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Square Peg Investor Letter Half Year Report 30 June 2024

Dear Investor,

Earlier this month, we launched the fundraise for our next vintage of funds – Square Peg Fund 6 and Opportunities Fund 3. Many of you have already registered your interest in participating in the new funds, and we are very grateful for your ongoing support.

It is worth reiterating that other than a change in the fund vintage, very little has changed in our strategy and approach; our team, the target size of our funds, and our geographic focus remain the same, as do our core investment themes of AI, fintech and SaaS. The other thing that has not changed is our passion for identifying the very best founders in our corners of the world and backing them early and frequently. We love what we do!

We are now more than 12 years into our journey and clearly understand our strategy and who we are. Our strategy is predicated on a high-conviction investing approach across Australia, Southeast Asia and Israel. The large size of the opportunity set across these three markets enables us to be highly thematic, and as a result, we benefit from the compounding of domain knowledge, networks and reputation over time. These benefits have led to us building a significant competitive moat. We have the conviction to move quickly when the right opportunities present themselves and the discipline to say no when an opportunity is not right for us or is outside our areas of expertise.

We operate in a highly competitive industry, and ultimately, sustained success is as much a function of building a highly aligned, dedicated, and hungry team as it is of having the right strategy. Across all of these dimensions, we are pleased with our progress and believe we have improved year on year since 2012. At the same time, we are conscious of the room for improvement and how much better we have to be to meet our aspiration of building a globally leading and enduring venture fund.

A look back at the last few years in venture capital

From an overall market perspective, the last two years have been the toughest since our inception, but we also believe they have been our best years of performance. Venture capital operates in cycles, and it is hard to fully assess the performance of a venture capital fund until you see a full cycle of performance. In 2012–2021, we operated in a buoyant environment, while 2022–2023 was a much more challenging environment and perhaps the toughest period experienced by venture investors in the last 15–20 years. We have seen our best-performing portfolio companies continue to create significant value, we have identified opportunities to invest in new companies that we hope will be the future Canva, Rokt, Kredivo, and Airwallex in our portfolio, and we have returned significant capital to our early investors.

Our report for the six months up to 31 December 2023 indicated that we were pleased with our portfolio companies' growth rate but that growth had slowed across many portfolio companies. This was a function of both a tougher economic environment in 2023 and companies adopting a less aggressive growth strategy. Pleasingly, we have seen an acceleration of growth in many of our most significant portfolio companies over the past six months, achieved with attractive unit economics. Our founders are doing an outstanding job creating value for their customers and shareholders.

We're continuing to back founders from our investment regions

Over the past six months, our investment cadence has increased. We have invested in several new portfolio companies, including AI-first businesses and others that operate at the intersection of SaaS and fintech. From a geographic perspective, these businesses span our investment geographies, including Australia and New Zealand, Southeast Asia, and Israel. We have also made a number of follow-on investments in existing portfolio companies.

Our exit activity was also higher than anticipated during the half. In total, we returned US\$187m to investors over the past six months from the sale of DeciAI to Nvidia and secondary sales of Canva (partial sale) and Bugcrowd (full sale). We have now returned almost US\$800m to you since inception. Most importantly, we are now at a point in our evolution where the default should be for us to return more capital in a given period than we invest during that same period.

The rapid rise of AI technology and value creation

We have previously shared our views on AI and our belief that it will be the defining technology theme for an extended period of time. The rapid rise of AI is a good illustration of the benefits of our multi-geography strategy. Since our first AI investment in Israel in 2013, we have actively invested in AI businesses. This has enabled us to build our knowledge base, form a clearer view of where we think value will be created, and build our reputation and networks in this area. Going back half a decade or so, there were relatively few AI opportunities in Australia and Southeast Asia, and the opportunity set has only been built out meaningfully in the last 1–2 years. The building of our "AI muscle" over several years has allowed us to have a running start in identifying and leading rounds in some of the best AI-first businesses now emerging from all three of our investment geographies.

While we are pleased with our progress in the early stages of the AI era, there is much more we don't know than we do. We are approaching the coming period with excitement, curiosity, humility, and a deep desire to roll up our sleeves and get to work. Undoubtedly, we will make many mistakes, and all views we hold at this point are lightly held.

One of the reasons we are so excited by the rise of AI is the unprecedented intersection of rapid technological advancement, the creation of applications arising from that innovation, and the size of addressable markets. The multiplier effect of ongoing technology innovation multiplied by business model innovation multiplied by enormous addressable markets will result in a pace and scale of innovation and value creation that has never before been experienced.

Let's look at each of these elements in turn.

Firstly, the rate of technological innovation in AI over the past 5–10 years has surprised almost everyone to the upside; however, we are still in the very early days of technological advancement. We will almost certainly see further remarkable advancements in AI technology, driving decades of new applications. This is very different from the Internet era, where the primary technological building blocks were in place fairly quickly in the mid-1990s, and we saw the explosion of applications arising from those building blocks. A similar phenomenon occurred in the mid to late 2000s with the rise of the mobile Internet, where technological innovation occurred over a much shorter period of time than is anticipated to be the case for AI. It is difficult to predict the rate of technological progress in AI technologies over the coming decades, but it is likely to be profound. The applications that AI innovation will drive will, in turn, impact most sectors of our society and economy.

Secondly, technological innovation provides the foundation for developing new applications that deliver value to consumers and businesses. While not all of those innovations will be driven by startups, if history is any guide, many of these new applications will be created by startups. Trillions of dollars of shareholder value will be created. We have just scratched the surface in terms of creating practical consumer and business applications from the advancement of AI technology to date.

Lastly, these startups operate in a vastly larger market than their Internet-era peers were operating in the late 1990s and early 2000s. For example, Open AI is reported to have annualised revenue of \$3.5 billion just 19 months after the launch of ChatGPT. This is a remarkable scale in a very short period of time. Compare that to Google and Amazon. Google was launched in September 1998, and three years later, its annualised revenue was less than \$100 million. Amazon was launched in July 1994, and it took five years for annual revenue to exceed \$1 billion. Even allowing for inflation, these are dramatic differences of scale and offer some insight into the significant scaling of addressable markets in the last 25 years.

Square Peg team updates

In the last half, we were pleased to announce a number of team promotions in recognition of their ongoing contributions to Square Peg. We're incredibly proud that Leila Lee has joined the Square Peg partnership. Since joining Square Peg in 2017 as Head of Distribution, Leila has led Square Peg's capital raising and investor relations, and we congratulate Leila on this well-deserved recognition. In addition, Matt Linklater from our Investor Relations and Distribution team has been promoted to Investor Relations Manager. Matt has done a fantastic job ensuring our investors are supported and updated on our portfolio's latest developments.

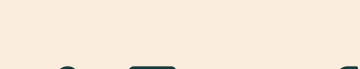
In our investment team, Jethro Cohen has been promoted to Principal, and Kimchi Roy has been promoted to Senior Associate. Jethro and Kimchi will continue backing and supporting founders in Australia and Israel, respectively. While in our operations team, Mick Viney takes on an expanded role as Head of Technology, where he will further support our team and portfolio on their technology needs.

Thank you for your support

We are grateful to our investors for your continued support over many years. Your support enables us to do the work we love. We remain as excited as ever to find the next generation of founders solving significant problems and partner with them.

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PAUL BASSAT



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We're hiring! Investor (Associate)

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