VCAPITAL

Market Update:

The venture capital industry continues on a strong up cycle. During the first six months of 2018, $57.5 billion was invested in venture backed companies, more than any other previous six-month period. Early-stage investing, where VCapital is focused, similarly continues to grow in dollars, as QII 2018 saw the 7th consecutive quarterly increase in capital invested, at $11.5 billion. [1]

While it is always good to see such robust venture capital investment activity, we are particularly pleased by market dynamics that we believe make VCapital's market position extremely attractive. VCapital remains focused on Midwest-based early stage deals, where valuations remain far below deals on the West Coast and Northeast, presenting an opportunity for greater ultimate returns, and that is in fact what leading market trackers are reporting.

The growth in deal dollars nationally reflects increasing deal size, especially in later stage deals. The first half saw 94 financings completed of at least $100 million and 42 unicorn financings (deals with a valuation of at least $1 billion). Early stage deals are also increasing in size, driven by exuberant demand from investors in the traditional California and Northeast hot bed regions, with an average deal size of $18 million. Deals over $25 million made up more than one-half of the early stage deals done thus far in 2018. Even angel and seed deals on average have reached decade-high dollars, with median sizes of $830k and $2.1 million, respectively. [1]

We believe strongly that VCapital benefits from its Midwest focus. There has been considerable documentation of the region's lower deal valuations but ultimate exit values in line with the West Coast and Northeast, meaning superior returns for Midwest-focused investors. The Midwest's lower deal valuations have been enabled by more prudent investor demand as well as a much lower cost of doing business. For example, it costs 42% more to operate in San Francisco than it does in Chicago, meaning San Francisco/Silicon Valley ventures need more funds to develop, tempering ultimate exit returns.

Further, recent Midwest venture successes have encouraged rapid growth in the Midwest's entrepreneurial venture infrastructure, fueling increased regional deal flow. According to a report from Hyde Park Angels [2] , in 2017 the Great Lakes region (which encompasses much of the Midwest) was one of the most active regions of the country outside of California, increasing its deal count from 462 in 2016 to 623 in 2017, with the amount invested in the region increasing from $2.7 billion to $3.8 billion. Over the last ten years, the Great Lakes region has produced the greatest percentage of exits that returned over 10x to investors.

As for exits, the news is also positive. QII 2018 was the fifth consecutive quarter with more than ten venture backed IPOs, primarily driven by biotech companies, which account for the majority of

[1] Statistics in this paragraph were obtained from Venture Monitor 2Q 2018 published by PitchBook and the National Venture Capital Association

[2] 2018 Midwest Startup and Venture Capital Market Analysis by Hyde Park Angels

such IPOs. M&A activity, however, had a slow first half. The average time to exit VC investments through the first half of the year was 6.1 years from the date of the first VC financing. This figure has been steadily rising over the past decade and is a major reason for the increase in unicorns and other higher valuations. The median exit size during the first half of the year was $105 million, while the average was $225 million, each of which were the highest amounts ever recorded. [1]

Portfolio Update:

Below is a schedule of the investments made by VCapital and BVC during the second quarter and the investment amounts held as of June 30, 2018:

Portfolio Company	QII 2018 Investment	Investment at 6/30/18
Atlas Space Operations	$0	$505,000
Camras Vision	$0	$1,471,000
Intensity Therapeutics	$0	$2,321,667
Padcaster	$735,000	$735,000
simMachines	$0	$1,203,500
Synap (Imagineer)	$0	$559,984
Xaptum	$680,000	$830,000

Atlas Space Operations *(Developing Products for Space Communication)*
As mentioned in last quarter's report, NASA announced it is collaborating with Atlas to test Atlas' technology for potential use with NASA's ground-based communications network, the Near-Earth Network. During the second quarter, NASA provided Atlas with instructions on how to integrate their system with the Near-Earth Network. The company expects a gradual ramp-up of their services under this contract over the next 12 to 18 months, with annual revenue potential from the contract ranging from $500,000 to upwards of $10 million.

Atlas was recently awarded an additional option on its contract with the National Oceanic and Atmospheric Administration (NOAA) to support a satellite mission called KOMPSAT from NOAA's Finland location. NOAA is also working on exercising the option to add its American Samoa station for Atlas support. These two options are expected to add approximately $490,000 in annual revenue.

The company is also working on a proposal with Telespazio, a European leader and one of the world's main players in satellite solutions and services. The plan is to deliver three Atlas LINKS™ systems to Telespazio's headquarters in Italy over the next eight months for its next generation constellation of earth observation satellites called Cosmo-SkyMed, scheduled to launch in 2019.

Finally, the company has submitted a proposal to Planet IQ, an organization launching satellites for better weather forecasting and monitoring, for support of Planet IQ's constellation. This contract could be worth $3.5 million over three years.

Atlas will soon be going to market to raise $3-$4 million, the terms of which are currently being negotiated. We will let you know once this round is available for investment through VCapital.

Camras Vision *(Developing a New Device to Treat Glaucoma)*
Camras has identified and implemented a modification that is likely to increase significantly the life of the Camras Shunt, and initial manufacturing of this new version is complete. The company plans to implant this version of its shunt in a monkey study and then in future human clinical trials. Because of this change, the company has put the previously planned Early Feasibility Study with the FDA on hold, as it no longer represents the quickest pathway to FDA approval.

The Dominican Republic study is moving forward slowly, as patient screening has begun but has not yet yielded any suitable candidates.

The company recently added a VP of Product Development and Engineering to its team.

Intensity Therapeutics *(Developing a New Approach to Fight Cancer)*
As mentioned last quarter, Intensity was approved to test its drug (delivered via intratumoral injection) on deep body tumors. In the second quarter, the company recruited and tested its drug in eight patients, four with deep body tumors and four with superficial tumors. There were no drug-related serious adverse events in any of these patients. In addition, patients receiving the drug at a more appropriate dose relative to tumor volume have maintained disease stability (i.e. no further tumor growth) during treatment and some even with visual appearance of tumor regression. As a result, the Study Steering Committee approved the initiation of tests for all tumor types with even higher doses of the drug.

In June, the company presented at the American Society of Clinical Oncology (ASCO) annual conference in Chicago. ASCO Chicago is the world's most important clinical cancer gathering, with over 30,000 attendees. In addition, the National Cancer Institute and Intensity agreed to extend their Collaborative Research and Development Agreement for another year.

As you may know, the company is currently raising a $9.0 million Series B preferred round of financing at a $58.4 million pre-money valuation, with VCapital's allocation from $1.0 to $2.0 million. Proceeds from this offering will be used for further product development, the ongoing clinical trials, increasing the number of hospitals in the study, conducting new product research, and legal, patent and G&A expenses. Please contact us if you are interested in participating in this financing.

SimMachines *(Developing Artificial Intelligence Software)*
The simMachines product has been well received, with specifics of customer reception leading the company over the past few months to sharpen its marketing focus. As you may recall, the company's greatest initial focus was on selling to the marketing technology sector. The company has enjoyed, however, strongest positive response in the fraud prevention market (especially dealing

with credit card use) and has therefore shifted its strongest focus to this industry. The growth in available data that can contribute to fraud prediction and prevention is very high, and simMachines, with its rapid setup, ability to "learn on the fly," and ability to produce predictions in milliseconds, is well suited to this industry.

It is not, however, abandoning interest and a lower level of activity in marketing optimization, as that market may still contribute significantly to ultimate exit value. As discussed in last quarter's Investor Letter, though, since simMachines has found purchase decisions by larger organizations in this space to take longer than expected, its continued efforts in this area for now are targeting small to medium size organizations. Reception among these customers has been encouraging.

The company has a robust sales pipeline, with projected revenue of $1.7M for 2018, $7M in 2019, $20M for 2020, and $42M in 2021. The company's current annual recurring revenue for already signed contracts is currently $675k. The company's margins are 80%, and the churn rate for its customers is expected to be very low.

The company is currently raising a $3.5M Series A round, of which VCapital's allocation is $1.0M. Currently, we have $635,000 committed, and will likely close out the remaining $365,000 by the end of August. The proceeds from this offering will be used for working capital purposes. Please let us know if you are interested in participating in this round.

Imagineer Technology Group (f/k/a Synap) ***(Developing CRM Solutions for Customer Service Teams)***
During the second quarter, Imagineer released a web version of its Clienteer product (an intuitive and highly configurable relationship management platform designed specifically for hedge funds and institutional asset managers), an important milestone for the company which it hopes will open doors to new customers that were previously closed. The company also released a large number of updates to its other products as well.

The company signed up ten new customers during the quarter and a few add-ons and upgrades for a total of $261k in new annual recurring revenue (ARR) bookings, bringing the 2018 YTD new recurring revenue bookings to $567k. Gross revenue for the first half of the year was $3.0 million, 96% of budget.

The company continues to strengthen its relationships with its customers and, as a result, customer satisfaction levels have remained high and incident response rates have stayed strong. Notwithstanding its product differentiation, however, the company is still learning how best to succeed in the competitive CRM space. Customer cancellations totaled $81k of ARR during the second quarter, bringing total cancellations for the first half of the year to $433k, 84% of the company's full-year churn budget. The company is keeping close tabs on and in close contact with "at-risk" customers, to learn how best to prevent cancellations.

On the personnel front, the company hired five new engineers during the quarter, boosting its ability to write, test, and ship code. The company also hired a sales and marketing analyst to help streamline sales and marketing efforts and efficiency. Imagineer will be looking to hire inside sales representatives and another full-time product designer during the second half of the year.

Padcaster ***(Products to Turn Tablets and Smartphones into Video Recording Studios)***
During the second quarter, VCapital and BVC invested $735,000 in Padcaster in the form of Series A Preferred LLC Units.

The company made significant progress during the first half of 2018. QI and QII 2018 revenues were $833k and $2.0 million, respectively, compared to $372k and $823k for the same periods in 2017. Gross margins for the company's products average 65% to 70%.

The company added some notable customers during the first half of this year, including Apple, Nissan Automotive, Dentons (the world's largest law firm by number of lawyers), and Fox News. The company's sales at B&H, the largest non-chain photo and video equipment store in the United States, are up 75% year-over-year.

Padcaster international sales remain an under-developed opportunity. The company is in the process of evaluating its international distribution strategy. It recently signed a deal with 1Source Video, one of the premier video equipment distributors in North and South America.

The company's product line has expanded as it "soft-launched" the Padcaster VERSE, its mobile phone product, which will be aimed at the consumer market. The company also added a sun shade, headphones, and tripod to its product line.

The company has made the following key hires in 2018: CFO, COO, VP Sales (it now has three full-time Sales VPs), VP of HR and Administration, and a Taiwan-based Manager to oversee the suppliers and manufacturers in that region. It is currently looking to hire a VP of Marketing.

Xaptum ***(Developing Security for the Internet of Things (IoT))***
In the second quarter, VCapital invested $680,000 in Xaptum as part of a $3.5M Series Seed Plus Preferred round, bringing our total investment in the company to $830,000 as of June 30, 2018. Subsequent to the end of the quarter, VCapital invested an additional $252,500, bringing our current investment in Xaptum up to $1,082,500.

The company made significant progress during the quarter in both product and sales/distribution. On the product front, it validated its "Reduced Sales Cycle" model from nine months to less than one month by using a plug-n-play router card. Customers can now simply plug in the pre-provisioned router card and immediately begin using the software. Prior to this, the Xaptum offering was delivered to a customer via a Software Development Kit which required the user to install Xaptum agents and develop code in order to use the software.

On the sales and distribution front, Xaptum has established a go-to-market model using sales channel partners and fulfillment through distributors. This model allows Xaptum to leverage the sales channel partners' existing sales force and relationships. The company then distributes its product through a relationship with Avnet, one of the world's largest distributors of electronic components and embedded solutions, enabling Xaptum to fulfill its sales orders at scale.

The company is targeting September 30 for the commercial availability of its product. It is projecting revenue of $83k for the 12 months ending September 30, 2019, and then $7.0M and $29.6M for the subsequent two 12-month periods. These revenue projections are based on cumulative unit sales of 11,000, 63,250, and 275,000 as of 9/30/19, 9/30/20, and 9/30/21, respectively.

The company has a number of immediate hiring needs in order to meet its goals. On the sales side, it is actively looking to hire two sales channel managers, a digital marketing assistant, and a marketing content specialist. On the technical side, it is looking for a product architect – big data and one product engineer.

Companies in Due Diligence:

Deal flow continues to be strong. As many other VCs focus increasingly on late stage deals at high pre-money valuations, we are seeing a large number of high potential early stage investment opportunities. Two of the more promising are a company developing a novel approach to the flu vaccine and another company developing a device to help with the safety of the mother and unborn child in the last trimester of pregnancy. We will let you know if/when we commit to make investments in these or other companies.

We encourage you to visit our website (vcapital.com) to learn more about our current portfolio and investment opportunities.

We appreciate your continued support of VCapital. Please feel free to reach out to either one of us should you have any questions.

Sincerely,

Leonard Batterson
Chairman & CEO
(312) 203-6820
lbatterson@vcapital.com

Jim Vaughan
Managing Principal
(312) 450-4363
jvaughan@vcapital.com