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Hungarian Private Equity and Venture Capital Association

Jubilee 25 Years Yearbook

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JUBILEE 25 YEARS YEARBOOK

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Hungarian Private Equity and Venture Capital Association

Jubilee 25 Years Yearbook

2016

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2011-2014	NIKOLAUS BETHLEN

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Levente Zsembery
President, 2015-

About HVCA

The Hungarian Private Equity and Venture Capital Association (HVCA) represents virtually every major source of funds and expertise of private equity in Hungary and is dedicated to promoting the venture capital and private equity industry for the benefit of funds, entrepreneurs, private equity professionals and the economy as a whole.

The Association aims to promote the development of the industry, and to create a set of rigorous professional and ethical standards for its member companies to follow. The members involve all the important investors or advisors in the sector dealing with non-quoted companies.

The Association provides a regular forum for the exchange of ideas among members, high-level discussions on the topical issues of venture capital and private equity industry and the future trends. As the most and only important representative of the industry it is in constant discussion with the financial and legislator institutions of the Hungarian State and with other professional organisations.

Executive Summary

Levente Zsembery

The Hungarian venture capital industry between 2011 and 2016 Trends and market players

Venture capital

The Hungarian venture capital and private equity industry has seen major changes during the period ranging from 2011 and 2016. Before this time the domestic market had been dominated by CEE focused venture capital funds. Although they have taken several businesses to international success, their investments were sporadic in Hungary. There were only few VC transactions in the country and, pursuant to the standard industry practice, only a fraction of these were visible for the Hungarian entrepreneurs. The number of transactions failed to reach the critical mass, and most entrepreneurs were not prepared to cooperate with venture capital funds. As a result, venture capital did not have a chance to become a widely used financing instrument in Hungary.

The primary factor that influence the change in the market was the JEREMIE Programme launched by the European Union. Both the number and importance of venture capital funds financing early-stage ventures increased significantly, the infrastructure and ecosystem for supporting start-ups was established, including business incubators, accelerators, co-working offices and start-up competitions. In addition, the number of companies actively seeking venture capital has boomed.

The first JEREMIE Programme co-financed by the EU and private investors was launched in 2010. Under this programme, eight venture capital funds were established followed by the establishment of ten additional funds in 2012, including four dedicated seed-financing funds. Further, eight and two venture capital funds were set up in the third and fourth phase in 2013 and 2014, respectively. By the end of the period, there were 28 EU co-financed venture capital funds looking for investment opportunities in the market.

The fast sequence of JEREMIE Programme's phases had a mixed reception in the industry. Although everyone welcomed the availability of ample funds for financing innovative early-stage companies, many experts expressed their concerns mentioning that the abundance of the sources could also potentially jeopardise the success of the programme. There is little use in having a multitude of funds available if the number of start-ups ready to partner with a financial investor fails to increase proportionally. Several experts were concerned that the oversupply of venture capital and the pressure on funds to invest will result in investment in a large number of start-ups with no real business potential.

The main problem was the similarity of investment policies followed by the different funds. Twenty-three out of the twenty-eight funds active in the market financed the same early-stage companies in terms of geography and lifecycle. There was only a single fund authorized to invest in Central Hungary, that is, in Budapest and Pest county, and only four funds dedicated to seed financing. The amounts invested were also similarly distributed. Sources provided by the JEREMIE funds were added up when calculating the limits (like maximum investment size), and although many companies gained access to round 'A' financing, those who successfully utilized this amount had to seek foreign investment partners to raise the next round of capital (EUR 3-5 million).

Fierce competition and similarities of investment policies created challenges, especially for JEREMIE funds set up during the subsequent waves of the programme. Some changes occurred, for example, several funds were taken over by other investment companies. The investment period of JEREMIE funds was closed at the end of May 2016. As announced by the Ministry of National Economy, which supervised the programme, nearly HUF 130bn was invested into 350 portfolio companies under the programme.

Venture capital funds financed by private investors focusing on Hungary were also launched like Day One Capital, Hungary's first private seed fund.

In addition to co-investment and private venture capital funds, state-owned investment funds using public funds were also set up. The most

***Table 1** – Venture Capital Fund managers participating in the JEREMIE Programme*

Jeremie 1	Jeremie 2	Jeremie 3	Jeremie 4
• Primus Capital • Morando • Finext • Euroventures • PortfoLion • DBH Investment • Central Fund • X-Ventures Alpha (formerly known as BNV Equity)	**Seed funds:** • Carion (formerly known as Core Venture) • Első Magyar Venture Capital Fund Management Ltd. • Kaerous (formerly known as Kairos) • GB & Partners (formerly known as Prosperitás) **Growth funds** • X-Ventures Béta (formerly known as New York) • Finatech (formerly known as X-Tech) • Venturio • Bonitás • Kaerous (formerly known as Kairos) • GB & Partners (formerly known as Prosperitás)	• Alliance Jura-Hongrie • Perion Invest • Tőkepartner • Dinamo Ventures • ABC (formerly known as Hemisphere) • PBG FMC • Valor Capital • Carion Ventures • (formerly known as Core Venture)	• Gran Private Equity • Garangold Investment Investor Ltd.

active one was Széchenyi Capital Fund Management Company, which invested in over a hundred ventures until the end of its investment period in 2016. Due to the high number of transactions, they could not give as much professional support as the private venture capital funds managers, however, the state-owned investment funds provided access to funding for many companies that had no chance to gain funding from private or public-private co-investment venture capital funds.

Having realized the risk posed by the oversupply of capital, several fund managers set up business incubators. The first incubator, Kitchen Budapest, was launched in 2007. In the period after 2011, many other start-up incubators were funded with the aim of identifying promising ideas and teams and providing them with strategic support and funding at an early stage of their lifecycle. Besides fund managers, the incubator landscape attracted an increasing number of other players, too. Although part of these early initiatives were discontinued later, they made a great contribution to the development of the Hungarian institutional framework.The Incubator Report, published by BDO in 2014, introduced 11 active market players in detail[1].

The Gazella Programme established in the second half of 2013, also aimed to support the development of the business incubators. The initiative launched by the National Innovation Office (NIH) envisaged the establishment of four business incubators using EU funds. Although the four candidates were selected, the programme was eventually suspended.

The incubator programme launched in 2016 by NIH's successor, the National Research, Development and Innovation Office (NKFIH), has been more successful. This programme aims to promote the development of the institutional framework and provide early-stage companies with access to funding in regional towns. Some of the eight selected candidates were previously running business incubators, but most of them are new players in the market. This is expected to give momentum to the start-up community in the countryside as well.

The industry has seen major changes over the past five years. Many new players entered the market, several of them following international best practices. Although the number of exits is still behind expectations, there are many promising stories indicating that venture capital financing might become a common instrument of corporate financing in Hungary.

The continuation of the JEREMIE Programme is still an open issue. The amount of available venture capital declined by the end of May 2016. Although both the European Union and the Hungarian government decided to continue the programme, the details are yet to be known.

Private equity

The number of investment targets attractive for private equity funds has always been limited in Hungary. First, after the privatization of state-owned assets in the early 1990s, most state-owned companies were either discontinued or were purchased by strategic investors, and only a small number were acquired either by Hungarian private investors or financial investors. Second, a major portion of larger Hungarian private businesses are family owned and the idea to involve a financial investor has seldom occurred to founding families. Third, as a result of limited growth opportunities due to the small size of the internal market, many Hungarian businesses never reach the size that would make them an attractive target for financial investors. As a result, the private equity industry has historically been less active in Hungary than in larger markets of the region, particularly Poland and the Czech Republic.

In the period between 2011 and 2016, the Hungarian market was shrinking compared to previous years both in terms of the number and volume of private equity transactions and in terms of the number of private equity investors based in Budapest, a number that has decreased. The past few years saw only seven high-value transactions. Although their combined value significantly exceeded the size of the venture capital market, the overall role of institutional private equity in corporate financing has been declining.

At the same time, several regional private equity fund managers (Advent, Argus, Bancroft, Riverside) decided to close their offices in Budapest due to the lack of portfolio companies in Hungary.

Statistics

HVCA has published regular quarterly reports on the trends of Hungarian venture capital and private equity markets since the first quarter of 2014. Given the limited role of private equity in Hungary, these statistics primarily reflect activities in the venture capital industry. Based on these statistics, Hungary had 107, 132 and 85 transactions in 2014, 2015 and the first half of 2016, respectively. Of these transactions, 12, 8 and 3, respectively, were buyouts carried out by private equity investors, while the rest of the deals were concluded by venture capital investors.

The years 2014, 2015 and the first half of 2016 saw 8, 15 and 4 exits, respectively, in the Hungarian market according to HVCA statistics.

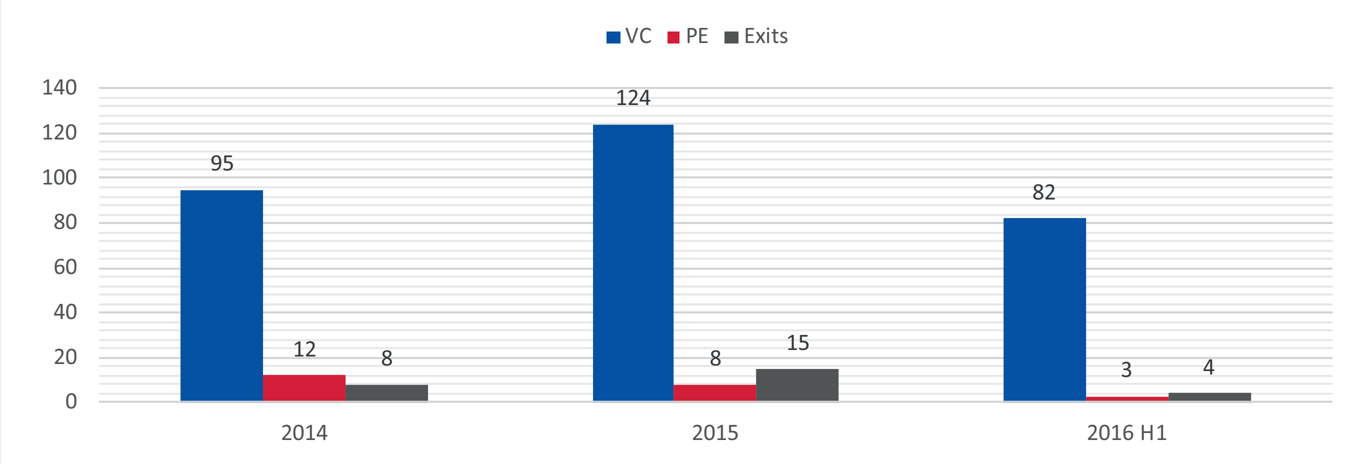
In a breakdown by sector, Business and Industrial Products took the lead with 69 transactions, followed by Life Sciences (49) and

***Table 2** – Private equity transactions in Hungary at a value of over EUR 100 million, 2011-2016*

2011	Provimi Pet Food	Advent International	188 m€
2011	BorsodChem	VCP Vienna Capital Partners + Wanhua	400 m€
2011	Révai Nyomda	GED PE; Pollstar Group	100 m€
2014	Euromedic	Ares Life Sciences	800 m€
2015	TriGránit	TPG Real Estate	500 m€
2015	Partner in Pet Food (Provimi Pet Food)	Pamplona Capital Management Llp.	315 m€
2016	Waberer's	Mid Europa	na

[1] http://frazir.com/inkubatorjelentes

Figure 1 – Number of venture capital and private equity investments and exits in Hungary between 2014 and H1 2016



Consumer Services (35). In terms of total value, Business and Industrial Services was the most active sector (HUF 42.3bn), followed by Energy and Environment (HUF 23.3bn) and Business and Industrial Products (HUF 7.9bn)[2].

HVCA

Market changes had an impact also on HVCA's operation. In line with both the increase of the number of venture capital investors among full members of HVCA and the decline of the weight of regional private equity funds and fund managers, HVCA has been playing an increasingly active role in Hungary. With the implementation of the Alternative Investment Fund Managers Directive (AIFMD) in Hungary, fund managers and funds are now subject to broader supervisory control, which requires regular consultation between HVCA and the National Bank of Hungary (NBH), which acts as a supervisory authority. Fund managers supervised by the National Bank of Hungary established a Back-Office Roundtable. Cooperation between HVCA and ministries preparing new legislation has become closer in particular with the experts of the Ministry of National Economy.

HVCA also has launched several programmes to support the investment activities of its full members. On the one hand, it has initiated a dialogue with Hungarian universities and research institutions to facilitate the utilization of universities' academic achievements (university spin-offs). On the other hand, it has launched joint programmes with several companies and organizations (M27 ABSOLVO, AMCHAM, HIPAVILON, etc.) and held conferences to familiarize venture capital with as many businesses as possible. It has launched educational programmes at universities and secondary schools and organized the so-called VC Grill, an annual summer event for the start-up community. The associated members of HVCA, who provide consulting services, have played an important role at these events.

[2] www.hvca.hu/statisctics

Table 3
Number and value of venture capital and private equity investments in Hungary between 2014 and H1 2016

Sectors	No. of transactions	Amount (HUF million)
Business and Industrial products	33	7 913
Business and Industrial services	69	42 316
Chemicals and materials	5	381
Construction	1	43
Communication	15	2 349
Computer and consumer electronics	29	4 054
Consumer goods and retail	31	4 684
Consumer services	35	5 271
Energy and environment	32	23 352
Financial services	5	560
Healthcare services	1	210
Life sciences	49	6 374
Real Estate	2	601
Transportation	12	1 982

4. table
The number of HVCA members, 2012 – 2016

Members	2012	2013	2014	2015	2016
Full	23	24	25	24	27
Associated	39	48	47	43	43
Individual	7	9	12	9	12
In all	69	81	84	76	82

The number of HVCA members has significantly increased over the past five years. HVCA is not only one of Hungary's largest professional association, but it is also one of the most active private equity and venture capital associations in Central and Eastern Europe.

The re-positioning of its annual conference held early in the summer has improved the name recognition of HVCA both in Hungary and internationally. This event has been organized every year for more than two decades. Since 2013, it has been targeting not only a Hungarian audience but the region as a whole. Over the years, it featured keynote speakers including George Soros (2013), Nouriel Rubini (2014), Georg A. Papandreou (2015), Joseph Andrews and András Simor (2016). The ratio of foreign participants has been on the rise, and HVCA conferences have generated more coverage both in the Hungarian and in the international media from year to year. Thanks to the speakers and sponsors involved, the HVCA Annual Conference has grown to become a brand both in Hungary and the CEE region.

Dr. Cornelius Mueller
Research Director,
Invest Europe

About Invest Europe

Invest Europe is the association representing Europe's private equity, venture capital and infrastructure sectors, as well as their investors. Invest Europe aims to make a constructive contribution to policy affecting private capital investment in Europe. It provides information to the public on its members' role in the economy. Invest Europe's research provides the most authoritative source of data on trends and developments in the VC/PE industry. Invest Europe is the guardian of the industry's professional standards, demanding accountability, good governance and transparency from our members.

Invest Europe is a non-profit organisation with 25 employees in Brussels, Belgium. For more information please visit www.investeurope.eu

5 years of venture capital of European perspective

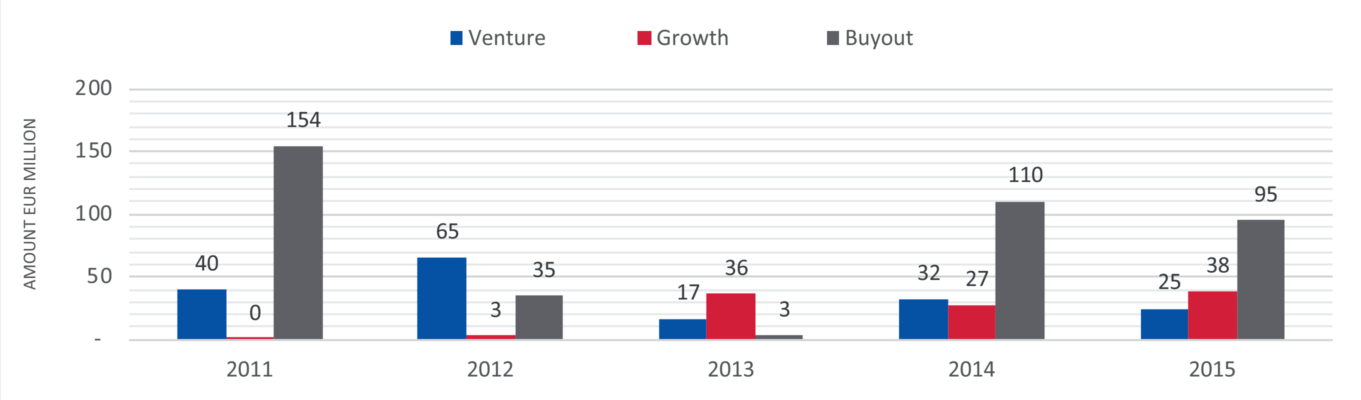
Dr. Cornelius Mueller

Private equity and venture capital investment into Hungary-based businesses has increased in the five years since the Hungarian Private Equity and Venture Capital Association's (HVCA) 20th anniversary. While the CEE region private equity and venture capital market grew on average 7% a year between 2011 and 2015, Figure 1 shows that investments in Hungary developed strongly in the last two years. The increase in value was driven by larger buyout transactions, as well as a robust trend in growth investments that started in 2013.

Venture capital investments continue to dominate the share of the number of companies that receive investment[3]. The proportion of venture capital investment in the Hungarian market is consistently higher than the corresponding figure for the CEE region as a whole for the period between 2011 and 2015 (see Figure 1.1). This is also

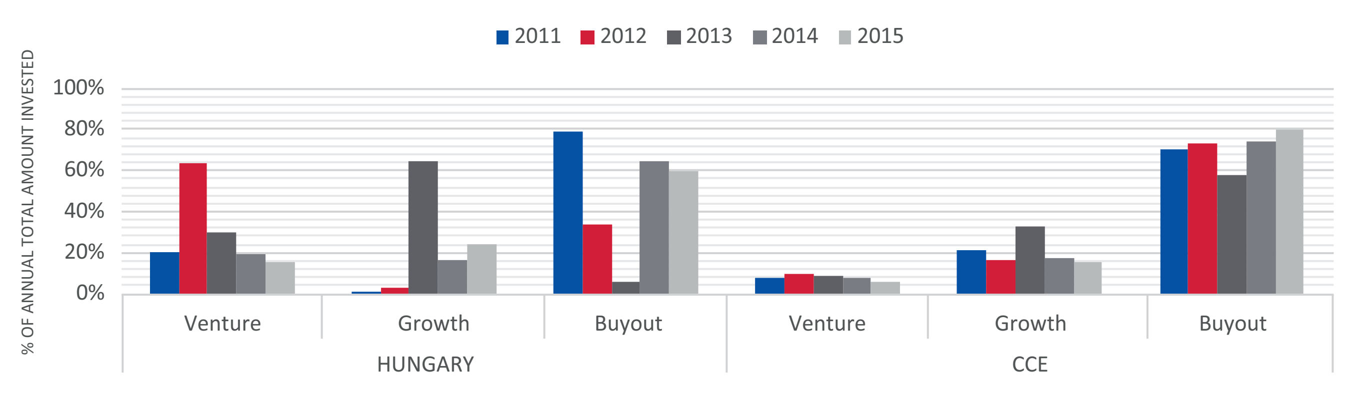
[3] Only investments by formal venture capital funds are considered here. Accelerators, incubators and business angel investment are not captured.

Figure 1: *Investments in Hungarian companies by stage and amount*



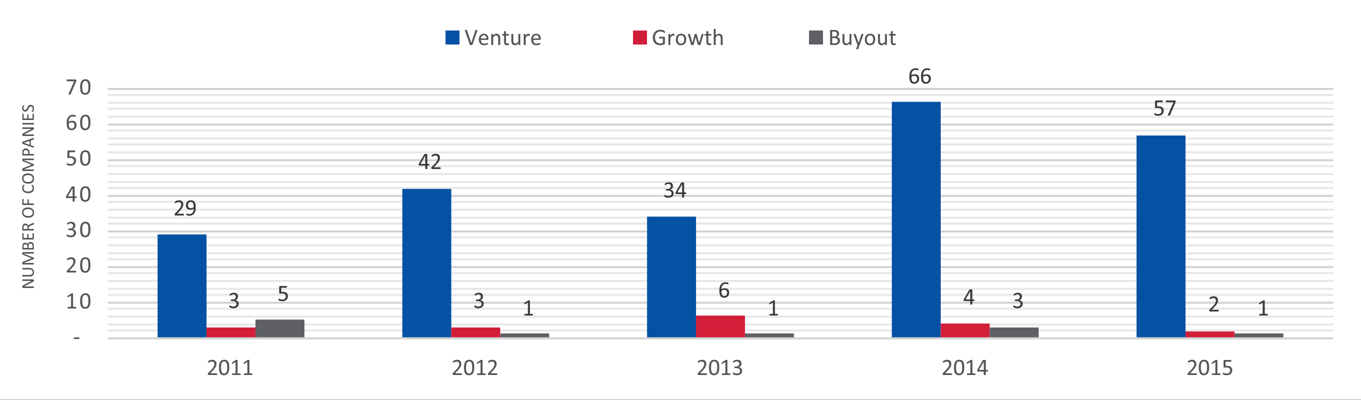
Source: Invest Europe\PEREP_Analytics

Figure 1.1: *Investment by stage and % of annual total amount invested*



Source: Invest Europe/PEREP_Analytics

Figure 2: *Investments in Hungarian companies by stage and number of companies*



Source: Invest Europe\PEREP_Analytics

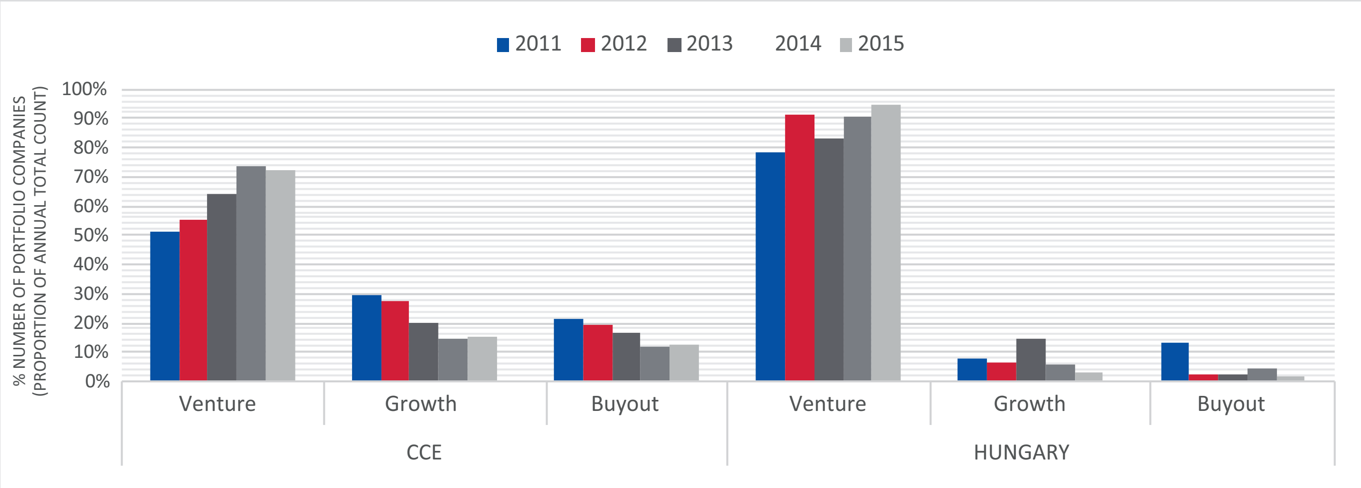
reflected in the number of portfolio companies and their proportion of the annual total (see Figure 2.1).

Furthermore, when expressed as percentage of GDP, venture investments into Hungarian businesses reached a significant level when compared to other European markets (see Figure 3).

Absolute investment levels by private equity and venture capital also mark out Hungary as among the largest markets in the CEE region over the past five years. Due to the high impact of larger buyout investments, we recommend reviewing each market's investment profile as it is outlined in Invest Europe's dedicated CEE Report each year.

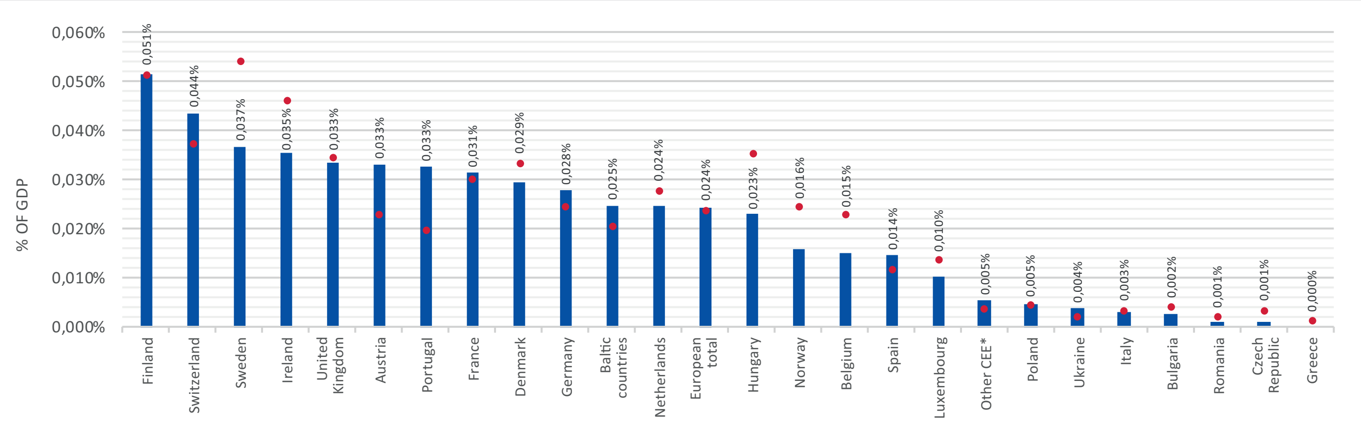
The CEE region accounts for about 5% of overall European investment activity. The differences in activity across the major regions in Europe are summarised in Figure 5. Variations in the structure of the private equity and venture capital markets in Europe become more visible when measuring investments as a percentage of GDP. For example, regions like DACH and Southern Europe, in which local bank sectors traditionally fund small and medium-sized companies, show lower levels of investment (according to this metric) than the UK & Ireland and the Nordics, where there are also large domestic bases of institutional investors that invest in private equity and venture capital funds.

Figure 2.1: *Investments by stage and number of companies (proportion of annual total)*



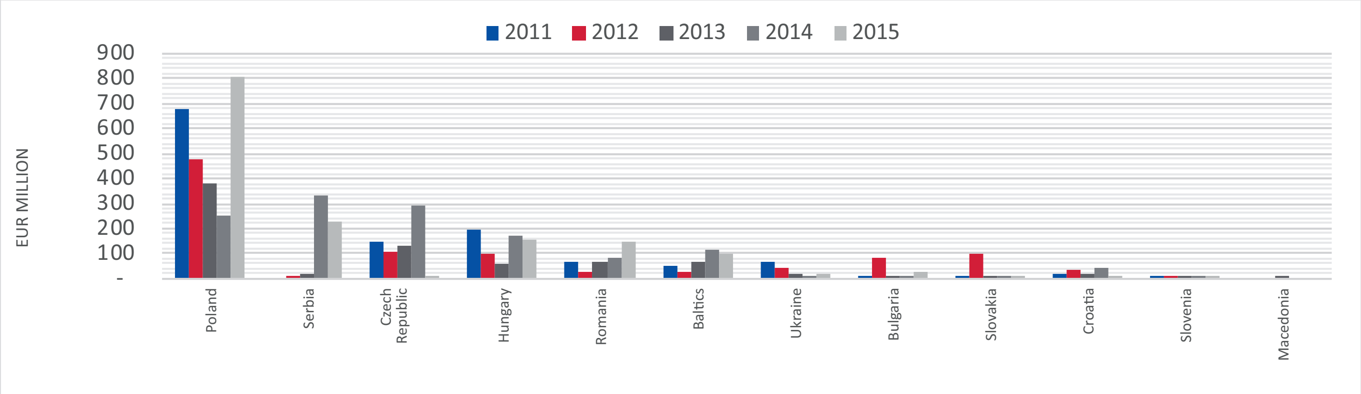
Source: Invest Europe/PEREP_Analytics

Figure 3: *Venture investments by location of portfolio company as % of GDP in 2015 and annual average 2011-2015*



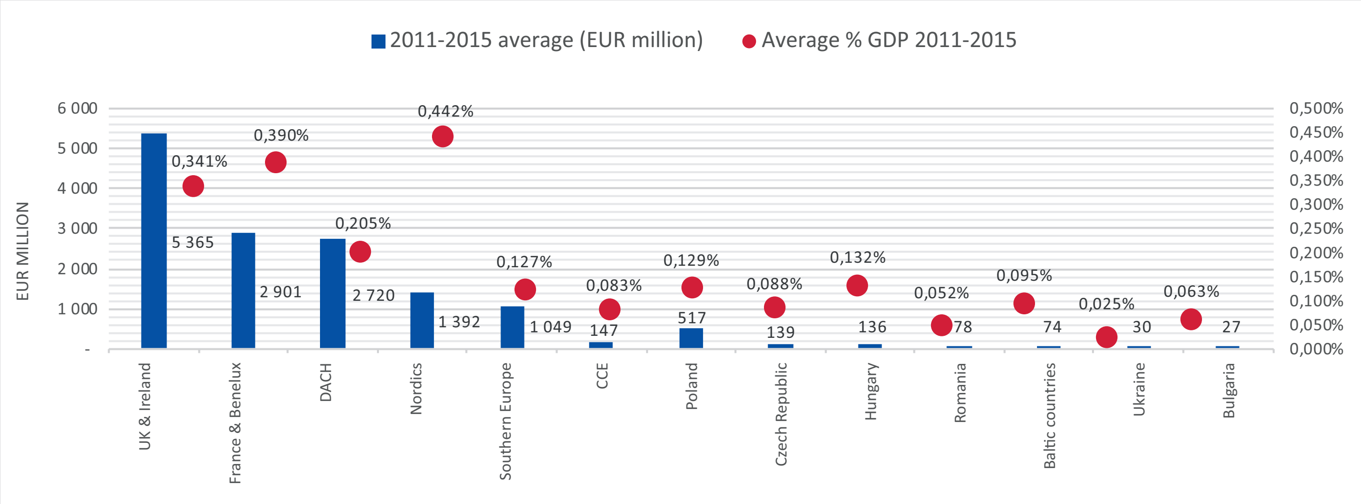
Source: Invest Europe\PEREP_Analytics

Figure 4: *All private equity investments - by location of portfolio company*



Source: Invest Europe\PEREP_Analytics

Figure 5: *All private Equity - Average annual investments 2011-2015 by amount and % of GDP*



Source: Invest Europe\PEREP_Analytics

The ability to raise funds from investors is also a main driver for the strong differences in distribution of assets under management that appear when looking at Figure 6.

The availability of institutional capital and resulting structural differences between European funds and those from the CEE region more specifically are shown in Figure 7. With access to large international capital pools, funds from the UK, France and the North of Europe are more frequently able to attract pension funds and insurance firms. For fund managers in the CEE region, pan-European and domestic public pools of capital in the form of government agencies remain an important source of capital. However, as shown in Figure 7, a diverse mix of institutional investors has invested in funds managed in the CEE region over the past five years.

Looking at divestments in the Hungarian market (see Figure 8), the predominant exit route by amount is via a trade sale (73%). This is also the case for the CEE region as a whole (53%). However, the second most important exit route for the CEE region (i.e. sale to financial institution, 17%) is almost never pursued in Hungary.

Figure 6: *Assets under Management in Europe – All Private Equity*

1 UK & Ireland
€266bn

2 France & Benelux
€131bn

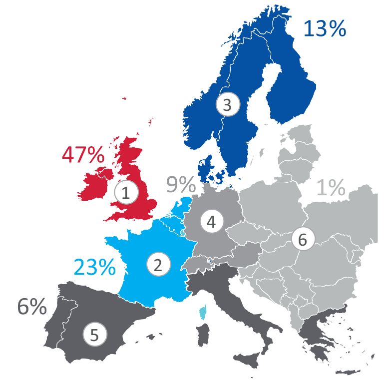
3 Nordics
€72bn

4 DACH
€53bn

5 Southern Europe
€34bn

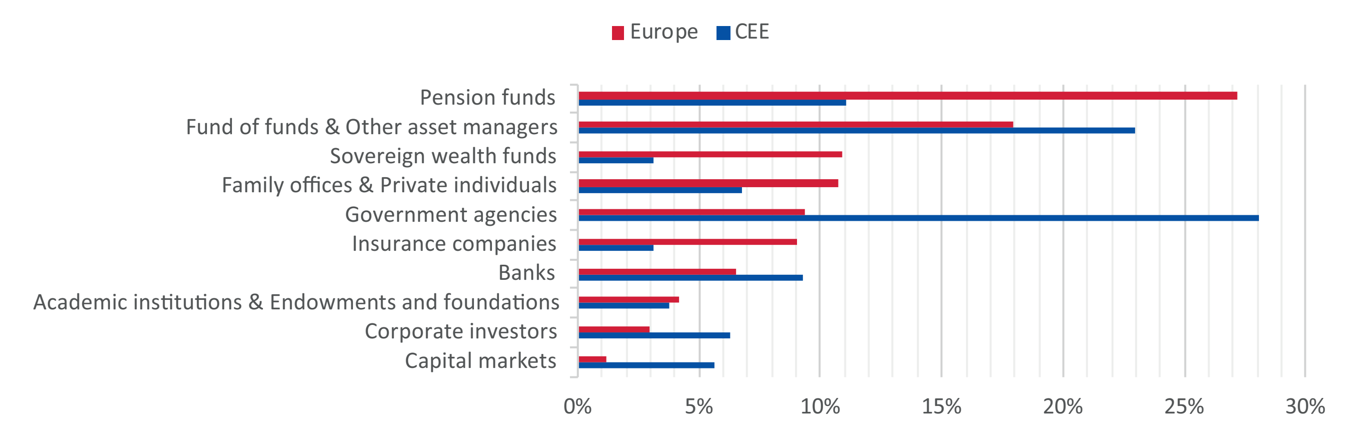
6 CEE
€8bn

Source: Invest Europe / PEREP_Analytics
DACH: Austria, Germany, Switzerland / Southern Europe: Greece, Italy, Portugal, Spain /
Nordics: Denmark, Finland, Norway, Sweden / CEE: Central and Eastern Europe



Source: Invest Europe\PEREP_Analytics

Figure 7: *Institutional investors in private equity funds managed from Europe and the CEE region 2011-2015*



Source: Invest Europe\PEREP_Analytics

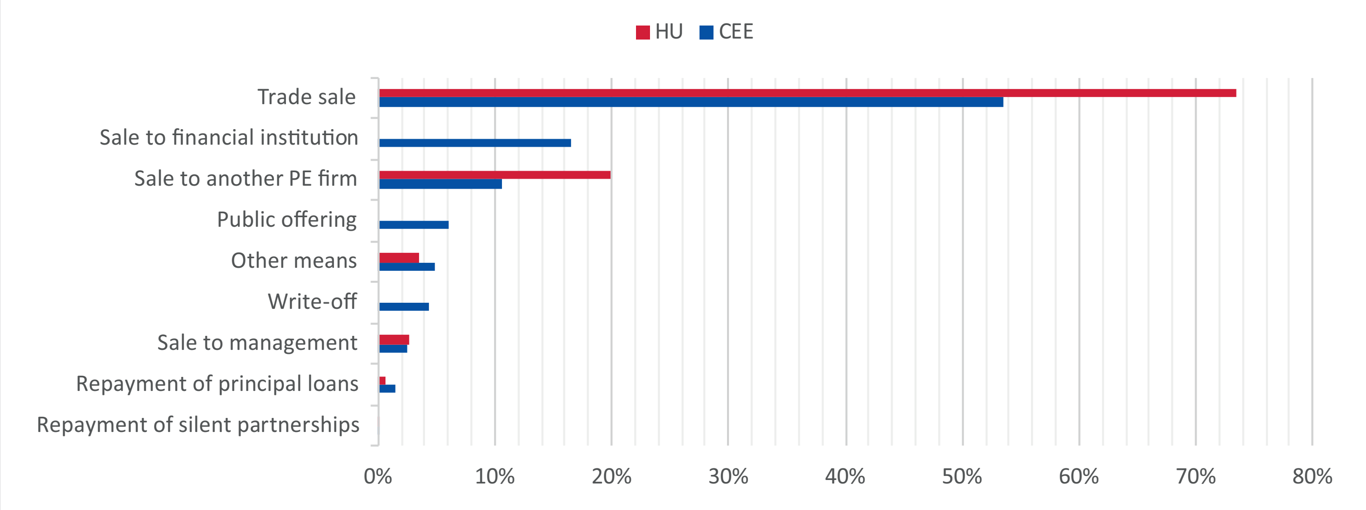
When looking at the divestment routes by number of companies, and comparing the corresponding proportion to the overall CEE region (Figure 8.1), the preferred exits in the Hungarian market appear to be quite different. Sale to management is the principal exit route in Hungary, representing about 50% of the total number of companies divested in the last five years. The second and third most common exit routes in Hungary are repayment of principal loans (24%) and trade sale (20%).

To ensure the most robust statistics, the data discussed in this feature is predominantly collected directly from the fund managers investing in the region. A close coordination and collaboration between national associations and Invest Europe helps minimise the work and duplication needed by fund managers to input data into different systems. Another benefit of using a single database for this purpose is the ability to apply a single methodology that assures meaningful comparison of the private equity and venture capital activity data across countries.

Invest Europe and its partner national associations are further developing this approach through the European Data Cooperative (EDC) initiative. In addition to fundraising, investment and exit data, fund performance and economic impact data will be added in the future. This will allow Invest Europe and the industry to better demonstrate private equity and venture capital's track record and benefits to an audience which includes policymakers, institutional investors, regulators and academics.

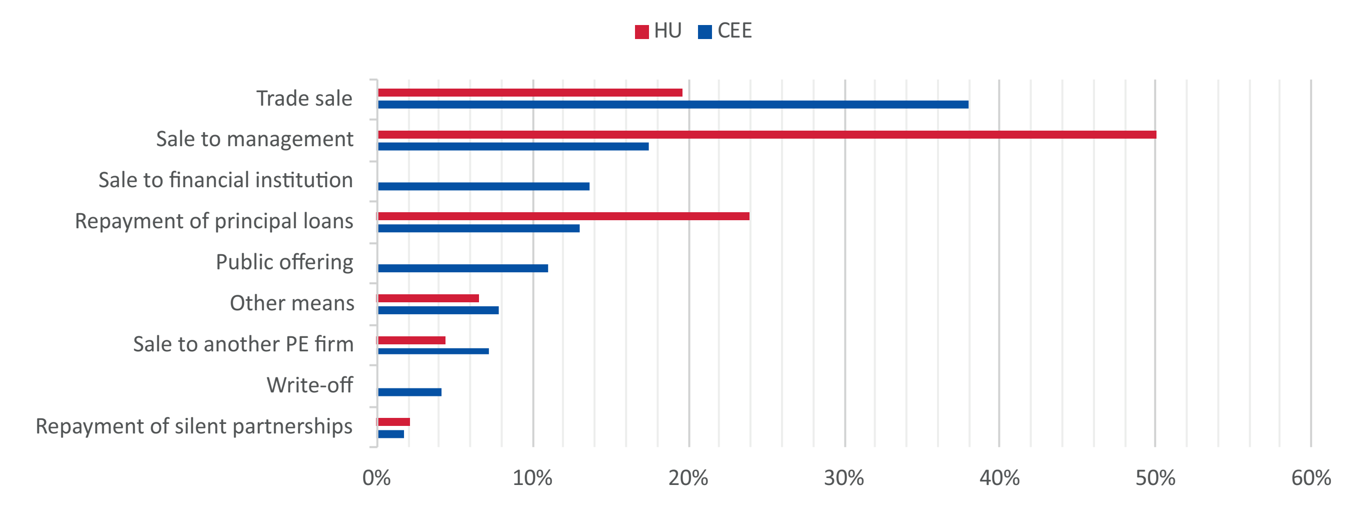
In summary, the Hungarian and CEE markets show steady development of investment, which frequently corresponds with the macroeconomic conditions and prospects of the region. Scaling up and developing the domestic base of fund managers and their access to international capital pools will be key in the future. To achieve this ambition, Invest Europe is committed to working with its members and partner associations in the region in order to track the market and educate with robust statistics.

Figure 8: *Divestments, amount divested at cost (%) by exit route*



Source: Invest Europe/PEREP_Analytics

Figure 8.1: *Divestments, number of portfolio companies (%) by exit route*



Source: Invest Europe/PEREP_Analytics

Attila Balogh

Personal Portrait

Attila Balogh is Chairman & CEO of Partner in Pet Food (PPF) and joined the company eight years ago. During that time he has returned PPF to profitability, twice overseen a management-led buy-out of the business, expanded its geographic presence to 37 countries and dramatically increased sales organically through a successful programme of new product development and via strategic acquisitions. Since joining PPF, the company has reported record profits each year.

Attila has held senior business roles in both the United States and Europe at a range of retail, and FMCG companies, including at Tchibo, Hero and General Electric. Attila spent 11 years at Tchibo, with six of those years as CEO of the company's international business, returning it to profitability and growth. In total, Attila has spent over 20 years working for privately-owned businesses, including private equity backed businesses, and is a turnaround and growth expert with a track record of transforming underperforming companies to create significant shareholder value.

About PPF

PPF operates across 37 countries, supplying many of Europe's top retailers. The company has grown rapidly over the last six years to become one of Europe's leading pet food producers.

In 2016 PPF produced enough pet food to feed approximately 2.5 million cats and 2 million dogs for a year. Under combined private equity and management ownership, PPF has thrived.

Private ownership has allowed PPF to invest for growth through developing leading R&D capabilities, strategic acquisitions and expanding into new markets. PPF is a prime example of a successful, privately owned European business that has expanded to become a leader in its sector.

Interview with Attila Balogh

Can you just say a little bit of your history with Private Equities? You worked with a number of PEs in the past.

Yes, I've worked with three PE companies so far, all with my current company: Partner in Pet Food. First was Permira for about 2.5 years, and Advent for about 4 years and now Pamplona for the last 1.5 years. Before that I was with General Electric in America and also with Tchibo and Hero which are German family owned companies. Therefore I have experience in all the sectors, public, private family, and private equity. I have to say that my experience with PEs so far has been very positive. They've all had different approaches but they have all been very successful and very supportive while working with them.

From the perspective of a CEO, what would you say, what is the most significant difference between a strategic investor and a PE investor?

Surprisingly many times people think that PE is only looking at short term, but my experience is that this is not true. They are looking at the longer term similar to a family owned company or quite often a publicly owned company. The investment period, if things go well, is typically from 3 to 5 years for a PE company but they do have to look at the long term, because when it comes to selling their stake they have to be able to demonstrate not only how they built value in the past but that there is future value to be realized over the next 5 to 7 years. If you just extract everything during your stewardship it is impossible to successfully sell. That is why it is important for them to look at the long term as well.

The strategy development for the PE starts with the due diligence that they do prior to purchasing and most PE think 'if you don't have an exit, then don't buy the company'. So when they buy the company there already has to be an investment thesis of the strategy during the stewardship of the PE with the acquired company. There also has to be an exit thesis as well. Could be the same strategy, or could be that it's a modified strategy or a totally mixed strategy - it depends on the development phase of the business. And with PPF when I joined together with my team we defined a new strategy which we've been successfully implementing.

With Advent we accelerated the investment in the company. Many people think PEs don't invest into companies. With Advent we doubled the level of investments and that of course led to accelerated profits. But we had the same strategy and when Advent sold PPF to Pamplona, then we kept the strategy but focused on different areas as well. We found that the strategy although developed earlier on, was still relevant. In all cases management worked together with the PE company to make sure we had a valid strategy during their stewardship. But it was also important to have an exit thesis as well.

What's important is that the exit story is the truth. If it's not true shortly after buying, the PE companies are often disappointed and management is often disappointed and probably not around shortly thereafter as well. If the story is the truth, that is the best case because they can work on enhancing shareholder value.

What would you say to companies that are currently considering selling part of the business to a PE company or what's your recommendation, what to watch for or what to expect from that relationship with the PE?

I have been working with a PEs for the past 8 years and I think it's very positive if the interests are aligned between the PE and management. If management is capable and confident and they can take decisions and succeed then it is a really perfect marriage for that period of time. I would make sure that you understand the specific needs of the PE companies. They do have slightly different areas of focus, let's say different personalities. Some are more strategic, for example, others are more operational. Management has to understand their priorities and needs and at the same time achieve the present goals. If they are successful with that, it can be a positive relationship.

PE also has a vast network which in my case for the three companies I worked with, they opened their network up as well. That has helped us strategically, in purchasing and distribution and in understanding the markets in many areas. So it's important that you are just honest with each other and work to the same goal. Open communication is a critical success element as well.

In summary, working with private equity can be a positive experience if goals are clear and mutually agreed. Significant shareholder value can be created along with building great companies and having fun along the way.

Attila Balogh was interviewed by:
Balázs Csűrös, Partner, Advisory M&A Transaction Services, Deloitte Co. Ltd.

Dr. Balázs Vinnai

Personal Portrait

As General Manager of Misys Digital Channels, Balázs is responsible for retail digital channels business.

Balázs Vinnai is known as the CEO of IND Group, a company he established in 1997. IND specialised in the innovation and development of digital banking solutions, grew rapidly to a market leader in the EMEA region and was acquired by Misys in 2014.

Since 2007 Balázs has also held the position of Vice President in the Software Development and Innovation Committee of the ICT Association of Hungary (IVSZ).

Interview with Dr. Balázs Vinnai

You have to learn how to operate as a company

Balázs Vinnai, General Manager of Digital Channels at Mysis, believes that the greatest challenge for Hungarian start-ups is to realize that they need to think of themselves as a company in order to secure continued growth. And this kind of thinking can be facilitated from the outside, for example, by a financial investor.

This piece of advice comes from a trusted source. As the founder of a garage company himself, Vinnai had an eye on the international market from his first years in business. His start-up, IND Group, "grew up" as a supplier to Brokat Technologies of Germany. The group's history spans 15 years, a fairly long period in today's start-up landscape, and includes two crises. Partnering with international companies from the outset, IND was directly affected both by the dot.com bubble and by the financial crisis. Vinnai claims that these crises provided IND with an opportunity to step to the next level. Acquiring Brokat Technologies, which went under when the dot.com bubble burst, initially seemed to be a surprising move, but eventually it gave IND access to international markets, while the financial crisis redefined the market environment increasing demand for digital technologies, especially mobile banking technologies.

Starting from 2007, the growth of IND was fuelled by private equity investor Euroventures that participated in the company's operation for more than six years. When asked about the reasons for a capital injection, Balázs Vinnai said it was clear that they had to raise external capital to restructure their revenue streams and shift from fulfilling one-off orders placed by banks and service type assignments to product-based licence sales. "We were a start-up based in Miskolc with an office in Budapest's sixth district. Colleagues from Miskolc practically lived in the office. During this period, we had to learn how to think strategically and not give up everything just because a particular order would increase our sales and profit. Partnership with Euroventures has clearly contributed to the establishment of this kind of strategic focus, which I'm sure was a major success factor for IND."

Partnership with a private equity investor

One of the biggest challenges in cooperation was understanding each other's motivations. This is not something that can be learned at university, and there was no available business model to follow at that time. There were some other businesses relying on external capital in Hungary, but they were either the spin-offs of some multinational companies or followed a highly conservative business model. "We expected, for example, that our partner will check the key figures in our books. But they were never interested in that. Instead, they wanted to know the amount of our revenue coming from software sales, the ratio of exports, the size of our customer base and our potential to acquire new customers," says Vinnai.

He believes it is important to grow your profit and grow your sales, but overall market value is the key. It does not matter how it changes over the years, whether it is high or low on a given day. The goal is to have it at the highest level upon the exit.

Key to success

According to Vinnai, "We both had a common goal. Euroventures wanted to transform our rather disorganised Hungarian start-up into a financially transparent company in international terms and we were strongly committed to this transformation. In hindsight, I have the impression that they did this very cleverly as we never felt under pressure to move forward in any specific direction. They only set a framework to help us make the right decision."

Vinnai continues, "At that time, we were a step ahead of the Hungarian market and many people did not understand our vision and considered spending significant amounts on it to be a waste of money. To prevent our company from becoming a one-man show, we spent a lot, for example, on hiring a competent and experienced management team whose members joined us from banks and major auditing companies. We spent more than others, and we really needed venture capital type of support to become an internationally acknowledged supplier to UBS or Deutsche Bank." Euroventures were important for IND not only because it was an owner, but also because their financial transparency and reporting system were much closer to international standards than IND's initial practices.

Exit

Vinnai believes that a start-up relying on PE support should also keep the end of the investment period in mind. "Today I know that if you get funds from an investor you need to be aware that your partnership will end one day, preferably to your mutual satisfaction. Around 2013, we also had to consider whether to raise the next round of investment or look for a strategic investor." The end of the investment cycle coincided with IND gaining market attention. "After 7 years, our marketing strategy focused on the necessity of digital transformation, the importance of customer experience and innovation and targeting primarily opinion leaders started to bear fruit. Top market experts knew our products and were talking about them. IND was always featured in interviews and professional reports on digital technology and it gained visibility in the international landscape. Together with our competitors, we became the focus of attention. I believe this focus was slightly more than was actually deserved by these companies."

Misys

A company with 30 years of history and a broad-based software offering for the financial services sector, Misys was looking for an opportunity to reinvent itself. Acquiring IND gave Misys an opportunity to take an active part in digital transformation and enhance its product portfolio with innovations. Vinnai believes that this has helped the company learn a valuable lesson based on the practical experience that achieving cultural change is even more difficult than adopting a new strategy. You have to understand each other's motivations and goals, implement them, and adjust the entire organization accordingly. Vinnai admits that this period has also brought the company losses, especially that of intellectual capital. "It is easy to explain these things clearly in retrospect, but it was far from being clear back then. It took long months and lots of discussions to find out which steps were taken in the right direction and how the company progressed with each step."

The marketing strategy of Misys followed the same growth path as the company itself. Instead of trying to compete with IBM's marketing spending, in the first round Vinnai and his team targeted bloggers and the IT opinion-forming community emerging in the 2000s and sought to position the company and its products in this segment. "Their analytic and our technology brands were presented together, a clear win-win for both parties. This made our products visible and valuable for the target audience. Initially, we were talking specifically about our products in every publication and placement because it was important for us not to have the reputation of being just a bunch of young guys who develop software as a hobby. When this message was understood by the market, we changed our sales focus and started to sell the goals, rather than our products that can help reach these goals. We discussed future directions for the industry with the final message that the products to support these directions are available from us. The third and most difficult step was to shift our focus from our own customers (that is, the needs of banks) to our customers' customers. We make ordinary people's lives and finances easier by selling software to banks. These two things were often in conflict with each other. I mean that the banks' vision was not in line with their customers' expectations, and we always sought to satisfy the latter. This so-called 'outside in' strategy was fully taken over by Misys under the name 'frustration-free banking'."

When asked to give a piece of advice to those currently looking for the next step at an early stage of the road he's been through, Balázs Vinnai said that the most important thing to keep in mind is that the next 20 years will clearly be about intellectual capital. "The digital world is about intellectual capital. You don't need to have millions of dollars to launch a business. Market entry barriers are disappearing in the industry (manufacturing, logistics, infrastructure, etc.) and hundreds of millions of consumers can be reached immediately. This gives the next generation a great opportunity to create something unique and special."

Dr. Balázs Vinnai was interviewed by:
Margaret Dezse, Partner, Transaction Advisory Services
Ernst & Young Advisory Ltd.

Szabolcs Valner

Personal Portrait

Szabolcs Valner an Internet serial entrepreneur, including the founder of Vatera.hu. Currently helping to build Budapest-based startups, focusing on the global market, as a co-founder, investor, consultant.

Interview with Szabolcs Valner

Vatera story

Vatera was a brainchild of a member of the class of 1999 at Harvard Business School. A Greek-American student came up with the idea of copying eBay into the Central and Eastern European region. The original seed investor was a fund managed by Edgar Bronfman Jr, CEO of Vivendi-Universal and heir to the Seagram's empire. The company launched in late 2000 in Turkey, Greece, Hungary, the Czech Republic and Poland – and, as the internet bubble of that year burst, went bankrupt within months. So, really bad timing.

The transition period was painful but very educational. Investors "under water" need to be managed as they are no longer interested in maximizing the company's value. Yet the business needs to grow, if possible. So we needed to downsize the team drastically yet at the same time offer vision to the staff that stayed. This was made possible through the buyout of the company by new investors and management, which provided funds for growth. The biggest learning for management from that time was that you can build a healthy business not from investor's money but from the only valuable funds that matter: profitable revenues from your customers.

What did the financial investor change in the company?

The new investors leading the buyout were Esther Dyson from New York and iEurope Group from New York/Budapest. They brought in the funds to execute the buyout, which in turn gave the staff the confidence to remain. They also brought more analytical rigor to the company and monthly board / operating review meetings that really helped management focus. Esther Dyson also acted as an invaluable mentor to management, sharing years of wisdom into single sentence takeaways that help you avoid mistakes. My favourite professional quote is still "Hire people who are better than you are".

How could the financial investor support management development?

One of the biggest value-ads of a financial investor is its analytical approach to focusing resources (money and human resources) to where it has the highest returns and making sure results come with the least capital required. Young as startup founders are, they can benefit from more seasoned individuals to help make those decisions. Also, someone external needs to bring in the objectivity to balance the natural positivity of startup founders to make sure decisions are optimal.

Another great value added of financial investors is the simple fact that they help maximize exit value. Foremost startups with professional investors tend to attract buyers who are willing to pay more. Also, the exit process can be engineered so that it maximizes returns.

One might say it was unusual in this case how you met the financial investor. At the same time, could you give any guidance that would generally apply to entering investors, with whom there would be plans to work together?

I believe that the combination of an angel investor, with a lot of practical advice, and a small hands-on VC fund, is important for early stage investments. I suggest HVCA members consider the same setup.

(Note from Editor: Szabolcs Valner was Vatera Group's Hungary country manager from 2000. After the 2001 buyout in which he participated as a small investor and therefore can be considered a Co-founder along with other management and investors involved in the buyout, Szabolcs was made in 2003 the Chief Executive Officer of Vatera Group until 2005. Viktor Gero, who joined in 2005 as Vatera Group Chief Executive Officer, and Eric Csupor, who joined in 2003 as Chief Operating Officer, then built Vatera to a successful sale to Naspers, a South African media group. After the acquisition, Viktor Gero remained with the company until 2011 as Regional Manager responsible for Romania, Serbia and Hungary. Eric Csupor remained with Vatera Hungary as General Manager until 2013.)

Szabolcs Valner was interviewed by:
Zoltán Dömötör, Executive Director,
Transaction Advisory Services, Ernst &
Young Advisory Ltd.

The Hungarian Private Equity and Venture Capital Association's investor members 1991-2016

The Hungarian Private Equity and Venture Capital Association's investor members 1991-2016

1991 Founding members

Euroventures Hungary B.V. / ANTRA Kft.

Innofinance Rt.

Ipari Kockázati Tőke Kft.

Multinova Kft.

Venture Capital Hungary B.V.

1997-2001

3TS Capital Partners

ABN Amro Capital (Hungary) Kft.

Advent International Corporation

AIG Global Investment (Hungary)

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Baring Communications Equity (Emerging Europe)

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Eclipse Rt.

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Erste Bank Befektetési Rt.

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GE Equity

Hungarian Innovative Technologies Fund

Innova Capital Ltd.

Invesztor Rt.

KFKI Investment Kft.

Kvantum Investment Bank Rt.

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Postabank és Takarékpénztár Rt.

Raiffeisen Private Equity Management

Riverside Zrt.

Róna és Társai Rt.

Venture Capital Hungary B. V.

Wallis Rt.

2002-2006

3TS Capital Partners

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AIG Capital Management

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COVENT Ipari Tőke Befektető Zrt.

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DBG Eastern Europe Kft.

Dresdner Kleiwort Capital Tanácsadó Ltd.

Eclipse Rt.

Erste Bank Befektetési Rt.

EUROPE Kft.

Euroventures Capital Kft.

Fast Ventures Üzleti Tanácsadó Kft.

GE Equity

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Hungarian Innovative Technologies Fund / HITF

IBH Innovációs és Befektetési Holding Rt.

iEurope Capital Kft.

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Mezzanine Management Kft.

Mid Europa Partners Kft.

Mihályi Consulting Ltd.

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Raiffeisen Private Equity Management

Regionális Fejlesztési Holding Rt.

Riverside Zrt.

Róna és Társai Rt.

Societé Génerale Asset Management Alternative Investments

TDA Capital Partners Inc.

T-Venture Holding

Wallis Zrt.

2007-2011

3i Group

3TS Capital Partners

Advent International Corporation

AIG Investments

AIG-CET Capital / AIG New Europe / Central Europe Trust

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Arx Equity Partners

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Elan SBI

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IBH Innovációs és Befektetési Holding Rt.

iEurope Capital Kft.

KBC Private Equity Tanácsadó Kft.

Kisvállalkozás-fejlesztő Pénzügyi Zrt.

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Warburg Pincus

2012-2016

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Website	www.deloitte.com

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Head of company	Dr. Ákos Erős
Contact person	Dr. Judit Nádor
Website	www.squirepattonboggs.com

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Company name	Forgó, Damjanovics and Partners Law Firm
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Head of company	Dr. Zoltán Forgó
Website	www.fdlaw.hu

Company name	Hipavilon Kft.
Address	H-1054 Budapest, Zoltán u. 6.
Head of company	Dr. Viktor Botos
Website	www.hipavilon.hu

Company name	Horváth & Partners DLA Piper Hungary
Address	H-1124 Budapest, Csörsz utca 49–51.
Head of company	Dr. András Posztl
Contact person	Dr. Gábor Molnár
Website	www.dlapiper.com

Company name	Invescom Corporate Finance Ltd.
Address	H-1026 Budapest, Pasaréti út 83.
Head of company	Zoltán Siklósi
Website	www.invescom.hu

Company name	Jalsovszky Law Firm
Address	H-1124 Budapest, Csörsz utca 41.
Head of company	Dr. Pál Jalsovszky
Contact person	Dr. Ágnes Bejó
Website	www.jalsovszky.com

Company name	Jeantet-d'Ornano Office
Address	H-1051 Budapest, Széchenyi István tér 7-8.
Head of company	Francois d'Ornano
Contact person	Katalin Zsömböly
Website	www.jeantet.fr

Company name	Kajtár Takács Hegymegi-Barakonyi Baker & McKenzie Law Firm
Address	H-1051 Budapest, Dorottya utca 6.
Head of company	Dr. Pál Takács
Contact person	Dr. Barnabás Simon
Website	www.bakermckenzie.com

Company name	Canadian Chamber of Commerce
Address	H-1052 Budapest, Vármegye u. 3-5.
Head of company	Nicholas Sárvári
Website	www.ccch.hu

Company name	KBC Securities Hungarian Branch Office
Address	H-1051 Budapest, Lechner Ödön fasor 10.
Head of company	György Herczku
Contact person	Ádám Hegyi
Website	www.kbcsecurities.hu

Company name	Kovács Réti Szegheő Attorneys at Law
Address	H-1121 Budapest, Zugligeti u. 41.
Head of company	Dr. Attila Ervin Kovács
Contact person	Dr. Attila Pintér
Website	www.krs.hu

Company name	KPMG Hungária Kft.
Address	H-1134 Budapest, Váci út 31.
Head of company	Robert Stöllinger
Website	www.kpmg.hu

Company name	Lánchidi and Partners
Address	H- 1016 Budapest, Hegyalja út 7-13. Buda Center
Head of company	Dr. István Lánchidi
Website	www.lanchidi.com

Company name	Lengyel Allen & Overy LLP
Address	H-1075 Madách I. u.13-14. Madách Trade Center
Head of company	Dr. Zoltán Lengyel
Contact person	Dr. Balázs Sahin-Tóth
Website	www.allenovery.com

Company name	M27 ABSOLVO Consulting
Address	H-1115 Budapest, Bartók Béla út 105–113.
Head of company	Lénárd Horgos, Tamás Horgos
Website	www.m27.hu

Company name	Hungarian Export-Import Bank
Address	H-1065 Budapest, Nagymező utca 46–48.
Head of company	Zoltán Urbán
Contact person	Balázs Winkler
Website	www.exim.hu

Company name	Hungarian Association for Innovation
Address	H-1036 Budapest, Lajos u. 103.
Head of company	Dr. Gábor Szabó
Website	www.innovacio.hu

Company name	Hungarian Telecommunication Plc.
Address	H-1013 Budapest, Krisztina krt. 55.
Head of company	Christopher Mattheisen
Contact person	Károly Schweininger
Website	www.telekom.hu

Company name	Mazars Kft.
Address	H-1123 Budapest, Nagyenyed utca 8–14.
Head of company	Philippe Michalak
Contact person	Zoltán Benedek
Website	www.mazars.hu

Company name	Noerr & Partners Law Firm
Address	H-1011 Budapest, Fő utca 14–18.
Head of company	Dr. Zoltán Nádasdy
Contact person	Dr. Ákos Bajorfi
Website	www.noerr.com

Company name	OXO Labs
Address	H-1061 Budapest, Paulay Ede utca 55.
Head of company	Péter Oszkó
Contact person	Bence Makai
Website	www.oxolabs.eu

Company name	PricewaterhouseCoopers Kft.
Address	H-1055 Budapest, Bajcsy-Zsilinszky út 78.
Head of company	Nick Kós
Website	www.pwc.hu

Company name	Raiffeisen Bank Ltd.
Address	H-1054 Budapest, Akadémia u. 6.
Head of company	Heinz Wiedner
Contact person	Andrea Újvári
Website	www.raiffeisen.hu

Company name	Réczicza Dentons Europe LLP
Address	H-1061 Budapest, Andrássy út 11.
Head of company	István Réczicza
Contact person	Edward Keller
Website	www.dentons.com

Company name	Réti, Antall & Partners Law Firm, PricewaterhouseCoopers Legal
Address	H-1055 Budapest, Bajcsy-Zsilinszky út 78.
Head of company	Dr. László Réti
Contact person	Dr. György Antall
Website	www.pwclegal.com/hu

Company name	Roland Berger Ltd.
Address	H-1051 Budapest, Sas utca 10–12.
Head of company	Frigyes Schannen
Website	www.rolandberger.hu

Company name	START Garancia Ltd.
Address	H-1037 Budapest, Szépvölgyi út 135.
Head of company	Csaba Zoltán
Website	www.startgarancia.hu

Company name	Szecskay Attorneys at Law
Address	H-1055 Budapest, Kossuth tér 16–17.
Head of company	Dr. András Szecskay
Contact person	Dr. Judit Budai
Website	www.szecskay.com

Company name	Trusted Adviser Kft.
Address	H-1133 Budapest, Váci u. 76. 3. em.
Head of company	Zsolt Szovics
Website	www.trustedadviser.hu

Company name	UniCredit Bank Hungary Ltd.
Address	1054 Budapest, Szabadság tér 5–6.
Head of company	Mihály Patai
Contact person	Balázs Sarlós
Website	www.unicreditbank.hu

Company name	Weil, Gotshal & Manges LLP
Address	H-1054 Budapest, Szabadság tér 7.
Head of company	David Dederick
Contact person	Anita Mónus
Website	www.weil.com

Company name	Vistra Corporate Service Kft.
Address	H-1062 Budapest, Andrássy u. 100.
Head of company	Matty Ryan
Contact person	Márk Horváth
Website	www.vistra.com

Company name	VJT &Partners Law Firm
Address	H-1126 Budapest, Kernstok Károly tér 8.
Head of company	Dr. János Tamás Varga
Website	www.vjt-partners.com

Individual Members

Dr. Attila Ágoston	
Company name	Közép-Európai Tőkebefektetési Kft.
Address	H-1143 Budapest, Ilka utca 31.
Title	managing director
Phone	+36 1 801 9346
Email	attila@goston.hu

Gábor Baranyai	
Company name	QualyPlan Kft. /CEU Business School
Address	H-1039 Budapest, Királyok útja 299. A. 2.
Title	managing director/adjunct lecturer
Phone	+36 30 222 1925
Email	gbaranyai@t-online.hu

Zsolt Berta	
Company name	Purple Star Kft.
Address	H-1013 Budapest, Pauler u. 11.
Title	managing director
E-mail	berta.zsolt@purplestar.hu

Dr. Judit Karsai	
Company name	Institute of Economics CERS HAS
Address	H-1112 Budapest, Budaörsi út 45.
Title	senior research fellow
Phone	+36 30 816 4269
Email	karsai.judit@krtk.mta.hu
Website	www.econ.core.hu/~kar

Dóra Kis	
Title	progressive management consultant
Phone	+36 20 320 2978
Email	dora.kis@live.com
Website	https://hu.linkedin.com/in/dóra-kis-9410832

László Makay	
Company name	KPMG Tanácsadó Kft.
Address	H-1134 Budapest, Váci út 31.
Title	Director
Phone	+36 70 3331414
Email	laszlo.makay@kpmg.hu
Website	www.home.kpmg.com/hu/hu/home.html

Dr. Ákos Mátés-Lányi	
Company name	Kinstellar
Address	H-1054 Budapest, Széchenyi rkp. 3.
Title	Managing Associate, Mainstream Corporate
Direct line	+36 1 428 4458
Mobile	+36 20 417 6552
Facsimile	+36 1 428 4444
Email	akos.mates-lanyi@kinstellar.com
Website	www.kinstellar.com

Milos Milicevic	
Company name	CEU Business School
Address	H-1051 Budapest, Nádor u. 9
Title	Business Administration PhD Candidate
Phone	+36 20 348 1300
Email:	milos@milicevic.net
Website	www.business.ceu.edu

Ildikó Adamecz	
Email	ildikoraj@t-online.hu
Phone	+36-30-919-3782

Balázs Szabó	
Company name	Konetik Gmbh.
Address	Breite strasse 1. 10178, Berlin, Germany
Title	CEO
Phone	+36 30 453 0016
Email	b@konetik.com
Website	www.konetik.com

Károly Szigeti	
Company name	Central-Fund Venture Capital Fund Management Ltd.
Address	H-1065 Budapest, Révay utca 10
Title	investment director
Phone	+36 30 242 7537
Email	szigetik@centralinvest.hu
Website	www.centralinvest.hu

Dr. Tamás Záhorszky	
Company name	Portörő és Záhorszky Law Office
Address	H-1118 Budapest, Ménesi u. 100.
Title	lawyer
Phone	+36 20 567 1115
Email	tamas.zahorszky@pzlaw.hu

Ibolya Pintér
Executive Secretary

Hungarian Private Equity and Venture Capital Association (HVCA)

Address: H-1013 Budapest, Pauler u. 11.
Website: www.hvca.hu
E-mail: hvca@hvca.hu
Phone: (+36 1) 475 0924

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