The Quest for Entrepreneurial Growth in a Tumultuous Brazil
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Thesis presented to Escola de Administração de Empresas de São Paulo of Fundação Getulio Vargas, as a requirement to obtain the title of Master in International Management (MPGI).

Knowledge Field: Entrepreneurship & Venture Capital

Adviser: Prof. Sérvio Túlio Prado Júnior

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ABSTRACT

This case introduces the concept of entrepreneurial funding and tackles the issue of how start-ups can find growth amidst economic downturn. Students follow the development of Carrinho em Casa, an entrepreneurial venture that offers a grocery delivery service to its clients in less than two hours. Although it offers a unique service in its marketplace, Carrinho em Casa is having trouble scaling its business due to difficult economic conditions and limited financial flexibility. Nearly a year after its launch, the co-founders of Carrinho em Casa are at a crossroads and remain unsure of how to take their business to the next level. On the one hand, co-founder David is advocating the need for external capital, arguing that obtaining VC-backed funding would provide Carrinho em Casa with the boost it desperately needs. On the other hand, co-founder Ricardo believes bootstrapping is the wiser solution. He insists that Carrinho em Casa should continue to grow organically through its already unit-profitable business, and as a consequence maintain total ownership of the company. The case introduces the concepts of VC funding and bootstrapping and encourages students to explore the opportunities and challenges of these different types of financing. The case allows students to grapple with the strategic and tactical decisions related to funding and pushes them to better understand how such decisions can impact all aspects of the business: sales, profits, management, motivation, incentives and exit opportunities, amongst others. Finally students are encouraged to reflect on the numerous challenges and opportunities related to starting an entrepreneurial venture in emerging markets under difficult economic, political and social conditions.

KEY WORDS: Entrepreneurship, Entrepreneurial Funding, Venture Capital, Emerging Markets, Bootstrapping
RESUMO

Este caso apresenta o conceito de financiamento empresarial e aborda a questão de como as start-ups podem encontrar crescimento, mesmo durante uma crise econômica. Neste trabalho, os estudantes seguem o desenvolvimento da Carrinho em Casa, um empreendimento que oferece um serviço rápido de entrega de compras de supermercado. Apesar de oferecer um serviço único no mercado brasileiro, a empresa Carrinho em Casa está tendo problemas para escalar suas operações, devido a condições econômicas difíceis e flexibilidade financeira limitada. Quase um ano após o lançamento da start-up, os cofundadores de Carrinho em Casa estão em uma encruzilhada e estão discutindo como levar a empresa para frente. Por um lado, o cofundador David está defendendo a necessidade de capital externo, argumentando que a obtenção de financiamento apoiada pelos VC daria à Carrinho em Casa o impulso que precisa desesperadamente. Por outro lado, o cofundador Ricardo acredita que o “bootstrapping” é a solução a mais sábia. Ele insiste que a Carrinho em Casa que já é “unit profitable”, deveria continuar a crescer organicamente. Consequentemente, eles deveriam manter a propriedade total da empresa. Este caso apresenta os conceitos de financiamento VC e bootstrapping e incentiva os alunos a explorar as oportunidades e os desafios destes diferentes tipos de financiamento. O caso permite que os alunos pensem nas decisões estratégicas e táticas relacionadas ao financiamento e empurra-los para entender melhor como essas decisões podem afetar todos os aspectos do negócio: vendas, lucros, gestão, motivação, incentivos e oportunidades de saída, entre outros. Finalmente, os alunos são encorajados a refletir sobre os inúmeros desafios e oportunidades relacionadas com lançar um empreendimento em mercados emergentes caracterizados por condições econômicas, políticas e sociais difíceis.

PALAVRAS CHAVE: Empreendedorismo – Brasil, Empresas Novas, Capital de Risco, Financiamento, Investimentos
## LIST OF ABBREVIATIONS AND ACRONYMS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>BM&amp;F BOVESPA</td>
<td>Bolsa de Valores, Mercadorias &amp; Futuros de São Paulo</td>
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<tr>
<td>B2B</td>
<td>Business to Business</td>
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<tr>
<td>B2C</td>
<td>Business to Consumer</td>
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<tr>
<td>BNDES</td>
<td>Banco Nacional de Desenvolvimento Econômico e Social</td>
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<td>CVM</td>
<td>Securities and Exchange Commission of Brazil</td>
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<td>FINTECH</td>
<td>Financial Technology</td>
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<td>IPO</td>
<td>Initial Public Offering</td>
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<td>LAVCA</td>
<td>Latin American Private Equity &amp; Venture Capital Association</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>PE</td>
<td>Private Equity</td>
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<td>VC</td>
<td>Venture Capital</td>
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<td>SaaS</td>
<td>Software as a Service</td>
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<td>S&amp;P</td>
<td>Standard &amp; Poor’s</td>
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<tr>
<td>SWOT</td>
<td>Strengths, Weaknesses, Opportunities, Threats</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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Part 1: Case Study - The quest for entrepreneurial growth in a tumultuous Brazil

1.1 Introduction:

As David Russel sipped on his suco de maracuja, he admired the view of the distant Pão de Açucar and thought to himself: “Choosing Brazil as the place to launch our start-up really was a good idea after all. I could do this forever!” Yet summer was coming to an end and it was time for David to return to São Paulo and get back to business. The break had given him a lot of time to think about his company and where to take it next. His start-up, Carrinho em Casa, was somewhat stuck in a rut. Carrinho em Casa, a grocery delivery service, allowed customers to buy groceries online and receive their orders in less than two hours. The main revenue stream came from the R$9.90 fee charged per delivery. Although Carrinho em Casa’s business model was very promising, the company lacked scale. For now, it was only operational in a select number of neighbourhoods in São Paulo. David felt it was time to reach out to external investors. Obtaining a round of funding from a venture capital firm would most definitely accelerate growth. Yet he wasn’t sure his friend and co-founder Ricardo Prelhaz would hop on board. Ricardo, who had already returned to work, believed Carrinho em Casa should continue to fund growth organically, through the company’s retained earnings. Convincing him to see otherwise would not be an easy task and David knew the upcoming week would be a busy one. There was a lot to be discussed.

David settled in his seat and asked the flight attendant for a copy of his favourite Brazilian newspaper: Valor Econômico. The headlines weren’t as pleasant as Rio’s sunny skies. The Brazilian real had plunged yet again and the start of an impeachment trial against president Dilma Rousseff seemed increasingly likely. Brazil was, undoubtedly, facing one of its worst economic and political crises yet. With very low growth, deepening fiscal deficit, increasing unemployment and ongoing corruption scandals, Brazil did not seem very business friendly. Yet, David and Ricardo had decided to make it their home.

Two years prior, in 2013, while still post-graduate students at NOVA business school in Lisbon, Portugal, David and Ricardo went for a drink after class and started discussing their future plans. The school year was coming to an end, and while some of their other classmates were applying for corporate jobs in banking or consulting, David and Ricardo had other goals in mind. They were both entrepreneurs at heart. As a matter of fact, they had taken all of the entrepreneurship courses offered at NOVA and had done the same during their 6-month exchange at the Fundação Getulio Vargas in São Paulo, Brazil.

David and Ricardo had already discussed the possibility of launching a business together. They were a good match. David, born and raised in New Mexico, United States, didn’t fit in any of the most common stereotypes of American young professionals. Before moving to Portugal for his master’s degree in international finance and management, he had studied economics at McGill University in Canada. David spoke four languages and loved traveling, having lived and worked in a handful of cities including Washington, Montreal, São Paulo, Madrid, Barcelona, and even Luanda in Angola. Ricardo on the other hadn’t moved
around as much. He was Portuguese and had completed both his undergraduate and graduate studies at NOVA business school in his hometown of Lisbon. Yet, he was passionate about Latin America and had worked in Argentina and Brazil at Dafiti, one of the region’s most successful e-commerce start-ups. He too spoke several languages fluently and had a strong entrepreneurial spirit just like David.

One of the ideas they tossed around that day was that of a grocery delivery service. David knew how successful US-based start-up Instacart was and thought it could be interesting to launch a similar business model somewhere else. Instacart, founded in 2012, by former Amazon employee Apoorva Mehta, was an internet-based grocery delivery service that relied on independent contractors, what they called “shoppers” to deliver groceries to customers in less than 1 hour. In 2015, Forbes magazine had ranked Instacart number one on its “America’s Most Promising Companies” list. In just over 2 years, the company had expanded to 15 US cities, was contracting over 4,000 personal shoppers and had received funding from some of the most notable Venture Capital firms of Silicon Valley: Sequoia Capital and Andreessen Horowitz, amongst others.

Since both David and Ricardo spoke Portuguese and had previous experience in Brazil, they felt Sao Paulo could be a great place to test the concept. They also knew how long supermarket lines tended to be in the city. Traffic was also an issue. Back in 1996, the city of Sao Paulo had been a pioneer in relieving traffic congestion through the introduction of a travel restriction scheme called “rodizio veicular”. The driving restriction, still applicable today, is based on the last digit of the license plate and each day, two numbers are restricted to travel during rush hours. Providing a grocery delivery service could finally be the solution to both of these issues. Carrinho em Casa’s service could be a true time-saver for busy professionals unwilling to waste time in supermarket lines or traffic jams. In addition, with a population of over 200 million and a rising middle class, they both felt Brazil was still one of the most promising Latin American markets despite the economic crisis.

1.2 Launching Carrinho em Casa:

Carrinho em Casa was officially launched in September 2015. The cofounders had decided to implement a business model similar to Instacart’s in the U.S. Customer’s would set-up a profile on the Carrinho em Casa website by entering their personal details, including their home address and credit card information. They then had access to the platform from which orders could be placed. According to the neighbourhood in which the customer lived, different supermarkets would show up as available for delivery service. A unique feature of Carrinho em Casa, was that the customer could then pick and choose the food items he or she wanted from the different supermarkets available, knowing that everything would then be delivered together, at once. The customer could even order in advance and then choose the most convenient delivery time. Since most apartment buildings in Sao Paulo had door guards for security concerns, the groceries could often be left with them even if the customer was not at home, adding to the convenience of the service. The delivery service cost R$9.90 per order
and the minimum value of an order was of R$29,90. If, for some reason, the customer needed to cancel his or her order, he could do so by contacting Carrinho em Casa. As long as the shopper had not yet purchased the items from the supermarket, the customer would be fully reimbursed.

The website was up and running but David and Ricardo hadn’t managed to contract “shoppers” yet. When they received an order, the co-founders would quickly call an Uber and personally deliver the groceries to their customers themselves. In subsequent months, they were able to get a decent amount of press coverage from some of Sao Paulo’s most important newspapers. Word-of-mouth and their Instagram and Facebook accounts were also useful in attracting first clients. David insisted Carrinho em Casa employ the American principal that “the customer always comes first”. If the products received weren’t exactly what a client had ordered, Carrinho em Casa promised to fix the issue the same day, free of charge. This rarely happened however and customer reviews were consistently positive, which helped the company build a solid reputation.

David and Ricardo had each personally invested close to R$100 thousand to launch the company. They had also received a small amount of seed capital from a business school classmate, turned investment banker. This initial money had mainly been used to kick-start the business. David and Ricardo had hired an engineer to write the code for their website. They had also out-sourced a free-lancer to take care of the website design. A couple of employees were hired as well, to help out with operations and accounting. With this initial equity and the company’s revenue stream, Carrinho em Casa was actually unit profitable. This meant that the amount they made from each single delivery combined with the equity they still had left-over, allowed to cover the costs associated to the service. This also included the salaries of the shoppers in charge of purchasing and delivering the groceries to customers’ doors. Although this allowed David and Ricardo to maintain a decent lifestyle in Sao Paulo, it didn’t leave much room for big expansion projects. With limited financial flexibility, it was often hard for the co-founders to visualize the long-term outlook of their company.

One year after its launch, Carrinho em Casa now had 7 full-time employees. In addition, they contracted nearly 20 personal shoppers and received over 1000 orders per month. Their delivery services were now available in 30 different neighbourhoods of Sao Paulo. They had also managed to secure several partnerships with some of the largest supermarkets in the city including Carrefour, Pao de Azucar and Quitanda, which allowed them to get special discounts on certain products. Although some supermarkets provided their own delivery service, Carrinho em Casa differentiated itself in the sense that clients could order from various places at once, and groceries would systematically be delivered in under 2 hours. In the city of Sao Paulo, David and Ricardo were the only ones to offer both speed and variety of choice when it came to such delivery services.

Still, according to both David and Ricardo, the company hadn’t reached its full potential. They had found a service that worked, yet they needed more customers. The ones who used their service left glowing reviews. What was difficult was acquiring new ones. Was
it due to the economic crisis? Or perhaps due to lack of brand awareness? If Carrinho em Casa were to become the Instacart of Latin America, David and Ricardo would need to find a way to scale their business and fast. Agreeing on the company’s future growth strategy was now the number one priority on their to-do-list.

1.3 Country Background

In 2008, Brazil was considered by investors around the world as the place to be. While developed nations were still suffering the pains of the financial crisis, emerging markets and especially Brazil seemed to be sailing smooth seas. Indeed, numerous social, political and macroeconomic shifts indicated that Brazil was heading in the right direction.

Macroeconomic Stability

In 1994, then Minister of Finance and later president, Fernando Henrique Cardoso, established a set of measures intended to stabilize the Brazilian economy. These measures, known as the “Plano Real” were a direct response to Brazil’s hyperinflation episode of the 80’s to early 90’s. Throughout this period, Brazil’s social situation had been severely aggravated. By 1989, inflation in Brazil had reached over 1,000% per year and 35% of the population was considered poor. The introduction of the Plano Real helped Brazil achieve numerous milestones. These included: balancing the country’s budget, introducing a new currency, the real, fixing the exchange rate, and driving down inflation from 2,500% in 1993 to 16% by 1996.

In the eight years that followed, during both Luis Inacio Lula da Silva mandates, the country was capable of keeping macroeconomic stability on track. Lula’s ministers of finance imposed price stability and attempted to increase fiscal responsibility. These initiatives reassured international investors and by 2008, Brazil reached investment grade status by several rating agencies including Fitch and Standard & Poor’s. As a consequence, foreign direct investment increased substantially, reaching its all-time high of US$20.5bn in December of 2010.

Resumption of Economic Growth

In parallel to the improvement in economic stability, Brazil witnessed a notable resumption of economic growth. From 2005 to 2010, average aggregate GDP year-over-year grew by nearly 5.5%. Deal flow increased significantly during this period due in part to increasingly active foreign investors. Brazil was gaining in popularity around the world, with global media dedicating more and more attention to the country. Announcements of major international events such as the 2014 World Cup and the 2016 Summer Olympics, both expected to take place in Brazil, further boosted media coverage and confidence in the country’s attractiveness. Everyone wanted a piece of the pie and as a result overall foreign direct investment grew annually on average by 18% from 2005 to 2010.
Development of Capital Markets

The development of Brazil’s capital markets was yet another contributor to the country’s economic growth and stability during the early 2000’s. With an expanded menu of available financial instruments, companies were able to obtain new sources of funding to support their growth strategies. The Sao Paulo stock exchange, Bovespa, founded in 1890 as a state-owned company, was initially used mainly to trade commodities such as sugar, cotton, coffee and rubber. Yet, by 2007, the Brazilian stock market had evolved greatly. That year, the exchange demutualized and became a for-profit company. A year later it merged with BM&F, creating the world’s second largest stock exchange at the time. The number of IPO’s soared as well, totalling over 100 between 2004 and 2007. As a matter of fact, in 2007, only the United States and China recorded a larger number of IPO’s. By 2015 however, Brazil’s IPO market was close to null. The insurance broker, PAR, was the only company to go public that year, raising R$603m, less than 1% of the total amount raised during the 2007 peak-period.

Improved Income Distribution and Poverty Reduction

Another growth driver was the significant expansion of Brazil’s middle class accompanied by an increase in the population’s purchasing power. These factors were related to unique external and macroeconomic conditions during the period as well as the redistributive policies set in stone by Lula. One of the major programs introduced was Bolsa Familia. This program was created with the intent to have a dual social effect. First, to reduce short-term poverty through direct cash transfers and second, to fight long-term poverty by providing conditional transfers. These conditions required families to commit to keeping their children in school and ensure that they received regular medical visits and vaccinations. As a consequence of such programs, Brazil witnessed a strong increase in the size of its middle class. Whereas it only represented 38% of the population in 2003, the country’s middle-class represented nearly 56% of the 200+ million population just 10 years later. At the same time, the country’s Gini coefficient, most commonly used to measure inequality, fell from 0.6 to 0.53, reflecting the improvement in income dispersion.

The combination of all of these factors indeed made Brazil seem like the place to be. Local and foreign investors alike sought to take advantage of the country’s numerous “gems”: massive oil discoveries, rising agricultural exports and an up-and-coming consumer base, the second-largest in the Americas. There was a general feeling of excitement and possibility in the air. In 2012, Henrique Alhante, Partner at JGP, a Brazilian asset management firm, enthusiastically stated: “This is a whole new story. Consumption has structurally shifted up. What gets us excited is the local domestic consumer market”. Unfortunately, this sentiment would be short-lived. Brazil’s smooth waters were becoming increasingly choppy.

On September 9th, 2015, an alarming headline could be read on the Wall Street Journal’s front page: “S&P Cuts Brazil’s Debt Rating to Junk”. The article highlighted the
sharp contraction of the economy, the 13-year low currency, the government’s deficit and the increase in political friction as decisive factors leading to the downgrade. Just 5 months later, in February 2016, S&P further cut Brazil’s debt rating into junk territory. The country’s BB rating, two steps below investment grade, put it on par with countries including Bolivia, Paraguay and Guatemala. In its official statement, S&P claimed: “The political and economic challenges Brazil faces remain considerable. We now expect a more prolonged adjustment process with slower correction in fiscal policy, as well as another year of steep economic contraction. Despite government plans to table structural reform, such as on pensions, we expect the political environment after the conclusion of the impeachment process to also limit the viability of reforms – regardless of who is president”.

The passage from glory to dust surprised many. Former president of Brazil’s central bank, Henrique Meirelles, argued that the country’s decline was closely related to changes in economic policy. In a 2015 Financial Times article, Meirelles was cited saying that: “In 2010, Brazil applied a “new economic matrix” that involved artificially reducing interest rates. Interventionism, coupled with policies that incentivised demand and consumption but neglected the supply side, reduced investment, increased inflation and created fiscal fragility, generated much uncertainty”. By early 2016, the once resilient Brazil did indeed seem to be sinking, and fast. The country found itself in the midst of its worst recession in more than a century. Furthermore, with improving economic conditions in developing economies, investors were becoming less willing to tolerate risky, high return investments. Brazil and many other emerging markets’ economic prospects were darkening due to significant capital flights. Charles Collyns, chief economist of the Institute of International Finance, stated in October 2015 that: “Flows to Emerging Markets have weakened sharply in volatile market conditions and a jump in risk aversion. We now project overall negative flows for the first time since the emerging markets concept was first devised in the late 1980’s”.

Capital outflows were not the only thing concerning Brazil however. China, the country’s largest trade partner, was dealing with a slowdown of its own and the ripple effects on Brazil were proving to be quite harsh. Certain economists claimed that Brazil had fallen under the “resource curse”, a theory describing how countries with abundant natural resources sometimes perform worse than countries without them. In 2000, Brazil’s annual trade with China was around US$2 billion. In 2013, this number had soared to US$83 billion. China’s growth had boosted commodity prices, yet as the country’s economic growth began to slow, Brazil suffered a range of economic setbacks, including a weaker currency, a tumble in stock prices and an increase in government debt.

Yet Brazil’s challenges did not limit themselves to external factors. What made this crisis perhaps deeper than previous ones was that most of the problems were home-grown. Alexander Schwartsman, a former Brazilian central-bank official claimed: “We managed to produce this recession ourselves”. By 2014, the government, anticipating commodity sales, was spending increasingly heavily and banks were supplying Brazilians with easy credit. The country’s national development bank, BNDES lent so much that its loan portfolio became larger than the World Bank’s. Oil production also ended up being a lot lower than expected.
Petrobras, the state-run Brazilian oil company, was struggling to develop oil fields in difficultly exploitable environments. To top things off, the energy-giant was engulfed in a major corruption scandal involving some of the government’s most senior politicians, including the president herself, Dilma Rousseff. Some even theorized that Brazil’s strong dependence on China and the commodity boom had turbocharged some of the country’s unhealthy practices. A former emerging markets investment banker argued that due to the commodities’ support of the economy, “Brazilian leaders were able to put off addressing certain problems that had long bedevilled the nation, such as corruption. Brazil became complacent because of the intoxicating effects of China trade, but was now suffering a hangover”. The Brazil mania had effectively turned into Brazil nausea.

**Brazil’s tech, venture capital and start-up ecosystem: finding opportunity amid turmoil**

Not everyone was ready to cut the party short however. For some, the post-carnaval was just beginning. While the overall Brazilian economy had shrunk nearly 4% in 2015 alone, certain industries such as tech were fairing quite well and private equity and venture capital investments in the region were reaching some of their highest levels yet.

**1.4 Growing Tech Industry:**

Local and international newspapers were quick to stress Brazil’s many challenges. Through the media’s lens, everyday seemed like a possible tipping point. Yet, looking beyond the headlines, one could see that certain sectors were actually outperforming others, and by a lot. Tech was one of them. In late 2015 the renown private equity association, Privcap, hosted a conference focused solely on Brazil and its existing opportunities. Guest speaker Anderson Thees, partner at the Sao Paulo based venture capital firm Redpoint e.Ventures, stated that the Brazilian tech industry had grown 20% in 2015 alone. The rapid increase in connectivity amongst Brazilians was a clear contributor to this remarkable growth. Hernan Kazah, partner at the Argentina-based VC firm KaszeK Ventures, agreed that Brazil’s tech sector was indeed promising: “Looking beyond the ‘crisis’, the adoption of smartphones keeps growing, ‘consumer internet’ keeps going, and companies are incorporating more technology to lower costs, seek cost efficiencies or provide a better service.” According to LAVCA, the Latin American Private Equity & Venture Capital Association: “Only half of Brazil’s population of 200 million is online, but it’s already the fifth largest internet and mobile economy in the world, a top three market for Facebook, Google, and Twitter, and the most socially active population on the planet. WhatsApp is the most used app in Brazil, with 93 million users. To top things off, Brazilians out-perform the world in terms of mobile penetration and have the highest SIM-to-subscriber ratio in the world, with over 240 million SIM connections and 283 million mobile phone lines”.

**1.5 Burgeoning Start-up Ecosystem:**

Brazil, alongside Chile, was also considered one of the most active Latin American
countries in terms of entrepreneurship. Despite the government’s efforts to curb overall spending, the start-up ecosystem had been barely affected. It actually seemed to be receiving more attention than ever before. Many initiatives and accelerators were put into place to boost entrepreneurialism throughout the country. In September 2015, Cubo, a tech hub for start-up entrepreneurs in Sao Paulo, was launched. 2015 was also a year of numerous start-up success stories in Brazil. A handful of companies received first round or add-on funding from international and local sources. iFood, the leading Brazilian online take-out service, was even searching to expand its business outside its own borders. In March 2016, it acquired US-based, Spoon-Rocket, adding to the company’s 15 recent acquisitions. Commenting on iFood’s flourishing M&A activity, LAVCA stated: “iFood’s acquisition streak is an example of the apparent dislocation between Brazil’s political and economic crisis and a relatively thriving tech sector which grew 20% from 2014 to 2015 while GDP was flat”. The country’s poor economic performance did not seem to be hampering the amplification of Brazil’s start-up scene. Anderson Thees insisted on this idea by stating in an interview with Privcap that: “if the crisis remains for too long, it could indeed affect us, but for right now what we notice is a detachment between what is happening in the start-up ecosystem and the macro-economy.”

However, the most successful start-ups did seem to have something in common. They all addressed, in one way or another, a uniquely Brazilian inefficiency. For mobile credit card start-up, Nubank and online lending platform, Bank Facil, it was the country’s high interest rates. Sergio Furio, founder and CEO of Bank Facil, argued that his company had benefited from the economic downturn by helping Brazilians save up to 70% on loan payments. He added that: “Brazilians pay 10 to 20 times more interest on debt than American consumers. At Bank Facil, we’re using technology to create efficiencies in processes that are extremely inefficient”. On-demand shipping platform Mandae, was also on the list of start-ups to receive funding in 2015, obtaining a Series A investment from Valor Capital and Sao Paulo firm Monashees. Mandae CEO Marcelo Fujimoto claimed that the economic downturn had not rendered his search for funding more difficult: “Mandae operates in a very large market and we also solve a very real, very big pain point shared by millions of people. As a result, we are showing very rapid growth – 30% month over month. For our Series A round, we received a lot of investor interest, both national and international, and were thus in a position to be selective”. Fujimoto further accentuated the successful development of Brazil’s start-up ecosystem by stating: “There are amazing, big things, happening behind the scenes in Brazil. While foreign perception of the potential here was perhaps too optimistic in 2010, it’s now swung way too far to the negative, which isn’t accurate either”.

Yet, there was one challenge hindering Brazil’s start-up ecosystem. This was the lack of ease in launching a business in the country. Brazil was often considered one of the more complicated places to start a company due to its significant “red tape”, which included important taxes and high labour costs. According to the OECD, starting a business in Brazil in 2015 required 12 procedures and took 83 days, whereas in neighbouring countries such as Chile, Colombia and Mexico, fewer procedures were required and often took less than 11 days. With this result, the OECD ranked Brazil 167 out of 185 economies surveyed for
starting a business. The government was attempting to reduce the administrative burdens however. In mid-2015, a pilot reform project, started in the capital district of Brasilia, was launched and allowed companies to be registered in less than an hour. The initiative gave “low-risk activity” start-ups the right to begin operations while awaiting their formal license. The government was excepting to later rollout these simplified rules on a nationwide scale.

1.6 Growing VC industry:

In parallel to the country’s growing tech industry and burgeoning start-up ecosystem was the emergence of an increasingly active set of venture capital investors. At first glance, it seemed as if VC investors would be turned away by Brazil’s obstacles. They indeed could have many reasons for concern. These included the country’s significant macroeconomic challenges, expected to persist in the coming years, with low growth and high inflation. Brazilian capital markets were also essentially frozen. This made for an absence of long-term affordable leverage and limited exit opportunities, as IPO activity had become minimal to null.

Yet according to LAVCA, even in the context of Brazil’s economic downturn, “venture capital investors deployed record levels of capital in Latin America in 2015, with SUS$594 million invested across 182 deals”. In describing Brazil’s VC scene, Anderson Thees, partner at Redpoint e.Ventures, argued that: “It is really a new world. Brazil’s VC scene is growing extremely fast compared to five or seven years ago. We have a completely new breed of providers, so lawyers and accountants are getting specialized on the Internet start-up scene. The terms and the way we do investments is very new. We also have a new wave of support agents in the industry such as accelerators and incubators. There is a new generation that is more aligned with what we see in Silicon Valley, and activity in general is greater”.

For PE and VC investors the crisis did not necessarily translate into an absence of opportunity. When macroeconomic conditions were at their peak, valuations were sometimes considered a limiting factor. Yet with the sharp depreciation of the real, certain target companies were becoming more attractive in US dollar terms. In September 2015, Cate Ambrose, president and executive director of LAVCA stated: “If you raised funds in US dollars, now would be a very attractive time to buy. The 50% decline in the real over the past 4 years has made the nation more competitive as an investment destination”. And Brazil, considering its size, still remained the largest Latin American market due to its rising middle class and favourable demographics. Many agreed that the country was just “too big to ignore”. Furthermore, with traditional sources of lending becoming more expensive, PE and VC were turning into the go-to option for business owners seeking financing. In an interview with Privcap, Eduardo Alcalay of Brazilian Private Equity firm GP Investimentos commented: “Although it may sound counterintuitive, you can still find fast growing companies in Brazil despite the macroeconomic conditions. Brazil is a relatively young economy compared to the US or Europe. There are many new business segments like consumer financial services, education, healthcare, technology and infrastructure, that
regardless of an overall negative environment, are growing because they have a big market to support. They have a big demand to supply. And yes, you find some great champion companies that have growth capabilities ahead of them. They need capital. There is no public capital out there. And with interest rates reaching 14+%, debt is just too expensive. Credit capital is scarce and these companies need strong managerial support, so that is where PE and VC’s come in”

In 2015, the predominant sector for VC activity in the region was by far information technology with 126 transactions and $US500 million in invested capital. The dominant players were Kaszek Ventures, e.Bricks, Redpoint e.ventures, Monashees Capital and Bozano Investmentinos, a fund partnering with the Brazilian development bank, BNDES. These firms were investing greatly in fintech and e-commerce companies. They also seemed to be convinced by start-ups addressing the uniquely Brazilian economic inefficiencies mentioned above. In early 2015, Buenos Aires based VC, Kaszek Ventures, announced a series A round in Contabilizei, a Brazilian accounting services platform for small business and freelancers, intended to help them navigate “one of the most bureaucratic tax codes on the planet”. According to TechCrunch, Contabilizei grew 350% in 2015 alone.

Funding in 2015 did seem to have a different tone to it though. Not only were VC’s investing in companies that tackled economic inefficiencies, they were also deploying larger amounts of capital upfront. VC’s were looking for the golden-token, and if they believed to have found it, they were clearly unafraid to write some of the largest checks ever witnessed in the region. Of the $US594 million VC dollars invested in 2015, nearly 30% went to four companies alone. Mobile-based credit card start-up Nubank was by far the winner, raising a total of $US80 million, including a US$30 million series B round from Sequoia Capital, Tiger Global, Kaszek Ventures and QED Investors, and a US$50 million series C from Peter Thiel’s Founders Fund and previous backers Sequoia Capital, Kaszek Ventures and Tiger Global. The three other companies to top the list of VC deals by amount each received US$30 million. These included Brazilian digital security company PSafe, Brazilian beauty platform BelezaNaWeb, and Argentinean e-commerce start-up Avendia!. These major deals were all led, in part, by foreign investors. 2015 therefore marked the resurgence in Latin America of certain prominent US-based VC firms. With its investment in Nubank, Sequoia re-entered Latin America for the first time after having existed the country in 2013. Founders Fund’s, Tiger Global and Qualcomm Ventures were also taking a second shot at the region in hopes to find Latin America’s hidden gem.

The majority of these larger investments continued to be geared towards Brazil. Despite the major impact on capital markets of Brazil’s negative growth and numerous corruption scandals, LAVCA ranked Brazil 2nd, right behind Chile, in its bi-annual Scorecard on the Private Equity and Venture Capital Environment in Latin America. The Scorecard measures the regulatory landscape for PE and VC investments across 14 countries and takes into account numerous criteria such as: level of entrepreneurship, corporate governance requirements and capital market development. In commenting on Brazil’s top-3 ranking, LAVCA stated: “the regulatory framework for fund formation, the ongoing revision of PE
and VC regulation by CVM, and the quality of accounting standards are among the country’s major strengths, though Brazil scores strongly on most indicators”.

1.7 Growth Strategy Decision:

David and Ricardo sometimes felt like they had dodged a bullet. Although the country was indeed facing one of its most difficult economic crises yet, they had managed to step into a niche ecosystem that was actually growing. Due to the country’s increasing interest for tech, and thanks to numerous government initiatives, the co-founders had been able to accelerate the launch of Carrinho em Casa. Yet, at the end of the day, even if the tech industry and startup and venture capital ecosystems were blooming, what mattered most was the customer. And with shrinking GDP and rising unemployment, consumer confidence was at an all-time low.

David and Ricardo were well aware of these challenges, yet they truly believed their company had great potential and were determined to find a way to take it to the next level. However, they didn’t necessarily share the same views when it came to deciding which growth strategy would be most appropriate. On the one hand, David was advocating the need for external capital, arguing that obtaining VC-backed funding would provide Carrinho em Casa with the boost it desperately needed. On the other hand, co-founder Ricardo strongly believed bootstrapping was the wiser solution. He insisted that Carrinho em Casa should continue to grow organically through its already unit-profitable business, and as a consequence maintain total ownership of the company.

Carnaval season was coming to an end, and business in the city of Sao Paulo was slowly starting to pick-up again. As David and Ricardo returned from their respective vacations, they decided it was time to sit down and discuss the pros and cons of each growth strategy. David grabbed his favorite marker off of the meeting table and drew a long vertical line across the white board. At the top of the board he wrote in large capital letters: 

EXTERNAL FUNDING vs. BOOTSTRAPPING.

External Funding Rationale:

David took the lead and began jotting down bullet points in favor of a VC-backed growth strategy. He argued that obtaining a round of funding would allow Carrinho em Casa to accelerate growth by providing the company with greater financial flexibility. He added that, with the newly received capital, they would be able to hire additional dedicated staff members. Up until then, the few people Carrinho em Casa did employ had very general roles, mainly because they actually did do a bit of everything. David exclaimed: “The VC dollars would allow us to finally hire a marketing director or partnerships manager for example. That would take some work off our plate! And we could then spend more time actually focusing on bigger picture issues”.

David also argued that they could use the newly received capital to launch a major marketing campaign. Indeed, Carrinho em Casa had done minimal marketing efforts, mostly
due to its strict financial constraints. The company relied greatly on word-of-mouth and its online presence via its Instagram and Facebook accounts. David believed that a large marketing campaign could be beneficial on two levels. First, it could attract a greater amount of new customers, previously unfamiliar with Carrinho em Casa’s service. Second, it could also attract potential “shoppers”, those in charge of delivering groceries to customers’ homes.

Furthermore, David truly believed that entering into a partnership with a VC fund would open Carrinho em Casa’s doors to a larger network and give way for greater business opportunities. Citing Steve Blank, one of his favorite serial-entrepreneurs and Silicon Valley venture capitalists, David stated: “The investor’s experience, pattern recognition and contacts can bring a lot to the table.” He added: “I’m sure they could help us expand into new markets and put us in touch with possible buyers later on! And with all that extra capital we could become the definite leaders of the Brazilian grocery delivery market, just like Instacart in the US”.

Ricardo had his doubts however. First of all, he wasn’t even sure Carrinho em Casa would be able to convince VC’s to invest in their company. He quickly cut David off and said: “Remember Guy Kawasaki’s wise words: the probability of an entrepreneur getting venture capital is the same as getting struck by lightning while standing at the bottom of a swimming pool on a sunny day. What makes you think we’ll be the lucky ones?”

Although the start-up ecosystem and VC industry were performing well in Brazil, Ricardo was still quite worried about the economic crisis: “I’m not sure VC’s will be convinced by the sustainability of our business model in these difficult times. They will argue that consumers are being prudent nowadays and won’t be willing to pay our R$9.90 fee for a delivery service when they can save that money by shopping for their groceries themselves. And I’m positive they’ll pull out the consumer confidence index to remind us that it’s at its all-time low!”

Ricardo’s biggest concern however was related to equity dilution. He knew that having a VC on board would reduce his overall ownership of the company. He strongly believed that this could have several adverse consequences that needed to be carefully considered. First of all, he worried management and employee incentives would diminish. Knowing his potential return post-exit would be lower, Ricardo felt that he, and others would perhaps be less committed to creating the best business possible. Second, he feared David and himself would have less flexibility in terms of running their business the way they seemed best-fit. The VC involved would most likely want to have a say in how the business operates and could even request management cuts or changes. He added: “You know what they say, the day you raise money from a venture investor, you’ve also just agreed to their business model. I’m not sure how much decision power I am willing to concede to external hands”.

Finally, Ricardo brought up the time factor. It was well known in the start-up community that pitching VC’s was a full-time job in itself. Reaching out to different funds, preparing presentations, and scheduling meetings was extremely time consuming and David
and Ricardo already had an enormous amount of work on their plates. “We should be spending that time focusing on acquiring new customers and landing partnerships with supermarkets”, he claimed.

**Rationale for Bootstrapping:**

It was now Ricardo’s turn to take the lead and try to make the case for bootstrapping. From his point of view, growing organically and funding development through internal cash flows, was the wiser solution. David tossed him the marker from across the room, and Ricardo began jotting down his main arguments.

He started by stating that Carrinho em Casa already had a business model that sustained the concept of bootstrapping. Up until now, David and Ricardo had mainly used revenues to fund their early stage development. Considering they were unit profitable, bootstrapping was a viable, low-cost option that Ricardo felt would allow them to focus more time on customers rather than investors. He had just read a blog post by Laurence McCahill, co-founder at the Happy Startup School, in which the concept of “Minimal Lovable Product” was discussed. Ricardo argued: “We need to use our time finding more recurring customers that will pay for our service. Scale is what’s missing here. And as stated by McCahill, a ‘Minimal Lovable Product’ isn’t just about creating a great product or service, but a passionate user base that loves us and will become an advocate for our business.”

Ricardo also believed that sticking to bootstrapping would give them more time to establish greater tangible evidence of the success of their business model: “I’m convinced that investment will come a lot easier if we truly focus now on increasing our customer base and lowering churn rates”. He added that, perhaps having a stronger, proven business model, would allow them to secure a better deal, negotiate further, or receive more attractive valuations from investors later on.

Finally, Ricardo brought up the idea of financial discipline. He felt that they had successfully been able to manage their finances up until now, and was afraid securing a round of funding could derail their solid track record. He mentioned one of his friends back in Portugal, also an entrepreneur, whose start-up had received a first round of VC funding. “I remember how overwhelmed they were by the whole thing. They completely mismanaged their funds and burned through the cash without actually leading the company to sustainable growth”. Reflecting on Carrinho em Casa, he added: “Having limited financial flexibility would at least allow us to truly focus on developing the most vital elements of our company”. He reached for his desk and pulled out an article on Bootstrapping written by Harvard Business School professor Amar Bhide. It read: “Successful bootstrappers take special care to expand only at the rate they can afford and control. They tend to invest in people or capacity only when there is no alternative, not in advance of needs. Keeping growth in check is not only financially prudent but it also helps the entrepreneur develop management skills and iron out problems under less pressure. Even entrepreneurs who don’t have to make radical changes in strategy may have to make adjustments as they learn about the nuances of
their chosen industry. Learning the nuts and bolts of running a business is particularly important for first-time entrepreneurs”.

While Ricardo spoke, David was already brainstorming a list of counterarguments in his head. In his opinion, maintaining a bootstrapping strategy inevitably meant limiting growth to the viable minimum. He knew Carrinho em Casa wouldn’t be as quick at expanding and tuning profits if its growth strategy was solely based on retained earnings. This wasn’t the version of Carrinho em Casa he had initially imagined. In David’s mind, Carrinho em Casa had the potential to become a success story just like Instacart. He had envisioned not only disrupting the grocery delivery market in Sao Paulo, but also in Rio, Buenos Aires, Santiago, Bogota and why not all of Latin America. Reaching that vision via bootstrapping seemed far-fetched. David wanted to hop on the speedboat. His arms were already getting soar from all of the rowing they had done up until now.
Part 2: Appendix to the Case

Appendix A: Brazil’s Macro Uncertainty Creates VC Opportunities

Brazil’s Macro Uncertainty Creates VC Opportunities

October 7, 2015

Brazil’s economic and political woes are creating some opportunities for venture capital investors, according to panelists at a conference last week. Private equity, particularly buyout fund, returns are somewhat correlated to economic cycles, while VC operates relatively independently of the economy, Scott Voss, managing director at HarbourVest Partners, said on a panel at the LAVCA Venture Investors New York Summit last week.

“Venture capital returns are correlated to innovation cycles,” Voss said. “Arguably if you are a startup and you are looking to disrupt an industry, the best time to do it is when the incumbents are weak. There is an opportunity if you are focused on startups and innovation, regardless of what part of the economic cycle it is.”

The weaker Brazilian currency means U.S. dollar investors are “getting a lot of value”, whichever stage of venture capital they are investing in, he said. Investors in Monashees Capital’s latest fund asked few questions about the macroeconomic conditions, according to Eric Acher, the firm’s managing partner.

He expects the firm will, in a few years, reap the rewards of investments made today. “The really true, long-term venture capital investors, they believe that this is a phase of the cycle,” he said. “The new investors that we were able to attract to this new fund, we heard from them ‘it’s not about macro, it’s about investing in the globalization and applied technology . . . in which Brazil [is a] hub, it’s about trying to be with the leading and dominant VCs.”

Source: http://lavca.org/news-item/brazils-macro-uncertainty-creates-vc-opportunities/
Appendix B: ‘Smart Money’ VC’s Continue to Back Food Delivery Startups

'Smart Money' VC’s Continue to Back Food Delivery Startups

Jun 9, 2016

Many venture investors agree that there too many founders launched food delivery startups when funding was flowing freely into such businesses over the past few years.

But that doesn't mean the money spigot has been turned off, according to a report this week from CB Insights.

The investment research firm follows where "smart money" VCs — the top 24 firms ranked according to portfolio valuations and investment success — put their money and found they are continuing to back some of their favorite food fetchers.

"Collectively, the top two-dozen VCs participated in 5 food delivery deals worth over $330 million in Q1’16, up from just 2 deals in Q4’15," the report said. "The rounds they participated in represented over $300 million ... a quarterly record for deals with smart money backing."

Of course, when the VC darling of food delivery — San Francisco-based DoorDash — raised a big $127 million round in March it did so in what's known as a "down round." That means it sold its private shares at a lower price than in a previous round. It's a Y Combinator company that has raised about $187 million from "smart money" investors such as Sequoia Capital, Kleiner Perkins Caufield & Byers, Khosla Ventures and CRV (Charles River Ventures).

Another food delivery startup with four "smart money" investors is San Francisco organic food delivery startup Sprig. Its top investors include Accel Partners, Battery Ventures, Greylock Partners and Social Capital.

The two "smart money" firms with the food delivery startups in their portfolios, according to CB Insights, are Accel with seven and Andreessen Horowitz with five. In addition to Sprig, Accel backed London-based Deliveroo, Latin America-based Cornershop, San Mateo-based Din, Chicago-based Abe's Market and India-based Teabox and Swiggy.

Andreessen Horowitz put its food delivery bets on San Francisco-based grocery delivery startup Instacart, Palo Alto-based Gobble, San Francisco-based private chef service Kitchit (which shut down in April), Kansas-based organic meat deliverer AgLocal and San Francisco-based Caviar.

Appendix C: Tech in Brazil is Booming Despite the Country’s Political Troubles

Tech in Brazil is Booming Despite the Country’s Political Troubles

May 25, 2016

It was a balmy night in Rio de Janeiro and a pretty J.P. Morgan Private Wealth representative was buying drinks for newly paper-rich entrepreneurs. Nearby at the pool of the city’s only Relais et Chateaux property mingled investors who had flown in from New York, San Francisco, London and Berlin.

The next morning the Hotel Santa Teresa’s projector beamed countless up-and-to-the-right charts as entrepreneurs presented their well-funded ideas to the participants of Founders Forum Brazil 2012.

Few of those companies still exist today.

The hype of that era is long gone, overwhelmed by a political and economic crisis that regularly fills the front pages of global newspapers. However, unfazed by the high-profile failures of many foreign-backed startups, technology in Brazil continued its forward march. While Brazil’s overall GDP fell 4 percent in 2015, the tech industry has been largely immune to the slowdown, growing 20 percent from 2014-2015.

Contrary to conventional wisdom, venture investments in Latin America have also consistently grown from those heady days, reaching US$594 million in 2015, up from US$387 million in 2012, according to the Latin America Venture Capital Association. Surprisingly, recession-racked Brazil consumed 63 percent of the region’s total investment, with the city of Sao Paulo receiving the lion’s share of VC dollars.

The reality is that the recession and political crisis created a clear divergence of fortunes among Brazil’s technology companies. Many of the companies that presented at Founders Forum Brazil 2012 were plays on the emergence of Brazil’s middle class. The entrepreneurs and investors were wagering that these newly empowered consumers would snap up furniture, shoes and baby supplies at record rates. Unfortunately, an economy fueled by ever-looser credit and constantly increasing government spending could not last.

As in most countries, recessions lead to belt-tightening among companies and consumers. Just as expected, the technology companies that thrived are those that offer consumers and businesses a way to improve efficiency and sustainably reduce their costs. Examples include small business SaaS ERPs like Conta Azul and Omie, consumer productivity apps like Gympass and GuiaBolso, and companies that facilitate B2B transactions like Intelipost and Loggi.

The relative unconcern about the recession among Brazilian technology entrepreneurs was evident last week at the award gala hosted by Latam Founders Network, a group made up of
founders, executives and investors from across the region. Camera crews from all of Brazil’s major television stations were there to cover what Brazil’s leading business magazine, EXAME, dubbed the “Oscar for Startups.” Companies competed in eight categories, including B2C, Best Investor, and Most Innovative. (Full disclosure: My company, Gaveteiro.com.br, was nominated in the B2B category). Past winners have included Printi, Nubank and iFood, all of which went on to raise large rounds.

Taking home the prizes were companies that fit the trend of efficiency-driving technology. Contabilizei, SaaS accounting software, won in the B2B category. Dr. Consulta, a chain of low-cost, technology-enabled health clinics serving poor areas, won Most Impactful. Finally, Pipefy, a SaaS workflow tool with global ambitions, won Most Innovative. Entrepreneur of the Year went to Bruno Pierobon, CEO of Zup, a company focused on helping companies deal with all the complexities of systems integration and outsourcing services.

Investors, too, have recognized this trend. Kaszek Ventures, one of the region’s largest funds, has invested heavily in B2B and consumer finance (credit card interest rates in Brazil can pass 200 percent a year). Eight of their last 10 investments listed in CrunchBase have been in these two categories. Ditto for Redpoint Ventures, another large fund focused on Brazil that took home this years’ Investor of the Year award.

No one knows the final outcome of Brazil’s political crisis — until now it has been an unpredictable cross of Gabriel Garcia Marquez’s surrealism and Netflix’s House of Cards. What we do know, however, is that efficiency-driving innovation will have its place, come whatever market environment. Those entrepreneurs and investors who can thrive in a tough macroeconomic scenario are surely well-positioned for long-term success in the world’s seventh-largest economy.

Source: https://techcrunch.com/2016/05/25/tech-in-brazil-is-booming-despite-the-countrys-political-troubles/
Exhibit 1: Carrinho em Casa’s Facebook Page

Source: Facebook.com/carrinhoemcasa

Exhibit 2: Carrinho em Casa’s Instagram Account

Source: Instagram.com/carrinhoemcasa
Exhibit 3: Carrinho em Casa Website

Source: carrinhoemcasa.com.br

Translation: *Your supermarket order delivered in under 2 hours*
Exhibit 4: Empreendedores Criam Negocio Que Faz o Supermercado Por Voce

São Paulo – Você provavelmente é ou conhece alguém tão ocupado que nunca tem tempo para ir ao supermercado. Ou alguém que adoraria receber itens recorrentes em casa, como fraldas para os filhos, sem ir comprar toda semana. Ou, ainda, um idoso que tem dificuldades em se locomover – inclusive para o mercado. Esses clientes são justamente os que procuram a Carrinho em Casa, startup que registra pedidos online de compras e entrega em até duas horas na porta de casa. O serviço deu tão certo que a expectativa é faturar quatro milhões de reais em 2016.

Source: http://exame.abril.com.br/pme/noticias/empreendedores-criam-negocio-que-faz-o-supermercado-por-voce

Translation: Entrepreneurs Create a Business That Shops For You – Ricardo Prelhaz and David Russell: Entrepreneurs that were able to bring a US established business model to Brazil
Exhibit 5: StartUp Brasil – Brazil’s National Startup Acceleration Program

What Start-Up Brasil offers?

Start-Up Brasil aims at boosting the acceleration of tech startups, bringing new and innovative products and services into the local and international market, and at connecting our companies with global trends and markets. Through a partnership between Government and private sector, the program intends on contributing to generate an ecosystem favorable to tech based entrepreneurship.

Complimentary to the activity of accelerators in this process, Start-Up Brasil also offers:

- **ACCELERATORS**
  - Access to the best accelerators in Brazil.

- **ACCESS TO R&D&I GRANTS**
  - Up to 500 mil Reais in Research, Development and Innovation grants for professionals indicated by the startup.

- **12 MONTH VISA**
  - A 12 month research visa for foreign professionals.

- **INTERNATIONAL HUB SPACE**
  - Co-working space in the Silicon Valley for startups supported by Start-Up Brasil.

- **DEMO DAYS**
  - Events for presenting the startups to investors to be held in Brazil and abroad.

- **EVENTS AND NETWORKING**
  - Events for education, networking and mentorship.

Source: http://startupbrasil.org.br/sobre_programa/?lang=en
Exhibit 6: Latin American Private Equity & Venture Capital Association Country Scorecard

Source: http://lavca.org/2015/07/14/20152016-scorecard/
Exhibit 7: Conversion of Business Opportunities Into Investments in Brazil

Source: Gvcepe Database – Getulio Vargas Foundation

Exhibit 8: SWOT Analysis of the PE/VC Industry in Brazil

<table>
<thead>
<tr>
<th>Positive Aspects</th>
<th>Negative Aspects</th>
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<tr>
<td>Government Support for SMEs Increase in the number of companies listed on the stock market Development of an environment conducive to PE/VC activity Demographic Bouns</td>
<td>High perception of corruption Slow and cumbersome process for registering patents and intellectual property High taxation</td>
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<tr>
<td>Legislation favorable to PE/VC Convenient regulations for institutional investors Strong Entrepreneurship</td>
<td>Corruption in the public sector with few sanctions against those involved</td>
</tr>
</tbody>
</table>

Source: Gvcepe Database – Getulio Vargas Foundation

Exhibit 9: MIT Brazil Venture Capital Study – Business Model Focus

Business model focus

- Investors are moving up a maturity curve in terms of business model focus:
  1. Fast follow – directly applying a proven business model / technology platform from another geography to the Brazilian market
  2. Localized business model arbitrage – applying proven business models customized to address local frictions and cultural norms that serve as barriers to entry
  3. Uniquely Brazilian models – solving problems unique to the Brazil / LATAM context, often in categories overlooked in the U.S market (e.g., education, financial services)
  4. Innovation for global export – IP-driven innovation associated with Brazilian industrial strengths, e.g. food-business and energy, presently primarily funded by government (e.g. Cidade program)¹

- Current concentration of investment in Type 2, but general belief that as investors become more comfortable with Brazil, they will be willing to take more business model risk, shifting investment focus up the curve

Source: https://mitbrazilventurecapitalstudy.files.wordpress.com/2013/03/mit-brazil-vc-study-2012-2013.pdf
**Exhibit 10:** Latin American GDP Growth, 2010-2015

![GDP Growth Chart](image)

Source: Ernst & Young, Private Equity Roundup Latin America, 2015

**Exhibit 11:** Actual and Expected GDP Growth by Country, 2014-2017

![GDP Growth by Country Chart](image)

Source: Ernst & Young, Private Equity Roundup Latin America, 2015
Exhibit 12: Market Attractiveness Rankings, Greatest Shift 2010-2014 (1 = Most Attractive)

Source: INSEAD – PwC, Study on Private Equity in Brazil, 2014
Exhibit 13: GDP Per Capita X Income Inequality (GINI Index)

![GDP Per Capita X Income Inequality (GINI Index)]

Source: Apex Brasil, The Competitiveness of the Brazilian Venture Capital and Private Equity Industry, 2014

Exhibit 14: E-Commerce Sales (Billions R$)

![E-Commerce Sales (Billions R$)]

Source: Apex Brasil, The Competitiveness of the Brazilian Venture Capital and Private Equity Industry, 2014

Exhibit 15: Emerging Consumer Class (% of Population, By Social Class)

![Emerging Consumer Class (% of Population, By Social Class)]

Source: Apex Brasil, The Competitiveness of the Brazilian Venture Capital and Private Equity Industry, 2014
**Exhibit 16:** Top Latin American VC Capital Centers, 2011-2015

- **Santiago**, $171,700,000
- **Belo Horizonte**, $179,500,000
- **Rio de Janeiro**, $145,613,360
- **São Paulo**, $747,172,710
- **Bogotá**, $55,000,000
- **Buenos Aires**, $256,000,000
- **Monterrey**, $160,000,000
- **Mexico City**, $196,352,012

**Source:** LAVCA – Latin America Venture Capital: Five-Year Trends

**Exhibit 17:** 2011 - 2015 VC Fundraising, Investments & Exits

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
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<td>6</td>
<td>20</td>
<td>18</td>
<td>7</td>
<td>60</td>
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**Source:** LAVCA – Latin America Venture Capital: Five-Year Trends
### Exhibit 18: 2011 – 2015 VC Investments By Sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>2011</th>
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<th>2014</th>
<th>2015</th>
<th>Total $</th>
<th>Total %</th>
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</thead>
<tbody>
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<td>Agriculture / Livestock / Agribusiness</td>
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<td>$4</td>
<td>$0</td>
<td>$4</td>
<td>$12</td>
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<td>0.90%</td>
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<td>$10</td>
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<tr>
<td>Media &amp; Entertainment</td>
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<td>$4</td>
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<td>Total</td>
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<td>$425</td>
<td>$526</td>
<td>$594</td>
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<td>100%</td>
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</table>

Source: LAVCA – Latin America Venture Capital: Five-Year Trends

### Exhibit 19: 2015 IT Sub-Sector Breakdown, # of Transactions, US$

- **Fintech** (21) $142,955,200
- **e-commerce** (27) $112,657,033
- **Transportation** (3) $45,120,600
- **Other** (33) $43,129,071
- **Digital Security** (4) $36,799,080
- **SaaS** (10) $26,284,449
- **Edtech** (9) $21,153,543
- **Logistics and Distribution** (4) $17,642,500
- **Consumer/Retail** (1) $15,930,257
- **Marketplace** (8) $15,712,508
- **Adtech** (5) $11,659,480
- **Big Data** (1) $10,389,200

Source: LAVCA – Latin America Venture Capital: Five-Year Trends
### Exhibit 21: 2015 Highlighted VC Deals

<table>
<thead>
<tr>
<th>Country</th>
<th>Date</th>
<th>Target Company</th>
<th>Stage</th>
<th>Sector</th>
<th>Lead Investors</th>
<th>Deal Description</th>
<th>Amount (US$m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>Feb-15</td>
<td>Jampp</td>
<td>Early Stage</td>
<td>Adtech</td>
<td>Highland Europe, Endeavor Catalyst, Innova, NXTP Labs</td>
<td>Jampp, a platform for promotions and marketing of mobile apps, raised a US$7m Series A led by Highland Europe, Endeavor Catalyst, Innova and NXTP Labs</td>
<td>US$7</td>
</tr>
<tr>
<td>Argentina</td>
<td>Nov-15</td>
<td>Avenida!</td>
<td>Expansion Stage</td>
<td>e-commerce</td>
<td>Tiger Global, Naspers</td>
<td>E-commerce startup Avenida! raised a US$30m Series C from returning investors Naspers and Tiger Global</td>
<td>US$30</td>
</tr>
<tr>
<td>Brazil</td>
<td>May-15</td>
<td>EduK</td>
<td>Early Stage</td>
<td>Edtech</td>
<td>Accel Partners, Monashees Capital, Felicis Ventures</td>
<td>Edtech startup EduK raised a US$10m Series B from Accel Partners and previous backers Monashees Capital and Felicis Ventures</td>
<td>US$10</td>
</tr>
<tr>
<td>Brazil</td>
<td>Jun-15</td>
<td>Nubank</td>
<td>Early Stage</td>
<td>Fintech</td>
<td>Tiger Global, Sequoia Capital, KaszeK Ventures, QED Investors</td>
<td>Mobile-based credit card startup Nubank received a US$30m Series B round from Tiger Global and existing investors Sequoia Capital, KaszeK Ventures, and QED Investors</td>
<td>US$30</td>
</tr>
<tr>
<td>Brazil</td>
<td>Jun-15</td>
<td>GetNinjas</td>
<td>Expansion Stage</td>
<td>Marketplace</td>
<td>Tiger Global, Monashees Capital, KaszeK Ventures</td>
<td>GetNinjas, an online platform for hiring services, received a US$12.8m round from Tiger Global and existing investors Monashees Capital and KaszeK Ventures</td>
<td>US$12.8</td>
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<tr>
<td>Brazil</td>
<td>Jul-15</td>
<td>PSafe</td>
<td>Expansion Stage</td>
<td>Digital Security</td>
<td>Redpoint e.ventures, Qihoo 360 Technology, Pinnacle Ventures</td>
<td>Digital security company PSafe received a US$30m round from previous investors Redpoint e.ventures, Qihoo 360 Technology, and Pinnacle Ventures</td>
<td>US$30</td>
</tr>
</tbody>
</table>

Source: LAVCA – Latin America Venture Capital: Five-Year Trends
Part 3: Teaching Note

3.1 Synopsis

This case introduces the concept of entrepreneurial funding and tackles the issue of how start-ups can find growth amidst economic downturn. Students follow the development of Carrinho em Casa, an entrepreneurial venture which offers a grocery delivery service to clients in under two hours. Although the company faces little competition and offers a unique service in its marketplace, Carrinho em Casa is having trouble scaling its business due to difficult economic conditions and limited financial flexibility. Nearly a year after its launch, the co-founders of Carrinho em Casa are at a crossroads and remain unsure of how to take their business to the next level. On the one hand, co-founder David is advocating the need for external capital, arguing that obtaining VC-backed funding would provide Carrinho em Casa with the boost it desperately needs. On the other hand, co-founder Ricardo believes bootstrapping is the wiser solution. He insists that Carrinho em Casa should continue to grow organically through its already unit-profitable business, and as a consequence maintain total ownership of the company. The case introduces the concepts of VC funding and bootstrapping and encourages students to explore the opportunities and challenges of these different types of financing. The case allows students to grapple with the strategic and tactical decisions related to funding and pushes them to better understand how such decisions can impact all aspects of the business: sales, profits, management, motivation, incentives and exit opportunities, amongst others. Since the case does not provide financial data on the start-up itself, students should be encouraged to reflect on the numerous challenges and opportunities related to starting an entrepreneurial venture in emerging markets under difficult economic, political and social conditions.

3.2 Teaching Objectives

The case may be used in a corporate finance class during a “Funding”, “Private Equity & Venture Capital” or “Entrepreneurship” module to illustrate the challenges and opportunities related to a company’s different funding options. The case encourages students to think through the strategic realities that each funding option presents for the start-up and offers them the chance to debate and plan-out the consequences of one strategy versus another.

The case may be used in a “Doing Business in Emerging Markets” type course as well, to illustrate the main differences between starting or funding an entrepreneurial venture in a development country versus a developed market. Student discussions should bring to light the challenges related to doing business in environments facing economic crisis and political turmoil. Furthermore, unique aspects of Brazil’s capital markets, PE/VC industry and start-up ecosystem can be discussed.

Finally, the case may be used in an “Entrepreneurship” course, during an “Entrepreneurial Finance” or “Scaling Ventures” module. The case helps bring forth the
challenges start-ups face as they strive to escalate their business past the introductory stage of
development. The case also helps illustrate the struggles faced by founders in evaluating next
steps, possible exit strategies, and whether to dilute ownership or not.

The specific teaching objectives for this case include:

- Introducing the concepts of bootstrapping, VC funding, equity dilution and exit
  opportunities.
- Understanding the implications of each funding strategy and how one strategy versus
  another can affect various factors such as: growth rates, business development, exit
  opportunities and management incentives.
- Evaluating the time and cost-benefit implications each funding decision can
  potentially have on the business’s overall development.
- Exploring ways in which entrepreneurs can convince VC’s to finance their venture
  considering the particular company’s maturity and outlook.
- Understanding the specificities of the PE/VC industry in Brazil and how it differs
  from other more mature markets and evaluating how certain uniquely Brazilian factors
  such as expensive debt and fund concentration can affect a local start-ups’ financing
  decisions.
- Identifying the challenges related to launching a successful venture in an emerging
  market characterized by decreasing GDP, political scandal and corruption.
- Assessing the sustainability of Carrinho em Casa’s current business model considering
  the unique market it operates in, Brazil, and evaluating the implications of copy-
  pasting a foreign, yet already proven, business model to a market with its own culture,
  characteristics and set of specific customer needs.
- Reflecting on the idea of “entrepreneurial tourism” and whether foreign entrepreneurs
  in Brazil are serious about their ventures or using them as a “travel pass”.

3.3 Suggested Assignment Questions

**Q1:** Do you agree with David that obtaining external financing from a Venture
Capital fund is the best way for Carrinho em Casa to find rapid and sustainable growth?

**Q2:** Do you agree with Ricardo that bootstrapping is the wiser growth strategy
considering it would allow the founders to truly focus on improving their business while
maintaining full ownership?

**Q3:** What challenges do entrepreneurs like David and Ricardo face when starting a
venture in an emerging market such as Brazil?

- Why would Carrinho em Casa’s business model be so successful in the United
  States (Instacart) yet have trouble growing and reaching customers in Brazil?
• Rather than copy-pasting Instacart’s business model, which is only present in the United States, should Carrinho em Casa attempt to tailor its offering to make it more “Brazilian”?

• Do you think David and Ricardo are truly serious about their venture, or could their idea to launch a start-up in Brazil be a case of “entrepreneurial tourism”?

3.4 Analysis

There are three main areas of discussion in this case. These include:

• Understanding the risks and benefits associated with different growth strategies and assessing their respective implementation feasibility

• Evaluating to which extent each strategy can successfully take the start-up to its next level of development

• Identifying the main challenges related to building a robust venture in emerging markets and more specifically in Brazil, considering its economic, political and social turmoil

Do you agree with David that obtaining external financing from a Venture Capital fund is the best way for Carrinho em Casa to find rapid and sustainable growth?

On the one hand, co-founder David believes that the best next step for Carrinho em Casa is to secure external funding, ideally from a venture capital fund. David argues that obtaining a larger investment from a VC fund would allow the company to grow at a much faster rate than currently observed by broadening Carrinho em Casa’s scope of possibilities. According to David, these new possibilities would include, but not limit themselves to: hiring additional staff, launching a marketing campaign, increasing partnerships with local supermarkets, expanding to new markets and testing ideas for new revenue streams.

In order to tackle this first question, students should ideally layout the risks and benefits associated with the external funding strategy. While evaluating whether or not Carrinho em Casa should reach out to VC’s for funding, students should make sure to keep in mind the unique specificities of the Brazilian economy, VC/PE industry and entrepreneurship ecosystem. In evaluating this decision, several factors should be taken into consideration.

Rationale for choosing the external / VC funding strategy:

• Obtaining a round of funding would allow Carrinho em Casa to accelerate growth by providing the company with greater financial flexibility. With its newly received capital, Ricardo and David could hire additional dedicated staff members. Up until now, the select few employees at Carrinho em Casa seemed to have very general roles, mainly because everyone actually did do a bit of everything. Having the budget to hire
a person specifically in charge of marketing, or accelerating supermarket partnerships
for example, could help Carrinho em Casa make a substantial leap towards growth. In
addition, it would allow the co-founders to focus on “bigger picture” issues, inciting
them to maintain a longer term vision of the business rather than a day-by-day one.

- Carrinho em Casa could also use the newly received capital to launch a large
marketing campaign. Currently, Carrinho em Casa does very minimal marketing
efforts, relying mainly on word-of-mouth and its online community (Facebook page,
Instagram account). A larger scale marketing campaign would be beneficial on two
levels. First, it could attract a greater amount of new customers, previously unfamiliar
with Carrinho em Casa’s service. Second, it could also attract potential “shoppers”,
those in charge of delivering groceries to customers’ homes. Both are needed if the
business is to grow substantially and a large marketing campaign could have this dual
effect.

- Considering Brazil’s difficult economic situation, having a thicker cushion of capital
could also allow the company to weather the storm in a smoother way. Relying solely
on revenues to maintain the business afloat may prove to be difficult considering
Brazil’s rise in inflation, currency devaluation, decrease in GDP and cautious
consumer spending trends. Indeed, the additional financial security might be just what
Carrinho em Casa needs if it is to keep its business up and running during the current
economic turmoil.

- The additional capital provided by the VC could also support Carrinho em Casa’s
expansion into new markets. For now, the company’s business model has proven to be
sustainable and repeatable. In addition, with its fixed R$9.90 delivery price, the
company is unit profitable. What seems to be missing is scale. The next step towards
substantial growth would be performing a greater amount of per day deliveries by
acquiring a larger customer base. The company’s initial plans were indeed to expand
into Rio de Janeiro and other Brazilian cities. However, with limited available capital
and staff, these projects were put on hold. With the VC’s financial support, network
and connections, Carrinho em Casa could launch an initial test program in these areas
to gauge interest and the scale of potential customer acquisition. According to serial
entrepreneur and academician Steve Blank, one of the main reasons to take venture
money is to “scale like there is no tomorrow”. Mr. Blank argues that VC funding
provides a great opportunity for “companies to invest money in creating end-user
demand and later driving these customers into the company’s sales channel”. In
order to take Carrinho em Casa to the next level, a VC’s support in achieving scale
would be a definite plus.

- Entering into a partnership with a VC fund would open Carinho em Casa’s doors to a
larger network. According to Steve Blank, “the investors’ experience, pattern
recognition and contacts can bring a lot to the table”. This could be a valuable
resource for Carinho em Casa if it is serious in pursuing an aggressive growth
strategy. Not only would the VC’s larger network benefit Carrinho em Casa’s actual business development, it would also help the company establish a range of possible exit strategies. The VC fund would be able to rely on its previous experience and put the co-founders of Carrinho em Casa in contact with potential buyers, both locally and internationally.

- The accelerated growth that could be obtained by partnering with a VC fund could also be a way for Carrinho em Casa to establish itself as a leader in the Brazilian grocery delivery market, which is still very young. Indeed, Carrinho em Casa only has 2 direct competitors, who are smaller and less developed. The funding would be a way for Carrinho em Casa to truly step over the competition and perhaps force them out of business. Being the sole player would give Carrinho em Casa greater negotiation and price setting power with both partner supermarkets and end-consumers.

- Closing a deal with a VC fund could also have the effect of increasing Carrinho em Casa’s credibility and attractiveness. This improved reputation would most likely have a positive ripple effect on securing partnerships with supermarkets for example and entering in deal discussions with possible buyers. On the one hand, supermarkets would be more willing to enter into a partnership with a company that is financially stable with a proven business model. For them, a deal with Carrinho em Casa essentially means they are outsourcing their grocery delivery service to a third party. The supermarkets would want to make sure they partner with a company who has a stable and credible reputation in order to minimize their own risk and brand image. For potential buyers, seeing that other investors have already committed to the business is usually a reassuring factor. In addition, having a VC involved can often facilitate discussions and negotiations since the fund usually has had previous experience with various types of exit strategies.

**Challenges related to VC funding:**

- One point to consider is whether Carrinho em Casa would even be able to attract VC investors and close a deal. Prominent Sillicon Valley venture capitalist Guy Kawasaki provocatively states that: “the probability of an entrepreneur getting venture capital is the same as getting struck by lightning while standing at the bottom of a swimming pool on a sunny day”. The amount of pitches received by PE and VC funds that actually turn into concrete investment is usually very slim. Furthermore, Carrinho em Casa may not meet the criteria Brazilian VC’s use when making investment decisions. First, in terms of size. Although unit profitable, Carrinho em Casa’s total monthly revenues are rather small since the number of returning customers is still low. In addition, the Brazilian VC industry is quite concentrated with 2-3 major players leading the investment scene. According to LAVCA, Brazilian firms e.Bricks, Monashees Capital and Redpoint e.Ventures each closed 10 or more deals per firm, making them the most active local early stage investors in 2015 for Latin America. These firms possess significant negotiation power since they have already been
established as “market leaders”. As a consequence, they tend to require startups to have proven and substantial financial results before investing. Carrinho em Casa would not necessarily make the cut for these funds, and would therefore have to reach out to “second-tier” players, who would most likely write much smaller checks if they even agree to invest at all.

- Another factor that might make VC’s reluctant to invest in Ricardo and David’s company is related to Brazil’s economic crisis and the perceived sustainability of Carrinho em Casa’s business model during such turmoil. Carrinho em Casa is betting on the fact that customers will be willing to pay a premium to receive groceries at home. Although practical, during times of economic crisis, customers may prefer spending extra time in line at the supermarket rather than extra dollars for a delivery service. Whereas adoption to the service was very successful in the United States, Brazil is faced with an entirely different economic and social context that might not justify the need for such a service. Furthermore, as data from Bloomberg suggests, consumer confidence in Brazil is now at a historical low. Consumers seem to be cautious in their spending as disposable income has decreased due to inflation, currency devaluation, increased unemployment and overall sluggish growth. Even if the VC’s do have a bullish long-term view on Brazil, they may be wary of how long it would actually take to “weather the storm” and make positive returns on their investments. In turn, VC’s may prefer to make other investments that are less dependent on the country’s economic ups and downs. In his article “Bootstrap Finance: The Art of Startups”, Harvard Business School professor Amar Bhide’s, states that: “Most start-ups begin by pursuing niche markets that are too small to interest large competitors or venture capitalists. Venture capitalists are hesitant to pursue small opportunities where even high-

percentage returns will not cover their investment overhead. They favor products or services that address hundred-million-dollar markets or that have “the potential to change the world”. Would Brazilian VC’s consider Carrinho em Casa as their “home-run” investment? And although investors in the United States seemed to think that Instacart did have the potential to completely disrupt the way consumers shop for groceries, would Carrinho em Casa have that same impact in Brazil?

- Another issue related to VC funding is that of ownership dilution. Indeed, when a VC agrees to fund a certain company, the counterpart is most often a demand of stake in that respective company’s equity. Having a VC on board would effectively dilute Ricardo and David’s ownership of their business. This can have several adverse consequences that need to be carefully considered. First of all, management incentives may diminish. Knowing that their potential return post-exit will be lower, David, Ricardo and other employees alike might be less encouraged or committed to creating the best business possible. Second, the co-founders may have less flexibility when it comes to running their business the way they seem best-fit. The VC involved will
most likely want to have a say on how the business operates and may even request management cuts or changes. In his article entitled “The Consequences of Raising Venture Money”, Steve Blank argues that “The day you raise money from a venture investor, you’ve also just agreed to their business model”. David and Ricardo would have to evaluate how much decision power they are willing to cede to external hands.

- Related to the issue of ownership dilution is also that of funding amounts. The larger the amount of capital received by the VC, the more likely the fund is to ask for a greater share in the actual ownership of the business. The founders would have to take this aspect into consideration as well when negotiating with potential investors. According to Fred Wilson, partner at Union Square Ventures, “Entrepreneurs should keep the funding amounts small in the early rounds when the valuations are lower and then scale up the amounts in the later rounds when it is a lot more clear how money can create value and when the valuations will be higher”. Fred Wilson gives the example of successful entrepreneur David Karp, founder and CEO of short-form blogging platform, Tumblr. “This model worked out pretty well for Karp. He raised $600k, then $4mm, then $5mm, then $25mm, then $80mm. And at the time of the sale to Yahoo!, he owned a very nice stake in the business even though he had raised well north of $100mm. He did that by keeping his rounds small in the early days and only scaling them when he had to and the valuations offered were much higher”. Since maintaining ownership is important to David and Ricardo, the size of their external funding and related ownership issues would need to be thoroughly thought through before agreeing to any particular deal.

- Another point is the time factor. Pitching VC’s is time consuming. The time David and Ricardo spend conducting due diligence on potential investors, preparing pitch presentations, and actually meeting with VC’s, is time spent away from improving and growing their actual business. As outlined by Bill Trenchard, partner at seed stage venture firm, First Round, fundraising is a full time job that takes significant time and commitment: “For the vast majority of early-stage companies, raising capital is a slower, relationship-building exercise. It is critical that your fundraising process be organized and methodical. Never run an ad hoc process or be half-heartedly fundraising. As a founder, you should either be fundraising or not — and if you are, it should be done with great intention.” Can David and Ricardo afford to dedicate so much time fundraising?

Do you agree with Ricardo that bootstrapping is the wiser growth strategy considering it would allow the founders to truly focus on improving their business while maintaining full ownership?

In evaluating this growth strategy, students should ideally break down the different aspects of bootstrapping, and consider their viability within Brazil’s unique economic context. Students should also assess the advantages and disadvantages bootstrapping would have on
Carrinho em Casa’s business.

**Rationale for sticking to bootstrapping:**

- The main principle behind bootstrapping is to grow organically and fund development through internal cash flow. Considering Carrinho em Casa is unit profitable, they are in a position where bootstrapping would be viable. This is the strategy they had used up until now, as it is one of the lower-cost available options. Indeed, the business model employed by Carrinho em Casa is quite suitable for such a financing strategy. According to Harvard Business School professor Amar Bhide’s article entitled: “Bootstap Finance: The Art of Startups”, several conditions need to be met in order for bootstrapping to be effective. These include, “getting operational quickly” and looking for “quick, break-even, cash generating projects”. Carrinho em Casa has done both. By imitating an already proven business model (Instacart in the United States), David and Ricardo were able to skip certain steps of the brainstorming process and hit the ground running. In addition, as previously mentioned, the company is unit profitable when it comes to the deliveries they perform, so although they lack volume and scale, they do have positive internal cash flow. Keith Kakacek, founder of the commercial insurance group, SIR Llyods states that he: “learned early that it is better to have a low-profile, positive cash-flow job than a high-ego, negative cash-flow job. If the market doesn’t pay for your business—and you can’t develop positive cash flow—you probably don’t have a good enough concept.”

- Adopting a bootstrapping growth strategy is also a way for David and Ricardo to keep a majority stake in their business. Indeed, by growing through retained earnings rather than external funding, the co-founders do not need to worry about diluting their ownership. One of the reasons the founders started the venture in the first place was to eventually obtain a high return on investment through a strategic sale or M&A deal. By maintain ownership David and Ricardo would be able to receive the majority of proceeds if such a deal were to eventually happen.

- Bootstrapping also gives founders greater flexibility in how they choose to run their business. By not being attached to demanding investors, entrepreneurs have less pressure to get “everything right” from the start and can experience with their brand and service more. Professor Amar Bhide argues that one of the “hidden costs of other people’s money” is that it can compromise flexibility: “Outside investors can hinder entrepreneurs from following the try-it, fix-it approach required in the uncertain environments in which start-ups flourish”.

- By sticking to bootstrapping, David and Ricardo can truly focus on customers instead of investors, which in turn may increase the likelihood of a profitable business. This
growth strategy allows the founders to dedicate a greater portion of time to building relationships with customers and other relevant partners such as supermarkets. Rather than being distracted by the many steps involved in obtaining external funding, the entrepreneurs can focus on perfecting their business model while preserving control over all decisions.

- By maintaining the current bootstrapping strategy, David and Ricardo would also have more time to establish greater tangible evidence of the success of their business model. They could truly focus on diminishing churn rates and increasing their number of recurring customers for example. Then, once these issues have been properly dealt with, the company could reconsider reaching out to investors. Having a stronger business model would perhaps allow them to secure a better deal, negotiate further or receive more attractive valuations from investors. Timing is therefore something that needs to be thoughtfully considered.

- The bootstrapping approach also forces David and Ricardo to spend with discipline. After receiving a round of funding, founders often find themselves with large sums of money and are unsure how best to spend these sums. Many will mismanage these funds and burn through the cash without actually leading their company to sustainable growth. Having limited financial flexibility allows entrepreneurs to truly understand and focus on the most vital elements of their business. Professor Amar Bhide stresses the importance of this point in his article by stating that: “successful bootstrappers take special care to expand only at the rate they can afford and control. For example, they tend to invest in people or capacity only when there is no alternative, not in advance of needs. Keeping growth in check is not only financially prudent but it also helps the entrepreneur develop management skills and iron out problems under less pressure. Even entrepreneurs who don’t have to make radical changes in strategy may have to make adjustments as they learn about the nuances of their chosen industry. Learning the nuts and bolts of running a business is particularly important for first-time entrepreneurs”. If David and Ricardo are serious about building the best business possible, choosing bootstrapping as a growth strategy may actually help them achieve that goal and should therefore be considered.

**Disadvantages of a bootstrapping strategy:**

- One of the risks associated with pursuing a bootstrapping strategy is that it can lead entrepreneurs to micromanage their sources of income as well as their overall business venture. As stated by professor Amar Bhide, focusing too much on cash management can block founders from prioritizing strategic goals. In his article on bootstrap finance, he stresses the fact that one of the most difficult phases of any entrepreneurial journey is successfully shifting gears and reminding management to “think more about the big picture and worry less about the little expenditures”.


Sticking to a bootstrapping strategy inevitably means disposing of less financial flexibility. As a consequence, Carrinho em Casa may not be as quick at turning profits. Funding growth would therefore be achieved at a much slower rate than if external capital had been provided upfront. In addition, considering the difficult economic context the company is operating in, relying solely on bootstrapping to fund growth may be a risky and unsustainable strategy. Another adverse consequence is the risk that competitors will catch up and surpass Carrinho em Casa if they are able to fund growth at a faster pace.

The essence of a bootstrapping approach is to grow ones business through retained earnings. Growth is therefore often limited to the viable minimum. There is little room for additional expenses, even though these could add significant value to the company’s development. Expanding the business through aggressive marketing campaigns for example would not be possible and the entrepreneurs would need to rely on cheaper, slower and perhaps less effective strategies, such as word-of-mouth.

One of the options that would fit into the bootstrapping strategy would be to take out a loan from a local bank. This alternative is often taken into consideration because it allows founders to have access to capital without diluting their ownership of the company. Although taking a bank loan may seem like a good strategy in the United States or Europe, where interest rates are at historical lows, it is not the same case in Brazil. Indeed, Brazilian interest rates are extremely high, making debt very expensive, especially for entrepreneurs with little financial flexibility. In June 2016, the SELIC interest rate, set by Brazil’s central bank was 14.25%, whereas in the United States, rates set by the Fed were at 0.50% for the same period. Brazil’s capital markets and more specifically its private debt market are far from efficient. Due to the strong presence of the BNDES, Brazil’s development bank, the corporate debt market has been crowded out, leading to market inefficiencies and high costs of capital. In the event that David and Ricardo choose to opt for a bank loan, they eventually would be required to pay the loan back. Since they are entrepreneurs and their company is still very young with little to no collateral, it would most likely be difficult for them to negotiate attractive terms with the bank. Another factor to consider is that the debt they take on would be denominated in local currency. In 2015 alone the real depreciated nearly 40%. If these macroeconomic conditions were to persist, forecasting and financial planning would be quite difficult. The company’s already limited financial flexibility would therefore be further hindered if it eventually agreed to go ahead with such a deal.

In their version of bootstrapping, David and Ricardo currently have been able to grow through retained earnings and by securing very small investments from angel investors. These investments are vital to the company. However these rounds need to be renewed on a regular basis as the capital is used up quite rapidly. The constant need to reach out to potential angel investors is time consuming and most definitely diverts
the entrepreneurs from maintaining focus on building a sustainable and scalable business.

What challenges do entrepreneurs like David and Ricardo face when starting a venture in an emerging market such as Brazil? Furthermore, why would Carrinho em Casa’s business model be so successful in the United States (Instacart) yet have trouble growing and reaching customers in Brazil? Rather than copy-pasting Instacart’s business model, which is only present in the United States, should Carrinho em Casa attempt to tailor its offering to make it more “Brazilian”? Do you think David and Ricardo are truly serious about their venture, or could their idea to launch a start-up in Brazil be a case of “entrepreneurial tourism”?

To take the case one step further, this third question can be analyzed if time permits. Rather than focusing solely on funding strategies, this question encourages students to consider the different obstacles entrepreneurs may face when starting ventures in emerging markets. More specifically, it encourages a discussion on the challenges related to doing business in Brazil considering the current economic, political and social turmoil. Furthermore, it pushes students to assess the challenges and benefits associated with “copy-pasting” an American business model to a unique Brazilian context. Students are expected to reflect on the reasons why a business such as Instacart could be so successful in the United States but not necessarily in Brazil. Some of the factors that can be discussed include:

- Students can assess the potential and risks Latin American customers have to offer. The drivers behind Carrinho em Casa’s success are mostly related to consumer’s choosing or not to adopt to the service. Yet this service comes at an additional charge. In times of economic crisis, will consumers be willing to pay Carrinho em Casa’s delivery fee? How valuable is this additional benefit to the end-consumer? And are all consumers the same? Perhaps families with children would still be willing to pay the R$9.90 fee as the service is very convenient and practical for them. On the other hand, younger clients may choose to opt out of the service in order to save. It would be interesting for students to reflect on Carrinho em Casa’s different customer segments and the specific needs of each. In terms of potential, middle-class Latin American and more specifically Brazilian customers are growing in size. In addition, they are extremely connected and rates continue to increase. As Carrinho em Casa is technology-based, having a large connected client base is essential to the success of the company.

- In relation to the challenges associated with doing business in emerging markets, students can reflect on the Brazilian notion of “red tape” which includes but does not limit itself to: high costs of capital, unreliable infrastructure, high labor costs, steep taxes…Students should think of how each of these factors could affect Carrinho em Casa and its development potential.
- As seen in the exhibits, although Brazil is facing difficult economic and political conditions, the country’s start-up ecosystem is actually improving and venture capital and private equity investments have grown consistently. Rather than solely focusing on the challenges associated with doing business in Latin America, students should also reflect on the unique advantages emerging markets can offer. Some points of discussion can include: foreign investors searching to diversify their portfolios, local funds ready to use their dry-powder on innovative ventures, entrepreneurs’ access to relatively untapped markets and limited competition…

- Students should consider if the American business model of Instacart is suitable for Brazilian consumers. What factors made Instacart extremely successful in the United States and do those apply to Brazil? What changes could David and Ricardo implement to tailor their company to Brazil’s unique context and consumers? Students can also think of examples of historical start-up success and failure stories. As a reference, companies NuBank and Rocket Internet can be evaluated to see how and if they adapted their business model to Brazil’s specificities.

- The graph below (MIT) should be observed and discussed. Students should attempt to position Carrinho em Casa on the graph and see if there is any potential for the company to evolve towards a more disruptive and competitive business model.

Source: https://mitbrazilventurecapitalstudy.files.wordpress.com/2013/03/mit-brazil-vc-study-2012-2013.pdf

- Finally, students can reflect on the concept of “entrepreneurial tourism”. Are David and Ricardo truly committed to their start-up or was the idea of launching a venture in Brazil a way for them to remain in the country? Both co-founders received an investor visa, valid for up to 5 years, when launching Carrinho em Casa. This trend seems to be increasingly common amongst young entrepreneurs and could be an interesting point to discuss if time permits.
3.5 Teaching the Case

There are several ways to open the case discussion:

One approach is to start with a general discussion of Brazil’s current economic situation and how it affects companies and entrepreneurs seeking growth. This should lead to a reflection on the challenges and opportunities related to doing business in emerging markets and more specifically Brazil.

The case also offers the opportunity to have a more in depth discussion of Brazil’s unique VC/PE industry and start-up ecosystem. Students can analyze how these have evolved over time and how they are faring through the current economic turmoil. Students can then debate what impact these changes may have on Carrinho em Casa’s development.

Another way to open the case is with a decision focus, by asking students the following: “If you were David and Ricardo, which growth strategy would you choose to move forward? Why would you choose this strategy versus another and what remaining concerns would you still have?” There will most likely be advocates on both sides, with some arguing that the only way to survive as a consumer focused business operating in Brazil’s current economic context is through external funding from a VC. Others will argue that the wiser strategy is to maintain ownership and grow the already unit profitable business through internal cash flows. Although both strategies are possible, to foster the debate, students should choose a side and make sure to back their opinion with specific and legitimate arguments, such as the ones listed above.
### Suggested Time Allocation for a 1h30 class

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<thead>
<tr>
<th>Time</th>
<th>Activity</th>
<th>Suggested Plan of Action</th>
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| 10 minutes    | Read Case and Annex       | • Student should have prepared the case in advance: read the material ahead of time, think about the reading and reflect on how it is connected to other course material  
• Sort out relevant facts and information                                                                                           |
| 30 minutes    | Initial discussion        | • Ask questions that require students to review and organize information:  
  - What is the situation, what are the possibilities for action, what are the consequences of each, what action, then should be taken?  
  - What general principles and concepts seem to follow from this analysis?  
  - How do the relevant facts translate into major themes or issues?                                                                 |
| 30 minutes    | Central Discussion and Debate | • Ask open ended questions to fuel debate and conversation: Why do you think it is appropriate for David to suggest X vs Y? What challenge arguments run counter to that view? What might have been the result if David or Ricardo had done Y instead of Z? What immediate action should they take? What do David and Ricardo need to do to achieve their stated goals? How else may they handle the situation? What assumptions underlie David and Ricardo’s behavior and actions? What are the downside risks of one approach as opposed to another?  
• Ask questions that probe into the reasoning behind conclusions, since some students may want to jump quickly to a solution without carefully examining the evidence on their assumptions  
• Center discussion on objectives and solutions  
• As students to identify key concerns - these can be listed on the board for future reference, along with a separate list of possible actions  
• As a facilitator, organize the discussion by seeing if the class is satisfied that each action or recommendation is discussed fully before moving on to the next  
• Listen carefully to students’ responses, paraphrase when necessary and give students sufficient time to reflect on questions or issues that are raised  
• Use the board as a tool to record the conversation. Build discussion pathways, re-organize material, and validate individual student comments  
• Stop and ask students to reorganize visually the recorded thoughts  
• Jot down points that should be addressed later on in the case                                                                 |
| 15 minutes    | Wrapping Up and Debrief   | • Focus not only on the content of the case but also on the process of analysis and evaluation  
• Take charge at this point and offer an assessment of the case or ask the students to themselves pull together the various strands of the discussion  
• Ask students to take a few minutes to write down their thoughts on what they consider to be the summary and conclusion of the session |
| 5 minutes     | Follow-Up, Assessment & Feedback | • If some issues weren’t resolved fully or if answers to questions seemed to demand more information, students can be assigned research tasks for the next class session  
• To get the most of the class discussion, give students feedback on how you think the discussion itself went in terms of group interaction and progress. This will help students improve their ability to understand future cases and participate in analyzing them |
Part 4: References


Latin American Private Equity & Venture Capital Association (2016). Brazil Guide to Venture Capital and Private Equity Term Sheets


