



Visionaries

~The YVCS Newsletter~

Upcoming Happenings @ YVCS

Career Link:

YVCS and **Glocap Search** (www.glocap.com) have partnered to offer members and visitors the ability to search for open opportunities within venture capital, investment banking, asset management, equity research and a multitude of other job categories all within the YVCS.org site.

American Venture Magazine.

YVCS and **American Venture Magazine** (www.avce.com) have joined forces to offer **members** a free subscription to their quarterly magazine.

YVCS – Biotech

In the coming months, the Young Venture Capital Society will look to focus more on the life sciences and biotech space. In that effort, we will be interviewing and developing proprietary content to provide interested members and visitor’s insight into what are the basic growth and trends in the industry.

Key Terms In This Issue

Powered by VC Experts

Bridge Loan - A limited amount of equity or short-term debt financing typically raised within 6-18 months of an anticipated public offering or private placement meant to "bridge" a company to the next round of financing.

Pre-Money Valuation - The valuation of a company prior to a round of investment. This amount is determined by using various calculation models, such as discounted P/E ratios multiplied by periodic earnings or a multiple times a future cash flow discounted to a present cash value and a comparative analysis to comparable public and private companies.

BREAKING INTO VC – AN INTERVIEW WITH SEAN CARROLL, SVP, PEQUOT CAPITAL

June 6, 2005

Q: What is your view of the recruiting landscape for venture capital (both from a junior resource perspective and senior officer perspective)?

~ It is important to understand that the industry is going from a position of massive expansion to one of consolidation, and as a result there will be fewer firms after the shakeout. You can witness the shrinkage with examining who has been successful and who has not; who is raising another fund and who is not. The fact that fewer firms are raising less money means there are fewer employment opportunities. Additionally, I believe the opportunities are isolated. No longer are firms or sectors expanding rapidly, so consequently, firms are no longer interested in multiple hires. However, this type of growth can be witnessed in other investment sectors. Previously (late ‘90s – 2000) graduate students were extremely interested in the venture industry, while now MBA students are focusing more on mid-to-late stage buyout shops, and hedge funds.

Q: How important is an MBA in getting into VC?

~ I believe it is not a necessity, but it is a good route for some people to take. If one needs a catalyst to change his or her career. In order to make the jump to a new level, analyst to associate for example, an MBA provides a credible and valuable method to make that leap. Also, it is important to mix with different types of people. For instance, interacting with different venture capitalists, professors, and alumni can help shape your path to landing in VC, post graduation. Additionally, a critical element to success in venture capital is your network and MBA programs offer individuals a means of expanding their rolodex.

Q: How important is an MBA in being successful in VC?

~ My answer is pretty consistent with the answer to the above question. An MBA is not the driver of success. It is more important to have a nose for a good deal and a strong network that gives you access to talent and deals.

Q: For those individuals who are deciding to pursue an advanced degree but can either choose MBA or Engineering (but not both), which one is more beneficial to successful VC careers and why?

~ An attractive profile for Pequot Ventures is someone with an undergraduate degree in Computer Science or EE (Electrical Engineering), who participated in an investment banking analyst program, modeling and learning deal structure, and then went to venture capital to understand the venture process. Having a base of technical knowledge combined with strong quantitative skills is a must for our firm. Understanding how to develop complex financial models is critical for us, as

Private Placement (AKA a Reg. D offering)

- The sale of a security (or in some cases, a bond) directly to a limited number of investors. Avoids the need for S.E.C. registration if the securities are purchased for investment as opposed to being resold. The size of the issue is not limited, but its sale is limited to a maximum of thirty-five non-accredited investors.

Warrants - A type of security that entitles the holder to buy a proportionate amount of common stock or preferred stock at a specified price for a period of years. Warrants are usually issued together with a loan, a bond or preferred stock --and act as sweeteners, to enhance the marketability of the accompanying securities. They are also known as stock-purchase warrants and subscription warrants.

The Write Time

EXPOSE YOURSELF

The Young Venture Capital Society is looking for **new contributors** to the newsletter and resources page on interesting and educational content. Topics we are focused on include:

- Angels and angel networks
- Biotech and life science primers
- Security primers
- Secondary investing
- Placement agents
- Raising capital in 2005
- Tech transfer investing
- And numerous other topics....

If you **interested in contributing** on these or other topics, please contact us at info@yvc.org

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it would be for other later stage funds. We are often involved in M&A and roll-up transactions where Associates must understand how to model a complex deal correctly.

Q: In your experience, what do you look for in interviewing candidates?

~ Culture and chemistry fit is the most important criteria to understand when evaluating candidates. The venture capital business is an apprentice business. You are working for a partner or a series of partners and the right candidate must be able to work closely and fit into the culture of Pequot Ventures. Beyond cultural fit, each venture firm is different. We emphasize both how candidates think and how quantitatively proficient they are. Since roll-ups, spinouts and M&A are typical transactions for us; the Associate's analysis becomes more significant, and can materially impact our decisions. These quantitative skills are a crucial. Additionally, we like to see that they have a financial focus. At Pequot Ventures, no matter what the technology is, the team moves quickly to comprehend how the company makes money. Lastly, and the most difficult to determine in an interview, we like to gage the candidate's nose for a deal. Can they demonstrate ideas and sources for deal-flow? It is important to us at Pequot Ventures to see if the candidates know where the puck is going (e.g., where should we be investing). Candidates perform poorly in interviews as a result of not having thoughtful ideas. Professionals looking to become venture capitalists should have very specific ideas on what sectors and sub-sectors are interesting and sources for deals.

Q: What are some difficult questions that candidates have stumbled on?

~ If you had a \$50 million fund, where would you invest? The question is really testing the candidate's logic and thinking; we want to determine if the candidate is thoughtful about how they look at investing. Another critical aspect to understanding the candidate is by examining the questions they ask. They should ask about the firm's track record, where the firm has made money and what companies make up the current portfolio? Candidates should be prepared and want to understand the portfolio, and why certain investments were made. Lastly, many candidates have struggled when answering the question of "what makes a good venture capitalist?" Lots of candidates do not focus on how important the people element is to this business. Being brought in on a deal, means that management and co-investors want to work with you to make a company successful.

Q: What are some of the ways candidates have done well, and exceeded expectations, and where have they failed?

~ Pequot Ventures is very focused on conducting deep due diligence. Associates have exceeded our expectations through their level of detail and depth of questioning. When assignments are given to Associates, they need to address all the possible scenarios. Follow-up needs to be extremely high. If a partner pushes back on an associate with 5 or 6 items, the Associate should resolve all 5 or 6 items; the associate should never leave any issues dangling. Moreover, intellectual curiosity is a key to distinguishing yourself. Probing into a deal, management and the technology is extremely important. Associates should do this not because they have to, but because they want to. What separates the good Associate from the pack is how well they take advantage of being empowered. Many people come into this business being very task oriented and reactive to what is required to complete a deal. The ones that are empowered and proactively become experts in a given area are the ones that thrive.

Q: How should candidates aim to advance up the ladder in a VC firm?

~ Again, it is about being proactive and empowered. Executing flawlessly is a must. But in order to advance to the partner level, one must become an expert in a specific sector and drive successful deals.



Book Review

Inside Secrets to Venture Capital

Brian E. Hill, Dee Power

ISBN: 0-471-41406-9

304 pages

Published April 2001, by John Wiley & Sons

Inside Secrets to Venture Capital, written in 2001, is primarily for entrepreneurs and is a good read for those people just or recently beginning to learn about the venture capital industry, its players and the general process of finding, accessing and working with venture investors. While not highly technical, the book will allow readers to understand the basics on venture capital, get acquainted with key terms and definitions such as “burn rate, and tranches”, while also providing insight through the quotes, or “Advice from” a venture capitalist, entrepreneurs, angel investor or others spread throughout the book. Below are only some sample take-aways from reading the book (there are many):

Basic Information

- The book defines the typical profile of a venture capitalist, and what they can provide.
- Inside Secrets provides the venture capitalist point of view on working with entrepreneurs as well as the entrepreneurs’ point of view in working with the VCs.
- Comprehend how to find VCs and learn how they prefer to be contacted

Definitions

- Learn the different stages of financing (start-up, first stage, second stage, established and turnaround)
- Understand what a business plan looks like (the book provides the elements or table of contents in a business plan)
- Comprehend how angel investors work

Insight

- Entrepreneurs should know that when competing for capital they are competing against the venture fund’s entire deal flow.
- VC provide critiques and criticisms of different elements of the business plans they have received
- Learn the critical factors that influence venture capitalists decision on funding a start-up (and why they pass on deals).

Q: How important is operating experience as compared to transactional experience?

~ We at Pequot Ventures have gone back forth on this. Both are very useful. Most of our recent hires have transactional experience. Down the road, if someone is looking to join a venture firm as a Partner, proven successful operating experience becomes more important. Also, operating experience can provide more value in certain sectors. For instance, in the Biotech space, it is more beneficial to have come out of industry. But in the software and services sector, if a person is coming out of business development or marketing, it is not considered as valuable and can be a more difficult path to get into venture capital.

Q: How should interested professionals go about networking and meeting with VCs (cold calling, alumni, and organizations)?

~ Be persistent! Passionate candidates should leverage their entire network, and should use cold calling and cold emailing as a method of connecting with VCs. Again, candidates should be professionally persistent. In the event, the candidate gets a meeting, they should be extremely organized. Time is precious. You don’t want to waste people’s time.

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Venture Debt –Another tool of the VC

June 10, 2005

By: Mathew Guliner

Paul J. Marino

In the ever evolving world of venture capital, many venture capital firms (“VCs”) have found it difficult to find investment opportunities that present the promise of higher than market returns with traditional style investing. As a result, many VCs have deviated from typical investing styles and have begun to create new (at least in the VC world) formulas for investment success. One such formula is debt based investing.

Within the last few years, due to a variety of factors including, risk averse behavior, lack of exit strategy (partially due to the poor performing IPO market), and a dearth of investment ready companies, debt based investing has become a viable alternative to traditional investing for many VCs. Venture debt as it is known, is usually structured as a (i) term loan, (ii) generally 2-4 years, (iii) whereby the VC lends money to the company using a promissory note (often collateralized by the company’s equity and assets), and (iv) the VC receives either warrants with the loan, or (v) the note is convertible to equity at the option of the note holder. This structure has become popular with some VCs because it allows the same protection as traditional debentures (bonds, *etc.*) on the downside (by using securitized debt) as well the ability to participate in the upside of a deal by use of a conversion feature or warrants.

Lending venture debt usually comes in one of two forms, venture lending or venture leasing. Lending relates to money needed for operating expenses where venture leasing is more often for purchase of equipment, land, or other tangible assets. Generally, one thinks of a loan being issued by a traditional lender (such as a bank) and not by a VC. However, as many companies have found, since a VC is not tied to rigid state and federal regulations, a VC often offers more competitive rates and features than a traditional lender and more importantly it can structure a loan in a variety of ways, including as subordinated debt. This is an important

~Book Review Continued~

- Understand what VCs look for in management teams
- Where to find or locate VCs, venture capital clubs or organizations and all other related resources.
- Understand some basics on venture capital valuation

“Advice From...”

- David Cowen, Managing Partner, Bessemer Venture Partners
- Mike Carusi, General Partner, Advanced Technology Ventures
- Patrick Sheehan, Partner, 3i Group
- Shanda Bahles, General Partner, El Dorado Ventures

In all, the book is helpful and resourceful, and especially worth the time if you are relatively new to understanding the venture capital industry (or you are a first time entrepreneur). For those more advanced or more knowledgeable on venture capital, you might find the read a bit repetitive, but still probably worth your time.



~Blogs and Links~

Below are some interesting and educational blogs and links to check out.

BLOGS

VentureBlog – www.ventureblog.com
Allen Morgan - <http://allensblog.typepad.com/>
Steve Brotman - <http://brotman.blogs.com/vcball/>
Steve Jurvetson - <http://jurvetson.blogspot.com/>
Fred Wilson - <http://avc.blogs.com/>

LINKS

VCfodder – www.vcfodder.com
VC Experts – www.vcexperts.com
SJ Mercury News - <http://www.siliconbeat.com/>



element for many VCs and companies because it removes any possible impairment that the funding could have on other lending facilities. Additionally, (again as a direct result of the lack of regulatory oversight) VCs can fund start-up companies with less collateral to pledge, less cash on the books or assets to secure because they do not have to meet governmental structured thresholds.

A company usually seeks venture debt either (i) before participating in a round of preferred financing (as a bridge), (ii) in conjunction with financing (as a means to stave off further dilution), and/or (iii) following equity financing (again to stave off immediate dilution and to create more free-cash flow). Regarding the first scenario, a bridge loan can prove invaluable to many start-ups because many start-ups need the extra time to improve revenue, ink another deal (contract), and (hopefully) improve their valuation.

The same could be true about the second scenario whereby VCs lend money side by side with a private placement. In that scenario, a VCs lender may not be intrigued enough in the company to make an equity placement but is keen enough in the company that it believes in its ability to continue and improve operations. In the third scenario, a company may not wish to further dilute investors (or may be prohibited from doing so) and the prospect of adding debt will not immediately dilute current shareholders.

Another benefit of venture debt is that debt financing is often cheaper than equity financing. For instance, an equity investment of \$1mm at a pre-money valuation of \$1mm will buy the VC 50% of the company. If the company succeeds and the future valuation is \$20mm, the VCs stake is now worth \$10mm; a return that is excellent on a \$1mm investment. Whereas the venture debt holders would receive their preference rate plus warrants. Additionally, venture debt providers are usually less involved than typical VCs and usually are not on the board and only provide (usually) strategic guidance to start-ups (which is not always good and certainly (from the company’s perspective not always bad).

However, venture lending is not for every company. Start-ups must be able to pay the monthly interest associated with the loan (unless the loan has a preferred in kind payment structure). Assuming that the debt is structured in a traditional manner, the interest payment from venture debt may not be a perfect fit for some early stage pre-revenue companies. Also, venture lenders want to ensure that the officers of the company realize that the loan is in fact a loan and not an investment and often times make the loan a recourse loan thereby making the company’s officers execute a personal guarantee.

However, in general debt is beneficial to both parties. It allows a risk averse VC to engage a start-up all the while avoiding the downside of a crash and burn scenario and share in the upside of a homerun. For a start-up company, venture debt is often a good first experience with VCs because it allows the company to retain ownership (no dilution) and can extend the amount of time, or runway, before needing a new round of financing.

Some providers include: RBC Centura , Lighthouse Capital Partners, Silicon Valley Bank, CoAmerica Eastward Capital Partners (CommVest), Horizon Technology Finance, and Sand Hill Capital

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The 2005 Women's Technology Cluster Entrepreneur Venture Conference

Tuesday, November 1, 2005, at the Microsoft Silicon Valley Conference Center, Mt. View, CA.

The conference showcases high-caliber, women-led technology and life science companies to an audience of VCs, angel investors, and industry experts. Last year's conference, produced in conjunction with Springboard Enterprises, had over 400 attendees, 50 exhibitors, and 24 presenters – 1/3 received funding, and two companies received over \$5M in investments – a success measure unparalleled in the industry. In fact, it was at this conference that Hummer Winblad Venture Partners and portfolio company Palamida first met, leading to a \$5M investment together with Walden VC. It is because of this that we are pleased to participate in and endorse the 2005 Venture Conference.

Presented annually, the WTC venture conference offers a unique approach to the investor presentation. The Conference, coupled with an Entrepreneurial Immersion Program (EIP), is designed to prepare the Entrepreneur for the fundraising process and to help mitigate the inherent risks associated with equity investing. Through the EIP sessions, entrepreneurs engage industry experts and work side by side with seasoned CEOs and coaches. The EIP includes half-day sessions on topics such as Market Analysis, Business Plans, Financials and Term Sheet Negotiations.

When considering opportunities to meet quality entrepreneurs, we hope you will consider the value of attending the 2005 WTC Entrepreneur Venture Conference. We encourage you to register early.

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