

The Case for Cloud Computing

Published September 17, 2019

Jeremy Schwartz, CFA

Global Chief Investment Officer

With last week's large change in factor returns—notably, the large outperformance of small-cap value strategies over growth, technology and momentum factor indexes—it was an interesting time for a podcast focused on the longer-term case for technology companies.

The “Behind the Markets” podcast went to San Francisco for the Cloud 100 event, which celebrated the 100 largest private cloud computing companies in the world, as determined by *Forbes*.

We spoke with Byron Deeter, partner at Bessemer Venture Partners, about the case for cloud computing and what makes Bessemer a special partner in the cloud space. We also spoke with Dan Springer, the CEO of DocuSign, one of the leading public cloud computing companies, about the opportunity he sees in the cloud market.

Some highlights from our conversation include:

- How Deeter went from the founder of a software-as-a-service business in the early 2000s to return to venture capital at Bessemer, which has now brought two dozen cloud computing companies from private markets to initial public offerings. Bessemer made more than 150 cloud computing investments to date.
- What makes cloud computing a prime focus of technology growth? What we heard at the Cloud 100 event was that software is consuming the technology sector, and software is migrating to cloud-based systems. Deeter sees cloud technology extending into all branches of life, from the home to the workplace, and into automobiles and mobile phones.
- Are valuations too hot? Deeter recognizes as a buyer that valuations seem to be running high, but he said that quality companies are never cheap and never look like bargains. They only do in hindsight, he said, after they have delivered a lot of growth.
- In technology, there is a “rule of 40” for delivering efficient growth: if you can combine a free cash flow yield with net income growth and have the combined two metrics equal 40, those are the types of investments that Deeter believes compound to deliver long-term attractive returns. The cloud computing public companies are delivering these efficient growth metrics above this level, and that is why Deeter is so excited about that market.
- Deeter believes we are still in the early days of cloud computing, and Bessemer is putting its venture dollars to work aggressively in the early-stage businesses.

The conversation with DocuSign's Springer added further examples and a case study of where the opportunity is at the company level.

- Springer noted that DocuSign is still in its early innings, with only 4% market share. His biggest competitors? Paper forms and manual processes.
- DocuSign has been expanding with a high 30% growth rate, and believes it can compound at this rate.
- Springer said that opportunities in future acquisitions may be in the areas of machine learning and artificial intelligence.

These were both great conversations on the future of cloud computing at a macro level, along with a more specific example at the company level. Thanks to both guests for sharing their time with "Behind the Markets." Please listen to the conversation below.

Important Risks Related to this Article

There are risks associated with investing, including possible loss of principal. The Fund invests in cloud computing companies, which are heavily dependent on the Internet and utilizing a distributed network of servers over the Internet. Cloud computing companies may have limited product lines, markets, financial resources or personnel and are subject to the risks of changes in business cycles, world economic growth, technological progress, and government regulation. These companies typically face intense competition and potentially rapid product obsolescence. Additionally, many cloud computing companies store sensitive consumer information and could be the target of cybersecurity attacks and other types of theft, which could have a negative impact on these companies and the Fund. Securities of cloud computing companies tend to be more volatile than securities of companies that rely less heavily on technology and, specifically, on the Internet. Cloud computing companies can typically engage in significant amounts of spending on research and development, and rapid changes to the field could have a material adverse effect on a company's operating results. The composition of the Index is heavily dependent on quantitative and qualitative information and data from one or more third parties and the Index may not perform as intended. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.