Equity Crowdfunding Guide

FOR INVESTORS

Crowd88

Disclaimer: Crowd88 does not provide investment advice. This guide has been prepared as a support document to provide Investors with a greater understanding of Investing in Companies through Equity Crowdfunding platforms like Crowd88. It is recommended that before you make any investments you discuss these with your financial advisor

The different stages of Companies

There are four common stages a Company goes through when seeking investment;

Seed stage: Seed stage is the earliest stage of financing. Typically, the finance provided at this stage is to develop the product or service

Early-stage: Companies that have begun operations, but are yet to produce a commercial product or service seek early stage financing

Growth stage: Growth stage financing is often invested through a process of financing rounds called Series A, Series B, Series C. In this stage the company's product or service is generating cash flow and the finance is used to grow the company

Late stage: In this stage capital is provided usually before the company goes to an Initial Public Offering (IPO)

At Crowd88, we typically will not list companies that are seeking seed stage investment. Our focus is on Companies that are in early, growth and late stages.

Risks when investing in early, growth and late stage companies

No one can forecast the future of an early stage company, and that's why investment in early stage companies involves a higher degree of risk. Growth and Late stage financing present lower risks as typically the company has a revenue stream and a proven product or service. Four common risks involved when investing in companies via Equity Crowdfunding are:

Business risk: As many companies in Equity Crowdfunding are in early stages of development with a lack of historical business performance there is a greater risk of failure. Whilst companies in growth and late stage have generally reached a positive cash flow and profitability, valuations are typically much higher and therefore investors receive a much lower % of ownership in the company.

Liquidity risk: For equity crowdfunded companies there is currently no readily available secondary market for any of the shares you buy unlike shares you may hold in a listed company. Investors who would like to sell their shares in equity crowdfunded companies, typically need to find another investor to purchase them.

Return risk: The rate of return on any investment in early stage companies is highly variable. Whilst a good investment can provide returns commensurate with the risk taken a bad investment could see no return at all. Some companies even in growth and late stages may still not be paying any dividends to Investors. This may give rise to an opportunity cost for investors, as they could have successfully invested that money elsewhere.

Dilution risk: This risk occurs when companies issue more shares to raise further capital thereby decreasing the % of ownership you have in the company.

At Crowd88 to minimise this risk with investing in early stage companies we invite companies to obtain a Cornerstone Investor from our Cornerstone Club before listing on our platform. This ensures that a seasoned Investor (High net-worth Individual and/or Venture Capitalists) undertakes extensive due diligence on the company before Investing which should minimise the risk to crowd investors.

Crowd88 recommends that Investors read all information carefully, ask questions of the Company before committing an investment.

Rewards of investing in early, late and growth stage companies

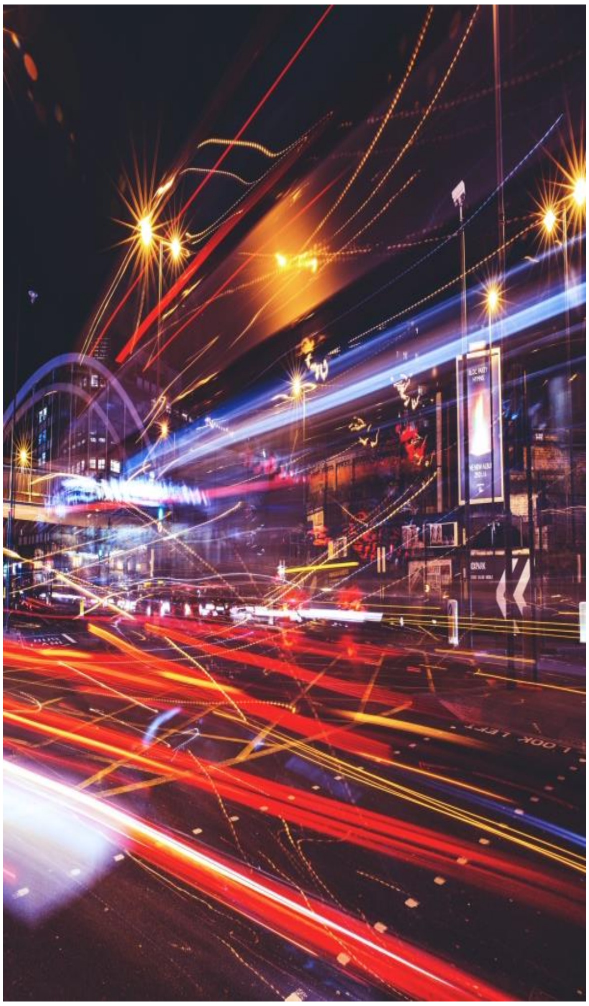
Equity Crowdfunding platforms like Crowd88 provide opportunities for Investors to have access to companies at all stages of development. Crowd88 does not only have early-stage companies we also support Companies that are in later stages of development and growth. However, the earlier you invest the greater chance of higher returns commensurate with the risk. Some demonstrated rewards when investing in companies include;

Potential of very high returns: Investing in early-stage and high growth companies has the potential to deliver huge returns if the business proves successful. Whilst there is a higher level of risk in the early stage the potential for higher returns is greater.

Investing alongside seasoned investors: Before Equity Crowdfunding the opportunity for most retail investors to invest in early or growth stage companies was low as these were typically only available to High net-worth individuals, Institutions or Venture Capitalists. At Crowd88 we have built a Cornerstone Club for this group of Investors and Companies can seek a Cornerstone investment prior to making their offer available through our platform. Once on offer the “Crowd” get primarily the same investment terms as the Cornerstone Investor/s.

Satisfaction: Investing in early and growth stage companies can provide a great level of satisfaction. This is because the Investor is providing an opportunity to an early and growth stage company and in many cases, it is within an industry that resonates with the Investor. It can also provide a greater level of satisfaction than investing in a company that is already listed on a Stock Exchange.

Job creation: Small, medium enterprises (SMEs) are critical for job creation and are a key factor in a thriving economy. Equity Crowdfunding has proven to create jobs and Investors in companies via Equity Crowdfunding platforms are the driving force behind this.



How the return is realised

Your return will be based on the increasing value of the company you have invested in. Returns can be realised in the following way;

Initial Public Offering (IPO): The company goes through an IPO and shares are listed on a Stock Exchange which the Investor sells at a profit on the price they paid for their shares

Trade sale: The company may elect to sell the company at which time your shares may also be sold

Dividends: Investors may gain dividends on their shares. Each company will have their own dividend policy so it is recommended you investigate this before you invest

Selling shares: You can sell your shares in a secondary market (if available) or you can find an Investor to purchase your shares at a higher price than what you paid

The rights that shareholders will hold

Your specific rights will vary from offer to offer. Your rights will be summarised in the information materials posted by the company raising capital. As a general rule, holders of ordinary shares have rights to vote at meetings of shareholders, to receive any dividends that may be declared on the shares and to a return on capital should the company be liquidated (and should there be funds available for distribution to shareholders).

If you are unsure of your rights you should ask the company directly or seek independent advice before Investing.

Funding model

Most Countries that have regulated Equity Crowdfunding have taken an All or Nothing (AoN) funding approach. This means that when a Company reaches the end date for its Capital Raise, investments are only accepted if the Company has met its minimum target amount. The minimum target amount is the minimum amount of money a Company is looking to raise. In most cases the company will also set a maximum target amount that can be invested. If a company does not meet its minimum target prior to its end date the AoN approach has all investments returned to the investors.

Companies do have the option to extend their end date but typically only do this if they are close to reaching their minimum target or they are expecting a sizable investment to be made that would see them meeting their minimum target.

Making the right investment decision

Any investment requires relevant analysis and due diligence before deciding. Some common areas that investors may consider include;

Company prospects: Do the products and/or services the company sells have a real market place advantage and if so, what is the likelihood of this continuing? For example, a disruptive technology with patent protection and proven demand may satisfy this requirement.

Management: Are their interests aligned with equity holders? For instance, do they have significant equity ownership in the company? Is their remuneration structured in such a way so as to work towards long term equity performance? Does this management team have the right balance of skill and experience to be operationally and financially efficient?

Cashflow generation and revenue: Are they generating sales and, if so, are they generating positive cash flow? If they are not generating sales and/or cash flow, are management forecasts of when this will happen realistic? Have the costs been accounted for?

Industry: Is this an industry that I believe can grow into the future? If so, can the company's position be protected and expanded within it?

Future growth: What is the forecast growth of the market as a whole in the next 2-3 years? What is the Forecast Market Share of the Company in the next 2-3 years? Is there a timeline for the business' scalability?

Long term strategy: Carefully think about and understand the value creation strategy put forward by management and current owners. Make sure you believe it intuitively aligns with the needs of the company.

What is their Marketing strategy: It is important to understand the marketing profile of the company now and into the future. You could investigate the marketing platforms the company uses and gauge how efficient they are eg: Social media, Print media, TV etc.

Capital raising and share dilution: Will this company have to raise further funds in the future (due to insufficient cashflow for example)? If so, am I comfortable with the prospect of dilution or buying more shares?

Capital structure: What financial commitments other than to common equity does the company have? Is the equity I am investing in subordinated? Where do my claims on cash flows sit in the hierarchy? For instance, convertible note holders, if they exist, may have prior cash flow claims to equity holders, and may dilute equity holders' ownership though conversion.

Risk Management: Does the company have a satisfactorily established contingency plan? What are some factors the company may see as potential risks? As an investor, am I comfortable with the risk management the company has proposed?

Investors Types in Equity Crowdfunding

In financial services laws many regulators will define investors into certain Investor types. The key purpose of financial services law is consumer protection. There are various types of Investors the most common being Retail and Wholesale.

Wholesale investors are considered more financially savvy and have deeper experience and information when investing and therefore not all the consumer protections that are required for Retail investors are needed. Typically, on Crowd88 you will find our investors defined into these two categories; Retail or Wholesale.

We define investors into these categories partly to comply with financial services law and manage our regulatory obligations eg: In New Zealand restricting aggregate investments to NZD2m from Retail Investors. In other Countries, there may be a cap on the total investment a Retail Investor can invest per Company.

The second reason that a crowdfunding operator may do this is to cater for certain issuing company requirements eg: Some companies raising money may prefer to have a higher minimum investment amount or restrict the number of Investors and in these cases, they may wish to provide the offer to wholesale investors only.

Retail Investors: A Retail Investor is classified as anyone who does not meet the requirements of a wholesale investor (refer Wholesale Investor definition below). Retail investors usually trade in smaller amounts than Wholesale Investors.

Wholesale Investors: A Wholesale Investor may also be referred to as a Professional, Sophisticated, Qualified or Accredited Investor. To be classified as a Wholesale Investor the Investor will typically need to meet certain criteria in the relevant jurisdiction to be classified as Wholesale. This usually includes the total assets held or the total income received over the past two years. Each Country has their own relevant criteria to classify a Wholesale investor.

We recommend a Diversified Portfolio

When investing in early, growth or late stage company's experts recommend you do this as part of a diversified portfolio. Diversification will reduce your exposure to any one asset or asset class and thereby reduce the negative impact of risk arising in any one investment. Crowd88 recommends you talk to your financial advisor to discuss your diversification strategy.

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Connecting companies with investors