



Inside Argentina's Private Equity, Venture & Seed Capital Industry

ARCAP

Asociación Argentina de
Capital Privado,
Emprendedor y Semilla

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This is an abstract of the study that will be
shortly available in its entirety at

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Letter from the President

The development of innovative companies in our country is not a transient phenomenon. It is the result of the intense activity carried out by a new generation of businessmen—entrepreneurs—who think outside the box and use new technologies and new business models to create companies that seek to solve multiple issues or deficiencies in both our country and the region.

However, entrepreneurs are just one side of the coin. Because for startup companies to be able to test their business models, grow, and develop at different levels funding is needed throughout all these stages.

In that sense, the streamlining and growth of the investment ecosystem in Argentina has become the essential factor to drive the creation of a virtuous circle of sustained growth in our country.

In addition, we are extremely lucky to have excellent human resources available that, throughout several decades, have proven their ability to build impactful and sustainable companies with a regional—and sometimes global—outreach.

There are several examples of that included in this report, as well as testimonials from the founders of these companies, which were founded in the late 90s and early 2000s and today are among the largest quality employment generators, creating opportunities across all social classes and setting the example for the new generation of businessmen.

It is important to stress that these new companies, supported by private funding and by the legal provisions necessary to facilitate their development, can become instrumental in increasing overall productivity, consumption, and formal employment.

Similarly, the activity of investors will become more dynamic as long as they find a clear economic policy that provides legal certainty and offers incentives oriented towards such purposes. The recently promulgated Entrepreneurs Law 27349 is a perfect example of this, as it offers plain

and simple rules to create companies while at the same time it establishes incentives for the investors funding them, among other provisions.

Thus, at ARCAP, as part of our objective of developing the investment market in Argentina by facilitating the arena for more local investors to decide to invest in the country and attracting international investors with the opportunities offered by this new generation of companies, we considered it was essential to generate proprietary and reliable information on the Private Investment market in Argentina. Until now, this information was limited, scattered, and, therefore, impossible to consult so as to assess the evolution of the market and make decisions based on reality. That is why we decided to develop this report throughout this year.

Although there is still much work to be done in terms of investments in companies created in our country, both in terms of transaction volumes and availability of instruments, the outlook is very promising. This greater foreseeability will attract local and international LPs to invest in local funds and/or directly in companies that have the potential to obtain extraordinary returns while being innovative and impactful.

In short, we believe that the future will belong to purposeful investors who want to invest in companies that generate economic, social and environmental impact.

A handwritten signature in black ink, appearing to read 'Marta Cruz', with a stylized, cursive script.

Marta Cruz

President
ARCAP

November 29th, 2017

Methodology

This report provides an overview of historical trends in fundraising and investment among private equity (PE) funds investing in Argentina, including Venture Capital (VC) and other types of early stage investment. Most of the statistical data included in this report is based on the S&P Global Market Intelligence's database of funds and transactions. All data sets are based on information gathered from websites, press releases and trade publications of relevant firms, as well as from communications established with industry participants. The overview covers the time period

ranging from January 1989 to December 2016.

The private capital activity reflected in this report is mainly that of various investment firms, each one of them with their own set of goals, preferences, and investment strategies. Yet, all of them have provided working capital to target companies to nurture their expansion, new product development, or the restructuring of their operations, management, or capitalization table. Among the most common investment strategies in private capital transactions, two main classifications are worth highlighting. On the one hand, Private Equity Firms, typically involved in buyout transactions, seeking significant equity stake in an existing or matured company. On the other hand, Venture Capital Firms, by means of which investors usually invest in young emerging companies (startups) through incubation/acceleration services, seed funding, or growth capital transactions, rarely acquiring a majority interest.

Three main firm statuses are shown in this report to reflect the evolution of private capital and its current status in Argentina. In conjunction with S&P Global Market Intelligence, ARCAP breaks down firms into Active, No Longer Investing and Out of Business (OOB) statuses. 'Active'

refers to firms in operation and fully committed to their investment standpoint, seeking new business opportunities. 'No Longer Investing' refers to firms that are not incorporating additional companies to their portfolios, but are still actively managing their current investments. Finally, 'OOB' refers to any firm that has been completely liquidated and/or has ceased operations permanently. The 'OOB' status has been determined as per information from public disclosures and, in certain cases, on proprietary S&P Global Market Intelligence's criteria and methodology, validated by ARCAP.

The charts showing Deal Volume and Deal Value per year in Argentina have been defined considering the type of investor—in terms of their preferred investment stage—involved in the buy side of the transaction. Fundraising totals reported herein reflect only official closes (interim and/or final) as disclosed in public sources and by the firms themselves. Capital commitments accrued prior to official closes are not included.

The Total Deal Value chart included in the report reflects the total equity amounts for transactions in which financial details have been reported. In the case of both fundraising and investment data, the amounts

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have been verified through sources available at the S&P Global Market Intelligence platform. Any discrepancies between the aggregate statistics published by ARCAP together with S&P Global Market Intelligence and the constituent data files may be attributed to confidential information omitted from public reporting.

S&P Global Market Intelligence industry classification is based on both the S&P/MSCI Global Industry Classification System (GICS) and the S&P Global proprietary classification, to expand the GICS and achieve greater granularity. GICS is the global standard for categorizing companies into sectors and industries. It was developed to address the need of a global financial community for a single, complete and consistent global set of sector and industry definitions, thereby enabling asset owners, asset managers, and investment research specialists to make seamless company, sector and industry comparisons across countries and regions. We constantly strive to gather as much information as possible to better reflect the current situation of the PE/VC industry in Argentina, thus our data may undergo adjustments year over year. This is due to several factors, and the most significant one is related to the increased

availability of public information over time, so we continuously add historical data on investments and capital raised from funds we did not have record of before.

The statistics included under the Seed section of this report were produced by the Latin American Observatory of Entrepreneurial Financing (OLFE), Universidad Austral, based on a data set on the seed activity of investors within the entrepreneurial ecosystem in the country. In this case, by investors we mean accelerators, incubators, angel investors, angel clubs, and venture capital firms with seed funds, provided there is public information available on their

activity, and/or data reported in commercial third-party databases. Public information refers to databases/specific web platforms such as Crunchbase, AngelList, and other similar specialized sites, websites of relevant organizations, and public press releases. We have completed this information by means of telephone interviews. This data does not include nascent companies or small enterprises that have received private capital but maintain such information strictly confidential. The Seed section also excludes Argentine startups that have raised funds abroad. Further details can be found in the corresponding chapter.

Executive Summary

The development of the Private Equity and Venture Capital industry has a critical role in the emergence and growth of new companies, thus in overall economic growth as they become sources of job creation, and it has proven to have a direct impact on economic development and poverty reduction. This report provides an overview of the trends in this industry particularly in Argentina, and its goal is to review the recent history and current situation of not only the Private Equity (PE) and Venture Capital (VC) industry but also of other specific related arenas, such as

Corporate Venture Capital (CVC), Impact Investment, and Accelerators, Incubators, and Angel networks and clubs as the emerging actors in Seed Investment. The report also seeks to provide a brief overview of the recent developments in the legal and regulatory framework, as well as of policy-related initiatives in place, which are currently reshaping the sector.

The overview starts by introducing and analyzing summary statistics and trending patterns, which, in some cases, were collected specifically for this report. This is particularly valuable as access to and validation of relevant data had remained an outstanding issue yet to be addressed, despite the significance of the PE / VC industry. In the case of this report, this challenge has been tackled with the joint efforts of ARCAP, S&P Market Intelligence, and the OLFE (Latin American Observatory of Entrepreneurial Financing). The report combines aggregate data with in-depth analysis of a selection of leading cases, such as the PE investment of Victoria Capital in Peñaflor and of Linzor Capital in Hoyts and the VC financing experience behind the growth of MercadoLibre, Globant, OLX, and Despegar, among other selected cases. Finally, the report also features the opinion of many key players,

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specifically interviewed for this report. Testimonies include renowned fund managers, accelerator managers, expert lawyers, and policy makers such as representatives of international development banks. Their testimonies further expand and enrich the various topics reviewed.

The following are some key topics worth highlighting, which shall be developed further throughout the report:

- In its recent history, the country has experienced two major expansionary cycles in its overall investment activity. The first one of these expansionary cycles was the sound development of the PE industry that took place during the 1990's, but ended abruptly in 2001 as the country experienced one of its worst macroeconomic crisis. In the 15 years following the crisis, investment activity by PE firms fluctuated back and forth but the sector has never fully recovered since then. The second expansionary investment cycle

The second expansionary investment cycle concerned the early-stage arena within the VC industry. It started around 2005/06, grew importantly after 2010, and peaked in 2014

concerned the early-stage arena within the VC industry. It started around 2005/06, grew importantly after 2010, and peaked in 2014. This boom was also spiced by the raise of new early-stage investment and incubation models such as the Accelerator Programs. Although this boom appeared to slow down in the year that followed (2015), the outlook for the market brightened with the new administration that took office in December 2015. Since then, a number of policies have been implemented in the country, resulting in international attention and improved overall expectations of most local players.

- Currently, there are 31 active fund managers in Argentina. This total is comprised by 10 active firms specializing in PE, 3 hybrid investment firms involved in both early and mature stages—PE and VC stages—, 12 active private equity firms purely investing in VC stage, and 6 seed-stage funds, including incubators, accelerators, company builders, and micro-VCs. The number of fund administrators, or General Partners (GPs), have doubled in the last 10 years—in line with the positive trend mentioned above—and this growth has been concentrated in VC and seed funding, while PE funds are relatively stagnant. It is important to note, however, that direct

investment in mature-stage companies is not necessarily aligned with said trend in PE funds, since only approximately twenty percent of sponsors raise funds, and the majority makes non-intermediated investments—run through balance sheets, a third company, or an alternative investment vehicle.

- Fundraising for PE and VC funds is collected mainly from foreign investors. Foreign participation represents nearly the totality of investments in the case of active PE funds and close to 70% when it comes to VC funds. The composition of these investors (also Limited Partners, or LPs), include foreign funds of funds, international development banks, endowments, and foundations. Development banks—such as FOMIN-IADB (Inter-American Development Bank), IFC-World Bank, and CAF (Andean Corporation)—have also proved to play a critical market development role. The prevalence of foreign investors in fundraising explains to a large extent why trends in overall investment activity are still greatly influenced by the international state of affairs and by the ability of the local market to become globally competitive and attract international investors.
- Sectors traditionally chosen for PE investment have included

consumer staples, infrastructure, oil and gas, renewable energy, mining, agribusiness, knowledge-based services, and financial services. VC has expanded to these sectors and many more, yet it still shows a great concentration around the information technology (which secures approximately half of the investments). The country's growing trend in smartphone penetration, high-speed Internet connectivity, and e-commerce penetration, create an exciting ground for entrepreneurs and VCs to thrive, and is highlighted by experts as a true opportunity for technology disruption in FinTech, AdTech, EduTech, E-health, Big Data/AI/Machine Learning, Cloud Services, IoT/Smart Cities, Entertainment (Games, VR/AR, etc.) and e-commerce. Such disruptions are expected to have a huge impact in traditional sectors such as agriculture and education, among others.

- Over the last five years, a significant growth has been registered in terms of seed capital and early stage investments, in a variety of forms and shapes. The Corporate Venture Capital (CVC) sector is an example of this growth. CVC has witnessed a significant upturn in the last five years, accounting for 149 deals disclosed and an aggregate total value of approximately 22 million USD. Again, in this case, the

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highest peak was experienced in 2014, with more than 40 investments. Nonetheless, seed capital investors encompass a variety of business models and vehicles that combine investment with advice, support, and networking, to only name a few dimensions.

- Estimates for seed capital financing also show that the activity peaked in 2014, declined in the last three years, and is estimated to start a recovery period and to reach at least 80 closed financing rounds during 2017 (accounting for more than

150 million USD). Estimates also suggest that nearly half of the financing rounds closed in the 2011-2017 period were led by accelerators. Seed funds also come from incubators (21% of total rounds), angel clubs (15%), and venture capital seed funds (13%). In terms of amounts, the average rounds reach nearly 50,000 USD, but there is also significant variability, with a third of the rounds closing at or below 25,000 USD, and another third of rounds closing at or over 165,000 USD. A large number of these rounds are closed using convertible notes or similar convertible agreements such as Simple Agreement for Future Equity or SAFEs.

In terms of the environment for doing business in the country, such as with respect to the regulatory and legal framework or the current policy agenda, the following aspects may be highlighted:

- As mentioned above, the new administration has been implementing a number of reforms that have already raised the expectations of local market players and attracted international attention. These reforms are refreshing in a country that has been perceived, by many measures, to have deteriorated its investment environment throughout the 2002-2015 period.

- Among the reforms, the promulgation of the Entrepreneurship Law in April 2017 intends to create the conditions to continue developing the entrepreneurial finance market in the country and to attract seed and early stage investments to tech-based Argentine startups.

- Other noteworthy regulatory changes are the simplification of the company incorporation process for startups and the creation of a new special legal vehicle for startups. Other measures include a number of tax-exemptions for startup-related investments, the regulation of crowdfunding, the creation of a registry of startup capital-related institutions, and a number of provisions on the role of the national government in direct investment initiatives in these institutions.

- In what can be understood as a regional trend, the government is increasingly active in developing investment vehicles for entrepreneurial financing. The National Trust Fund for Entrepreneurial Capital (FONDCE), which was created within the framework of the previously mentioned Entrepreneurship Law, promotes tax incentives for investment in entrepreneurial ventures, early-stage loans, and other

means of support for new business creation in Argentina. FONDCE will be comprised by 10 funds, 40% of which account for public investment. The funds will have a minimum of 30 million USD each and will be run by private fund managers who will be responsible for selecting the projects to be invested.

- The government is also currently introducing a program to directly support accelerators, including non-refundable funds for operating expenses and funds to be used as co-investment in startups.

- The opinions of the market players expressed in this report generally agree with the view that the reform agenda of the current administration is rapidly improving the investment environment. While investors continue to pay attention to potential political swings and fiscal variables as sources of risk, the overall positive perception is that steps are being taken towards easing the context for doing businesses in Argentina and enforcing a framework that guarantees the rule of law.

About ARCAP

The Argentine Association of Private Equity, Venture and Seed Capital (ARCAP) is a non-profit organization aimed at promoting the development of the Private Investment Industry in Argentina. It seeks to stimulate local investment in companies with high economic, social and environmental impact that can generate high-quality employment in the country.

Since its foundation in 2009 and its re launching in 2016, ARCAP's main goals have remained the same:

- Make contributions to the growth of Argentina's economic activity through the development of the Private Investment Industry and the country's insertion in international markets
- Promote investments across different sectors in Argentina to help develop and grow the country's economy by creating and producing world-class goods and services
- Create and distribute information tools about the news and activities of the industry in Argentina, and promote the generation of statistics and research on the contribution of these investments to the economy
- Encourage the implementation of best practices with ethical and professional standards that facilitate the participation of foreign institutional investors in Argentina.
- Represent the industry and its players at local and international level in business communities, government authorities, the academic world, and the media.

ARCAP offers membership options for different industry players such as Investment firms, Family Offices, DFI's, Service Providers, Corporate Investors, Accelerators, and Angel Clubs and provides the following benefits:

- Qualified networking
- Local, regional and global representation
- Outstanding participation in ARCAP's digital channels
- Inclusion in press and PR campaigns
- Participation in the industry directory
- Access to industry research studies such as publications and specialized documents
- Access to discounts for ARCAP and ARCAP's partners events
- Access to events and education programs
- Participation in frequent meetings with top industry players

Find out more about ARCAP at www.arcap.org

About S&P Global Market Intelligence

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About OLFE, Universidad Austral

The Latin American Observatory of
Entrepreneurial Financing (OLFE)

OLFE is a joint initiative of the IAE Business School and the Faculty of Business Sciences at Universidad Austral. Its objective is to develop key performance indicators to monitor entrepreneurial activity, particularly in regards to financing sources, in Argentina and Latin America.

The mission of the initiative is to generate information tools and research studies on entrepreneurial financing to increase the understanding of the phenomenon and its participants, covering all modalities, instruments, and platforms available in the market, to generate greater transparency and benefits for both entrepreneurs and funders. Objectives:

- Monitor the Latin American startups financing ecosystem.
- Work jointly with other academic institutions, regional observatories, and other key players within the entrepreneurial and financing ecosystem.
- Prepare and disseminate research studies on entrepreneurial financing.
- Evaluate the impact of public policies aimed at promoting the entrepreneurial financing market.
- Organize activities such as conferences, seminars, and round tables to promote the topic, with the participation of relevant academics and professionals.

Find out more about OLFE at

<http://www.iae.edu.ar/es/ConocimientoElImpacto/iniciativas/Observatorio/Paginas/default.aspx>

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