

Overview

Brazil Digital Report

This document provides
a perspective of Brazil's
Digital Landscape



Today's Objectives

During the months of November 2019 and February 2020, together with Brazil @ Silicon Valley, McKinsey built the second edition of Brazil Digital Report – a broad view of the Brazilian Macroeconomic scenario, digital landscape, startup ecosystem and the digital maturity of incumbent companies

However, due to COVID-19, we decided to postpone the publication

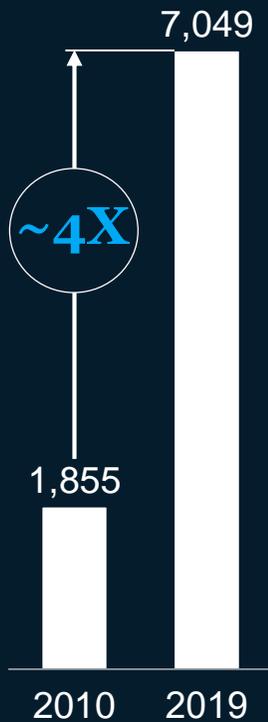
Today, we bring a summary of the findings from the startup ecosystem in Brazil pre-Covid-19

Dominant Incumbents

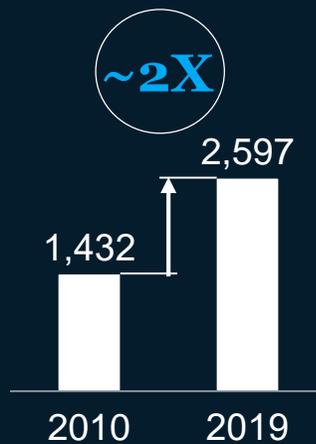


xx Growth in market cap

Top 10 companies market cap¹
USD B



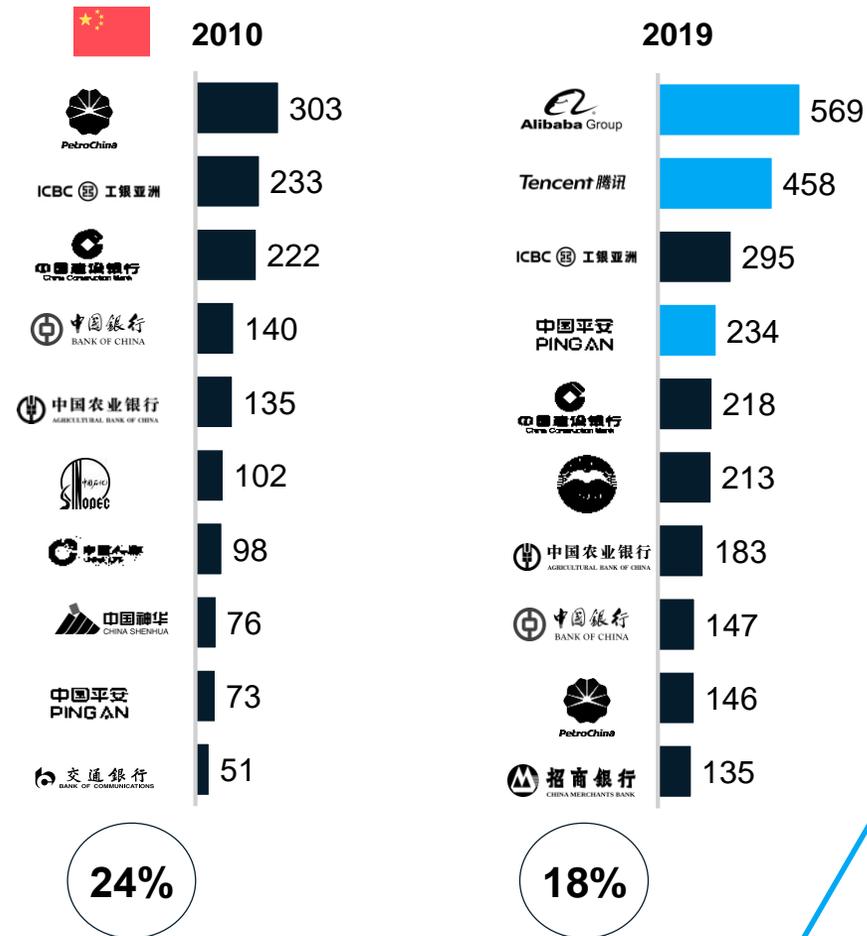
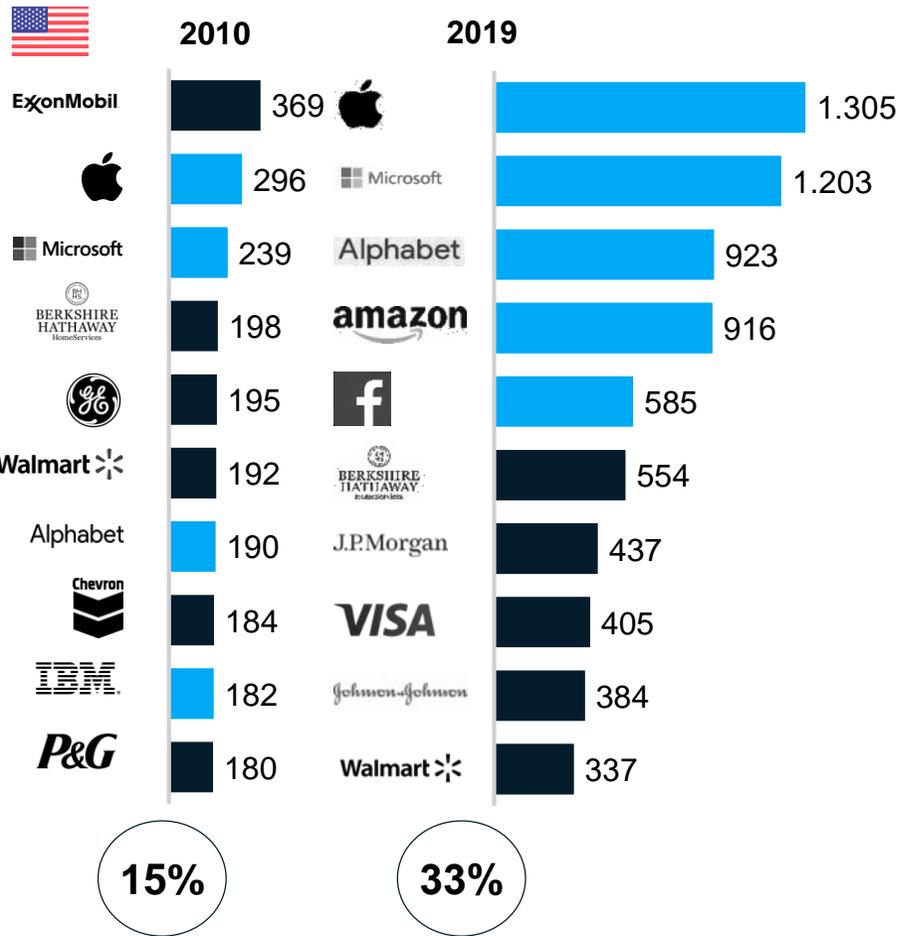
USA



China

While the top companies in the US and China became more valuable...

Top 10 companies market cap¹
USD Bi



■ Other companies ■ Technology companies (XX) % of total GDP

And more high-tech over the years...

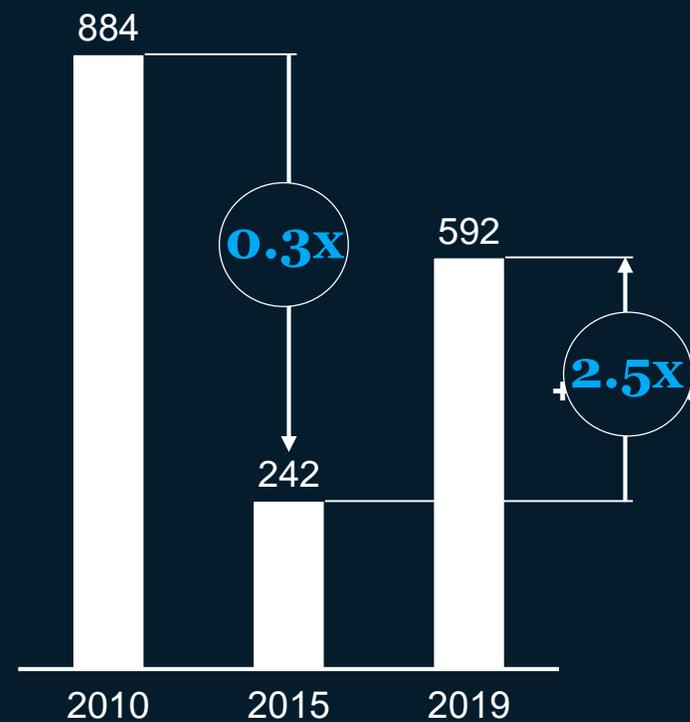


Brazil's top companies experienced considerable value loss before recent recovery...



Top 10 companies market cap¹
USD B

xx Growth in market cap



¹Top 10 companies market cap on Dec 31st of each year
Source: Capital IQ

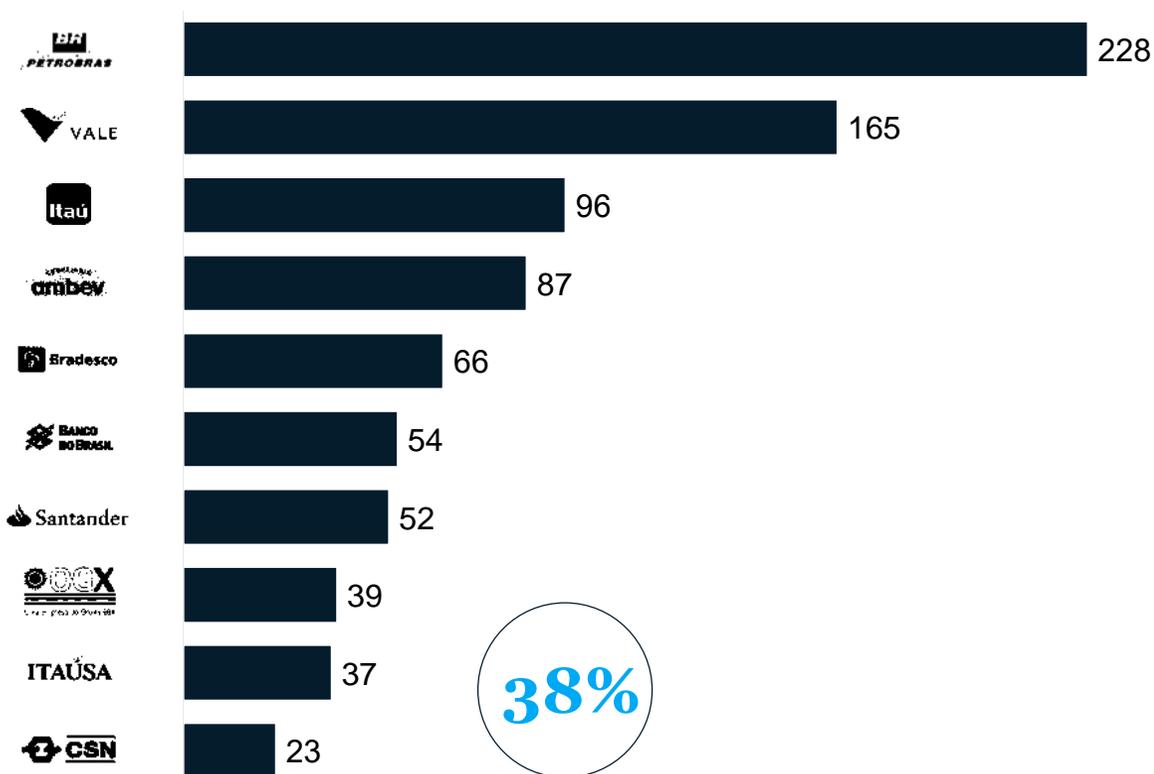
...and remained mostly traditional players

Other companies
 Technology companies
 x % Market cap / Country GDP

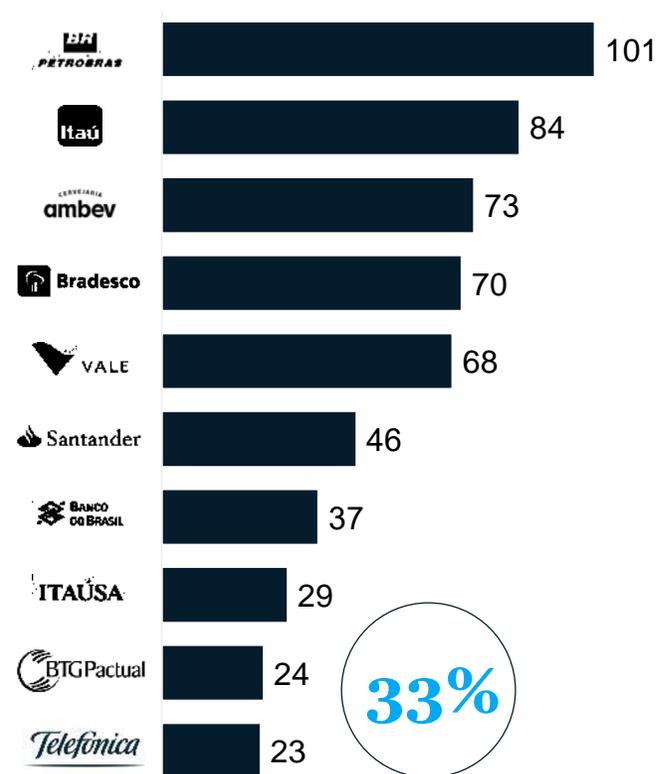
Top 10 companies market cap¹

USD B

2010



2019



¹ Considers market cap on Dec 31st of each year

Source: Capital IQ

**The new
tech era**



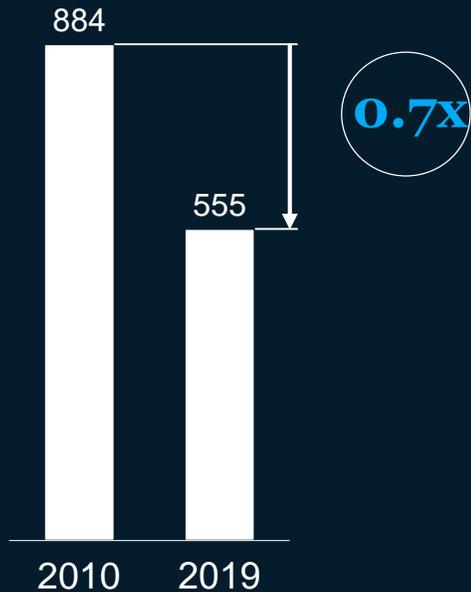
Tech companies greatly outperformed companies from other sectors...



xx Growth in market cap/value

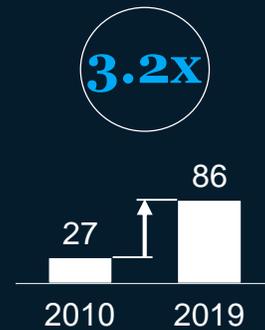
Top 10 non-technology companies market cap¹

USD B



Top 10 technology companies value¹

USD B



1. Considers market cap for listed companies and latest valuation for non-listed companies
Source: Capital IQ

... while their profile changed: most top 10 technology companies in 2019 are digital attackers

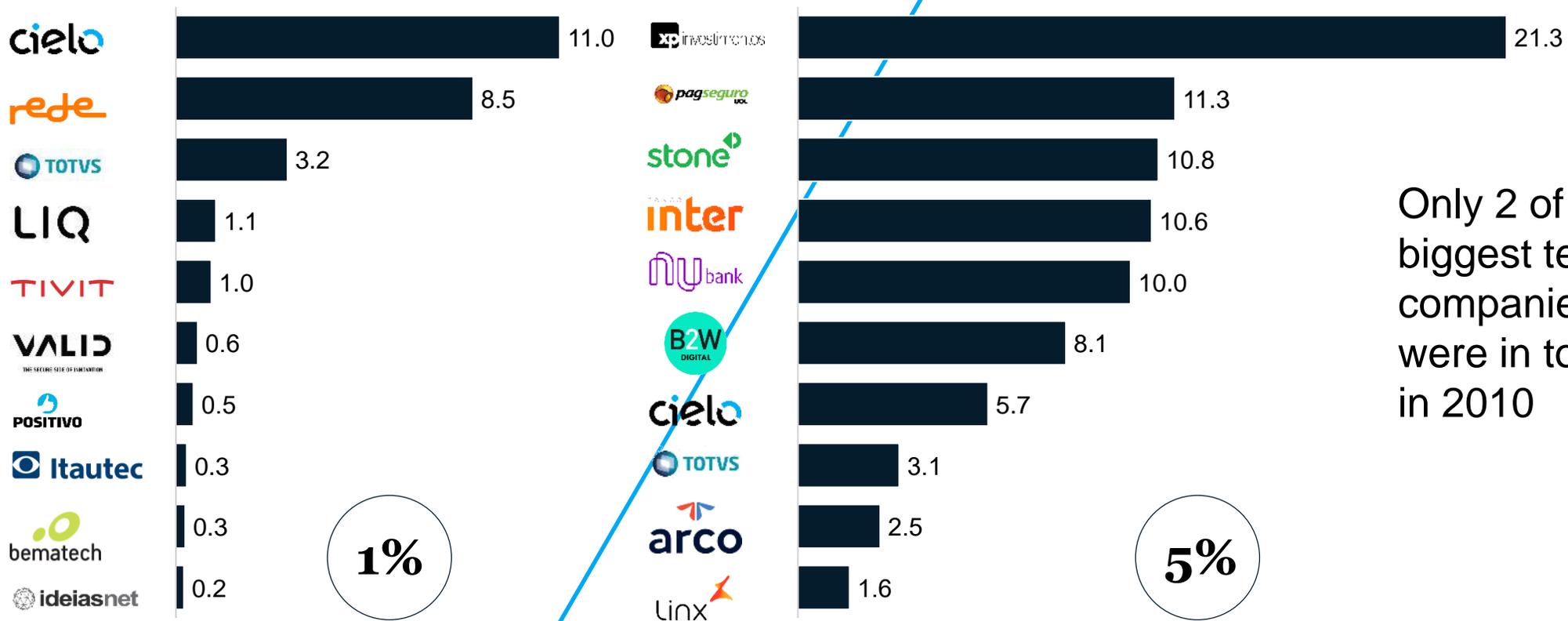
Top 10 technology companies market cap

USD B

2010

2019

■ Other companies ■ Technology companies (x) % Market cap / Country GDP



1%

5%

Only 2 of the biggest tech companies were in top 10 in 2010

1 Considers market cap on Dec 31st of each year
Source: Capital IQ



**For Brazil to
evolve on the new
tech area...**

**... Brazilian start-
ups need to thrive**

**To understand
Brazil's
technological
start-up
environment,
we surveyed
400+ start-ups
and interviewed
~40 leaders
between Nov/19
and Feb/20**

Quantitative survey

400+

Brazilian start-ups
across different
industries,
regions, and
development
stages

Qualitative interviews

~50

Leaders occupying various
positions in the market:
Start-up founders, top
executives, Venture Capital
investors, Institutional
leaders, regulatory experts

The surveyed start-up landscape presents a diversity of ventures

Region **56%**
are in the South East region

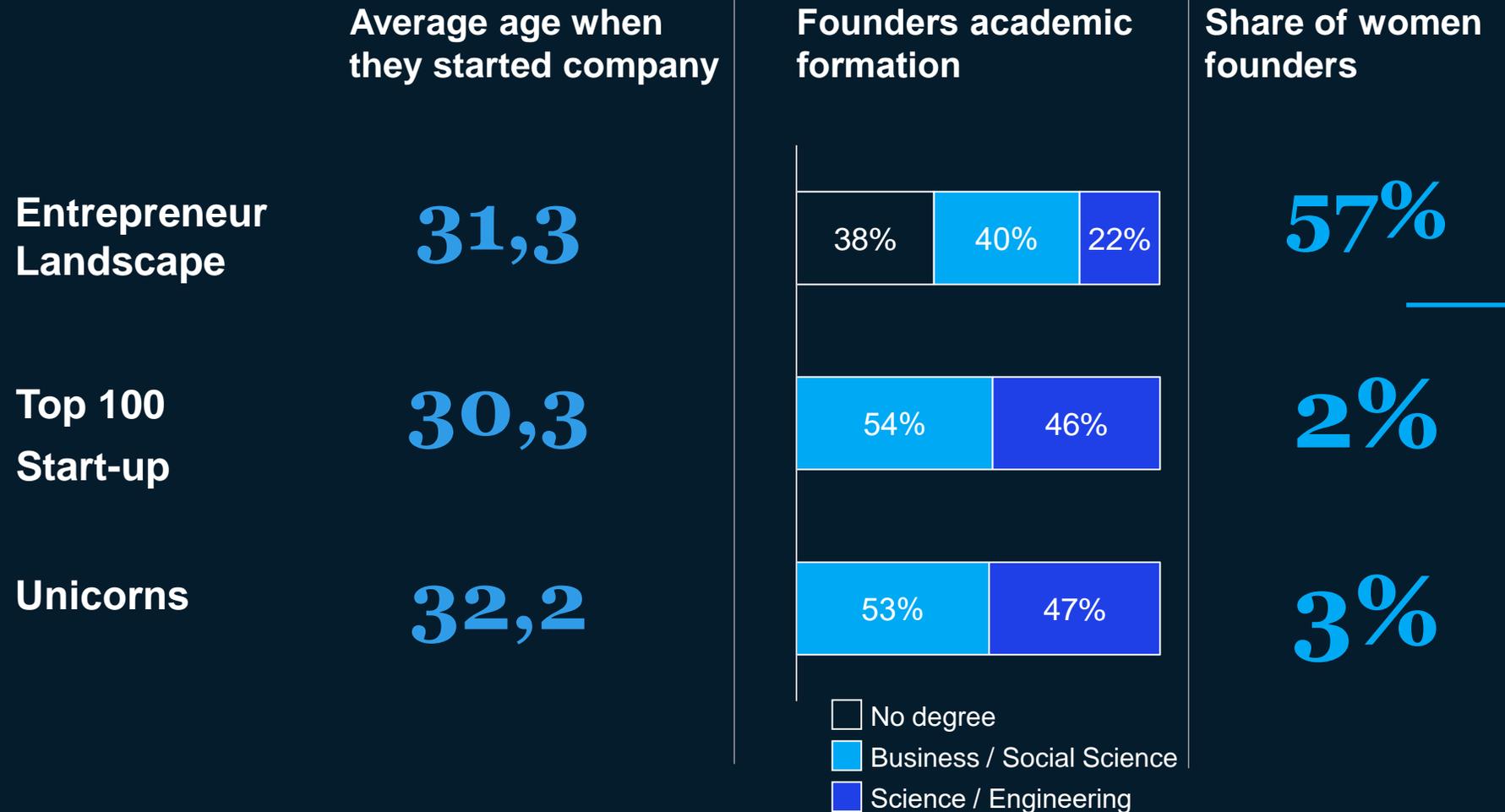
Team Size **66%**
have less than 21 members

Age **55%**
are less than 4 years old





In Brazil, start-ups are typically founded by individuals with business-education background profiles



Chances of success are significantly higher for serial entrepreneurs

26%

Top 100 founders had a previous start-up experience before launching their business

Unicorn founders, the share of serial entrepreneurs rises to

44%

Investment and Growth

The image features a dark blue background with a light blue diagonal line running from the bottom-left towards the top-right. A horizontal light blue line is positioned below the text, extending from the left edge to the diagonal line.

**Most startups
are
funded with
own,
friends & family
money**



54%

of Brazilian start-ups begin their businesses with the founders, family and friends funding

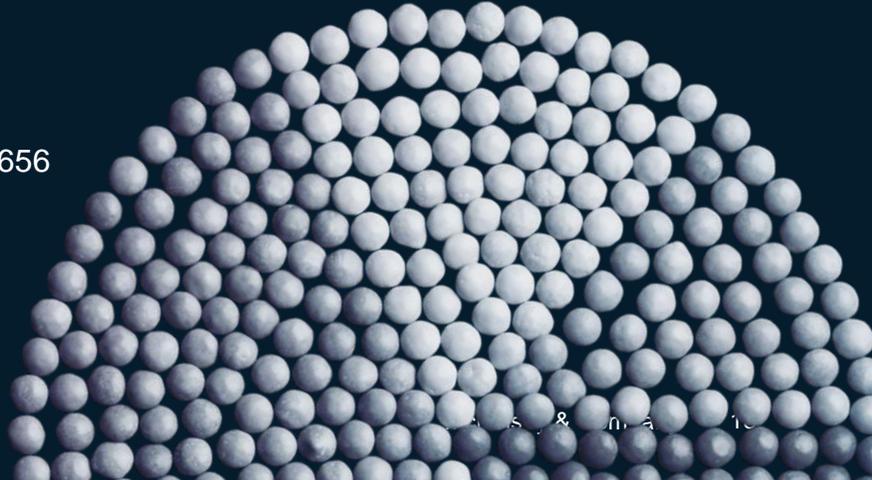
Angel investment is growing but still little developed

Angel investment
USD M

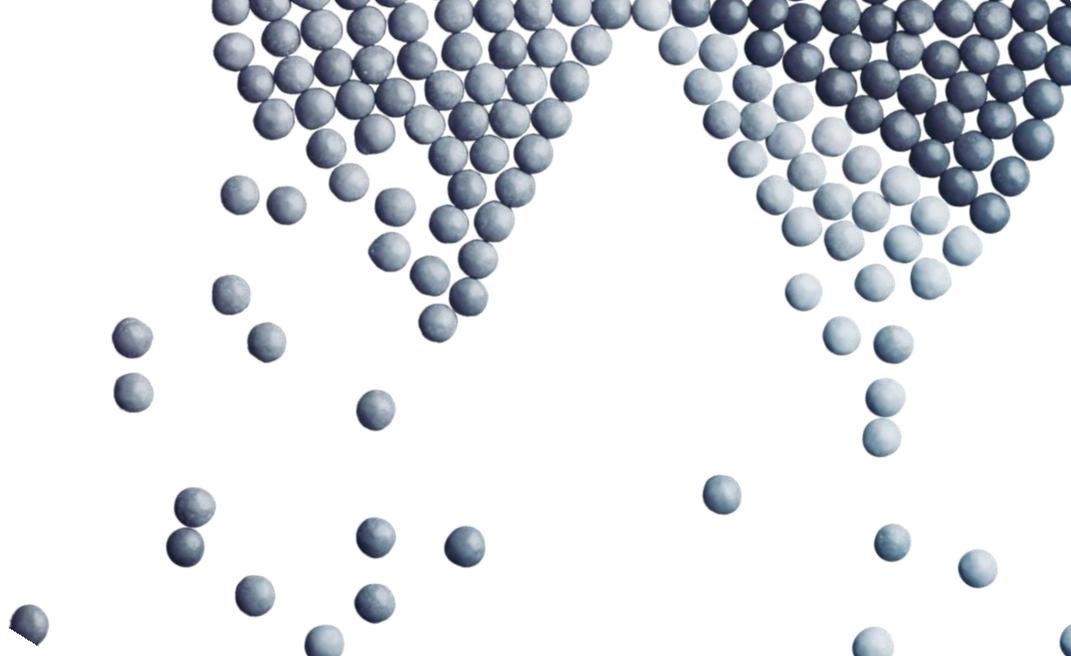
xx Brazil / USA investment gap



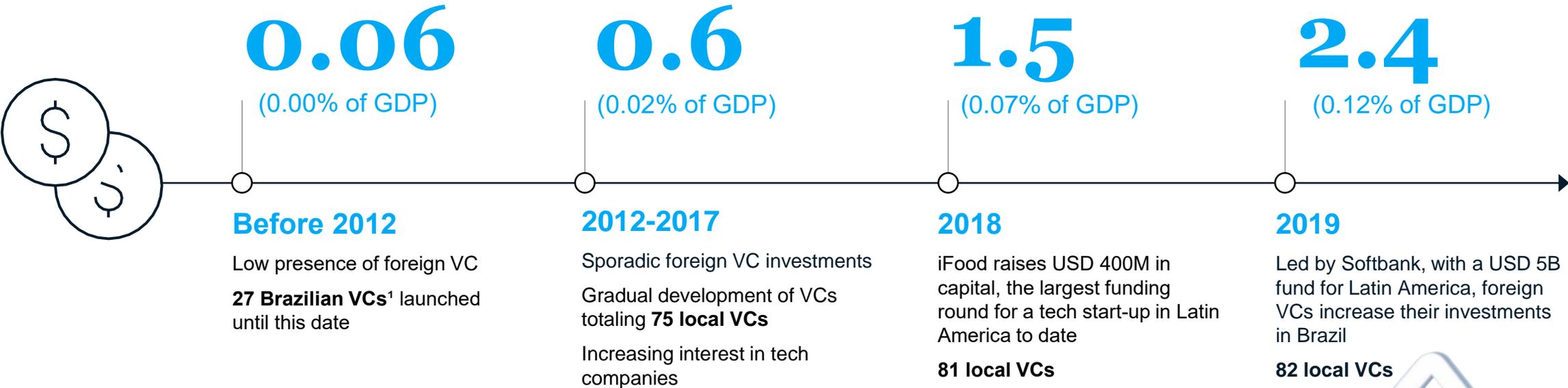
Source: Pitchbook



There has been a major increase in venture-capital investment over the last 5 years



Average yearly VC investment
USD B



Before 2012
Low presence of foreign VC
27 Brazilian VCs¹ launched until this date

2012-2017
Sporadic foreign VC investments
Gradual development of VCs totaling **75 local VCs**
Increasing interest in tech companies

2018
iFood raises USD 400M in capital, the largest funding round for a tech start-up in Latin America to date
81 local VCs

2019
Led by Softbank, with a USD 5B fund for Latin America, foreign VCs increase their investments in Brazil
82 local VCs

1. Considers tech-related VCs
Source: Distrito; Pitchbook

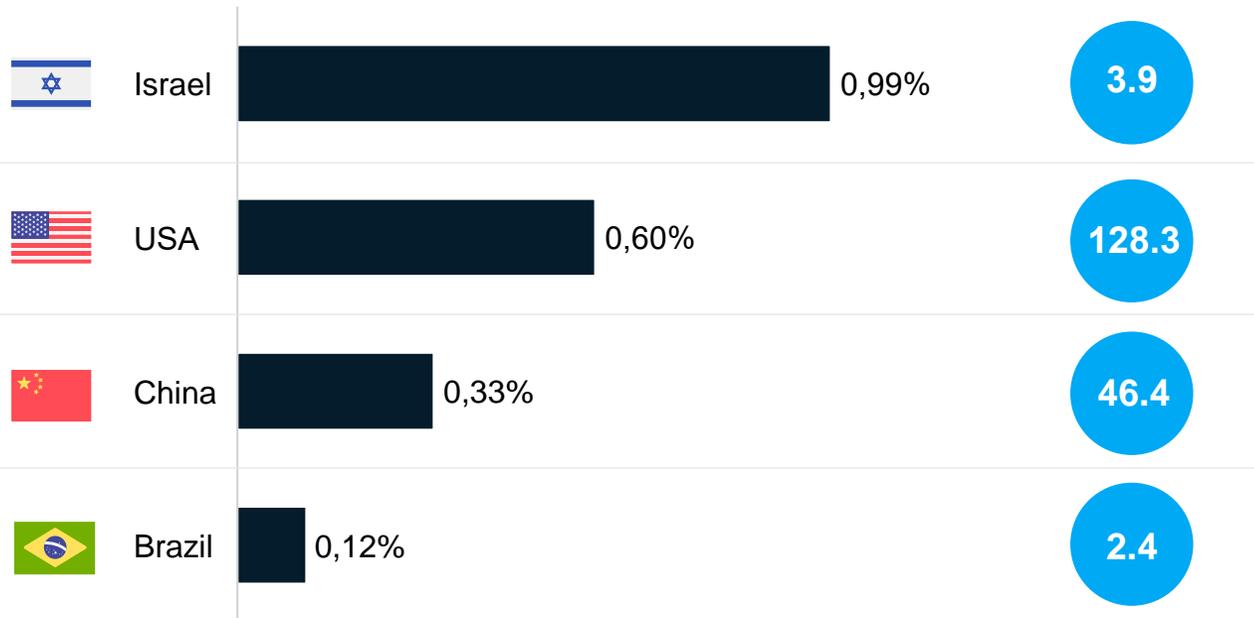
However, as a % of GDP, VC in Brazil still lags behind mature nations

Total Venture Capital activity - 2019

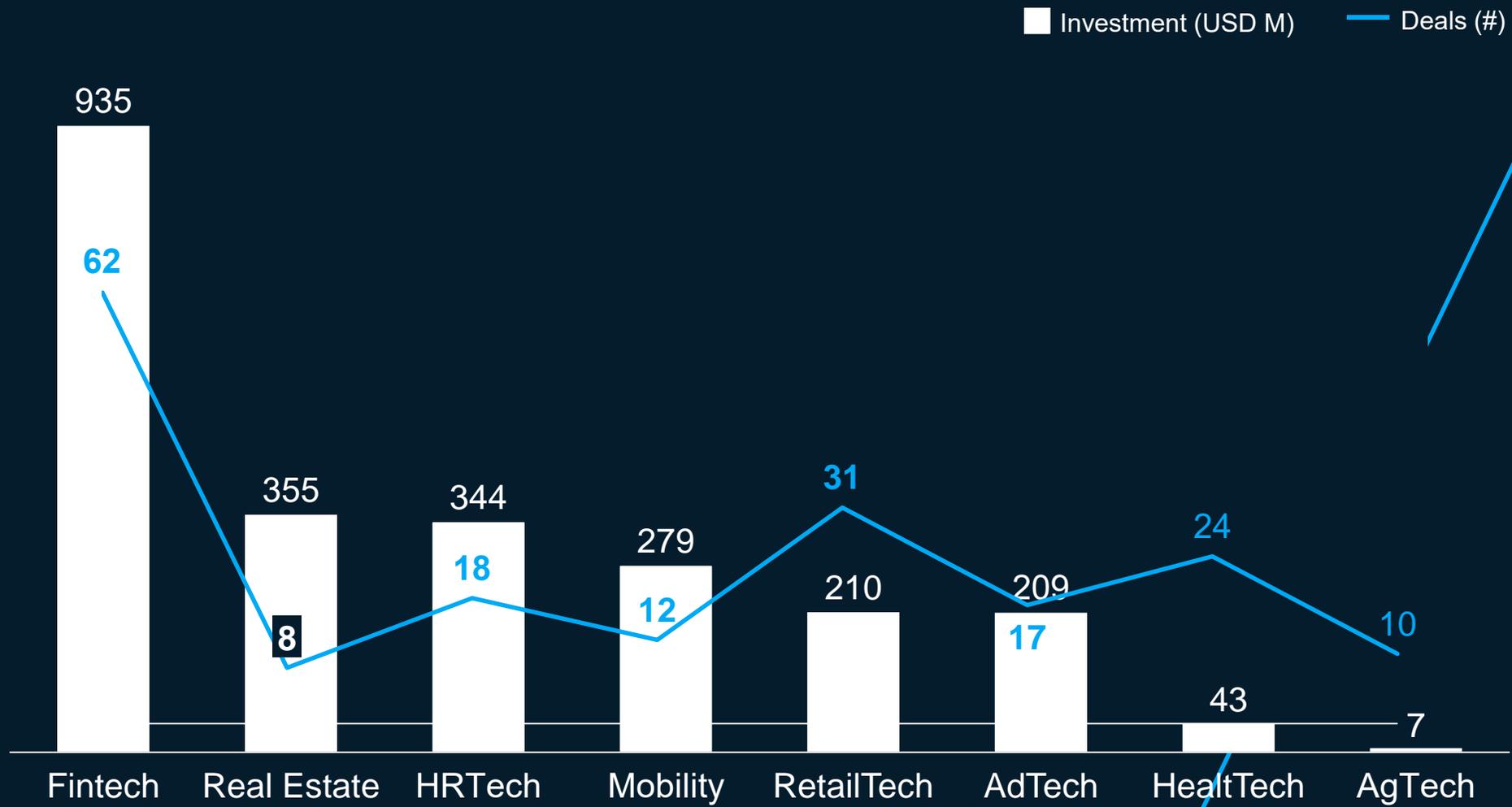
Total Venture Capital/GDP

Total Venture Capital amount

USD Bi, 2019



In 2019, FinTech's have attracted ~40% of VC investment volume



Source: Distrito Dataminer



Higher valuations created the imperative to go big or go home...

35%

Had as the main objective expand locally

19%

Had as the main objective expand internationally

Launch ¹

2014



40

2015



34

2016



38

2016



24

2017



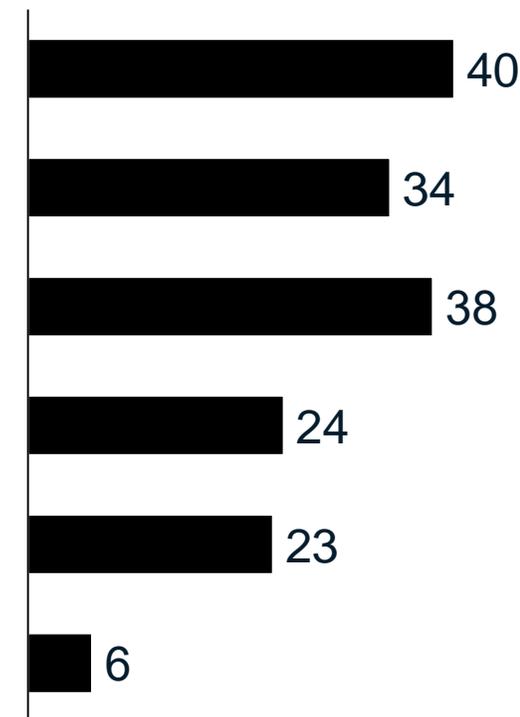
23

2019



6

of months to reach 1 million clients



(...ent or credit card)
2020; McKinsey analysis, Press search, Company websites

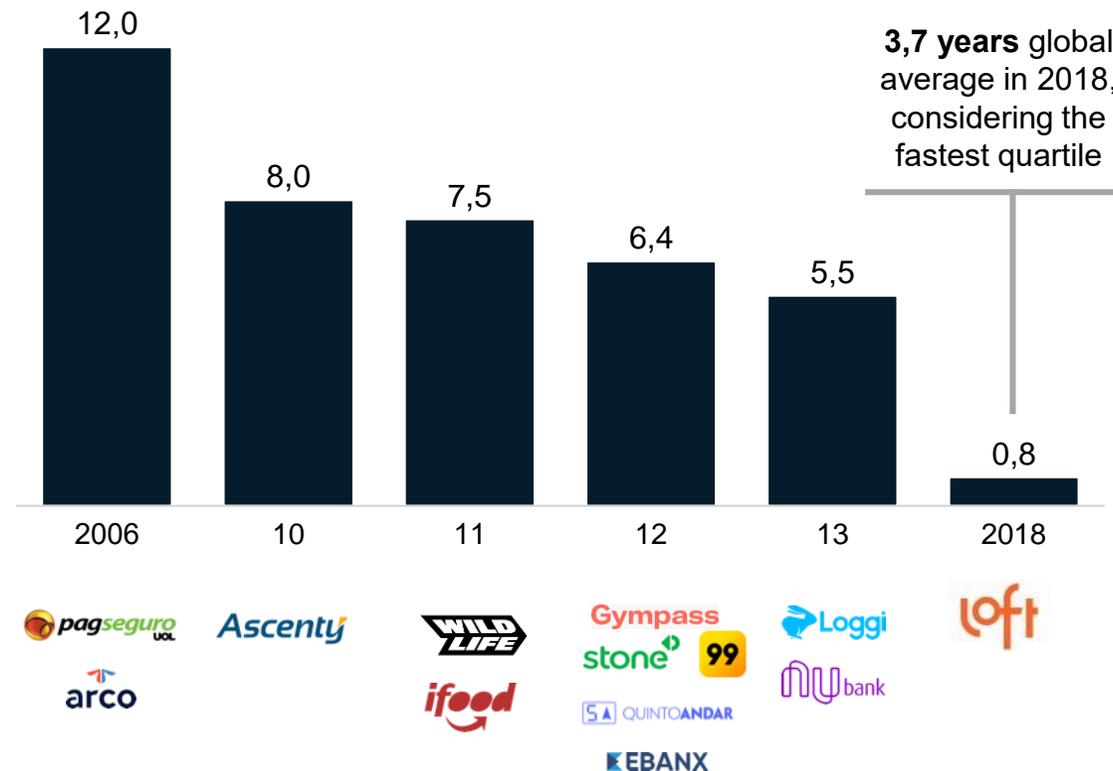
Faster burn rates, faster unicorns and faster failures

“With higher burn rates, there’s no more room for zombie start-ups just trying to survive.”

VC Founder

Average time to become a unicorn since year of foundation

Number of years to reach a USD 1B valuation or more



Brazil has consolidated itself as a continental hub, attracting players from all over the world...



2/3
of gross revenue

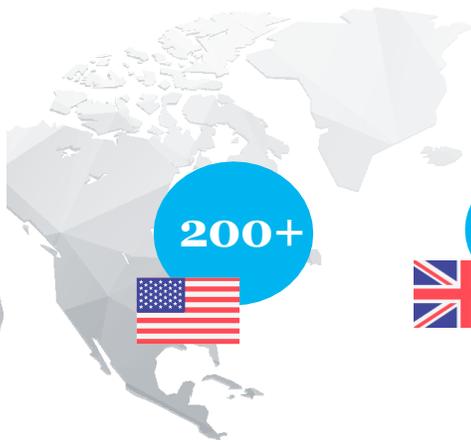


#1
Fastest growing market
for Prime users



... and a top unicorn builder

13 Unicorns¹
In Dec/2019



1. Considers disclosed private investments over USD 1B, recent IPOs by companies with a market cap over USD 1B, and non-disclosed investments with a market perspective over USD 1B
2 CB Insights criteria
Source: CBInsights Unicorn Ranking, Crunchbase, 2019; Team analysis

2019 M&A activity in start-ups

Company	Segment	Acquirer
	Business Software	
	Personal Products	oBoticário
	Consulting Services (B2B)	neon
	Consumer Finance	
	Mobility	grow
	Entertainment Software	IMMORTALS
	Business Software	linx 
	Media and Information Services	
	E-commerce	
	Retail	

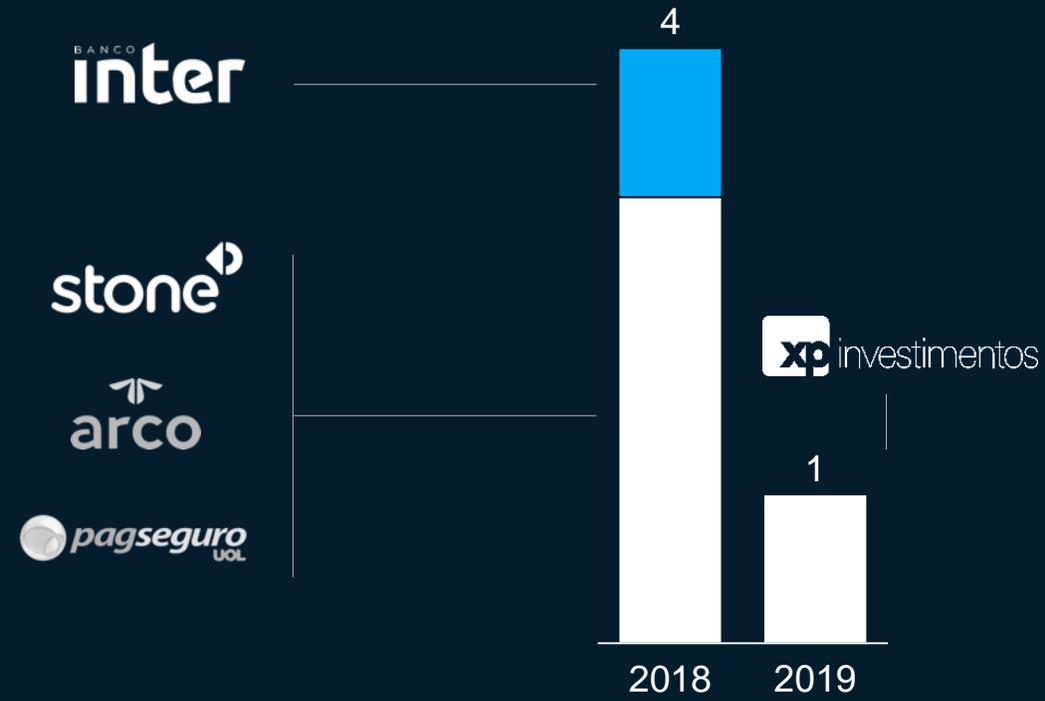
In 2019, there were big structural exit opportunities through M&As...

... and IPOs



Main tech IPOs per year Number of IPOs

- Brazilian Stock Exchange
- American Stock Exchanges



Local champions favored US stock exchanges



Higher demand and volume



More savvy and specialized investors

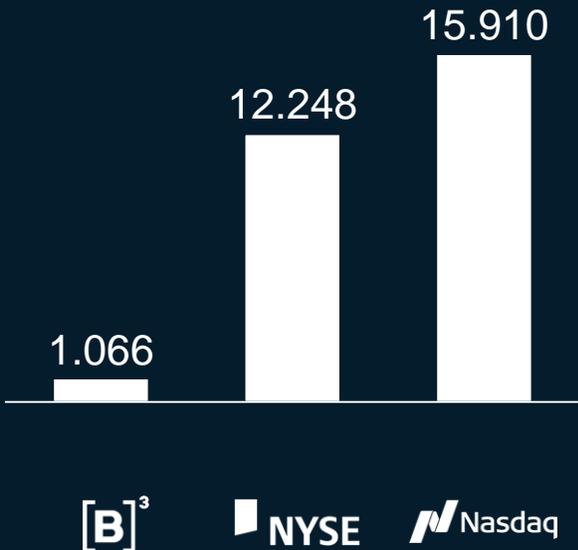


5x cheaper trading and clearing costs



Greater control over company voting rights

Volume of equities traded
USD B, 2019, annual



of listed companies



Source: World Federation of Exchanges, McKinsey Analysis

COVID-19, however, already impacted funding rounds...

“For those during fundraising process, how was your fundraising impacted by COVID-19?”

30%

Of startups **canceled** their Fundraising process due to COVID-19

16%

Of startups had **informal agreements that were canceled** or are in re-negotiation

11%

Of startups decided to focus on **insiders investors** instead

20%

Of startups **maintained** their Fundraising process unchanged during COVID-19

13%

Of startups were **able to close** their Fundraising round during COVID-19 (2% after renegotiation)



... And should impact future valuations...

“What is your expectation on the funding scenario after COVID-19?”

Valuation adjustments according to FX exchange depreciation

0-25% reduction on valuations

25-50% reduction on valuations

>6-month freeze in funding activity

13%

24%

22%

27%

Source: Atlantico Survey April/2020

Talent and retention

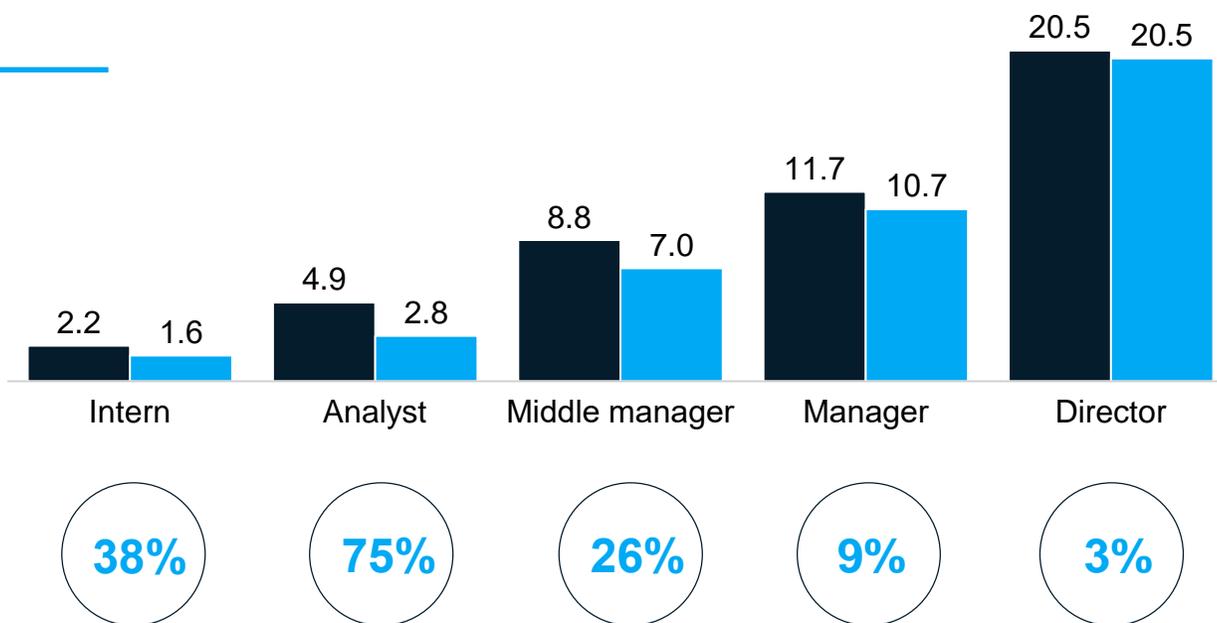




Salary gap tends to decrease with more-senior roles

Average monthly Salary¹

BRL thousands, 2019



Start-ups compete for top talents

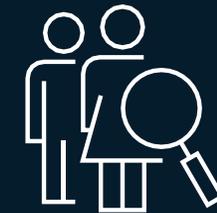
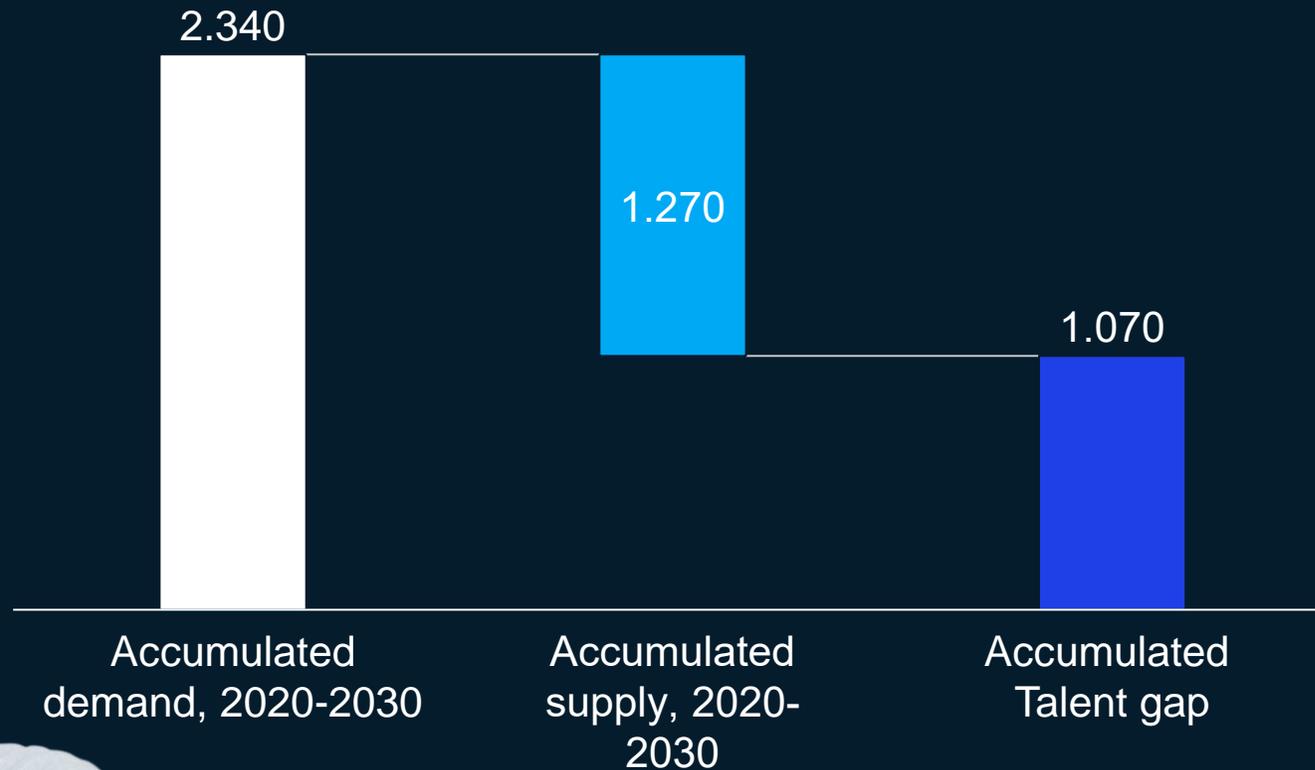


1. 8,373 salaries, 12 start-ups and 12 incumbent corporations – does not include equity
 Source: Brazilian Start-ups Landscape Survey – McKinsey 2020, Love Mondays

However, tech talent seems to be a bottle neck

Expected demand for tech professionals

Thousands, 2020-2030



> 1 mn

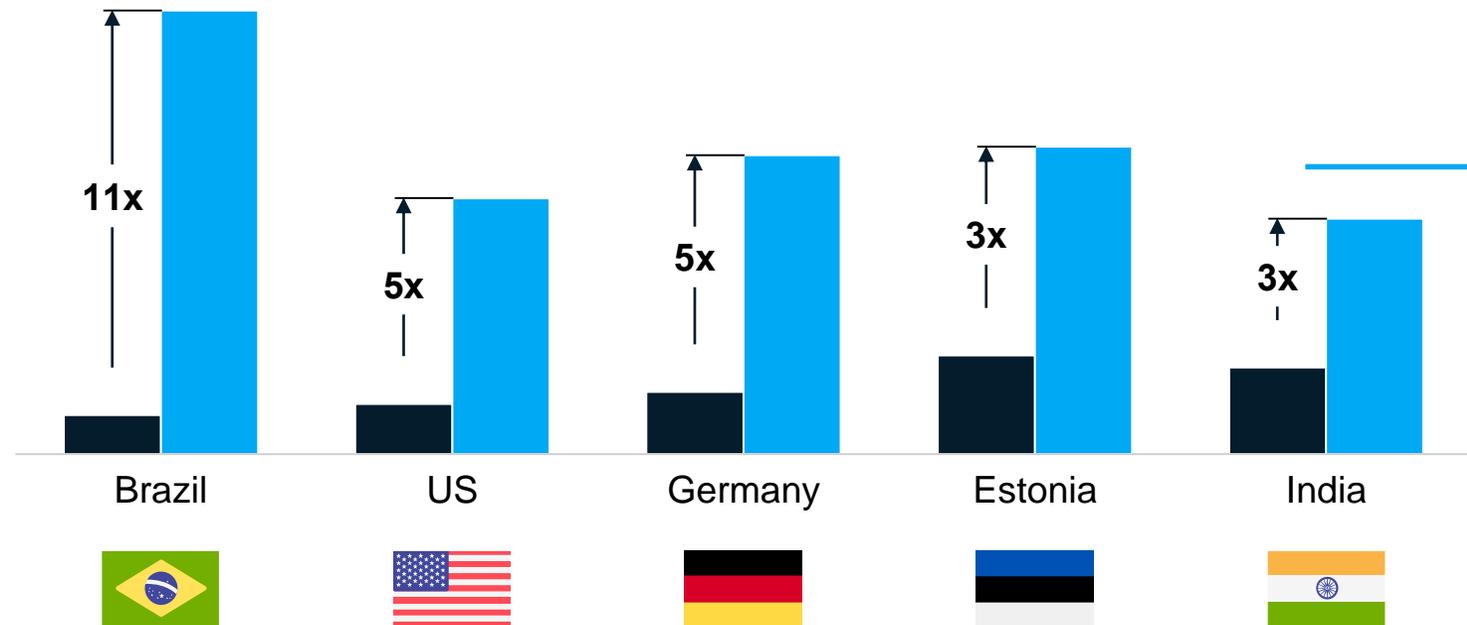
Cumulated talent gap for tech professionals by 2030

Data Scientists / Engineers, UX designers, Mobile and Web Developers and Agile Coaches are among the most wanted profiles

Technology talent-gap remains significantly bigger in Brazil: for each new tech professional, Brazil graduates more than 11 law or business students

Graduates by field of study

■ Technology-related courses ■ Business Administration and Law



There is a huge quality gap in tech education

‘ Tech education in Brazil is oriented to academia, and there is a gap between what students learn and what the market needs. ’

Start-up CEO

35%

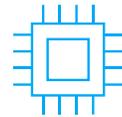
of tech courses are below minimum level¹ to satisfy market expectations

Globally, governments have been promoting education initiatives to address the gap in technical education



Type of initiatives

Global example



Increase of technology spots at traditional universities

In 2019, China opened around 400 majors related to big data, artificial intelligence (AI) and robotics in universities



Revamp university curricula to address market needs

Traditional universities have been adapting the programs



Develop online learning to increase access to technical education

In 2020, India's government authorized its top 100 institutions to offer fully online degrees to support its ambition to double graduates by 2035



Investment in **alternative technical-education** initiatives

The Israel Innovation Authority funds extra-academic coding bootcamp since 2018



Offer incentives for **tech professionals immigration**

Beijing government is easing visa policies and offering cash incentives to attract top class global talent



Start-ups develop their own alternatives to fill the talent pipeline



Going where talents are



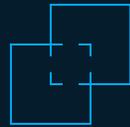
Rising own talents



Strengthening ties with academia



Importing talents



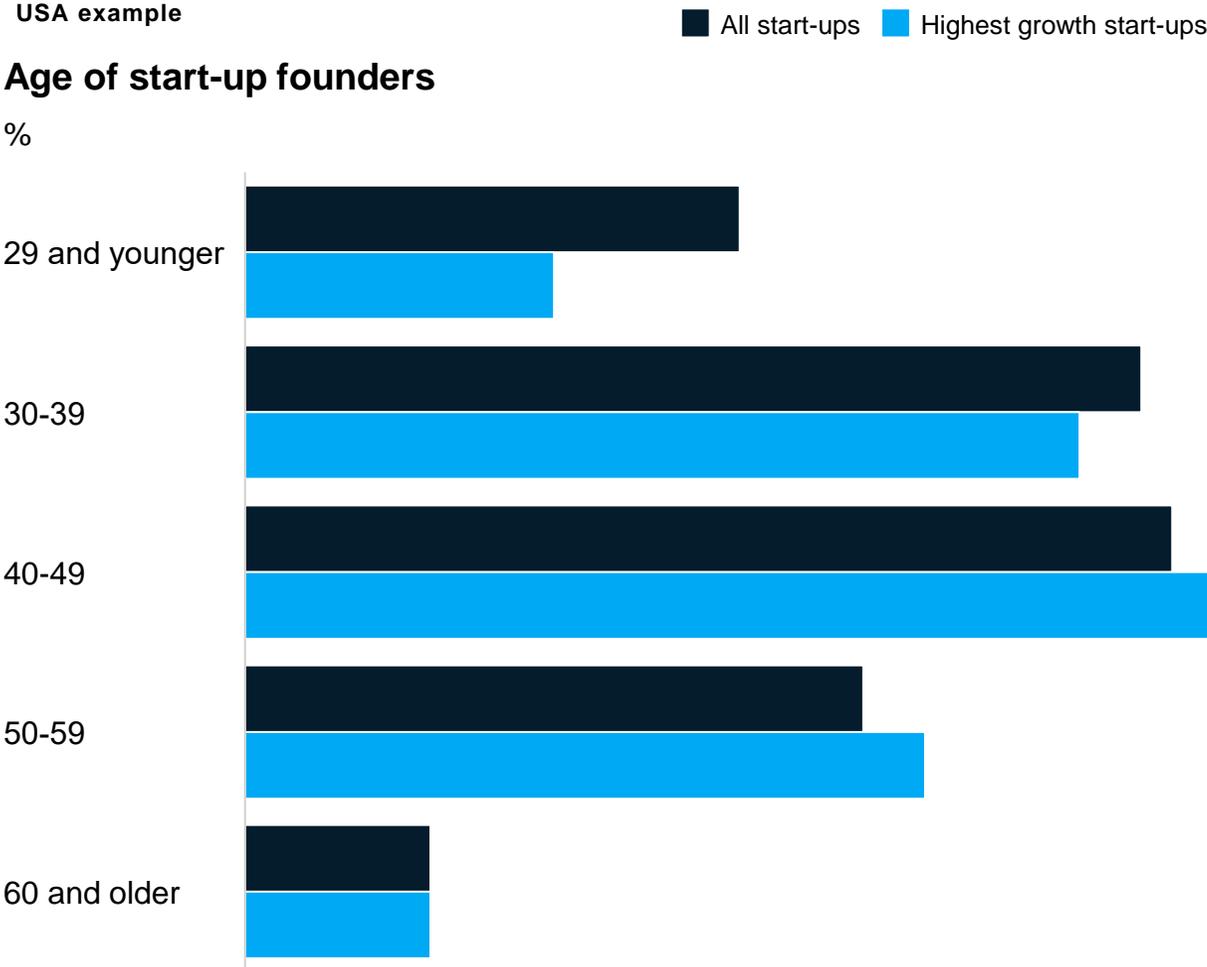
Acquiring companies for talents



Offering non financial incentives



The “young entrepreneur” is a myth



42

is the average age of entrepreneurs at the time they founded their companies

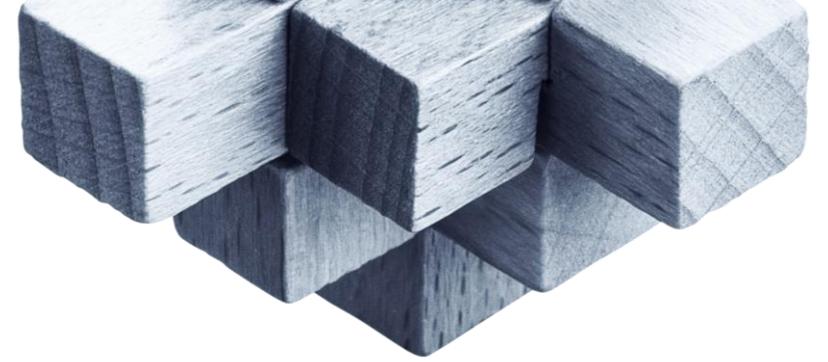
45

is the average age of founders starting the top 0.1% of start-ups



Source: Age and high-growth entrepreneurship; MIT, Northwestern and U.S. Census Bureau

As they grow, start-ups thrive on “white hair” experience

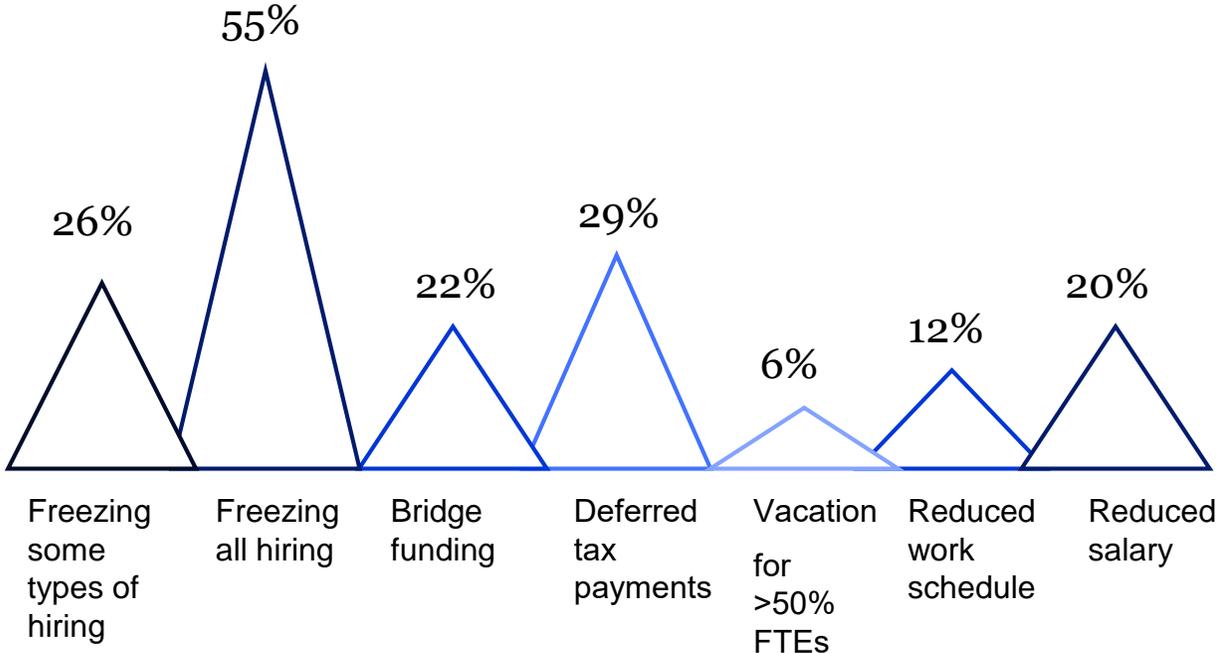
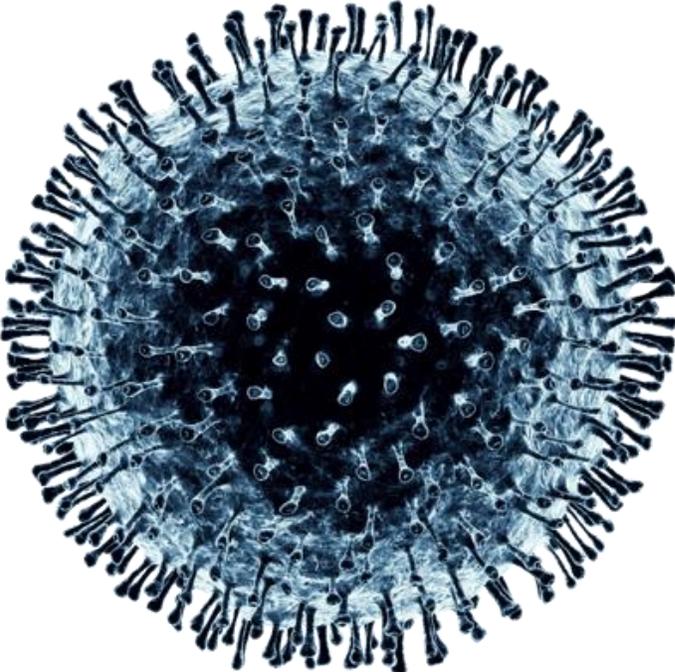


‘ *Fast growth comes with talent challenges: the young professionals that were great on starting the business not necessarily are good on leading a big organization. When growth comes, startups need **experience professionals to lead big operational teams and standardize processes.*** ’

CEO of Startup

The pressure for lower burning rates due to the COVID-19 crisis should impact talent acquisition...

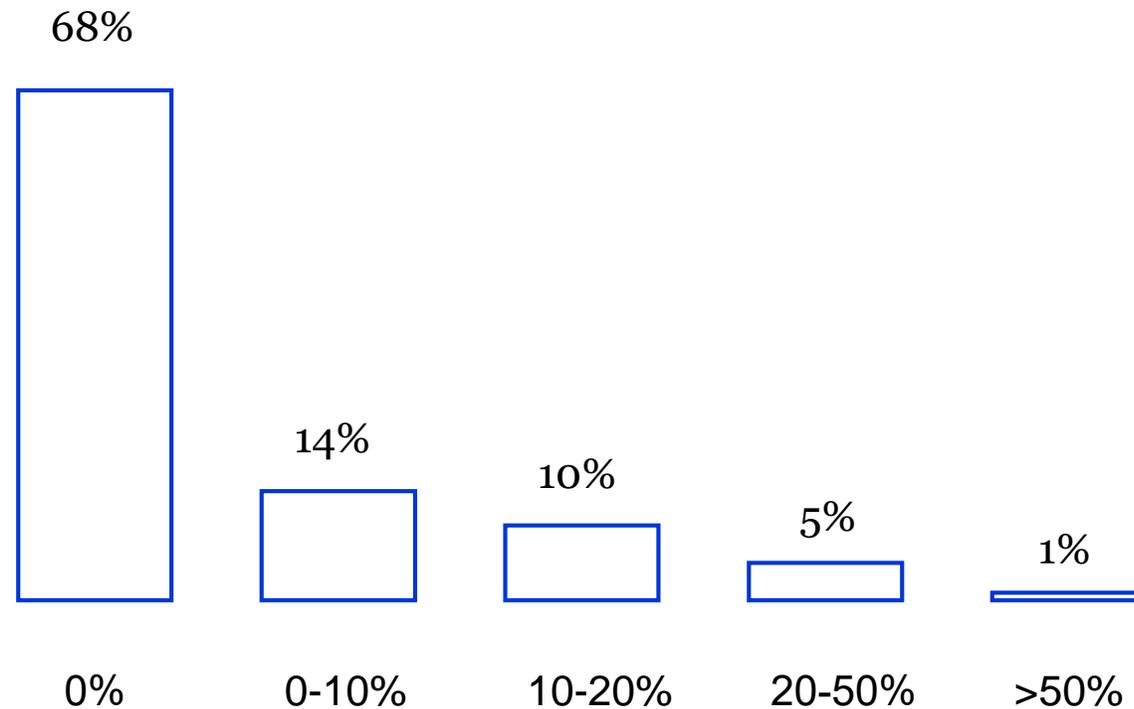
“Which of these actions did you already implement (post COVID-19 crisis) or will implement?”



Source: Atlantico Survey April/2020

... but massive layoffs are yet a question mark

Predictable layoff due to COVID-19



Source: Atlantico Survey April/2020

In summary:

On funding: we were happy and we knew it!

- We reached an all time high in terms of money inflow for innovation, with higher valuations and faster growth
- COVID-19 should cool down momentum, but maintaining higher landing
- Bridge funding or new rounds on lower valuation will likely emerge

On talent: the challenges of BC are still here, but now is time to bootstrap and hang in there.

- Startups are competing for top talents
- Tech skills are a bottle neck and companies need to be creative to attract and retain; the country should have a broad plan to close the gap
- The young entrepreneur is a myth, and with growth, comes the need for experienced professionals
- COVID-19 should put pressure on new hiring and massive layoffs are yet a question mark

McKinsey
& Company

Obrigado, stay safe!