

# Venture Capital

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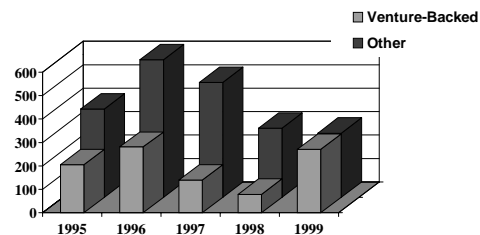
## Sources of Fund - Start-ups

- Personal savings (72%)
  - Pros: Total control of business
  - Cons: Limited resources
- Family members/friends (28%)
  - Pros: Lowest/no cost
  - Cons: May jeopardize relation
- Banks/financial institutes (45%)
  - Pros: Total control of business
  - Cons: Higher cost, harder for start-ups

## Sources of Fund - Start-ups

- Angel investors (10%)
  - Pros: More flexible
  - Cons: Harder to find, give up ownership/future income
- Government-guaranteed loans (7%)
  - Pros: Lower cost
  - Cons: Higher restriction, red tape
- Venture capitalist (1%)
  - Pros: More than \$\$\$
  - Cons: Industry-focused, Give up ownership/future income

## IPOs 1995 - 1999



## Questions?

How much do you know about Venture Capitalists?

What do Venture Capitalists look for in an investment?

## VC Investment by Industry

57% of total investment → Internet-related Companies ←

Of the \$ invested in:

- ① communications 50%
- ② software & information 70%
- ③ distribution & retailing 90%
- ④ business services 80%
- ⑤ consumer categories 72%

### How long is the VC process?

Under 30 days:	1%
30 ----- 60 days:	18%
90 ----- 120 days:	26%
More than 120 days:	10%
Average:	over 80 days

### What's the odds?

In 1998: 7 out of every 1000

In 1999: Lower than the above



### What info do VCs require on initial contact?

2 --- 3 page Executive Summary:	56%
10 --- 15 page "Mini" Business Plan:	22%
Full Business Plan:	14%
Information by telephone only:	7%
A cover letter describing the company:	1%

### What an executive summary must show?

In general:

- ① What the business intends to do;
- ② Who the management team is, and who it will be in five years;
- ③ What the company's capabilities are that enable it to achieve its business objectives.

It distills the essence of your business plan ----- Real Value !  
It hooks the prospective investors ----- Venture Capitalists !

### Worst mistakes in a business plan!

- Not clear in explaining the opportunity
- Unrealistic projections
- Underestimate competition and risks
- Overstate management strengths

### How do VCs value a business?

Quality of management:	4.5
Size of the market:	3.8
Product qualities:	3.7
Rate of market growth:	3.5
Competition:	3.5
Barriers to entry:	3.4
Stage of development of the company:	3.2
Industry the company is in:	3.0

### What questions do VCs ask?

- What type of business experience does the management team have?
- How does your company and product fit into the industry?
- Why will this business succeed?
- What advantages do you have over your competition?
- What is the current backlog?

[http://www.datamerge.com/financing\\_news/vcinquest.html](http://www.datamerge.com/financing_news/vcinquest.html)

### What kind of companies do VCs stay away from?



#### **“Money Trap” Companies**

Because .....

### Why do VCs reject your business proposal?

- Lack of an experienced, complete management team;
- Company does not fit their investment criteria;
- Market size and needs are too small;
- No competitive advantage & non-compelling technology;
- Strategic weaknesses.

### Tips to Improve Chances of Venture Financing

#### **I. Do's**

- Do define the business clearly
- Do identify target market clearly for the product or service, present marketing strategy that supports financial projection
- Do demonstrate a thorough understanding of the industry sector your products/service belongs
- Do outline management ability of the business
- Do outline proposed financial frame work for the deal

### Tips to Improve Chances of Venture Financing

#### **• II. Don'ts**

- Don't advance unrealistic market projections
- Don't ignore sources of risks and uncertainties
- Don't use biz plan that is the product of consultant's template plans unless you are fully conservant with the content

### What to prepare prior to meeting with VCs?

#### **I. Prospect target VC list**

- find VC geographically close to you
- make sure the VC specializes on the stage of deal
- check for VC's deal priorities

#### **II. Initial contacts**

- determine VC list's past records before contacts
- call/ send initial executive summary of biz plan

#### **Quality Business Plan**

- unique business concept or product
- management team qualification
- accurate, concise, realistic, not undercapitalized

### III. Initial interview

- honesty is the best policy
- all management team participate
- president lead, all key managers represent expertise

### IV. Due Diligence

- legal term: check things out or prudent investing
- VC questioning what the company is all about
- VC probing for tragic flaw & red flag on this investment decision

### Due diligence (..cont.)

- Process
  - several weeks/initial meeting
  - entire business team will present
  - tour facilities (high strength, uniqueness of investment)
  - quiz on business plan
- Old adage
- Be cautious on VC unique red flags and personal taboos

### VI. Negotiation

- Prepare objectives, attributes and strategies for negotiation
- Keep the negotiation and terms of the final agreement as straightforward as possible
- Fair representation
- Retain ownership of as much preferred stock as possible
- Include your own antidilution provision to preserve your share of equity
- deal-making lawyer is essential

### \* Major points to remember for negotiation

- It's only money
- Once the terms are agreed upon, keep your sense of humor, the deal will close
- Let the deal-making lawyer do his job
- Show up at the closing to collect check(unless it's wire)
- Turning the negotiation into a personal competition with the venture capitalist

### Negotiation Con..

- Forgetting that price is not everything
- Pitting the venture capitalists against each other
- Having your brother-in-law, the divorce lawyer, close the deal
- Shooting yourself in the foot at a final showdown

### VII. Closing

- Patience is the best
- Stay flexible--almost success

### Venture Capitalists in Hawaii

#### **HMS Hawaii Management Partners**

Davies Pacific Center,  
841 Bishop Street, Suite 860, Honolulu, HI 96813  
Contact person: **Bill Richardson**  
Tel no. (808) 545-3755; e-mail: bill@hms-hawaii.com

#### **Hawaii Venture Group, LLC**

1188 Bishop Street, Suite 1610, Honolulu, HI 96813  
Contact person: **Randy Havre and Sheila Chong**  
Tel no. (808) 533-1400; e-mail: hvg@aloha.net

#### **Pacific Venture Capital, Ltd.**

222 S Vineyard St., Suite PH1, Honolulu, HI 96813  
Contact person: **Frank Tokioka**  
Tel no. (808) 521-6502

### HMS Hawaii

- started in 1995
- area of specialization - telecommunications and information technology
- investment size - \$500,000 to \$2,000,000
- Hawaii and Asia
- exit strategy in 3-5 years
- return on investment: 5 to 10 times depending on holding period
- requires 2-3 page executive summary

### Hawaii Ventures Group

- started in 1998
- area of specialization - information and bio technology
- investment size - \$50,000 to \$500,000
- venture catalyst
- seed and start-up capital
- Hawaii
- fund syndication
- exit strategy in 3 years

### Pacific Venture Capital

- started in 1970
- caters to small businesses
- equity share couldn't be more than 50%
- area of specialization - communications and internet
- investment size - \$50,000 to \$200,000
- Hawaii and mainland
- exit strategy in 5 years
- latter stage investing preferred
- hurdle rate - 30 - 40% in the mainland; 20% in Hawaii
- executive summary and full-blown business plan should be ready

### Advantages of Local VC

- Accessibility
- Better understanding of the local market
- Network with other local businesses
- Commit more attention
- Less competition

### What do they want to see?

- Initially, 2-3 page executive summary of the business plan

#### Reasons for investing in your business

- strong management team
- compelling business idea
- barrier to entry
- huge market
- presence of exit strategies
- synergistic fit with existing business investments

#### Reasons for rejecting your business proposal

- weak management team
- no proprietary advantage
- incomplete financial plan
- limited market

### Value-Added Services

- assistance in the management
- provide expert advice
- strategic planning
- key personnel search
- business network

### Profile of Portfolio

<u>Industry</u>	<u>Sample Companies</u>
<ul style="list-style-type: none"><li>• software and technology</li><li>• internet and e-commerce</li><li>• telecommunications</li><li>• aquaculture</li><li>• biotechnology</li><li>• health innovation</li></ul>	<ul style="list-style-type: none"><li>• Digital Island</li><li>• Pixinet</li><li>• New Genesis</li><li>• Kona Bay</li><li>• Wireless</li><li>• Aloha Network</li></ul>

### VC Associations/Network

- **Hawaii Venture Capital Association**  
805 Kaimui Drive  
Kailua, HI 96734  
Tel. (808) 262-7329  
enture@htdc.org  
<http://www.htdc.org/~venture/>
- **Tignet**  
c/o City Bank, Inc.  
201 Merchant Street, 10th Floor  
Honolulu, HI 96813  
<http://www.tignet.org>

### Professional Firms

- **CPA Firms**
  - e.g. PriceWaterhouseCooper
    - Help refine biz plan and financial model (\$2K - \$3K)
    - Introduce to appropriate VC firm
    - Audit and tax service at reduced rate before IPO (\$15K - \$25K)
    - Audit for IPO (\$200K - \$350K)
    - On-line Resources (<http://www.pwcerc.com>)

### More online resources

- **Venture Capital Resource Library**
  - <http://www.vfinance.com>
- **The National Venture Capital Association**
  - <http://www.nvca.org>
- **FinanceHub.com**
  - <http://www.financehub.com>
- **Garage.com**
  - <http://www.garage.com>

### Overseas Resources

- **Asia Venture Capital Journal**
  - <http://www.asiaventure.com>
- **AsiaTech Ventures Ltd.**
  - <http://www.asiatechv.com>
- **European Private Equity and Venture Capital Association**
  - <http://www.evca.com>