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Questions on an entrepreneur's mind- pre and post VC fund raising

Brave Entrepreneur

Business plans are several, ideas are even more but people with a gut of steel and an ability to face failure with a sense of humor are far limited!

The internet offers freely available guidelines on how to write a good investor pitch presentation (ex. http://www.idgvcindia.com/investment_process.htm).

Here, I am sharing my thoughts on some questions running on an entrepreneur's mind in the phases immediately *prior* to and *post* having raised Venture Capital (VC) money.

By no means can this be complete- as every entrepreneur has a uniquely interesting story of his own. And also there was a 1400 word constraint!

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Pre-VC

Q. Should I raise VC money?

VC money is not good for everyone- but only for certain types of businesses and entrepreneurs.

Several good businesses deliver enough cash flow to allow the founders, employees and their families a very comfortable lifestyle.

Whereas, a VC targets very aggressive returns driven by accelerated company growth. Thus, VC money is useful only if there genuinely is an opportunity to accelerate the pace of scale up with the money and substantially increase the size of the pie.

Else, raising expensive VC money could create a significant dent (due to lost shareholding) in the stable cash flows and result in an un-happy situation for all shareholders.

A VC enters with the hope of a good exit. Founders need to be willing to either go for an IPO or even sell 100% of their company to enable such exit.

Look at a VC for growth capital, resultant larger share holder wealth creation and value add that assists in achieving such company goals.

A VC may contribute in many of the ways below-

- Sounding board as a trusted advisor; priceless to a lonely entrepreneur
- External market and strategy perspective
- Recruiting senior management and advisory board members
- Opening doors with potential customers and partners
- Positive force in creating performance oriented/disciplined culture
- Extensive learnings from multiple portfolio companies
- Help with future fundraisings and liquidity events (IPO, M&A)
- Rub-off branding from a reputed VC fund; lends credibility to a young company

Clearly, the money and the above will come at a cost.

A cost of-

- Ownership Percentage
  - For the lure of creating a much larger pie in the future you will give up substantial shareholding today
- Diluted Management Control
  - Are you willing to be 'bothered' regarding key/directional decision making?
  - Do you truly want to professionalize into a Board run company?

If 'good enough' is just not enough then do consider making the sacrifices required in raising and managing a VC investment in your company.

VC money is certainly not a necessity in going beyond 'good enough' and neither is it a sufficient condition.

But, it could very well enhance your chances of significant success.

1. Consider raising angel money ('friendly sub $1M' money) and use the same to demonstrate initial market traction before talking to VCs.
2. Engage an investment banker instead of 'learning as you go'- a fund raising event will have huge impact on your company and future so don't treat it like closing one of many customer deals.

Q. How much VC money should I raise?

VCs in India tend to invest anything from $1M to $10M as an initial commitment into a company.

How much money you raise is a trade off between giving up shareholding percentage and having enough money in the coffers for growth through good and bad times.

Entrepreneurs can be over optimistic. Consequently, actual performance often lags expected performance.

Raise enough money to last you for about 24 months- repeatedly going in for fund raising is an energy consuming exercise and also a distraction for passionate entrepreneurs.

But, if the economic environment is expected to go bad then try and raise enough to see you through the time when VCs have gone holidaying on a one-way ticket

God favors you immensely if you don't encounter at least one or two or three of the below plan-spoilers:-

1. Revenue achievement lower than what you thought
2. First strategy unsuccessful
3. Longer than expected time at cracking the right product/service
4. First hired sales head not performing
5. Compensation expectations underestimated
6. Customer decision making cycles twice of what you estimated
7. Competition out of nowhere (most competition seems to be headquartered in a place called 'Nowhere'!)
8. Second strategy unsuccessful
9. Etc….

Resultantly, cash burn will be higher and cash break even further away than imagined.

So…raise enough money and don't be too stingy on shareholding and fearful of dilution.

At the other end founding teams have erred greatly by raising enough to start their own lending practice! Don't raise how much ever is available; instead raise how much your plan (+ a solid buffer) indicate. Going far beyond that will cost you precious shareholding and can be counter-productive.

1. Be smart about deploying capital in high ROI areas and not in near-dead investments like better offices
2. Independent of how much you raise keep budgets tight

Q. Any VC will do?

VCs are several and amongst them the colour of money can differ significantly.

So, you are expected to ask questions and exercise your reciprocal right to diligence the individual and his fund for things like-

1. Sector and stage fitment
2. Investment record/credibility
3. Board behavior and value add; speak with couple of their portfolio CEOs
5. Knowledge and connections
6. Long-term versus short-term orientation in supporting portfolio companies

Needless, to mention your ability to diligence an investor putting money on the table is directly proportional to the attractiveness of the investment opportunity that you present…and the number of VCs that are pursuing you.

Both, valuation and value add matter in significant measures and it is tough to trade off one against the other beyond a point.

Post-VC

Q. Will life be as usual after raising VC money?

Let me answer that with another question- Has life ever remained the same after getting married?

Certainly not!

More so if your spouse is the one with the boat load of money and affirmative rights to key decisions of the household!

A lot of changes happen; especially when the investor is an active one. Most part of it for the better management and return generation potential of the company.

VC funded early stage companies are likely to have following dynamics-

1. Board run professionally managed company; CEO reports to the Board
2. Aggressive scaling targets
3. Performance orientation and objectivity at all levels (including CEO/founders)
4. More considered decision making on strategic issues
5. Periodical transparent reporting
6. Faster pace of growth/initiative parallelization at the cost of burning capital in the early days
7. Big ticket moves not typically associated with early stage companies
8. Build out of senior management team beyond founding team
9. Independent director induction
10. Enhanced intellectual depth at the Board level
11. Thinking and planning for exit in the long run
12. Tough calls requiring emotional maturity and sacrifice
13. More public/industry scrutiny
14. Corporate governance procedures
15. Running smarter, faster and harder…

Q. Now that I have both- the money and the VC; what future pitfalls should I look out for?

Try and avoid typical pitfalls (some listed below) and work pro-actively with your VC/Board with the hope of taking right decisions majority of the time. You will know whether a decision was truly good or bad only if execution has been good in either case!

1. Lack of speed; consequent DNA impact and pace fatigue
2. Substandard execution and strategy overkill
3. Micro-managing; need to step back once in a while to notice the global big picture
4. Poor senior management hiring decisions
5. Not 'letting go'; let the company build beyond the founders
6. Losing perspective of productive versus non-productive deployment of funds
7. Leaving behind the cash consciousness from pre-VC days
8. Me-too products; kidding yourself about global differentiation
9. Technology over sales
10. Fluffy adjective laced foggy reporting; stick to insights and information
11. Poor investor relations management- performance drop, culture conflict, lack of transparency…no-confidence motion from Board
12. Future fund raises- raising too little or too much, unreal valuation expectations
13. Capital structure lock-jam
14. Not sharing wealth created with employees
15. Etc…