High-Tech Advisor

Inside the Mind of a VC

Whither PNW Venture Capital? No Way!

There's an old saying I rather like: "Conventional wisdom is always conventional, and almost always wrong." So it seems when talking about early-stage venture capital in the Pacific Northwest. The conventional wisdom in the local press and among many pundits is that startup investing is dead. But it turns out that that "wisdom" is not only conventional, but very wrong, too!

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If you were to believe the nay-sayers, you would have no choice as an entrepreneur with a bold new business idea but to claw your way to millions of dollars in sales before VCs will deign to give you a passing glance. If you were to believe the nay-sayers, venture capital being raised and put to work today is at some historical nadir. And if you believed the nay-sayers, the Pacific Northwest is somehow devoid of any reasonable number of active, early-stage venture investors. Wrong, wrong, wrong!

At a macro level, people point to the dramatic fall in U.S. venture partnership fundraising as clear proof of the assertions above. What they don't seem to notice is that while inflows to VC funds have indeed plummeted from their peak in 1999 and 2000, today they are at levels we saw in about 1997. For those of us who were investing then, we can tell you that 1997 was a very good year! It was a good year to raise VC partnerships and a good year to raise money from VCs. However, it was not (yet) a year when all you had to do was put a ".com" on the tail end of your business plan to obtain $10 million in instant cash. People are still focused on the bubble time as some sort of "norm." Present times are much closer to the norm than those ever were.

Of course, we are still working through the aftermath of the bubble's burst, and some VCs who were thrown from their horses are having difficulty getting up the courage to get on and ride again. Obtaining venture capital is hard, as it should be. We see between 100 and 200 proposals for every deal we make. That is true now, was true during the bubble, and was true before the bubble. Remember, no one deserves venture capital––no founder, no company, no industry sector, no region, no state. Everyone has to earn it, just as all of us who manage venture partnerships have to earn our investors' support. Every time I hear someone talk about how much money a venture "deserves," the hair on my neck stands up. So here's some straight talk. Great deals get funded – period. In this world of open communications, smart money will find the terrific deals. Middle-of-the-road deals don't have nearly as much luck, nor should they.

Let's back up my assertions with concrete data and some anecdotal evidence at the micro level. Below is a table indicating the approximate "Free Cash To Invest In New Companies" available from the four largest Pacific Northwest venture funds. The simple-

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Fund	1997 Fund or before	1997 Free Cash	Pre-2003 Fund	Estimated 2003 Free Cash
OVP	1997 - $60M	$60M	2002 - $185M	$150M
Ignition	none	$0	2001 - $285M	$190M
Madrona	none	$0	1999 - $250M	$60M
Voyager	none	$0	2000 - $215M	$60M
Total Free Cash		$60M		$440M

(Note: there are many fine VC firms in the PNW – the four largest ones were used here for simplicity.)

minded calculation to arrive at this data was as follows: For each fund, we took their most recent pool of money and reduced it by 25 percent for each year (pro-rated for partial years) since that fund was closed. This admittedly rough approximation stems from the observation that most VC funds create their portfolios over the first four years of each new partnership and then support those companies with no new deals thereafter. It also explains why most VC firms raise a new fund about every four years!

The numbers above may be imprecise, but there is no question that the available venture capital in the Pacific Northwest dwarfs what was there in 1997 – and again, 1997 was a very good year! So much for that conventional wisdom!

Now for the anecdotal data: The other day I was asked by a friend knowledgeable in the industry and in our region if OVP "was doing startups anymore." My answer was both swift and puzzled: "Of course we are! That is all we've ever done. Why would you think otherwise?" His reply was telling: "I've heard that VCs are only doing deals now where the company has significant revenues."

Here are the facts: Every deal OVP has done in our new fund (three as I write this, with one more with term sheet in hand) has been pre-revenue. Some are business plan only, some have a prototype wiggling. That is the norm for us. In addition, of the four deals mentioned above, three are in the Pacific Northwest. Our investing rate is about one deal every quarter. Again, that is right in our sweet spot. But this isn't just about OVP. Of those three pre-revenue deals already closed, we did one with Ignition. There are two other very interesting Pacific Northwest deals where we did lots of work and finally chose to pass, but other funds have come to a different judgment and will go forward. In every case, those startups are also pre-revenue. Our Northwest venture colleagues are right in the same mode. And again, the pundits are flat wrong.

Entrepreneurs take heart. There is plenty of money locally and plenty of willingness to take the risk of putting it to work – and early, too. But if you don't get funded, don't try to pass the buck to us. Look hard at your idea, your team, and your market. The great deals are getting done. Be one, and you will, too.

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