BLUMBERG CAPITAL

# VENTURE CAPITAL 101

## I. *Introduction*[1]

In this chapter I will attempt to effectively distill and convey some of the lessons I have learned as an entrepreneur and venture capitalist. I will address alternative sources of financing, an overview of the venture capital ("VC") market, targeting VCs and how to effectively penetrate this insular group of private equity money managers. It is important to know what you will need to best manage the fund raising experience, what you should expect from a VC during this courtship and ultimately what to expect if you decide to choose this path of funding.

To convey the VC process in a few pages is a formidable task. There are many vehicles (VC being one of them) for an entrepreneur to start and grow her business. It is crucial to consider one's overall objectives at the outset before embarking on the journey of starting your own company and raising VC funding. Raising capital from a VC is a marriage and getting a divorce is near impossible so choose wisely!

### A. *Bowling for dollars*

When starting a company, there are a variety of options in terms of financing. Many entrepreneurs choose to grow their companies organically, also referred to as "bootstrapping", meaning self-funding. Often, in the initial stages, you might require a small amount of seed capital—to "germinate" the concept—which is normally sought from friends and family. Typically, these represent the least sophisticated and most expeditious avenue for short-term capital. This group typically has limited resources and is sometimes referred to us as "dumb money", because they add limited value over and above the capital contribution.

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[1] This chapter is to appear in, *How to Value Your Business and Increase its Potential*, by Jay B. Abrams, McGraw-Hill, expected publication date August 2003.

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Angel investors generally invest hundreds of thousands of dollars and often contribute with more than just capital, including go to market strategy and key introductions. Angel investors metaphorically lift you on their "wings" and hopefully elevate your company to the next level of growth. Here you might benefit from some level of expertise if your angel is an industry expert and is in a position to spend time with you to develop your plan. The shortcoming endemic to all of the abovementioned sources of capital is that they typically lack deep pockets and are not necessarily investing in your company as a full time endeavor, but rather, at most, are looking to assist and add value where they can. The ideal structure of angel funding would be in the form of a "bridge" to the next round—called bridge financing—with a discount[2] provided, with warrants,[3] to the angel investor depending on the length of time between the bridge and the first round of investment, usually not to exceed 20% coverage for the money invested.

For example, if the investor puts in $500,000 in bridge financing and you close the Series A[4] round in 6 months, it is reasonable to provide the angel investor an additional 20% warrant coverage such that if you raise $5 million (including the angel bridge which converts into the Series A) at a $5 million premoney[5] valuation, the $500,000 would ordinarily buy 5%

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[2] Discount pertains to pricing shares below the market valuation offered to investors on the same round, which yields preferential pricing.

[3] Warrants are a form of stock shares similar to options, typically priced below market with an exercise time and price.

[4] Usually the first professional investor round of funding in a privately held company is procedurally labeled "Series A", the second round "Series B" etc.

[5] The "value" attributed to the company prior to the investment capital a.k.a. pre-financing.

($500,000/$10 million) of the equity. You would then provide 20% warrant coverage that would give the angel another 1% (20% x 5%). You might tie the bridge to the length of time it takes between the time the angel bridges you the money and the time you close the Series A, e.g., from 0-6 months the angel receives a 20% discount, from 6-12 months 40%, etc. You can change terms monthly on a sliding scale as well. The above can become quite complicated and it is probably wise to adhere to the adage of "Keep It Simple Stupid – KISS"!

Be careful of bringing angel investors onto the Board of Directors and giving up too much control too early. At this stage in the life of your company you do not want to lose control of your destiny to someone who invests only a few hundred thousand dollars and might not be the most experienced, active or knowledgeable investor. Keep the capitalization table simple in these early stages; complicated capitalization structures may scare off future investors (e.g., excessive debt or warrant coverage, inconsistent vesting schedules, equity transfers to inactive parties).

Another category of investor is the strategic investor. This can prove to be a wonderful source of capital, provided there is adequate communication and understanding from the beginning. Know the agenda. Often, a strategic investor will invest for a specific objective that might conflict with your goals. Most other investors will have a similar interest/agenda as you, namely to maximize shareholder value and generate the greatest possible return on investment ("ROI") [6] as possible. Strategic investors, however, might only be interested in leveraging your

[6] The annual ROI is net income divided by the average investment (equity) in the company. The firm as a whole has its own ROI, as does each separate investor group, since each investor group makes its own unique deal at its own implicit valuation.

technology for the benefit of their parent company, which might not always be in the best interest and long term goals of your company. Strategic investors will often seek a licensing or distribution agreement from your company with some preferential terms, the ability to purchase you if you achieve success, or seek to preclude you from partnering with their competitors. To the extent that you can leverage the strategic investor network and protect yourself from any downside, it can position you advantageously against some of your competitors in the marketplace. A strategic investor might be a vendor or partner you are currently working with on manufacturing or distribution or an actual customer that would be interested in investing in your company. Be cautious and maintain the proper balance of disclosure and confidentiality between your prospective strategic investor and partner. Limit the control or level of influence a strategic investor can exert by not giving them Board representation and always preserving your right to partner with potential competitors. Never constrain the company from being able to sell, license or partner with anyone that can add value to the company. Fortunately, strategic investors often provide a global perspective, excellent distribution channels, deep pockets, are less price sensitive, usually prefer a VC to lead the investment and rarely seek a role on the Board.

This leads us to venture capitalists—fulltime professional investors with deep pockets, whose sole task is to assist you with the growth of your company for maximum financial return. VCs are price sensitive, active investors who seek Board representation and expect you to deliver on your promises. Be careful on what you “sell” pre-financing, because you will be expected to deliver on those projections post financing in the form of milestones.

Recently, as a result of the burst of the Internet bubble, venture capitalists have been described as having deep pockets with short arms. This means that many large VC firms (sometimes managing in excess of $1 billion) have become so distracted by existing and legacy portfolio companies that they now have minimal time to investigate new investment opportunities and even less time to service and assist those existing portfolio companies that are in need of their professional help. Evaporation of the Initial Public Offering ("IPO") market and *de minimus* activity on the mergers and acquisition ("M&A") side have caused the average VC to be "stuck" with a number of companies with no viable exit in the near term.

*B. Overview of venture capital*

The venture capital community has been experiencing unprecedented change, both positive and negative, in the last decade. From 1998 through 2001, approximately 700 VC firms in the United States ("US") raised and invested $200 billion dollars in over 15,000 companies, the majority of them being software and communications companies. Roughly 33% of all venture investment activity in the US takes place in Silicon Valley, with the next highest regions (Southern California, Texas and Boston) together comprising another 21%. During this period over 500 companies raised $50 billion through an IPO, and 1,300 companies were merged or acquired for approximately $180 billion dollars. On average, it took 3.3 years from when the first venture capital firm invested money into the company until the company's IPO.[7] Needless to say, these were exciting times and many acquired inordinate amounts of wealth.

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[7] *Venture Capital Industry Report, VentureOne*

In spite of the recent and continued downturn in the overall US and global economies, the challenge of starting a company – office space, recruiting talent – has never been less expensive. As Warren Buffett, renowned investor and head of Berkshire Hathaway, likes to quote his mother as saying, "buy low and sell high." Moreover, if you are successful in raising venture capital it is less likely you will see as many competitors being funded as you might have in the past. Nonetheless, the standard/threshold has gone up on what is getting funded. Gone are the days of funding a great (or even okay) idea with no defined business model, viable path to profitability and significant barriers to entry.

On the negative side, it is a challenging time to sell technology to an enterprise. Many of the Fortune 500 companies have been impaired over the last few years by dedicating dollars and internal resources on early stage start-ups that have gone out of business. As the saying goes, no one ever got fired for buying IBM. Many enterprises were tantalized by the exciting technologies being developed in Silicon Valley and abroad by young, visionary entrepreneurs and were enticed to spend much resources on implementing these cutting edge technologies—only to see the companies disappear, leaving them frustrated and exposed. Once burned twice shy. This, coupled with Information Technology ("IT") budgets being dramatically reduced (one CIO of a large financial institution admitted that his 2002 budget was reduced 15% from 2001 to $1.5B), has made it exceptionally difficult for young start-ups to get traction from these typical early adopters of technology and allay the fears of the more established companies that they are financially viable in the future to service, maintain and support the technology they are selling. With IT budgets being reduced to cut costs, enterprises are pushing hard to see a more rapid payback, which also means a higher ROI. Historically, it might have sufficed to demonstrate a

payback over 24-36 months, while now expectations are 6-18 months. Naturally, this can wreak havoc on pricing models and revenue expectations for the early stage companies trying to penetrate into the market.

Make sure you are developing a product that is a "must have" and not a "nice to have" type of product. According to a recent Giga CIO survey, some of the spending priorities include: short-term and clear ROI, Internet security, integration and outsourcing.

*II. Targeting the right venture capital firm*

Do your homework before you meet with a venture capitalist. This means knowing in advance as much as you possibly can about his firm, background, prior board seats and existing investments. Time is money. Come prepared and on time. Keep your presentation short. Typically you will have less than one hour. If you can't convey your message in 30 minutes, you are not ready for prime time. If you are making a physical presentation, bring everything you need, including hard copies in case you have computer problems or the projector doesn't work.[8] Convey your message in 15 slides or less, discussing each of the following: agenda, team, vision, value proposition, barriers to entry, technology, products, competition, size of market, financials, use of funds, capitalization table, customers and exit comparables.

Notably, VCs tend to invest at different stages in the life of a company. Blumberg Capital is a seed/early stage VC, and we are usually the first professional investors, a.k.a. Series

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[8] Parenthetically, do not invest in a $3,000 projector. All VCs will have one, and you can always present slides in hard copy for the time being. Be frugal. You never have enough cash. Everything costs more and takes longer than you planned.

A on a deal. Next, there are middle and later stage VCs that prefer to invest in the Series B, C and D rounds. Finally, there are mezzanine, late stage and pre-IPO funds that prefer to invest in the final rounds before an IPO. One key differentiator is risk vs. return for the different stage VCs. The earlier the VC tends to invest and the greater inherent risks remaining—technology, competition, team, execution, future financing, customers—the higher return the VC will expect to achieve. An early stage Series A VC expects a 10X multiple, while a mezzanine investor will be happy with a 2X to 4X return. Similarly, an early stage VC expects to wait 4 – 7 years to exit via M&A or IPO, while a late stage investor expects an exit in less than 2 years.

Do not target one VC and expect to raise capital. Try and arrange as many meetings with as many appropriate VCs as you can. Nothing will better position you to negotiate favorable terms than having a variety of financing options. Try and keep the VC process at similar stages, so one group doesn't get much further ahead than another and force you to make a decision prematurely. Ideally, you would strive to have a few VCs culminating their diligence at the same time, so you might actually receive multiple term sheets and have alternative options. This will also provide an opportunity to create a syndicate. You should also try and improve your presentation and learn from each meeting to continuously enhance your presentation and communication skills.

Moreover, it is important to realize that not every start-up is appropriate for VC funding. You must be willing to bring partners into your company and share in the governance and key decision, direction and vision of your company. We look for opportunities where the company forecasts annual revenue growth in excess of 100% in the early years after investment and can achieve annual revenues in excess of $50 million by year five. The company also should be

focused on reaching an exit—IPO or M&A—during this time period. If you are looking to run your own business, remain privately held, and are not interested in reporting to a discerning Board of Directors, then VC is not for you. If you have been growing your business at a slower pace but believe the market you are addressing is ripe for incredible, as yet untapped, growth, you might consider approaching a VC.

*A. Sources of deal flow*

It is important to realize that the number one source of deal flow for most venture capital firms is their existing network of entrepreneurs that they have funded previously. The second most valued source is other venture capital firms. The third most reliable source is general service providers that work in the industry (accountants, lawyers, bankers, etc.). *You will be hard pressed to get too much attention from most VCs without having an introduction through one of the abovementioned sources of deal flow. I can't emphasize enough how important it is to attempt, where possible, to have your business plan submitted to the targeted venture firm through a "friendly" introduction or referral.*

*B. Evaluating your needs*

Some of the questions you should ask yourself before you decide whom to approach for investment capital are:

(1) Are you looking to grow the management team?

(2) Do you have customers that are ready to purchase from you in the near future?

(3) Are you in need of marketing talent that can help you hone your message?

(4) Are you looking for passive investors?

(5) Is your Board of Directors in need of more experienced industry experts?

(6) How much capital do you need to break-even?

(7) Do you expect to open up satellite offices?

(8) Which are the key alliances you need to form over the next 12 months and how will you best achieve these?

(9) Have the investors you are approaching founded, funded or exited a similar company to yours in the past?

As an example of (9), if you want to sign an Original Equipment Manufacturing (“OEM”) or channel agreement with a firm like Sun Microsystems, BEA, Intel, Amazon or Mercury Interactive, have the venture capital partners done this in the past? Have they sold companies to the abovementioned firms in the past? Maybe they even funded Sun, BEA, or Intel when they were start-ups! Ask the VCs if they are invested in, shareholders in or evaluating something that might be perceived in any way competitive. It is common for VCs to do exhaustive, analytical analysis of a particular segment in the market where they are interested in making an investment. The VCs often will attempt to meet with all the companies in the particular space and try and glean the “best of breed” for an investment.

Another essential consideration for an entrepreneur contemplating funding from a VC is for the Founder to appreciate what the VC can “deliver” on behalf of your company other than investment dollars. It is crucial for the start-up in these nascent stages to have investors that can facilitate introductions to prospective reference customers on behalf of the company. You must find a champion. This person will drive the process internally, will find the budget to pay you, and will act as a reference to other potential customers and investors. Without a champion, you will not close the deal. Getting the attention of a prospective customer, especially in the current

rescessionary climate, is challenging at best and agonizing, time consuming, or impossible at worst. Try to find as many champions as you can, because large organizations constantly go through restructuring. It is common to go through 6 months of meetings, pitches and negotiations, to be on the verge of signing a pilot, proof of concept or beta only to find out your champion was fired, left for another group or underwent a reorganization—and you are back to step one—except that you have been "burning your cash" without getting closer to the sale. Try and have as many points of contact as you can, as many champions as you can, and keep as many opportunities alive, because this will happen. This being the case, the ability of a VC to pick up the phone and contact the right person at the right company, a C-level person (CEO, CIO, CTO, CFO, etc.) that has the authority to drive the process and assist with getting you to present to the right team, is invaluable. Time to market is synonymous with survival. Hopefully, these initial beta customers will convert to your first paying customers, while providing crucial feedback regarding the feature set within your product and assist you with prioritizing your ongoing product development. You must be cautious to balance your needs, resources and objectives with the customers, as they obviously have their own agenda. Again, set expectations up front for everyone to avoid disappointment.

Your decision whether to seek venture capital should be based on a calculation of the costs versus the benefits, i.e., dilution of ownership and control of the business for the increase in the value of the company that arises from the greater speed to market and resulting size that the financing, connections, and wisdom that the VC brings to the table.

*C. The CEO*

It is worthwhile to discuss the CEO position. This is a very delicate and sensitive issue. Often, the existing CEO does not have all the skills to drive a company forward to an eventual IPO or M&A. The question is timing. Typically the existing CEO/Founder is usually either very technical and/or entrepreneurial, but will invariably have flaws and be deficient in some areas such as finance, sales, marketing, etc. Together, the VC and Founders should discuss this important issue prior to funding to avoid undue pain and suffering. Lack of communication can derail any company—all the more so a start-up.

*Everyone must set realistic expectations*. The entrepreneur must be honest with what he can contribute in what period of time, and the VCs should set candid expectations for what they can contribute in the overall process. Many of us, possibly with the best intentions, over promise and under deliver, which is damaging to all parties. Most VCs have in their *kerietsu* (network) a number of viable candidates to take the helm, some of whom might even assist the VC in its due diligence process thereby also providing an opportunity for the Founders, VC and prospective CEO to interact. A CEO prospect that has come through the ranks over the decades and has deep experience both technically and in sales can be well suited for the position, because he or she is a “fellow” engineer that earns respect from the Founders and obviously can understand and empathize with the team, while having a unique ability to contribute on all levels. It is common for a VC to collaborate with the Founders and an outside recruiting firm focused on CEO searches in a particular discipline, stage, sector, etc. The key is to maintain lines of communication at all times and to monitor expectations.

*D. Getting to a meeting*

A typical $100 million venture capital firm receives at least 1,500 business plans per year. Of those about 100 (6.7%) will be invited to meet with the partners. Perhaps 50 (3.3%) will result in serious due diligence, 10 (0.7%) of them will be offered a term sheet (see below), of which 5 (0.3%) of them ultimately will obtain funding.[9] Most VC firms this size will have 3-5 investment professionals and will likely have the resources to execute 1-2 deals per professional per year. The statistics of obtaining funding dramatically improve if you get that first meeting. If you get to a meeting, your odds of getting funding increase 30 times from 0.3% to over 10%. These statistics demonstrate why it is crucial *how* you get to your VC, because you are more likely to get a meeting if your materials reach the VCs desk through a trusted and friendly source.

On the communications side, be responsive and follow up. This sounds obvious and straightforward, but you would be surprised. If a VC asks you for more information – provide it as quickly and effectively as possible. Always try and get a face-to-face meeting!

*III. The venture process*

Talk to someone who has been through this process to get a sense of what to expect. VCs vary in their speed of funding, depending on stage, but expect the process to take 1 to 6 months from the first meeting to having money in the bank, with an average of 3 months. VCs tend to be extremely busy multi-tasking and are constantly traveling and working with portfolio companies; do not take a lack of a response as a negative or as a personal insult. It is often just a question of

[9] These numbers are only an estimate.

time. There are absolutely not enough hours in the VC's day. Try to follow-up in a friendly manner, email being the ideal form of communication.

Start the process with a personalized, friendly, short introductory email with a 3 – 5 page summary attached. In the text of the email state how you came to email this VC and why you believe this opportunity is appropriate for this person, firm, etc. In one paragraph or less convey your value proposition, barriers to entry, team, advisors, customers and anything else you think will entice the VC to open your attachment. At a later date you should be prepared to forward a full business plan, financial model with assumptions and comparables, a PowerPoint® presentation, white papers and marketing reports or customer references that validate your business plan. Good collateral materials address issues (the 5 Ts, see below) in a clear, concise and focused fashion.

*A. Non-disclosure agreements*

VCs will not sign non-disclosure agreements ("NDA"). We receive so many plans each week that if we signed every NDA request, we would quickly be overwhelmed with legal documentation. Our reputation depends on our professionalism and on our ability to maintain your trust and confidence. Conversely, you should absolutely insist on one from strategic investors/partners at some point in time.

*B. Valuation*

Be careful about providing a valuation. If your valuation is based on a discount to a market leader, do not assume in your financial model that you will surpass even the most successful companies in your space. You will lose your credibility, and this will impact negatively on your valuation. A VC will respect a well thought out financial model, *with*

*reasonable but aggressive assumptions*, as long as you can defend it. What can be helpful in the nascent stages—and much more so as the company matures—is a professional valuation (do not try this at home!) based on comparables in the industry with some level of discount.

Traditional methods used to value a privately held company are discounted cash flow, analysis of market comparables or some analysis of a company's net present value. In the early stage of a start up it is almost impossible for an amateur to apply the former analysis. Discounts to future cash flow are challenging on many levels. When you are contemplating investment in a company that doesn't expect to even have a product for 24 months let alone significant revenues for at least another 12 months, expect serious critique and "push back" from the VC on both your assumptions and your perceived valuation. This is very sophisticated work that needs to be well grounded with realistic assumptions, market research that accurately quantifies the size of the market and realistic expectations of market share over what period of time. The latter exercise (analysis of market comparables) is slightly more applicable, although often equally difficult to leverage. As an example, VCs often access VentureOne (www.v1.com) to review companies that are in a similar sector to get perspective on how much capital they needed to raise, at what valuations they raised capital, and how much capital was needed to achieve a liquidity event.[10] This is helpful, but it cannot be applied in a vacuum. Market conditions and volatility, availability of capital, macroeconomic and microeconomic conditions are only a few of the drivers that will significantly impact valuations.

[10] While you might be able to glean some information from their site, full access requires a subscription that costs in excess of $15,000 per annum.

*C. Advisory board*

How do you obtain a "friendly" introduction to a VC? How do you find a "champion" at your first customers? You are in the relationship business. Leverage your network of relationships to open up doors, to find your "friends and champions" and if it is feasible, make them advisors. Try and build a value added advisory board with industry experts that can add credibility to complement your management team especially if you are an early stage company. Advisors should be able to assist you with VC meetings, customer introductions, market and strategy, recruiting key management team and other critical functions.[11]

*D. Due diligence*

The due diligence process can be painstaking, expensive and incredibly time consuming for entrepreneurs and VCs alike. Think of this as an opportunity to review your strategy, financial model, business development and sales efforts, future product development, etc. As part of their due diligence, most VCs will introduce you to prospective customers and possibly some C-level management to determine their level of interest in your product. Is this a luxury purchase for the CIO or a must have over the next 12 months? These are reasonable questions, the answers to which you should also want to know before you start this journey. It is in everyone's best interest when an investor can help accelerate this "truth seeking" process to collectively arrive at a decision whether or not to invest.

Due diligence can be broken down into a number of broad categories: Technology, Market, Financial, Legal, Team, Comparables, Competition, and Exit strategy. Being a venture

[11] Advisory board compensation might be 0.1% warrants with a 3 year vesting period. This might represent 25,000 shares, so it is significant.

capitalist is not rocket science. For the most part it is being thorough and reviewing the above checklist of items. Many funds, depending on the stage of investment, are not willing to take some of these risks. Some later stage funds (expansion capital) do not take technology or market risk, and as such, prefer to invest in companies with a proven technology, many reference customers and significant revenues. As such, they might invest in a small team of 50 people that are on an annual run rate in excess of $10 million and are taking risk on continued execution, exit strategy, pricing, change in market conditions, etc. Of course the valuation of the company, dollars needed by the company and inherent skill sets of these varied investors, is quite different.

*E. Term sheets*

A term sheet is a document that puts forth a summary of the terms and conditions that will apply if the venture capital firm and the entrepreneur hope to consummate a transaction. Typically, a term sheet is non-binding, subject to further due diligence and is the necessary step before having counsel draft final, detailed documents. This is the document that contains the proposed valuation of the company along with many other essential terms that are equally if not more important as relates to governance, control, etc. Many significant terms are not addressed in the term sheet, but are typically left for the initial drafting of the full set of final documents. Entrepreneurs always seem to have angst over valuation, so let's take a few moments to discuss the perceived drivers of valuation, both traditional and from the perspective of a venture capitalist.

*IV. The 5 T's*

Team. Timing. Theme. Terrain. Technology. Each of these elements will drive your valuation and determine whether or not you will get funded.

**Team**. Team is the most important aspect. The first section I go to in reviewing an opportunity is the biographies of the team. I would rather fund a B technology or market with an A team. Great teams win. It's not just the people – it's the team. The key is that the talent of the individuals combines to form a superb team. Always look to recruit really smart people that can contribute. Most of the teams we fund are deep on the technology side and thin on the business, sales and finance side. As long as the core team is strong you can continue to grow from there and attract further talent in other disciplines. The deeper and more experienced the team, the higher the valuation you can expect. A number of strategic investors have conveyed to me that they would buy early stage technology companies for $1 million per head. Ironically, one of our portfolio companies was so efficient that their headcount was low and their sales price was not truly indicative of their tremendous value. The CEO was an individual with a great deal of integrity, and she refused to hire "heads" just to increase her sales price. In the end, she sold the company quite successfully for approximately 10X the future 12 months of revenue – impressive, especially in the current market.

**Timing.** Probably the only thing worse than being too late to market is being too early. Timing is everything. Blumberg Capital helped launch Check Point Software in the US and Japan. One of the keys to its success was that the Internet was just penetrating the corporate market, and every CIO that wanted to go online was concerned about obtaining a simple, "shrink-wrapped" firewall solution to protect the enterprise.

**Theme.** Theme relates to the sector you are in. For example, my firm uses the moniker N.E.W.S., which represents Networking, Enterprise software, Wireless infrastructure and Security to describe our sector focus. Therefore, anyone sending us a business plan for a medical

device company will not likely make it very far in our process. Focus. Like an entrepreneur, the VC needs to remain focused in its areas of expertise. VCs meet regularly with CIOs in Global 2000 companies to understand where, how and why they are spending their IT budgets.

**Terrain.** Terrain relates to the size and growth of the market you are attacking. Most venture funds look for multi billion dollar markets that are growing annually at double-digit rates with low penetration. A total market opportunity of $200 million growing 5% annually is unlikely to attract venture capital, even though it might create a wonderful niche market for you to dominate. VCs are looking for very large untapped markets with low penetration and very high compounded annual growth rates. Finding these unique opportunities is challenging.

**Technology.** Technology really defines the potential barriers to entry. Have you filed any patents? How many man-years might it take for others to replicate what you have done? Technology relates to funding a paradigm shift and not just a mild improvement. When the first person found ice and used it to store food, a pick axe and shovel were great inventions to help break the ice. VCs would not be excited about investing in a pickaxe with a sharper head, but probably would be very excited by the first refrigerator, which allows significantly longer food storage. The refrigerator was a paradigm shift and at least an order of magnitude more efficient than prior methodologies. That is exciting.

## *V. The 4 E's*

Probably one of the most renowned CEOs of the last few decades is Jack Welch, retired CEO of General Electric. He likes to describe the crucial ingredients found in a successful manager with "the four E's of GE leadership"[12] – *Energy, Energize, Execute, Edge*. Then you

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[12] *Straight from the Gut*, Jack Welch, p. 158.

need to connect the four E's with one P – *Passion*. Top performers need high *energy*. It's the playoffs, and the true All Stars bring their game up another notch. Moreover, you need to somehow elevate the play of everyone on the team and this means the ability to *energize* others on your team to do the same. You will be faced with difficult choices and you need to possess the e*dge* to make difficult yes-and-no decisions (even if you will sometimes be wrong; some managers are simply incapable and suffer from "analysis paralysis") and the ability to *execute* and deliver on your projections. Being an entrepreneur is very demanding, and without the *passion* to create something from nothing, you will not thrive. Marc Andreeson, co-founder of Netscape Communications and one of the leading figures of the Internet boom summed it up: "What really counts in getting through a tough period like this is a sheer level of energy and willpower. You need a group of people who are willing to walk through brick walls."

*VI. The day after . . .*

Congratulations. You have closed on your investment from a venture capital firm and have cash in the bank and are feeling pretty darn good about yourself. Now what? First, celebrate with your team. There is nothing wrong with a little indulgence after all of the hard work you and the team have undoubtedly gone through over the last 6 months to reach this point. Your team should be rewarded and given the opportunity to celebrate, and it's important for you as CEO to set the proper tone and balance of "work hard, play hard". Moreover, this fosters and promotes an *esprit des corp* that will be essential in the coming months. This does not mean you should buy a Ferrari the next day, fly your team to Sun City, South Africa (with spouses or significant others) and sponsor a concert featuring the Rolling Stones in Pacific Bell Park. You get the point. Second – don't spend it too fast . . .

Think of the newly formed Board of Directors as an extension of your existing network. Try to balance your board with industry experts that can add value at the Board level and communicate with them frequently. Follow the advice of Robert Duvall in *The Godfather* who said: “I have to go to the airport. The Godfather is a man who likes to hear bad news immediately.” This means *no negative surprises*. VCs can wait to hear the good news, but need to hear the bad news right away. “Directors know relatively little apart from what management tells them,” said John Smale, former CEO of Procter & Gamble and onetime chairman of General Motors.

*VII. Conclusion*

Hopefully, you have an overview of the financing options your company has with an emphasis on venture capital. If you choose the VC route, make an effort to get an entrée through the right source and be brutally honest with your needs and aspirations as the CEO and in your overall presentation to investors. Avoid some of the common mistakes made by many while embarking on the venture process, and you will dramatically improve your odds of “getting to a meeting” and successfully completing the diligence process. Work with professionals to negotiate your term sheet and valuation, and remember to enjoy the honeymoon, because this is the first day of the rest of your life.

Try to have fun. Know how to laugh at yourself. Life is too short so don’t take yourself too seriously all the time. If you don’t love what you do it’s time to move on. Always make time to be with the ones you love. Never do anything that you would be ashamed to tell your mom. Everything in moderation. Set expectations. Give back when and where you can. Be

humble. As Golda Meir, former Prime Minister of Israel, once said to a visiting diplomat, "Don't be so humble. You are not so great."