

DOTCOM BOOM 2.0 BOOTS UP

Investor interest in the information technology sector is heating up again.
Report: Jeanne-Vida Douglas

You may not have heard of him yet but taciturn Russian Yuri Milner is now one of the hottest investors in one of the hottest sectors in the world – despite the fact that his mezzanine finance company, Digital Sky Technologies (DST), has made only three investments in the past 18 months.

In May 2009, he put \$US300 million into Facebook. Six months later, Digital Sky formed part of a consortium that injected \$US219 million into social networking games company Zynga.

In January this year, Milner paid \$US135 million for a stake of group-buying upstart Groupon, which rejected a \$US6 billion acquisition bid from Google just a month earlier.

Milner is part of what is shaping up to be a second dotcom boom as investor interest in the information technology sector heats up. This time it is web businesses and social networking sites that boast huge footprints but small profits leading the price rises.

But it's not just Milner and DST fanning the flames. On January 4, Goldman Sachs confirmed it would invest not only directly in social networking behemoth Facebook but would assist its clients to do the same.

Then there's a new breed of investors called super angels, who seed large numbers of companies with small amounts of capital, rather than focusing on a selected few. Add to this a new generation of technology that has reduced the cost of entry for software start-ups and the result is entrepreneurial activity not seen since the dotcom boom in the late 1990s.

This time, most of the software companies involved are already cash-flow positive and are looking for investors to provide skills as well as cash and they are not necessarily based in California's Silicon Valley.

In July, Sydney-based software company Atlassian raised \$US60 million in venture capital from US-based Accell



Hot investor: Yuri Milner, is a significant player in social networking companies

Dismissing criticisms by some in the industry that Yahoo7 paid too much, Lund points to Spreets' rapid growth, having established a customer base of half a million, positive cash flow and the dynamism of a retail model that is booming all over the world.

"To build a business of this size within a year is impressive, particularly when you realise that growth has come organically," Lund says. "For an asset of this quality, in this space, we think we paid a very fair price."

Chief executive of Australian-owned micro-outsourcing website Freelancer.com Matt Barrie says venture capitalists from all over the world are taking an active interest in the Australian tech sector.


"We're going to see this bull market for technology continue at least until Facebook lists, when I think it will peter out a bit," Barrie says.

"The extra money that's being invested by groups like DST and the super angels is extending the boom longer than it would have been and creating opportunities for software companies to establish themselves where they might otherwise not have had a chance."

No everyone, however, is a fan of the increase in activity. Local venture capitalists are finding it tough as they are forced to compete with offerings from foreign firms and deal with local software developers that are revising their expectations upwards.

James Williams, investment director of Yuuwa Capital, which focuses on fast-growing companies in the areas of information technology and biosciences, says: "There's a real snowball effect. IT is moving terribly quickly and people will be coming to us expecting a grossly inflated valuation. As a result we won't be able to invest in companies which we otherwise might have considered."

The first dotcom boom ended in an inglorious mess as companies with no revenue received exorbitant valuations.

This time there is revenue but valuations are outstripping profits by a factor that usually would leave investors running scared. The trick, as always, will lie in deciding when hot becomes too hot. 

Partners, which was 10 times the average for young IT companies. Just weeks later, financial monitoring company SMARTS was bought by Nasdaq OMX Group, the company behind the tech-focused Nasdaq securities exchange. More recently Yahoo7 bought group purchasing company Spreets for \$40 million, before the company had celebrated its first anniversary.

Describing the group buying category as "exploding", Yahoo7 chief executive Rohan Lund is standing by his decision to invest in a young company and emerging sector.

"I like the natural efficiency of the model, which is unique in being able to broadcast to mass audiences through online social media," Lund says. "The challenge we see in most online businesses is their dependency on buying audience traffic."

"There are good reasons why Google and others are so enamoured of owning Groupon and willing to pay a premium for that market leadership."