An Investor's Checklist

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Investors have a rather straightforward wish list. The catch is-- they want the entire list filled at the beginning. And why not? Even the small firms read thousands of plans each year, and fund only a few. Larger firms see tens of thousands of plans each year, and fund only a few more. Yes, there is plenty of capital available, and a mad frenzy to invest it. But that doesn't mean it is easy to score the capital.

A Unique Idea in an Empty Space

Investors want a unique idea in an empty or near-empty space. It's OK to be second, if your competitor in first place has proven the market but not dominated it. Remember, in the Internet, there is only first and second place, nothing else. With all the new territory to explore, no investor needs to put his money on an also-ran in the making.

Scaleability

Once your unique idea has proven its empty space, it must be scaleable. Except for those tiny niche businesses grown in back bedrooms and sold for modest amounts, the rule of thumb holds that the business must scale to at least $100 million in valuation in three to five years' time. Yahoo and eBay are good examples of companies that could scale fast. We have already forgotten the names of those that couldn't. It will be interesting to see how many well-funded businesses actually achieve this $100 million goal in the coming years.

Defensibility

Sometimes overlooked by CEOs, but not investors, your business idea must be clearly defensible. "First to market" is often the defense put up against non-defensibility. It is an excuse. Yes, first to market gives a distinct advantage in an arena where there is only first and second place for players. But first to market does not make your idea defensible. You can be bumped off by copycats who do it better with more capital and brand. You become the pioneer with the arrows in your back.

One L.A. venture group passed on a start-up company with an in-depth site, good traffic, deeply experienced entrepreneurial management, and an impressive projected R.O.I, on a small initial investment — because the player in the number one position could create the same depth of the content already created by the startup, even though the number one's focus was elsewhere. Given the global exposure of the Internet and the low barriers to entry for new competitors, defensibility must be based on some proprietary technology, unique assets or licenses, or access to exclusive information, services or branding.

Management Team

Here's the catch-22: Investors tend not to fund companies that do not have a proven management team that can execute growth at the speed required to "flip" a company to a sale or to build the company to an IPO in the next few years. But without the capital, a company cannot attract the management team. It is critical to have the commitment of at least one executive with a proven track record in building an Internet business. Experience coupled with an entrepreneurial background is a big success with investors. Given the race to exit, there is no time for an executive's learning curve.

Investors will support a management team that has had Internet experience within a corporate structure, but no entrepreneurial background. If this is you, it is helpful to align your start-up with an Internet-experienced consultant specializing in start-ups to strengthen the team.

Enough Money to Get the Job Done

Investors like to see business plans that ask for enough money to create critical mass, then take first position, then accelerate the company's growth and defend its market position. So, make certain that you ask for enough money in your capital strategy to achieve your benchmarks for each tranche. It is best to declare your search for both the current and the subsequent tranche, to demonstrate that you understand the magnitude of money, particularly marketing money, required to take a significant position in this space.

The Adventure

There is no road map to capitalization in these uncharted territories. But sometimes the hand-drawn map will do. [d c r]

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