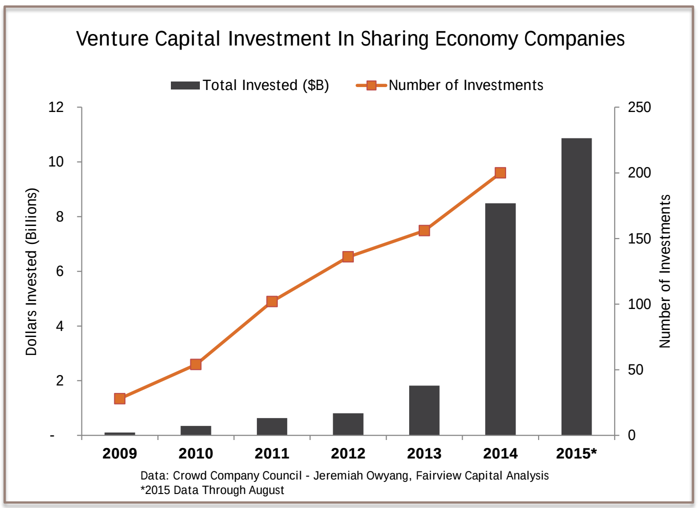
The Sharing Economy

Selling Access Instead of Ownership

The Sharing Economy is garnering significant attention as an area of early-stage venture capital investing. Driven by innovative apps, inexpensive cloud computing and the widespread use of mobile devices, the Sharing Economy has captured both the imagination of the public and the investment dollars of venture capital investors. Venture capitalists have poured more than $23 billion into the sector since 2009, funding more than 280 companies through August 2015.[1] In five of the largest sectors – travel, car sharing, finance, staffing, and music and video streaming – revenues are expected to total $15 billion in 2015 and are projected to grow to $335 billion by 2025.[2]



Broadly speaking, the Sharing Economy refers to business models in which software companies create a clearinghouse for goods and services without maintaining any inventory themselves. These companies typically add value by giving consumers easy access to assets, goods and services owned by others, generating revenues on transaction fees and value-add services. Examples include Uber and Lyft (car sharing), Airbnb (short-term home rentals), Rent the Runway (short-term rental of designer clothes and accessories), InstaCart (food delivery), and Prosper (peer-to-peer lending). Other names for this sector include the "Collaborative Economy" and "Peer-to-Peer Marketplaces."

Given the media coverage of companies such as Uber and Airbnb, most Americans say that they have heard of the Sharing Economy and would consider using one of the services, but only 25% have actually done so,[3] suggesting that there is significant room for future growth. Current barriers to adoption include the inconsistency of services and an unwillingness to try one until they received a positive recommendation from someone they trust.[4]

Trends Driving the Sharing Economy

Numerous trends have converged to spur the rise of the Sharing Economy. They include low-cost technologies, the increasing sophistication of data-collection and measurement tools, social changes driven by the Millennial Generation, and the growth of the freelance workforce.

Low-cost Technologies and Sophisticated Data Collection: Smartphones and tablets, mobile broadband, and cloud computing are three of the biggest drivers of the Sharing Economy. In the U.S., 64 percent of adults use a smartphone[5], and globally, there are an estimated 1.9 billion smartphone users[6]. This broadband-enabled "computer-in-your-pocket" serves as a gateway to powerful apps capable of displaying purchase options, collecting payments and scheduling sharing services. Low-cost cloud computing makes it possible for small teams of software engineers to create fully functioning apps that not only facilitate transactions but also manage inventory and collect usage data. In addition, cashless payment systems have removed a significant transactional barrier.

Demographic and Attitudinal Changes: Young adults around the globe have grown up with always-on computing and ubiquitous high-speed Internet connections. Their attitudes regarding convenience, ease-of-use, on-demand services and non-traditional jobs have all contributed to the rise of the Sharing Economy. Facebook's global penetration, with its reliance on

[1] Jeremiah Owyang, Crowd Company Council
[2] PwC Consumer Intelligence Series report 2015
[3] Leo Burnett estimate 2014
[4] PwC Consumer Intelligence Series report 2015
[5] Pew Internet Project 2014
[6] eMarketer 2015 forecast

true identities, has led to an environment in which strangers transacting business can experience a higher level of trust than in the past. As of 2013, more than 50 percent of Sharing Economy companies relied on Facebook's login feature to register users[7], marrying their user databases to Facebook's and essentially piggybacking on Facebook's security and privacy resources to build a trust environment. Furthering the trust environment, it is common for Sharing Economy companies to post unmoderated peer reviews of both buyers and sellers.

Growth of the Non-Traditional Workforce: Downsizing and other economic factors have contributed to a more transient workforce, which in turn has swelled the ranks of independent workers who are available for the non-traditional jobs associated with the Sharing Economy. Estimates vary widely, but employment experts predict that more and more workers will become independents in the coming years. There are already 53 million Americans who work freelance, and many more are expected to join their ranks.[8]

Keys to Success for Sharing Economy Startups

Not all Sharing Economy markets present the same opportunity for startups. While entrepreneurs will typically describe their market as ripe for disruption, some are easier to address than others.

As the sector has matured, venture capitalists have started to identify many of the characteristics common to successful Sharing Economy startups. These include:

- Offering economic incentives to both sellers and buyers, such as new revenue opportunities for the supplier (e.g., renting their car when they don't need it) and a good deal for the buyer in terms of price, selection, convenience and quality;
- Providing value to both buyers and sellers by aggregating market and usage data, and using that data to drive revenues and growth;
- Organizing fragmented markets, making it much easier for disparate suppliers and customers to find each other;
- Generating high frequency of usage by both suppliers and consumers, rather than occasional and sporadic;
- Developing well-designed user interfaces that offer a "magical first experience" and "no problems service" to hook users quickly;
- Creating network effects that make the marketplace more valuable, and harder to compete with, as users and transactions scale;
- Adding valuable services that discourage disintermediation, such as insurance, payment processing and unique add-ons such as on-call vets for a pet sitting service;
- Establishing a lean corporate infrastructure that facilitates expansion into new markets without major corporate overhead costs.

Venture capitalists are quick to point out that no Sharing Economy startup possesses all of these qualities. On the other hand, it is now a red flag for investors when they evaluate business plans and don't see these and other key attributes of success.

Examples of Sharing Economy Companies

Three examples of high profile companies in the Sharing Economy are Uber, Airbnb, and Rent the Runway. Below we take a look at each of these innovative startups:

Uber: The high-profile car-for-hire marketplace was founded in 2009 by Travis Kalanick (CEO) and Garrett Camp (Chairman), who raised $1.5 million in seed and angel funding in 2009-10. In 2011, Uber raised its first venture capital, an $11 million Series A funding round led by Benchmark Capital at a post-money valuation of $60 million. With its almost instant success, Uber has achieved the sector's highest valuation to date, after a $2.8 billion funding round in early 2015 valued the company at $60 billion. All told, Uber has raised $5 billion and its investors include a who's who of venture capital firms such as First Round Capital, Google Ventures, Kleiner Perkins, Menlo Ventures, NEA and Sequoia Capital.

Uber experienced immediate adoption by both drivers and consumers, and today boasts 160,000 drivers and eight million users in 230 cities[9]. One estimate puts its 2015 operating revenue at $2 billion, based on overall revenues of $10 billion and Uber's 20% commission rate.[10] Uber's fast growth has been fueled by the quality of the consumer experience, with users saying that they appreciate the convenience of ordering a car via smartphone, the immediate reassurance that the driver is on their way, the ability to pay instantly via their stored

[7] Altimeter Group, 2013 Collaborative Economy Report
[8] MBO Partners State of Independence Report 2014
[9] ExpandedRamblings.com, April 2015
[10] Business Insider, November 13, 2014

credit card, and the trustworthiness of using an Uber driver. However, the company has also experienced some challenges, most notably regulatory resistance from the taxi and limousine industry.

Airbnb: This home-rental marketplace was founded in 2008 by Brian Chesky (CEO), Nathan Blecharczyk (CTO), and Joe Gebbia (Chief Product Officer). The company has raised a total of $795 million in six rounds of venture capital, and is now valued at $13 billion. Airbnb operates in 34,000 cities in 190 countries, with more than one million listings and over 25 million guest-stays to date.[11] Prominent VCs that have invested in the company include Andreessen Horowitz, General Catalyst Partners, Greylock Partners and Sequoia Capital.

Airbnb describes its business as "a trusted community marketplace for people to list, discover, and book unique accommodations around the world — online or from a mobile phone or tablet." Both hosts and guests say they appreciate the system's ease-of-use, trustworthiness (both hosts and guests can leave reviews of their experience) and wide selection.

As a disruptive company, Airbnb has had its share of criticism, though that hasn't slowed its growth. Some local officials say that Airbnb hosts are violating hotel and tourism regulations, and some cities now require hosts to pay taxes on their income. In one highly publicized incident, Airbnb guests caused major damage to a home, leading the company to establish a $1 million damage guarantee.

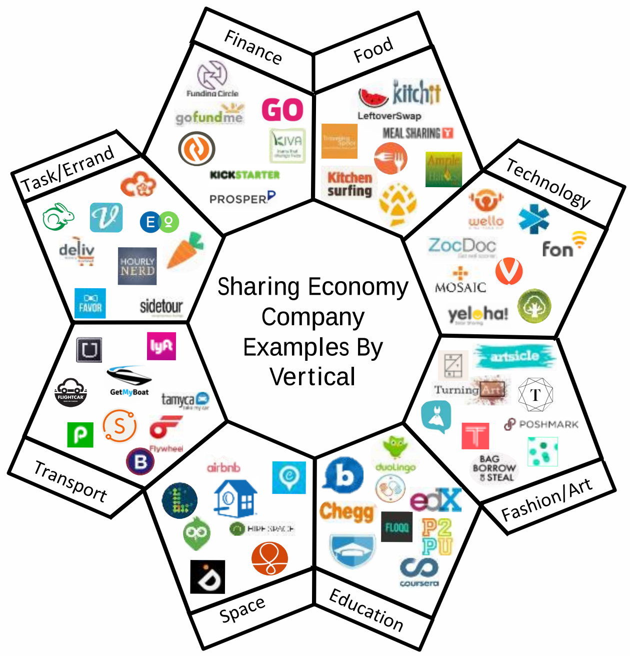
Rent the Runway: Founded in 2009 by Jennifer Hyman (CEO) and Jennifer Fleiss (Head of Business Development), Rent The Runway is an online service that facilitates rentals of designer dresses and accessories. Unlike many other marketplace companies, Rent the Runway does not match consumers seeking clothing with other consumers offering their clothes. Instead, the company works with 250 high-end designers to offer more than 65,000 dresses and 25,000 accessories to its five million members. Because they are only renting the outfit for a few days, users can dress up in fashions they could otherwise not afford. For instance, a Vera Wang dress than sells for $1,300 can be rented for $30 for a one-time rental.

[11] Airbnb

In addition to displaying models wearing its dresses and accessories, the site also allows customers to upload pictures of themselves wearing the apparel. Each page features a robust comments section for users to talk about wearing the outfit, which users say gives them greater comfort in making a selection that they will like.

Rent The Runway has raised $114 million from VCs including Bain Capital Ventures, Highland Capital Partners, Kleiner Perkins and Technology Crossover Ventures. After raising $60 million in a Series D round in late 2014, the company was valued at more than $500 million. The company generated 2014 revenue of $50 million, which is forecast to double to $100 million in 2015.[12]

Sharing Economy – Areas of Opportunity



Data: Fairview Capital Research

Venture Capital Activity in the Sharing Economy

As noted above, venture capitalists have become extremely active investors in the Sharing Economy, especially since early 2013, when Uber raised a $258 million Series C round that valued the four-year-old company at more than $3.5 billion. Since 2013, Sharing Economy startups have raised more than $18.4 billion in venture capital funding.[13]

With valuations continuing to soar, VCs are actively debating the future of the sector. Some see the

[12] Forbes article citing a company presentation, October 2014
[13] Jeremiah Owyang, Crowd Funding Council

Sharing Economy as still in its nascent stage, presaging an "everything-as-a-service" environment that meets the on-demand needs and expectations of today's consumers. Others see a contraction in the offing, if one or more of the so-called "unicorns" (startups that are valued at more than $1 billion) fails to meet expectations and triggers a change in investor sentiment.

At the same time, as consumers become more comfortable with the Sharing Economy model, VCs are looking for new markets ripe for disruption, including healthcare, education and even government services. The fever pitch of the sector is naturally bringing a rush of business plans from would-be entrepreneurs, but with so many to choose from, VCs are currently focusing most of their attention on current Sharing Economy sectors (such as financial services and travel) rather than branching out into new ones.

Fairview and the Sharing Economy

With numerous top-tier venture capital funds investing in this sector, Fairview's funds include many of the most highly regarded Sharing Economy companies in their portfolios. With so many companies still in development and privately held, our expectations for investment returns remain tempered. Additional data, such as revenue generation, profitability and public market receptiveness towards breakout companies in the space will ultimately provide a better sense of whether the investment activity and valuations in the sector are justified.

Despite these qualifications, we believe it is a very exciting time to be invested in the Sharing Economy, in large part because it is being driven by large-scale trends such as the rise of mobile devices and concerns about the environmental impact of over-consumption.

Mobile, in particular, appears to be one of the keys to the sustainability of the sector. The most highly valued company in the sector, Uber, relies almost exclusively on its mobile app to both connect drivers and riders and also to process the transaction, an important proof point of consumer acceptance of the business model. With smartphone adoption climbing rapidly and spreading into previously untapped global markets, there appears to be abundant growth opportunities for the strongest and most disruptive players.

The confluence of low-cost enterprise technology, widely available broadband Internet access, and powerful mobile computing devices is driving the Sharing Economy revolution. There are no doubt many interesting developments ahead as entrepreneurs and venture capitalists collaborate on building this exciting and rapidly expanding sector.