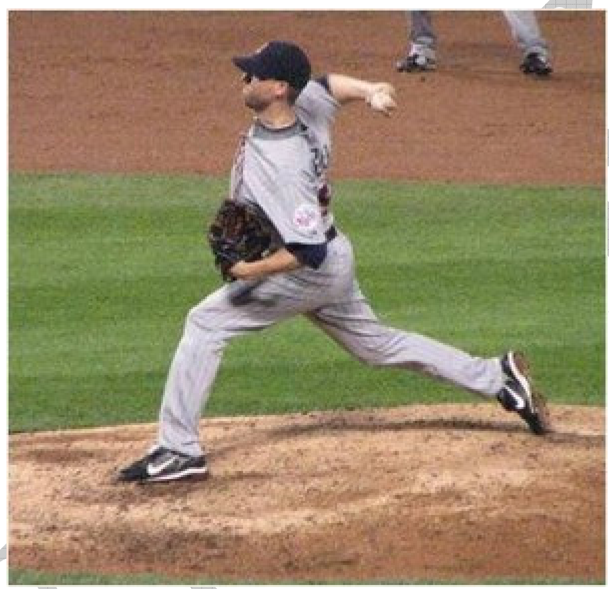
Management and Business Development Consultants
IMCA Registered Practice

Steps To Raising Venture Capital

Preparation Matters More Than Your Pitch

By
John Greathouse

1st June 2012



Disclaimer: The opinions expressed in this article are the personal thoughts of John Greathouse and may not reflect the views of his employer or their associates or those of WMJ Kelleher & Associates.

"One of the big misconceptions in baseball is that playing the game keeps you in shape to pitch. I wish that was true. It's not." Steven Ellis, Professional Pitcher

Major League baseball pitchers spend far more time preparing to pitch than they actually do pitching. The same should be true of an entrepreneur who is attempting to secure money from sophisticated investors.

The steps outlined below represent an ideal approach to raising capital from sophisticated investors. Unfortunately, your fundraising efforts will be less linear. You might be at Step 2 with one VC and Step 3 with another. However, the greater degree that you can sequentially follow these steps while keeping your discussions with each venture capitalist (VC) at relatively the same stage, the sooner you can spend less time in the company of investors and get back to running your business.

Prep Steps

Step 1: The Person, Not The Firm – As **Brad Feld** and Jason Mendelson make clear in their book ***Venture Deals***, entrepreneurs should identify specific venture partners, rather than target firms as a whole. Partners can differ greatly at the same firm, with respect to operational experiences, proclivities, temperament and capabilities.

One way to accelerate your research is to speak with other startup CEOs who recently closed fundraising rounds. They can provide insights into which firms are moving aggressively, which are nearly out of money, which partners are douches, etc.

Don Charlton, Founder and CEO of **The Resumator** (a **Rincon** portfolio company), recently took this approach. According to Don, "Even though we had high-profile clients such as Tumblr, Pintrest, Klout, Bit.ly, Mashable and Evernote, I knew that raising our B round was going to be time consuming. By comparing notes with a couple of other CEOs who were also raising money, I was able to short circuit a number of potentially dead-end meetings. VCs frequently collude, it's only fair that entrepreneurs compare notes every now and again as well."

Step 2: Get Personal & Give Freely – Once you identify a handful of potential VC partners, stealthily cyber stalk them. Follow them on Twitter and become familiar with their Facebook presence. Subscribe to their blog. Send them a private message via Twitter or other media that contains a compelling link relevant to their investment focus. Judiciously comment on articles they post to LinkedIn, retweet their tweets, vote up some of their Quora posts and establish a Google Alert on them and their firm.

Based on your research from Step 1, you should be able to communicate meaningful and insightful comments related to the partners' online presence. Even the most jaded VC cannot resist authentic flattery. The keyword here is *authentic*. Thoughtfully done in moderation, consistently over an extended period, these small, supportive gestures will not go unnoticed or unappreciated. Done excessively, you risk being labeled a clueless amateur.

Once you establish a modest level of the partner's cyber-attention, determine how you can help them. For instance, assuming your target VC has a portfolio of investments somewhat related to your business, it is likely that some of your partners, vendors and other stakeholders will be applicable to a subset of the investor's portfolio. If this is the case, offer to make a meaningful introduction to a potential customer or partner of one of their portfolio companies. If the investor connects you with one of his portfolio CEOs, it will facilitate completion of Step 3.

Step 3: Meaningful Referral

Fundraising books often instruct entrepreneurs to seek referrals to a VC from accountants and lawyers. While these referrals are not completely worthless, they are far from ideal. Professional service providers are incentivized to foster your business, as a portion of the funds you raise will go toward payment of their invoices.

The most impactful referrals are from: (i) people who's entrepreneurial judgment the VC respects, and (ii) people who have nothing to gain from your success. In particular, references from senior executives at the investor's portfolio companies are especially effective.

Obtaining an introduction from one of the investors' trusted entrepreneurs requires careful planning and patience. If you were unable to motivate a particular target VC to make introductions to their portfolio executives (as suggested in Step 2), directly initiate such discussions. An effective icebreaker is to tell the executive you are considering seeking money from one of his investors and you would like to discuss the entrepreneur's first-hand experiences with the investor.

Prior to the discussion, research the portfolio company and determine how your respective companies could potentially partner. For instance, you might propose a lead sharing relationship in which both companies trade customer introductions. If you cultivate a sufficiently healthy relationship with the portfolio executive, they will readily make a warm introduction/recommendation to your target investor.

If you performed Step 2 appropriately, your introduction will not arrive in a vacuum. The VC will recognize you as a productive and additive member of the online startup community.

Step 4: Reconnaissance Mission, Under Promise– An effective technique for acquiring investment capital is to initially *not* ask for money. As the saying goes, "Investors want to give you an umbrella when the sun is shining and then they take it away at the first hint of a coming storm." Thus, tell your targeted VCs that you want to preview your venture and seek their advice. It is ingratiating to be asked to share your insights and most VCs *immensely* enjoy sharing their opinions.

The goals of a preview meeting are to: (i) alert the VC as to the nature of your venture and your near-term milestones, (ii) obtain some free consulting, and, most importantly, (iii) pique the VC's curiosity so they will be receptive to your Step 5 updates.

During such meetings, emphasize your near-term and intermediate milestones. Under-promise regarding such accomplishments and discuss only those that you know you can deliver. For instance, if you think you will close ten paying customers in the next month, tell the VC that you plan on signing-up a few paying customers during the next three months. Yes, I am advising you to sandbag your prospective investors.

Just as it is hard for a public company to regain the trust of Wall Street when it fails to achieve its forecast, it is difficult for an entrepreneur to recapture a VC's attention if she does not meet her self-defined expectations.

Note: If you are unable to self-fund your venture or you have no alternative funding sources, this step is not appropriate. In such cases, you do not have time to be coy. Ask for money in your initial meeting with a VC.

Step 5 – Gain Traction, Follow-up – This step is iterative. As you accomplish your milestones, send your target VCs a brief email update (think eye-candy graphics and charts, not dense text). These updates will foster trust by demonstrating your ability to execute your stated objectives. Such follow-up are akin to a train whistle. Each note alerts the investors that your venture is gaining momentum and creating value and they better jump aboard before the train leaves the station.

Meaningful traction is third-party proof of your value proposition, the ultimate form of which is customer dollars. If your venture is not mature enough to generate customer revenue, achieve precursors to revenue, such as: partnerships, distribution agreements and OEM relationships. If you are deploying a freemium business model, test your upsell strategy on a portion of your users to establish concrete free-to-paid conversion metrics.

Step 6: Full Court Press – Once you identify an appropriate cadre of appropriate investors, gain their attention online, obtain a referral from a trusted source and then exceed the expectations you set, obtaining adequate capital will be relatively easy.

In ***Influence: The Psychology of Persuasion***, author Robert Cialdini discusses how an enterprising college student paid his way through school by buying and selling used cars. His secret was to invite multiple buyers to view the car at approximately the same time. The dynamic of a competitive atmosphere allowed him to sell his cars at their list price while increasing the velocity of the sales process.

To this end, simultaneously coordinate your discussions with multiple VCs. Your goal is to have several firms at the decision point at the same time. One way to do this is to drive your prospective investors to make a decision by a prescribed deadline. However, realize that the diligence process differs among firms. It is nearly impossible to rush a venture investor, as their biggest risk is making a bad investment, rather than potentially missing a good one.

Your objective is not to create a bidding war, as the funding round valuation is only one variable you are trying to optimize. The primary benefit of obtaining multiple Term Sheets is that it will accelerate the fundraising process and allow you to return to what you should have been doing instead of executing these steps: running your business.

No one wants to dance with the person leaning against the wall – everyone wants to be with the popular person who is cutting it up in the middle of the dance floor. Get dancing and surround yourself with a cheering crowd of VCs.

Even though you are engaged in discussions with a variety of VCs, be circumspect when asked to identify your current fundraising status; do not name names. By holding back specific information, you will temper the VCs' ability to collude against you.

If possible, make sure you have an alternative to a funding eent, such as growing organically, even if this involves slowing down your planned growth rate. If an unscrupulous VC smells blood, you are screwed. They will delay the funding until you are desperate and willing to accept an onerous valuation. Whenever you seek funding from VCs, be sure you also line up alternative sources of capital, such as government grants, angel investors, venture debt or friends, family and fools.

Stay Limber

Just like a professional baseball pitcher, your actions before and after you pitch an investor are more important than your actual pitch. If you follow the above six steps, you are not guaranteed to close an advantageous funding round. However, the discipline associated with these steps will help you focus your efforts, thereby reducing the overall amount of time you must allot to the fundraising process.

You can follow John on Twitter: **@johngreathouse**. He promises he will never Tweet about sunsets, unicorns or that killer burrito he just ate.