

Financing Start-Ups
and
Venture Capital
**Brown Forum for
Enterprise**
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Once Upon a Start-up . .
.. the beginning

- First Company Organized in 1999
- Formed with practicing cardiologists
- Devices for interventional cardiology
- Surgical wound closure
- Minimally invasive instruments

Identify the Need

- Had several ideas
- MDs: What do you think?
- Got lots of opinions and new ideas
- Most clever, none commercial
- Informal Survey: What is the biggest problem you face?

Getting Started

- Bootstrapped first 18 months
- All early participants made "Founders" – 10 total
- Outside expenses – legal, animal testing, prototypes – paid "out-of-pocket"
- Start! Tell the world what you are doing.

In Search of a Strategy

- W.C. Field's Approach
 - License w/ Development Agmt
 - 3 'verbals', but all were acquired b4 deal
- JV w/ mid-size Co.
 - Difficult to keep control
- Stay independent; raise money
 - Traditional venture capital
 - Angel investors

Financing

Venture Capital Market

- Hi-water mark in Q3 '99 – Q2 '01
- Investment in funds increases 4-5X
- >20 \$1B funds raised
- Annual investment by funds skyrockets

Implications of 'Irrational Exuberance'

- Huge funds require HUGE INVESTMENTS
- Huge Investments require:
 - Late stage companies, or
 - Money pits
 - Internet
 - Biotech
 - Telecom

Seed and Early Stage Gap

- Irony: Record Setting Funds but less money for start-ups
- Venture Funds
- Truly Wealthy Individuals
- Organized Angels
- Accredited Investors: Cherubs?
- . . . And they all have trade-offs

Angels

- High Net Worth
- Often Former Entrepreneurs
- Active and Growing Market
- Often Organized or Affiliated
- Small Average Invest: \$200K - \$500K from 4 – 20 people
- Act Like VCs, but with 10s of decision makers; invest like Cherubs

The Cherub World

- Net worth \$1-5M - untapped
- Looking for opportunities
- Tech Bubble improved Angel and Cherub Market
 - EMC, CMGI, Cisco, Amazon etc. were perceived as 'safe'
- Pure Retail Selling

Can Become Hell . . .

- "Accredited" does not mean sophisticated!
- Represent them and Company at the same time
- For most, no "dry powder"
- Interested in "fair" not legal
- No one understands dilution!

Venture Funds

- News Flash: They're in it for the \$\$\$!
- Motives Differ
- Small, Medium or Large Fund?
- Early, Middle or Late in Fund Life?
- Raising New Fund?
- How is the Portfolio performing?
- Motives affect investment decision and post-investment behavior

. . . And the Excuses

- All positives are negative!
 - Low penetration: mkt not interested
 - Simple concept: too simple, someone else would have already invented it
 - 2nd product: need first mover advantage
 - 1st product: high adoption risk
- It's a product not a company
 - Tell Henry Ford

Go on and on . . .

- Focusing on portfolio
 - We're losing our backsides
- Like to 'buy it right'
 - Only invest in desperate co's at rock-bottom valuations
- No Domain Experience
 - Come back next time
- Need a Lead Investor
 - We're venture followers not venture capitalists

In a new and different language

- Space, Domain, Bandwidth, Granularity, Disruptive tech, Inflection point . . .
- Angel money is dumb money
- Dumb money = dumb technology
- Too early; too late
- Valuation = \$10M or \$25M
 - **And you're not 25!**

The Rest of the Story

- First Company Raised \$21M equity from 200 investors: VCs, Angels and Cherubs and \$3.5M venture debt
- Sold Co. in November '04
- In 4 Start-Ups, raised over \$80MM equity and \$10M venture debt

Lessons Learned

- Promote Biz Constantly
- Keep raising money (ABC)
- Stay lean, but build Core Team
- Multiply all estimates by 2x – 4X
- Always have a backup plan or 2!
- Network with everyone
- Perseverance wins
- It's good to have a VC
