

# It's not about the money!





there is an entrepreneurship gap

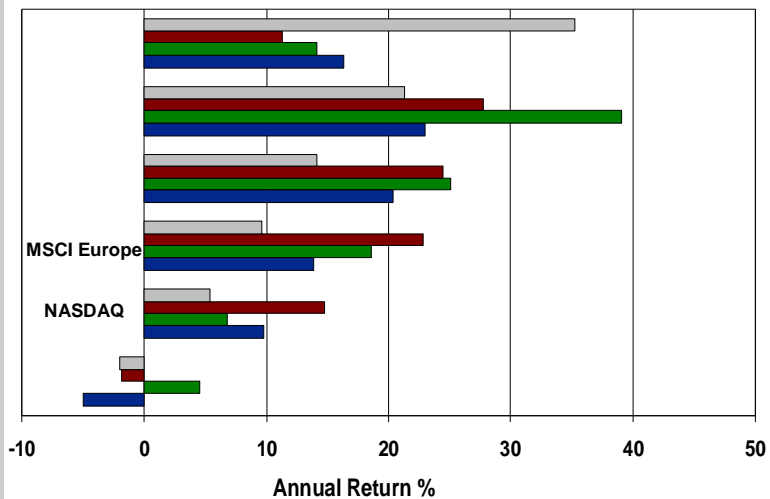
David Carratt

Kennet Partners

8 October 2008

## US & Europe VC Annual Return%

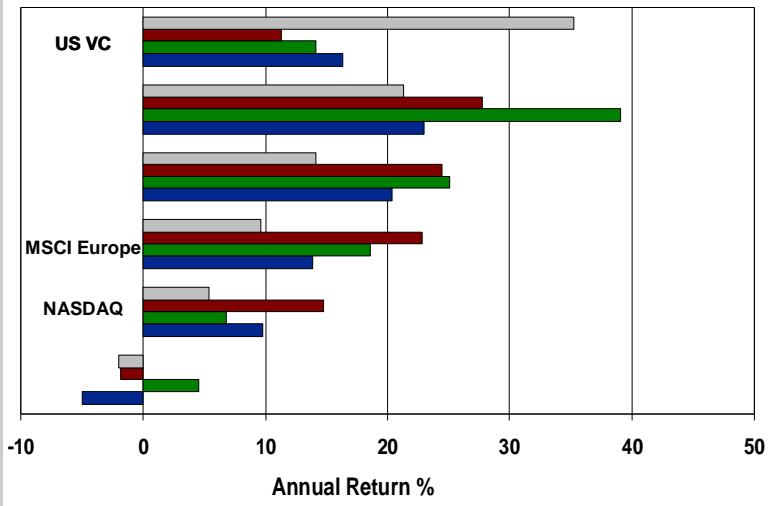
-  10 Year
-  5 Year
-  3 Year
-  1 Year



Source: Cambridge Associates Dec 2007

### US & Europe VC Annual Return%

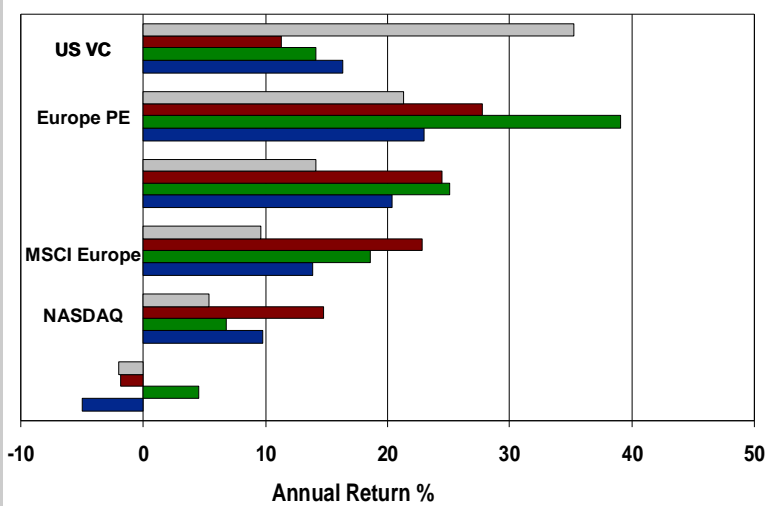
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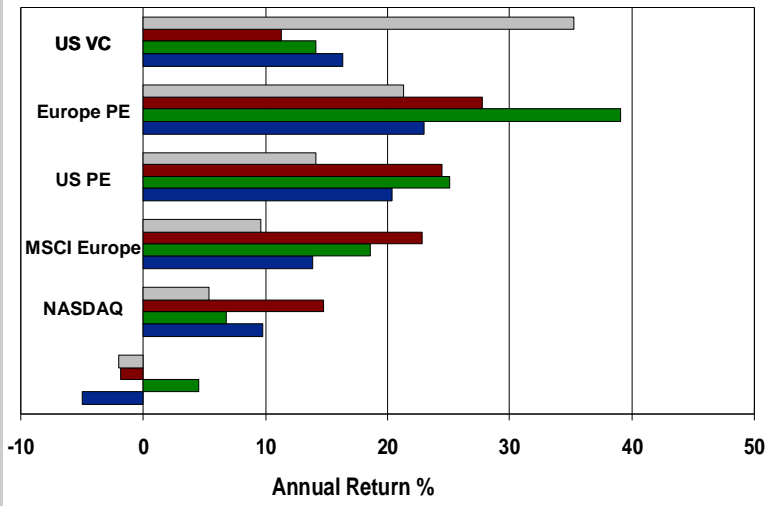
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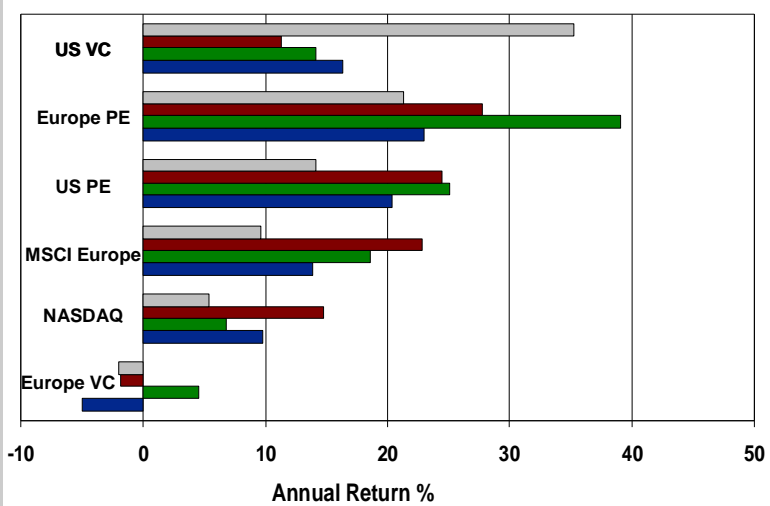
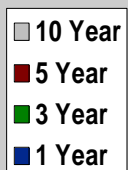
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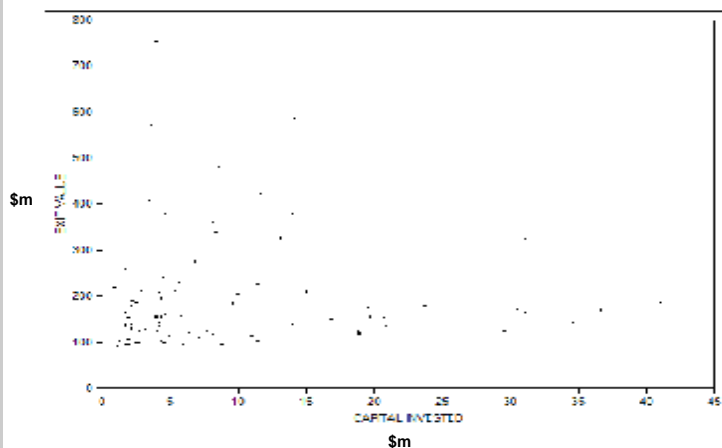
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## Only 82 European VC Exits > £45m since 2005

- n The upper echelon of European exits contained 82 exits with values of £45m
- n Capital invested in the companies with top exits ranged from £450k to £65m
- n These exits had value at exit ranging from £45m to £1,250m
- n What's the relationship between capital invested and the exit value?

## Zero Correlation between Capital Invested and Exit Value!

- n European VC exits – disclosed exit values



## European VC underperformance

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- n The “hits” came from only 82 investments and are unpredictable. You can’t guarantee by investing more capital you’ll get a “hit”.
- n Given the low overall return on European VC:
  - Either a few very large investments are being written off (unlikely, as European VC invest smaller amounts)
  - Or many small amounts of capital invested are failing to return (more likely, as European VCs invest small amounts)
- n Either investors are overpaying or future financial performance of companies is too low
- n Either of these mean that investing larger amounts will result in even lower returns

## Creating more winners

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- n 80% less capital is being invested in Europe than in the U.S.
- n 80% less capital is producing 25% of the total exits over £50m (for U.S. And Europe in total)
- n Europe is producing winners with less capital invested than the US
- n Need to channel more capital into business opportunities which can be winners and less into underperformers
- n On average, neither entrepreneurs nor VCs can tell the difference between a winning and an underperforming business opportunity!

## It's not about the money - what is it about?

- n Bootstrapping
  - Minimal use of capital to build company initially
- n Building board teams
  - Entrepreneur
  - Management
  - Serial entrepreneur
  - Investor
- n Marketing & Sales skills
  - Particularly selling the value of the business

## What Do All These Companies Have In Common?

**Microsoft**

**ORACLE®**

**SIEBEL.**

**CISCO SYSTEMS**  


**BROADCOM.**  


**DELL™**

**eBay™**

## They Were All Bootstrapped Startups

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Contrary to popular perception, many of today's market leaders built their initial business through "sweat equity"

- n Microsoft – Started as a contract software developer, raised money after the company was profitable
- n Oracle – Started as a software consulting business, development of initial relational database product was paid for by a government customer
- n Siebel – Substituted equity for employee pay for many founders, used customer revenues to help fund initial product
- n Cisco – Achieved \$5 million revenues, profitable prior to Sequoia's initial investment
- n Broadcom – Never raised capital from venture community
- n Dell – Did not raise outside capital until they achieved \$60 million in revenues
- n eBay – Achieved \$4.5 million revenue run rate and profitable before taking venture capital

## Board Teams

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- n Too many VC relationships are adversarial
- n VCs project an "entrepreneurs work for the investor" attitude
- n European entrepreneurs think they have complete experience
- n Most likely fewer than 200 VCs and entrepreneurs have been on the board of a European "hit" in the last three years
- n Less focus on "governance" more focus on quality business discussion

## Policy responses

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- n Encourage serial entrepreneurship
  - Serial entrepreneur participation in start-ups
  - Simplification of the EIS scheme
    - “connected party” rules alienate the serial entrepreneur
  - Institutionalise “business quality” goals
    - cap on CGT at £2m per exit event
    - R&D tax credit to include qualifying sales & marketing expenditure
  
- n Capital is mobile and will flock to successes!