THOUGHT-LEADERSHIP ARTICLES BY THE GROUP 11 TEAM

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Do Androids Dream of Electric Sheep?

By Roxane Googin and Dovi Frances | June 2021

Someday a human being, named perhaps Fred White, may shoot a robot named Pete Something-or-other, which has come out of a General Electrics factory, and to his surprise see it weep and bleed. And the dying robot may shoot back and, to its surprise, see a wisp of gray smoke arise from the electric pump that it supposed was Mr. White's beating heart. It would be rather a great moment of truth for both of them.

Dick, Philip K. "The Android and the Human" 1972

Getting Past COVID: Where are We Now?

As vaccines are administered and restaurants reopen, society seems to quickly be waking up from its COVID slumber. But just like after a bad hurricane, we are emerging from our quarantine bunkers into a surprisingly altered landscape, one that will be difficult to navigate. Our old maps no longer apply to the current reality. In earlier notes we have cautioned against assuming life will be like it was just a year ago, that in fact we cannot be the same economy or society we were before spending a year locked up as we collectively digitized every business process five years into the future.

This dilemma is playing out in the current inflation/deflation debate. Why the confusion over something so basic? Why do we have record open jobs with high unemployment? This confusion puts all eyes on the Fed, with their dual mandate of maintaining price stability and maximizing employment. But not only do we not know where prices are going, we would also ask what is the post-COVID definition of a "employment"? How do gig workers get counted?

Importantly, while COVID accelerated ongoing trends as much as it created new ones, not all of those trends are positive. Despite all the euphoria, two unpleasant trends that seem to have been accelerated are sovereign debt and GDP growth concerns, along with income inequality. They are actually related. As COVID hurt GDP and relief expenses expanded our debt, our debt to GDP ratio jumped to 129%, setting off alarm bells in the debt markets.

This matters to equity holders because without healthy debt markets equity markets become unstable. Debt historians have observed that under 50% of GDP, sovereign debt can be benign, but over that amount it suppresses growth and tends to cause interest rates to rise as bond buyers begin to suspect the quality of those bonds. In keeping with this trend, between the late 1950s and the 2008 debt crisis, the debt to GDP ratio barely exceeded the 60% limit considered to be safe, and the economy grew.

However, once the debt to GDP ratio reached 100% post the 2008 debt crisis, we experienced the slowest "expansion" on record. Growth was anemic. Now, at 129% we face an even more uncertain future. The question becomes how much of a burden on the economy will our outsized debt balances become as we struggle to grow the economy and deal with the ever-present risk of a bond sell-off rising interest rates.

This dilemma goes far to answer the inflation/deflation question. As prices jump while we put new demand on COVID-quieted supply chains, the debate rages as to whether we have entered an inflationary or deflationary future. The quick answer is; yes to both.

Prices are currently being bid up for scarce resources. It could take the better part of 2021 for supply chains to equalize, especially for long lead-time items like semiconductors. But after equalization, we are hard pressed to see drivers of continued inflation other than in response to outright currency debasement. Rather, with historically depressing debt burdens, an aging population and large income disparities, (limiting effective demand), combined with continued strong efficiency gains from ongoing workflow digitization, (increasing effective supply) - a flat economic outlook holding down prices is more likely than spritely growth pulling prices up, sort of like Japan.

We believe these concerns are behind Fed Chairman Jerome Powell's continued dovish stance on interest rates and his change in focus from the inflation to the employment side of his "dual mandate."

The Abstraction Layer of Work

Compounding and interacting with the core debt to GDP growth issue are digitization and income inequality, which again go together. To understand this trend, we will review the critical importance of the abstraction layer in both computer science and in the larger economy as "software eats the world" and how this increases inequality. In software, the abstraction layer is the point at which any small task can be simply invoked by a larger task via an API (Application Programming Interface) call, rather than having to write your own subroutine. It completely encapsulates and automates a small task so that it works predictably. The beauty of this capability is that the sub-task is "just done", exactly the same each time, without errors and with high quality and predictability.

This allows the higher level organizing system to operate much more efficiently. Importantly the entire history of progress of computer science has been for ever higher abstraction layers calling on ever more sophisticated API calls, saving ever more work in the system.

This is all well and good for the system until it automates your job. The problem for workers in highly automated industries is that they are effectively subroutines. They live in a very commoditized world with strong price competition and no chance to stand out. Their job is to be part of that flawless API call and doing anything else causes unwanted upstream errors. That Uber driver will not move to a supervisor's job. That Amazon warehouse worker gets repetitive motion injuries and stress problems because they must act for hours every day like the robots that will eventually replace them. The system works better because all the random noise has been streamlined out of the lower functions, resulting in perfect wage competition of fungible parts at the bottom, in exchange for more efficiency at the top. Thus, the further we automate, the more income disparity grows.

The Airplane Analogy

Moving to the entire economy this dichotomy is a bit like landing in a plane into a rainy city. At 35,000 feet life is good; the sun is out, white puffy clouds are evident below and the air is still. This is life above the abstraction layer. As you descend, you sort of brace yourself for some turbulence as things go dark. This is the abstraction layer. A lot is going on there and it separates "above" from "below". As you further descend you enter another world, a dark, dreary one you sort of dread as rain hits your window and the blue skies become a distant memory. This is the Blade Runner world of the Amazon worker and Uber driver. You work hard but never stand out and never progress.

Importantly, as we make advance on automation the layer between the sun and the rain keeps getting higher. Ever more sophisticated jobs become subroutines in more sophisticated abstraction layers. Those jobs are usually done better with superior data and AI. You get the results you want instantly and at a better price and never get put on hold for hours trying to figure out a $200 error. In fact, efficiency jumps and errors vanish under this automation. However, as more jobs operate below the abstraction layer, fewer people operate in the sun above it. As the layer rises, those at the top get more benefit from larger economies of scale while the income divide just grows. Importantly, COVID just lifted that abstraction layer up by five years, putting ever more knowledge workers below the API layer. **The question becomes then how to grow an economy if the very automation that can improve operations enough to grow GDP also creates enough income inequality to suppress growth overall? It is like we are in quicksand.**

A Brave New World

So as we eagerly greet a new spring with shots in our arms, be careful what you wish for. While we fully expect travel to get white hot and lots of people to celebrate, not everything is rosy. We have indeed moved years into a digital future that is alien to us, and not good for everyone. Meanwhile ongoing demographic and debt burden problems have only been exacerbated COVID. We are burdened by relief debt even as an ongoing demographic slowdown just got accelerated by a loss of 600,000 extra souls and an income divide just driven wider by significant automation.

While we lost “only” 100,000 working age citizens, our working age population was already shrinking. We are back to early 2016 levels after having formed a massive top. Importantly, partying will be fun but it will not help relieve our debt burden because that growth is not productive. What will help is, you guessed it, will be squeezing ever more productivity out of the flat economy we have via further automation. But this comes at its own cost. Back in September 2020 in our “Equities Gone Wild – Bubble or Beginning” we have actually predicted what we are now seeing far clearer – **Make no mistake, after an inflation burst the trends we face are quite deflationary, placing us in an even more alien land.**

In our upcoming pieces we will seek ask our brain trust of founders and CEOs to look further out into what may be an alien land and offer their insights as to the future.

Fintech's Quantum Leap

By Roxane Googin and Dovi Frances | Jan 2021

"Theorizing that one could time travel within his own lifetime, Dr. Sam Beckett stepped into the Quantum Leap accelerator and vanished...

He woke to find himself trapped in the past, facing mirror images that were not his own and driven by an unknown force to change history for the better.

His only guide on this journey is Al, an observer from his own time, who appears in the form of a hologram that only Sam can see and hear. And so Dr. Beckett finds himself leaping from life to life, striving to put right what once went wrong and hoping each time that his next leap will be the leap home."

Quantum Leap, Opening Narration

Turning Up the Dial

If the rapid digitization of commerce brought on by COVID has moved us years into our digital future during just a matter of months, it is relevant to ask "where are we now"? While many facets of our new life have grown to seem normal day-to-day, we need to appreciate that in a post-COVID world we will actually be strangers in a strange land, operating in an environment so altered we don't truly comprehend the change. This disconnect is most evident in equity markets where certain valuations seem to have no upper bound, implying a sudden appreciation of the net present value of their future cash flows. In response to these violent moves, people are putting on their tin-foil hats and yelling "Bubble!" But perhaps, the markets are telling us something.

While excessive liquidity intended to ameliorate the economic impacts of COVID shut-downs on entry-level workers has certainly found its way instead into stocks, it is also reasonable to believe well-placed companies are indeed much more valuable than they were in January because their revenues and competitive position has suddenly strengthened. To explain this, we will review the steps, starting with how the mechanics of raising the "abstraction layer" via automation supercharges productivity. Next we will highlight how this broader automation rush should turbocharge the fintech space specifically in 2021.

While the legacy financial system is clearly entrenched, the unprecedented digitization of all operations in response to COVID is set to finally change how payments are made. When e-commerce was 10% of sales, kludgy legacy payment systems that sort of worked were acceptable. However, when that needle moves to 50% and more, slowing everything down just to facilitate an aging payments infrastructure will become unacceptable. This should become painfully evident in 2021 as we re-open to a new landscape.

The Hidden Automation Explosion

One aspect of the post-COVID landscape people seem to under-appreciate is precisely how deeply digitization will have seeped into all operations. Before COVID hit, automation was a nice-to-have business owners would get around to when they had the time. Everyone knew it was coming, but it could come tomorrow. WIth COVID, automation suddenly became what you do to stay viable. As we moved to a war-like footing, all barriers to adoption were dropped like a hot iron as manual processes had to be replaced immediately. This was evident beyond retail, including historically automation-resistant verticals like fulfillment, education, healthcare and payments. Looking forward, what people do not seem to appreciate is that once the pressure of COVID gets lifted from the economy and people try to return to “normal”, this economic landscape will be barely recognizable.

While we are all adjusting to Zoom calls and food delivery at an individual level, the combined impacts of these newly automated processes on a mass scale are sure to be profound by next summer. But operating in our little COVID bubbles, we cannot see this happening. For instance, in education once a critical mass of classes are recorded, what new revenue models could educators leverage to broaden the reach of their intellectual property? In health care, how can recorded sessions and constant symptom recording be used to track disease progression as well as to save doctors’ time? What does the novel data sharing strategy used in COVID vaccine development mean to future drug pipelines? In fulfillment, what will the learnings of this holiday crush mean for future operations? In commerce, what does the rapid expansion of e-commerce mean to access to credit and digital payments as well as to overall business efficiency?

The Automation Chain Reaction

The common ground between these sectors, as well as others that have newly automated such as agriculture and other forms of production, is that automation is not an end in itself, but rather the first step in an economic chain reaction. Importantly, we have just lit the fuse. Once operations are analyzed and made repeatable enough to automate, the next step becomes a new level of orchestration and “abstraction”, along with superior data gathering and optimization.

In computer science, an abstraction layer is the point at which a compute task can be done with an API (Application Programming Interface) call rather than by completing smaller labor-intensive manual programming steps. Economically, once a manual function gets abstracted into an API call, the system gets much more productive as all the cost and uncertainty of performing low-level manual steps suddenly vanishes. At that point, true scaling can begin. What automation does is to essentially retrofit historically variable manual steps into a repeatable equivalent of an API call that can then be scaled via a higher level management platform, erasing all the random noise that tends to jam progress. This parallel between computer science and manual operations is but another example of "software eating the world" as digitization reforms the physical world in its own image.

The Economic Shift: Winners and Losers

This one simple act has significant economic ramifications. Once a function has been simplified and commoditized to the point it can be automatically repeated, it becomes a commodity because individual efforts no longer make any difference as long as the API call works. Instantly, all manual value-add vanishes and that low-level effort becomes completely subject to the dictates of supply and demand. Indeed the whole point of automation is largely to commoditize and standardize those efforts for the sake of larger system efficiency.

Importantly, the value-add that once accrued to those manual steps moves up to the API layer, where the collective productivity improvement becomes evident. Essentially, the devaluation of the lower-level steps accrues to the vendor getting more done for less by making the API call. This is why software platforms become so valuable while the value attributed to manual business processes supporting them keeps falling. In this world, the overall economy gets more efficient as manual waste is reduced while platform owners like Amazon do better than their third party sellers and Uber does better than their drivers. It collectively hurts small businesses and / or drives income inequality in the name of overall productivity gains. COVID has accelerated this trend.

By automating business processes like their hair is on fire, businesses are collectively devaluing equipment and labor beneath a new and higher abstraction layer across the economy while simultaneously turbocharging productivity. Because this is happening everywhere and all at once at an unprecedented rate, the economic impact over the next few years will be quite significant, and if history is any guide, quite mis-understood by economists and our Federal Reserve. The true impact of this aggregate move should only become broadly apparent after we quit focusing on COVID and try to return to a "normal" life that no longer exists. This is what our markets are telling us.

The Data Imperative

But wait; there is more! Along with owning APIs and controlling downstream inputs, the API owner also gets to collect data. As we focus on COVID remediation, data collection is silently growing at an alarming pace, everywhere you look. The owner of this data gets almost supernatural powers of prediction and coordination. While even the small business that automates collects significant data in the process to the betterment of their bottom line, the eye in the sky that watches all those newly automated businesses from their platform perch gets exponentially more benefit. Data becomes so valuable, it becomes profitable in the long term to give away the core commoditized services just to collect that data. This is in a sense the business model of Google and Facebook.

The FinTech Imperative

As we all madly automate, one aspect that permeates business still holds us back. That is payments and credit, a very critical last-mile piece of the puzzle. Our financial system is largely out of the 1800s, with patches that have dragged it forward at least until 2008. But it remains a rigid, slow, data-starved and expensive impediment to conducting business as transaction costs are high, money flows are slow and credit remains scarce. As the rest of business processes automate, these weaknesses should become glaring. In a world where savings are so excessive that $17T of bonds have negative yields, it is inexcusable that up to 50% of domestic small businesses lack access to credit and that 14M Americans lack even a bank account. It is inexcusable that in a world where 50% of Americans live paycheck-to-paycheck they have to pay a 2.5% transaction fee for online purchases. Credit cards were cool in the 1960s when they first appeared, but these fees are inexcusable in a world where everything else moves at both the low cost and high speed of API calls.

In short, post COVID, financial services will need to operate at internet speed and scale, just like everything else. What we need are low transaction costs, instant transfers and smart credit availability suited to the dynamic capabilities of the borrower. Accessing these services needs to be as fast, simple and secure as the rest of the digital transactions they intermediate. In short, finance needs to move to the 21st century, and soon. Importantly, it will take a broader revolution of the order we envision to truly up-end this entrenched model.

The FinTech Cambrian Explosion

If banks and credit card companies are not adjusting to an online world, fintech vendors are filling the void. The airwaves are getting saturated with offers of friendly financial services delivered over your phone. PayPal offers free payments via Venmo with the help of Plaid, while also inching into credit with their own credit card and free multi-payment service. Affirm and Sunbit also offer instant credit at the digital and physical points of sale, respectively.

Both Stripe and Plaid reduce banks to the dreaded API call. Square offers Square Card and Square Cash. Robinhood traders are moving stocks. Everyone wants to be the next Ant Financial. Even Bitcoin is experiencing a resurgence as an inflation hedge and a sure-fire way to deliver cheap transactions at global scale. Square CEO Jack Dorsey calls it "The currency of the internet." Slowly but surely, the barbarians are gathering at the banks' gates. Money will move and credit will be offered a thousand new ways. As we step through the looking glass into an automated digital world, the legacy manual banking and credit system is getting left behind.

The True versus Fake Revolution

However, these restlessly gathering forces are peering through the fog to a currently unknown future. Like the six blind men and the elephant, they are grasping onto part of the problem as if it were the whole. The current strategy is often to replicate or extend part of the existing banking structure, but ultimately many replicate and amplify the core structure of the legacy system under a pretty new face. They use the old system as an API call while extending the reach of that system literally, through cell phones instead of branches, as well as logically, by offering new features. But at the end of the day, the result is a better version of the same product; payments and credit. Because it is recognizable, it has not truly replaced the old system to better fit a radically new present.

The Fintech Disruption

True disruption appears not as a better version of a legacy product, but as an unrecognizable offering that obliterates the old value proposition. Frequently, the output of the old system gets offered for free as just one of many inputs to the new, higher order system. This is what higher abstraction layers do. In this case we expect transactions to be immediate and free, while credit becomes a feature not a product. Instead of faster-cheaper transactions and credit, the product will operate at a higher abstraction layer using both payments and credit invisibly as part of a larger solution of managing for larger business outcomes. Instead of just getting you a loan that may turn into a problem, they will help you save, budget and retire. This new layer is what grows a TAM as it becomes a self-referential system that actually modifies its environment. In this case fintech can improve the creditworthiness of the user rather than just extending them occasional (and expensive) credit they may not be able to handle, unlocking previously stranded resources and growing the entire economy.

And yes, the data this system collects will pay for giving those transactions away instead of charging 2.5%. But in addition to offering services for free, the data these systems collect through use gives them x-ray vision into creditworthiness unimaginable in today's manual environment. They can also intervene to improve credit worthiness by changing behavior for the better, either with a carrot via nudging or gaming cues, or through a known stick via their outright ability to take a slice of cash flows. It is this magnitude of letting go entirely of a successful existing business model that makes disruptive change so counterintuitive and difficult.

Higher Level Goals

An example of this type of disruptor is Shopify. Shopify is shaping up to be a huge new fintech winner. In their quest to “make commerce better for everybody” they stand to commoditize both payments and credit as we know them as those products become tools in a larger toolbox of running a store rather than ends in themselves. Note how their goal is not to “make credit cheaper”, but rather to “make commerce better”, using both higher-level software and the data they collect. Importantly, this higher level goal enables them to attract the needed critical mass of both users and data, fueling a flywheel of growth.

Importantly, this strategy gives Shopify two critical advantages in extending credit. One, is they improve the creditworthiness of their user-base by helping them manage their business better. Two, they know everything that their customers are doing in real time, to the point they can do aggregate and individual trend analysis to predict the success of future operations with great accuracy. Compared to this, banks are flying blind as they only have a few forms, faxes and individual hunches to work from. The collective impact can be transformative.

Group 11 Investments

Group 11 has focused on fintech platforms since 2014, and now their time has come. The portfolio contains several clear platforms, as well as some growing extensions. The platforms include; Tipalti, TripActions, HomeLight, Papaya Global and Lili Bank. Extensions include; Next Insurance, Sunbit and EquityBee.

Tipalti works at such a high abstraction layer that their very name literally means “I handled it.” Accounts payable and remittance has historically been a back-office rat’s nest of manual processes, made more difficult by a lack of payments standards. By forming API-level agreements with most conceivable payment systems and giving businesses a birds-eye view of the entire process, Tipalti becomes a classic abstraction layer. From there, businesses can measure the efficacy of their payments cycle. This agility has suddenly become necessary in a largely automated world.

TripActions has done the same to travel. They have automated the painful and aggravating manual steps we all just accepted as part of booking and expensing a trip. By reducing those steps to API calls and presenting a data-filled front end to users’ phones, TripActions has brought travel into the 21st century. Rather than booking flights and hotels, TripActions simplifies travel.

HomeLight works to do the same for home buying. While home buying platforms have historically focused on improving one aspect of home buying, the overall process remains difficult. Just seeing random listings or paying lower commission does not mean a seller gets the best overall price, or the buyer finds the house they really wanted. Even finding an acceptable sale does not mean the needed cash is available. Indeed, buying a house is a multi-variable puzzle that needs to be optimized at a higher level. This is exactly what sets HomeLight apart.

Lili similarly simplifies life for gig economy workers, a group that should grow even more quickly in a post-COVID world as legacy enterprises struggle to adjust. More than a source of affordable credit, Lili becomes a “pocket MBA” by helping independent contractors manage all aspects of their business, Like Shopify, Lili addresses a larger question than “how do I manage cash flows” but rather addresses “how do I intelligently automate my entire back office so I can focus on my work.” Importantly, independent businesses, now matter how small, need all the automation of larger businesses in order to thrive. This is essentially what Lili offers.

Somewhere between a platform and an extension, **Next Insurance** both extends traditional insurance offerings via a cell phone interface, and aggregates low level options into a higher abstraction package. While the act of buying insurance remains recognizable, the process is vastly improved because they seamlessly aggregate a myriad of maddening options into one optimized and affordable offering. Importantly, the insurance industry is vulnerable for the same legacy reasons banks are vulnerable; they are expensive, slow and data-poor. In this environment, Next becomes a very important partner.

While extending credit into four easy payments at the point of sale is the new fad, **Sunbit** goes further. They help ensure the buyer can afford the transaction. Just getting instant credit can get many buyers into trouble. The Sunbit platform screens buyers for their ability to pay and has known enforcement capabilities via access to their debit card account. In this way, Sunbit moves beyond a mindless front-end that can become a trap, to actually helping critical transactions get completed end-to-end, again by altering the credit cycle — allowing over 100 million Americans access to credit for non-discretionary expenses.

A Virtual Economy Reinvention

As we emerge from COVID, we should expect much more than any return to “normal”. That world is gone. Instead, as business activity heats up in the spring we foresee a surprising lurch into a highly automated future where business becomes frictionless and intelligent. While everyone madly automated to survive COVID, what they really did was to set the seeds for a new and shockingly productive economy overall.

But one fly in the ointment remains our antiquated banking system. The problem is that the high transaction costs and poor credit offerings from this legacy system are becoming not only more glaringly evident as the rest of the system streamlines, but literally an increasingly unacceptable final impediment to progress. Financial services are supposed to grease the gears of business, not throw sand into them. To improve this situation we need to automate both the credit and payments process by commoditizing the steps then automating their sequence under the guise of a larger platform.

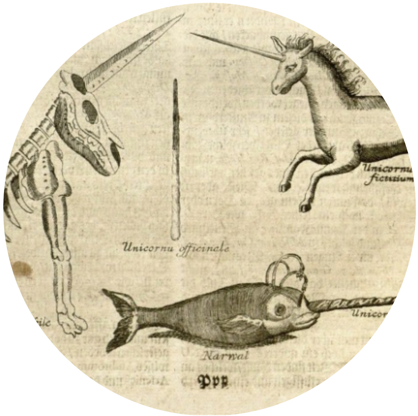
Into this gap is jumping a Cambrian Explosion of fintech companies, ranging from new front-ends to existing products, to platforms that strive to solve higher level problems. True disruption accrues to the historically unrecognizable higher level products. In the process, legacy products become commodity features rather than ends in themselves. The next generation fintech winners will solve problems like how to run a business or how to retire in 20 years. With low level task automation and superior data collection, historic imponderables become realistic solutions to the betterment of everyone.

Unicorns vs. Alicorns: Real vs. Fake Disruption
The Second Coming of Real Unicorns

By Roxane Googin and Dovi Frances | Oct 2020

"Surely some revelation is at hand;
Surely the Second Coming is at hand.
The Second Coming! Hardly are those words out
When a vast image out of Spiritus Mundi
Troubles my sight: somewhere in sands of the desert
A shape with lion body and the head of a man,
A gaze blank and pitiless as the sun,
Is moving its slow thighs, while all about it
Reel shadows of the indignant desert birds.
The darkness drops again; but now I know
That twenty centuries of stony sleep
Were vexed to nightmare by a rocking cradle,
And what rough beast, its hour come round at last,
Slouches towards Bethlehem to be born?"

W. B. Yeats, The Second Coming, 1919



A Hidden Pattern of Defiance and Resolve

If you have followed our Medium posts released during COVID, you will have seen an interesting pattern of defiance and resolve. We started releasing our pieces about COVID in early March where we essentially urged our peers not to fear this pandemic but rather maintain a long-term view. Since COVID, we have focused on what has seemed obvious –
#1 Absenteeism is the opposite way of human progress and #2 Nothing will stop the progression of mankind and man-machine symbiosis.

Our Managing Partner, Dovi Frances, then shared some personal thoughts of what it feels like to actually contract and recover from COVID. Most recently, Group 11 shared what is arguably our most important piece to date – 'Equities Gone Wild – Bubble or Beginning' where we came full circle and essentially summarized all the factors that have led us to the next-gen technology adoption stampede we are currently witnessing.

Tooting our Own Uni-Horn

Since June 2020, many of Group 11's portfolio companies, in which we are a major investor and own a significant stake, have announced massive financing rounds. Subsequently, these companies have been newly inducted into the global unicorn club, or are to become unicorns in the near future.

Amongst these companies, Tipalti just announced a $150MM financing round at a >$2BN valuation, Next Insurance just announced a $250MM financing round at a >$2BN valuation, and TripActions announced a $125MM in Convertible-to-IPO financing only a few months after its $250MM financing round at a >$4BN valuation. A handful of Group 11's up-and-coming companies such as SunBit, Papaya Global and HomeLight, have continued to attract investor money and are well on their way to joining Group 11's stable. In under a year, our portfolio companies have attracted close to $1BN dollars of fresh capital that will allow them to grow market share even faster, attract and retain top talent, and further develop their tech offering.

Fresh capital is very important to have when you have perfect product-market fit. Lots of capital allows: Step 1: Disrupt. and now, Step 2: *Dominate the market.*

Group 11 now houses a stable of FinTech unicorns. We have significant exposure to the above-mentioned companies and now rank as a Top 1% performing fund. All of these milestones confirm our original mission to become the nation's leading FinTech investor.

A Perfect Time for Contemplation

Aristotle (384–322 BCE) once said, *"The ultimate value of life depends upon awareness and the power of contemplation rather than upon mere survival."*

It has taken Group 11 about eight years since the launch of our Fund I, and six years since we started taking outside investor money, to get to where we are today.

Taking a moment to contemplate our current position, we ask ourselves fundamental questions about how we envision our own and our families' future, and how we envision Group 11's future and the future of tech. These are admittedly deep questions which we will address in another article. One question that we do wish to address today is around the definition, the title, and the substance of 'a unicorn'.

Taming Wild Unicorns

A unicorn is a mythical creature that has been described and depicted in various ways starting around the 8th century BCE. From the ancient Greeks, to the European Middle Ages, to the European Renaissance, and all the way to our modern era – unicorns continue to hold place in popular culture, often used as a symbol of fantasy and rarity.

It's no surprise that the term unicorn became popularized to designate privately held companies worth over $1BN. It is a fitting moniker. The unicorn term in the venture capital arena was first coined in 2013 by a venture capitalist named Aileen Lee who chose the mythical animal to represent the statistical rarity of such valuable and successful ventures. At the time there were only 39 companies that were considered unicorns.

Half a decade later, 2018 saw a big surge in the number of companies inducted into the unicorn list with over 120 companies being valued at or above $1BN dollars. This trend has further increased in 2019, and going into 2020, over 190 new companies joined this list which now boasts over 490 unicorns with a cumulative enterprise value of $1.5TN.

In other words, 63% of the companies on the unicorn list *joined the list in the last two and a half years.*

This recent surge in the number of companies joining the unicorn list, coupled with the mania we are seeing in the public markets (with the rise of SPACs and the extremely generous multiples assigned to many of the IPOs taking place since May), naturally raises the question of whether or not we are seeing overvalued campines (and thus, 'in a bubble').

Our short answer is: *NO.*

We addressed this question in our most recent article where we concluded that:

A demographically-driven flat GDP outlook, coupled with unattractive bond yields and the prospect of vicious core industrial restructuring it implies, only adds to the demand for next-gen winners, explaining their recent rise. In the final stage where 'software eats the world', the only growth is digital disruption. In fact, There Is No Alternative (TINA) and investors have a Fear Of Missing Out (FOMO). We suspect that part of the rise in earnings (or now, revenue) multiples is simply due to the increased present value of future cash flows in a zero inflation environment.

However, we suspect another significant impact is also in play, that of a capital reallocation of bond money into select equities. Digital disruption vendors with strong track records and stable dividends become bond proxies in this new world.

The longer answer is that not all unicorns are created equal and there is more than one *kind* of unicorn out there.

Unicorns vs. Alicorns — Past and Present

Winged unicorns are referred to as Alicorns, (which is also a Latin word for the horn of a unicorn), They have often been depicted in art and literature as representing evil. It is also worth noting that Alicorns, (unicorn horns), were considered the most expensive gifts and reputable remedies during the Renaissance, given as diplomatic gifts, presented as royal objects, and used as universal antidotes. The enthusiasm and mystique surrounding the Alicorn died down when its true source was discovered. It was not in fact a magical and rare object, but really a narwhal horn.

W.B. Yeats wrote of imagining a winged beast that he associated with ecstatic destruction. The beast took the form of a winged unicorn in his 1907 play '*The Unicorn from the Star*s' and later that of the rough beast slouching towards Bethlehem in his poem "The Second Coming" which is quoted above.

We find it opportune that Yeats wrote "The Second Coming" during the 1918–1919 Influenza pandemic, drawing a distinction between two opposing forces that fight furiously while the world is in disarray. How fitting to the world in 2020!

That is the case of Unicorns and Alicorns. Both are mythical creatures. Both appear somewhat similar. But upon taking a closer look, they could not be more different from one another. The Unicorn has been used to depict true rarity, innocence, and light whilst the Alicorn has been used for ages now to depict unrealistic beliefs, greed, and gluttony, thus propagating fraud, anarchy, and darkness.

Time is a flat circle and history tends to repeat itself not only in the way we reincarnate terms from the past but also in the way this reignites the same human tendencies that surrounded mythical creatures and stories.

How to Tell a True Unicorn From an Alicorn

The first step is to acknowledge that it is impossible that almost 500 unicorns are all indeed category-defining and worth their valuation outside their small list of investors. We will not go to scrutinize CB Insights unicorn list and the methodology used in compiling the list, but will simply acknowledge that some companies, (such as JetSmarter, MagicLeap to name a few) are not worthy of their private valuation for reasons that range from lack of real innovation, sheer mispricing by investors, to complete financial engineering.

They are fake unicorns. They are — Alicorns.

The second step is to read beyond the flashy headlines and ask a few fundamental questions about any alleged unicorn:

1. Is it a next-gen business? We define a next-gen business model by three primary criteria; it is cloud-based, it uses AI to process vast data stores and provide intelligent service, and it leverages consumer internet self-serve user interfaces. These characteristics together feed off one another to absolutely obliterate legacy client-server technology-based alternatives that often rely on manual intervention.

2. Is it scarce? Of equal importance is the fact that a successful next-gen attacker is rare. It is difficult and time-consuming to envision a new market, then develop the software and the corporate culture around that solution, and finally to attract users who feed that AI engine to the point it breaks from the pack. These maturation challenges, coupled with the fact the clock just moved up five years in a matter of weeks amidst COVID means alternatives to the existing leaders really don't have time to develop.

3. Is it continuing to take market share by restructuring the new environment in which it operates? This is not a simple TAM (Total Addressable Market) replacement exercise. The installed base of legacy client-server technology is vast and still powers the core infrastructure of enterprises in industries including banking and insurance, travel, retail, manufacturing, and energy production. A true unicorn fundamentally attacks the structure of these industries by delivering more agile, cost-effective, and customized alternatives. A fake unicorn, the alicorn uses these same next-gen technologies to deliver a look-alike product.

The simple truth often ignored by many of our peers in the VC industry is that new technology does not simply get added to an existing environment but rather, restructures it in its image thus opening many initially unforeseen doors. AAPL is not important because they are selling slick phone units but because they are transforming commerce as a result of selling phones. In the pressure-cooker of a post-COVID economy, it is the transformative offerings that will serve a redefined world.

4. Who has invested in the company and are they reputable, long-term investors? Selection bias plays a big role here because essentially any deep-pocketed investor can turn almost any company into a unicorn. However, raising capital alone does not miraculously add long-term value. Quite the contrary actually — Hiding the problems of an alicorn running on a flawed business model under a pile of cash only hurts investors in the long term, while shepherding a real unicorn in support of working and tangible KPIs builds value over time.

(Stable) Stable of Unicorns

In a world with a fundamental mismatch between legacy technologies and what consumers need, new solutions are filling the void while legacy enterprises slowly lose relevance and lose market share. As the world shifts under our feet, the best stability comes from creating the future, which is precisely what change-agent unicorns do.

We continuously ask the fundamental questions above as many of our portfolio companies continue to join the ranks of the unicorn list.

In Group 11’s growing stable of current (or soon to become) unicorns — Sunbit fills the void for consumer debt at the SMB point of sale. Similarly insurance companies are failing SMBs too, for the same reasons, Next Insurnce is filling that void. HomeLight is helping people buy houses in a more effective manner by completely disrupting a disjoined and manual process where AI and big-data were yet to be utilized. In the enterprise space, legacy complexity has led manual operations to be unacceptable in a post-COVID world, with TripActions, Tipalti, and Papaya Global serving once manual and human-intensive functions in accounting departments by similarly solving complexity problems with data, and then scaling out.

There is no doubt in our minds that many more new unicorns will emerge over the coming years as we expand the remit of digital automation beyond its current consumer and enterprise strongholds. However as we pass this initial step function of COVID-driven adoption , we also believe that the market will grow far more cautious, methodological, and thoughtful in pricing emerging vendors. After all, we are on the verge of man-machine symbiosis and certainly none of us wants to jeopardize the second coming of (now real) unicorns by diverting our energy to alicorns.

Equities Gone Wild - Bubble or Beginning?

By Roxane Googin and Dovi Frances | Sep 2020

"The future has imploded into the present. With no nuclear war, the new battlefields are people's minds and souls. Mega-corporations are the new governments; Computer generated info domains are the new frontiers. Though, there is better living between science and chemistry. We are all becoming slave-bots. The computer is the new cool tool. Though we say, "All information shall be free," it is not. Information is power and currency of the virtual world we inhabit. So we mustn't trust authority. Cyberpunks are the true rebels. Cyber-culture is coming in under the radar. An unordinary society, an unholy alliance with the tech world, and a world of organized descent"

Billy Idol, Cyberpunk Opening Manifesto, 1993.

Where to Begin...

For many centuries humanity has envisioned a future where computational power is almost endless and automation is all-encompassing. Beginning with the development of the tally marks in ancient days, to the abacus, the slide rule in the 1600s, the automaton in the 1700s, the perpetual calendar machine, the differential analyser in the 1800's, and of course the introduction of an analog computer, and then a digital computer at around 1938, humanity has evolved through countless generations to bring us to this moment of total man-machine symbiosis.

The breakthroughs of WWII brought upon us the first digital, programmable machine, The Colossus, and from there through the introduction of a Turing-complete ENIAC the road to PC was fast tracked.

The evolution accelerated after the World Wide Web was introduced to the public 29 years ago as the collective knowledge of billions of people interacting with machines in a quasi-symbiotic relationship paved the way for enormous technological breakthroughs.

Today, amidst massive demographic and technological changes, humanity has encountered a unique moment where physical interactions are interrupted by an external, biological threat which was initially considered unknown and life-threatening to our species.

In a coordinated effort, governments shut their borders and instructed billions of people to stay at home and so came about a global experiment of withholding physical presence whilst maintaining virtual connectivity to family, friends, and business through technology.

This six week global experiment has quantum leaped technology adoption by five years. While the remainder of this experiment is still ongoing at some capacity, the results of the experiment are similar to what modern day prophets, scientists, authors, script and song writers (yes, Billy Idol included) have long predicted:

A paradigm shift running in parallel across all industries and all people of all ages.

An utterly beautiful “Shock to the System” (also a great song from Billy Idol’s 1993 Cyberpunk Album but that’s besides the point).

A Cyberculture complete take-over of our old economy and a new-world order that will soon ensue. The last move of the white queen to H5 prior to calling checkmate towards a full man-machine symbiosis.

September 1st 2020 — Today:

In light of the above movement, tech equities are rallying with strength in the face of a weak GDP and political uncertainty. Investors looking to leverage this trend are justifiably concerned about a 2000-like bubble. However, rather than a bubble, we believe we have entered a new normal. We are in a new wave of automation that really began with the vision that drove the 2000 bubble. While the power of cloud computing, AI, and internet proliferation has created giants of international scope and threatening market power, we believe they represent the tip of the iceberg of a next-gen automation wave rather than the end game. Driving this phase are COVID-led behavioral changes that accelerated this penetration of new tech by five years in six weeks. Importantly, this represents a time-shift of a new normal rather than a temporary pull-forward of existing demand.

Couple the proven power and reach of this new technology with a demographically led lack of investment alternatives and you get the perfect storm that is brewing now. It is important to appreciate that COVID accelerated existing trends more than creating new ones. One of those trends is a global, mature market baby bust that promises to cap GDP growth for decades. Reflected in flat to negative bond yields, this very long term trend is forcing debt investors to consider investment alternatives. One of those alternatives is dividend income from extremely stable tech giants such as Apple. We submit that vendors like Apple are becoming the new sovereign debt; that a whole new class of investors is valuing these equities not on a revenue or earnings multiple, but on a yield basis, and that with low alternative yields, that yield is very low. We are at the start of this multi-decade trend, not the end.

Current Adoption

The social distancing required by COVID-19 has by many accounts accelerated digital adoption 5 to 10 years. In their Q2 2020 earnings call, Shopify management observed that e-commerce had moved from 10% to 30% of retail sales, reaching their 2030 30% goal in six weeks. While the claimed acceleration varies from 5 years (Microsoft) to Shopify's 10 years, a multi-year jump in just weeks is ubiquitous among next-gen winners. This trend towards cloud-based, AI-enabled and consumer-internet-like self-serve applications for ever more complex business processes was already underway.

What COVID did was make this migration mandatory overnight, especially in slow-moving industries such as healthcare and education. Seemingly, life goes on and users are adapting well to this new way of living. People generally do not miss going back to waiting in doctors' offices, and city-bound white collar workers are flocking to the suburbs. Boomers are learning how to use QR codes and how to buy groceries online. Clearly, there is no going back. Fortunately, the Group 11 portfolio of companies fit into this paradigm well, with next-gen leaders like Next Insurance, TripActions, Tipalti, and HomeLight progressing towards unicorn status in a rather short span of time.

Scarcity Value

We define next-gen business process vendors by three primary criteria; they are cloud-based, they use AI to process vast data stores and provide intelligent service, and they leverage consumer internet self-serve user interfaces. These characteristics feed off one another to absolutely obliterate legacy client-server technology-based alternatives that often rely on manual intervention. The installed base of legacy client-server technology is vast and still powers the core infrastructure of legacy enterprises in industries including banking and insurance, travel, retail, manufacturing, and energy production.

Of equal importance is the fact that a successful next-gen attacker is rare. It is difficult and time-consuming to envision a new market, then develop the software and the corporate culture around that solution, and finally to attract users who feed that AI engine to the point it breaks from the pack. These maturation challenges, coupled with the fact the clock just moved up five years in a matter of weeks means alternatives to the existing winners really don't have time to develop.

It is now or never for new product adoption and those offerings need to be ready today. Therefore, in large measure the offerings you see today are the ones you will see in a few years. They have proven penetration into very large markets and we generally assume they will not stop growing until those markets have been completely transformed.

This is not a simple TAM replacement exercise. The simple truth often ignored by many of our peers in the VC industry is that new technology does not simply get added to an existing environment but rather, restructures it in its image thus opening many initially unforeseen doors. AAPL is not important because they are selling slick phone units but because they are transforming commerce as a result of selling phones. (And oh yes, the dividend rocks.)

The GDP Problem

Just as adoption of next-gen solutions was at a tipping point anyway and COVID provided a pull-forward forcing function of adoption, so too will the threat of bankruptcy as technology adoption laggards soon represent a pushing function. We believe the persistently low interest rates in the bond market portend a flattening of global mature market GDP. Without GDP growth, unit demand especially for core industrial products including legacy financial services, energy, and autos stagnates. Importantly, all the profits in these high fixed cost industries come at the margin, when they grow. Conversely, if they shrink at all the impact is not subtle; they immediately go into negative cash flow, followed by desperate price cuts to gain enough share to cover those costs, leading quickly to restructuring and consolidation. We are predicting flat to down GDP performance in mature markets looking forward due to long-standing demographic issues precipitating just such a consolidation scenario.

The Demographic Problem

Perhaps due to the ever-growing cost of raising functional young people in a complex society, birth rates across mature markets have been falling for years. Starting in Japan, then spreading to Europe and even to China, birth rates below the 2.1 per woman needed to maintain a flat population have now even spread to the U.S. In fact, the 2020s should represent the first domestic working age population decline since perhaps the Civil War. In population-decline leader Japan, more people now die than are born. Domestically, the absolute number of babies born in 2019 was the lowest in 32 years when the general population was 25% smaller than it is today. The problem with these trends is that they are both long-term and impactful. They can only be solved via immigration or time; there is no quick fix.

The economic impact of population decline is pernicious. With fewer people, vendors have less unit demand, leading to the chronic over-supply that leads to the restructurings mentioned above. Fiscally, as a fixed number of vendors vie for fewer buyers, deflationary expectations creep in. The switch from inflationary to deflationary expectations becomes its own economic depressant as buyers delay purchases in search of a better deal. We suspect a growing fear of deflation was behind Federal Reserve Chairman Jerome Powell's relaxing of Fed inflation targets on August 27. By shifting their focus to the maximum employment side of their dual mandate of employment versus price stability, he seemed to imply employment was more of a worry than inflation. We could not agree more; now he needs employment to stave off deflation.

The Bond Problem

Once broad concern investors have about the future is the persistent and growing trend towards negative bond yields. Perhaps because bonds are more economically sensitive than many equities, coupled with their long duration, bond investors have a better track record at predicting economic downturns than equity investors. Again starting in Japan, the trend to negative bond yields has spread to Europe and is threatening our shores. Anyone willing to commit to losing only 0.5% to 1.0% of their capital over a 30 year period must be pretty cautious about the future. However, given the demographic trends outlined above we believe they are right. In fact, we suspect Fed Chairman Jerome Powell is actually praying for 2% inflation more than trying to avoid it.

TINA to FOMO

A demographically-driven flat GDP outlook, coupled with unattractive bond yields and the prospect of vicious core industrial restructuring it implies, only adds to the demand for next-gen winners, explaining their recent rise. In the final stage where "software eats the world", the only growth is digital disruption. In fact, There Is No Alternative (TINA) and investors have a Fear Of Missing Out (FOMO). We suspect that part of the rise in earnings (or now, revenue) multiples is simply due to the increased present value of future cash flows in a zero inflation environment. However, we suspect another significant impact is also in play, that of a capital reallocation of bond money into select equities. Digital disruption vendors with strong track records and stable dividends become bond proxies in this new world. Bond investors starved for yield will bid up certain assets (like Apple stock) not based on earnings or revenue multiples, but based on a dividend yield multiple. Importantly, in this environment they are happy with a pretty low yield. Thus, not only are new buyers crowding into a fixed number of names, but those buyers may be less price sensitive than traditional holders. These factors set the stage for the startling growth in asset values. Note that these drivers are both long term and fairly immutable in nature.

Conclusion

Investors have been shocked by the appreciation of next-gen vendor equities in the face of an uncertain overall COVID environment. Many compare this growth to that of the 2000 equity bubble. Rather, we see this is the start of a new normal, one that was at a tipping point anyway, but got cranked forward five years in six weeks. Once users changed their habits to accept these technologically-driven solutions over historic manual ones, they stuck. This places additional pressure on less digitally prepared vendors to either play catch-up or close their doors. Everyone realized that next-gen technology adoption was a necessity rather than a fashionable luxury all at once, leading to the adoption stampede we are witnessing at some of our more established portfolio companies such as Tipalti, TripActions, Next Insurance, HomeLight, Sunbit, Papaya Global, and also with some of our emerging portfolio companies such as Lili Bank and EquityBee.

But there is more. Long-standing demographic trends are starting to become evident in the larger economy. The gradual but constant spread of low and negative interest rates portend flat GDP performance in the years ahead. We believe this assumption is correct, and is driven by a baby bust that has also been spreading around the mature market economies for decades. No quick fix exists for demographic problems. Indeed the saying goes: “Demographics is destiny.” This yield and restructuring pressure makes the growth of digital attackers all the more appealing, drawing capital from other areas, including core industrials and bond markets. Importantly, some of those investors are content with low returns, forcing the price of growth equities up even further. It is because of the duration of these demographic trends we see this not as any bubble, but as the start of the new era into which we have just quantum leaped.

TO BE CONTINUED...

"There is Nothing New Under the Sun"

אין חדש תחת השמש

Ecclesiastes 1:9 (New International Version)

By Devon Morris | Aug 2021

Group 11 has announced a $11.5MM Series A investment in SMBX, the new exchange for issuing and buying US small business bonds. Group 11 is joined by co-investors Better Ventures, the Impact America Fund, and AltaIR Capital. In conjunction with the round, Group 11 will be joining SMBX's Board of Directors.

Led by CEO Ben Lozano, PhD, COO Jackie Chan, and CTO Bhavish Balhotra, The Small Business Exchange ("SMBX") has built a platform that, up until a few years ago, could not, and did not exist. They are the first to build the Small Business BondTM (yes, it's trademarked!), a new security that allows regular retail investors access to US Small Business growth. They have made "something new under the sun." We are excited about this opportunity and present the following written piece to: 1) share the history and context of the US Small Business Bond, 2) Understand SMBX's new bond and marketplace, and 3) explain why Group 11 strongly believes that SMBX's new offering will completely change the retail investment industry.

What Has Been Will Be Again, What Has Been Done Will Be Done Again

Most of the time, what civilization perceives as "new," is a rebuilding or a re-imagining of something that has already existed. While it boasts impressive features, the newest iPhone is not fundamentally different from the 2007 version; we have Blade Runner as a book, a movie, and a 2017 sequel; Han Solo's blaster is a Mauser C96; and for some reason we just can't get rid of The Charleston. None of these are necessarily new, but, instead, are reimaginings of elements that existed before. By recreating, and rediscovering the physical world in new ways, we learn more about ourselves and the world in which we live. In 2021, one of the ways humans reimagine the world is through creating digital or synthetic paradigms of life and work: essentially software.

A lot of investors and entrepreneurs will claim the "novelty" of their product or software service. It has "never been done," or "we're the first to do it," but this is rarely, if ever, true. This attitude of new is likely a little naivete, partly the obsession with feeling unique, and probably a little ego. In the cyclical nature of life, nothing is new. What has been will be again, and what has been done will likely be done again.

In the realm of fintech, in which Group 11 invests, the products and services are those that provide the digitization, the synthesization, the automation, and the re-imagining of existing physical financial products and services. The reimagination of life through software is what has enabled us to rebuild the financial markets in ways far more efficient than their brick-and-mortar bank predecessors of the past few hundred years. It’s why Group 11 has backed many fintech entrepreneurs and their market leaders that have now gone on to become unicorns in the landscape of financial services. These fintech market leaders, and their new, digitized financial products and services are “nothing new under the sun,” but are reimagined, digital formats, and empirically better than their previous iterations.

The Walls Go Up to Protect and to Exclude

The barrier that has for many years prevented anything "new," in terms of innovation and digitization within US financial services, is often attributed to regulation. Imagination, ingenuity, and thus risk, often come from the entrepreneurs pushing the boundaries; the boundaries in financial services are regulation. To protect markets and investors, there must be some forms of regulation. But these walls we use to protect, often become inverted prisons (locking people in, but also locking participants out). Fintech investors, entrepreneurs, and engineers’ ability to innovate and reimagine opportunities in fintech, for good or bad, will thus be inhibited by these regulatory walls.

Until very recently, the United States’ paradigm of financial securities regulation was defined in the landmark (and subsequent revision and additions of) Securities Act of 1933. Originating from the US Congress’ Constitutional power to regulate interstate commerce, its fundamental purpose was to define public and private securities, how they were registered (managed by the US Securities and Exchange Commission), who could sell them, and who could buy them. This regulation was enacted in response to the US stock market crash of 1929. Congress’ earnest intent behind the Act, and the creation of the SEC, was to protect individual investors and try to add some control, accountability, consistency, and transparency to the US securities market.

As previously stated, this regulation created the initial, necessary walls to protect Americans and financial firms from taking on excessive risk in investments, but by definition, excluded certain Americans and security types. One specific example of this inclusion/exclusion, was the definition of an accredited investor. The Act (and subsequent revisions) stated that only accredited investors were allowed to purchase and sell privately-held securities. The rationality was that this group of investors had the financial means, literacy, and assets to bear the brunt of a potential financial loss.

Because of this specific regulation, when US small businesses ("SMBs") wanted to begin or fuel growth, they had very specific and limited options to raise capital. Equity ownership (and some debt instruments such as SAFE loans and convertible notes) in a US small business was a security, and thus defined and regulated by the Securities Act of 1933. Until recently, only accredited investors could buy these equity securities in privately-held US SMBs. Thus, they were the only ones allowed within the walls.

On the debt side, SMBs had the following options: traditional commercial bank loans, revolving credit (through point-of-sale providers like PayPal or Square) based on cash flow and receivables, and traditional business credit cards. The final, and most widely used form of small business growth in the United States has been the Small Business Administration ("SBA") loan program. For the past 80+ years in the US, these were the financial instruments available to SMBs, and this is what the Securities Act and the SEC allowed. There was little "new" with these financial walls, and it kept certain participants in, but most people out. With all aspects of life, people and markets evolve over generations and regulation needs to change with it.

The Walls Come Down: the JOBS Act Actually Created Jobs

A good day for ingenuity, innovation, and the "new" in US financial markets, was the passing of the Jumpstart Our Business Startups Act, or, the JOBS Act of 2012. This act relaxed some definitions and regulations from the original Securities Act of 1933, with the purpose of allowing further financial access to more investors and more US business. Below are some of the important changes/updates:

- Increased the number of permitted shareholders for a company and allowed some non-accredited investors equity access to the cap table
- Provided a new exemption to a yearly limit on the amount each investor may invest in securities offerings, tiered by the person's net worth or yearly income
- Mandated reviews of companies' financial statements for offerings between $100,000 and $500,000, and audits of financial statements for security offerings greater than $500,000
- Defined "emerging growth companies" as those with <$1BN in annual gross revenues
- Lifted the ban on "general solicitation" on specific kinds of private placements of securities (as long as companies only sell to Accredited Investors)
- Raised the limit for securities offerings exempted under Regulation A from $5 to $50MM

Each of these was a sea change for retail investors and US privately-held SMBs. In addition to those listed above, the most important updates in regulation (and for our discussion today), was Title III of the JOBS Act, more commonly known as "Regulation Crowdfunding" or "Regulation CF".

This regulation more specifically defined US businesses' ability to raise funds from (sell securities to) non-accredited investors. It stated that:

- All transactions under Regulation Crowdfunding are required to take place online through an approved and SEC-registered intermediary, either a broker-dealer or a funding portal
- A company is permitted to raise a maximum aggregate amount of $5MM through Crowdfunding offerings during a single 12-month period
- A company is allowed, but limited to, the amount of individual non-accredited investors that can invest in the company in a 12-month period
- All disclosures and material information in filings are required to be submitted to the Commission and offered to investors and the intermediary facilitating the offering

What did these changes and new definitions of "Regulation Crowdfunding" fundamentally mean? The JOBS Act, and specifically Title III, expanded financial access. Or in other words, it democratized US private securities. It enabled 'more people to have a seat at the dinner table.' The walls which kept certain retail investors out (e.g. the accredited investors definition) and that prevented SMBs from publicly raising certain equity and debt instruments (revenue size, shareholder construction) were finally relaxed. The JOBS Act expanded the number of hands, and allowed more hands to shake in a larger, more inclusive marketplace.

The walls were coming down!

President Obama signs the JOBS Act (2012). Getty Images.

In 2015, the SEC adopted Title III and began reviewing, registering, and approving qualified online platforms that could legally solicit and sell privately-held security offerings. Initially, entrepreneurs seized this new opportunity by creating equity investment startups and registering with the SEC as approved funding platforms. Companies such as Crowdsource, WeFunder, Mainvest, Equifund, and Republic allowed everyday Americans, with registry and some KYC, access to buy equity (via stock issuance) in companies previously regulated to accredited investors only.

(In addition to registering the securities with the SEC, these 65 approved SEC Funding Portals are subject to regulatory oversight by the Financial Industry Regulatory Authority). Our industry had again expanded the digitization of financial instruments with something "new," and this time with software-based, democratized access.

However, until recently, these SEC-approved funding portals were all focused on the equity side of business. What about the debt side? Most investors know the bond business market (both Sovereign Bonds and Corporate) is massively more than that of equities (both US and globally). Why was all of the initial focus of fintech entrepreneurs and crowdfunding startups on the equity side of this "new" opportunity and marketplace, and not the debt side? SMB capital raising had been shaken, but not stirred.

Bond, Business Bond

As SMBX puts it: “your local coffee shop doesn’t do a 409a report.” High growth US software companies or digital-first tech-companies, such as the likes of Grubhub, Gusto, or Epic Games, may find crowdfunding their equity via a new online portal to be a suitable solution to raise capital for growth (and would thus need the above 409a valuation reports for their equity’s tax-basis and IRS requirements).

However, the equity option is not the preferred, or best, solution for most businesses. The majority of small businesses in the United States are slow-growth, localized SMBs with fewer than 50 employees. They don’t necessarily need venture capital money, nor do they want to give up ownership (equity) in their company for current growth. Most US businesses have initial cash flows (as opposed to most startups), and their primary product or service is NOT digitally originated. Instead of Grubhub, think of local coffee shops.

Small businesses like locally-owned coffee shops are the foundation of the US economy. According to the US Small Business Administration Office of Advocacy, small businesses (defined as companies with fewer than 500 employees) account for 99% of the number of all US businesses. As of 2020, there are 31.7 million registered SMBs in the United States, employing 60.6 million employees.

Many of these SMBs operate in the service industry: restaurants, breweries, at-home bakeries, and yes, local coffee shops. But, as previously stated, instead of giving up equity and thus ownership, these SMB owners just need capital (regardless of source) to accelerate cash flows and help them grow.

As opposed to selling equity, the best option for this type of capital is debt, where an SMB borrows against future receivables. As previously stated, SMB debt options were traditional commercial bank loans, revolving lines of credit, business credit cards, and the SBA loan program.

In each of these debt situations, the business gives up no legal ownership (equity) but pays back the lender from future cash flows with interest (with collateral often the personal guarantee of the owner or assets of the company).

The data speaks for itself: debt is the preferred option for US capital raising. US small businesses predominately opt for debt over equity, with 70% holding outstanding debt, and 43% of SMBs having applied for a loan in 2020. The most widely used type of debt in the world is the bond, business bond. The difference between a corporate bond and a business loan, is the bond is a larger amount of debt, spread across many investors (usually issued in $1,000 increments), that in the aggregate is substantial. A bond has a higher volume with a higher number of investors than a traditional loan, which has one lender and one debtor. The corporate bond can also be freely resold and traded as a security between investors in a regulated marketplace.

Larger, corporate debt (for companies with over 500 employees) amassed a staggering $11-13TN in balances towards the end of 2020. Just about every US brand you can think of has issued corporate bonds: Boeing, Apple, The Coca-Cola Company, or John Deere. Corporate bonds are a viable, and often the wisest, option for capital raising in most situations. Bonds are a great capital solution for large, publicly traded corporations, but what about small businesses? Well, we now know SMBs were never before allowed the opportunity to offer bonds. (See the JOBS ACT above!)

Which finally brings us to the SMBX.

Finally, Something New Under the Sun: The Small Business Bond

SMBX seized on this opportunity from the JOBS Act. To address the needs of this market, and provide a fitting and "new" digitized debt security, the SMBX built The Small Business Bond .

The Small Business Bond is a new digital security, issued by a business and purchased by everyday investors on the SMBX marketplace. Through Machine Learning ('ML') built into their underwriting engine, SMBX approves qualified SMBs, and issues their bond on their platform. Individual bonds are offered at $10 a piece (so everyday investors can actually afford one), issued with ~8-10% coupons (interest rate), an average target issuance of $250,000 (which is increasing with each issuance), and can be purchased by any investor who completes the basic, necessary KYC registration process.

SMBX structures the fundamentals of the bond (term, rates, size, issuance, and target companies) around the SBA loan program, one of the primary and most successful sources of GDP growth in the US. In 2020, the SBA 7(a) program lent directly approximately $22BN through ~42,000 loans, and $645BN was lent from US banks to US SMBs (the amounts overlap). These businesses are SMBX's exact market. Instead of debt capital in the form of bank loans, SMBX gives the SMBs capital via a community-based bond.

All businesses on the SMBX platform have healthy cash flows, and at least 18 months of financials (these are companies that would otherwise potentially qualify for SBA loans). SMBX can offer SMBs better rates than the SBA, with no SBA regulatory fees, through a faster, digital-first process (as opposed to commercial banks' 20th-century traditional pen and paper underwriting). On top of that, SMBX also works with the business to actively market the bond raise and the company's product/service. SMBX will work with founders to help build pitch decks, their SEC prospectus, and develop the story, vision, and then the digital and printed materials.

So Lo Mo Co

In addition to competitive Interest rates and a fast, digital-first process, why is the Small Business Bond *fundamentally* better than an SBA loan or another form of traditional SMB debt? ***Because, it actively involves the community and democratizes a financial product through digitization***. Instead of a bank in another geography providing a business the capital to borrow, SMBX enables a business' own community to lend the capital. Instead of a bank receiving the interest on the debt, a business' customers (who are also now lenders) receive consistent monthly payments for a set term. Instead of customers' money sitting in a bank account getting <.05% APR (and the bank making MORE money from lending those deposits), customers' money is active in the community and returning a solid yield via a bond. Instead of the bank making money on the business, the customers/community make the money alongside the business.

In the words of SMBX's founders, "We can give access to capital to businesses who REALLY need it, and then give the people who WANT to back the SMBs the opportunity to do so." The financial experience is the creation and fostering of customers, community involvement, and the connections through investment where each bond holder is "close to their dollar." The entire transaction with all parties is: "Social, Local, Mobile, and Community."

When businesses go to their customers for capital, this says something about the founders, the community, and what kind of business they want to be. The increased sense of community is further brought about by digitization (bridging gaps and inefficiency) and putting a financial instrument in the pockets of customers (enablement through mobile). As stated earlier, when we remake our "digital or synthetic paradigm through software, we learn more about ourselves and the world in which we live." As SMBX believes, you should be able to buy and sell securities, including business bonds, all from your phone (it feels like something we should already have!).

In addition to the democratization of a new financial instrument and market, SMBX has also put considerable resources into financial literacy for both businesses and their customers.

All disclosures for each bond issuance (as required by the SEC) can be searched on the EDGAR database, and SMBX has education resources throughout their website including a robust FAQ and a relevant investing Glossary. The entire SMBX platform serves to make investing easier. SMBX's founders believe they can help teach people (both business owners and customers) financial skills and concepts through a new, digital financial instrument that also creates an enjoyable experience.

Gobuilda Quesadilla Gorilla

There is no better proof than the pudding, well, in this case, the cheese. I've written extensively about the why, how, and what, but what about the where and who of the small business bond? How does the SMBX practically work? As is Group 11's customary process in its underwriting, we interviewed and collected feedback from customers of our potential investments. In the case of SMBX, this was testing the online platform, the sleek mobile app, and buying some SMB bonds ourselves. To test, we put in orders for bonds from an El Salvadorian restaurant, Popoca, in East Bay, California.

We also interviewed some of the SMBs who went through the process and ultimately issued bonds on the SMBX platform to their customers and community. As part of this endeavour, we were introduced to Miguel Reyes, co-founder of Quesadilla Gorilla.

The Quesadilla Gorilla founders Mikayla and Miguel Reyes.

The restaurant, which successfully closed its full $165,000 bond target raise on SMBX in early 2021, provided valuable and honest feedback to Group 11. Founder Miguel learned about SMBX through a Stanford program for Latino business owners. During mid-2020, they received EIDL funding as well as both PPP loans. Towards the fall of 2020, they explored more options for funding the growth of new locations. They had already gone through the SBA loan process twice before (and were approved), but did not consider that route again in 2020, noting the long SBA due diligence process involving lots of paperwork.

Miguel was also concerned that a quesadilla restaurant would be disregarded as "unbankable" by traditional lenders. Thus, they opted to raise funds through a bond offering on the SMBX.

Miguel and Mikayla were able to raise the maximum offering, and saw increased customer engagement (both in person and on social media) from SMBX's joint marketing efforts. The process was quicker and easier than SBA loans and SMBX's origination fee was a fair price for the value add.

From the feedback from Miguel, the experience was the best he could've imagined; it was a true "Win-Win-Win-Win." His growing business received the startup capital for a new location, his customers in Visalia and the surrounding areas were able to engage, learn about the company, and actually invest, SMBX helped them with marketing the offering, and their communities in Central California have more delicious, toasted tortilla+cheese+filling locations. Miguel explained that Quesadilla Gorilla would definitely consider doing another raise with SMBX for future growth and recommended it to other similarly positioned SMBs.

Our investment team has a penciled in field trip to finally test out one of these primate quesadillas...

Recipe for Success

As described, a business bond is not "new;" but the Small Business Bond is "something new under the sun" and could not, and did not, exist until now. The SMBX has recreated, and rediscovered a financial instrument in a digital paradigm that delights all participants, a true Win-Win-Win-Win. The investors, the SMBs like Miguel and Mikayla at Quesadilla Gorilla, the SMB's community, and the industry all win and benefit from this new debt security and marketplace. SMBX provides a financial security that is far more efficient, and closer to the investor, community, and the SMB, than their brick-and-mortar financial institution ancestors. What once was restricted and unimaginable due to regulation, has now been reimagined into a digital, mobile world that can put community first.

Group 11 strongly believes that SMBX's new bond product and their growing marketplace will permanently shift the fintech industry for all participants. SMBX is spearheading the evolution of a more equitable financial system, one that puts small businesses front and center. Their vision is one where people have the power to invest in what matters to them, and small businesses have new access to capital and new ways to engage with their customers and community. In the long term, the SMBX team wants to create a cycle of wealth that stays within the community, and earns everyday investors immediate, regular returns.

New Opportunities, New Plans

SMBX is manned by a self-proclaimed team of “recovering bankers, financial engineers, and technologists working around the clock to democratize small business finance," and they are a welcome addition to Group 11’s entrepreneur network, portfolio, and investment thesis. CEO Ben Lozano, PhD, COO Jackie Chan, and CTO Bhavish Balhotra are on a mission to build a dynamic small business marketplace network that unlocks wealth for small business owners and their surrounding communities, and Group 11 is excited to back them.

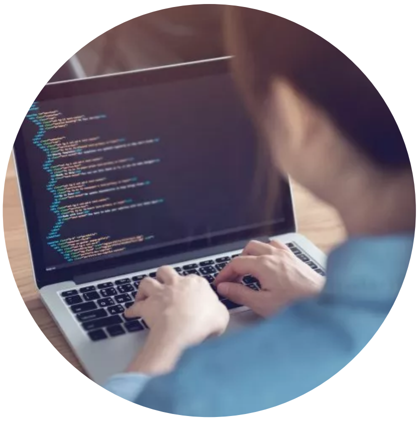
I encourage all of our readers to explore the SMBX online marketplace, their high level education materials about their platform and offering, and even some of their interviews and videos online that explain their proposition. Buy some quesadillas or music academy small business bonds in your community. There is a trove of useful financial information on SMBX’s site that can educate the reader on debts, investing, and the marketplace even beyond the SMB bond.

If you're a small business owner looking to grow your company, and looking for potential capital options, definitely look at SMBX’s funding portal as well!

Colleges are Getting Schooled

By Cem Basar | July 2021

Group 11 recently led a $10MM seed round investment into Masterschool, the digital education and financial technology company disrupting the massive $670BN U.S. “college-industrial complex” (WSJ) with its network of online, success-based schools, for which students pay no tuition until they are gainfully employed. This marks Group 11’s first investment in the company.

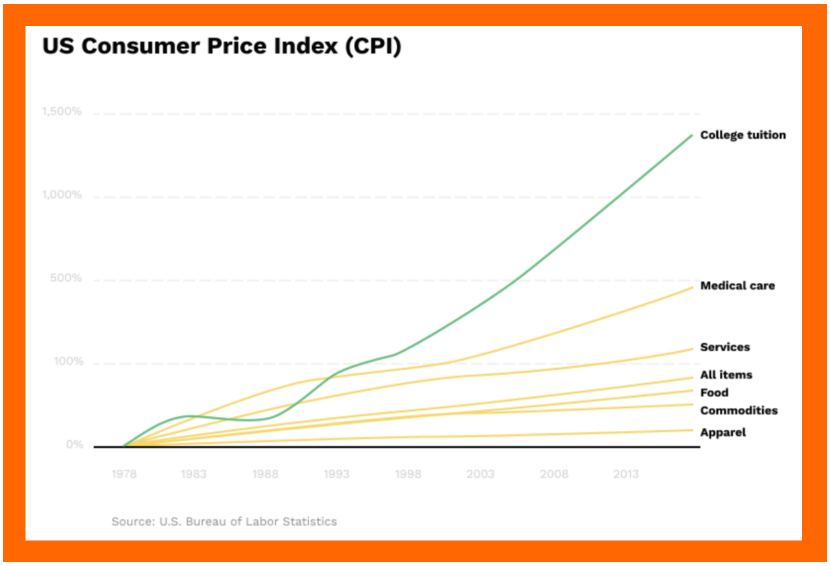


Higher Education is Inefficient and Outdated

The underlying dogma of traditional education is broken. It has been universally accepted for far too long. In its current state, the system simply does not serve its users effectively. There are two key parties to be considered in this equation — students and employers. In a perfect world, education effectively acts as the bridge between these two parties: students pay schools a tuition in order to gain valuable, employable skills, with hopes of entering the job market and earning a wage in return for contributing to the economy. Employers hire these qualified students and provide them said wages, enabling students to pay back the educators who invested them with the skills needed for the job.

Unfortunately, this is not how the system currently operates. Today’s higher education programs do not fulfill their role. They demand continually increasing prices of students (without necessarily increased quality of education), do not always teach relevant, employable skills, and ultimately are not efficiently converting students into prepared employees that meet the ever-changing demands of our job markets.

College is far too expensive. Students are committing more money than ever to gain an education; college tuition and fees are up 130% in the past 10 years, significantly outpacing inflation indices (U.S. Bureau of Labor Statistics Data, Visual Capitalist). Furthermore, aggregate U.S. student loan debt has surpassed $1.57TN, or an average of $38,792 per student (Experian). The trade-off is simply unfeasible; students are paying too much for traditional, four-year, on-campus programs that do not guarantee strong job prospects, thus leaving them in massive debt without the reasonable means to repay it.



Moreover, colleges are not aligned with students to help them secure jobs upon graduation. They overwhelmingly provide general, theory-based curriculums that leave students ill-prepared for real-world jobs. It is then incumbent upon the inexperienced students to secure job placements with little to no practical skills, and/or guidance or support from their educational institutions. The modern student needs applicable skills, in growing industries, obtained in a shorter time frame, and at a much lower cost than a traditional education.

As for the job markets, data shows the expansion of industries in the U.S. is in technical, high-paying engineering and software jobs. Companies are hiring for roles in computer science and data analytics in large quantities. Employment in Computer and Information Technology roles in the U.S. is projected to see an 11% overall increase from 2019 to 2029, much faster than the 4% average increase for all occupations (U.S. Bureau of Labor Statistics). Companies are even willing to pay higher wages to satisfy their growing talent needs. These roles have a median wage of $83,000, which is 41% higher than the $59,000 average across all other industries in the US.

In Computer Science (CS), one of the highest-demand job sectors in the market today, there is a significant shortage of qualified candidates. There are projected to be 2,938,983 Computer Science roles in 2023 (U.S. Bureau of Labor Statistics), while only 128,193 undergraduate CS degrees (NCES), 74,837 graduate CS degrees (NCES), and 97,226 online coding bootcamp certificates (Career Karma) are projected to be awarded. These programs produce a total of 300,256 potential new applicants for these roles, leaving a 2,638,727 deficit. This shortage of talent illustrates the inability of current education systems to satisfy demand in high-growth sectors.

In short, to better serve all stakeholders, this inefficient legacy system of physical, on-campus learning is in dire need of digitization in order to become more flexible, scalable, and affordable.

Enter, Masterschool

Masterschool recognizes these deficiencies, and is working to rewrite this equation entirely. The company started in 2018 with the goal of providing "Success-Based Education." Masterschool partners with leading professionals ("Masters") to train individuals so they can secure high-paying jobs upon graduation. Students attend six to nine month online schools for specific careers paths (i.e. Data Science) and skill sets, which cost $0 until they are hired. Masterschool actively works to place graduates in high-growth industries such as technology. Only once the graduates are gainfully employed do they pay back their tuition (via an Income Share Agreement) by returning a fixed percentage of their monthly income. This directly aligns the school's incentives with the student's — the way all educational systems should operate.

The founders of Masterschool strive to eliminate the financial obstacles that prevent individuals from integrating into the workforce. They hope to optimize the balance between the length, cost, and value of education programs. For example, a traditional two to four year program costs too much, takes too long, and still may not produce strong job prospects. On the flip side, a four-week unguided coding bootcamp may be a more affordable option, however it is too short and unstructured to be considered a legitimate career-changing program. This is why Masterschool is targeting the under-served middle ground — offering guided, intensive programs taught by industry experts, at lower costs and reasonable lengths, with tangible career placement results.

From Zero to Hero

Let's look at a real example. Take Jade (name changed for privacy purposes), a student in the final year of her Economics program. Jade was struggling to find internships or full-time job prospects during school. Her program's curriculum focused on theoretical topics, not technical skills, and thus left her unqualified for many roles she was interested in. She wanted to explore ways to become a more qualified candidate in the job market, without taking on more debt to enroll in another long, expensive program. That's when Jade learned about Masterschool.

By attending Masterschool's Data Analysis program, Jade learned essential technical skills in Python and Structured Query Language (SQL), and utilized Masterschool's career development resources to secure interviews at top technology companies. She was able to earn a high-paying job at Google and will begin paying back her tuition to Masterschool each month. Jade is the textbook example of a candidate with no prior programming experience, who was able to secure a highly-coveted, technical role at a major technology company through Masterschool — all in less than a year.

Jade’s success highlights a crucial element of Masterschool’s offering: the placement process. Unlike the average college career center, which is ill-equipped and not incentivized enough to work with every single student, Masterschool is committed to helping every graduate achieve successful employment. They go above and beyond to provide students with all they need — CV/LinkedIn workshops, live coaching sessions, networking and interview preparation — to best showcase themselves and the new skills they’ve learned.

Why We’re Excited About Masterschool

We believe Masterschool has built a proven and scalable business model to disrupt this massive market. Moreover, by incorporating innovative financing solutions like Income Share Agreements, they empower students to bypass the financial and operational inefficiencies of legacy education. As is the case with other Group 11 portfolio companies, Masterschool is digitizing outdated, manual processes. They are improving the user experience on a large scale as well as rectifying market imbalances, including the ROI of current higher education and the talent shortage in high-demand sectors. As the company continues to grow, they will further develop their network of schools, Masters, students, alumni, and hiring companies, to establish themselves as a trusted household name in education.

Group 11 is proud to back the impressive founders of Masterschool — Michael Shurp, Otni Levi, Roi Tzikorel, and Eran Glicksman — who have proven expertise in the Education Technology industry. Congratulations to the entire Masterschool team as they work to eliminate the outdated barriers that prevent students from obtaining successful careers and financial freedom. We look forward to the company’s continued progress.

The Scoop on Sorbet

By Michelle Chang | June 2021

Sorbet announced a $21MM Series Seed financing round led by Group 11 with participation from Viola Ventures, Meron Capital, Rocket Internet Capital, and Global Founders Capital. This is Group 11's first investment into the paid time off (PTO) optimizing platform. Sorbet incentivizes employees to take more vacation days while dramatically reducing the balance sheet liability of unused PTO for companies.

We Aren't Taking Enough Vacation, and it's a Problem

Paid time off is a vastly underutilized, mismanaged, and poorly understood asset that has an outsized impact on both employees and the companies they work for.

American employees, compared to peers in other countries, underutilize vacation time and often feel guilty about the time they do take off. On average, U.S. employees only use 72% of their PTO, leaving over 28% of their PTO unclaimed at the end of the year (LinkedIn). Unused PTO balances are an illiquid asset that employees unknowingly forfeit (somewhere to the tune of over $66.5BN in earned benefits annually), or can only access when they leave their companies (CNBC).

The trend of not taking time off has only accelerated during the COVID pandemic. In 2020, the average workday lengthened by nearly an hour; however, 92% of Americans shortened, postponed, or cancelled their scheduled PTO. This has caused increased levels of employee burnout and declining mental health. A Zapier study found that 22% of Americans are currently experiencing burnout, 20% feel more burned out than usual, and 72% say their mental health has been negatively impacted (Zapier). Workplace productivity is also taking a hit with 53% of workers feeling less productive and 44% having trouble focusing (Occupational Health & Safety).

For employers, the rapidly increasing balance of unused PTO equates to $272BN in PTO liability on their balance sheets which they cannot control or plan for (LinkedIn). If employees don't use all of their vacation time for the year, employers can end up owing them large, unknown sums of money at unpredictable times, putting companies in risky financial positions.

Additionally, employee burnout, which The World Health Organization (WHO) now recognizes as a disease, is responsible for up to 50% more turnover and $190BN in annual burnout related healthcare costs — a nightmare of CFOs and CHROs (Forbes). Burned out, disengaged employees, who are defined as “unhappy and unproductive at work and liable to spread negativity to coworkers,” cost employers 34% of their annual salary (LinkedIn) or $550BN in additional churn-related annual expenses (Glassdoor).

And while there is increased focus on employee wellness, heightened by the pandemic, unused PTO continues to be a problem for company balance sheets and workplace satisfaction because leadership does not fully understand the murky economics of PTO liability and existing solutions are inadequate.

Optimization for the No Vacation Nation

Enter Sorbet. Sorbet is the wellness and optimization fairy godmother we all wish we had, including our employers. With a patent pending model that predicts the amount of PTO that will be left unused by each employee (based on preferences, PTO balance, work schedule, company policy, etc.), Sorbet recommends an optimal time plan that maximizes PTO usage and promotes wellness. Sorbet's platform increases the time off employees actually take by 14%.

In addition, Sorbet enables employees to cash out the value of the predicted unusable time (a traditionally illiquid, inaccessible asset) onto a prepaid, virtual Visa card, which they can use to book experiential offers on the Sorbet marketplace or spend anywhere online or in-person. It is worth noting that while Sorbet offers cash out benefits, the company's mission is not to disincentivize employees from taking time off, but to optimize the value of their time both on and off the clock.

For employers, Sorbet's PTO factoring provides a number of benefits:

1. Cash Flow Predictability: The platform decreases the balance sheet liability of unused PTO by incentivizing employees to take more time off, while providing cash flow predictability through the employee cash out feature, which smooths out the otherwise incalculable payouts of unused balances.

2. PTO Refinancing: Sorbet provides funding for the employee cash out in the form of a low interest loan that the employer can pay back on their desired terms over time. Sorbet's refinancing rates are much lower than average annual wage inflation rates, thus significantly reducing the cost of financing the PTO liability.

3. Wage Inflation Protection: On average, U.S. employee salaries increase 3–5% annually (Investopedia). The increase in employees' accrued, unused PTO balances compound annually with wage inflation. Sorbet's platform enables employees to cash out the full, present value of their accrued PTO, preventing balances from being left unused and increasing at year end.

4. Increase Tax Deductions: Under the IRS' "2.5 Month Rule," employers are only able to recognize accrued employee PTO as a tax-deductible expense during the first 2.5 months of the following tax year (The Tax Adviser). With Sorbet, employers can recognize accrued PTO as an expense year-round, in effect increasing tax deductions up to 4x. Additionally, by liquidating the balance of outstanding days through Sorbet, companies can save approximately 27.25% in combined federal and state corporate tax rates on their net gains (Tax Foundation).

Brain Freezing Savings

The financial benefits of Sorbet's platform result in significant company savings. To illustrate, let's use Walmart, which is as American as not taking vacation, as an example.

Only accounting for Walmart's 740,000 full-time, salaried employees in the U.S., who have an average annual salary of $55,000, Walmart incurs a whopping $941MM in unused PTO liability annually (Walmart). And this is just from a fraction of their >2.3MM global workforce.

With Sorbet, modeling a 70% platform utilization rate and an 80% uplift in tax deductions, Walmart can conservatively save $243MM annually (a quarter of their current liabilities from salaried employees), while gaining control over their cash flows, and providing thoughtful wellness benefits to their employees.

We encourage you to go to our model to view our assumptions (which are publicly available information) and calculation methodology.

Case in point, Sorbet's platform is a sweet solution for a massive $272BN pain point (less than 2% of U.S. companies offer unlimited PTO), successfully solving both employee and employer problems (Society for HR Management). There are tangential providers that offer seemingly comparable employee PTO benefits. However, Sorbet is uniquely differentiated as the only solution that improves wellness by quantifiably increasing the amount of time employees take off (by 14%) and alleviates the employers' headache of unpredictable liabilities and cash flows.

We find this opportunity compelling because Sorbet provides an inventive and necessary enterprise solution that sits at the tricky intersection of wellness, productivity, and finances, and addresses all facets well. This is in large part due to Co-Founder and CEO Veetahl Eilat-Raichel, who is a seasoned financial services executive and brilliant brand strategist.

We are excited to watch Sorbet rapidly expand market share in the U.S. as they serve up significant savings to their customers and time optimization for employees. Congratulations to Co-Founders Veetahl Eliat-Raichel, Eliaz Shapira, and Rami Kasterstein, and the growing Sorbet family!

Where Everybody Knows Your Name

By Michelle Chang | Jun 2021

Making your way in the world today
Takes everything you've got
Taking a break from all your worries
Sure would help a lot
Wouldn't you like to get away?
Sometimes you wanna go
Where everybody knows your name
And they're always glad you came
You wanna be where you can see
Our troubles are all the same
You wanna be where everybody knows your name

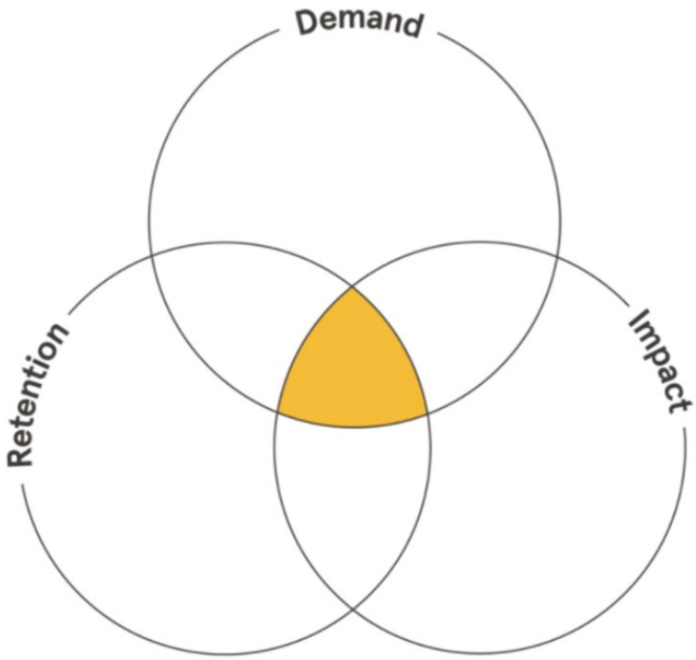
—"Where Everybody Knows Your Name,"
NBC sitcom Cheers theme song

Venn announced a $60MM Series B financing round led by Group 11 with participation from investors Pitango Venture Capital, Bridges Israel, and Hamilton Lane. This is Group 11's first investment into the innovative urban-tech that is transforming developing neighborhoods into vibrant communities through its revolutionary operating system.

To underwrite the investment opportunity, I had the pleasure of travelling to Tel Aviv to meet the Venn team and tour one of the Venn-managed neighborhoods. But before I share my experience of Venn in action, let's first start with the problem.

Loneliness has become an epidemic that rivals obesity and smoking as a health risk in America (WebMD). Nearly eight in 10 Gen Zers (79%) and seven in 10 millennials (71%) are lonely (Cigna). Only one in five Americans has close, real world connections (YouGov). Lonely urbanites do not feel connected to where they live and thus move every two years on average (ResidentRated). COVID-19 only heightened this sentiment, resulting in people feeling at least 20% lonelier and less attached to where they live (SocialPro).

For property owners, this translates to declining tenant satisfaction, low retention, high vacancy rates, and nearly 50% turnover a year, or $100BN in tenant turnover costs annually, drastically reducing their net operating income (NOI) and bottom line (CBRE).



The Venn Diagram of Impact, Demand, and Retention

Venn solves these two problems with a first-of-its-kind software platform. Venn's platform enables active, multi-faceted, communication between multifamily landlords and their residents, resulting in an unprecedented level of service and participation. Venn creates a new way of urban living by connecting residents, landlords, and property developers through various services including community engagement, managing homes, creating shared community spaces, supporting local businesses, and programming social events among other offerings.

Venn's goal is to create belonging for Neighbors (residents) and better business for Partners (property owners) by designing neighborhoods at the intersection of *Impact*, *Demand*, and *Retention*.

For residents, Venn's platform drives a sense of belonging and community participation, creating at least 50% more personal connections and increasing their satisfaction with their home and community. For landlords, the outcome is an additional $120 per unit per month increase in net operating income (NOI) due to improved resident retention and demand, which translates to an approximate $55MM increase to the bottom line for a landlord with an average 3,000 unit portfolio. This is an undeniable value proposition in the U.S. multifamily market, where tens of thousands of landlords cumulatively own over 44 million units (U.S. Census Bureau).

Witnessing the *Vennaissance* First Hand

When I traveled to Tel Aviv to conduct my due diligence, from the moment I arrived in my hotel room, where I was greeted with a welcome note and Venn swag bag, to my last evening before my flight back to Los Angeles, which CEO Or Bokobza made sure I didn't spend alone by connecting me with friends, the Venn team shared their community with me and made me feel like I belonged.

My experience of Venn's community spirit and brand was reinforced by my tour of the company-managed residential buildings, coworking spaces, music studio, and a local bar in the Shapira neighborhood of Tel Aviv. Shapira is historically a low-income area home to a large group of migrants and foreign workers that has become a vibrant, energetic, and artistic community in recent years thanks in large part to Venn.

While checking out the community music studio, I was invited by a rehearsing troupe of singers to watch them practice a hilarious song about the perils of hyper-PC culture. I had a candid conversation with the owner of Atlas Bar, who invited us in as we were passing by, about how Venn has been a partner and advocate for his local business, the first bar in Shapira. I witnessed a rooftop meditation session, hobbyist painting and young families lunching in a neighborhood courtyard, and gaggle of laughing kids playing on the brand new play structure.

None of these encounters were planned. They were serendipitous and authentic. They showed me Venn's positive ripple effect in transforming a previously neglected area into a charming, engaging, and desirable community, and how beautifully the neighborhood residents were responding.

As a millennial who is renting, Venn's value proposition and the impact I witnessed first hand in Shapira strongly resonate with me on two levels:

1.Socially: While I don't consider myself a lonely person, I want more opportunities to expand my social circle, truly get to know my neighbors, and build roots in a larger community à la Cheers (cue "Where Everybody Knows Your Name"). Currently, the extent of my neighborhood engagement is limited to encounters with fellow dog owners when I walk my dog Enzo, or awkward small talk in the elevator. I can't honestly say I know my neighbors outside of remembering a few of their names, only because I've saved them in a phone note. And the only attachment I have is to the location of my building because I'm in a great area. I could easily move tomorrow and never look back, much to my landlord's chagrin.

2. **Livingwise:** I live in a 90-unit apartment building in LA that is owned by Greystar (which owns 500,000 units across 1,600 properties in the U.S.) and utilizes ActiveBuilding (a subsidiary of RealPage) for its residents' portal. I'm happy with my unit but the residents' portal does nothing for me. I haven't logged on since setting up automatic rent payments when I first moved in. I would much rather have the access to the thoughtful amenities, community spaces, resident services, and host that Venn offers through its digital platform (which also manages service requests, rent payment, messaging neighbors, marketplace to support local businesses, in addition to so many other things). In fact, I would happily pay more in rent (my landlord wishes!) for these upgrades, which are free for Venn Neighbors.

When I think about myself and the 140 million other millennials and Gen Zers like me in the U.S., the case for Venn is obvious. But on top of the resident experience-centric offering, Venn's invaluable insights and incomparable property management software for landlords make it a slam dunk.

Venn's Neighborhood platform is uniquely differentiated with best-in-class user experience and a robust technology moat that is lightyears ahead of the competition. With significant year over year growth, 37% reduction in vacancies, and 20% increase in new tenants through the platform in 2020, Venn has only just begun its hyper-growth phase. In 2021, Venn plans to expand to five more cities in the U.S. and rapidly increase unit volume.

A new Venn Neighborhood in Florentin, Tel Aviv

Like any long-term investor, we evaluate Venn not only based on past and present performance but how we expect the company to continue to grow well into the future. Venn's opportunity to increase market share in the $97BN total addressable market (U.S. property management systems) and revenue growth potential, thanks to its diverse platform, are truly endless.

Venn is led by an elite team of former IDF Special Operations officers with experience leading other successful technology companies who are as thoughtful and fun as they are skilled in execution. Group 11 is proud to back co-founders Or Bokobza (CEO), Chen Avni (CXO), and the entire Venn team as they eradicate urban loneliness and create the new Neighborhood-as-a-Service model for living where everybody knows your name.

Financing All Necessities Under The Sun(bit)

By Michelle Chang | May 2021

Sunbit announced a $130MM Series D financing led by Group 11 with participation from previous investor Zeev Ventures, as well as new investors Migdal Group, Harel Group, AltaIR Capital, and More Investment House.

The round values the company at a $1.1BN post-money valuation, adding Sunbit to the Global List of Tech Unicorns, making it the fifth in Group 11's continuously growing stable of unicorns. This is a major milestone not only for the company but also for Group 11 as it is the first time we are inducting a unicorn by leading a Series D financing round. Group 11 has been a backer of Sunbit since its inception 2016, when we led the company's first institutional financing round. We joined the company's board of directors and have connected the company with key employees and investors, including but not limited to Zeev Ventures, who also led the company's most recent Series C round, and all investors in this financing round.

While we have all seen various Buy Now, Pay Later (BNPL) players such as Affirm (AFRM) and Klarna rising to prominence recently, we believe Sunbit is poised to win the BNPL race as a truly disruptive and category-defining company. Sunbit's physical point-of-sale BNPL offering is unique with differentiated technology featuring a superior, AI-led underwriting infrastructure that creates value for both merchants and customers. Led by a stellar, veteran founding team, with perfect product-market-fit, and defensible technology and infrastructure, Sunbit is without a doubt the winning solution to take market share in the massive, underserved market.

Got 99 Problems and a Toothache is One

63% of Americans live paycheck to paycheck. 39% of Americans don't have enough money on hand to cover a $400 emergency. 56% of Americans have $5,000 or less in savings, while a third have $1,000 or less.

If Jill, an average American, found out she had to have an emergency root canal for her tooth pain, she would be slapped with a terrifying $1,800 bill. Without the money on hand, Jill would have very limited options. She could try one of the few legacy financing providers in the healthcare space. However, they only accept applicants with credit from the higher end of the spectrum, and still decline 50% of applicants. Or, instead of trying to apply for a new credit card at the POS, Jill would have to take out a personal loan with exorbitant interest rates and unfavorable terms, or try to come up with the money another way.

Unfortunately, Jill's situation is not uncommon. In fact, tens of millions of Americans find themselves similarly with their backs against the wall in dire financial situations because they have limited available cash and oftentimes cannot afford essential purchases.

In an effort to address this pain point, which is prevalent in various industries ranging from dental and eyewear to automotive services, point-of-sale (POS) financing in the U.S. has grown into a massive $391 billion market, comprising approximately 3.5% of the total annual consumer spending in goods and services. However, despite the market need and opportunity, until the launch of Sunbit in 2016, the POS financing system was broken and lacked adequate solutions. With long application processes, low approval rates, little transparency in the fine print, hidden fees, and unfavorable payback terms, legacy providers failed to help customers pay for necessary transactions during their time of need.

Sunbit's Genesis

Sunbit was founded by co-founders Arad Levertov, Tal Riesenfeld, Ornit Dweck-Maizel, and Tamir Hazan PhD in 2016 with the mission of making financing in-person purchases fast, fair, and easy with high approval rates for customers across the credit spectrum. Sunbit's offering is unique with an application that takes less than 30 seconds, requires nothing but a state-issued ID, phone number, email address, and does not involve a hard credit check. Once approved, unlike other legacy competitors, Sunbit approves 90% of applicants almost immediately, customers are given clear and fair rates for purchases up to $8,000 that can be split to 3, 6, or 12 monthly payments.

Because Sunbit is offered as a financing option at the physical point-of-sale, and the underwriting process takes seconds, Jill can apply for a loan at her dental office and be approved instantly, taking the fear and stress out of an unexpected but necessary transaction. No awkward conversations, no hassle at the time of payment, all the ease and control at her fingertips with an online tool to manage her plan, adjust payments, view activity, or pay off early.

The Physical Point-of-Sale Savior

Though Sunbit initially started by helping with emergency purchases, such as Jill's root canal or auto repairs, it has become the de facto Buy Now, Pay Later partner of choice for everyday needs across the auto, healthcare (dental and vision), veterinary, and education verticals.

For many customers, Sunbit was the first and only financial partner that *lent* a helping hand (pun intended) when no one else would. This early show of good faith in the customer has built immeasurable brand loyalty and equity amongst over a million customers who now increasingly turn to Sunbit to finance their other everyday purchases across expanded verticals. History, and Sunbit's incredible performance, have shown that when someone gives you financial access when no one else would, you become a loyal customer.

Sunbit's good faith has proven to be a successful business model. Sunbit originated over 125,000 loans in the first quarter of 2021 and is available at almost 7,000 locations. The company is on target to end the year with a million loan originations, a presence at almost 10,000 locations, and 2.4x year-over-year revenue growth.

The Sunbit Prophecy: What the Future Holds

Building upon the company's good faith business model, Sunbit's ultimate vision is to eliminate financial waste for Americans at every point-of-sale without having to be at every point-of-sale. This means "connecting all the dots", becoming the customer's preferred payment method across all channels: at the retailer's physical point-of-sale, online, and through device integrations with POS systems and card readers which will exponentially expand Sunbit's footprint.

In the future, Sunbit will be used to finance all types of transactions, not just essential or everyday purchases. Sunbit will effectively become a bank of sorts for customers, meeting all of their financing needs while encouraging financial literacy and responsibility.

We believe that Sunbit is a thoroughly differentiated platform that is rapidly increasing market share in a blue ocean opportunity. With triple digit year-over-year growth, Sunbit is on target to reach over 10 million loan originations since inception and $500 million in revenue in 2023. To read more on why we believe Sunbit is a category-defining company, read our previous article Gone in 60 seconds: How Sunbit is revolutionizing point-of-sale financing.

Group 11 is thrilled to welcome Migdal Group, Harel Group, AltaIR Capital, and More Investment House to this round. We are proud to continue supporting co-founders Arad Levertov, Tal Riesenfeld, Ornit Dweck-Maizel, and Tamir Hazan, PhD, and the entire Sunbit family in their mission to eliminate financial waste while passing value back to both merchants and customers.