INNOSPHERE VENTURES’ REVIEW OF THE

ARKANSAS VENTURE CAPITAL ECOSYSTEM

2021

DATA PROVIDED BY PitchBook

Introduction

Innosphere Ventures has been working at the intersection of entrepreneurship, venture capital (VC), and economic development for over two decades, and we believe that if we want our local, regional, and national economies to advance, we need to make sure we're doing all we can to support the tech sector. When science and technology startup companies have the resources they need to advance technologies and grow businesses, we see through the data that these younger firms are creating most net job growth and driving the most coveted job creation in the U.S.

As the world faced the 2020 global pandemic, Innosphere took significant strides to position our organization for more meaningful economic impact by purposefully expanding throughout the Mid-America Mountain Plains Region and laying the groundwork to launch a second regional venture capital fund. Why? Because as we head into the next decade, we can only be a competitive region if we increase our ability to innovate at an unprecedented level.

In their report, "Competing in the Next Economy," The Council on Competitiveness challenged organizations to do more, stating that our nation needs to boost U.S. innovation capacity tenfold. Achieving 10X in anything is challenging, and innovation at scale requires many factors to work in sync.

Innosphere Ventures is dedicated to ensuring that our science and technology startup companies have accessible capital to fuel their growth because that's how these young companies will start creating jobs and powering the economy. Historically, regions in the U.S. with more available venture capital are the same regions known for driving innovation and being a hotspot for entrepreneurs.

The performance of venture capital, at a national level, has been outstanding over the last several years – with investors and limited partners (LPs) being especially keen in investing in the asset class. Even in the middle of a global pandemic, 2020 was a record year for venture fundraising and deployment, with nearly $80 billion in capital raised for VC funds — with 2021 looking to be on pace to top $100 billion.

While this is good news for the U.S., a closer look at regional VC trends in 2020 reveals challenges for up-and-coming innovation hotspots such as Arkansas:

- An increasing amount of capital is concentrated within large VC funds, and fewer emerging funds have been capitalized in recent years, with 2020 being a low spot since the great recession. This declining number of small VC funds is problematic because they are essential in leading investment rounds and investing at the seed and early-stage level.
- An increasing amount of capital is concentrated in coastal regions, leaving companies in Mid-America with scarce availability of local capital.
- The Arkansas startup ecosystem has shown impressive growth and consistency moving into the new decade.

In this environment, the general partners announce our second venture capital fund, Innosphere Ventures Fund II, which will positively impact economic growth, accelerate the path to successful exit events, and create returns for investors. We'll accomplish this by investing in businesses in the middle of the U.S. and by supporting entrepreneurs in building companies and technologies that matter in today's world.

Enjoy the read,

Mike Freeman, CEO & General Partner
John Smith, General Partner

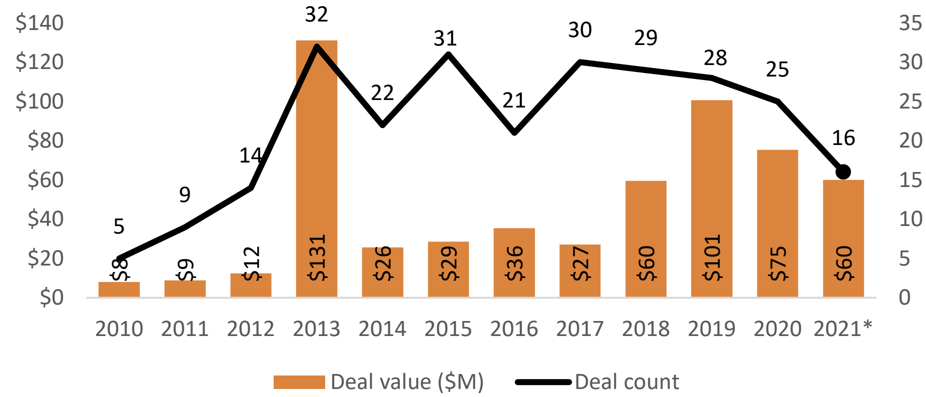
EDA
U.S. ECONOMIC DEVELOPMENT ADMINISTRATION

Note on methodology: References to investments and funding at the "early stage" consist of angel, seed, and Series A funding rounds.Series B and beyond represent late-stage investment activity. Unless otherwise noted, investments refer to venture capital invested in Arkansas-headquartered companies. Figures for summed investment rounds only represent publicly disclosed transactions. A special thanks to Clayton Castro, Innosphere Associate, for his support in producing this report.

Arkansas Venture Capital Trends

2020 showed significant overall investment activity in the Arkansas venture capital ecosystem. The total investments of $75 million only lagged 2 other years of the past decade (2013 and 2019). There were 25 deals throughout 2020, which was slightly below the deal count of the prior 2 years. The VC ecosystem in the state has seen steady growth, with total deal value in the past few years growing at an impressive rate.

Arkansas VC Deal Activity



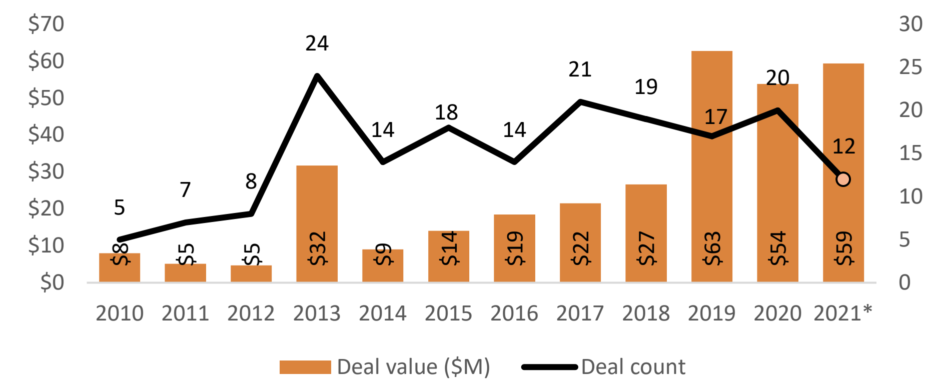
So far in 2021, there have been 16 total deals with a cumulative $60 million in value. Which, at this pace, will easily exceed the investment and number of deals from last year. Early-stage investments have repeatedly captured the majority of the investment activity. Most years have posted large portions of their total investment and number of deals in these early-stage companies. 2020 had a strong showing in early-stage companies, with $54 million in total investments over 20 deals. While 2021 early-stage investments are off to a blazing start, already surpassing the total investment from last year, with $59 million in cumulative deal value over 12 different deals.

The state hadn't seen a new record of total VC deal value since 2013 when the state raised $131 million on an impressive 32 deals. Much of that value ($82M) was driven by One Country, a media platform that offers country music, news, and entertainment. However, in the following 4 years, Arkansas failed to reach $50 million in total deals. After 2017, the state has seen a drastic increase in VC activity and has consistently posted elevated investment numbers.

During the pandemic year, the total activity was slightly lower than the previous three years, but the state is showing great strength in its 2021 rebound. Early-stage total investment value is surging this year, driven by larger average deal sizes.

Arkansas Early-Stage Investments

Angel, Seed, and Series A Activity

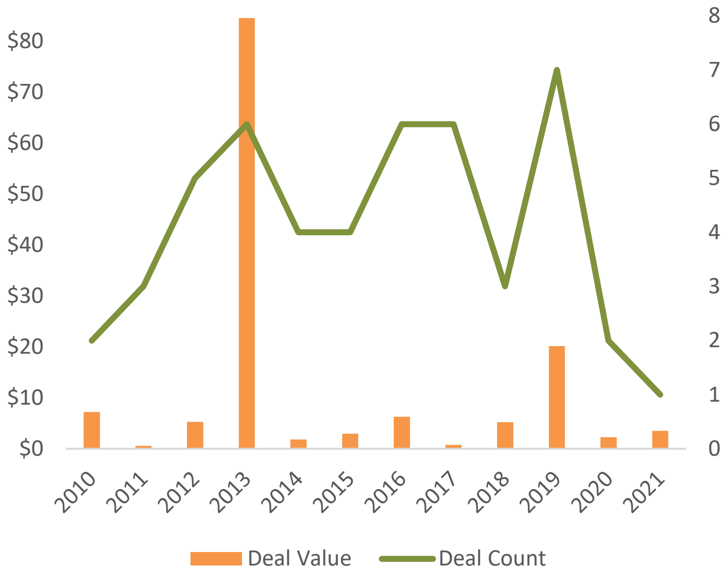


The state of Arkansas has a wide array of tax incentives for different economic development activities. The equity investment incentive is a popular program, where up to 1/3 of the capital invested may qualify as a tax credit, up to 50% of taxable income. The Arkansas Venture Capital Development Fund is focused on matching investments in technology companies. It offers a maximum match of one million dollars. Additionally, the Arkansas Institutional Fund, which was enacted in 2005, provides capital to qualified venture capital and private equity groups. These programs are designed to develop the Arkansas economy through the consistent support of small companies in need of funding. The Arkansas Development Finance Authority is in charge of authorizing the funds for these programs. It is expected to distribute over $420 million through its first 2 rounds of investments.

Arkansas VC in Depth

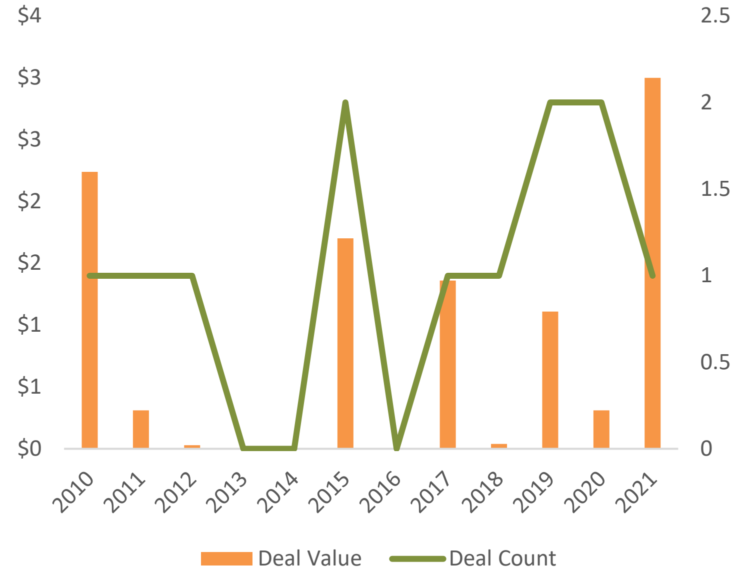
SaaS deals show yearly variation

Arkansas SaaS VC deal activity ($M)



HealthTech deals rebound after period of low activity

Arkansas HealthTech VC deal activity ($M)



Source of graphs and chart: PitchBook | * As of August 9, 2021

Notable Investors in Arkansas

The 10 most active Arkansas-based investors are primarily all geographically close to either little Rock or Bentonville, AR.

Investors	Active Portfolio	HQ Location
The Venture Center	72	Little Rock, AR
Cadron Capital Partners	24	Conway, AR
The Stephens Group	20	Little Rock, AR
NewRoad Capital Partners	18	Rogers, AR
VIC Technology Venture Development	14	Fayetteville, AR
Tyson Ventures	10	Springdale, AR
Tonic Regional Funds	8	Fayetteville, AR
Hayseed Ventures	5	Fayetteville, AR
Arkansas Development Finance Authority	4	Little Rock, AR
Rockfish Brand Ventures	2	Rogers, AR

The Venture Center

Based in Little Rock, AR, The Venture Center is an incubator and VC focused on accelerating economic growth through various programs. The Venture Center is focused on investing and aiding financial technology startups and early-stage companies.

Cadron Capital Partners

Founded in 2017, Cadron Capital Partners is located in Conway, AR. Cadron Capital invests in high growth technology companies. The group is focused on disruptive technologies and creating a sustainable venture ecosystem.

Heartland Forward

As a nonpartisan and nonprofit "think and do tank," Heartland Forward is focused on improving economic performance in the center of the United States. Heartland Forward pursues its mission through independent, data-driven research, action-oriented convenings, and impactful policy recommendations.

Public Research Universities

University of Arkansas

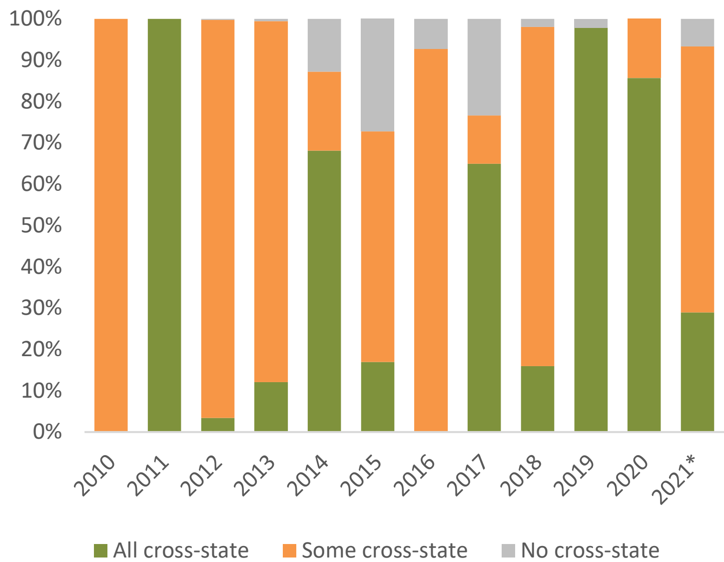
The Office of Entrepreneurship and Innovation at the University of Arkansas has various programs designed to initiate and propel startup success. The office offers services and events from pitch competitions with prize money, all the way to commercialization training and access to Venture Mentors.

Arkansas State University

The Arkansas Small Business and Technology Development Center has been in place since 1983, where its main goal is to aid startups in the Northeast and North-Central regions of the state. It is a part of the college of business and allows startups to receive critical consultation and guidance.

Arkansas Ecosystem Benefits from Out-of-State Activity

Arkansas VC deal activity by cross-state investor involvement
AR VC deals ($M) by investor HQ



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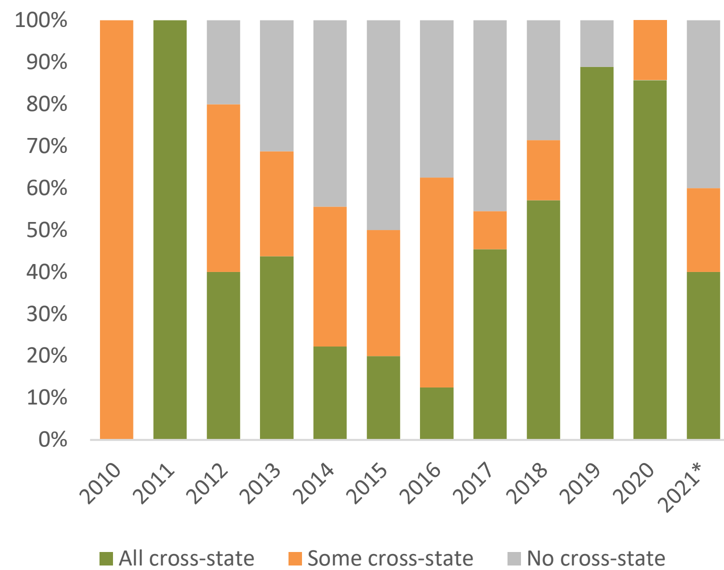
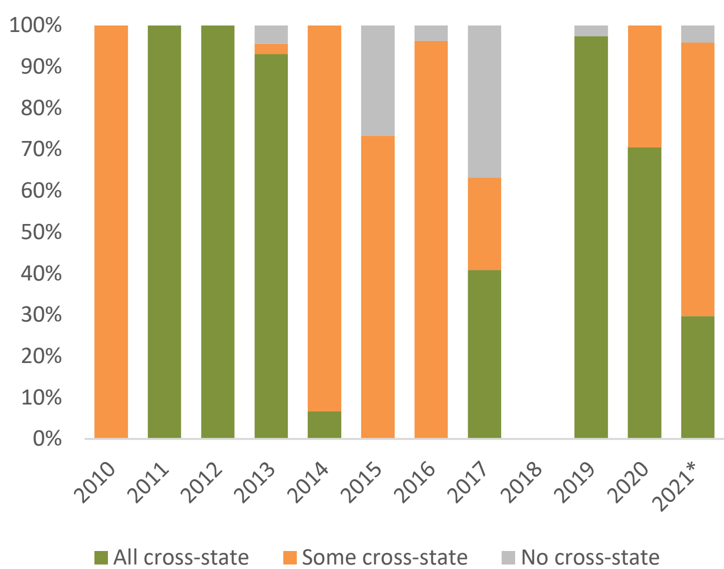
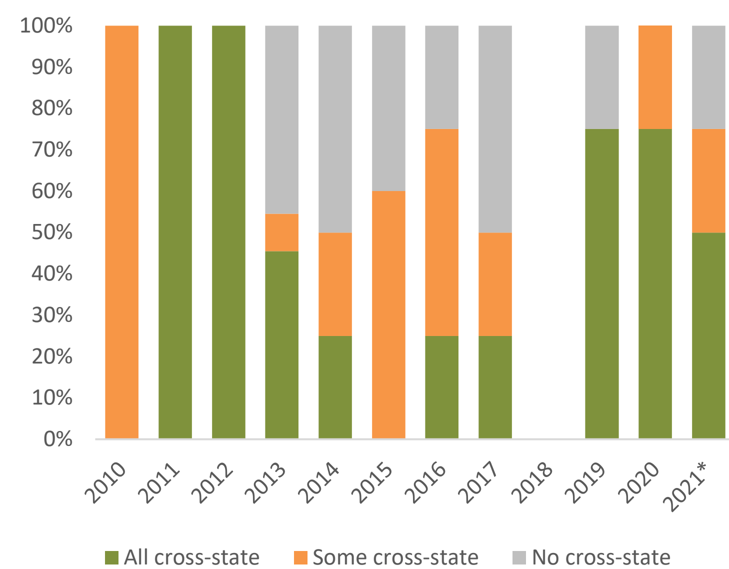


Source: PitchBook | *As of August 9, 2021

Early-Stage VC investments are supported by cross-state investors
AR VC deals ($M) by investor HQ



Arkansas Angel, Seed, & Series A VC deal activity by cross-state investor involvement
AR VC deals (#) by investor HQ



Data not available for 2012 and 2018

Source: PitchBook | *As of August 9, 2021

Local investors and out-of-state investors

In looking at the total activity of investors, Arkansas greatly benefits from investments that originate out-of-state. In the last couple of years, in-state investors have taken the back seat as out-of-state activity has taken a majority in both deal volume and the total number of deals.

Conclusion

The state of Arkansas has been posting elevated deal counts and total deal value over the past few years and was able to achieve comparable investment activity during the pandemic year. 2021 VC activity is currently on pace to surpass 2020 and potentially be the largest on record.

Some of this growth is attributed to the continuous efforts from the state incentive plans and investment funds and the general VC environment. With $61 million already invested in the first 2 quarters of the year, a comparably strong or even more vigorous second half will place this year close to or further than the all-time high of 2013.

For the local venture ecosystem to keep expanding, the state will need to continue to attract out-of-state investments and increase the activity in locally based venture capital firms. The state's tax benefits are an essential step into creating a sustainable and active system for startups. However, increasing activity will depend heavily on the quality of Arkansas-based startups looking for funding. Technology commercialization programs at public research universities should certainly increase the number of quality ventures emerging in the state.

Innosphere Ventures Fund is a venture capital fund leading early-stage investments for companies who are driving innovation in the B2B SaaS Software, Cleantech and Medtech sectors. The Fund's general partners have extensive operator knowledge and industry experience. Our team is small, fully integrated, and impact oriented to produce successful results. We bring more than just capital; we bring differentiated domain knowledge and access to our expert partners from across the globe. Innosphere Ventures Fund has a strong foundation built on its successful first fund and its leading accelerator program which has operated for over two decades. www.innospherefund.com

Innosphere Ventures is a non-profit incubator that grows the region's entrepreneurial ecosystemby supporting science and technology startups with a specialized commercialization program, a variety of incubation programs, and venture capital.