

Venture Microdebt

Don't just invest from Hong Kong

Invest in Hong Kong

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- The current presentation can be found at
- <https://github.com/joequant/bitquant/blob/master/pitchdecks/venturemicrocodebt.pdf>

Disclaimer

- This presentation is for informational purposes only and does not constitute an offer or solicitation for investment. No representations or warranties are given as to the accuracy of the information herein.

Who are we?

- Bitquant Research Laboratories (Asia) Limited
 - We research ways of improving financing
 - Business model – Make money from new ideas
- Open source and transparent
 - Want to create methodology that everyone can use
 - If you see something useful, copy it

The Hong Kong paradox

- People invest from Hong Kong
- People invest through Hong Kong
- Few people invest in Hong Kong
- WHY???

The Hong Kong paradox

- Not lack of capital
 - Major financial center
 - Massive pools of local capital
- Not lack of projects
 - Hong Kong is a major center of fashion, financial technology, legal, mobile, UI/UX
- Not lack of need
 - As China changes, Hong Kong must also change and generate new types of employment

The problem

- Lack of a financial model
- VC model is not enough
 - Most firms in Hong Kong are small and non-scalable. A few may take over the world. Most will become stable solid local businesses
 - No easy exit at the IPO/pre-IPO stage
 - Hong Kong securities regulations are antiquated and hostile to startups. This is changing but not fast enough.
 - Bank employees cannot do VC investments for compliance reasons.
 - Creates a game show/lottery ticket winner mentality
 - High failure rate will not work

Other issues

- Cultural issues
 - Tendency to regard equity investments as "money for nothing" and as reward for founders
 - Results in reluctance of investors to put money as equity
 - US – Social obligation to equity holders but not debt holders
 - Greater China – No social obligation to minority equity holders, but large social obligation to debt holders

Bank loans / Friends and Family

- Bank loans
 - Banks will not lend to companies without stable sources of revenue or which have an innovative business model
- Friends and family
 - Perfect if you have a rich uncle. Not everyone has a rich uncle

Solution – Client centered finance and Venture microdebt

- Client centered finance – Focus the interaction on the SME client and not the product
- Venture microdebt – Loan based financing system based on loans
- Product create working with actual creditors and borrowers

High attrition will not work

- High attrition is possible in Silicon Valley because entrepreneurs are mostly professionals with cash reserves. There is also an active job market. Your startup fails, no big deal. Get a job at one that succeeded.
- High attrition is unacceptable in HK. Most entrepreneurs are college students with no alternatives. Your startup fails, there are no alternative jobs

Ways of reducing attrition

- End lottery ticket / game show model
- Training and professional mentoring
- Eschew unnecessary innovation
 - Create cookie-cutter business models
- Create effective methods of corporate reorganization and salvage

Venture microdebt

- Friendly regulation
 - Not a security or structured product under Hong Kong law
 - Regulated under money lending laws and not securities regulation laws
 - Loans can be easily resold and no compliance restriction by financial workers
- Easy exit
 - Loan automatically exits in one year
 - Can be easy to resell cash flow

Venture microdebt

- Typical loan – USD 10000
- Principal in one year, monthly interest payments
- Base interest – 10%
- Accelerated payment – If business hits target, loan plus interest becomes due immediately
 - If the business wins, the investor wins. Effective interest rate can hit maximum allowed by Hong Kong law (60%)
- Smart contract technology – Payoff is described by a program enforceable under Hong Kong law
 - Custom solutions for each business
 - Allows for bundling and automated credit analysis

Venture microdebt

- Aligns interests of investor and SME
 - Investor wants **every business** to succeed
 - Focus on creating a solid business and not winning at the lottery
 - Innovation for the sake of building a business, and not innovation for the sake of innovation
 - If the business runs into trouble, investor wants to maximize value
 - Business leaves the loan with a clean balance sheet
 - Extremely attractive to VC – 100% capital owned by founders. Solid revenue stream and proven business model
 - Extremely attractive to banks – Business exits loan with a solid revenue stream and good credit

Venture microdebt

- Cash flows can be combined into baskets without expensive fund structures
- Transparency – You will be able to see every loan that makes up the basket
- Open source
 - <https://github.com/joequant/bitquant> - Open source template
 - http://joequant.github.io/bitquant/smart-contracts/contract_analyzer.html - Contract demo

Social benefits

- Generates employment and increases social stability
- Local high tech businesses are needed for Hong Kong to attractive financing for external business
- Get rid of the lottery ticket/game show culture and replace with one that produces solid, profitable businesses
- No business left behind – Capitalism is a fun game. Everyone should play
- Improved social perception of the finance industry – We really do useful things

Opportunities for investors

- Direct sourcing of loans
- Bundling loans for wholesale money
- Credit guarantees
 - If I trust the businesses, and you don't know them. I can put my money on the line
- Buying baskets of loans
 - Custom designed baskets
 - Thematic – Fintech, biotech, fashion, mobile, cryptocurrencies
 - Area centered – HK business targeting Greater China, Middle East, Europe, South East Asia
 - Growth or value – SME's that want to be the next google vs. SME's that don't want to be the next google
 - Portfolio blends

Current status

- Currently beta testing methodologies
 - Venture microdebt drafted and have been issued
- Want to test loan in situation where borrower cannot repay – What happens?
- Expected rollout – Asian Financial Forum 2016
- Looking for beta testing investors to test methodology

To Do

- Create reorganization and default workout process
- Need actual test case
- Bankruptcy unsuitable for SME's
- What should/could happens if company cannot repay
 - Need mechanism to reorganize company and preserve capital
 - Contract could include shareholder agreement to have third-party take control of the board in case of insolvency.
 - Protects company against predatory lenders
 - Venture microdebt retains some value