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WHITEPAPER

Corporate *Venture* Capital

Profit and the Innovation Advantage

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Contents

Summary

P. 4

Corporate Venture Capital

P. 5

Goals

P. 10

CVC across Industries

P. 12

CVC in Europe

P. 13

A Spotlight on Banking and Insurance

P. 15

Key Considerations for Launching CVC

P. 18

Conclusion

P. 21

Endnotes

P. 22

Summary

As American big business evolved in the early 20th century, corporate venture capital (CVC) emerged as a tool both to strengthen the balance sheet and to uncover exciting new opportunities. A practice that started with industrial-age companies like DuPont is still employed by information-age companies like Google.

The objectives and structure of a CVC effort can vary greatly. Some companies take the approach of investing opportunistically when an attractive deal comes around, while others have created dedicated vehicles and robust in-house teams to manage the complexities of deal flow, diligence and portfolio support.

The reality is that venture capital (VC) is a risky asset class and, like all venture financing, CVC has more failures than success stories. There are plenty of examples throughout history of companies rushing into CVC during boom times, only to close up shop when the bubble bursts.

Today, a more enlightened path exists with partners like Anthemis, which can provide expertise in thesis building, investing and how this activity fits into an overall growth and innovation strategy. There are more resources than ever for companies to take a steady, professionally managed approach without a homegrown fund's labor and expense.

In this paper, we aim to provide insight into the practice of CVC, the exciting ways it is driving innovation, and the increasingly practical approach to partnering for corporate venture investing.

Corporate Venture Capital

History

At its most basic, CVC is an effort by corporations to invest in external companies. It is as simple as Company A taking a financial interest in Company B. But, most deals are much more complicated. The structure, strategy and goals that guide a corporate VC unit can take many forms.

In "Making Sense of Corporate Venture Capital," one of the most widely cited articles on the subject, Henry Chesbrough, professor at Haas School of Business at UC Berkeley, writes that a CVC investment is defined by two characteristics: 1) its objective; and 2) the degree to which the operations of the investing company and the startup are linked.[1]

This concept generally boils down further to: 1) Will you invest for profit or access to innovation?; and 2) Will you be an active or passive partner for your portfolio?

Considering these two variables is vital for the identity and direction of a company's VC effort. Some may operate like traditional venture capitalists (VCs) looking to maximize returns on a pool of investment capital. Others may be more focused on finding innovation to support their existing business lines.[2]

The common thread through the CVC ecosystem is a partnership to drive mutual growth. In most cases, investors want to experience a financial return, but they are also glad to get a close look at innovation occurring outside of their walls. In many cases, investing in startups can be more valuable than good market research because investors get insight through a real product with real customers.[3]

Companies receiving investment can often also leverage resources from inside the corporate investor, be it access to customers, subject matter expertise or, in the case of financial services, experience with regulation. Likewise, corporate investors may have immediate use for products within their portfolio companies.

It is worth noting that CVC is not synonymous with VC; rather, it is a subset of VC with its own nuances. A CVC effort may have more

What's your CVC mission?

1) Will you invest for profit or access to innovation?
2) Will you be an active or passive partner for your portfolio?

variables to consider than a traditional VC firm. For instance, a company needs to determine whether it will invest opportunistically off the balance sheet, create a dedicated venture capital arm of the business, or partner with a VC firm to help manage investments. Strategy can vary considerably depending on the sector focus or strategic goals of the company beyond maximizing returns.

We will go into more detail later regarding the advantages and challenges of the varying CVC structures and how a VC firm, such as Anthemis, can be a helpful partner in creating a framework to enable a corporate venture function to be successful.

Early days of corporate venture capital

CVC is far from a new concept; instead, it has been a tool used by pioneers and mainstays of American business for more than a century. Giants like 3M, Alcoa, DuPont, Ford and General Electric were among some of the earliest corporations to experience the rewards of a successful corporate investment program.

A significant proof-of-concept for CVC came from DuPont. In 1914, the company's head of finance, John J. Raskob, recognized some synergies with a six-year-old automobile startup called General Motors (GM), leading to a successful partnership. Raskob believed that a boon to the automobile industry would also create demand for products produced by DuPont, such as paint and artificial leather. He convinced the chemical and plastics manufacturer's president, Pierre S. du Pont, to invest in the fledgling GM.[4]

The investment was a blockbuster in many ways. GM went public in 1916 and saw its stock grow seven-fold as automobiles became essential during World War I. It gave DuPont an incredible return on its investment, a significant new customer and an opportunity to marry the innovation happening inside both companies. For instance, the companies discovered that a smokeless powder developed by DuPont during the war could be added to paint, cutting the drying time on a car from weeks to hours.

DuPont, alongside others employing the earliest instances of CVC, managed to prove that the model in various forms could benefit both corporations and startups.

Pioneers of Corporate Venture Capital:



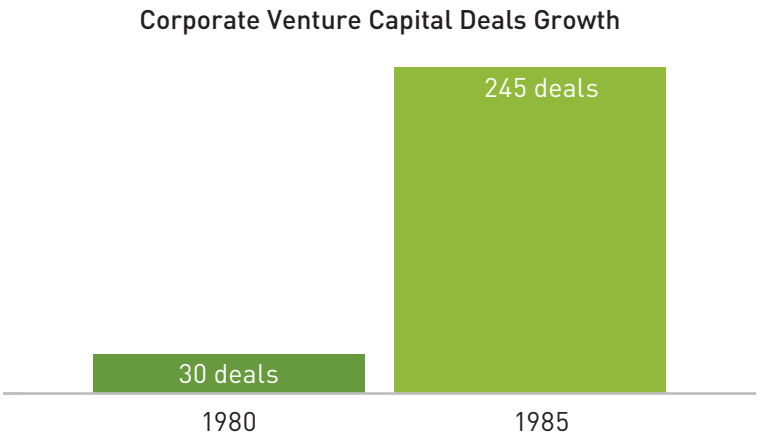








Expanding on the proof

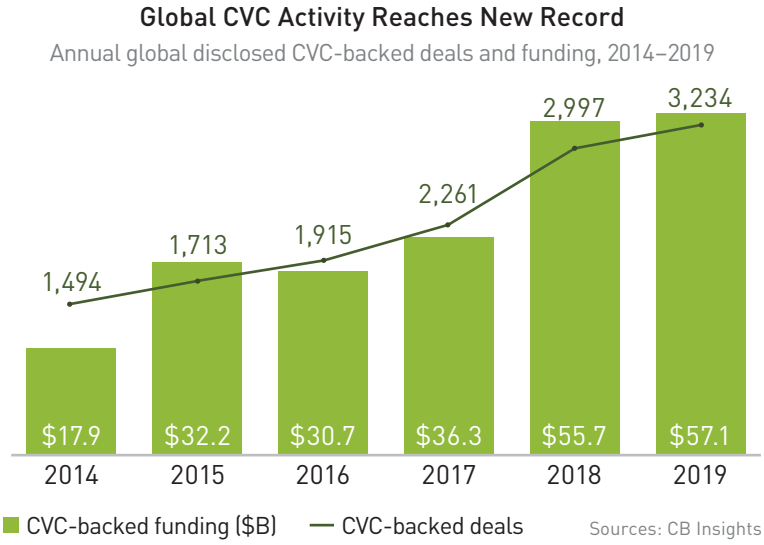


CVC had a significant role in helping some of America's most iconic companies diversify and driving the nation's entrepreneurial spirit. The investing practice has certainly evolved since the early days, but most of the fundamental goals have remained the same.

Fast-forward to the 1980s, CVC had grown to make up a meaningful portion of total VC dollars, up to 20 percent by 1989. As more companies looked to extract value from corporate venture initiatives, many began outsourcing investment activities to independent VC firms. Companies also leaned into a client-based fund approach, partnering with external fund managers dedicated to a company's investment goals. Others went all-in on their own in-house VC teams. The number of companies that built internally managed venture practices accelerated from just 28 in 1982 to 76 in 1988. And, CVC deals jumped from 30 in 1980 to 245 deals in 1985.[5]

This era continued to see CVC investments from those who helped develop the practice, including DuPont, General Electric and Johnson & Johnson. A new wave of CVC investors also developed alongside the technology boom (which itself was driven by a significant increase in overall VC) of the 1980s and early 1990s, helping spur the adoption and proliferation of computers across industries and eventually in consumers' homes.

Corporate venture capital lessons from boom times



This computing revolution enabled the emergence of the internet as we know it, kicking off an explosion in CVC funds and deals in the technology space. CB Insights data shows that nearly 100 companies made their first corporate venture investments between 1995 and 2001. The amount of capital in the market from CVC investors grew to $17 billion in 2000, a quarter of total VC funding that year. Corporations plowed money into venture initiatives, with less common players including media companies like News Corp., Comcast and WPP Group joining investment syndicates for dot-com companies. WPP, for instance, invested in an online cartoon-animation company, an arts-and-crafts portal, an online grocer and a bond-trading site. "This grab bag of Internet businesses reflects the uncertainty surrounding the Web," *The Wall Street Journal* wrote at the time.[6]

While this exuberance was great for startups of the era, CVC became a short-lived experiment for many companies. Excessive speculation of online enterprises created a bubble that finally burst in 2000, wiping out many of the gains posted during the era. Many venture-backed startups closed their doors and CVC efforts either paused or ceased.[7]

Interestingly, there is some evidence that companies, at the time, with corporate VC arms went public at a higher percentage than those without such strategic funding. Traditional funds still outperformed, but the benefits that corporate investors can provide beyond capital seemed to come into focus during the downturn.

While there was undoubtedly a retreat, CVC did not leave the market entirely. Investments from corporations across verticals hovered around $5 billion through the end of the decade before heating back up again in 2011. The Web 2.0 era offered investors another swing at internet businesses. Even Microsoft was back in the game, paying a whopping $240 million for a 1.6 percent share of social networking company Facebook at a valuation of $15 billion. The investment received plenty of speculative commentary, but, ultimately, it proved to be one of the most successful corporate venture investments in history. Ten years after Microsoft wrote that check at a $15 billion valuation, Facebook was worth $508 billion, up more than 30x from its 2007 level.[8]

Modern CVC

Today, CVC remains a significant contributor to the establishment and growth of young companies and a partner for accelerating innovation at established companies.

In 2019, CVC activity hit an all-time high. Globally, there were 3,234 CVC deals worth $57.1 billion. As of September 2020, CVC investors participated in 25.5 percent of all US VC deals.[9]

Also, 77 percent of Fortune 100 companies invest in VC, and 52 percent of Fortune 100 companies have their own investment arms.[10]

Goals

As we have discussed, CVC investments fall into two categories—financial or strategic.

In 2019, GV (formerly Google Ventures) was the most active investor in unicorn companies, backing nine companies valued at $1 billion or more.

FINANCIAL

Some corporate venture investors are all about the money. They expect to invest with terms as favorable as traditional VCs and bring significant returns to the parent company. Investors rely on the parent company's expertise in specific markets or technologies to assess the winners and then leverage resources from inside the company to help the investment scale.

Alphabet's VC arm, GV (formerly Google Ventures), has invested in more than 120 companies since its creation in 2009. While the company has invested across various sectors, including healthcare, fintech and artificial intelligence, its goals are not purely strategic. In addition to being one of the most prolific corporate investors, GV has been one of the most successful. In 2019, GV was the most active investor in unicorn companies, backing nine companies valued at $1 billion or more.[11]

STRATEGIC

Some investments are more weighted toward strategic results. In this instance, investments are intended to increase sales and profits of a company's existing businesses. The investor may also view a strategic investment as an opportunity to explore a new, adjacent customer segment or business line, learn about an emerging technology or exploit synergies between itself and a startup to test a product or market.

UPS, the multinational package delivery and supply chain management company, has operated a venture unit for decades. UPS Ventures has maintained a strategic approach, investing in ideas applicable to its business, such as a mail digitizing service, autonomous driving software and delivery tracking technology. UPS says of its portfolio or early stage companies: "All have one thing in common: what they do might help fuel each of our [companies'] growth for the next hundred years."[12]

Creating a segment

In most cases, these goals are intertwined. Corporate investors aim for successful returns as much as any VC, but there is a meaningful opportunity to drive innovation. Some corporate investors have taken a creative approach, investing in companies offering services that create new markets for the investor's core products.

An excellent example of this strategy is Salesforce, a publicly traded software giant with more than 150,000 customers using its cloud-based customer relationship management suite. The company's offer includes enterprise applications developed for customer service, marketing automation, analytics and application development.

The company's investment unit, Salesforce Ventures, invests in enterprise cloud companies with offerings it believes it can extend to Salesforce customers. Since 2009, Salesforce Ventures has invested in more than 400 companies, including DocuSign, Twilio and Zoom.[13] Salesforce Ventures was one of the most active corporate investors in 2020, adding 47 companies to the portfolio.

This model has produced considerable financial returns, a window into technologies that can be a positive addition to the Salesforce platform, and an opportunity for the company to build the world's largest ecosystem of enterprise cloud companies.

Intel Capital found similar success in the mid-1990s, setting a strategy to invest in "companies building technologies that supported, were sold alongside or improved the value of Intel's products in the marketplace," according to a *Harvard Business Review* case study.[14] In 2002, Intel was set to introduce its new Centrino chip, which included built-in support for both the 802.11a and 802.11b wireless LAN technologies. To drive demand for the chip, Intel Capital deployed a $150 million fund to invest in Wi-Fi companies.[15]

CVC across Industries

Johnson & Johnson

Johnson & Johnson is one of the pioneers of corporate investing and continues to operate a healthy practice. The VC unit rebranded in 2013 as Johnson & Johnson Innovation JJDC with a mission to "generate transformational healthcare solutions."[16] The fund invests across sectors—pharmaceuticals, medical devices and consumer healthcare—and at all stages, from seed level startups to Series B and beyond.

Kellogg's

In 2016, the Kellogg's Company—of Frosted Flakes and Pop-Tarts fame—announced a $100 million VC vehicle. Eighteen94 Capital (1894) invests in startup businesses "pioneering new ingredients, foods, packaging, and enabling technology."[17]

Ford Motors

Ford does not have a formal investing unit. However, the company has been investing directly in technologies that could support its mission. Last year Ford announced a $500 million investment in electric vehicle startup Rivian.[18] As part of its investment, the company intends to develop an electric vehicle that leverages Rivian's battery pack and electric motor design.

Bumble

Dating and networking app, Bumble, launched the Bumble Fund in 2018, a vehicle focused on early stage investments, primarily in businesses founded and led by women of color and those from underrepresented groups.[19]

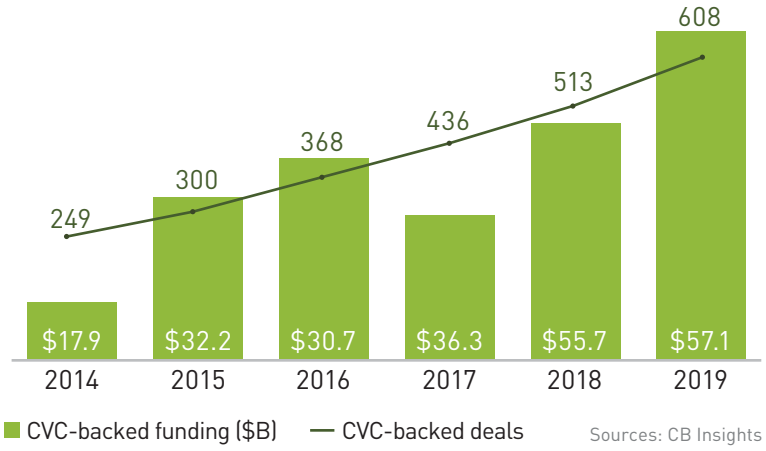
Sesame Workshop

You may not expect to find a VC fund on Sesame Street, but the producer of one of the most celebrated children's television shows in history started a VC arm in 2016.[20] Sesame Ventures aims to partner with kid-friendly startups and those addressing changes in the digital media landscape. Companies in the portfolio receive funding, coaching from Sesame executives and access to Sesame characters and branding.

CVC in Europe

Europe-witnessed CVC-backed Funding and Deal Records

Annual disclosed CVC-backed funding to Europe, 2014–2019



Sources: CB Insights

Europe has a vibrant ecosystem for CVC investment and there continues to be momentum in this area. Total deals in Europe-based companies grew to 608 in 2019, an increase of 19 percent over the previous year.

CVC-backed funding also increased, growing 38 percent from $5.4 billion in 2018 to $7.5 billion in 2019. There is particularly strong momentum in the UK and Germany, which account for nearly half of all CVC-backed deals in Europe.

In fact, CVC-backed funding to UK-based companies doubled YoY to $3.5 billion in 2019, surpassing the previous record set in 2016. CVC-backed deals in the UK grew by 11 percent from 131 in 2018 to 145 in 2019.[21]

One of the most exciting areas of CVC investment in Europe is the financial services industry. Investment in fintech, including insurtech, has skyrocketed in recent years as a result of the digital revolution across the industry and challenges faced by traditional financial institutions.

While, previously, banks may have viewed fintech startups as competitors, today they are more open to partnership than ever. By collaborating with burgeoning companies, CVC investors now have a window onto technologies and markets that are either emerging or being disrupted.

Increasingly, banks are recognizing the benefits of working with early stage fintech startups through incubator and accelerator programs. For instance, Anthemis has an active Venture Partnerships team that works with partners like BBVA and Barclays to create new businesses in sub-sectors of financial services, including insurance and banking. We also help to create companies that challenge the current definition of finance by exploring where this intersects with adjacent sectors to anticipate market shifts.

A Spotlight on Banking and Insurance

Aviva



Overview:

Aviva plc is the UK's leading insurer. It exists to be with people when it really matters, throughout their lives—to help them make the most of life. Aviva has been taking care of people for more than 320 years, in line with its purpose of being 'with you today, for a better tomorrow'. In 2020, Aviva paid £30.6 billion in claims and benefits to its customers.

Goal:

In August 2020, Aviva set out its priority to simplify Aviva's portfolio. Aviva is now focused on the UK, Ireland and Canada where it has leading market positions, significant potential and is investing for growth. Its businesses in continental Europe and Asia are being managed for long-term shareholder value and where strategic objectives cannot be met, Aviva will withdraw capital. Aviva has stated that it is looking to transform the group, improving its performance and efficiency whilst managing its balance sheet prudently, reducing debt and increasing the group's financial resilience.

Investments:

Aviva Ventures' role is to invest in emerging technology and customer trends that have the potential to transform the existing insurance business model, accelerate the Aviva strategy and provide insights into how Aviva will need to adapt to the changing savings, retirement and insurance landscape. Aviva has extended its relationship with Anthemis to enable the company to lean into the strategic insights and access to evolving later stage insurance companies that the partnership provides.

Baloise Group



Overview:

The Baloise Group is more than a traditional insurance company. The changing security, safety and service needs of society in the digital age lie at the heart of its business activities. The best possible customer service, combined with innovative products and services, makes Baloise Group the first choice for people who want to feel "simply safe". Located at the heart of Europe, with its head office in Basel, the Baloise Group is a provider of prevention, pension, assistance and insurance solutions. Its core markets are Switzerland, Germany, Belgium and Luxembourg.

Goal:

The thesis is to focus on startup investments in ecosystems that are important to the Group: core insurance and data, home and mobility. Alongside financial returns, additional goals are to recognize patterns and trends into new business models, link up with additional innovation initiatives in the Group, initiate collaboration with startups and accelerate overall digital transformation. Partnering with Anthemis allows Baloise Group to evaluate a much larger, global pool of potential investments, combine learning from adjacent ecosystems, as well as have a wider insight into the VC space.

Investments:

Baloise Group's portfolio companies are supported by an extensive network of advisors and experts from Anthemis, as well as access to the company's teams and expertise. The Baloise Group actively creates opportunities for investment portfolio startups to get insight and access into operations of a large insurer in cases where this creates mutual benefits, growth opportunities and product improvements. This can include risk and insurance expertise as well as ecosystem integration.

Barclays

Overview:

Barclays is a British Bank with a global footprint. A household name in the UK with its consumer banking and payments operations, Barclays also has a strong global corporate and investment banking presence in both the United Kingdom and internationally. Barclays recognizes the importance of partnering with Fintechs to drive innovation in their products and services. They have a robust Fintech offering including Rise, a global community of top Fintechs, physical co-working spaces in London and New York, investment through their Principal Investments business and dedicated Fintech programs to drive collaboration between Fintechs and the Bank.

Goal:

Alongside Barclays mission for Fintech collaboration, Barclays is committed to supporting and growing the next generation of female led businesses. Applying this lens to their work in the tech start-up ecosystem, the bank is on a mission to create gender equity in the start-up industry and recognizes that diverse founders are fundamental to developing tech solutions that will build a more inclusive future. Barclays and Anthemis have become natural partners in developing a solution to remove some of the key growth barriers of access to capital and support for female Fintech founders, with the hope this will drive a more diverse set of products and services that Barclays can collaborate with to appeal to a wider audience.

Investments:

As part of Barclays' unique approach to CVC, the bank partnered with Anthemis to co-create the Female Innovators Lab, a venture studio dedicated to cultivating entrepreneurial talent in women across the financial services ecosystem. Entrepreneurs who join the Lab will receive human, intellectual and financial resources, backed by an extensive network of advisors and experts from Anthemis and Barclays. Additionally, entrepreneurs will receive mentoring and guidance from subject matter experts from Barclays, all of which will be focused on helping founders develop their concept fully and refine it in advance of pursuing additional funding.

Key Considerations for Launching CVC

The in-house approach

Having a homegrown VC effort integrated closely with the parent company offers benefits. Some of the best in the game are well-staffed, sophisticated VC funds that are turbocharged by the knowledge and resources that exist across the company.

But, the fact of the matter is that running a venture firm is hard. An in-house effort requires a real commitment to infrastructure, talent and processes that may be unique to that business.

Will the fund's goal be profit or access to innovation? How will the fund complement other innovation activities in the company? Can a high-quality deal flow be established? Has a methodology for diligence been built in? Does the management team have the bandwidth to work closely with the portfolio? If other members of the company are involved, do they understand the uniqueness of corporate venture? Does the company have the resources in place to make sure the fund can meet its strategic objectives?

Another important consideration is how in-house investors will be recruited and compensated. Typically, compensation at traditional VC firms includes carried interest, a share of the profits of an investment paid to the investment manager. In the instance of a significant liquidity event, this type of bonus can be highly lucrative for investors. Such a big payday for the CVC team can cause friction within a corporation where there are executives of other units in the business. But, if a CVC unit cannot compete on compensation, it may not be able to attract the talent that would give the fund the best chance of success. This is a significant reason why many corporations have trouble sustaining an investment team that can have a lasting presence in the VC landscape.

Corporate venture investors have been called "tourist investors," meaning they pop into the ecosystem for the good times but back off in difficult economic circumstances. That type of swell was seen during various technology booms along with some reckless behavior from corporate investors who may have entered the CVC business

because of a 'fear-of-missing-out' rather than executing a thoughtful, dedicated strategy. An in-house venture capital effort can have incredible success, but it requires extraordinary commitment.

Building with an experienced partner

Keeping the investment team under the same roof is not always the best choice for CVC. In many cases, bringing in investors with existing knowledge and networks may be the more strategic approach. Partnering with an existing VC firm that can bring investing expertise and deep domain knowledge can make an ideal fit. For instance, Anthemis has become one of the world's leading fintech and insurtech investors with a portfolio of more than 100 diverse investments across geographies and more than $674 million in assets under management. The company has a 10-year track record cultivating change in financial systems, which has resulted in about 90 percent of the capital under management at Anthemis coming from banks and insurance companies. A partner like Anthemis can help a company establish a measured VC practice with far less friction than an in-house upstart investment team.

Anthemis has become one of the world's leading fintech and insurtech investors with a portfolio of more than 100 investments and more than $674 million in assets under management.

As an example, there have been instances where a startup has turned down a direct investment from a large brand bank or insurance company, afraid that this may deter potential clients fearful of exposure to a competitor.

By partnering with a venture firm such as Anthemis, a company can get a front-row seat to innovation without its brand interfering. This is an easier path to obtaining valuable insight across the market, helping inform in which direction to steer business objectives and investments.

Another significant advantage of working with an outside venture firm is built-in portfolio support. Anthemis provides a variety of services, including a purposefully designed platform to introduce portfolio companies to its ecosystem for business development, talent, marketing and fundraising. With a dedicated portfolio support team that spends each day finding helpful connections, the strategic benefits of a venture program are experienced much faster.

Finally, CVC is not the only path for corporates to engage in outside innovation. The number of ways that companies can execute experiments, proofs of concepts, mentoring and startup partnerships

that can be beneficial for all is increasing. For instance, Anthemis has been able to provide a bridge to companies that are anxious to know more about the evolving fintech ecosystem, but are not ready to go all-in with a CVC effort. There are still many ways corporations can help entrepreneurs advance meaningful ideas.

CVC CHECKLIST

TEAM

- ❑ Will you assign an internal team or hire an external team?
- ❑ Who does the team or function report to? Why?
- ❑ How will you compensate the team?

STRUCTURE

- ❑ Will you invest directly from the balance sheet, create a dedicated fund and/or invest in external funds?

FOCUS/STRATEGY

- ❑ What is the investment thesis?
- ❑ Is the investment thesis long-term in its thinking, or is it addressing near-term challenges?
- ❑ Can the companies operate anywhere, or do they have to be in the country/region of your company?
- ❑ Will you focus on returns or accelerating innovation?

DEAL FLOW

- ❑ How will you source deals?

DILIGENCE

- ❑ Do you have personnel and processes in place to analyze opportunities?

MAINTENANCE

- ❑ Do you have a plan for the many administrative tasks required to run a fund?

PORTFOLIO SUPPORT

- ❑ Do you intend to provide services beyond capital to nurture your investments?
- ❑ How can your company's employees and ecosystem support your portfolio?

Conclusion

CVC has played a significant role in building America. Consider that GM, which is now pushing forward with exciting advancements in electric powertrains and self-driving features, might not have been a part of the automotive landscape without an injection of capital from DuPont. Microsoft was willing to invest hundreds of millions of dollars into a company outperforming them on social products. That investment in Facebook returned billions to Microsoft. Salesforce has now written checks to more than 400 companies building tools and services complementary to its mission. There is even CVC on Sesame Street.

The CVC model has proven that it can be an incredible pipeline to innovation. In some cases, this could produce a key partnership, an acquisition target or, possibly, a meaningful return on invested capital.

A CVC effort is not a guaranteed success, even for the largest funds. In order to reach maximum potential, companies need to be thoughtful about how they will structure a CVC initiative. An in-house approach requires a plan for recruiting and compensating talent and a dedication to involving relevant business units that can find synergies with startups. Alternatively, a partner like Anthemis can bring both a strong investment team and an exceptional understanding of an industry. What is more, a partner probably has the portfolio support services necessary to win and nurture investments.

At Anthemis, we believe we are incredibly well-positioned for the future of finance and insurance. We continue to fill our portfolio with outstanding entrepreneurs working on next-generation tools and services. And, we are excited to find new partners that will help accelerate this dynamic era.

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anthemis

Anthemis cultivates change in our financial system by investing in, growing, and sustaining businesses committed to resiliency, transparency, access and equity.

Founded on three guiding principles—authentic collaboration, virtuous cycle outcomes and diversity and inclusivity—our deep understanding of markets and models, passion for emerging technology and values inspire everything we do.

By creating fertile ground for a diverse group of startups, investors, entrepreneurs, institutions, academics, and visionaries to converge, we believe we can solve the financial systems most pressing challenges faster, better and for the benefit of all.

For the latest on the Anthemis ecosystem, visit: anthemis.com/insights/

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