PUGET SOUND Business Journal
Business Leaders Get It.

OCTOBER 2008

Insider Tips: Engaging a VC

As professional investors that raise pools of capital from institutional, corporate and individual investors, Venture Capitalists (VC's), are a highly sought after group. Although many early stage CEO's seek VC funding, only a select few actually get it. For example,
at a recent Northwest Entrepreneur Network breakfast meeting, OVP Managing Director Lucinda Stewart explained, "OVP does about 6-9 deals a year, which is whittled down from about 3,500 contacts, of which maybe 200 or so are a possible consideration and only 10% move on to the due diligence stage." With so much at stake for both the CEO and VC firm, it's easy to see why both have to be selective. With that in mind, Lucinda Stewart shared some of the no so obvious decision making that OVP and other VC firms go through when determining which businesses to fund.

What VC's are Thinking

- **How big is this market?** VC's want a big opportunity so they're looking for big markets. In addition to market size they will be assessing how open the market is. A deal becomes very exciting when its part of a big, open market with no entrenched leader.
- **Who knows this person?** If you don't know anyone at the VC firm then leverage a backdoor contact that can recommend you. Lawyers are a great source, as is anyone the VC respects. When these sources are leveraged, a meeting is more likely. Without smart networking a CEO is forced to send emails or cold calls, which are usually dead on arrival.

Executive Insights

Cheryl Isen

- **Is this an out of the box idea?** VC's know that upside in typical categories isn't usually there. That's why they get excited by business ideas that demonstrate break-out thinking, or doing things in a completely new way.
- **Can they prove it?** If an idea is innovative it's just as critical to show a pathway to validation. Unfortunately this often presents a chicken-egg scenario. Without market validation or IP (intellectual property), a great advisory board should be assembled to reinforce concept validation. These individuals should be well-known industry veterans that can speak to VCs about why the idea has merit.
- **How deep is the management team?** What's commonly seen is a technology founder without a partner. VC's want biodiversity and sales DNA on the team. If you can't sign up partners without funding its advisable to find people that will confirm that they will come on board once funding is available. Expect the VC to contact these people.
- **Are the leaders experienced?** VC's want a smart, focused entrepreneur that can bridge the big idea with the right background, and has a logical execution plan. This demonstrates knowledge and experience and establishes confidence with the VC. If you're not a serial entrepreneur, the bar will be much higher.

Since most companies don't have everything a VC firm wants, it's important to know what a VC is willing to trade off. According to Lucinda Stewart, stable management beats the smartest team. When it comes to product vs. vision, product is king because it's key to getting market feedback. It's also important to emphasize your ability to assess and if needed, fire quickly. To a VC, that ability equates to time, and time is cash.

Understanding the Secret Language of VCs

Once you engage with a VC it's important to be able to accurately interpret VC code words so that you know where you really stand. Here are a few somewhat tongue in cheek interpretations of the most common VC phrases: *(More phrases can be found at www.OVP.com.)*

The VC Says:	The VC Really Means:
"Entrepreneurial CEO"	—totally uncontrollable, bordering on maniacal.
"We work closely with management"	—we talk to them on the phone once a month.
"Unique"	—no more than six competitors.
"Ingredients are there"	—given two years we might find a workable strategy.
"Basically on plan"	—expect a revenue shortfall of 25%.
"Acquisition strategy"	—the current products have no market.
"Core business"	—obsolete product line.
"Limited downside"	—it can't get much worse.
"Long selling cycle"	—yet to find a customer who likes the product.
"Repositioning the business"	—multi-million dollar investment recently written off.

Chuckles aside, VC's do understand that the road to a successful exit isn't easy. In fact, the most common pitfalls for derailing a well-laid plan are often some of the most difficult to overcome. They include:

- Timing of the markets;
- Failing to capture value;
- Focusing time on 20/80 meaning, doing the hardest part instead of the right part;
- Violating the laws of sales; and
- Confusion in branding.

With the average length of time from nurture/seed money to liquidity/exit being seven years, your VC relationship is going to last a long time. It's critical to take the time on the front end to select the right firm. Approach your VC selection like a marriage. Be selective. Not every VC firm will be right for your business. If you focus your attentions on the wrong VC firm you may be rejected for reasons that have nothing to do with the potential of your business. It might be as simple as your firm not fitting that VC firm's "model". More importantly, the VC firm might not fit *your* funding needs--after seed money can they support the investment downstream?

These "Executive Insights" are based on monthly presentations provided by leading entrepreneurs at the Northwest Entrepreneur Network (NWEN.org), a non-profit organization dedicated to helping entrepreneurs succeed. The column is written by Cheryl Isen, founder of Isen & Company, a strategic marketing and public relations firm that helps emerging companies increase corporate visibility and brand awareness Contact Cheryl at (425) 222-0779, Cheryl@IsenandCo.com or on the web at www.IsenandCo.com.