BUSINESS ANGELS AND VENTURE CAPITAL FUNDS: HOW TO SEDUCE THE INVESTOR?

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On March 10, 2010 I attended a conference well interesting titled "Business Angels and venture capital funds: how to seduce the investor?". This presentation was held within the framework of an event "Salón Mi Empresa S.A.", in the Palacio de Congresos de Madrid, on March 9 and 10, 2010, "the first large-scale annual event designed to allow entrepreneurs, businessmen and freelancers to find solutions to all their concerns regarding start-up, financing, development and management, and where appropriate, transfer or acquisition of SMEs." It was aimed at entrepreneurs, freelancers, students / alumni of business schools, top executives of SMEs and micro-companies, managers of large companies wanting to start working on their own own or who want to take advantage of the content of the Show to expand their knowledge, businessmen who want to sell their company or transfer business, etc. The organizers forgot to put investors, venture capital funds, business angels, in short, alternative sources of financing on the list of potential stakeholders in this event.

The conference speakers were:

Alejandro Santana García-Fuster, CEO of Perennius. The other speaker was Alberto Gómez , Managing Partner of Adara. Lastly, Jorge Aranzabe, General Deputy Director of Gestión de Capital Riesgo del País Vasco, in which 70% by the Basque Country Development Agency, the SPRI< /a>, 10% for the BBK, 10% for Kutxa, 7% for Mondragón Inversionesand 3% of Viana SPE. The panel was moderated by Eduard Saura, Managing Partner of Accuracy, a company that provides venture capital as well as large and medium-sized companies proven experience in areas in which specific knowledge in the financial area is required.

As an introduction to the conference, representatives from each fund introduced themselves. Adara is a Venture Capital fund and therefore does not enter the preliminary phase, that of seed. Invest in companies that already have a developed product and existing revenue. They launched their first fund in 2005, currently manage €55 million, have made 13 investments and have 9 companies still in their portfolio. They invest in software services & platforms, online and mobile services, components and semiconductors, telecommunications equipment and clean technologies or its equivalent in English "Clean Tech". 60% of their investment goes to companies based in Spain, the rest, 40%, based in Europe.

Perennius invests in the Seed Capital and Start-up phase, that is, in the phases prior to the one that reverses Adara. They have made 7 investments so far. They have a rather general approach when it comes to the sectors in which they invest. They did not have to raise funds as the funds for Perennius come from two wealthy families. One of them belongs to Alejandro Santana. It is a Family Office that manages different financial products, including the venture capital fund. Perennius considers itself a "structured" or professionalized Business Angel. They undertake investments between €150,000 and €400,000.

The management company Gestión de Capital Riesgo del País Vasco was founded in 1985 and its funds are, above all, of public origin (70% of SPRI). They have €100 million of capital under management. They invest in the Seed phase, Start-up and also later phases, of growth of a company. The preferred sectors at the moment are Biotechnology, Nanotechnology and emerging sectors, although in this area he did not specify which ones.

They then described the phases of evolution of a company in its beginnings, that is, the 1st phase is called Idea, the 2nd phase is Prototype, the 3rd phase is commercial development and in the 4th phase, profitability is achieved. .

Between each phase, there is a value jump. Between each phase, the investment obtained must cover at least getting to the next phase. Venture capital, or Venture Capital as we know it, invests rather from phases 3 and 4. The investor type and phase depends on their investment capacity and risk aversion or not.

Phase 1 normally implies, and if they are not investments in Biotechnology that are usually quite high, around several million Euros, they are usually investments in the order of €50,000 - €200,000. They are usually attacked by the 4Fs (Founder, Friends, Family and Fools), Business Angels and some Family Office. Venture Capital, at least in Spain, does not usually invest in this phase. It tends to be more common in Anglo-Saxon countries, less risk-adverse, such as the US or the UK.

In phase 2 the objectives are clearer, the Business Plan is more advanced, the investment is usually more professionalized. In this phase the figure of the Business Angel usually enters, in co-investment many times because a greater investment is involved than in the first phase, with Family Offices such as Perennius.

During phases 3 and 4, the relationship is less personal with the management team, the investor, that is, Venture Capital, tends to focus more on results.

The speakers talked about the degree of involvement of each type of investor. They said that it varied a lot even at the level of Business Angel, Family Office or venture capital entities. Variables such as financial variables tend to predominate in investment criteria and, above all, between venture capital entities. In the case of the Business Angel there are usually also personal motivations. Depending on the origin of the funds, the criteria also tend to vary. If they are third-party funds, as in the case of the manager, the manager is tied to financial investment criteria and has less flexibility. In the case of being a personal investor (Business Angel, for example) it is usually more flexible, decisions can be more personal and subjective.

When a company has venture capital in its shareholders, facing the market, it gives it more credibility, solidity and increases the attractiveness also facing a future sale. Venture capital implies having a professional investor who provides highly defined and professional management criteria.

The round table attendees then answered questions from the audience:

1. Entrepreneur's decision-making capacity, once venture capital enters a company, how does it affect it? It affects quite a lot. The entrepreneur who obtains capital has partners who are quite involved in the business project. Venture capital has a lot to say since it is normally on the Board of Directors. It is involved in the Business Plan, budget, relationship with suppliers, etc. There are many decisions that depend on the approval of the Board of Directors.

2. How to seduce Venture Capital? The team is essential when it comes to seducing Venture Capital entities!!! The speakers put a lot of emphasis on this. They prefer an A team, with a B product, than the other way around.Perennius values the team, not only technical, but also commercial and management , and the project to execute. The product must be revolutionary and innovative. But here you also have to take many factors into account, for example, the consumer's aversion to change. Venture capital seeks an excellent product, but supported by a complete team (technical, commercial and management).

3. What risks do they usually assess? Technological, technical, commercial, business model and management risk. They tend to look a lot at the track-record, the history of each person who is involved in the business project. If they have had previous experience, either in functional or sectoral areas, it is a plus and mitigates the risk for the investor. Venture capital seeks scalable businesses, with exponential growth, in order to compensate for the projects in its portfolio that do not go ahead.

4. Experience of Biotechnology in the Basque Country. The representative of the management company Gestión de Capital Venture del País Vasco spoke on this issue. and from your experience. Biotechnology projects arose in the university environment, spin-offs were carried out and all with public aid. Companies led by researchers and technicians resulted. This model at one point was sold out. In the next phase, managers were incorporated who not only came from the pharmaceutical field, but also had management experience. Bringing drugs to the market is complicated due to the little liquidity that exists at the moment, which requires a lot of money and there are not many examples of success either. However, offering services, diagnostics, etc. has a higher chance of success. What is taking place at the moment is a market cleansing of all the Biotechnological ones that exist. Only companies that have a very good management team with a salable product will survive.

5. Current funding situation. The public has remained stable during the years of "financial crisis", from 2008 - 2010. The private has fallen more than 50%. Venture capital has problems raising funds. Investors have lost a lot of money in the crisis and risk appetite has diminished. Investors seek profitability in less time. The problem with "early stage" or very initial investment is that it takes a long time to achieve profitability, between 6 and 10 years, in the worst case. In short, investor appetite is fatigued by the long term.

6. Venture capital trend. More staggered investments are undertaken with a vision of achieving "early wins" or early benefits, until the next round of financing.

7. What returns does venture capital seek. Between 2 or 3 times the invested capital. On other occasions they have obtained up to 20 times the capital invested. They spoke of a 25% annual IRR. For a 10% annual IRR, the investor does not get into venture capital. Invest in an investment fund that invests in the stock market or in state bonds. Adara has achieved IRRs between 30-35%. They are high, but we must also take into account the companies that get lost along the way, that is, that do not prosper. The exit period in the ideal world is usually between 3 and 5/6 years. However, we are now talking about periods of permanence between 5 and 8 years.

The investing capital usually enters in the minority, generally with a participation of 20-30%. Valuations are usually made by DCFs (discounted cash flows) or by multiples of transactions or trading, that is, of listed companies. In a scenario prior to the crisis, we were talking about 7-8 times the EBITDA multiple, now we are talking about half.

8. Interesting sectors to invest at the moment for venture capital. Clean energy technology (Green Tech or Clean Tech) currently has a lot of pull among investors. Health, that is, technologies applied to health. Internet security. The effect of social networks is creating a lot of fear in the face of the loss of digital identity. All the issues related to security on the Internet in this aspect are liked by the investor.

Adara also said there is a lot of appetite for e-commerce. It does not require a lot of money as an initial investment but you must have the "first mover advantage". Gestión de Capital Riesgo del País Vasco said they had a bad experience in ICTs because there are a lot of global players who already make many innovative products/services in this area. However, they are very positive about Biotechnology. Perennius commented that the higher the risk, the more likely you are to get higher returns. For this reason, they prefer investment in companies with a technological component.

They were all very insistent on making it clear to the public in the auditorium that out of 10 investments, 4 disappear, 3-4 more or less go ahead and only 2 are the ones that really turn out well.

And that there are two types of business: the cash-generating company is rather owned by an industrial or private investor. The long term is decisive. A business where profitability is pursued in the medium and short term needs to grow exponentially, be scalable. They can only be technology companies. Venture capital tends to invest more in this type of business.

The speakers also gave some advice to the audience, to the entrepreneurs:

1. To the entrepreneur who is offered financing in these times, take it and not waste time in valuations, in negotiations, in discussing minorities or majorities.
2. It is ideal to have a business plan that does not require external financing, from venture

capital. That the capital a priori comes from the 4Fs. Once it is self-financing and grows, it can look for external financing.
3. Finding funding is a full-time job that takes a lot of the entrepreneur's time and energy. To the extent possible, they advised hiring someone to do the job.

After the conference, I had a brief meeting with Alejandro Santana García-Fuster, CEO of Perennius, with offices in Madrid. The main shareholders of Perennius are two families who pooled their assets and founded a family office. They co-invest a lot with another fund Inveready, with offices in Barcelona. In fact, all the investments they have made, except the first one, which was a flop, have been co-invested. He also told me that the "track-record" is very important, the history of the fund's management team, especially at the beginning, when raising the first fund. They must have experience in entrepreneurship, or another type of experience in this area, in order to attract investors, to make the objectives of the fund credible. Then once you have that track-record, you can calmly go for the 2nd bottom. Co-investment is common, above all, because you share risks. Taking into account the business model of a manager, which is to charge an annual management fee of 3%, if you raise €2 million, you would charge €60,000 per year. With this income you barely cover the structure costs, that is, salaries, maintenance costs, etc. Once you've had a divestment with capital gains, you can start talking about a sustainable business model on its own. He also told me that in a first fund, the partners or the people behind the project should put a third of the investment capital. If it is not difficult to raise funds, make the project credible to potential investors. Lastly, he told me that in the Start-up phase, that is, in the phase between the investment of a Business Angel and the entry of a venture capital fund, we already have to have larger investments, from €300,000 and up. .

It is always interesting to get first hand information. In this particular conference there was a lot of interaction between the speakers, the representatives of venture capital, and the public, generally entrepreneurs. I hope you have found it of interest.

There are no comments yet.