The 12 Fold Way to VC Funding:
A Roadmap For Technology-based Product Companies

Robert Weber
Managing Director
Strategy Kinetics, LLC
Weber@StrategyKinetics.com
www.strategykinetics.com

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Assumptions

- Getting funded is among the most difficult tasks in the universe
  - Statistics show that few companies actually raise money from Venture Capitalists – 1 in 75 or worse depending on VC & market
  - They see a gazillion business plans and hear a bazillion ideas every year
- VCs are risk adverse
  - VCs look for reasons not to invest
  - Risk control and mitigation are key
- All the “go” items must be in place; problems readily fixable
- There must be no show stoppers; some examples:
  - Unfundable CEO – must have made someone money previously
  - Incomplete management team
  - Excessive rigidity – founders unwilling to part with an appropriate portion of equity
  - Excessive ego, disharmony – team players are essential
The 12 Fold Way To VC Funding

1. People and Board with the “Right Stuff”
2. The Elusive 10X Advantage
3. Service Providers On Board
4. Intellectual Property
5. Productization Roadmap
6. Market Validation
7. Market Entry Strategy
8. Business Plan
9. Funding Strategy
10. Research VCs [and Angels]
11. Investor Pitches - Plural
12. Prepared for Due Diligence
People – Team Identified

- Fundable CEO – someone VCs recognize as having done it before, deep domain knowledge, outstanding leader and people manager
  - VCs fund CEOs and teams
  - If you don’t have a CEO or the right CEO, some VCs may help
- Management team identified – they have to be ready to join on funding if not already on board
- Specific roles may vary by business
  - Chief Technology Officer / Chief Scientist
  - VP Engineering / Development
  - VP Business Development / Sales / Marketing
  - VP / Director Finance & Administration
People - Boards

- **Board of Directors**
  - Legal, fiduciary obligations
    - Typically 1 or 2 inside people plus 1 from each VC in the investor syndicate
    - Investors effectively running the company – get used to it
    - Not friends and family; usually not Angels

- **Advisory Board**
  - Depends on the nature of the business
    - May be all scientists and engineers with public visibility, positive reputation
    - May include industry-relevant executives, leaders
    - Some should be identified and on board before approaching investors – enhances credibility
The Elusive 10X Advantage

- Best funding case demonstrates at least one important 10X advantage
  - 6X to 8X may do fine, depending....

- Price / performance advantage
  - Often important because it reduces the likelihood that price competition will succeed against new product

- Demonstrating advantages requires:
  - Convincing cost projections
  - At least some engineering data / performance data
  - May require competitive benchmarking (if feasible)
  - Simulations and modeling may be helpful, depending...
Service Providers

● Have Corporate Legal firm on board:
  - Company formed in Delaware
  - Founders’ documents signed, sealed, delivered
  - Employee stock option plan filed (if necessary)
  - Basic legal document “starter set” received

● Have IP law firm on board

● Line up:
  - Accountant
    ● Examples: Deloitte, Coopers
  - Bank
    ● Example: Silicon Valley Bank
  - Outsourced HR (if going that route)
    ● Example: Administaff
  - Insurance
Intellectual Property

● IP matters to VCs
  - Asset in worst case scenario
  - Have at least one provisional or utility application on file before seeking funding
  - Find patent attorney with background in the specific technology or related field

● VCs may request “freedom to operate” opinion
  - Would product possibly infringe the IP of others?
  - Possible tricky question because of potential willful infringement issues
  - May want to seek advice of patent litigator with relevant experience
Productization Roadmap
(For pre-commercial technologies)

● Working product prototype best
  - Means that this is what you intend to go to market with investor’s money and additional engineering
  - Sufficiently advanced to get a handle on component and manufacturing costs
  - Convinces investors that the idea is not a “science project”

● Working key components good
  - Better than “the drawing board”
  - Initial proof of concept
  - Need to have roadmap with engineering milestones showing how to get to a product prototype
  - Open engineering questions, problems, issues identified
Market Validation

- Paying customers are best. Period.
- Otherwise:
  - Beta customers who will sing praises and say they are committed to paying the amounts in the business plan
  - Potential customers:
    - Letters of Intent saying that the product solves real problems for them and that on launch they will pay the amounts in the business plan
    - Reference letters indicating customers would buy if product were available commercially and that the price / performance is very attractive if delivered.
  - Customer as (potential) investor / partner
    - Provides validation BUT may entail strategically negative terms such as Right of First Refusal.
Market Entry Strategy

- Does not matter one iota that the Total Available Market is a bazillion bucks globally
  - Your not solving world hunger or boiling the ocean
- Realistic estimate of first Target Market
  - Who is the customer? Who makes buying decisions?
  - Key value proposition
  - Sources of customer resistance? Substitution threats?
  - Referenceable potential customers / partners required
- 5-year market-share forecast has to be attainable
- Channel / Direct / Mixed distribution strategy identified
- Marketing / communications strategy
  - Key messages for target market and how delivered and at what cost
Business Plan

- Varies by business, but highlights may include
  - $60M-$100M+ in revenue in 5 years
  - Cash flow breakeven in segment-appropriate timeframe
  - Margins appropriate to business, industry
  - 5 year financial P/L Pro Formas
- Built month by month and bottoms up
- Short 5-8 page narrative Executive Summary
  - People, product value proposition, market, technologies, financial highlights, financing desired, contact info
- 30 slide BP presentation, which is not the same as the pitch presentation
  - Hold in reserve for follow-on meeting if invited back
Funding Strategy - Financials

- Capital requirements driven by BP
  - Series A, B, [C] round forecasts
- Take as little money as truly needed to achieve Series A milestones
- Know projected capital to cash breakeven
- Have detailed Use of Proceeds (“UofP”) for Series A funding
  - Tells investors how their money will be spent
  - Month by month, bottoms up expense projections
  - Include all costs
  - Explore equipment leasing options where appropriate
  - Bring people, equipment on board as needed
- Expect VCs to own 40% to 55% of company at the close of the Series A
Funding Strategy – Term Sheets

- Investors get Preferred Equity, not common stock
- Preferences typically include:
  - Liquidation preferences – what happens if the company is sold or fails – for entrepreneurs, the most important term. Period.
  - Dividend rights – may only apply if declared by the Board [remember who controls the Board]
  - Anti-dilution – if the follow-on round is at a lower price, additional stock issued to participants in the prior round to maintain their proportional ownership
  - Voting rights – what items require approval by the Preferred investors
- Angel round frequently a Convertible Note financing
  - Loan to company that converts at the terms of the Series A
  - Typically with a 20%+ discount to the Series A price depending on the contribution of the Angel investment to risk reduction
Research VCs and Angels

- Find out who in your region is interested in your market, product, customers, etc.
  - What have they invested in previously?
  - What’s their investment strategy
    - Seed? Early Stage? Middle? Mezzanine?
  - Which Partner made which investment?
  - Do they have any money left for new investments?
  - How did their previous fund(s) do?
  - Talk with a company or two they invested in

- Don’t blast your Executive Summary to 40 VC firms
- Do identify 4 to 6 target firms in your region
- Find someone to introduce you to the firm, e.g.,
  - One of their investors – Limited Partners
  - CEO, Board Member of a portfolio company
Investor Pitches

- **Elevator pitch** – one your mother could understand

- **VC Pitch**
  - 15 slides plus supporting material at the end
  - Sell the business opportunity – not the technology
    - Why is this a great opportunity for VC and their investors?
    - If they care about the business, they will look at the technology in detail
  - Practice the pitch with friendlies; someone role-plays VCs
  - Define everyone’s role in the meeting, if you get one
    - Meeting discipline is absolutely essential

- **Angel Pitch** –
  - Company usually seeking a portion of the Series A from Angels
  - Pitch, Financing Strategy, Use of Proceeds adjusted accordingly
Prepared For Due Diligence

- **People**
  - Complete bios, references lined up for CEO, direct reports

- **Engineering**
  - Product definitions, specifications, requirements, documentation
  - Test data, performance data, competitive benchmarks

- **Market**
  - Third party market data if possible
  - Original market research plan / data
  - LOIs, testimonials from prospective customers, channel partners

- **Business Plan**
  - Details of the financial projections, UofPs
  - Confirmations of assumptions, sources, channels

- **IP due diligence**
  - Patent Office communications, Information Disclosure Statements, etc.

- **Corporate and IP Legal**
  - All the corporate paperwork neatly tied up
  - Employment agreements, NDAs, non-competes, etc.
Be Persistent – Good Luck

- May take 6 to 9 to 12 months from start to close

- Be Churchillian:

  “Never give in. Never give in. Never, never, never, never--in nothing, great or small, large or petty--never give in, except to convictions of honor and good sense.”

  Winston Churchill
How We Assist Entrepreneurs

- Strategy assessment and strategic planning;
- Startup formation, launch, and preparation for Angel or VC fundraising;
- Business scope definition and planning;
- Strategic negotiations with potential investors, partners, and customers; and
- Pre-investment strategy and business evaluation,
- Technical (in selected areas) and business due diligence
Contact Information

Robert Weber
Managing Director
Strategy Kinetics, LLC
Skype/AIM: BobWeberBOS
Weber@StrategyKinetics.com
www.strategykinetics.com