



MORGENTHALER

Necessary But Not Sufficient: What Works in Venture Capital

Greg Blonder

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■ Success Factors

- Company (Two)
- Market (Two)
- VCs and the Board (Three)

And how these relate to
East Coast Investing

■ # 1 - Outstanding CEO

- In 38 years of MV experience, ALL our big successes were led by outstanding CEOs
- Adequate CEOs led to adequate exits
- Apparently great CEOs also fail

**SINGLE MOST IMPORTANT SUCCESS
FACTOR**

Recycle this scarce resource

■ #2- Match the Method to the Market

- Low burn, organic growth in slow markets
- Higher burn, leveraged growth in fast
 - Make vs buy
 - Feature vs product
 - Engineer vs marketeer

Slow death for inattentive company

■ #3 - Goldilocks Timing (microeconomic)

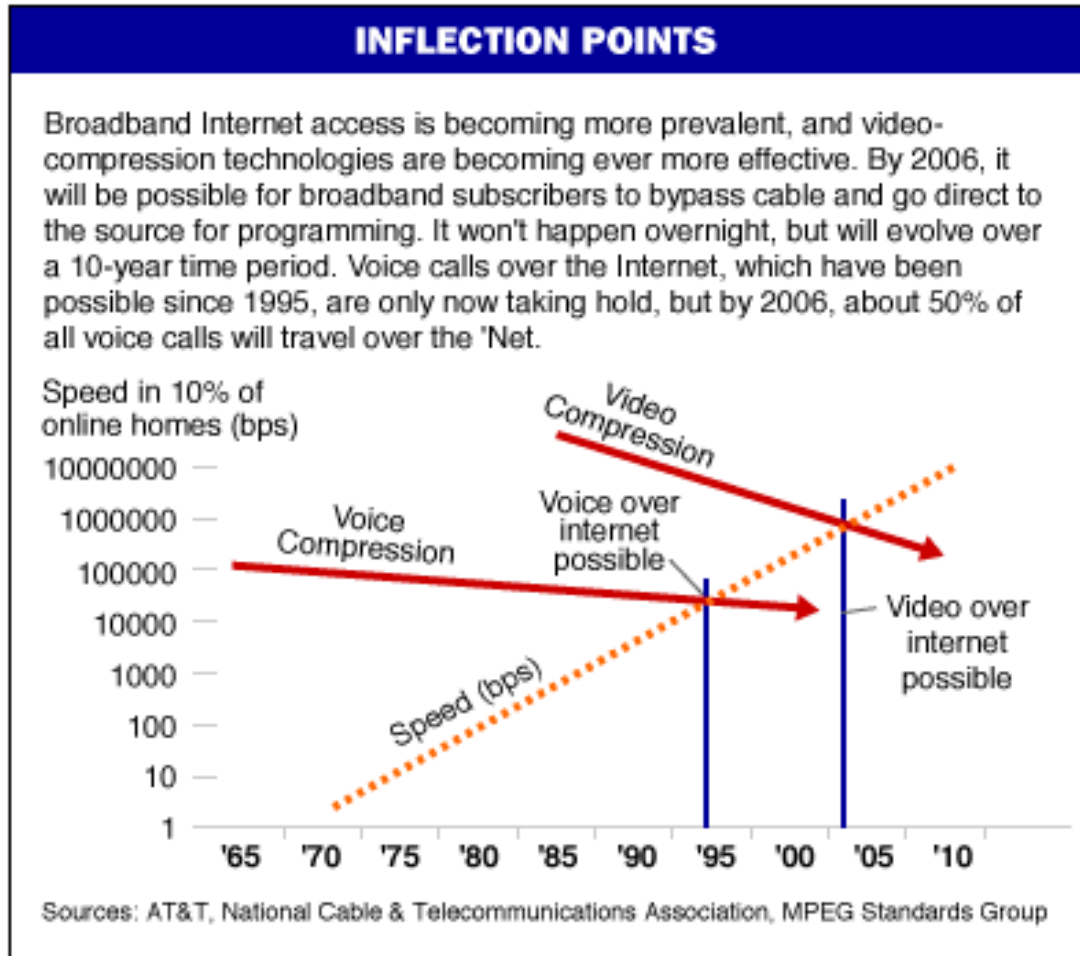
- Too early is indistinguishable from too late
 - Google vs AV
- As hard to get right as to time the stock market

Experience, luck and fast-following key

■ # 4 - Leverage Sector Rotation (macro)

- Hard to lose money on
 - LANs in early '80s
 - Internet anything in late 90's
- Unlike market timing, CAN be predicted
 - Scenario planning

■ Vonage, YouTube, ...



Sometimes you
can make your
own luck

Roll-ups next
opportunity

Predicted in 1993 using Scenario Planning

■ #5 - Optimize the Exit

- “Companies are bought, not sold”
- “Price is perception”
 - Buzz
 - Dinners
 - Rolodex

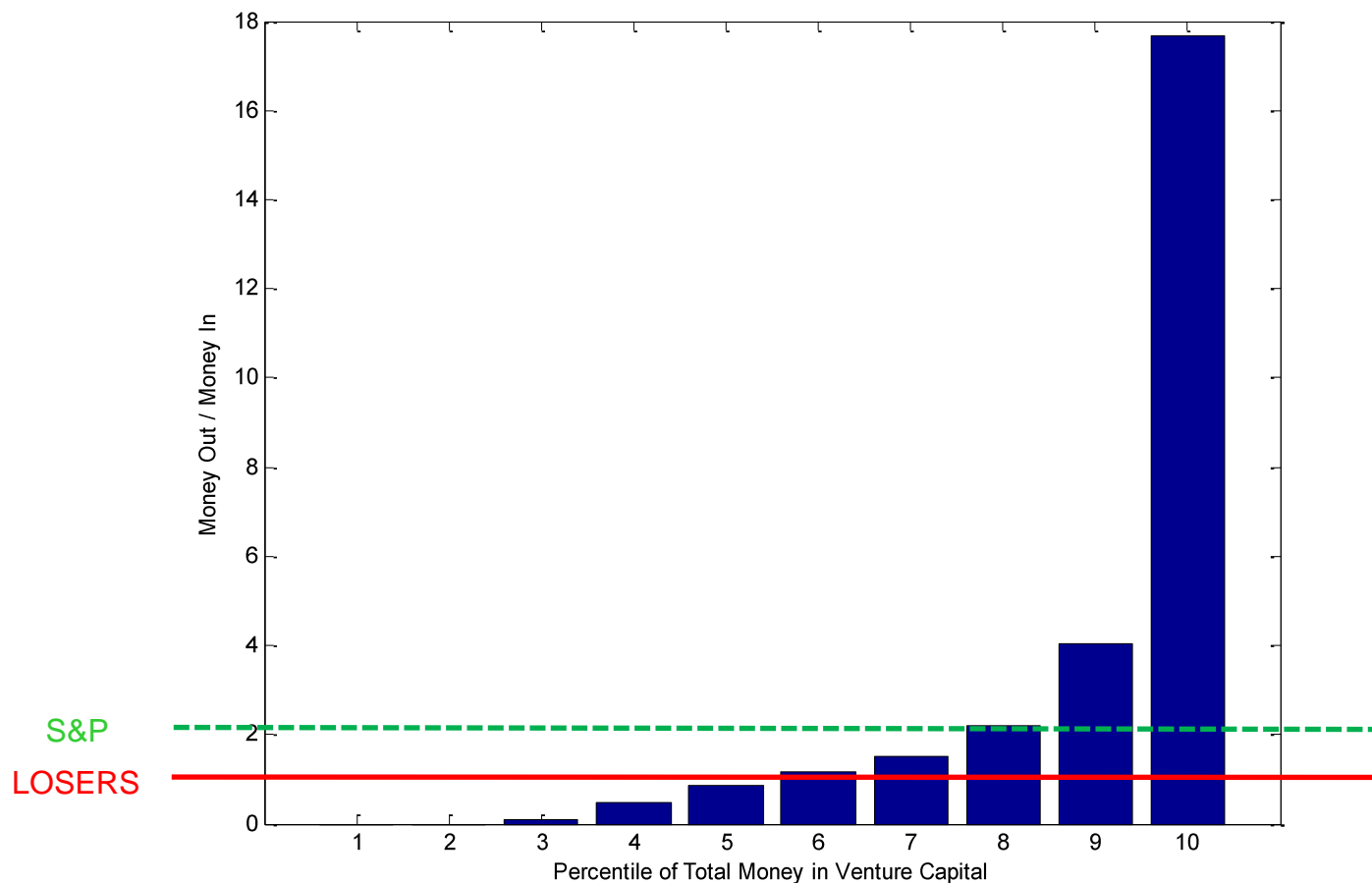
2x to 10 x difference in outcome

■ #6- Scope matters

The **MEDIAN** VC investment **LOSES**
money (depending on the vintage year)

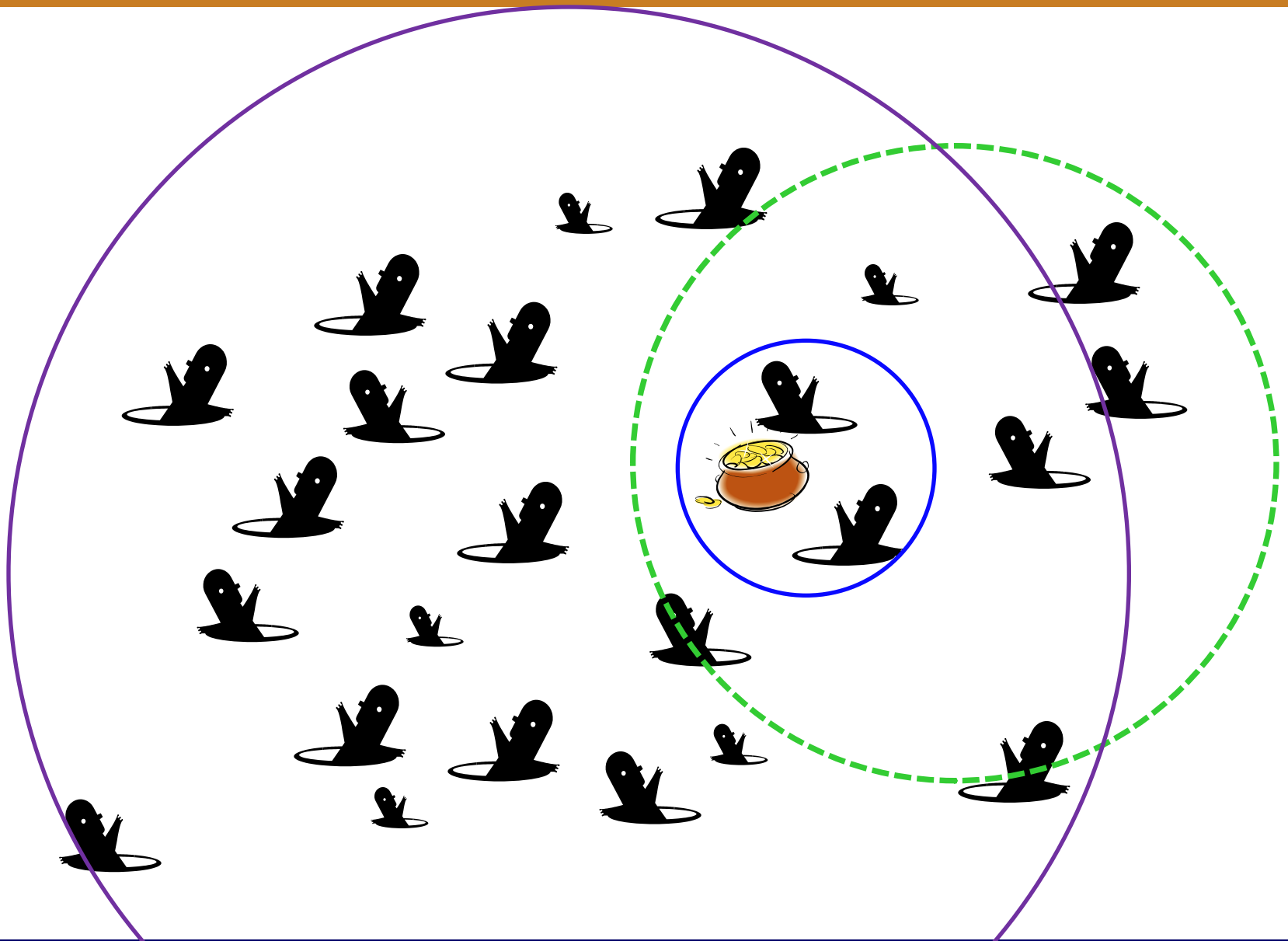
The **AVERAGE** beats the Stock
market.

Highly skewed returns



Data courtesy of Susan Woodward, Sand Hill Econometrics. Please do not reproduce without their permission.

■ Too few or too many...



- Only 2-4 investors/ company- NOT like the public market
- Dramatically increasing returns if you have access to the 10x winners
 - Previous gorilla winners
 - Firm brand and visibility
 - Deal flow network

■ #7 - Location, location, location

- Life Sciences is scattered around the country
- IT Hardware predominately in Silicon Valley
- IT Services “ “
- Semiconductor increasingly “ “

50% in CA, 25% in NE

- But East coast should have led in
 - Financial Services
 - Pharmaceutical
 - Advertising Services

■ #7 - Location, location, location

• East Coast

- Nascent entrepreneurial culture

- Pharma spinouts few and far between

- Financial services

- Incumbents too profitable and powerful and innovative

- Advertising

- A recent, growing area for VC backed firms

• Challenging

- Great CEO

- Fast following

- Buzz

■ Net net

- VC is a small, idiosyncratic endeavor
- Not quite an asset class
- But some best practices tip the odds in favor of outperforming the market significantly...