New Directions in Russian Venture Capital

International Chemical Summit
Moscow Russia
1-3 July 2004

Innovative Ventures Inc.
Grand Rapids MI USA
Moscow Russia

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New Directions in Russian Venture Capital

- What Can This Group Accomplish Today?
- What are the Objectives?
  - Create More Enterprises/Grow Existing Ones
  - Access More Capital/Raise More $$
  - More Growth/Jobs
  - More Taxes Paid
- What are the Issues?/Solutions?

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Recommendations to this Group

Enterprise Managers

- Seek $$ Sources Other than VC
- Be More Flexible in Your Business Expectations – Be 200% Transparent
- Seek Multiple Sources of Technology

Institutes: Technology Commercialization

- Document Accomplishments, Customers & Revenues

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Discussion Topics

- Background of IVI
- Current Situation: VC in Russia
- Strategies for Growth
- Recommendations
- Q&As

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Background of IVI

- Began Operations in 1986

Business:

- Manage US Venture Funds
- Advisor: Create Int'l & Emerging Market Venture Funds
- Implement Initiatives to Develop Emerging Market Countries & SMEs for Venture Investment

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Direct Venture Capital Management

- US$4.3MM Michigan Product Dev. Fund-USA
- US$30MM Lower Volga Regional Venture Fund-Samara, Saratov & Volgograd Oblasts
- US$440MM US-Russia Investment Fund (Delta Capital)-Russia Far East

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US$4.3 MM, Michigan Product Dev. Fund

- Financed Seed/Early Stage SMEs
- Technologies; Machine Vision, Software, Instrumentation as examples
- Investments structured as royalty, royalty/equity

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Liquidity Events

Applied Intelligent Systems Inc.

Machine Vision for Electronic Inspection Applications

- US$700k invested in US$1.4MM financing
- US$500k in cash & 10x equity gains
- Acquired by Electro-Scientific Instruments

Personal Bibliographic Systems Inc.

Software for accessing & managing bibliographic data

- US$200K invested
- US$150k in cash & acquired by ISI, subsidiary of Thompson Corp.

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Liquidity Events Cont'd

Neogen Corp

Immunoassay Diagnostic kits & Electronic instruments for Animal & Plant Health Care

- US$700k invested in US$2.8MM financing
- IPO; Valuation increase from US$10MM to US$22MM

Face Technologies

Computer Motherboards for PC Applications

- US$330,000 invested in US$500,000 financing
- Total write-off & loss of entire investment


LOWER VOLGA RVF
$3MM
$2,6MM
$3,2MM
ST. PETERSBURG
SAMARA
$3,2MM
CEMENT
MOSCOW
SARATOV
25%
$8,75MM
75%
$24,75MM
$1,1MM
VOLGOGRAD
$600,000
$3,2MM
BANKS

U.S. Russia Investment Fund

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Advisor in Int'l & Emerging Mkt. Funds

- C$100MM Venture Loan Fund- Federal Bus Dev. Bank of Canada
- €1.5B Financiere St. Dominique - Royalty Fund for W. Europe
- €15MM EU-Technology Performance Scheme
- $5MM E. Africa Fund of Funds - World Bank
- $200MM African Enterprise Fund – IFC
- $30MM South Africa Succession Fund - IFC
- Investment Priv'z Funds – Kazakhstan Govt.

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IVI Activities in Market Development

- Some emerging market countries need development assistance as preparation for venture capital
- Example: Russian technology sector
  - Underdeveloped for VC investment
  - Lack of quantity/quality of company (deal flow) for investment

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- The Russian Technology Investment Forum™ (2001)
  - The Russian Technology Venture Capital Workshop™
- CIS High Technology Partnership Initiative™ (2004)

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Current Situation: PE/VC in Russia

- EBRD, IFC & US Govt. Supported Funds
  - Most are Fully Invested/Raising Capital
- Intel Capital (Corporate VC)
- Russia Technologies (Alfa Group, $20MM)
- US$150-$400MM in Un-Invested Capital (Informal & Unofficial Est., Not for Quoting)
- US$ from Russian Sources for PE/VC is ???

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- Why are More $$ Not Finding its Way to Russian Tech Investment?
  - Capital Seeks the Highest Rate of Return
    - Strong Domestic Growth in Non-tech Sectors, Retailing, Distribution, FMCC, etc.
  - Competition from Other Asset Classes with = &/or > Liquidity, ex. Stock Mkt., Bonds, even Real Estate

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- Many Tech Opts Focused on Int'l Mkts
  - Where Demand Is
  - Gaining Access is Expensive/Requires Latest Technology/Best Mgt/Etc.
  - Penetration & Growth Takes Much Time

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Raising the $$ is a Challenge

- Developed Mkts, 1 of a 100 deals financed
- In Emerging Mkts, 1 of 200/300 deals financed

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Individual Event	Probability
Company has enough $$	80%
Mgt Capable & Focused	80%
PD Successful	80%
Mfging & Component Sourcing Successful	80%
Competitors Behave as Expected	80%
Customers Want Product	80%
Pricing is Correct	80%
Patents Issued & Enforceable	80%
Combined Probability of Success	**17%**

Reason why Invest 1 of a 100

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How be in the Group of the 1/200 that gets the $$ to Modernize & Expand?

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Strategies for Growth

1. Seek Corporate Partnerships 1st
   - For Joint Project/Technology Development
   - To Create Supply-Chain Linkage
2. Be 200% Transparent
3. Then Seek VC/PE
   - After Demonstrating Skills/Value-Added, Ability to Meet Customer Demands, & Transparency

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- Learning Curve Lessons in Commercialization-Russian Technology
- Ex. #1: Shell Technology Ventures & IVI
  - Objective: Id technology to commercialize
    - Transfer of IP (License/Sale of Technology)
    - VC Investment in an Existing SME or New SME

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Bring More Corporations Here

Objective: Create Cross-Border Partnerships

Corporate Characteristics:

- Global Search for Technology
- Internal Incubation Group
- Internal VC Dept., & Invest in VC Partnerships

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Technology Categories

- **Технологии для поиска и разведки углеводородов (нефть и газ)**
- **Технологии для разработки и эксплуатации нефтяных и газовых месторождений,**
- **Энергетические аспекты устойчивого развития**

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Specific Technology Focus (IVI & STV)

1. Повышение нефтеотдачи
2. Переработка и преобразование углеводородов
3. Новые технологии бурения
4. Новые методы строительства скважин
5. Механизированная добыча

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Ex. #2 (Schlumberger):

- Gyroscopes: Russian Enterprise
- Design Innovation, 2 parts vs. 3 parts
- Directed at Oil/Gas Industry
- Cost/Price Reduction from $10k to $2k

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Example: Corporate Partnering

- Analyze/Confirm the Need-Price/Performance
- Prepare Product Development Plan & Budget/Revise
  - Original Budget/Time – US$800k & 3 years
  - Revised Plan – US$200k & 1 Year

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Three Year Project Plan

first year second year third year

Task 1. **Finishing of the construction of the gyroscope and the electronic system** _____
Coordination of the characteristics on vibration resistance and thermostability
Edition of the design documentation
Manufacturing of the electrical circuits
Correction according to the results of tests

Task 2. **Acquiring special equipment** _____
Coordination of the questions on delivery and installation
Engineering and manufacturing of special equipment

Task 3. **Manufacturing of an experimental copy of a gyroscope** _____
Manufacturing of the mechanical part
Manufacturing of then electronic part
Docking of parts and debugging of a gyroscope

Task 4. **Creation of a workplace for the tests** _____
Technical documentation for the workplace
Preparation of the devices and the equipment

Task 5**. Drafting of the program and testing procedures** _____
Drafting and coordination of the procedures
Drafting and coordination of the program.

Task 6. **Testing of the gyroscope**. _____
Specification of technical characteristics
Shake-table test.
Test in a thermal chamber.

Task 7**. Edition of the reports on the project**. _____

Capital Expenditures

Equipment	**#**	**Price US$**	**Total US$**
Circular grinding machine	1	$300,000	**$300,000**
Portable vibration bench	1	$20,000	$20,000
Climatic scoop	1	$6,500	$6,500
Vacuum furnace	1	$47,000	$47,000
Leak tester	1	$12,500	$2,500
Soldering station	2	$500	$1,000
Computer	4	$800	$3,200
Plotter A2	2	$2,500	$5,000
Printer	2	$400	$800
Copy device	4	$350	$1,400
Radiometric devices (oscilloscope, generator, voltmeter, frequency meter)	10	$1,500	$15,000
		Total	**$412,400**

One Year Project Plan: US$180,000 Budget

1 2 4 6 8 10 12
|_____|_____|_____|_____|_____|_____|_____|_____|_____|_____|_____|_____|

Task 1. Modernization of design of gyroscope mechanical part and production of its prototype _____+

Coordination of the performances with a customer
Issue of design documentation
Technological background of manufacture
Production of mechanical part of gyro

Duration 7 months
Cost 80000 $

Task 2. Development and production of gyroscope electronic control system _____+

Development of math model and and control algorithms
Development of technical requirements on electronics
Search for the partner on development and production of electronics
Development and design of electronic circuits
Production of gyroscope electrionic block
Installation and debugging of electronics

Duration 7 months
Cost 20000$
Cost of development and production as agreed with a partner.

Task 3. Debugging of electronics together with gyro mechanical part, background to tests _____+

Experimental work and launch of a gyroscope
Selection of electronic optimum functional modes
Determination of gyro performances at the laboratory test

Duration 4 months
Cost 20000 $

Task 4. Background of work place to tests and testing of a prototype _____+

Issue of technical documentation for the test bed
Development and coordinatioin of method and programm of test
Purchase of devices needed for testing
Setup of workplace
Testing according to test programm

Duration 5 months
Cost 60000 $

Task 5. Issue of project reports _____+_____+_____+_____+

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- Learning Curve Lessons in Partnering
  - Partnering Requires Active Selling to Create Interest
  - Russian Side Needs to Demonstrate Technical Capabilities first, to create interest
    - Technical Paper/Proof of Concept/Test Results
    - Accomplishments/Clients

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Learning Curve Lessons in Partnering Con't

- Foreign Partners Seek Demonstration of Capabilities First:
  - to Reduce Cost, Uncertainty & Risk
- Russians Want to Demonstrate Capabilities too:
  - Create the Whole System
  - Increases Cost, Risk & Uncertainty

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Learning Curve Lessons in Partnering Con't

How Solve the Differences?

- Create the Plan/Business Model to Do the Technical Minimum-Demonstrate Performance & Grow from there
- Seek other partners to assist, reduce cost, risk & uncertainty

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Where Access the Technology?

- Internal Development
- Small/Medium Size Enterprises
- Institutes

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Institute Directors:

Technology Commercialization

- Publish List of Your Accomplishments, Customers & Revenues
- Demonstrates that You can Add Value to the Market

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Potential partners are extremely interested in three things:

- Your past successes, creative & innovative capabilities
- Your ability to deliver to objectives/criteria, on-time and to budget
- Management (project planning, execution, control, risk & contingency strategies)

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This is Not Important Info For Partnering

- Education focused on science & technology
- Technology pool strong in space, avionic & military
- Large pool of scientists & high-tech specialists
- Still competitive cost of development
- Major improvements in business environment
- 250MM domestic population & growing market
- Western educated Russian managers & engineers returning to Russia
- Ability to spin-off a technology from institute

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Give Examples of Who Benefited From Your Skills: Achievements or Milestones in the Development & Growth of the Institute

A. For Example: International/Domestic Clients of Your Institute

- Company W, Company X

B. For Example: Domestic/International Recognition through patents/awards received, commercial development, membership with other leading int't institutes, etc.

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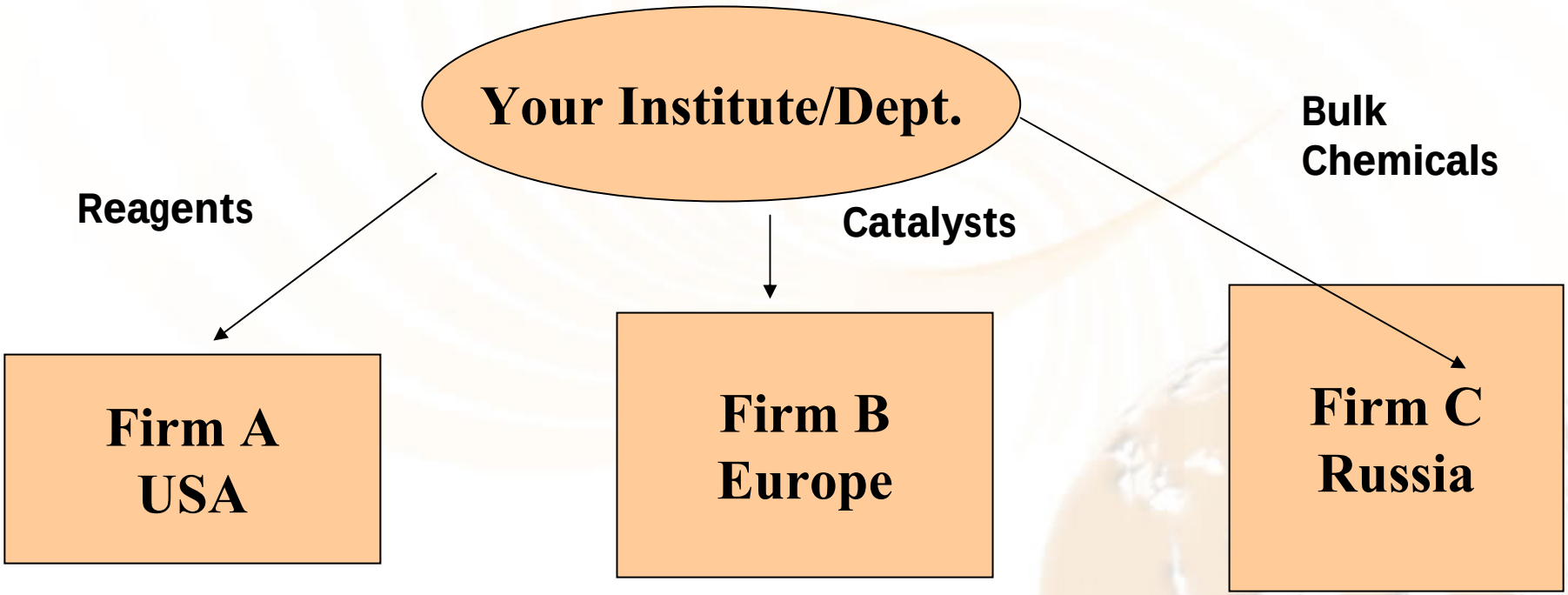
Demonstrate Your Accomplishments



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Demonstrate Your Accomplishments

Year	Client	Project	Budget	Result
2000	Firm A	Improve gyroscope accuracy by eliminating one or more parts	US$200,000	Finished Design to Req't s

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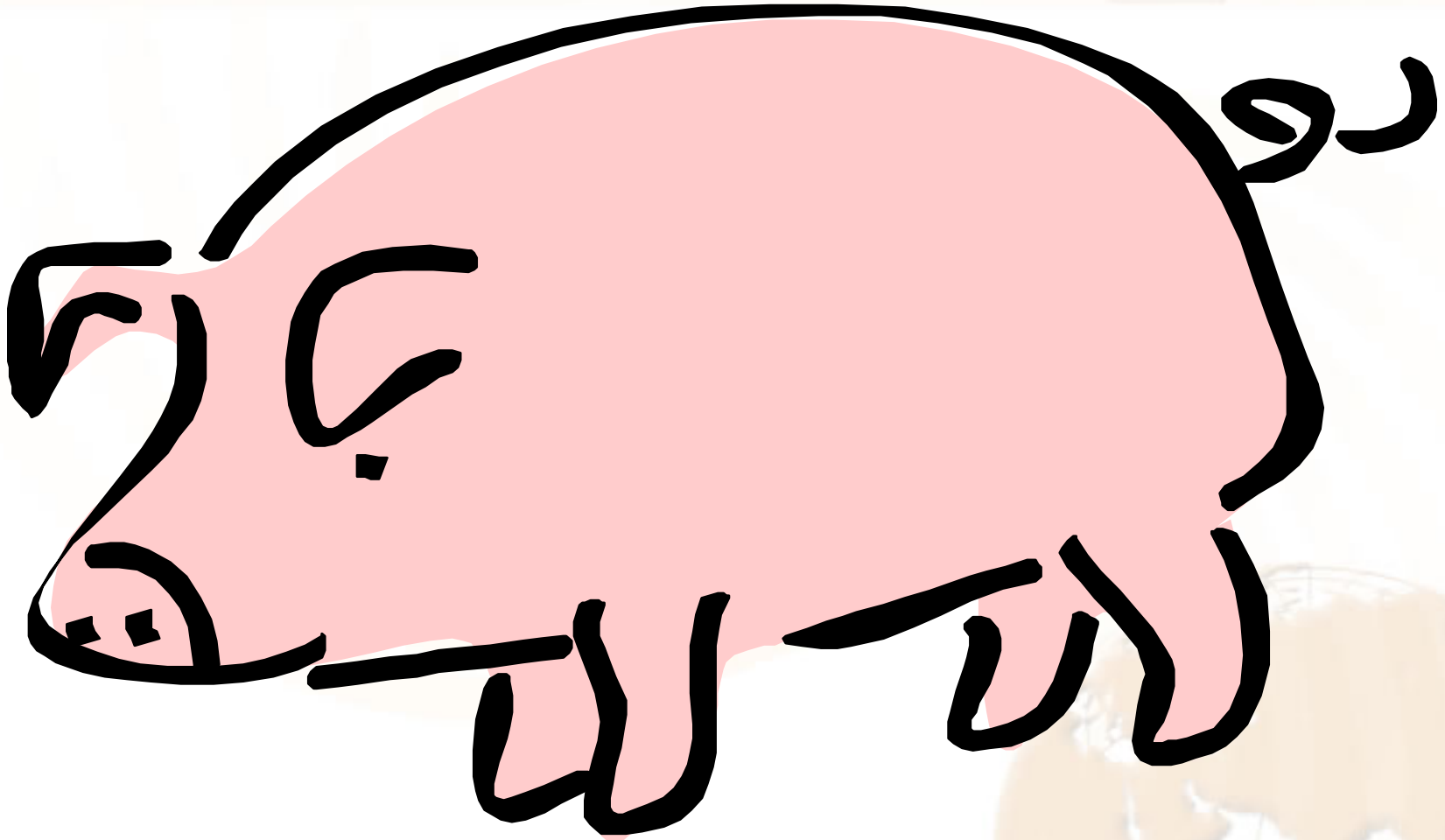
How Much Value?



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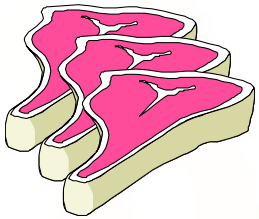
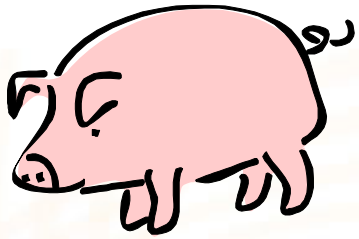
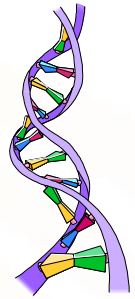
Where is Value Added Created?



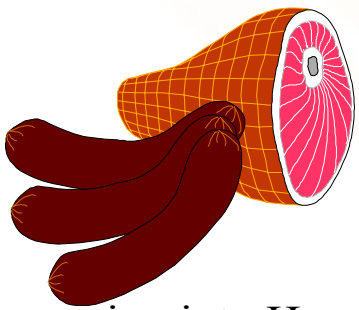
Slaughter



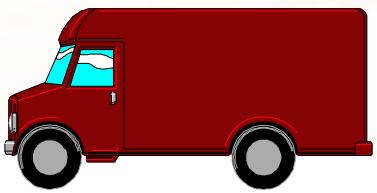
Raising



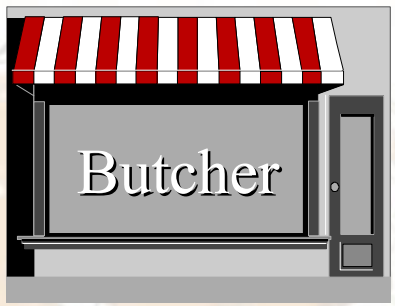
Genetic Engineering & Breeding



Processing into Ham, Kielbasa



Distribution, Storage & Delivery



Retail Locations

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Questions & Answers: Discussion

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