

Milan, 29 January 2014

LETTER TO SHAREHOLDERS AND TO PARTNERS OF DIGITAL MAGICS

Dear Shareholders and Partners,

2013 has been an exciting year for Digital Magics.

We have successfully completed our stock-exchange listing project, We have assessed more than 1,000 dossiers; we have selected 100 worthy of evaluation and we have invested in 11 digital startups.

As a matter of fact, some of our investee companies have shown a significant growth in value.

We have also developed an industrial process to systematically manage the co-financing and the exits of shareholdings.

Thus we can be proud of the results achieved and look forward to 2014 - that is just beginning - with optimism.

1) Market scenario

The situation in Italy is obvious to everybody.

The economy is showing some signs of recovery, but still very weak ones. However, if we consider our specific reference area, we are bucking the general trend.

In particular:

- *Status of the Digital Economy*

The digital economy in Italy continues to show high growth rates.

For example, e-commerce – a driving locomotive in our local digital economy - grew by over 18% last year by exceeding 11 billion euro (Netcomm Politecnico data); online advertising increased by 8% (IAB data).

The other segments of the digital industry - digital services for companies, online financial services, cloud computing market, digital marketing services.- have shown a similar trend:

As described below, many of our startups have shown similar growth trends.

- *Risk capital market*

The Italian venture capital market is currently going through a development process targeted to achieve full compliance with the European standards.

In Italy, only 0.004% of the Gross Domestic Product (GDP) is invested in venture capital, which is one sixth of the European average, and only 2% of the private equity is intended to be invested in risk capital against 6% in Europe.

Although the *early stage* segment registered a 18% growth in the first half-year of fiscal year 2013 compared to the first half-year of fiscal year 2012 (AIFI data), the fiscal year 2013 is estimated to break even with an amount of about 110 million euro invested in hi-tech startups (data resulting from Politecnico di Milano) .

It can be reasonably expected that in the next years the Italian risk capital market can achieve a development stage similar to the one of France and Germany, i.e. report higher figures than the current one.

This maturity scenario of the risk capital market may positively affect all relevant operators, including Digital Magics.

2) Decree for Growth 2.0

In this context, an important and positive innovation that is directly affecting us consists of the Decree for Growth 2.0 that will be soon implemented and which was already converted into law (Law 221/2012).

This law provides for the following:

- A 19% Irpef deduction (Personal Income Tax) of the amount invested by the tax-payer in the share capital of one or more innovative startups directly or through funds, accelerators, incubators, ventures and other organizations investing in startups calculated on the basis of an amount invested up to 500,000 euro per year, provided this amount is invested for at least 2 years;
- A 20% Ires deduction (Corporate Income Tax) of the amount invested by the company in the share capital of one or more innovative startups directly or through funds, accelerators, incubators, ventures and other organizations investing in startups calculated on the basis of an amount invested up to 1.8 million euro per year;
- Privileged access to the Central Guarantee Fund for SMEs with regard to incubators and innovative startups;
- Tax relief on labor cost with exemption from the additional social security contribution equal to 1.4% and tax relief and benefits for fixed-term contracts and term extension;
- Tax exemption of stock options issued by innovative startups and certified incubators.

In 2013 **Digital Magics** achieved the **status of certified incubator of innovative startup** thus benefitting from tax concessions as envisaged by law.

These positive innovations allow us to reasonably expect to achieve a substantial growth in the risk capital market in a short time.

3) Stock-exchange listing

Our Group got listed on 31 July 2013 on AIM Italia of Borsa Italiana.

We achieved this important objective through the **subscription of a capital increase** performed in two tranches:

- **The first tranche of about 8.5 million euro**, subscribed concurrently with the listing on the Stock Exchange (31 July 2013);
- **The second tranche of about 2 million euro**, subscribed on 31 December 2013.

The total fund raising of about 10.5 million euro results from the placing of convertible bonds worth about 4 million euro and from new cash worth about 6.5 million euro; the relevant amounts were used for investments in 2013 and we will use them also in the next two years' period to further increase our pace of investment in digital startups in the industries we consider more promising.

The initial trading price amounted to 7.50 euro per share.

In these first months following the listing process, the security showed its **highest peak of 8.39 euro per share** and its lowest peak of 6.99 euro.

The exchange counter-value amounted to over 2 million euro and was in line with the exchange volumes of the securities listed on MTA in the Small Cap segment.

At the end of the fiscal year (31 December 2013) the security's price was 7.45 euro per share and showed a slight decrease compared to the time of listing with an **overall capitalization of about 27.4 million euro.**

4) Investment activities and financial status

In 2013 **Digital Magics invested 3.47 million euro** - directly or through **56CUBE** - in **11 new startups** and 5 investee companies, already existing in its portfolio; the new startups are:

- **Buzzoole**, social media marketing platform with capabilities to evaluate the business impact of network users;
- **DeRev**, vertical crowdfunding platform for the service sector;
- **ilmangione**, "user-generated" guide of the best restaurants in Italy;
- **Intertwine**, collaborative editing platform aimed at producing multimedia e-books;
- **Prestiamoci**, "peer-to-peer lending" platform (licensed by Banca d'Italia) for the capital lending among private individuals and companies;
- **Private Broker**, financial consulting service 2.0;
- **QuitePeople**, digital tour operator specific for low-cost holiday offerings;
- **Sinapsi**, software house specialized in the FinTech sector;
- **Skillme**, social guide to find online the best professionals such as lawyers, physicians and certified public accountants;
- **Tasteet!**, search engine for the Italian wine-and-food environment;
- **ulaola**, international e-commerce platform for the sale of Made in Italy handicrafts worldwide.

With ongoing confidence we have **invested in 5 investee companies already existing in our portfolio** (Jumpin, Digital Bees, Growish, Wazzap, Profeeling) which required further support to grow up.

The total amount of the investments made in 2013 amounted to a counter-value of **3,470,000 euro**. **The total amount of the investments made by third parties in 2013** in startups controlled by Digital Magics was equal to **1,350,000 euro**.

At the end of 2013, the cash on hand of Digital Magics amounted to about 4 million euro and showed a positive net financial position of about 2.6 million euro increased by about 6 million euro in comparison with the end of fiscal year 2012.

5) Growth of our startups

With the investments made in 2013, we have a portfolio of 29 startups, directly or indirectly through 56CUBE; 10 are innovative startups in accordance with Law 221/2012.

In 2013, we have seen some of our investee companies register a substantial growth in value.

In the following two case studies are outlined. One refers to a “mature” startup and the other one deals with an investment recently made, still in the incubation stage; these cases allow us to understand the growth rate and the purpose of our work and role as a development partner.

- *4w MarketPlace*

4w MarketPlace is a company founded in 2009 in the R&D lab environment of Digital Magics; over the time it has become the leader advertising network in the performance-based advertising market.

Today, 4w MarketPlace has a team made up of over 25 people, works with the main Italian publishers (e.g. Gruppo RCS, Gruppo Editoriale L'Espresso, La Stampa, ANSA, RAI, etc...); to support its development plan, it has leveraged a venture capital fund (managed by Principia SGR) that has invested 2 million euro.

The core business line of 4w MarketPlace increases in double figures over the years since the company startup and today it generates a volume of revenues higher than 4 million euro.

Digital Magics has played the role of deviser and co-entrepreneur of this company and today it operates as advisor supporting the development of the company.

- *Prestiamoci*

Prestiamoci is a company operating in the “Peer-to-Peer lending” area, a new “asset class” that is revolutionizing the “consumer credit” industry and that is spreading in the most advanced financial markets.

When the investment was proposed to our Group, Prestiamoci was a company licensed by Banca d'Italia, with 412 lenders, 351 financed projects and a volume of loan expenditure amounting to about 2 million euro.

We have been proposed to take part in the turnaround of the company that was going through some difficulties.

We have trusted the project and decided to participate in the company together with co-investors of our Network interested in it.

Following the investment, in only two months we have set up a new management team, re-designed and developed the website, re-defined the business model, completely re-modeled the risk control process concerning the loans granted and dramatically reduced the monthly “cash burn rate”.

Prestiamoci has restarted its activities with more soundness and currently it can successfully operate in a booming sector.

In the major Western economies, P2P Lending models are registering the most high growth rates of the digital industry.

At least two thirds of the investments made in this “asset class” result from financial institutional investors (hedge funds, pension funds, family office, etc...) which have understood the benefits in terms of “risk/yield” compared to other already existing products.

In the United States, the two most important companies have already granted loans for an amount of over 3 billion dollars (Lending Club and Prosper), while in the United Kingdom the main operators have granted loans for an amount of more than 300 million pounds. (Funding Circle, Zopa, Ratesetter).

6) Digital Magics Angel Network

In the stock-exchange listing process, we have **involved more than 100 subjects**, i.e. private investors, industrial companies and institutional investors.

Among the various investors that have joined the Network by participating in the listing process, there are: **Fondo Atlante Seed (Gruppo Intesa Sanpaolo), Banca Sella, Tamburi Investment Partners, Gate14 Group and Gruppo RCS**, with which we have signed a **corporate venture capital agreement** for the creation of the **joint RCS NEST incubator**.

The Network is continuously increasing in new subjects. **In December, the Uvet Group has joined our shareholding structure** with the objective to deploy an *Open Innovation* program dedicated to online travel and tourism.

This network has rapidly become a **strategic asset** for our company.

We have soon realized that the experience, the competence and the relationship value of our new shareholders are an important asset that can significantly help a startup to boost its development and success.

Consequently, we deem appropriate to formalize our network of relationships through the setting up of the **Digital Magics Angel Network**.

The Digital Magics Angel Network will be set up through the establishment of a an association that will be formally defined in the next weeks.

Digital Magics will play a key role within this association which will be controlled by the company shareholders intending to join the initiative.

The major objective is to foster the creation of “**club deals**” supporting the startups selected by Digital Magics, in accordance with the provisions concerning the promotion of investment ventures.

At the same time, we also intend to create a place of debate and discussion related to the digital economy prospects in order to enhance the know-how asset of the company and of the Network.

We firmly believe that the Digital Magics Angel Network can provide the perfect venue for informal and professional investors of the *seed* stage sector, where they can find the best opportunities; moreover, we believe that this network is a pillar on which to build the development plan of our company.

7) **Open Innovation programs**

Driven by the same spirit with which we have set up the Digital Magics Angel Network, we have recently launched **several Open Innovation programs**.

An *Open Innovation* program is a framework of initiatives that aim at helping large Italian enterprises to boost innovation through the *scouting* of digital startups in their reference industry segment.

Our objective is to develop close relationships with industrial stakeholders who can play the role of partner or of investors while supporting the development of our investee companies.

The objective of our industrial partners is to accelerate an innovation process targeted to identify the best initiatives existing in the market, which however have not yet reached the relevant maturity.

The purpose of the *Open Innovation* program is to take the selected startups into the company scope of our partners.

In this regard, the *Open Innovation* activity is therefore crucial for our company as for the creation of an industrial process targeted to the sale of our shareholdings.

8) **Exits**

The exit strategy is a key issue for an operator such as Digital Magics.

Today we have a portfolio of 6 companies we consider mature for a total or partial sale of our shareholding.

In the light of a strong structural development of this market (development to which we are trying to provide a systematic contribution) and driven by a strong conviction that our shareholdings must increase in value and not sold off, we are working on two different fronts in order to speed up the exit process:

- On the one hand, we are creating **partnerships with corporate finance operators**, specialized in cross-border M&A operations in the digital market;
- On the other hand, we are increasing the number of collaborations with industrial partners which will support this process within *Open Innovation* programs.

These actions complete the work we carried out in the last years to develop an industrial process targeted to the selection, development and transfer of our shareholdings.

IN BRIEF:

- We have developed an industrial process targeted to the “go-to-market” of digital startups;
- We have created a new “asset class” with the listed security of a certified incubator of innovative startup, thus effectively supporting the development of risk financing in Italy;
- We are endowing us with an effective instrument - the Digital Magics Angel Network - to deploy the co-financing process of our investee companies and to implement *Open Innovation* programs dedicated to large Italian industrial groups;
- We are creating the right conditions for overcoming the current exit limitations of the Italian market.

Consequently, we can say that we are satisfied with the results achieved in 2013; we seize this opportunity to thank all the ones who invested and trusted in our project and we look forward to 2014 - that is just beginning - with optimism.

Enrico Gasperini
Founder and Chairman of Digital Magics