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2009 Venture Technology Investment Outlook

Current Conditions Criteria and Advice

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January 2009. The world economic conditions have changed the investment and venture environment significantly.

Venture Investment

Venture investment during 2008 has not been so bleak since 1996:

During 2008, there were 682 IT-focused VC firms.

- 152 made 4 or more investments this year. The average capital under management of these firms is ~$1B.
- 163 did only 2-3 deals
- 367 did only 1 deal

Source: DowJones, VentureSource (thanks to Tim Chang at Norwest Venture Partners)

So: You can expect a significant number of the smaller venture firms to make no new investments in 2009, and some will be gone in the next two years. That said, VCs are in business to invest money, and will look to their new companies to support their return on investment, from the new investment itself and in synergy with their other portfolio companies.

Valuations and Exits

Beginning a year ago, the IPO market dried up. With no likelihood of IPOs, your valuations on acquisitions could lower to 33% to 50% of their earlier valuations.

Criteria for Venture Funding

Venture capitalists are re-calibrating their priorities on new and early-stage investments. They want:

- Innovation: not just in your products, but in your business model as well. Consider Netflix, which used old technology (the U.S. Post Office) to create a new model of distribution.
- Timing: Your company must be positioned to optimize market timing (that is, be ready to scale soon).
- Scalability: Your use of these funds must get you to profitability or market share.
- Proven growth market segments: For example, mobile, online gaming, and any product or service that clearly will save money for the Fortune 500 (i.e., that support NOT the top line but the bottom line).

New Competition for Funding

Venture firms that usually focus on early-stage ventures are now taking a broader view, and looking for the best deals not just at early stage but at later stage as well.

So: This means that early stage entrepreneurs are now competing against more players and against later-stage (less risky) players.

What to Do If You Are Looking for Venture Funding

1. Make certain you meet the criteria listed above. Having a unique product in an empty space, an experienced management team, and some defensibility of that product helps too.

2. Do your homework: VCs whose funds are still young will look at new investments; VCs with funds near their end-stage will reserve what funds they have to ensure the survival of their portfolio companies. Determine which VCs have Funds less than 12-18 months old. Don't just believe them when they say they are investing; verify this.

3. Do more homework: Make sure the VC you want to approach invests in your market segment and in your company's stage. Look for other companies in their portfolio where synergy with your company can enhance the portfolio company (and make sure that portfolio company is strong, not failing).

4. Work your network to obtain introductions for your company to venture firms. All VCs say that they best way to get a meeting is to be introduced by one of their colleagues or friends.

The current market demands that you cut back, get lean, and show that your company can use your existing and new capital wisely to reach profitability and/or market share. This, more than hockey-stick growth, is the focus of investors now.