SAMI MAHROUM

BLACK SWAN START-UPS

Understanding the Rise of Successful Technology Business in Unlikely Places

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This book is dedicated to my parents, Mounir Salim Mahroum and Douha Fatima Badiha, who have thrived all their lives in less likely places.

Foreword

Unicorns, which are start-ups with valuations exceeding US$1 billion, have become a worldwide phenomenon. A decade ago, all unicorns were from the USA. Nowadays they hail from every corner of the globe. They come from Europe but also from emerging markets, Israel, Korea, Indonesia and, above all, India and China.

This tectonic shift is part of the ongoing rebalancing of the wealth of nations. Emerging markets are no longer (only) low-cost factory locations but the home of some of the largest ever tech initial public offerings (IPOs) (e.g., Alibaba) and the largest ever "score" of venture capital. Years ago the investment arm of South African firm Naspers invested around US$40 million in an unknown Chinese start-up called Tencent. Today that stake is worth US$40 billion. This "score" is by far the largest ever, more than that managed in Google by legendary venture firm Sequoia, for example.

The shifting wealth of nations is today more than ever about tech, start-ups and venture capital. This century will witness an increasing number of rising tech stars from emerging markets and from the margins of the start-up world. For example, Edinburgh, Scotland, known more for its annual music festival than its tech companies, has given rise to two unicorns, FanDuel and Skyscanner. But this trend, as this book will show, is also evident in other traditionally peripheral places such as Bergen,

Tallinn, Lahore, Amman and Dubai. The major news is that successful tech start-ups can rise up now from anywhere around the globe – and emerging markets are a big part of this story.

The Emergence of Less Likely Places

While Europe is slowly losing its technology icons – the latest to fall being Nokia, now in the process of reinventing itself with its 2015 acquisition of Alcatel-Lucent – the emerging markets are becoming ever stronger in innovation and technology. Some of their companies are already world leaders in their respective sectors.

This is the real news: the emerging markets and the periphery of mature economies are no longer low-cost, low-technology-intensive countries. It is no longer a matter of trade and financial flows, but of countries and regions betting on innovation and technology. And their bets far exceed the usual European perception.

In 2015 the four so-called BRICs (Brazil, Russia, India and China) alone accounted for 43 % of the world's population, 21 % of world gross domestic product (GDP), and 20 % of direct foreign investment (nearly US$205 billion). In less than a decade, trade among these nations increased tenfold to surpass US$200 billion. These four countries are respectively already the seventh, eighth, tenth and second world economic powers. China already has as many companies as the UK (33) in the Financial Times (FT) Global 500, which is composed of the world's 500 largest companies by market capitalisation. The same trend can be observed with India and Brazil, which, with ten each, are already ahead of Spain, with nine companies in the top 500.

Other countries, such as Singapore, are unseating the major western financial centres, particularly those of Switzerland. Singapore is in fact the first emerging economy to join the select club of triple-A countries with the top international credit rating. Chile, Turkey and Mexico are already members of the Organisation for Economic Co-operation and Development (OECD). The greatest concentration of millionaires is in Qatar, ahead of Switzerland (in fact, Qatar has the highest GDP per capita in the world). Similarly, the world's biggest airlines are now those

of emerging market countries, with the United Arab Emirates in the lead. All seek to acquire iconic assets and, above all, to acquire knowledge with the aim of providing services within their respective countries. Thus, in 2015 the Fosun Group bought Cirque du Soleil in order to round out its offering of entertainment for China's middle class, after buying Club Med, also in 2015, and having bought a stake in travel agent Thomas Cook.

From Raw Materials to Killer Apps

But above all we are seeing a wave of technological expansion. We are no longer dealing with countries with cheap labour full of raw materials but with economies that are downloading so-called technological killer apps' at breakneck speed. In 2015, the world's biggest supplier in the telecommunications industry is no longer an American, French or Swedish company but a Chinese one (Huawei). The world's largest producer of personal computers (PCs) is no longer American but Chinese (Lenovo). One of the world's most research and development (R&D)-intensive companies is Korean (Samsung), which since 2013 has also been ahead of its Finnish and American competitors as the leading producer of mobile phones and devices. We are witnessing an unprecedented tectonic shift. The spread of technology is accelerating as never before, in space and in time, as Diego Comín points out.[1]

A clear case in point is that of South Korea. In the 1960s, South Korea was poorer than Spain or any Latin American country.[2] In 2015, it surpassed them all in terms of GDP per capita, to say nothing of its performance in education (equal with Finland in the OECD's PISA reports). In 1963, Korea exported goods at a value equivalent at current prices to slightly more than US$600 million, comprised mainly of agricultural and fishery products. In 2015, it exported more than US$600 billion worth of goods, mainly electronics, machinery, chemical

[1] See Diego Comín, Mikhail Dmitriev and Esteban Rossi-Hansberg, "The Spatial Diffusion of Technology," Harvard University, Boston College and Princeton University, March 2013 (unpublished). http://www.dartmouth.edu/%7Edcomin/files/SDT.pdf

[2] For a comparison between Spain and Korea, see one of the chapters in the book by Javier Santiso, *España 3.0: Necesitamosresetear el país, Barcelona*, Planeta, 2015.

products and shipping technology. The giant Samsung Group consists of more than 80 companies and employs over 380,000 people around the world. In 2013, it even surpassed Apple, selling more smartphones and generating more profits than its California-based rival.

Until recently, innovation, particularly corporate innovation, was largely a western story. Multinationals from OECD countries designed, produced and sold innovative products. Gradually another model established itself: innovation was still conceived in the West, but it was produced in emerging markets. This is Apple's model with iPods and iPads, which are partly produced in Taiwan, Korea or China. Now we are seeing a third model emerge, in which innovation is not just produced and sold from the emerging markets, but increasingly also being conceived in them.

New Companies from an Old World

This shift is bringing about an accelerated reordering of world company classifications. The classifications of the most innovative companies produced by Boston Consulting Group (BCG) or Forbes tell a similar story. BCG's Top 10 is headed by Tencent and also features a Taiwanese company (Mediatek), a Mexican one (AméricaMóvil), another Chinese one (China Mobile), two Indian companies (Bharti Airtel and Infosys) and one South African company (MTN). In the Forbes list, too, Tencent features in the Top 10 (again ahead of Apple and Google), and other names include Brazil's Natura Cosméticos and India's Bharat Heavy Electricals.

The world of the Internet has always been dominated by US multinationals. However, Tencent now has a market capitalisation of US$45 billion, ahead of eBay and Yahoo. From Moscow, Yuri Milner is revolutionising the rules of digital venture capital, hitherto dominated by California-based funds. His company, Digital Sky Technologies (DST), owns mail.ru, one of the successful Russian start-ups listed on the London Stock Exchange at a valuation of more than US$8 billion. His venture capital fund is one of the few with holdings in Facebook, Zynga and Groupon. In 2011, Milner launched a second fund, DST Global 2, at a valuation of US$1 billion, an unheard-of size in Western Europe. From Singapore, telecommunications operator Singtel also launched its own

venture capital fund in 2011, with more than US$250 million, in order to accelerate the acquisition of technology start-ups. All these initiatives show, as if further proof were needed, the extent of the emerging Asian countries' commitment to carving out an ever bigger space for themselves in the world of start-ups and venture capital.

This phenomenon is not confined to Asia. The case of Naspers, a South African multinational in the digital world, is a prime example: it obtains more than 70 % of its revenues from the African continent but has also made many acquisitions in emerging markets. The 45 % stake in Tencent which it bought in 2011 has increased in value by more than 3100 % since then: so the biggest "score" in the history of the Internet belongs to a fund based not in California but in South Africa. Naspers has also invested US$390 million in Russia's mail.ru and holds 91 % of Brazilian start-up Buscapé, for which it paid more than US$340 million. In Eastern Europe it bought Tradus for more than US$1 billion in 2008. Since 2010 it has continued its buying spree in Latin America, acquiring the Argentine start-up DineroMail, the continent's biggest online-payment firm, and Olx.com, in 2011, for nearly US$145 million. Naspers now has a presence in 129 countries; with annual revenues of approximately US$4 billion, it has 12,000 employees and has become one of the main investors in emerging market start-ups.

We still tend to think of Silicon Valley as the all-powerful global centre of innovation and technology. However, since 2013 China has occupied second place as a global venture capital hub. There are more start-ups per capita in Israel than in any other country in the world: there, venture capital per capita has reached a record of more than US$140, double the US$70 figure for the USA.

Brazil already has a more powerful ecosystem of start-ups and venture capital funds than Spain does: in 2015 Brazil already has several venture capital funds with more than US$100 million for investments exclusively in Brazil (Spain has no fund of this size dedicated exclusively to investing in Spain). Brazilian media group RBS launched e. Bricks, a fund of more than US$100 million, to invest in Brazilian Internet companies. The major California-based funds have now set sail for this new El Dorado: Redpointe.ventures closed a US$130 million fund to invest in Brazilian start-ups. European funds are on the move, too; in 2012, London-based venture capital fund Atomico landed in Brazil.

In 2013, Amadeus, another major European fund, closed a US$75 million fund with the South African telecom company MTN to invest in start-ups in emerging markets, including African markets, such as Kenya and South Africa, where there is also considerable movement. Telefónica for its part made a massive commitment to emerging markets, particularly those in Latin America, by means of a network of accelerator funds in eight Latin American countries (Wayra) and venture capital funds in three of them (Amerigo). Mexico's América Móvil also invested in start-ups in 2013, including the UK's Shazam, in which it acquired an 11 % stake for around US$40 million, proposing to spread the Shazam app throughout the region.

Spanish groups have not been idle either, particularly BBVA, which set up a US$100 million venture capital fund to invest in the USA and also, occasionally, in Latin America. In 2013, it took part in an investment of more than US$20 million in SumUp, a German financial services start-up. Santander did likewise with Sweden's iZettle in 2013. Both banks are supporting these European start-ups in their internationalisation, opening paths to the emerging markets of Latin America.

This leads us to imagine that, in addition to having executives based in Spain to cover the Spanish market, these European start-ups, oriented by Spanish banks towards Latin America, could also use Spain as the headquarters for executives responsible for developing new markets or, in any case, Latin American markets (in the case of iZettle they are in London, and in the case of SumUp they are in Berlin). Why not imagine Spain (Madrid and Barcelona) becoming a hub for European start-ups looking to enter Latin America (and viceversa, a gateway to Europe for start-ups from Latin American and other emerging markets)?

From Copacabana to the NASDAQ: The Silent Latin American Revolution

Technological change, beyond commercial and financial change, is evident in China, India, Korea and Singapore. But it also encompasses other regions of the world. Specifically, there has been a silent revolution in certain Latin American economies. In several countries in the

region we are seeing an extraordinary flowering of entrepreneurship and an unprecedented boom in multinationals that now extends well beyond Mexico and Brazil, the two dominant regional powers.

For example, in 2010, when it joined the OECD, the Chilean government launched Start-Up Chile, an ambitious and determined programme which has already brought more than 1000 start-ups to Chile, leading to the emergence of a "Chilecon Valley" in the Southern Cone. In 2013, Brazil launched Start-up Brasil, and Peru followed suit in 2014. Colombia for its part has promoted one of the continent's most ambitious programmes for digitalizing the economy. Through its Ministry of Information and Communication Technology (ICT), it has launched a powerful digitalization programme. These countries are thus leading the wave of expansion in the region towards innovation, and let us not forget Mexico, which has succeeded in carving out a place for itself in the aerospace industry, with a powerful cluster in Querétaro.

In just a few years these activities have begun to bear fruit. Chile has succeeded in putting itself on the world start-up map: in 2010, its acceleration programme received some 100 applications, leading to the selection of 22 start-ups; in the latest round, nearly 1600 projects were presented, of which around 100 were selected. A key aspect is that 80 % of them came from abroad; one in every four start-ups selected comes from the USA, with others coming from India, Spain, Russia and the UK, as well as neighbouring South American countries. However, the most powerful and unexpected effect of this programme has been to arouse the entrepreneurial appetite of the Chileans themselves. Of the 100 or so start-ups selected in 2013, 19 were Chilean – and the figure increased further in 2014 and 2015. In barely 5 years, the programme has launched nearly 1000 start-ups. Meanwhile, Chile's venture capital industry has also grown, with no fewer than six new funds being launched in 2013, which will contribute some 125 million euros for financing new start-ups.

As in Brazil and Colombia, Chile's public institutions have played a key role in promoting this boom. In Chile, the Corporación de Fomento de la Producción de Chile (Corfo, or Chilean Production Development Corporation, a government body) is a key instrument. In Brazil, the driving force is split between the powerful BNDES (Brazilian Development Bank)

and Financiadora de Estudos e Projetos (FINEP, or Funding Authority for Studies and Projects, a government organisation for funding science and technology). In Colombia, the Ministry of ICT (through Apps.co) and the Banco de Comercio Exterior (Bancoldex, or Bank of Foreign Trade, a state-owned bank that also acts as an entrepreneurial development bank) are the prime movers of these changes. Admittedly, the continent still has a long way to go before it can join the ranks of the world's most innovative regions: not a single Latin American company appears among the world's 100 most innovative companies as identified by Thomson Reuters.

Some of the region's technology companies, for example, Chile's Sonda, already have annual revenues exceeding US$1 billion. This Latin American wave has only just begun: in 2013, in a Financial Times–Telefónica Global Millenials survey carried out in 27 countries, young people in Latin America led the responses of those seeing themselves as technological leaders. In Colombia, 27 % of young people surveyed were identified as technological leaders, just ahead of Peru (26 %), Chile (22 %), Mexico (21 %) and Brazil (18 %). All these countries surpassed the USA (16 %), the UK (13 %), Germany (12 %) and Spain and France (6 % each). In other words: the youth of Latin America is being pushed along on a wave of technological expansion that is much stronger than what we are seeing in Europe.

Clichés about Latin America abound. We continue to see the region as one big open-cast mine, brimming with raw materials and populist uprisings. And in part, this is indeed still the case. But we would do well to take note of the other Latin America that is emerging: thrusting, innovative and disruptive. We should not be surprised to see before long a Latin American start-up leap from Copacabana to the NASDAQ. In fact, it has already happened: MercadoLibre has leapt from the shores of Mar de Plata, and another called Globant, also from Argentina, took the leap in 2014. Others will soon follow, from Brazil, Chile and Colombia. We should not be surprised by this. Nor should we harbour any doubts about whether it will occur. Perhaps in the future the next Google will come from Rio de Janeiro. After all, the creator of Kinect, Microsoft's star product, is Brazilian.