penjana Kapital presents

The Kapitalist Monthly

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Editor: Ilyas Ishak

An informal partner ecosystem network, dubbed as MyTED which includes Penjana Kapital, recently hosted a roundtable. Amid the pleasant industry chatter and coffee, an odd question cropped up. "How do you stay positive?". It came from an institutional investor. She was puzzled by my posture against a backdrop of uncertainty, doom-mongering and dour outlook – the economy, the energy, the environment, you name it. In answer to her question, I think there is plenty to be upbeat about. The purpose of venture capital is to look beyond short-term cycle, and I keep reminding myself that we are investing in innovation and for the long-term. We look beyond the headlines to find fresh ideas and solutions that nudge the world towards more nuanced and nicer outcomes. We pride ourselves on embodying our motto "no great idea goes unfunded".

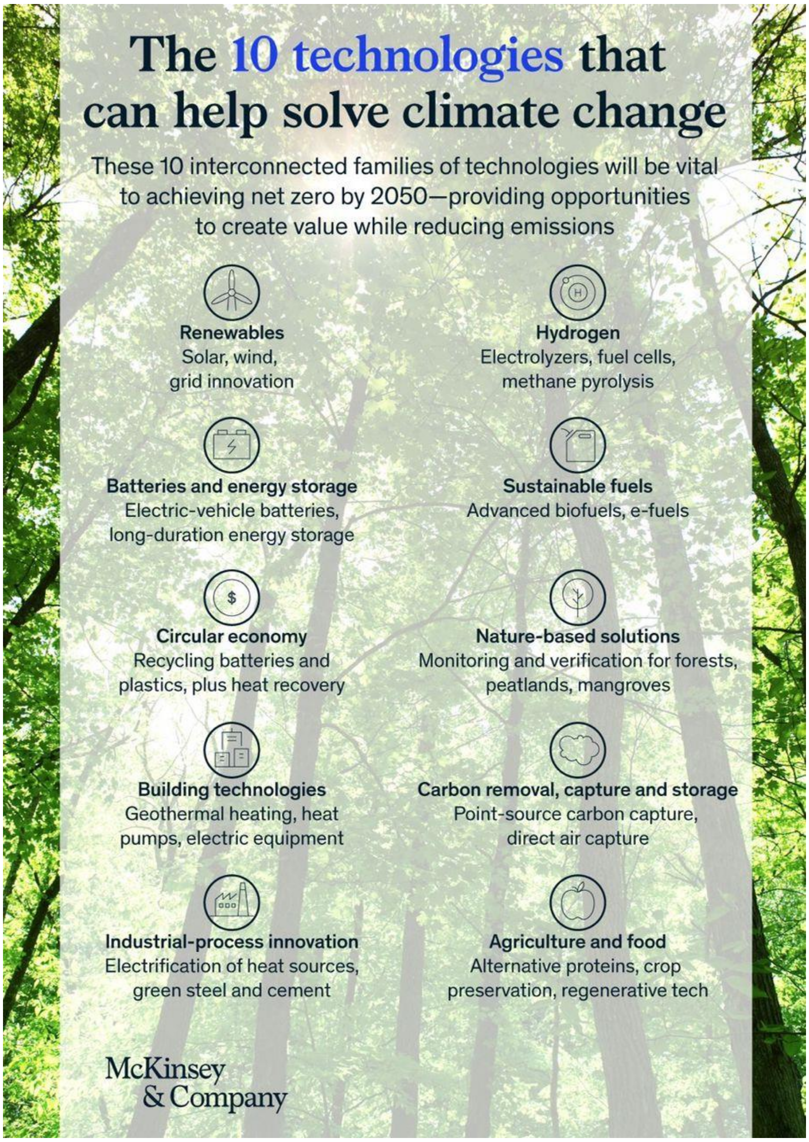
As temperatures soar and the cost of living continues to rise, governments scramble to hire their own chief heat officer. In the UK, the newly created post is called director-general of winter resilience. Jonathan Mills was recently appointed to the post and his immediate priority is to ensure that the country does not bear the brunt of looming energy-supply issues this summer and in the winter. That means managing the rise in costs, making sure that people can keep their homes cool in hot weather and heat their homes in the colder months and avoiding power cuts. My British friends have complained that their summer evenings are too warm, leaving them sleepless in the heat. And most Malaysians who went to school or worked in the UK would know that it is not easy to reach for air conditioning. Just 1% of the buildings in the country have fixed cooling systems, and a further 3-5% have portable cooling systems. That is likely to change as summers get warmer.

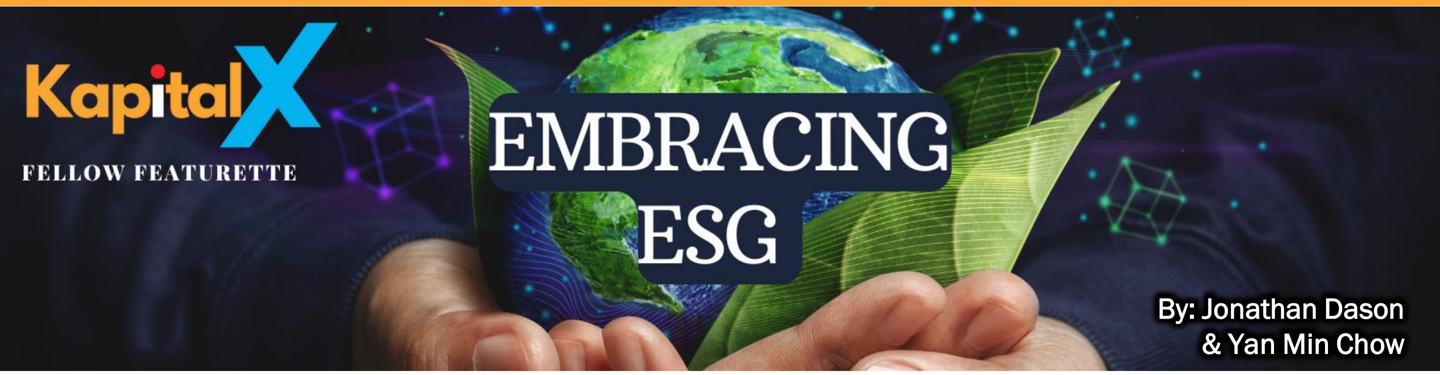
By 2035, it's reported around 20% of London homes will require air conditioning. That is a lot of new AC units. These will use huge amounts of electricity, far more than any other appliances in the house, and they will have an emissions impact to match. As the UK embarks on its air conditioning spending spree, it mirrors a transition that is already under way in much hotter places. In Malaysia and other emerging Asia, AC demand is soaring as incomes rise. Owning an AC unit can be life-changing for us living in tropical climate. By 2050, two-thirds of the world's households will have an AC. Collectively, this will have a gigantic impact on our energy use. AC and fans already account for around 10% of the world's electricity consumption. And they are particularly challenging for electricity grids because demand surges on hot days and often threatening the network stability if the grid cannot keep up. All these new AC units currently being bought will also have an emission impact namely from the carbon dioxide produced by the electricity grid (unless it is all clean power). Yet as the planet gets warmer, more AC will be necessary to sustain human life especially in the world's hottest places, driving a vicious cycle. Access to air conditioning exacerbates the inequality at the root of climate change. People who are poor produce the least emissions, yet they are also the most exposed to the effects of warming. Meanwhile the rich can afford to buy their way out of it and stay comfortable.

Scientists have been busy documenting our changing climate over the past few years and predicting that more adverse weather is to come. They hope to use creative ways to showcase the changes as they happen. As rain clouds gather (no pun intended), policymakers need to unite by vulnerability to the world's warming and find ways to humanise the climate crisis. Virtually every activity in modern life – growing things, making things, getting around from place to place – involves releasing greenhouse gases, and as time goes on, more people will be living this modern lifestyle. In 2020 disaster struck when a novel virus Covid-19 spread around the world. Because of lockdown measures and economic activities slowed down so much, the world emitted fewer greenhouse gases in 2021 than previous years. The reduction is probably around 5%, and in real terms, that means we release the equivalent of 48-49 billion tonnes of carbon, instead of 51 billion. A meaningful reduction and the world would be in great shape if we could continue that rate of reduction every year. Unfortunately, this is impracticable. Consider what it took to achieve this reduction, millions have lost their lives and many more lost their livelihoods. This is not a situation that anyone would want to repeat. This is evidence that we cannot get to net zero carbon emissions simply by giving up on what we have. Just as we needed new vaccines for Covid-19, we need new tools for fighting climate change: zero-carbon ways to generate electricity, make things, grow food, keep our homes cool and warm, and move people and goods around the world.

> *"**Venture capital** has effectively functioned as the gatekeeper to the deployment of capital in the past and is presently seeking **cycle-proof investments in more promising and more** sustainable **opportunities**."*

Venture capitalists call for breakthrough ideas, chase innovations and catalyse impacts. Given the focus on long-term, venture capital is mobilised to finance innovations that deliver future needs and fund entrepreneurs who seek to effectively solve current societal problems. The world currently faces an unprecedented combination of compounding high-stake crises: the climate emergency with its increasingly dramatic consequences, the growing concentration of wealth as well as social inequality, and the national political dysfunction that serves as a headwind to overcoming socio-economic malaise. These are E,S,G-related megatrends that define us. Venture capital has effectively functioned as the gatekeeper to the deployment of capital in the past and is presently seeking cycle-proof investments in more promising and more sustainable opportunities. And after events like the Global Financial Crisis and the Covid-19 Crisis, there is a recognition that we need to factor in risks. We cannot let short-term interests affect decisions that will hurt in the long run. There has never been a time of greater promise or of potential peril. The heat is on, and the time is now.





Editor's Note: In this month's edition of the The Kapitalist Monthly, Penjana Kapital's KapitalX fellows, ***Jonathan*** *and* ***Yan Min****, weigh in on the topic of ESG. Jonathan and Yan Min are both part of Penjana Kapital's KapitalX programme, a Venture Capital (VC) talent development programme that equips participants with a detailed overview of the VC ecosystem with real-time practical application and networking opportunities. KapitalX is organised by Penjana Kapital together with Sunway iLabs.*

What really is ESG?

ESG (Environmental, Social and Governance) is a holistic concept that encourages businesses to seriously consider issues beyond the traditional scope of a company's bottom line. This includes thinking about the business' environmental impact, employee culture and the ethics of how the company itself is run.

The **Environmental** criteria evaluates the company as a responsible steward of nature. The **Social** criteria focuses on how the company manages its relationship with employees, suppliers, customers and the communities in which it operates. **Governance** refers to how the company manages itself and its operations which includes the company's internal controls, compensation policies and shareholder rights among others.

With an increasing number of venture capitalist firms jumping on to the ESG bandwagon (e.g. 500 Global, Kinnevik, Gobi Partners), the future of VC is being shaped through ESG. It's likely a trend that's going to stay.

Why should VCs care about ESG, especially for their portfolio companies?

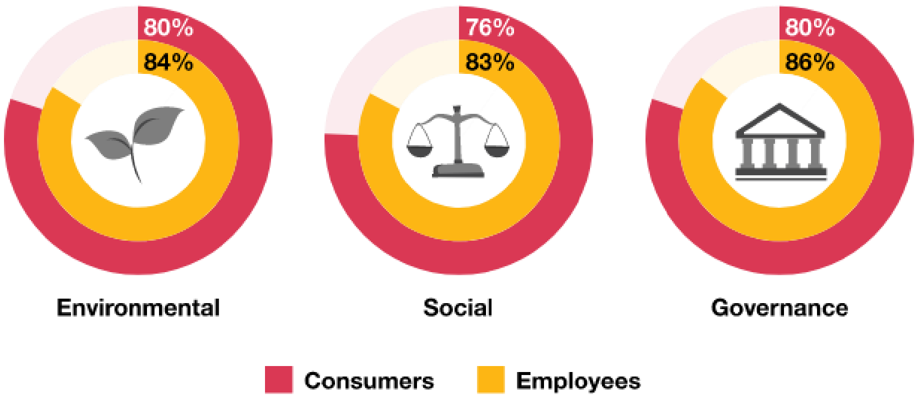
As allocators of capital, VC often plays a crucial role in shaping innovation and the way in which society develops, not to mention a role in driving the engine of job creation. Historically speaking, VC has brought about the growth of many iconic companies such as Uber, Airbnb, Twitter and Google, among others, that have gone on to transform society. VC fund managers, as early investors, therefore have the opportunity to determine start-ups' direction of growth as well as to help set the culture and values of these companies as they scale.

There are a number of reasons as to why VC firms should embrace ESG. First, multiple studies have shown that the neo consumer increasingly care about ethical business practices along with the impact of their consumption on the vulnerable and the planet. This has resulted in a shift in consumer markets, where we see the rise of sustainable fashion, food and the like.

Second, the rise of "mission driven" founders. Perhaps it's a generational trend or that these individuals might be neo consumers themselves. Either way, more and more founders are starting companies producing products and services while running their operations with 'sustainability' in mind, adhering to many ESG principles early-on. This care for sustainability applies to many young talents too, as they look for employment.

ESG commitments are driving consumer purchases and employee engagement

I am more likely to buy from / work for a company that stands up for...



Q: Please indicate how much you agree or disagree with the following statements.
Consumers (n=5,005) | Employees (n=2,510)
Source: PwC Consumer Intelligence Series June 2, 2021

Third, for limited partners and investors, ESG represents a robust toolkit for risk management. This applies to both the investee companies and the operations of the VC firm. For example, the industry has been criticized for its lack of diversity and a poor track record of sexual harassment incidents - embracing ESG can help mitigate these issues while protecting both the firm and investee companies from the downsides such as climate-related risks, social risks (e.g. human rights) and governance concerns.

In addition, studies have shown that managing ESG risks results in better financial outcomes and it comes with the added benefit of improving the brand while strengthening customer relationships.

Fourth, from an ecosystem perspective, a focus on ESG fosters a healthy investment chain by starting early-stage companies right. As the business scales, the level of risk associated with poor ESG management also increases and at some point the business will have to treat one or more of its Environmental, Social and/or Governance issues more seriously. Addressing these issues at the early stage with the goal of being “ESG ready” helps to improve the investment ecosystem for future strategic corporate buyers, later stage investors or the public market should the company go public.

Finally, having an ESG focus is considered a subset of sustainable investing - that is, investing with a holistic and a long-term mindset. This encourages investee companies to resist the urge of unsustainable short-term gains and improves the chances of a business sustaining its operations into the following years.

How can a VC get started with ESG?

It can be daunting to navigate the ESG space with its numerous frameworks, acronyms and standards. In general, there are 3 ways in which a VC firm can approach integrating ESG into its operations: (1) Systematic approach - this method premises itself on integrating ESG factors across the investment process; (2) Targeted approach - this method sifts through the ‘universe’ of ESG issue to only focus on what is material to the respective businesses; (3) Outcome-oriented approach - this method prioritises progress against a well-established framework, for example the United Nations Sustainable Development Goals (UN SDGs).

Although a number of established ESG frameworks do exist, adapting them for a VC fund is not necessarily a straightforward ‘cut & paste’ process. This is because the available frameworks may not be fit-for-purpose and offer little in the way for early stage companies to easily adopt, as they are often strapped for resources. Given VCs’ focus on long-term impacts, the funds often strike a balance of integrating shareholders’ consideration and ESG in assessing promising start-ups.

ESG integration is a function of the VC’s internal operations and the ability to communicate its commitments and requirements to its limited partners, the wider public, its portfolio companies as well as potential investees. This process begins with the development of an ESG policy. This policy covers the scope of the fund’s ESG investments, defines its ESG goals and strategy. The important thing here is not to make ESG a ‘box ticking exercise' but rather a tool used to holistically review both potential and current portfolio companies. Here are some key ESG areas that the policy should focus on:

- Diversity & Inclusion
- Team & Working Environment
- Climate-liked Risk and Environmental Impact
- Supply Chain Considerations
- Data Privacy & Security
- Responsible Product Design & Marketing
- Legal & Regulatory Considerations
- Governance

Please note that these ESG areas should not be limited to the evaluation of investee companies but should be also used as a tool to improve the VC’s own internal operations.

Next, once the ESG policy has been defined, it should be used to guide the screening of companies in the pre-investment stage. Some of the best practices in the industry include integrating ESG considerations into the due diligence process as well as including ESG-based clauses into term sheets.

Once an investment is made and the start-up becomes a portfolio company, the VC should play an active role in identifying the ESG gaps of the portfolio company, set ESG-based developmental targets and KPIs for the company, track and measure progress as well as offer support in terms of resources for the company to meet the fund’s ESG targets. And finally, on a regular basis, the VC firm should produce an ESG report on both the fund’s and portfolio company’s progress.

ESG Trends in Private Markets

The topic of ESG has been on the lips of most investors, especially in the public markets. Incorporation of ESG encapsulates the Stakeholder Theory as introduced by Edward Freeman, leading to a more holistic value creation. The private market players, though have been lagging behind, are slowly adopting ESG frameworks and moving towards more sustainable investments.

The United Nations Principles for Responsible Investment ("UN PRI") has released a discussion paper titled "Starting up: Responsible investment in venture capital" exploring the development of ESG incorporation across the venture capital industry. The report outlines how VC investments could potentially be disruptive to the broader economy and society, both in a positive and negative manner.

In the investment fraternity, timing is a vital consideration in decision making: too early, the investments may not yield the best returns; too late, the opportunity is missed. Investors unfortunately do not have the benefit of having the foresight to precisely predict market movements every time. However, a crystal ball is not required to see that VC fund managers who do not incorporate ESG into decision making is at risk of falling behind.

VC fund managers can shape the culture, values and behaviours of their investee companies, especially while they are at the more malleable younger stages of their start-up lifecycles.

However, these opportunities are rarely acted upon due to challenges faced, such as limited influence by both general and limited partners, perceptions that ESG issues are not material to the asset class as well as a lack of standardised ESG practices across the industry.

One major risk in the VC industry is the regulatory aspect, particularly in broad technology areas in which the investee companies are exposed to. As ESG concerns all stakeholders, start-ups that incorporate ESG practices early on will be more prepared for future regulations as opposed to implementing reactionary measures as and when new policies are imposed. VC fund managers, who typically come in at the onset of a start-up's growth trajectory, can be valuable advisors in this aspect.

To that end, there are evidence suggesting that increasingly more funds are moving towards the incorporation of ESG best practices through industry initiatives such as VentureESG and ESG VC. Momentum is stronger across European countries as compared to other regions including the US, where ESG incorporation is often seen as just box-ticking exercises.

VC Company Spotlight: Molten Ventures plc

Molten Ventures plc (formerly known as Draper Esprit) invests across the United Kingdom and Europe in high-growth technology companies from Series A onwards focusing on four sectors, namely consumer technology, enterprise technology, hardware & deeptech as well as digital health & wellness.

They also indirectly support companies in the earlier stages through their fund of funds programme as well as their partnerships with external fund managers that invest in companies in the Seed stage up to Series A.

Gross Portfolio Value as at 31 March 2022 stands at £1.5 billion which consist of notable companies including Trustpilot, Graphcore, Revolut, Ledger, Aiven, Form3, UiPath, Lyst, Aircall, Thought Machine, RavenPack, CoachHub, Cazoo, M-Files, N26, Isar Aerospace and Smava.

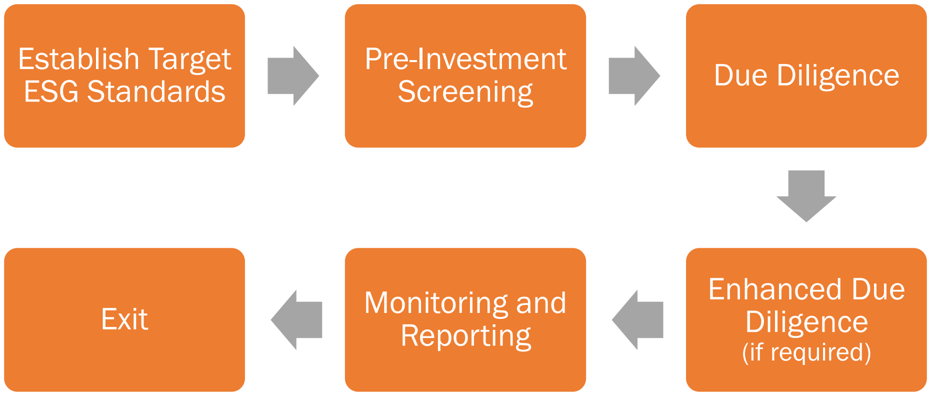
Recently, Molten Ventures has been included as one of the top performers and have been included in the ESG Transparency Index published by Orbis Advisory Ltd and Energised Environments Ltd in recognition of their commitment to incorporate ESG into their investment decisions.

How do they evaluate ESG in investments?

In line with their company values, Molten has adopted an ESG Policy which outlines, amongst others, their approach to responsible investment*. Other policies published as part of their commitment include an annual Sustainability Report, Board Diversity & Inclusion Policy as well as Modern Slavery Statement.

** Does not apply to their Fund of Funds strategy where they have no control or co-control over investment strategies or processes but seeks to partner funds who have an ESG focus.*

Evaluation is done throughout the investment lifecycle, from pre-screening up to exit, aligned to the UN Sustainable Development Goals and the UN PRI, as outlined below:



Key takeaways from Molten Ventures' approach is that VC players can and should integrate ESG considerations into investments as the long term benefits far outweighs the costs. In fact, sustainability of investments should be a priority considering the long term nature of this asset class to reduce long term risks associated while enhancing exit returns.

Capital Connections

Featuring

Eric Feng

By: Marcus Lim

<u>Capital Connections 5.0 – Featuring Eric Feng</u>

We love it and judging by the RSVP list, so do our esteemed guests. Therefore, to keep the momentum going, Capital Connections 5.0 was held online on 7th July 2022.

This time around, we spoke to a prominent Venture Capitalist all the way from Silicon Valley: **Eric Feng**. He shared with us his views on the market, fundraising activities and valuation of start-ups as well as how to brace for a slowdown in the economy.

More on Eric Feng:

Eric Feng is the Co-Founder and CEO of Cymbal and the General Partner of Gold House. Prior to that, Eric was a partner at Kleiner Perkins investing in cleantech and was also a tech advisor to former Vice President Al Gore. He was previously the founding CTO of Hulu and the founder of social networking site Erly, which was acquired by Airtime.

A summary of our discussion with Eric:

<u>**Q:** What is the impact of current macro headwinds to fundraising and financing activities?</u>
Eric: Deal flow within the VC industry will not stop or stagnate as VC funds have to deploy their capital within a set time period and investors are incentivized to invest, during good or bad market conditions. Moreover, we see a change in leverage – in a bull market, the leverage is on the entrepreneurs. In a bear market, the leverage is on the investors where investors can dictate more terms and squeeze the price further. During market corrections, this will flush out all the "bad" companies and what we will see are strong companies that is reflective of their performance which presents a buying opportunity in the second half of 2022.

<u>**Q:** What are the available opportunities within the Web 3.0 sector?</u>
Eric: Web 3.0 has a high correlation with tech stocks and revolves around blockchain technology. They are seen as growth assets. When tech stocks are rallying, we see investments in Web 3.0 performing well too. Historically, the growth of Web 3.0 has also been contributed by 'narratives'. The next growth in Web 3.0 will be led by a new 'narrative' within the sector.

<u>**Q:** What was the lesson learned from Kleiner Perkins' misstep of investing too early in cleantech? What did you learn from your days working in Kleiner Perkins with John Doerr?</u>
Eric: John taught me a framework for investing that has been tested for about 50 years by Kleiner Perkins which essentially revolves around three aspects, with the first one being **timing** (i.e., Is this the best time to invest?) In the case of cleantech, Kleiner Perkins was too early when they invested during the early 2000s. There other two aspects are market/business size, and the team involved.

<u>**Q:** What advice do you have for young individuals entering the VC industry:</u>
Eric: For investors: Venture Capital is the most intellectually rewarding profession that you could possibly be involved with. Stay curious and ask: "Why now?", "Is it big enough?", and "Is the founder a 'mercenary' or a 'missionary'?". For entrepreneurs: The VC industry is one of the most emotionally-rewarding industry to work in. There is value in peer-support network although it can be lonely at times. More importantly, understanding risk-removable in the right order is very important i.e., which risk to eliminate first.

"**Venture Capital** is the <u>most intellectually-rewarding profession</u> that you could possibly be involved with."
- **Eric Feng** -

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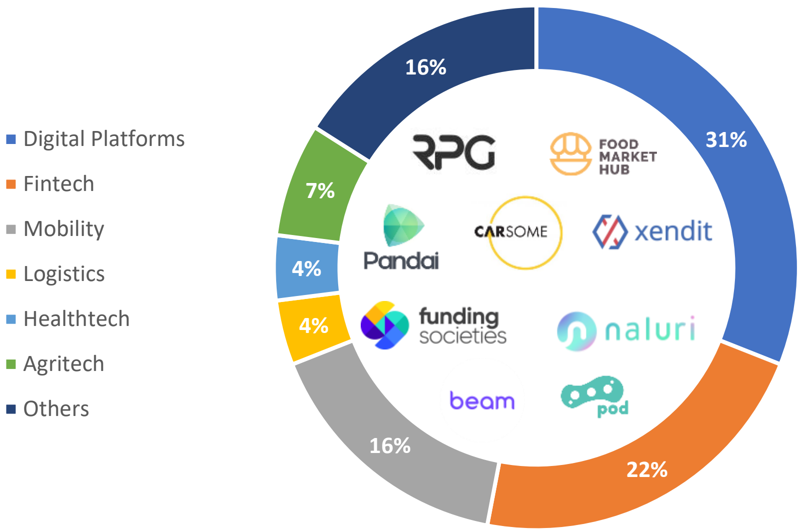
Key Highlights

As of 14 July 2022

Portfolio breakdown

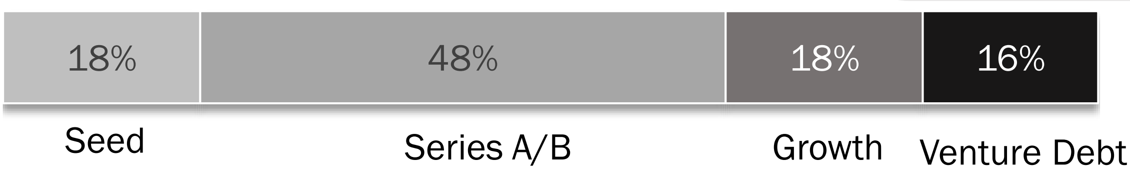


Fund Snapshot

RM1.30 bil
Fund Size

RM418.29 Mil
Approved Investments

2
Unicorn



Note: Investee stage are based on number of approved investment (45)

DPN Investee Spotlight

- Established in February 2021, **GetGo's** hourly car rental service makes renting a car hassle-free, affordable and enjoyable. GetGo has a fleet of more than 1,400 vehicles spread across 1,300 locations in Singapore.
- GetGo's car-sharing business model solves the issue of car affordability while encouraging ESG-friendly practices among its user base. GetGo recently announced that they will be adding around 50 Hyundai electric vehicles (EVs) to its fleet in 2023. GetGo already has a few EV models such as the Hyundai Ioniq EV, Hyundai Kona EV and MG ZS EV on its platform.
- GetGo also has an arrangement with charge point operator CDG Engie (a JV between transport group ComfortDelGro and French energy firm Engie) which allows GetGo's users to recharge the cars for free.

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