A CASE STUDY OF QUALITATIVE FACTORS IN MAKING VENTURE CAPITAL INVESTMENT DECISIONS

by

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DEDICATION

I am dedicating this thesis to my children Ashton, Saffron, Cinnamon, Collin, and Sage, that they may take this as an inspiration to overcome fears and challenges, to push past perceived boundaries and reach great things in life.

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LIST OF ABBREVIATIONS

Abbreviation	**Description**
Biz dev	Business Development
IPO	Initial Public Offering
Med-tech	Medical Technology
M&A	Mergers & Acquisitions
SaaS	Software-as-a-Service
SME	Subject Matter Expert
VC	Venture Capitalist

ABSTRACT

When a startup requires large capital backing, it can expect to seek out the venture capitalist. Understanding the process and priorities of the venture capitalist is necessary to gain funding approval on more than just a good business plan, a positive revenue model, or being a likeable person. This study gives a current view of the modern venture capitalist and the elements of their decision making for the edification of entrepreneurs in the funding stage, to understand and avoid pitfalls of their presentation and unspoken communication for nonfinancial components of their business persona. Five interviews have been conducted with venture capitalists residing in the Austin area and two interviews with subject matter experts (SMEs) who have been directly influenced and are consultants in venture capital decision making. These individuals have shared their experiences and methodologies in finding inimitable opportunities for high growth ventures. An explanation of venture capital review methods is presented, followed by a case study and summary of commonalities and contradictions between interview outcomes.

1 BACKGROUND

1.1 Prologue

Venture capital funding accelerates businesses by giving entrepreneurs the means to scale ideas and develop more quickly than through organic growth. However, entrepreneurs who need funding to fuel accelerated success are often denied by venture capitalists (VCs).

The question is, what factors matter, and are these the most obvious factors? Traditionally, investment decisions are made based on quantitative numbers such as revenue growth, addressable market, and profitability. By the very nature that highly innovative startups are also considered high risk and are venturing into unknown territory, quantitative factors are not sufficient measures for the future success of a company and therefore necessitate the investment of venture capital. This means that venture capitalists have to base their investment decisions mainly on qualitative factors. The question is what are these qualitative factors and to what extent can the entrepreneur influence these? Does a common set of favorable factors exist?

In this thesis, I am conducting a case study with a small set of selected venture capitalists to capture the diversity of decision making. My thesis is, that there is no common set of decision factors, perhaps overlapping factors that are more common, and others that are uniquely dependent on the decision makers, their background, and experiences from past investments.

Therefore, the focus will be on qualitative evaluation factors.

1.2 Current Economic and Political Climate

Within the last five years, the economy has been steadily strengthening from its lows during the Great Recession that peaked in 2006. In 2016, unemployment was close to a low since 2007. Consumer confidence is steadily improving. 2016 was dominated by the presidential election.

After being in office for two terms, President Barack Obama handed over his office to Washington outsider, entrepreneur and entertainer Donald Trump, who introduced both hope as well as uncertainty. December 2016 ended with an unemployment rate of 4.7%, down from 5% a year ago, with increases in jobs for manufacturing, healthcare, education, construction and mining (Ycharts 2017). Housing markets are recovering and showing strength and perhaps overvaluation in some markets. Federal interest rates rose to .5% in December 2015, from effectively 0% since 2008, up to .75% in December 2016 to 1% in January 2017 (Amadeo 2017). The stock market recovered and hit 20,000 points for the first time in January of 2017. National Average gas prices dropped below $2 and remained under $2.50 for 2016, saving consumers billions of dollars (Weisbaum 2017).

Though still at historical lows, rising interest rates influence the venture capital industry. Early stage and seed investors want to collect money now, since it is harder to obtain when interest rates are higher and the same initial capital comes at a higher cost to investors (Loizos 2016). Late-stage investors have been benefitting from the added capital investors are putting into ventures instead of fixed income securities like bonds, since the yield has been low (Loizos 2016). In both cases, rising interest rates will give investors more alternatives for returns, and the info of dollars to venture capital will decrease as interest rates rise.

The Trump administration has been proposing tax cuts in 2017, which will also benefit venture capitalists through tax cuts on the wealthiest top 1% of households, estimated at $37,000 on average, and a total of $158 billion on investment income for Americans (Rappeport 2017).

1.3 Statistics on Venture Capitalist Activity in the United States

1.3.1 Venture Capital

Venture capital firms are defined by the National Venture Capital Association (NVCA) as “professional, institutional managers of risk capital that enable and support the most innovative and promising companies” (Buyouts Insider 2016). Among companies once backed by venture capitalists are Apple, Amazon, Facebook and Dell. Venture capitalists make deals at all stages of a start-up, but are more often investing during the development and growth stages of a company, when large amounts are needed to keep up with new hires and production (Pitchbook Data 2017). Venture capitalists spend a great deal of time and effort in the companies they back, and each new deal requires their ongoing participation in different ways.

Venture Capital firms are commonly funded through limited partnerships, where the venture capitalist firm is the general partner and limited partners are capital sources such as public pensions, corporate pension funds, insurance companies, high net-worth individuals, family offices, endowments, foundations, fund-of-funds, and sovereign wealth funds (Pitchbook Data 2017). As of 2016 there are 898 venture firms in the United States, backing 7,750 firms and providing $69.1 billion in funding (Pitchbook Data 2017). Start-up funding can also come from international sources, and outside of the United States, 54% of venture funding is made to companies within the United States (Amadeo 2017).

Venture capitalists receive deal flow from a variety of sources, including professional, private and referral networks, actively seeking out investments, and receiving business plans and pitches from entrepreneurs. Once a company has been funded, hold times to exit can vary. Starting at the time of funding, the firm supports the company on a high accelerated growth path to exit. Typical exit strategies are Initial Public Offering (IPO) and more commonly acquisition. Only 39 IPOs were completed by venture capitalists in 2016 (Pitchbook Data 2017).

In 2016, software was the leading sector of investment, and the only sector, other than IT hardware, that has shown growth from 2015 (Pitchbook Data 2017).

A 2016 study '*How Do Venture Capitalists Make Decisions*' took a qualitative approach on venture capitalists' decision making, estimating that only one in 100 investments received by a venture capitalist firm will ultimately get funded (Gompers, et al. 2017). According to this study, for early-stage investments, 17% of venture capitalists did not use any quantitative factors in their funding decisions, and 9% of overall investments were made solely on qualitative factors (Gompers, et al. 2017).

1.3.2 Angel Investment

Angels are individuals or groups of individuals with a high net worth who typically invest during earlier stages of companies than venture capitalists. They focus smaller investments, less than $1 million per startup, and often provide various levels of assistance to their investment companies such as through mentoring or industry expertise. The exact border between Venture Capitalist and Angel Investor is fluid.

Angels invest their own money into start-ups and can come together in groups to achieve funding comparable to that of venture capital.

Angels, like venture capitalists, must be SEC accredited to provide funding to start-ups, since both are considered to be high-risk. Accredited investors are defined as those who have a net worth of over $1 million in addition to their primary residence, or an income of $200,000 per year for at least 2 years or $300,000 for married couples (AngelList 2015).

1.3.3 Crowdfunding

Crowdfunding is defined as financing a project or venture directly through individuals (Armin Schwienbacher 2012). The Journey of Business Venturing article' “Crowdfunding: Tapping the Right Crowd” evidences that rewards of funding can be realized in the form of rights to pre-order new products or owning a share of equity in the new company after it has been fully backed, a profit-sharing model, or lending contract, but sometimes funding is obtained in the form of donations, thus expecting no compensation (Belleflamme, Lambert and Schwienbacher 2013). Profit-sharing is more often the choice for larger investments, and smaller investments would fall into the category of funders wanting pre-ordering rights (Belleflamme, Lambert and Schwienbacher 2013). Due to recent legislation and the growth in online availability and awareness of crowdfunding, the 2015 United States total for crowdfunding is $17.25 billion dollars and $34.4 billion globally (Massolution 2015). 2016 global results are expected to surpass that of venture capital funding (Massolution 2016).

Crowdfunding is usually done through internet sources such as CircleUp.com and Kickstarter.com. Kickstarter.com alone launched 57,515 project and funded 19,235 projects in 2016 (Kickstarter 2017).

The drawback to crowdfunding is that it is not managed by professional investment partners. A study of Kickstarter by Pennsylvania State University's Wharton School of business showed that since 2009, 9% of Kickstarter projects failed to deliver promised rewards to their backers (Kickstarter 2017).

There is little research done on crowdfunding since legislation has largely prohibited crowdfunding. In 2015, the Securities and Exchange Commission filed Title III of the JOBS Act to allow crowdsourcing for individuals who are not registered investors as long as the amount raised does not exceed $1 million in a 12-month period, and individual investments are limited to $2,000 or 5% of a participant's annual income or net worth, or 10% if annual income is over $100,000, not to exceed $100,000 of total investments in a twelve-month period (Securities and Exchange Comission 2015). This legislation has largely allowed for smaller investments which can be harder to track and regulate, but still requires registered investors to account for investments over $1 million, so new legislation is beneficial for early stage start-ups, but would not be applicable to venture capital-seekers over $1 million. Crowdfunding can potentially be used to prove products, or establish traction required before obtaining venture-capital funding in some circumstances.

1.3.4 Statistics on Venture Capitalist Activity in Austin

In the United States, Silicon Valley is known as the leading venture capital hub. In 2016, venture capitalists in Silicon Valley made more deals outside of the greater San Francisco area than within it (Pitchbook Data 2017). Of these, Austin was ranked #6 by metro area, see Table 1: Venture capital investment per area (Tom 2017) (Tom 2017). Though the total number of venture capital firms rose in 2016, there has been a decline in those residing in the Austin area.

But why is venture capital activity increasing in the Austin area? Austin is growing as a hub for entrepreneurial growth and the tech sector. Austin venture capitalists know this and have strategically placed themselves in various Austin incubators, accelerators and universities for finding and growing opportunities in the city of Austin.

Austin is home to the University of Texas, with an entrepreneurial program, its own startup incubator, and a workforce with a wealth of knowledge provided by the prestigious university's engineering and business schools. Venture capitalists and entrepreneurs work with the university and companies like Structured Polymers, former University of Texas students, received funding of $1.5 million dollars from a local venture capital firm through the firm's crowdfunding platform (Grisales 2014) .

Table 1: Venture capital investment per area (Tom 2017)

METRO AREA	2010	2011	2012	2013	2014	2015	2016	SUM
NEW YORK CITY	98	161	190	219	327	326	287	1608
BOSTON	88	110	141	135	134	147	124	879
LOS ANGELES	75	95	113	134	136	170	116	839
SEATTLE	39	45	67	82	66	87	80	466
SAN DIEGO	49	42	36	45	54	51	50	327
AUSTIN	24	31	29	47	29	52	43	255
CHICAGO	16	37	35	34	43	39	27	231
WASHINGTON, DC	28	23	26	31	40	34	33	215
DENVER/BOULDER	20	27	24	29	29	42	27	198
PORTLAND	12	24	15	22	22	20	24	139
ATLANTA	17	16	17	19	17	29	10	125
PHILADELPHIA	14	11	17	12	22	22	23	121
RALEIGH/DURHAM	10	11	8	6	15	18	12	80
MINNEAPOLIS/ST. PAUL	7	12	12	12	12	7	10	72
SALT LAKE CITY	5	12	8	9	16	10	12	72
DALLAS/FORT WORTH	9	9	6	14	9	10	10	67
MIAMI	1	4	6	15	11	13	15	65
PHOENIX	2	2	10	8	9	15	4	50
HOUSTON	7	6	6	11	9	7	4	50
SANTA BARBARA	6	5	5	6	5	6	4	37
TOTAL	527							

Venture capitalists work closely with incubators and accelerators to find opportunities. Tech Ranch, Techstars, and Capital Factory are all located in Austin, and are places for seed and startup companies to network, share knowledge and receive mentoring for business growth and strategic development.

1.4 Reason for Thesis

This thesis is written as part of the Masters of Business Administration requirement at Texas State University. It is intended to add to the knowledge and understanding of venture capital and high growth investing. While much literature has been done on financial valuation methods used by venture capitalists, there is very little qualitative case study research to identify and find commonalities of startup evaluation from the standpoint of venture capitalists and decision makers. This thesis will attempt to understand common heuristics which can make or break an entrepreneur's deal potential. The participants are experts in the field of venture capital and have had several years of experience working with startups and holding board positions in ventures, including their own startups. Interviewees have agreed to share business-specific information on the premise that their names, affiliates, or information linked directly to them would not be given without their permission. Participants were interviewed in 60-120 minute timeframes, and responses were recorded using handwritten notes.

The challenge in such a study is to find relevant and representative participants who are willing to talk off-record and share insider secrets. All interviews are conducted anonymously, and the privacy of study participants is being preserved.

This thesis will focus on analyzing responses to a common set of interview questions and putting them into the context of an investor's personal background. The answers to questions are compared to each other and analyzed.

1.5 Methodology

Analysis of interview data was dissected through the practice of coding and analyzing natural similarities through conceptual relationships to come to conclusions.

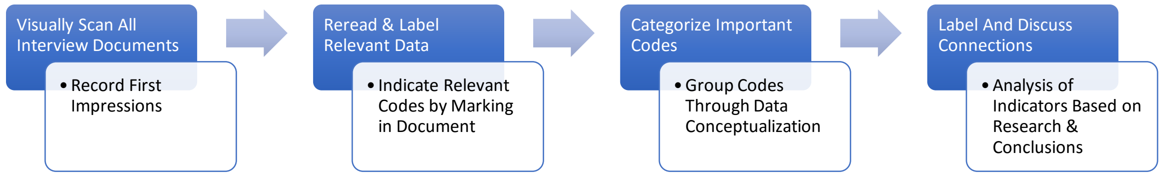

Figure 1: Methodology to analyze interviews

All interview transcripts were overviewed together and notes on broad first impressions were collected. Transcripts were reread in their entirety and relevant words, data, sentences and principles were marked. The relevant data are codes which were found based on the interviewer's stressed importance, repetition, and special convictions. Codes were also found through individual interest, impression of relevance and surprising findings. These codes were used as indicators of qualitative relevance to the venture capitalist and decision maker.

All codes were collected together and conceptualized. These concepts were grouped into broad general categories through relative comparison, and outliers were removed. Categories were labeled and the connections between relevant indicators are discussed in section three of this case study. Section four is an analysis of conclusions based on these connections and supportive research related to findings.

The process is depicted in Figure 1: Methodology to analyze interviews.

2 INTERVIEWS

2.1 Purpose of Questions

Interview questions are intentionally open-ended, in contrast to the more typical questionnaire with given choices of answers, to provide individualized responses and are not guided except to give clarification when requested. The research focus is the qualitative answer that cannot be easily captured with a quantitative questionnaire with prepared responses or empirical processes. The objective lies in understanding how decision makers interpret funding opportunities, and whether generalized industry commonalities occur. The interviews do not draw statistically significant conclusions, but rather shed light on the complexity and variety of methods that are used in the venture capitalist industry. Basis for this interview assumes that social cognitive theory will yield responses based on the individual's perceptions drawn from past experiences.

Questions are based on three phases of entrepreneurial interaction in the venture capitalist funding process and the overall social perception of the entrepreneur or entrepreneurs by the venture capitalist.

Questions 1, 2, 3, 6 and 7 give a basis of context for the portfolio, fund size and deal flow of the firm, which allows an understanding of the magnitude and availability of the venture capitalist to fund new ventures.

Questions 5, 12, 13, 14 and 15 are specific to the funding process and sets expectations for the entrepreneur in stages after the pitch and initial interest is established.

Questions 4, 8, 9, 10 11, 14, and 15 provide a framework for the entrepreneur's individual experience to understand what similarities in background and experience venture capitalist may have in common, and how these perceptions translate into pre-conceived notions of startup evaluation.

2.2 Interview Questions and Explanations

1. With how many other investors do you prefer to invest in a venture?

The question is whether a venture capitalist prefers to invest within a team of other groups together, and if so with how many, or if they prefer to invest alone. Answers demonstrate the rate of portfolio diversity, which is a measure of leveraged risk for the firm.

2. How many investment opportunities do you review in a year?

This questions gives perspective on both the total number of opportunities reviewed in relation to opportunities being funded. This allows an understanding of the breadth of their portfolio, and the number managed per partner. This will give an estimate of portfolio turnover, and subsequently a suggested rate of opportunity for an entrepreneur to receive funding from a typical firm in a calendar year.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

The question is about the required deal pipeline that optimizes capacity of the firm and maximum benefit point. It is also a follow-up question to opportunities reviewed.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

These questions size the kind of companies an investor would back, and the deterministic criteria guiding a preference for larger teams or sole proprietors.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

What does it take from the first presentation to a decision to invest, and how can an entrepreneur gauge progress?

6. What is the average amount that you invest in a project?

This question senses whether an investor has a certain amount they want to place in mind. It could depend, for example, on risk distribution, size of fund, or stage of the funded company. There also may be a relationship to question one, the number of investors.

7. What is your target return rate? What is your average return rate?

How much yield does a venture capitalist target, or how much yield do they have to make to survive. How many deals end in losses, and how are venture capitalists funding choices influenced by this?

8. How long have you been in the venture capital business?

How long has the investor been doing deals? This can be expressed in total number of years, or total deals. This gives a sense of industry knowledge, and if approach can be linked to years of experience.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

How are entrepreneurs measured initially? Is it in a framework of a pitch event, or socially, as an individual? What is the focus of the venture capitalist within the presentation? Possible answers can vary, but common points of interest may emerge that show particular focus on certain human attributes for success.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

The origin of this question to find out whether an investor is averse to an entrepreneur that had failed or even may prefer one because that entrepreneur had learned lessons. This information can contribute to foreseeable opportunity for the founder who has experienced previous failure, and how to recover.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

When is capital too much for a startup? Or is there ever too much capital? When and why does an investor think the business does not need added capital?

12. What questions should founders be asking you when you are making a decision whether to invest?

This gives venture capitalists insight to the dangers of other firms, and brings out the positive points of their own firm. A collective understanding can help the entrepreneur to better evaluate venture capitalists, and avoid unfavorable experiences.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

What is the added value of a venture capital backing? Do they offer expertise, contacts, marketing, etc.? Responses will indicate qualities to measure when receiving venture capitalist backing, and the venture capitalist's conceptual understanding of their role.

14. What other business experience do you have?

What is the background of a venture capitalist? Are there similarities?

15. What industries do you specialize in? Are these the only industries you fund?

Are investors searching for the next big innovation or sticking to industry expertise? Is it likely that a venture capitalist will fund an idea outside of their investment focus?

2.3 Description of Participants

Participant 1

Participant 1 is a subject matter expert and serial entrepreneur. He started his career in the mid-90s while still in business school with a management consulting firm advising the

SMB space. He was a co-founder spinning out CRM software development from his management consulting firm, which he grew into a solid business that included raising venture capital. On the successful exit on his first venture, participant 1 joined in an executive role in an early startup, developing and marketing a line of recreational equipment, that he successfully grew. From this marketing experience, he went into Sales leadership, where he helped grow a small electronics parts distributor into a major Fortune 150 company. Centered around a strategic board game, he founded a consulting company that helps companies to develop and fund activities focused on entrepreneurial innovation. Participant 1 has taught lectures on global entrepreneurship, marketing, and international business at a major public university for over 13 years. Participant 1 is a regular speaker on topics of startups, entrepreneurship, and innovation. He is also a director of a non-profit, and is a published author.

Participant 2

Participant 2 started a career in a Sales role in in the 70s, and was responsible for financial reporting, forecasting, and planning for several business units. Participant 2 immigrated to the United States in the 80s. Participant 2 accepted a CFO position at a venture backed company, and kept this for three years. Participant 2 then left the private sector, founded a technology incubator at a major public university and joined the university where participant 2 led the commercialization program for university research and intellectual property for five years. Participant 2 founded the current venture capital firm in the late 90s and led it until recently. Participant 2's venture capital firm specializes on the commercialization and spinout of technology from private sector and universities. Participant 2 returned into the public sector accepting a role outside the

United States to lead a public research institute that focuses on funding, networks, and research facilities.

Participant 3

Participant 3 started his career in investment banking advising Internet, hardware equipment, and business services companies in the late 90s. He briefly joined an early hosting startup, and then a venture capital firm as an analyst where he stayed for five years, and worked on eight deals. He joined another firm for two years where he worked on another deal. Participant 3 founded his own venture capital firm that is now going into its tenth year after successfully executing over 100 transactions. His venture capital firm focuses on providing liquidity to stake holders as well as growth capital by building public market funds that extend into the post IPO phase.

Participant 4

Participant 4 is a seven-time startup veteran. Participant 4 started his career in the Silicon Valley as software and systems engineer. He founded a skunkworks development consulting company that assisted large companies in adopting emerging technologies. This resulted in $2 billion of revenue for one single ecommerce client. He moved into a role of a CTO growing the initial team of a price comparison engine. He took a stint in professional services extending the Internet to the Intranet. He then went on to found a software and services company. He is the founder of one of Texas' major incubators that he is running now for almost a decade. That incubator spread out globally, first to South America, Europe, and now Asia. Participant 4 specializes in multi-cultural teams actively supporting his portfolio companies in a phase of rapid growth and change.

Participant 5

Participant 5 started out his career in finance and investment banking. His first role was a commercial portfolio manager for a regional bank, that he held for three years. He joined a private equity firm where he stayed for another three years. Participant 5 joined a venture capital firm and became a principal where he has served for over seven years. Participant 5 serves on various boards as a member and observer.

Participant 6

Participant 6 became a venture capitalist in the 90s. He specialized on syndication, developing deal flows where he recruits institutional and private investors that invest along with him. He started both a venture scholar program as well as an online case study learning facility that is being utilized by MBA programs across the United States.

Participant 7

Participant 7 began as an electrical engineer in the technology sector, designing and developing new products. He founded a storage technology company that patented many of the fundamental storage technologies used today. After going public, he founded a venture capital firm that he has led for over two decades now.

2.4 Similarities and Differences Between Interview Participants

Participant 1 is a bit special in the sense that he did not manage a portfolio, but as an academic, he advises venture capital firms on making portfolio decisions. Participant 1 draws his expertise both out of experience founding companies and his teaching and research activity as a faculty of a major public university.

Participant 2 through 7 all manage their own portfolios and remain actively involved in their portfolio companies.

Participant 2 started out on the revenue side, growing sales and sales organizations. Participant 2 went into public service and dealt with both helping students form their businesses as well as the helping the university to monetize on intellectual property, before founding a venture capital firm. Participant 3 has a more classic career path starting out in investment banking and established a razor-sharp focus on venture capital very early in his career. Participant 4 started his career as an engineer and in technical leadership roles. He utilized knowledge that he gained from working for these companies, translated this into a consulting role, before deciding that he could take on a stake and building up a portfolio that led to starting his firm. Participant 5 also has a more classic career path, but started out in commercial real-estate portfolio management, before he shifted his focus to venture capital. Participant 6 has a venture capital history that leads more than two decades back. He focuses on building networks, both to syndicate with institutional and private investors, as well as providing deal flow, that incorporates a growing advisor base through MBA programs. Participant 7 started his career as an engineer and founded a company that went IPO. With his IPO proceeds, he founded his venture capital firm that he has led for over 20 years.

Although this is a small sample size, these participants show that the background of venture capitalists can be very diverse. Some started in financial services, others in sales or engineering. All participants have in common that they built up a deep and diverse expertise. To note, is that none of the participants have backgrounds in legal or began their careers with independent wealth, such as managing family trusts.

2.5 Interview Responses

1. With how many other investors do you prefer to invest in a venture?

Participant 1

In an early stage, VCs are looking for market validation and scalability

Participant 2

It depends on the business and stage of the business- typically two-three members in each round, and sometimes we will have the same investors in each round or sometimes there will be an additional investor in a new round. This does not always happen and isn't always a good thing. It can be a good thing to have a new investor comes in and makes an independent assessment of what the company's equity is worth. Sometimes you don't want to dilute the investment by adding an additional person. It is beneficial when a new member can evaluate what each new share is worth independent of existing investors.

Participant 3

Investments range from three-ten institutional investors, like insurance companies, and three-five on average.

Participant 5

We do investments by ourselves a lot and we are totally comfortable. Groups of wealthy people tend to pull funds together, and sometimes we will join in if a company already has a term sheet, but there is no true preference. If you have a lot of firms together on a deal managing them can be difficult, so no, we don't prefer the more partner approach.

Participant 6

This answer is more complicated now than five years ago, since there are more funding options now than five years ago. For example, there were not as many crowdfunding sources or funding mechanisms. If you team up, you may have a lot of investors - you could have two big angels or 30. It depends on the company. Generally, fewer is better. It makes the capitalization table less complicated, and there are not as many disparate opinions. Sometimes, if there are a lot of investors, you may organize to have them vote as one group, 50 angels counting as one vote and that’s it. There are other ways to simplify - sometimes they don’t like it, but if they are interested in the company and like the terms, they may accept this.

Participant 7

We are pretty open-minded - it is ok to go in it alone. Sometimes we will invest with an angel, or family member or another firm, but this is not done intentionally. As a rule, the smaller the number, the better. What I have noticed is investors that write the larger checks - say one million and greater - tend to be less loud than angles, for example, who write smaller checks. The smaller the checks, the more pain they are. Investors that write checks over one million tend to be less involved because they already know what they are doing and are not worried about the daily processes of the company. Skill, experience and tenure contribute to the lesser involvement.

2. How many investment opportunities do you review in a year?

<u>Participant 1</u>

Some information on this - if a pitch isn't personally referred, it is already out of the running. Deal flow is so large, more than they can look at in a year. Take the example of 3i, the largest VC in Europe. They once were quoted they received one hundred thousand potential deals a year and looked at none of them.

Referrals are made through networking. First, the entrepreneur should target VCs with an interest in their industry. Then attend live networking events and use LinkedIn to find partners.

<u>Participant 2</u>

About 1,000 each year for the firm. Of these 1,000 submissions, we dwindle it down to about 14 opportunities which are viable. This includes pitches and business plans, some of which come in unsolicited. We are not trying to find quantity as much as quality of prospects received

<u>Participant 3</u>

Personally over 300. As a company, we review hundreds, per person each year. As a company total, over 1,000.

Participant 4

6,000 entrepreneurs have gone through our programs. Many started and blew up, and blew up the second time. Some blew up first, then achieved wild success on the second try.

Participant 5

We have about 500 opportunities a year come through the door, and out of 500 we end up making two-four investments. A lot of businesses are way out of our focus - one time we got a plan from China for an off-shore fish farm. A lot of what we receive are quick, easy passes and we are not going to spend time on those. For the ones we do, we end up setting meetings with (a rough estimate) 150-200, maybe upwards of 200 companies. We will spend an hour with these and hear their pitches, and of those, we will really look into around 150 companies a year and have multiple meetings with them.

Participant 6

My firm reviews about 1,500 in a year. 1% of these are typically highly competitive for funding.

Participant 7

700 for the firm. Out of these, three-four become investments, and five-eight more are viable. They may not become investments for different reasons. These may be opportunities which reach agreement but we don’t close for one reason or another or they decide they’re not going to do it.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

Participant 1

Investment projects are based on the size of the firm's total fund and the number of partners a firm has. The total fund is divided by the number of deals a partner can handle. So, if there is 100 million in the fund and there are two partners, and each deal is ten million, the portfolio will have ten deals and each partner will be responsible for five.

Participant 2

I end up investing in one-two ventures each year, and try to optimize a portfolio of about 13 companies if possible.

Participant 3

This question depends on the type of investment. For equity-based funding, I keep a portfolio of 15-30 investments, and each investment lasts three-six years. An early stage investment would last six years. I have no minimum number to invest, but a year may go by and I didn't invest in anything because I didn't find anything interesting, or other competitors beat out our firm.

Participant 4

In this way, I am different than the average investor – [omitted] was named top three social impact incubators in the United States by UBI Global. Part of my mission is to help as many tech companies get to scale as possible. I want to add to society through accelerating products that change the world for the better. I am not concerned with adding x# of deals in x amount of time; I want to optimize for the long-term benefit of society. I want to realize how can I build a 100 thousand plus network of entrepreneurs. I am looking at it more from an impact standpoint.

Participant 5

So, we typically invest in two-four new start-ups a year, and internal financing is something we do every month. I sit on five boards and observe on another. Ongoing we have about 16-17 companies and three people to be on boards.

Is there a maximum number or suggested number you operate under?

No, it depends on the person and the deal. Our founder sits on ten boards currently - and he says that's too many.

Participant 6

My answer would probably be - the more the better. In order to do a good job managing, though, you would probably need four-eight per partner. Actually, eight would be – ridiculous - six is better. four-six.

Participant 7

Four is about the velocity the firm can handle.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

Participant 1

The stage matters more than the number of people in the organization. What is important is that what they have is what they need. If it is a single individual, it is important that they know what is required. What we look out for is when a single person doesn't know what they need, or doesn't have people because they were unable to recruit talent, or unwilling to fill in their own gaps with additional people. It is important that the entrepreneur knows what is needed and has the minimum people and skill sets required to perform.

Participant 2

Generally, my investments have two-three entrepreneurs. I would not invest in a company of one - if something happens to that person, then what? The venture is gone. When a team has more than seven in it, it becomes harder.

Participant 3

Start-ups are more Angel/seed investing, and my company currently invests in late stage growth, so generally these investors have already been through several rounds of funding.

The answer is yes, I would definitely invest in a company of one if they had a track record of success and have done it several times before and I have a relationship with them. I have invested in a single member company before - there is a man who has proven success and I will invest in anything he presents. That said, I would not invest in a one-man-band I was not familiar with who came up with to me with an idea.

Participant 4

For founder teams, the most successful are two-founder teams. One can cover voice of customer, the other side is manufacturing. In a two-person situation, they seem to more naturally able to handle those roles. With groups of three or more there are typically communication problems. One-person start-ups there is usually too much blindness, or not enough perspective, or the founder is limited because they can't be available or present 100% of time.

Participant 5

To answer this question, you need to define startup. Our seed investments start at 250 thousand, 500 thousand and about one million. We mostly invest in series A and B and some C. However, you have to understand that an Austin Series A and a Silicon Valley series A are different. A series A in Austin is around three million, and that would be a series C in Silicon Valley. A Silicon Valley series A is more like eight-ten million. If you are talking about seed investments that have no present customers, we currently do not invest in those. We typically do not get individuals - we want the business to be at least at a stage that we can see the product and the business has tens of thousands of recurring revenue. A class C investment would already have 12-13 million a year and would not be as risky, whereas a company turning three-four million is not proven yet, and not as viable. You increase the risk/reward as you go up, so a company making less revenue would have more risk, and you should earn a higher return on a company you funded from a napkin.

Participant 6

The number of people employed depends on the stage, Earlier on they need fewer employees, later they will need more. After signing for funding, they need to staff up like yesterday. It's not a one-shoe-fits-all approach.

For teams, three-five founding members is a great team. Minimum three. If there are less than three, there is not enough group dynamic the efficacy of the team. It is harder to tell whether the team agrees or disagrees. For example, if a team member is answering a question and someone disagrees and interrupts the person answering, it can be refreshing. It shows that they are a collaborative team and are able to come to conclusions together. You can also see when the interruption is disruptive, and one team member's viewpoint is radically contrary to another. There is a difference between collaborative and combative. With one person, well, you can't really see them argue with themselves.

Participant 7

Yes. One founder is ok. More often you will see two or three or four. Maybe two is the most common, I don't know the actual statistic. We don't typically do seed investments. At the firm, we mostly do series A, so the company already has 10-15 employees, maybe 20. For numbers of founding members, think smaller, single digits.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

<u>Participant 1</u>

A lot - first the analyst takes the business plan apart, then there are several less structured meetings, and a lot of back and forth questions and answers. They are trying to probe - then comes the term sheet., the offer to fund. There is at least one meeting to negotiate, and the whole process from start to finish can take three-six months. There is one term sheet if there is a lead investor, and other investors join in. Sometimes an investor will only put capital in if the founder can find another investor for the rest of what is needed.

<u>Participant 2</u>

It takes several rounds of meetings with an entrepreneurial team before I make the decision to invest. We will meet about six times as I gather more information and background checks and find out more about the individual.

<u>Participant 3</u>

N/A – relevant to start-ups, small investments.

<u>Participant 4</u>

Easily 100. Lots of examples where the entrepreneur had 50-60 meetings.

<u>Participant 5</u>

This can vary widely; I'd say the fastest I've seen is three in-person meetings before making a decision to invest. Usually I will meet people for coffee, or they will come into the office and give a presentation, and if so sometimes I will have a junior associate sit in. We will spend one to two hours listening and asking questions.

In the best case, follow-up with a "3Q Diligence Day." We call it a 3Q Diligence Day because it takes three-quarters of a day going over every aspect of the business, including history, tech development, roadmap, financials, everything - and decide after that whether or not we will offer them a term sheet.

For other investment opportunities, there will be a lot more meetings. We will find their customers and ask questions about their product, check the competition, and have ten meetings or so. After this, if we still have questions, we may have to dig in deeper into the total market and other factors. I have followed one company for over five years, and have watched them switch their business model, and met with them six-eight times without having funded them.

<u>Participant 6</u>

By the third meeting, you should have a good understanding whether or not you want to fund the company. After that, you are looking at additional information and the terms of negotiation. If you are the lead investor, you're creating the term sheet. Afterwards, you can ask for a due diligence checklist. It is basic but fundamental - checking financials, IP, whether or not they have a bank account, if they keep their receipts in a shoe box. We actually had a company who kept all their receipts in a shoe box! At that point, you let them know they have to hand it over to an accountant to create financial statements. So between handing out the term sheet and actually signing it you engage in due diligence.

Participant 7

First, we see market data, look at the financial plan, then spend half a day in a meeting with the company for high diligence. After that we find experts on their products. This process takes about four-six months. Then when we decide to invest, we will meet another five-eight times to discuss terms. We also can take a long-term approach to looking at businesses. In some cases, we are not unwilling to wait and watch the company for an extended period of time. For example, there was a company we watched for five years before investing in. If we are going to invest right away, we should know this by meeting eight. If it's a long-term approach, we could have 20 meetings before taking any action.

6. What is the average amount that you invest in a project?

Participant 1

The project amounts are based on the fund size and the number of investments currently funded. If there are available funds, it doesn't mean the whole amount is available for one deal.

Participant 2

This also differs depending on the stage of the business and the amount needed. Some businesses that come to me do not need funding at all. For the ones that do, it can be up to four million for an individual round, depending on the company. On a broad range, the typical initial investment is one to two million.

Participant 3

Varies.

Participant 4

Investment is access to network more than capital

Participant 5

We typically invest five million. The minimum for our firm is three-five million.

Participant 6

Generally, I invest 250 thousand-500k thousand per round, and expect to engage in three rounds per company. You need to have a follow-on investment or you can get washed out. For example, if you fund a 900 thousand company with 100 thousand, the valuation is at one million and you own 10%. Then the company is successful in raising five million. Now, you are responsible for 500 thousand, or you lose your initial investment of 100 thousand. This is the dilution aspect.

Participant 7

This depends on how you break down the amount. Our check size for the first round can range from 2.5-8 million. Over the life of the investment this can be 6-30 million. For a series A investment, the check size is three-four million on average. For series B it's more like five million or six million. It depends on the stage of the company.

7. What is your target return rate? What is your average return rate?

Participant 1

What venture firms typically expect is five or six of their deals will bust. Two or three will bring the return that was put in, and one to two will be homeruns, and have a huge return. These will make up for all the others. Of course, venture firms are also under pressure to perform - they need to make money for their investors or they will withdraw.

Participant 2

41%, 45%.

Participant 5

It is all about risk and reward. In real estate, for example, they might target in the mid to late teens. In private equity, in late stage buyouts would expect 20-30% returns, and asset-class slightly higher than that. Our targets are in the 30-40% ranges. Venture capitalists are in the highest asset class. If investors are only getting a 25% return, they could go to private equity, which is less risky.

Participant 6

We don’t share that information. I can tell you that the industry average puts VCs at a 700-800 basis above the S&P 500. So, if the S&P is at 5%, VC will be 12-13%.

Participant 7

We don’t normally disclose an average return rate. Our target return rate is 50%. Actual is less than that.

8. How long have you been in the venture capital business?

Participant 1

I have had three businesses funded through venture capital.

Participant 2

Decades.

Participant 3

About 17 years.

Participant 4

I have had this career 13 years. I began working in Chile in 2003

Participant 5

I have been directly working with VC for seven years, and before that, buyouts for three-five years.

Participant 6

Since 1996. 21 years.

Participant 7

About 17 years.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

<u>Participant 2</u>

Our process is to first look at the executive summary, then dig into the business plan. After that we will invite the entrepreneur to give a presentation. Sometimes the business plan is great and the entrepreneur turns out to be a crazy person. This is an extreme example, but it happens. You need to make sure the person you're giving money to can take it and execute, that they are going to do what they say they will do.

Qualities I look for in the entrepreneur are attitude, the ability to be persistent. They need to be able to take adversity and learn lessons. In other words, if something isn't working, they can change directions. The entrepreneur needs to really be committed to what they are doing when implementing an idea and really believe in it, instead of continuing to change their minds.

In things that I would avoid – this is the type of judgement where you know it when you see it - you can't articulate it. One indicator is when their only aptitude is to express mental superiority. When their ego gets in the way and they are unable to relate to others. They can't speak in a way that others can understand. The company founder needs to be able to stand behind their product or service and have the ability to comfortably interact. If the entrepreneur can't sell their product this does make a difference.

Other times I need to use due diligence to uncover their past environments. For example, you need to be able to trust that if they say they will spend x number of dollars on y that they won't spend it on z without explaining why, or without telling anyone they are spending it on z instead. This is the type of thing you want to try to avoid.

Participant 3

Yes, I usually start with the pitch/presentation, no business plan-it's pretty much the same thing. In my industry, I have to be opportunistic. I receive leads through relationships and proprietary deal flow.

Participant 4

Traction - nothing else counts. I want to hear this within the first 30 seconds of an entrepreneur's pitch. The German-style is to tell you about their education, their background, and why they're so important. The method for those in Latin America is to do everything they can to build a relationship with you. Chileans want to first establish how you know each other. Koreans lead their pitches with technical and product information. The American way, I like to say, is to talk about traction. I want to hear that you already started x and you already have something moving before you say anything else - even before I know how it works. Traction means the business is making money.

Participant 5

I'll start with the pitch. I assess the team, their experience, and the market's opportunity - does the product work? Will people buy it? How many people would buy it? How much would they pay?

I want the entrepreneur to ultimately answer the questions, why should we buy this product? Why buy it from them? Why buy it now?

When providing venture funding, almost all the money goes to hiring people - I need a CEO who can tell a story and recruit people. If the answer is ‘no,’ I would not invest. If you don’t have a CEO who is convincing, you do not have a company. It is a good sign when the company already has seasoned professionals early on who have agreed to join, (sometimes for less pay) the new company.

Participant 6

Are they believable? Does their presentation build trust? I do both, usually. My team reviews the information first, then I listen to the entrepreneur’s presentation and I have the data available to me. After I listen to the pitch, I dig into the team’s data.

Participant 7

Clarity, self-honesty, market understanding - we really need a crisp view of opportunity size, and the sales model - unit economics. What about the team - do they have who they need? Defensibility of technology, customers. It takes about five minutes to understand whether or not I’m interested in the business, or sometimes it takes a little while.

I try to the pitch first, along with the overview and financial plan. Of course, you can get inundated hearing pitches five times a day. You need content first. The entrepreneur’s goal should be to get investors to a ‘no’ as fast as possible.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

Participant 1

Everyone wants to invest in a winner. Failures can be due to two things: 1) It was either out of the person's control, or 2) It was within their control.

1) If it was out of their control, it may have been a bad idea or just bad timing. For example, the stock market crash in 2001 put several businesses out - including mine. It was something that happened quickly and was not foreseeable.
2) If it was within their control, the entrepreneur has to be able to articulate the problem and not reproduce it. This can be harder to prove.

Participant 2

When looking at a potential investment, I check the individual's track record, who they have worked with, their employment history - their references, the skills they possess and how they relate to the company they are starting. I look at their resume, but this is just the beginning. I talk with other people they know - friends, relatives, and people they have done business with. I try to get a good picture of their character. At a later stage in the review process I also do background checks and find out more about their business connections.

Participant 3

Failure creates a higher bar. It depends on their story - was the failure out of their control? How did they react to it? Failure by itself is not categorical, but it is a grand indicator of replication. If the entrepreneur for example showed poor character, or had a lack of collaboration in the process, well, life is too short to spend time on those ventures.

Participant 4

Nothing teaches a stronger lesson than scar tissue. Not the best way to learn, but happens to be the one I've done the most. An entrepreneur is a lifelong learner. In my experience, the successful ones are the ones that have that long-term outlook. Some get lucky, but then some use failure as a springboard for future success.

Of course, there are also those that repeat their mistakes and their start-ups are destroyed again and again. Entrepreneurial failures are not necessarily out of their control. Being an entrepreneur forces self- reflection much more than in a traditional corporate business-setting. Great visionaries like Rich Branson and Steve Jobs were reflective entrepreneurs. The founder of Enron would be the contrary.

Participant 5

The origin of this question to find out whether an investor is adverse to an entrepreneur that had failed or even may prefer one because that entrepreneur had learned the lessons.

Having and entrepreneur with a positive track record of building and selling companies is great. Those who have failed can also be very interesting. Having an entrepreneur with past failures doesn't scare me in the least - but I want to know what happened, and I would want to do due diligence. This kind of entrepreneur has probably learned more lessons than the one who has always had success. I would rather fund an entrepreneur that has had a failure than someone who is starting a company for the first time.

Participant 6

The entrepreneur may have a previous experience with failure and it be real positive or negative. How they frame it is super important. If they say, 'Yeah, well I couldn't get enough VC funding' - that's no Bueno. If the entrepreneur says they failed because they failed to manage a critical factor such as the supply chain - it is ok if they can elaborate on the problem and what they learned. Just having flippant dismissal or blaming the failure on outside factors does not build credibility.

Participant 7

We've all had successes and failures. I want to understand their track record, where they've worked and their character. Do they have blind spots? How do they speak about their failures? Do they try to cover it up or do they bring it forward? The level of self-honesty is important to read.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

Participant 1

Today, there are many ways to access funding, because of two dynamics: 1. It is cheaper than ever now to build products, and 2. There are alternatives to raising capital now that didn't exist before, and people need less capital for business growth than ever before.

Websites like ‘Kickstarter’ are an example of this. Some businesses may not need funding, or, may not need venture funding.

Participant 2

Some people just need money because they need money. Sometimes they have the means to accelerate. There are many ways to receive funding: you can have your customers prepay, which is effectively crowdfunding, or engage as a service at the end of the day.

Some owners ask for money too soon. By the second or third round they own so little of their company, there is no incentive to keep growing. Some people tell me, “If we only had venture capital.” Money is a commodity, and there are other resources if you need it. Some see capital as an end. In truth, it is the beginning of a new chapter in the life of your business, and you need to know what you are going to do with it. It is a new beginning. Some spend all their time looking for money and they don’t realize they now have a responsibility with it.

Participant 3

N/A - small stage.

Participant 4

There are so many people that say they need it, and most will not receive it. I tell entrepreneurs initially to see how to build a business without getting funding. This is a healthier approach, but it’s not always possible. There are certain businesses that shouldn't be funded, but people get stuck on the notion. One example was a simple business that was self-sustaining and the entrepreneur was so obsessed with the idea of getting funding that he eventually got exasperated and threw in the towel. Some entrepreneurs don't understand it can take as long to get funding as to build the business. They should go ahead and build their base product or get their business off the ground.

Participant 5

Sometimes companies ask for capital too early on, and I'll tell them, do these three things and come back in six months. This doesn't mean they don't need funding. Sometimes an entrepreneur will have unrealistic valuation expectations - they want to raise capital at a certain multiple of a valuation and I tell them, 'go do it - I wish you luck.' I have had a person wanting five million in funding, and come back with a one million contribution, probably from someone that doesn't understand business valuation. The entrepreneur asked us for the rest, and we still didn't fund him.

Often before funding, I need to see more milestones, or more sales processes, or often if it's a medical business we need more data.

Participant 6

If their expense structure is very low, or the company can afford to bootstrap, or, they have a high gross margin, or they can be cash flow positive in six-twelve months they may not need funding. It depends on the finance model of the company and whether it has much maturity of business.

If the company has a minimum viable product and minimum viable sales, or minimum viable product and proven sales and is scalable doesn't mean we will invest because it is not necessarily sustainable. It needs to have a proven sales model beyond the company's network to show that it's viable. The company should have a step-by-step process from start to closing. Some businesses develop this proactively - if they do more of this, they get more of that. If a company makes its first sales to friends and family, that doesn't mean it has a proven model. When they continue, and make a cold relationship, with no prior knowledge of the customer that's super valuable. The first sales could be significant, but it's not as great as one cold close to model the company's value. There is a difference between generating revenue vs having a process model.

<u>Participant 7</u>

We often see businesses that should not receive funding such as lifestyle businesses, businesses that won't make more than three-five million, businesses that are profitable on their own. People get caught up in the 'glamour' of VC funding, but businesses don't need it if it will not produce a high rate of return. Doctors, lawyers, dentists-lifestyle businesses like that which have a linear business model. If one of these wants to make more money, they work another day, or put in more effort. Businesses like that should not take money from us.

12. What questions should founders be asking you when you are making a decision whether to invest?

<u>Participant 1</u>

On the term sheet - entrepreneurs should be concerned with valuation, liquidation preference and the board of directors. The valuation dollar amount can be negotiated. The liquidation preference is the percent owned by the investors vs the entrepreneur. The board of directors is the most important part because this can potentially give the capitalist control of the company through washout or recapitalization.

<u>Participant 2</u>

Do we have the skills in the areas we are representing? Are we going to be a good partner vs. a dominant one? Are we going to help them in the areas they don't know as well? Is the entrepreneur going to be treated like a human being, or are we going to talk and bother them daily and they don't have time to run their business?

<u>Participant 3</u>

Often there are companies which are given several investment proposals. When founders are deciding between investors they need to ask, 'Who can help me the most? Are they experts in my industry? What is the reputation of the firm? What references do THEY have?' Entrepreneurs should also look at this in the same way you look at a marriage. At first everything is perfect, right? But it's hard and it takes work. The business relationship can also be incredibly stressful and difficult at times, and people will want to bail out, then it becomes a matter of whether you trust and depend on the people you're working with. Sometimes the entrepreneur will take whichever firm provides more capital, and this is the wrong way to look at it. If the venture is successful, the difference in funding turns out to be a rounding error, and the principal value is not going to matter. Entrepreneurs need to ask, 'Who is going to be the better partner?'

<u>Participant 4</u>

Do I really want money from this guy? Do I really need money? How long do I think this investor will keep me? Are they committed to me or to the business? Entrepreneurs need to understand that when you take money you become an employee, and it is no longer driven by you.

The other side of this is knowing when to take funding. There were two separate times when I should have taken outside funding. You can make mistakes both ways.

<u>Participant 5</u>

They should do reference checks on VCs. Some venture firms are low touch and some are high touch - we are high.

Has the firm invested in the city where you're located? At a minimum, that VC is committing to travelling to that location at least four times per year for at least the next 5 years. If they are not already committed to that area they may not be all in or may not have investigated the market. Our position is to invest in Texas and invest locally. It is also very important when recruiting talent, and being local is the key to doing that.

They should also ask how much dry powder is left in the VC fund. For example, the firm may invest five million and have another four million or five million on reserve.

Participant 6

The entrepreneur should be doing due diligence before receiving a term sheet. They should check the investor's reputation in the market. They should look at prior portfolio companies and talk to other partners. I am always happy to share the numbers of other CEOs. Due diligence is not so much asking as doing their homework. The entrepreneur should come already knowing I'm a valued investor and that I specialize in their industry.

Participant 7

Would I like to work with you? Can I talk to someone that works with you? What is my role in the future - product, lead, sales? Ask the hardest questions today, because in the future when things get hard you need to be able to calm down when under pressure.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

Participant 1

Depends on the terms of the contract

Participant 2

Sometimes I take on a board position, attend monthly meetings, or help with issues the company is facing.

Participant 3

For equity investments, we become shareholders in the firm. For some investments, we become board members, help recruit executives, manage and oversee different aspects of the company. We are not interested in operating the day-to-day functions of the company.

Participant 4

My network is my most valuable asset. That, and my pattern recognition to problem sets. I am also able to give creative solutions to problems. These three things are more valuable than any funds I can offer.

Participant 5

Post investment, we are talking with the founder every week, and hiring. We also help with bizdev and analytics. There was a credit card company we invested in who was getting a lot of chargebacks, and thought it may be due to the timing of the machine - we ended up doing several weeks' worth of research, collecting data and analyzing it, and ultimately found out the root cause - though it wasn't what the founder suspected. In VC, most of the funds go toward recruiting talent, and sometimes you have to hire people fast. There is no better value I can add than through my network. I spend a significant amount of my time meeting with people who are looking for jobs and I recruit salespeople, executives and interns, usually people director-level and above.

Participant 6

I become a board member, help hire, mentor, fire. I help with the company's compensation strategy, advise, domain expertise. I help in ways that accelerate their business.

Participant 7

Different funds have differing levels of participation. Some are low touch and will come in for quarterly feedback and then leave. We are a high-touch firm, we communicate with the portfolio companies at least monthly, if they grow past a certain size it can move to quarterly, but I've noticed that the most experienced CEO's call me the most, and the least experienced call me the least - it's almost like they feel they have to prove they can do it all themselves. The experienced ones know relationship matters when hard times hit. So there are many CEO's that talk and email on a regular basis.

So, a sales leader may have lead the company to produce ten million in revenue, but doesn't necessarily have the level of discipline to bring the company to 50 million or 100 million and he's never done it before, we may need to find him a new role in the next twelve months. The person may need headlights to be able to identify problems. We need different people at different phases.

When you've built 35 or more companies you start to see patterns and can spot a disaster happening, and develop pattern recognition.

14. What other business experience do you have?

Participant 1

I have owned and managed startups for 15 years, managed sales of a fortune 150 company for ten years, and teaching/nonprofit for ten years.

Participant 2

I started out training to be a chartered accountant, then did some work in M&A, then created a startup myself. I leveraged my financial background and M&A experience in marketing, project management and sales to a point where I had those skills. Now, I have more experiential expertise vs. those with financial engineering. Financial engineers are obviously needed - they bring something different to the table, and you need both at different times.

Participant 3

Founder, investment banking, business development, finance, strategy, analyst.

Participant 4

I built seven of my own startups that got to interesting levels.

Participant 5

My background is in finance, banking and buyouts. One of my partners has a strong technical engineering background, so we complement each other well. I like to say I have enough tech knowledge to be dangerous, but it helps to have an expert in the industry you are looking at funding.

Participant 6

For my capstone paper in college, I wrote a business plan for my family's business. I built, ran and sold the business, and my parents were able to retire. I was one of the only people in Austin at the time who had done this. I liked the challenge, so I made a career of it.

Participant 7

Product development was a big one. I also built my own startup - so I have empathy for the entrepreneur, and can relate to the joys and the challenges. I lead people in the company for over four years, and experienced things not unlike what they're going to see - a lot of similarities that are very relevant.

15. What industries do you specialize in? Are these the only industries you fund?

Participant 1

AI, healthcare, internet of things, autonomous vehicles.

Participant 2

I specialize in information technology, energy-related technologies, advanced materials and communications, but I consider other areas as well. When identifying new markets, I research to learn and understand until I have enough knowledge to consider looking at deals. I research about the business model in a specific sector, how the industry works, the differences in them. There is a lot to learn. We're open to them, but the probability of receiving funding is a lot higher in one of our current areas of expertise. It has to be an area I understand. If someone handed me a business plan on Uber, a transportation system without owning a single vehicle fleet - I would have to investigate how a model like that could work without owning any assets. One needs to understand the difference between clean tech vs. not clean tech in the oil and gas industry, as another example, and basic knowledge about these industries is always helpful.

Participant 4

Impact innovation, HC analytics, education technology, smarter commerce (includes cognitive computing), water, mental health.

Participant 5

I specialize in medical and software. Sometimes I fund medical pre-revenue with early-human trials. There was a startup which had a new way to remove tattoos. With software, it is primarily B2B, such as solutions financial institutions. I have also invested in direct to customer solutions, scientific devices and food services.

Participant 6

Social media.

Participant 7

Software, SaaS, scientific instruments, med-tech devices.

3 RESULTS

3.1 Time is Worth More than Money

Venture capitalists have time constraints, and reference time as an asset which can be invested or wasted. In the interviews, venture capitalists often refer to their activities as 'spending' time meeting others, 'spending' time on ventures, or even 'spending' time listening to pitches or reading business plans. The amount of time which is being processed is optimized, through speed and efficiency. Venture capitalists state they have to be 'opportunistic' and are not interested in 'day-to-day functions' which can be taxing on efficiency. When acquiring a new investment, acceleration is key to growing the business as well as a quick exit. In these cases, participant 5 mentions having to 'hire people fast' and participant 7 relates to this by depicting an urgency when a business is funded, stating they need to 'staff up like yesterday'.

Time constraints also come into play with the way information is received and processed. The time it takes for a venture capitalist to process a pitch ranges from five minutes to two minutes to 30 seconds. Venture capitalists want to hear the major facts of a potential deal and many do not even read the business plan first, or just the executive summary, or approach the pitch first and then reference metrics and company data only in the framework of their questioning. The time constraint in these cases originates from the venture capitalist and is imposed on the startup or company.

Venture capitalists view business plans and pitches with a negative perspective, asking disqualifying questions to break down the hundreds of plans they see annually into the ones which are viable. It is self-evident that each venture capitalist is looking for a winning company, but instead of using leading questions to determine qualifying factors, they engage in probing questions like ‘why should people buy your product?’ ‘Why buy now?’ and refer to investments related to founders they have disqualified stating ‘life is too short’ to pursue deals with difficult people.

3.2 Venture Capitalist Perceived Value

The venture capitalist and decision makers think of themselves as an alternative to revenue. The capabilities of the venture capitalist to build the business are signature traits of their business models and personal value. ‘Investment is access to my network more than capital’ was said by participant 4 and this sentiment is repeated by venture capitalists related to entrepreneurs. Two participants described their firms to be ‘high touch’, engaging with the venture frequently to give advice, solve problems, hire and also fire employees as needed. Wanting to invest locally in Austin, participant 5 illustrates the necessity of participation in a long-distance venture by recommending quarterly visits on-site over the life of the investment.

The time aspect of the venture capitalist requires understanding the business value in as short an amount of time as possible, comparing the pitch to a resume. Conversely, the venture capitalist invests in entrepreneurs, and entrepreneur hires the venture capitalist, through stating that they should do ‘reference checks on venture capitalists.’ ‘What references do they have?’ When pitching, venture capitalists are very interested in the value proposition of the company. The venture capitalist views their own personal value as their competitive advantage. There is also a competitive undertone in venture capitalist comments related to recruiting desirable investments. 'Who's going to be the better partner?' should be a deciding characteristic in decision making, and conversely, the investment dollar amount itself should be treated as secondary to the firm's reputation, track record and references, since this amount will become 'a rounding error' compared to the value the venture capitalist provides the firm who has high potential.

3.3 Venture Capitalists Are Not Sole Decision Makers

Within venture capital the herd mentality dominates. There is safety in numbers when betting on a company, and venture capitalists require personal referrals through their networks to take a potential deal seriously. Participant 1 solidifies this claim, 'if a pitch isn't personally referred, it's already out of the running.'

And venture capitalists in the interview also recognize the habit of investors who fund conditionally based on the entrepreneur finding multiple investors to back. Often when writing term sheets, there is a lead investor and potentially multiple other investors who will contribute less than the lead. Sometimes the investor will require the company to find a lead before they will contribute. Participant 3 stated he would not fund a single founder if he was 'not familiar with' them.

Participant 3 receives half of his opportunities through relationships and deal flow. Participant 1 named as an example European private equity firm 3i to highlight the importance of referrals. 3i has been quoted of having received investment requests into the six-figures, but only actually funded those that were referred to them personally.

Present Companies decide venture capitalist investments in relation to the total market, the key players and, in some cases, all the players in the market. All venture capitalists look at the total available market, total market expenditure and the way the company fits or can claim this marketspace. Participant 3's model is to 'rank the entire sector of businesses in order of the ones I would most like to invest' as part of his proactive approach to deal finding. The questions 'Who would want to buy you?' and 'Would investors be willing to buy your company?' shows that the company is evaluating the business in the framework of its exit. The company needs to know how they would be 'strategic for another company to acquire' to hold the interest of the investor.

3.4 Reasons for Positive and Negative Precursors to Entrepreneurial Failure

It is a unanimous position that success is easy to for venture capitalists to invest in. A 'track record of success', 'proven success,' and 'a positive track record' are all indicators that an entrepreneur that has been successful in the past knows what it takes to accelerate a business and has already jumpstarted the investor's faith. It is also a good sign when a lot of people are interested in a deal. Still, some interviewees have acknowledged failure in their professional lives, so what is their approach to failure?

Some venture capitalists view past failure in a prospective opportunity as a default negative. No one has decided that failure is an absolute, but it has been viewed as 'a grand indicator of replication' and that the negative experience 'raises the bar' and is recognized as a pattern. Of those who have failed, there has been a repeated pattern of failure evident to the witness. Conversely, some see failure as a positive learning experience at first response. The response 'nothing teaches a stronger lesson than scar tissue' implies empathy. Participant 5 states that 'those who have failed can also be very interesting' and continues to mention the lessons learned because of failure are more valuable to greater future success than the past mistake. This represents failure in an unconditionally positive light. The same interviewee also favors the failed entrepreneur to the green one.

3.5 Indicators of Entrepreneurial Success: Timing

Short of having a record of successful startups and exits, there are indicators which will increase the likelihood of venture capitalist funding:

Venture capitalists want to know and understand the traction related to the company. Since not all venture capitalists invest at the early stages in a startup, the company must have already demonstrated high growth and the need for funding. In addition, the company needs to prove its product in the market and that the product or idea is capable of growth to a mass market state. In addition, interviewers suggest an urgency factor to their decision making. They ask timely questions such as 'why buy now' and expect, in most cases, to have an answer in the least possible amount of time.

3.6 Indicators of Entrepreneurial Success: Network

When venture capitalist investors look at the founding members, they measure 'who they have worked with' and their 'business connections' as indicators of potential for success. The network of the entrepreneur is valued highly by the venture capitalist and they see the entrepreneur as the main spokesperson for the company. Since referrals often come through the venture capitalist's network, building relationships to firms, accelerators and incubators, and establishing connections via social media are important to building awareness and trust.

3.7 Character Traits

The interviewed venture capitalists have communicated there are personality and character traits they seek in the founder, not just predicted success of the business. They have indicated there are individual 'success' indicators which should be apparent to the venture capitalist, including 'self-reflection,' 'showing character,' 'self-honesty' and 'collaboration.' There are also demonstrative abilities company leaders should possess which are valued by investors, such as the ability for others to trust you and want to follow you. A 'CEO who can tell a story and recruit people' is necessary for growth, and it is a 'good sign when seasoned employees already want to join.' Participant 5 argues that there is no company if the CEO is not convincing.

4 DISCUSSION

4.1 Time is a Discriminating Factor

For a company to get large-scale funding from investors, they must provide a sense of urgency for accelerated growth, and link the funds requested to this growth. The San Francisco-based Pitch Clinic advises to make this urgency subtle and true, but to let investors know if other investors are looking at your company (Soorjoo 2017). Venture capitalists are looking for the right time to invest in the company, not just the right company. Entrepreneurs should also focus on this and that the earlier stages are not necessarily the best when bringing in funding, because the venture capitalist will demand a higher ownership than if the company has reached a stage of more mature growth (Nunogawa 2017). Instead, entrepreneurs should wait until such a time that the added capital will cause a significant increase in personnel necessary to fuel expansion or the product needs funding to push it to the masses.

When speaking with an entrepreneur, every word should be valuable and every moment optimized. The venture capitalist is looking for a partner who can keep pace, and is committed to using time as an advantage to growing the business. Attempts toward achieving capital should not slow down the process of business growth - it should be portrayed as another business opportunity. Participant 7 stated the goal of the entrepreneur should be to get to a ‘no’ as quickly as possible. This method gives the business integrity and the perception of value.

The venture capitalist founder of Kepha partners wrote about his day, noting that from 5am until after 9pm he is engaged with functions mostly related to his position as a venture capitalist, with minimal time for activities not related to venture capitalist (Tango 2012). A venture capitalist's day is full of research, networking and meeting entrepreneurs.

4.2 More Likely to Get Funded if Referred

Venture Capitalist investors can be divided into a mentality of herders and leaders. The herder mentality requires some distributive risk among other investors. Leaders by contrast, have larger funds and more experience, and have the capitalization and decisiveness to take on risk independently.

Neither wolf packs nor lone wolves are motivated by cold calls and connections due to the importance of networking in high growth companies. It is suggested to get a "warm" introduction to speak with venture capitalists (Iskold 2015).

Venture capitalists receive business plans from all around the world (Wagner 2013) and many of them are never read. To get an audience with a venture capitalist, cold calling can be more damaging than helpful. The venture capitalist is very aware of his or her time and expertise, so passing a business plan to mass venture capitalists will not be helpful if your plan does not fall into the category of their knowledge or interest. It may also be passed over without a personal introduction, since there is no diligence in seeking out the investor who is the right fit for the company. Venture capitalists see an introduction as an obvious step to obtaining capital, yet they see many not going through the tie and effort to do so (Wagner 2013). Networking to meet the individual venture capitalist will make an impact on their evaluation.

4.3 Wolf Pack

The 'wolf pack' mentality takes on the approach that more investors interested in a company is more favorable than fewer, and that entering in on an investment opportunity alone is not optimal. These are also heavily dependent on their network for support, guidance, and to build the confidence of others to participate in an opportunity. Herders also exhibited the quality of calling prospective buyers of companies or product contract purchasers to see if they would potentially be interested in the company needing funding. The herder also looks at the total available market, and seeks out players in this market for associative confirmation that the potential investment is differentiated or a market leader.

Since wolf packs are interested in minimizing risk through partnering in investments, the warm introduction is also a way to show an association to trusted members of their personal network. Successfully achieving a referral is a signal to the venture capitalist that the entrepreneur can be trusted and will reduce assumed risk, ultimately speeding up the evaluation process (Iskold 2015).

4.4 Lone Wolves

Lone Wolves take the approach that judgement of the success of an opportunity lies in their industry expertise and their own decision making abilities. They are not concerned with networks or names. I was in the office of one of these firms and the interviewer did not ask who else I spoke with or how I was referred. They were not interested in my social credentials which contrasts with the herder. However, the herder is also more open to building relationships and giving out referrals as opposed to closed communication.

Literature suggests that that the wolf pack mentality is more frequent among venture firms, and that venture capitalists use this as a way to mitigate risk (Zider 1998). Still, the network may get you closer to the radar of a firm even if it is not a determining factor for funding. Referrals through the network will help establish credibility, and keep the idea from being overlooked (Dekker 2015).

4.5 A Venture Capitalist’s main resource is not capital

Empirical research indicates venture capitalist firms with a ‘high reputation’ are worth more to entrepreneurs than ones without (Paul Gompers 2006), and becomes a determining factor to a company with multiple deals (Hsu 2004). Hsu further quantifies this relationship with the following equation:

Pr (Offer accepted = 1) = F(VC Reputation, Valuation, Controls) (Hsu 2004).

Within a multiple investment opportunity for the entrepreneur as the control, this equation determines the likelihood of an individual investment firm’s offer to be accepted. The success factor has also been concluded that the first-time entrepreneur derives value from the venture capital expertise, network and background, but those with previous success do not (Gompers, et al. 2017). The entrepreneur with previous success is subsequently able to receive funding at an earlier stage since their success is perceived by the venture capitalist as talent. The empirical literature along with the results of this study imply there is an inverse relationship between the functional value of the venture capitalist and the success (and subsequently perceived value) of the entrepreneur. In sum, the value of the venture capitalist is worth less to the entrepreneur with a track record of success than one with previous failures or a first-time founder.

4.6 Failure is like Kryptonite

Failure in the context of the venture capitalists and decision makers in this case study has been represented as an evaluative process, with both positive and negative precursory dispositions. However, both the default positive and default negative positions are linked in that if out of the entrepreneur’s control, it is beneficial, or if in control and learned from it. Negative if in control and did not learn from it - shows pattern/repetition. “What is much more important is how you fail and how transparent you are throughout the process” (Forrest 2014).

If both sides feel the same, but some have a negative outlook, failure must be prevalent in the venture capitalists historical operant conditioning and frequency of reinforces related to the volume of entrepreneurs who have failed in the past (McLeod 2015). Entrepreneur Magazine quotes a second-time success story entrepreneur: "I think you are better prepared, mentally and financially, but you never know if it's going to be successful. That's called maturity" (Wang 2013). Other entrepreneurs cite confidence and timing as reasons related to success after failure (Wang 2013).

As a third result to failure, the venture capitalists with the longest tenure in the industry had an objective precursory approach to failure. These two were the most experienced investors, and had track records of several well-known, successful companies. The fact that they did not see failure as either positive nor negative on the onset shows that after a certain level of tenure, failure can be seen on a truly case-specific basis, without bias. These more tenured individuals also encompass the leader mentality as it applies to funding referral.

Failure should be approached with honesty, openness and conviction. Since those who have failed already know the warning signs, some investors find failure to be a positive trait, in the right context. Know what your personal failures are and you know your weaknesses. Superman already knows his weaknesses, so all he needs to do is avoid them and he is invincible.

4.7 Qualitative Ingredients for Entrepreneurial Success

Assuming financial predictions toward the prospective venture are positive and sufficient, the resulting factors are key to receiving a positive perspective from the venture capital vantage point: urgency of funding to accelerate growth, the network in and around the entrepreneur, and the entrepreneur’s honesty. Mark Suster blogs that in his experience, funding comes down to 4 things: management, market, money and momentum (Suster 2010). Of the four, conveying a sense of urgency can suggest momentum and the character of the entrepreneur and his or her network is tied to management.

Of these three indicators found in the case study, a follow-up questionnaire was developed to rank the relative importance of each indicator towards the venture capitalist's decision to invest, and a hierarchy emerged. The results are as follows:

1. Honesty
2. Network
3. Urgency

Results from the follow-up questionnaire show honesty as the most important ingredient of the investor's funding decision. Venture capitalists view honesty as the foundation of trust in the partner relationship between entrepreneur and venture capitalist. Network is also important, and urgency is always relevant, but the financing decision will go to the company whose leaders can be trusted that the millions of dollars invested will serve to grow the company and that the firm will be able to collaborate to make the best decisions for the interests of all interests involved.

5 EPILOGUE

5.1 Insights and Recommendations from the Experts

Founders that are in an accelerated growth state in the business, or need funding to get their business off the ground, should exhaust all other means before pitching to venture capitalists. Participant 4 cautions in his interview that accepting funds from venture capital means the founder will 'become an employee' since the firm now owns part of the company, and has a say in the way your company is run. Participant 1 asks the founder to introspect whether money is even needed, since it is cheaper to build products now than ever, and alternatives like crowdfunding can help startups with less expense to the company itself.

5.2 Insights and Recommendations from the Venture Capitalists

The founder should approach venture capital when the business has outgrown other types of funding options and their company has become desirable enough to create competition among venture capitalist firms. For a good fit with the business, and the founder, It is vital to do due diligence to choose the right firm. This case study suggests factors to consider are references, communication, industry specialization, likeability, ability to apply foresight, and firm complementation.

Qualitative venture capital opinions are useful in determining perception and preparing to request or receive funding to accelerate growth, but it is not the only option for entrepreneurial growth. In the words of the accelerator-experienced interviewee: ‘In the meantime, build the business’ because ‘most will not get venture capitalist funding.’

APPENDIX SECTION

Definitions

Startup

A startup company is an entrepreneurial venture which is typically a newly emerged, fast-growing business that aims to meet a marketplace need by developing or offering an innovative product, process or service (Wikipedia 2017).

Seed stage

The state of a company when it has just been incorporated and its founders are developing their product or service (Buyouts Insider 2016).

Early stage

The state of a company after the seed (formation) stage but before middle stage (generating revenues). Typically, a company in early stage will have a core management team and a proven concept or product, but no positive cash flow (Buyouts Insider 2016).

Washout round

A financing round whereby previous investors, the founders and management suffer significant dilution. Usually as a result of a washout round, the new investor gains majority ownership and control of the company (Buyouts Insider 2016).

Recapitalization

The reorganization of a company’s capital structure

Term sheet

A document confirming the intent of an investor to participate in a round of financing for a company. By signing this document, the subject company agrees to begin the legal and due diligence process prior to the closing of the transaction. Also known as “Letter of Intent” (Buyouts Insider 2016).

Dry powder

Money set aside as reserve funds

Biz dev

Business Development, building and fostering business relationships, that can range from partner, to OEM, and joint venture relationships, that are short of capital investments.

Deal flow

A measure of the number of potential investments that a fund reviews in any given period (Buyouts Insider 2016).

Angel

A wealthy individual that invests in companies in relatively early stages of development. Usually angels invest less than $1million per startup (Buyouts Insider 2016).

Complete Surveys

Participant 1

1. With how many other investors do you prefer to invest in a venture?

Investors like strength in numbers - it is more interesting if lots of people like a deal. It is a herd mentality, and if there is more competition, the entrepreneur gets a better deal.

In an early stage, VCs are looking for market validation and scalability

2. How many investment opportunities do you review in a year?

Some information on this - if a pitch isn't personally referred, it is already out of the running. Deal flow is so large, more than they can look at in a year. Take the example of 3i, the largest VC in Europe. They once were quoted they received one hundred thousand potential deals a year and looked at none of them.

Referrals are made through networking. First, the entrepreneur should target VCs with an interest in their industry. Then attend live networking events and use LinkedIn to find partners.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

Investment projects are based on the size of the firm's total fund and the number of partners a firm has. The total fund is divided by the number of deals a partner can handle.

So, if there is 100 million in the fund and there are two partners, and each deal is ten million, the portfolio will have ten deals and each partner will be responsible for five.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

The stage matters more than the number of people in the organization. What is important is that what they have is what they need. If it is a single individual, it is important that they know what is required. What we look out for is when a single person doesn't know what they need, or doesn't have people because they were unable to recruit talent, or unwilling to fill in their own gaps with additional people. It is important that the entrepreneur knows what is needed and has the minimum people and skill sets required to perform.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

A lot - first the analyst takes the business plan apart, then there are several less structured meetings, and a lot of back and forth questions and answers. They are trying to probe - then comes the term sheet., the offer to fund. There is at least one meeting to negotiate, and the whole process from start to finish can take three-six months. There is one term sheet if there is a lead investor, and other investors join in. Sometimes an investor will only put capital in if the founder can find another investor for the rest of what is needed.

6. What is the average amount that you invest in a project?

The project amounts are based on the fund size and the number of investments currently funded. If there are available funds, it doesn't mean the whole amount is available for one deal.

7. What is your target return rate? What is your average return rate?

What venture firms typically expect is five or six of their deals will bust. two or three will bring the return that was put in, and one to two will be homeruns, and have a huge return. These will make up for all the others. Of course, venture firms are also under pressure to perform - they need to make money for their investors or they will withdraw.

8. How long have you been in the venture capital business?

I have had three businesses funded through venture capital.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

Everyone wants to invest in a winner. Failures can be due to two things: 1) It was either out of the person's control, or 2) it was within their control.

1) If it was out of their control, it may have been a bad idea or just bad timing. For example, the stock market crash in 2001 put several businesses out - including mine. It was something that happened quickly and was not foreseeable.
2) If it was within their control, the entrepreneur has to be able to articulate the problem and not reproduce it. This can be harder to prove.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

Today, there are many ways to access funding, because of two dynamics: 1) It is cheaper than ever now to build products, and 2) there are alternatives to raising capital now that didn't exist before, and people need less capital for business growth than ever before. Websites like 'Kickstarter' are an example of this. Some businesses may not need funding, or, may not need venture funding.

12. What questions should founders be asking you when you are making a decision whether to invest?

On the term sheet - entrepreneurs should be concerned with valuation, liquidation preference and the board of directors. The valuation dollar amount can be negotiated. The liquidation preference is the percent owned by the investors vs the entrepreneur. The board of directors is the most important part because this can potentially give the capitalist control of the company through washout or recapitalization.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

Depends on the terms of the contract

14. What other business experience do you have?

I have owned and managed startups for 15 years, managed sales of a fortune 150 company for ten years, and teaching/nonprofit for ten years.

15. What industries do you specialize in? Are these the only industries you fund?

AI, healthcare, internet of things, autonomous vehicles

Participant 2

1. With how many other investors do you prefer to invest in a venture?

It depends on the business and stage of the business - typically two-three members in each round, and sometimes we will have the same investors in each round or sometimes there will be an additional investor in a new round. This does not always happen and isn't always a good thing. It can be a good thing to have a new investor comes in and makes an independent assessment of what the company's equity is worth. Sometimes you don't want to dilute the investment by adding an additional person. It is beneficial when a new member can evaluate what each new share is worth independent of existing investors.

2. How many investment opportunities do you review in a year?

About 1,000 each year for the firm. Of these 1,000 submissions, we dwindle it down to about 14 opportunities which are viable. This includes pitches and business plans, some of which come in unsolicited. We are not trying to find quantity as much as quality of prospects received.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

I end up investing in one-two ventures each year, and try to optimize a portfolio of about 13 companies if possible.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

Generally, my investments have two-three entrepreneurs. I would not invest in a company of one - if something happens to that person, then what? The venture is gone. When a team has more than seven in it, it becomes harder.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

It takes several rounds of meetings with an entrepreneurial team before I make the decision to invest. We will meet about six times as I gather more information and background checks and find out more about the individual.

6. What is the average amount that you invest in a project?

This also differs depending on the stage of the business and the amount needed. Some businesses that come to me do not need funding at all. For the ones that do, it can be up to four million for an individual round, depending on the company. On a broad range, the typical initial investment is one to two million.

7. What is your target return rate? What is your average return rate?

41%, 45%.

8. How long have you been in the venture capital business?

Decades.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

Our process is to first look at the executive summary, then dig into the business plan. After that we will invite the entrepreneur to give a presentation. Sometimes the business plan is great and the entrepreneur turns out to be a crazy person. This is an extreme example, but it happens. You need to make sure the person you're giving money to can take it and execute, that they are going to do what they say they will do.

Qualities I look for in the entrepreneur are attitude, the ability to be persistent. They need to be able to take adversity and learn lessons. In other words, if something isn't working, they can change directions. The entrepreneur needs to really be committed to what they are doing when implementing an idea and really believe in it, instead of continuing to change their minds.

In things that I would avoid – this is the type of judgement where you know it when you see it - you can't articulate it. One indicator is when their only aptitude is to express mental superiority. When their ego gets in the way and they are unable to relate to others. They can't speak in a way that others can understand. The company founder needs to be able to stand behind their product or service and have the ability to comfortably interact. If the entrepreneur can't sell their product this does make a difference.

Other times I need to use due diligence to uncover their past environments. For example, you need to be able to trust that if they say they will spend x number of dollars on y that they won’t spend it on z without explaining why, or without telling anyone they are spending it on z instead. This is the type of thing you want to try to avoid.

10. How could an entrepreneur’s previous experience (even if a failure) contribute to your evaluation and decision to invest?

When looking at a potential investment, I check the individual’s track record, who they have worked with, their employment history - their references, the skills they possess and how they relate to the company they are starting. I look at their resume, but this is just the beginning. I talk with other people they know - friends, relatives, and people they have done business with. I try to get a good picture of their character. At a later stage in the review process I also do background checks and find out more about their business connections.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

Some people just need money because they need money. Sometimes they have the means to accelerate. There are many ways to receive funding: you can have your customers prepay, which is effectively crowdfunding, or engage as a service at the end of the day.

Some owners ask for money too soon. By the second or third round they own so little of their company, there is no incentive to keep growing. Some people tell me, “If we only had venture capital.” Money is a commodity, and there are other resources if you need it. Some see capital as an end. In truth, it is the beginning of a new chapter in the life of your business, and you need to know what you are going to do with it. It is a new beginning.

Some spend all their time looking for money and they don't realize they now have a responsibility with it.

12. What questions should founders be asking you when you are making a decision whether to invest?

Do we have the skills in the areas we are representing? Are we going to be a good partner vs. a dominant one? Are we going to help them in the areas they don't know as well? Is the entrepreneur going to be treated like a human being, or are we going to talk and bother them daily and they don't have time to run their business?

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

Sometimes I take on a board position, attend monthly meetings, or help with issues the company is facing.

14. What other business experience do you have?

I started out training to be a chartered accountant, then did some work in M&A, then created a startup myself. I leveraged my financial background and M&A experience in marketing, project management and sales to a point where I had those skills. Now, I have more experiential expertise vs. those with financial engineering. Financial engineers are obviously needed - they bring something different to the table, and you need both at different times.

15. What industries do you specialize in? Are these the only industries you fund?

I specialize in information technology, energy-related technologies, advanced materials and communications, but I consider other areas as well. When identifying new markets, I research to learn and understand until I have enough knowledge to consider looking at deals. I research about the business model in a specific sector, how the industry works, the differences in them. There is a lot to learn. We're open to them, but the probability of receiving funding is a lot higher in one of our current areas of expertise. It has to be an area I understand. If someone handed me a business plan on Uber, a transportation system without owning a single vehicle fleet - I would have to investigate how a model like that could work without owning any assets. One needs to understand the difference between clean tech vs. not clean tech in the oil and gas industry, as another example, and basic knowledge about these industries is always helpful.

Participant 3

1. With how many other investors do you prefer to invest in a venture?

Investments range from three-ten institutional investors, like insurance companies, and three-five on average.

2. How many investment opportunities do you review in a year?

Personally over 300. As a company, we review hundreds, per person each year. As a company total, over 1000.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

This question depends on the type of investment. For equity –based funding, I keep a portfolio of 15-30 investments, and each investment lasts three-six years. An early stage investment would last six years. I have no minimum number to invest, but a year may go by and I didn't invest in anything because I didn't find anything interesting, or other competitors beat out our firm.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

Start-ups are more Angel/seed investing, and my company currently invests in late stage growth, so generally these investors have already been through several rounds of funding.

The answer is yes, I would definitely invest in a company of one if they had a track record of success and have done it several times before and I have a relationship with them. I have invested in a single member company before - there is a man who has proven success and I will invest in anything he presents. That said, I would not invest in a one-man-band I was not familiar with who came up with to me with an idea.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

N/A – relevant to start-ups, small investments.

6. What is the average amount that you invest in a project?

Varies.

8. How long have you been in the venture capital business?

About 17 years.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

Yes, I usually start with the pitch/presentation, no business plan-it's pretty much the same thing. In my industry, I have to be opportunistic. I receive leads through relationships and proprietary deal flow.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

Failure creates a higher bar. It depends on their story - was the failure out of their control? How did they react to it? Failure by itself is not categorical, but it is a grand indicator of replication. If the entrepreneur for example showed poor character, or had a lack of collaboration in the process, well, life is too short to spend time on those ventures.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

N/A - small stage.

12. What questions should founders be asking you when you are making a decision whether to invest?

Often there are companies which are given several investment proposals. When founders are deciding between investors they need to ask, 'Who can help me the most? Are they experts in my industry? What is the reputation of the firm? What references do THEY have?' Entrepreneurs should also look at this in the same way you look at a marriage. At first everything is perfect, right? But it's hard and it takes work. The business relationship can also be incredibly stressful and difficult at times, and people will want to bail out, then it becomes a matter of whether you trust and depend on the people you're working with. Sometimes the entrepreneur will take whichever firm provides more capital, and this is the wrong way to look at it. If the venture is successful, the difference in funding turns out to be a rounding error, and the principal value is not going to matter. Entrepreneurs need to ask, 'Who is going to be the better partner?'

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

For equity investments, we become shareholders in the firm. For some investments, we become board members, help recruit executives, manage and oversee different aspects of the company. We are not interested in operating the day-to-day functions of the company.

14. What other business experience do you have?

Founder, investment banking, business development, finance, strategy, analyst.

15. What industries do you specialize in? Are these the only industries you fund?

I mostly invest in the tech industry. Other sectors include: Internet, software, eCommerce, business services, communication & infrastructure, financial technology and healthcare

Participant 4

2. How many investment opportunities do you review in a year?

6,000 entrepreneurs have gone through our programs. Many started and blew up, and blew up the second time. Some blew up first, then achieved wild success on the second try.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

In this way, I am different than the average investor – [omitted] was named top 3 social impact incubators in the United States by UBI Global. Part of my mission is to help as many tech companies get to scale as possible. I want to add to society through accelerating products that change the world for the better. I am not concerned with adding x# of deals in x amount of time; I want to optimize for the long-term benefit of society. I want to realize how can I build a 100 thousand plus network of entrepreneurs. I am looking at it more from an impact standpoint.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

For founder teams, the most successful are two-founder teams. One can cover voice of customer, the other side is manufacturing. In a two-person situation, they seem to more naturally able to handle those roles. With groups of three or more there are typically communication problems. One-person start-ups there is usually too much blindness, or not enough perspective, or the founder is limited because they can't be available or present 100% of time.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

Easily 100. Lots of examples where the entrepreneur had 50-60 meetings.

6. What is the average amount that you invest in a project?

Investment is access to network more than capital

8. How long have you been in the venture capital business?

I have had this career 13 years. I began working in Chile in 2003

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

Traction - nothing else counts. I want to hear this within the first 30 seconds of an entrepreneur's pitch. The German-style is to tell you about their education, their background, and why they're so important. The method for those in Latin America is to do everything they can to build a relationship with you. Chileans want to first establish how you know each other. Koreans lead their pitches with technical and product information. The American way, I like to say, is to talk about traction. I want to hear that you already started x and you already have something moving before you say anything else - even before I know how it works. Traction means the business is making money.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

Nothing teaches a stronger lesson than scar tissue. Not the best way to learn, but happens to be the one I've done the most. An entrepreneur is a lifelong learner. In my experience, the successful ones are the ones that have that long-term outlook. Some get lucky, but then some use failure as a springboard for future success.

Of course, there are also those that repeat their mistakes and their start-ups are destroyed again and again. Entrepreneurial failures are not necessarily out of their control. Being an entrepreneur forces self - reflection much more than in a traditional corporate business-setting. Great visionaries like Rich Branson and Steve Jobs were reflective entrepreneurs. The founder of Enron would be the contrary.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

There are so many people that say they need it, and most will not receive it. I tell entrepreneurs initially to see how to build a business without getting funding. This is a healthier approach, but it's not always possible. There are certain businesses that shouldn't be funded, but people get stuck on the notion. One example was a simple business that was self-sustaining and the entrepreneur was so obsessed with the idea of getting funding that he eventually got exasperated and threw in the towel. Some entrepreneurs don't understand it can take as long to get funding as to build the business. They should go ahead and build their base product or get their business off the ground.

12. What questions should founders be asking you when you are making a decision whether to invest?

Do I really want money from this guy? Do I really need money? How long do I think this investor will keep me? Are they committed to me or to the business? Entrepreneurs need to understand that when you take money you become an employee, and it is no longer driven by you.

The other side of this is knowing when to take funding. There were two separate times when I

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

My network is my most valuable asset. That, and my pattern recognition to problem sets. I am also able to give creative solutions to problems. These three things are more valuable than any funds I can offer.

14. What other business experience do you have?

I built seven of my own startups that got to interesting levels.

15. What industries do you specialize in? Are these the only industries you fund?

Impact innovation, HC analytics, education technology, smarter commerce (includes cognitive computing), water, mental health.

Participant 5

1. With how many other investors do you prefer to invest in a venture?

We do investments by ourselves a lot and we are totally comfortable. Groups of wealthy people tend to pull funds together, and sometimes we will join in if a company already has a term sheet, but there is no true preference. If you have a lot of firms together on a deal managing them can be difficult, so no, we don't prefer the more partner approach.

2. How many investment opportunities do you review in a year?

We have about 500 opportunities a year come through the door, and out of 500 we end up making two - four investments. A lot of businesses are way out of our focus - one time we got a plan from China for an off-shore fish farm. A lot of what we receive are quick, easy passes and we are not going to spend time on those. For the ones we do, we end up setting meetings with (a rough estimate) 150-200, maybe upwards of 200 companies. We will spend an hour with these and hear their pitches, and of those, we will really look into around 150 companies a year and have multiple meetings with them.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

So, we typically invest in two-four new start-ups a year, and internal financing is something we do every month. I sit on five boards and observe on another. Ongoing we have about 16-17 companies and three people to be on boards.

Is there a maximum number or suggested number you operate under?

No, it depends on the person and the deal. Our founder sits on ten boards currently - and he says that's too many.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

To answer this question, you need to define startup. Our seed investments start at 250 thousand, 500 thousand and about one million. We mostly invest in series A and B and some C. However, you have to understand that an Austin Series A and a Silicon Valley series A are different. A series C in Austin is around three million, and that would be a series A in Silicon Valley. A Silicon Valley series A is more like eight-ten million. If you are talking about seed investments that have no present customers, we currently do not invest in those. We typically do not get individuals - we want the business to be at least at a stage that we can see the product and the business has tens of thousands of recurring revenue. A class C investment would already have 12-13 million a year and would not be as risky, whereas a company turning three-four million is not proven yet, and not as viable. You increase the risk/reward as you go up, so a company making less revenue would have more risk, and you should earn a higher return on a company you funded from a napkin.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

This can vary widely; I'd say the fastest I've seen is three in-person meetings before making a decision to invest. Usually I will meet people for coffee, or they will come into the office and give a presentation, and if so sometimes I will have a junior associate sit in. We will spend one to two hours listening and asking questions.

In the best case, follow-up with a "3Q Diligence Day." We call it a 3Q Diligence Day because it takes three-quarters of a day going over every aspect of the business, including history, tech development, roadmap, financials, everything - and decide after that whether or not we will offer them a term sheet.

For other investment opportunities, there will be a lot more meetings. We will find their customers and ask questions about their product, check the competition, and have ten meetings or so. After this, if we still have questions, we may have to dig in deeper into the total market and other factors. I have followed one company for over five years, and have watched them switch their business model, and met with them six-eight times without having funded them.

6. What is the average amount that you invest in a project?

We typically invest five million. The minimum for our firm is three – five million.

7. What is your target return rate? What is your average return rate?

It is all about risk and reward. In real estate, for example, they might target in the mid to late teens. In private equity, in late stage buyouts would expect 20-30% returns, and asset-class slightly higher than that. Our targets are in the 30-40% ranges. Venture capitalists are in the highest asset class. If investors are only getting a 25% return, they could go to private equity, which is less risky.

8. How long have you been in the venture capital business?

I have been directly working with VC for seven years, and before that, buyouts for three and a half years.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

I'll start with the pitch. I asses the team, their experience, and the market's opportunity - does the product work? Will people buy it? How many people would buy it? How much would they pay?

I want the entrepreneur to ultimately answer the questions, why should we buy this product? Why buy it from them? Why buy it now?

When providing venture funding, almost all the money goes to hiring people - I need a CEO who can tell a story and recruit people. If the answer is 'no,' I would not invest. If you don't have a CEO who is convincing, you do not have a company. It is a good sign when the company already has seasoned professionals early on who have agreed to join, (sometimes for less pay) the new company.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

The origin of this question to find out whether an investor is adverse to an entrepreneur that had failed or even may prefer one because that entrepreneur had learned the lessons.

Having and entrepreneur with a positive track record of building and selling companies is great. Those who have failed can also be very interesting. Having an entrepreneur with past failures doesn't scare me in the least - but I want to know what happened, and I would want to do due diligence. This kind of entrepreneur has probably learned more lessons than the one who has always had success. I would rather fund an entrepreneur that has had a failure than someone who is starting a company for the first time.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

Sometimes companies ask for capital too early on, and I'll tell them, do these three things and come back in six months. This doesn't mean they don't need funding. Sometimes an entrepreneur will have unrealistic valuation expectations - they want to raise capital at a certain multiple of a valuation and I tell them, 'go do it - I wish you luck.' I have had a person wanting five million in funding, and come back with a one million contribution, probably from someone that doesn't understand business valuation. The entrepreneur asked us for the rest, and we still didn't fund him.

Often before funding, I need to see more milestones, or more sales processes, or often if it's a medical business we need more data.

12. What questions should founders be asking you when you are making a decision whether to invest?

They should do reference checks on VCs. Some venture firms are low touch and some are high touch - we are high.

Has the firm invested in the city where you're located? At a minimum, that VC is committing to travelling to that location at least four-times per year for at least the next 5 years. If they are not already committed to that area they may not be all in or may not have investigated the market. Our position is to invest in Texas and invest locally. It is also very important when recruiting talent, and being local is the key to doing that.

They should also ask how much dry powder is left in the VC fund. For example, the firm may invest five million and have another four million or five million on reserve.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

Post investment, we are talking with the founder every week, and hiring. We also help with bizdev and analytics. There was a credit card company we invested in who was getting a lot of chargebacks, and thought it may be due to the timing of the machine - we ended up doing several weeks' worth of research, collecting data and analyzing it, and ultimately found out the root cause - though it wasn't what the founder suspected. In VC, most of the funds go toward recruiting talent, and sometimes you have to hire people fast. There is no better value I can add than through my network. I spend a significant amount of my time meeting with people who are looking for jobs and I recruit salespeople, executives and interns, usually people director-level and above.

14. What other business experience do you have?

My background is in finance, banking and buyouts. One of my partners has a strong technical engineering background, so we complement each other well. I like to say I have enough tech knowledge to be dangerous, but it helps to have an expert in the industry you are looking at funding.

15. What industries do you specialize in? Are these the only industries you fund?

I specialize in medical and software. Sometimes I fund medical pre-revenue with early-human trials. There was a startup which had a new way to remove tattoos. With software, it is primarily B2B, such as solutions financial institutions. I have also invested in direct to customer solutions, scientific devices and food services.

Participant 6

1. With how many other investors do you prefer to invest in a venture?

This answer is more complicated now than five years ago, since there are more funding options now than five years ago. For example, there were not as many crowdfunding sources or funding mechanisms. If you team up, you may have a lot of investors - you could have two big angels or 30. It depends on the company. Generally, fewer is better. It makes the capitalization table less complicated, and there are not as many disparate opinions. Sometimes, if there are a lot of investors, you may organize to have them vote as one group, 50 angels counting as one vote and that’s it. There are other ways to simplify - sometimes they don’t like it, but if they are interested in the company and like the terms, they may accept this.

2. How many investment opportunities do you review in a year?

My firm reviews about 1,500 in a year. 1% of these are typically highly competitive for funding.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

My answer would probably be - the more the better. In order to do a good job managing, though, you would probably need four-eight per partner. Actually, eight would be - ridiculous - six is better. Four-six.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

The number of people employed depends on the stage. Earlier on they need fewer employees, later they will need more. After signing for funding, they need to staff up like yesterday. It's not a one-shoe-fits-all approach.

For teams, three-five founding members is a great team. Minimum three. If there are less than 3, there is not enough group dynamic the efficacy of the team. It is harder to tell whether the team agrees or disagrees. For example, if a team member is answering a question and someone disagrees and interrupts the person answering, it can be refreshing. It shows that they are a collaborative team and are able to come to conclusions together. You can also see when the interruption is disruptive, and one team member's viewpoint is radically contrary to another. There is a difference between collaborative and combative. With one person, well, you can't really see them argue with themselves.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

By the third meeting, you should have a good understanding whether or not you want to fund the company. After that, you are looking at additional information and the terms of negotiation. If you are the lead investor, you're creating the term sheet. Afterwards, you can ask for a due diligence checklist. It is basic but fundamental - checking financials, IP, whether or not they have a bank account, if they keep their receipts in a shoe box. We actually had a company who kept all their receipts in a shoe box! At that point, you let them know they have to hand it over to an accountant to create financial statements. So between handing out the term sheet and actually signing it you engage in due diligence.

6. What is the average amount that you invest in a project?

Generally, I invest $250 thousand to 500 thousand per round, and expect to engage in 3 rounds per company. You need to have a follow-on investment or you can get washed out. For example, if you fund a 900 thousand company with 100 thousand, the valuation is at one million and you own 10%. Then the company is successful in raising five million. Now, you are responsible for 500 thousand, or you lose your initial investment of 100 thousand. This is the dilution aspect.

7. What is your target return rate? What is your average return rate?

We don’t share that information. I can tell you that the industry average puts VCs at a 700-800 basis above the S&P 500. So, if the S&P is at 5%, VC will be 12-13%.

8. How long have you been in the venture capital business?

Since 1996. 21 years.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

Are they believable? Does their presentation build trust? I do both, usually. My team reviews the information first, then I listen to the entrepreneur’s presentation and I have the data available to m. After I listen to the pitch, I dig into the team’s data.

10. How could an entrepreneur's previous experience (even if a failure) contribute to your evaluation and decision to invest?

The entrepreneur may have a previous experience with failure and it be real positive or negative. How they frame it is super important. If they say, 'Yeah, well I couldn't get enough VC funding' - that's no Bueno. If the entrepreneur says they failed because they failed to manage a critical factor such as the supply chain - it is ok if they can elaborate on the problem and what they learned. Just having flippant dismissal or blaming the failure on outside factors does not build credibility.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

If their expense structure is very low, or the company can afford to bootstrap, or, they have a high gross margin, or they can be cash flow positive in six-twelve months they may not need funding. It depends on the finance model of the company and whether it has much maturity of business.

If the company has a minimum viable product and minimum viable sales, or minimum viable product and proven sales and is scalable doesn't mean we will invest because it is not necessarily sustainable. It needs to have a proven sales model beyond the company's network to show that it's viable. The company should have a step-by-step process from start to closing. Some businesses develop this proactively - if they do more of this, they get more of that. If a company makes its first sales to friends and family, that doesn't mean it has a proven model. When they continue, and make a cold relationship, with no prior knowledge of the customer that's super valuable. The first sales could be significant, but it’s not as great as one cold close to model the company’s value. There is a difference between generating revenue vs having a process model.

12. What questions should founders be asking you when you are making a decision whether to invest?

The entrepreneur should be doing due diligence before receiving a term sheet. They should check the investor’s reputation in the market. They should look at prior portfolio companies and talk to other partners. I am always happy to share the numbers of other CEOs. Due diligence is not so much asking as doing their homework. The entrepreneur should come already knowing I’m a valued investor and that I specialize in their industry.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

I become a board member, help hire, mentor, fire. I help with the company’s compensation strategy, advise, domain expertise. I help in ways that accelerate their business.

14. What other business experience do you have?

For my capstone paper in college, I wrote a business plan for my family’s business. I built, ran and sold the business, and my parents were able to retire. I was one of the only people in Austin at the time who had done this. I liked the challenge, so I made a career of it.

15. What industries do you specialize in? Are these the only industries you fund?

Social media.

Participant 7

1. With how many other investors do you prefer to invest in a venture?

We are pretty open-minded - it is ok to go in it alone. Sometimes we will invest with an angel, or family member or another firm, but this is not done intentionally. As a rule, the smaller the number, the better. What I have noticed is investors that write the larger checks - say one million and greater - tend to be less loud than angles, for example, who write smaller checks. The smaller the checks, the more pain they are. Investors that write checks over one million tend to be less involved because they already know what they are doing and are not worried about the daily processes of the company. Skill, experience and tenure contribute to the lesser involvement.

2. How many investment opportunities do you review in a year?

700 for the firm. Out of these, three-four become investments, and five-eight more are viable. They may not become investments for different reasons. These may be opportunities which reach agreement but we don't close for one reason or another or they decide they're not going to do it.

3. If it were possible, what would be your optimal number of projects to invest in each year (for equity-based funding)?

Four is about the velocity the firm can handle.

4. How many employees are ideal for a startup company that you fund? Why is this number ideal? Are there numbers you would not invest in? Would you, for example, invest in an individual?

Yes. One founder is ok. More often you will see two or three or four. Maybe two is the most common, I don't know the actual statistic. We don't typically do seed investments. At the firm, we mostly do series A, so the company already has 10-15 employees, maybe 20. For numbers of founding members, think smaller, single digits.

5. How many meeting rounds, on average, does it require for an investor to gain your funding?

First, we see market data, look at the financial plan, then spend half a day in a meeting with the company for high diligence. After that we find experts on their products. This process takes about four-six months. Then when we decide to invest, we will meet another five-eight times to discuss terms. We also can take a long-term approach to looking at businesses. In some cases, we are not unwilling to wait and watch the company for an extended period of time. For example, there was a company we watched for five years before investing in. If we are going to invest right away, we should know this by meeting eight. If it's a long-term approach, we could have 20 meetings before taking any action.

6. What is the average amount that you invest in a project?

This depends on how you break down the amount. Our check size for the first round can range from 2.5-8 million. Over the life of the investment this can be 6 million - 30 million. For a series A investment, the check size is 3-4 million on average. For series B it’s more like 5 million or 6 million. It depends on the stage of the company.

7. What is your target return rate? What is your average return rate?

We don’t normally disclose an average return rate. Our target return rate is 50%. Actual is less than that.

8. How long have you been in the venture capital business?

About 17 years.

9. What is the most important part of an entrepreneur's spoken presentation and why? Do you typically hear many presentations or start with the business plan and then invite the founder to present?

Clarity, self-honesty, market understanding - we really need a crisp view of opportunity size, and the sales model - unit economics. What about the team - do they have who they need? Defensibility of technology, customers. It takes about five minutes to understand whether o not I’m interested in the business, or sometimes it takes a little while.

I try to the pitch first, along with the overview and financial plan. Of course, you can get inundated hearing pitches five times a day. You need content first. The entrepreneur’s goal should be to get investors to a ‘no’ as fast as possible.

10. How could an entrepreneur’s previous experience (even if a failure) contribute to your evaluation and decision to invest?

We’ve all had successes and failures. I want to understand their track record, where they’ve worked and their character. Do they have blind spots? How do they speak about their failures? Do they try to cover it up or do they bring it forward? The level of self-honesty is important to read.

11. Are there business plans that you have concluded do not need funding? If so, what stages are they in and why did you determine they do not need funding?

We often see businesses that should not receive funding such as lifestyle businesses, businesses that won’t make more than three -five million, businesses that are profitable on their own. People get caught up in the ‘glamour’ of VC funding, but businesses don’t need it if it will not produce a high rate of return. Doctors, lawyers, dentists-lifestyle businesses like that which have a linear business model. If one of these wants to make more money, they work another day, or put in more effort. Businesses like that should not take money from us.

12. What questions should founders be asking you when you are making a decision whether to invest?

Would I like to work with you? Can I talk to someone that works with you? What is my role in the future - product, lead, sales? Ask the hardest questions today, because in the future when things get hard you need to be able to calm down when under pressure.

13. How do you assist companies in which you invest other than providing capital? What level of involvement should a founder expect from you upon being chosen by your firm?

Different funds have differing levels of participation. Some are low touch and will come in for quarterly feedback and then leave. We are a high-touch firm, we communicate with the portfolio companies at least monthly, if they grow past a certain size it can move to quarterly, but I've noticed that the most experienced CEO's call me the most, and the least experienced call me the least - it's almost like they feel they have to prove they can do it all themselves. The experienced ones know relationship matters when hard times hit. So, there are many CEO's that talk and email on a regular basis.

So, a sales leader may have lead the company to produce ten million in revenue, but doesn't necessarily have the level of discipline to bring the company to 50M or 100M and he's never done it before, we may need to find him a new role in the next twelve months. The person may need headlights to be able to identify problems. We need different people at different phases.

When you've built 35 or more companies you start to see patterns and can spot a disaster happening, and develop pattern recognition.

14. What other business experience do you have?

Product development was a big one. I also built my own startup - so I have empathy for the entrepreneur, and can relate to the joys and the challenges. I lead people in the company for over 4 years, and experienced things not unlike what they're going to see - a lot of similarities that are very relevant.

15. What industries do you specialize in? Are these the only industries you fund?

Software, SaaS, scientific instruments, med-tech devices.

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