

## Deep Pockets: Introducing the Limited Partner

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The **limited partner** (“LP”) is a key player in the venture capital (“VC”) equation. Publicly consumable content discussing LPs typically focuses on the legal distinction between their roles and that of a general partner (“GP”). This column will serve as a supplement to the aforementioned body of knowledge by shedding light on the LP as a portfolio manager rather than a legal entity.

LPs vary dramatically in assets under management (“AUM”) and allocation to VC. For the sake of narrowing this column's scope, the remaining commentary will focus on the following types of investors: pension funds, endowments, foundations, fund of funds, gatekeepers, consultants and family offices. Of which, the LP is expected to have at least \$100 million allocated to VC.

It is commonplace for large investors to implement a manager of managers strategy. This type of strategy involves the explicit outsourcing of company/security selection (“CSS”) to an outside manager. This permits the LP to keep a slim staff that focuses on asset allocation and other portfolio management responsibilities.

The portfolio management responsibilities include, but are not limited to, deal flow management, portfolio monitoring and board/principal management. Deal flow management and due diligence are tasks shared by both GPs and LPs. The difference here is that LPs are sourcing deals with GPs, while GPs are sourcing deals with companies. The time spent on deal flow management is typically inversely related to the age of the VC allocation. This means that newer VC investors typically need to spend a significant amount of time building relationships within the community. The longstanding programs typically see sufficient deals because they are already on the radar of many of the GPs.

For preexisting investments, the LP typically monitors cash flows for performance and portfolio companies (that the limited partnership holds) for exposure. This information is critical to the investment officer because he/she is “flying the plane.”

### **Common questions may include the following:**

- What is the aggregate exposure (across all limited partnerships and coinvestments) to early/seed companies?
- What is the exposure to company X?
- On average, how long does it take for a VC fund to return all of the capital invested?
- What is the exposure to Japan?
- Should the portfolio liquidate partnership Z via the secondary market?

At the end of the day, most investment management teams end up answering to some sort of board and/or principals. The information analyzed during the deal flow management and portfolio monitoring processes are typically presented to the board on a quarterly basis. Some boards opt to have a hands-off approach and let the investment team make the majority of the decisions. On the other end of the spectrum is a very involved board that requires that all investment decisions be approved. Nevertheless, it is important that the investment officers maintain a clear line of communication with the board in order to foster a nimble environment.

These concepts and many others will be expanded upon in future articles. Stay tuned.