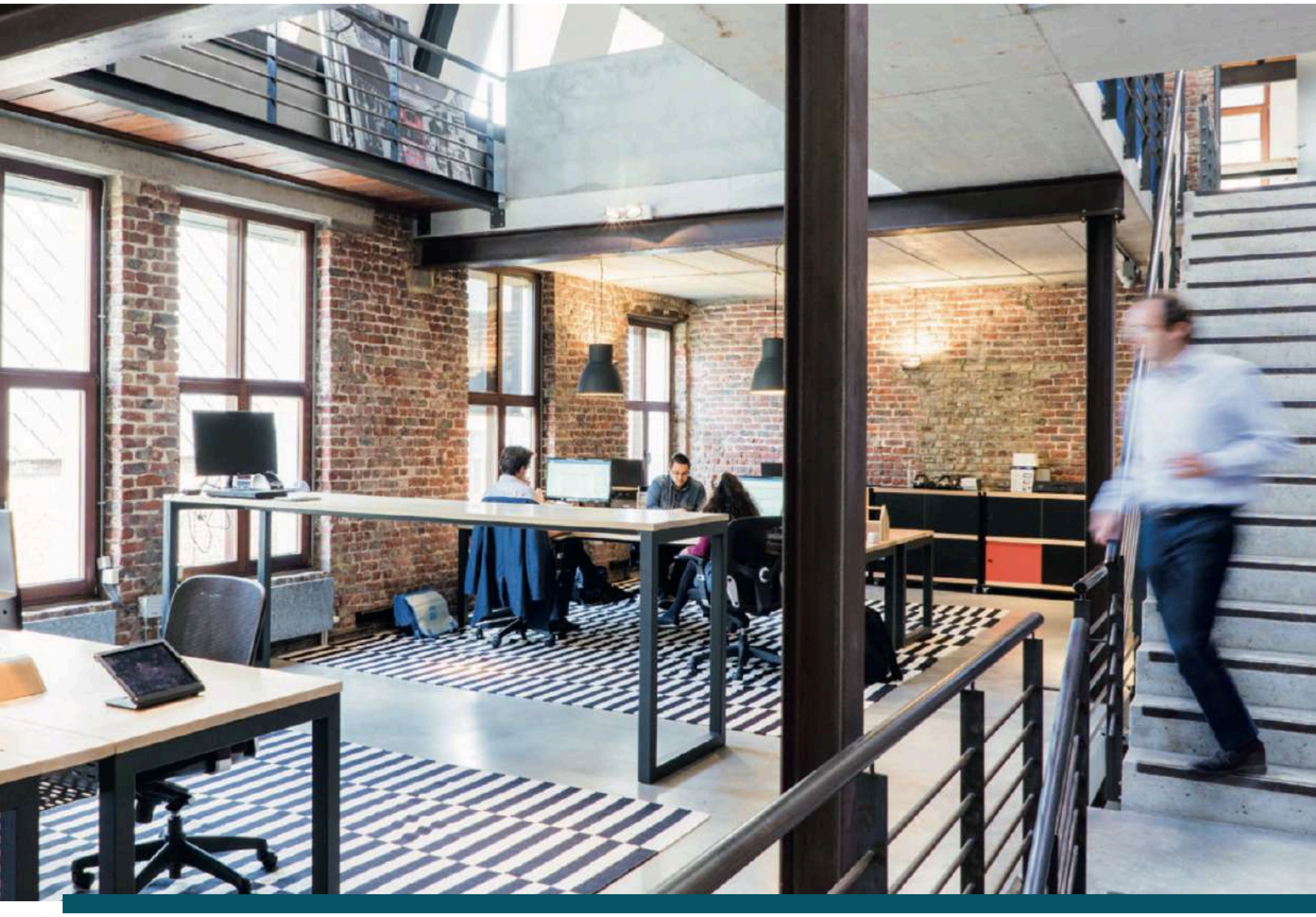
LATE-STAGE VENTURE INVESTING

The Essentials You Need to Know



STABLETON

LATE-STAGE VENTURE INVESTING

In the current market environment, making a decent risk-adjusted return in traditional asset classes has become rather tricky. Startups are looking to commercialize business models of the future, with promises for new inventions, innovations, and technology that stands to change the business landscape forever. As the Coronavirus wreaks havoc on worldwide economies, now is the time to invest in those companies that have set out to look beyond the current market uncertainty.

CHALLENGES FOR INVESTORS INTO STARTUPS

- Problem #1: Investing very early in a startup can either be impossible, risky, or difficult to analyze or any combination of those factors. Early startups are at an idea stage, which means valuations are nearly impossible to specify. After all, the focus is on potential growth, and not yet on actual profitability. Which means there are few significant numbers to base investment decisions on.
- Problem #2: Investing at or post-IPO could resemble partaking in a Russian Roulette. The IPO valuations can be sky-high, often with a post-listing dip that has nothing to do with the firm, but rather, the overall exit market.

Therefore, there must be a strategic investment window in which one can reap most of the benefits of startup investing but with the least amount of risks and challenges.

PRE-IPO INVESTING AS THE SWEET SPOT FOR VISIBILITY AND PREDICTABILITY

There's that sweet spot, known as the pre-IPO investment, where one can gain visibility, and with that, increased predictability, yet being spared the public mayhem and oversubscriptions that come with it. In other words, investing in growth equity positions of late-stage startups, who have a clear path forward to going public, reduces the risk compared to early-stage investing.

BIGGEST HIGH-POTENTIAL COMPANIES ARE STILL PRIVATE

The challenge is identifying when this pre-IPO time is right, as well as getting access to the startups during this critical time. Some of the biggest companies in the world, like Robinhood and Airbnb, are still private. If one could gain access to their equity before an IPO, the payout potential could be enormous.

DIGITAL BUSINESS MODELS ARE HERE TO STAY

Today, more than 4.5 billion people use the internet which causes several business models to profit from it:

Platform businesses could now reach a breakthrough even faster due to the current global situation. A lot of companies with intrinsically digital business models are still private. This fact holds enormous potential for those with access to pre-IPO investments.

THE UNIQUE APPEAL OF THE DIGITAL PLATFORM BUSINESS MODEL

In the area of the digital platform business model, there is a concept called "harnessing spillovers" which helps to grow the volume of interactions rapidly. For example, an e-reader issues book recommendations from past purchases and thus creates value for other participants, who, in turn, consume more. We can assume that this dynamic is a sign of a strong network effect amongst interactions of the same type.

As we are increasingly going digital, whether it be just for buying or even reading online, this effect becomes even more relevant. It is likely to boost sales and revenues. One can expect the same effect to benefit providers of digital education, another highly scalable business model that relies on strong network effects.

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OUTPERFORMING TRADITIONAL INVESTING

Late-stage investing still provides one of the best risk-adjusted returns on the market, if you have the chance to get a foot in the door. Late-stage venture investing delivers increased predictability and visibility which often leads to a future IPO.

THE RATE OF RETURN ON VENTURE CAPITAL

"...the mean return on VC investments is 57 percent per year, still very large but less dramatic than the 700 percent mean before correcting for selection bias*. VC investments are still extremely volatile, with an annual standard deviation of about 100 percent. This is much greater than the roughly 10 percent standard deviation for the S&P-500 in the same period, but similar to the volatility of small publicly traded NASDAQ stocks."
– National Bureau of Economic Research (NBER)

To summarize this study by John Cochrane, an NBER Research Associate, the returns on pre-IPO & late-stage venture investments are nearly six times higher than returns on the S&P 500 with about the same volatility as small NASDAQ stocks.

IPO VALUATION

According to The Motley Fool, over 60% of 2019 IPOs were trading (in January 2020) above their issue prices. While that sounds great, it also means that 40% all IPOs in 2019 lost money, some of them epically:

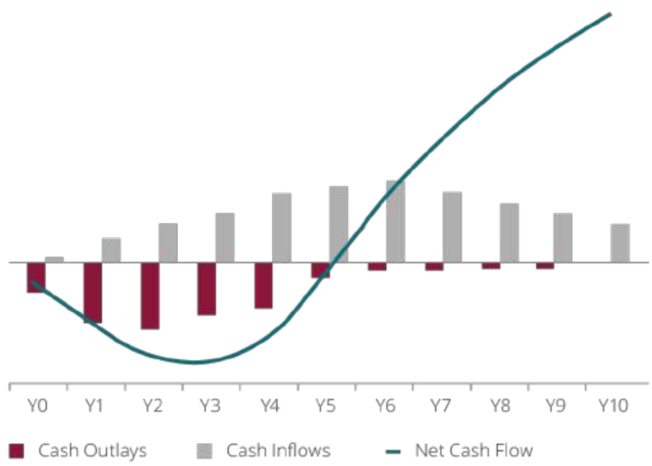
- Super League Gaming: IPO at $11 in February of 2019, it was trading at $2.90 on April 20, 2020.
- Sonim, a company that manufactures rugged phones: IPO at $11 on May 10, 2019, this stock is now trading at $0.84 (4/20/20).

The problem that IPO valuation has is that it often cannot account for the very fickle stock market. Some IPOs offer products that are popular and successful, but the stock market doesn't know how to handle them. They end up being very low priced simply because investors aren't sure. One of the greatest assets of late-stage investing is that it's a lot less about hype and "the talk on the street" and more about proven successes and data. Investors look at the offerings with clear eyes and decide if the investment has value as a business, not as a stock investment. Successful late-stage investments often reach the pre-IPO stage after 1-2 years and then finally go public after its final private financing round.

HIGH RETURN WITH MODERATE RISK

The key to return in late-stage venture investing is that the investment comes in a very late-stage of value creation, often a bit before the stock finally goes public. An investor at this life-cycle stage can still capture some of the risk premiums that a private company investment brings along and is still enjoying a high upside potential in the form of a potential IPO but without the level of risk that early investors incur when these projects are in their infancy and subject to rapid collapse. These late-stage venture investments are done when the product-market fit has been confirmed and often there is already moderate sales activity.

MANAGING THE CURVE



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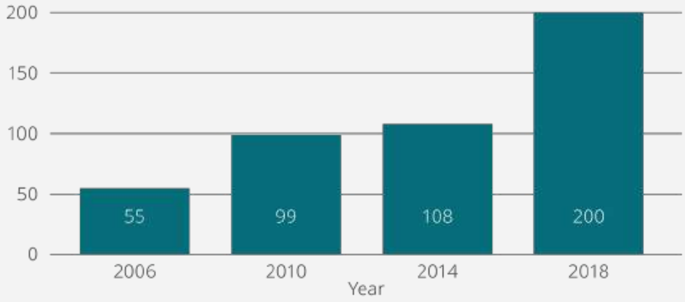
VENTURE INVESTING HAS GONE MAINSTREAM

Family offices and institutional investors have integrated venture investments into their portfolios. Some have even started to build internal teams specialized in the segment. And large, established companies have increasingly moved from funding internal research & development departments to partnering with startups to drive innovation in their field.

VENTURE INVESTING CREATING SIGNIFICANT PRE-IPO VALUE

Recent years have seen a lot of capital flowing into the venture space. This capital allows startups to develop better products faster, grow their revenues quicker and become more valuable before they decide to go public. For example, the median revenue at the time of the initial public offering (IPO) has quadrupled between 2006 and 2018. This also means that a larger part of the value creation is taking place in private markets now, leaving only limited upside for traditional equity investors.

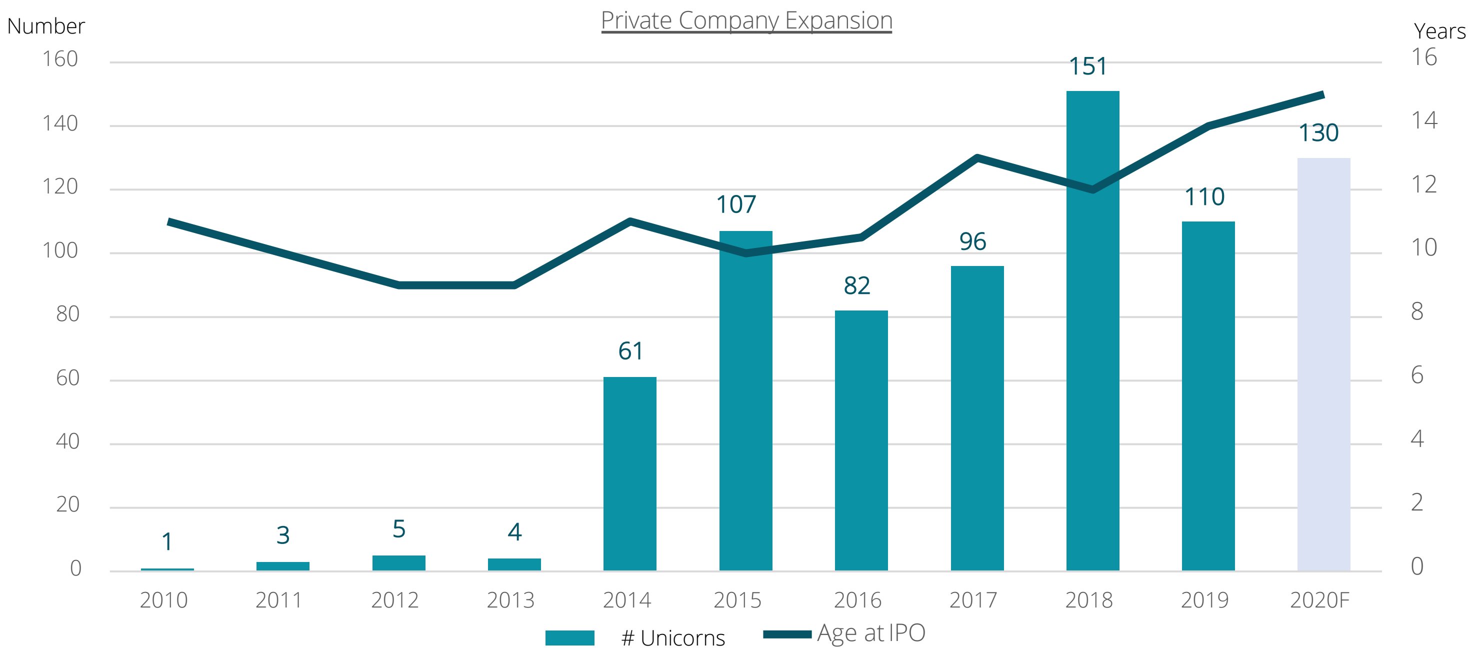
MEDIAN REVENUE AT IPO HAS QUADRUPLED IN 12 YEARS



Source: tomtunguz.com

RISE OF THE UNICORNS: COMPANIES ARE STAYING PRIVATE LONGER

The 558 companies valued as unicorns in 2019 share a cumulative valuation of $1.9T while average age from inception to IPO has surpassed 14 years.



STABLETON AND LATE-STAGE INVESTING

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We're on a mission to provide investors with pre-IPO opportunities, and the tools to access them efficiently. By enabling low investment minimums, the diversification that is essential for such investments is much easier to accomplish.

WHY INVEST WITH US?

Investors can access, choose, and create their own custom alternative investment portfolio across any asset class. Investors buy these bankable products with low minimums and improved liquidity at any bank for themselves or their clients. We take all the hassle away from the clients through our complete offerings. For providers, we significantly expand their reach to thousands of pre-screened qualified investors.

OUR EXPERTISE

Stableton Financial AG is a rapidly growing smart financial technology company. Stableton's alternative investment Fintech platform is Europe's leading gateway for qualified investors and financial advisors seeking access to world-class absolute return and alternative investment strategies such as hedge funds, startups, alternative lending, and real estate. We combine financial technology, deep investment know-how, structuring expertise, an innovative distribution platform and an intelligent sourcing engine to innovate and disrupt a USD 21 trillion market opportunity.

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ANDREAS BEZNER, CFA
Co-Founder &
Managing Partner

KONSTANTIN HEIERMANN
Co-Founder &
Managing Partner

CARMINE MEOLI
Co-Founder &
Investor Solutions

VINZENT ZERNER
Co-Founder &
Business Development

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Marketing & PR

RAFAEL ZANONI
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GET IN TOUCH

Stableton Financial AG
Poststrasse 24 CH-6300 Zug
Phone +41 41 552 59 00
info@stableton.com
www.stableton.com

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