

Informal Investors, Angels and Venture Capitalists: A Worldwide View



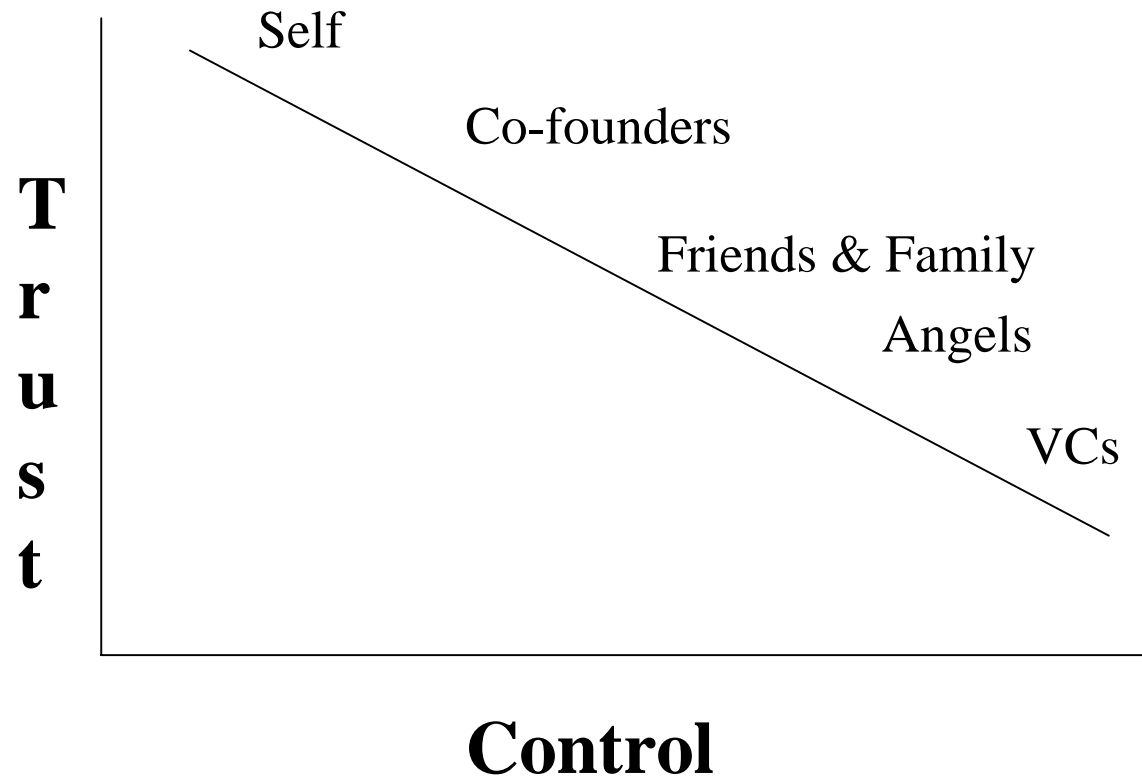
Andrew "Zach" Zacharakis

The John H. Muller, Jr. Chair in Entrepreneurship

Arthur M. Blank Center for Entrepreneurship

Babson College, USA

Equity Funding Food Chain



Shepherd, D.A., & Zacharakis, A.L. (2001)

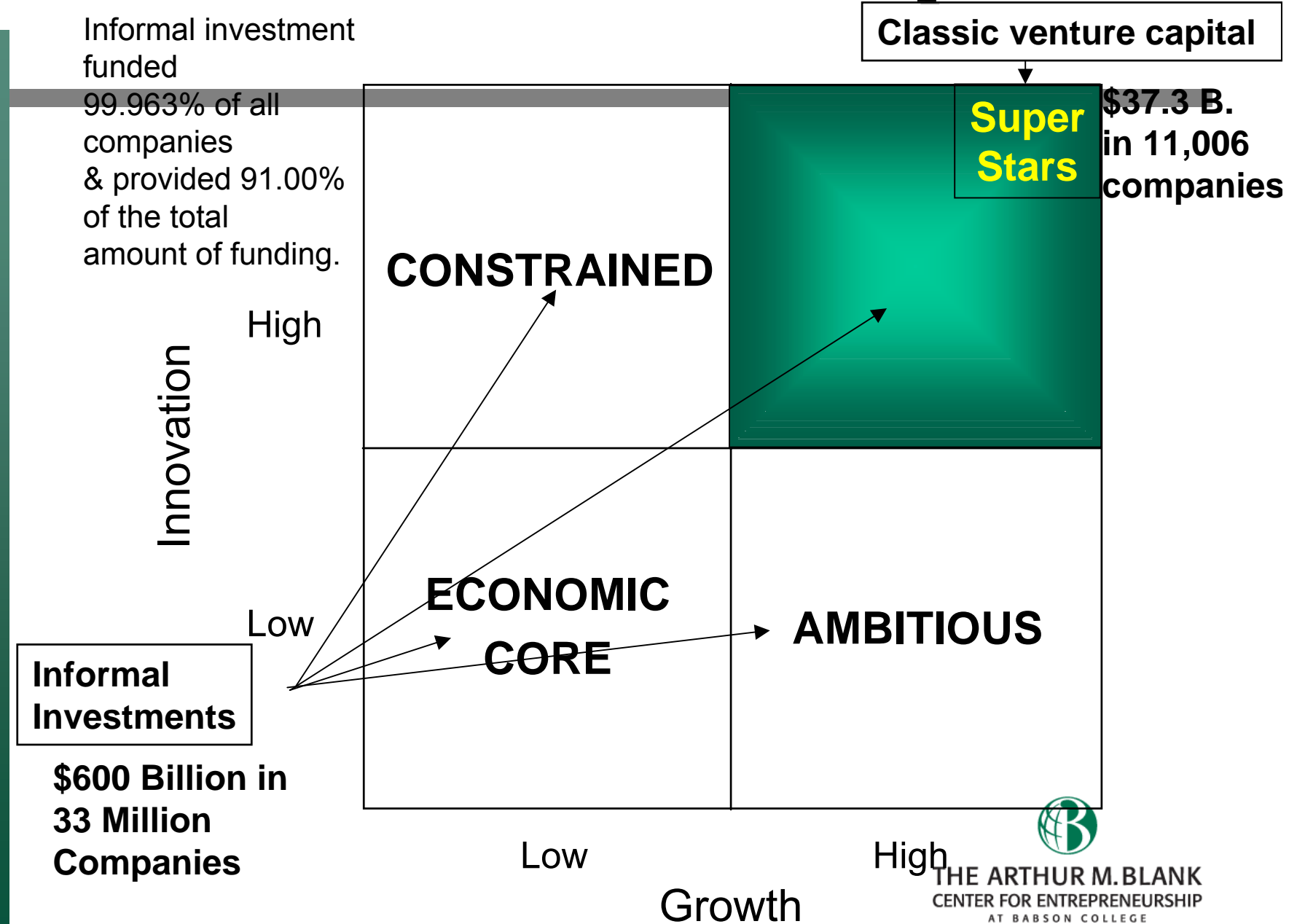
Bygrave and Zacharakis ©



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

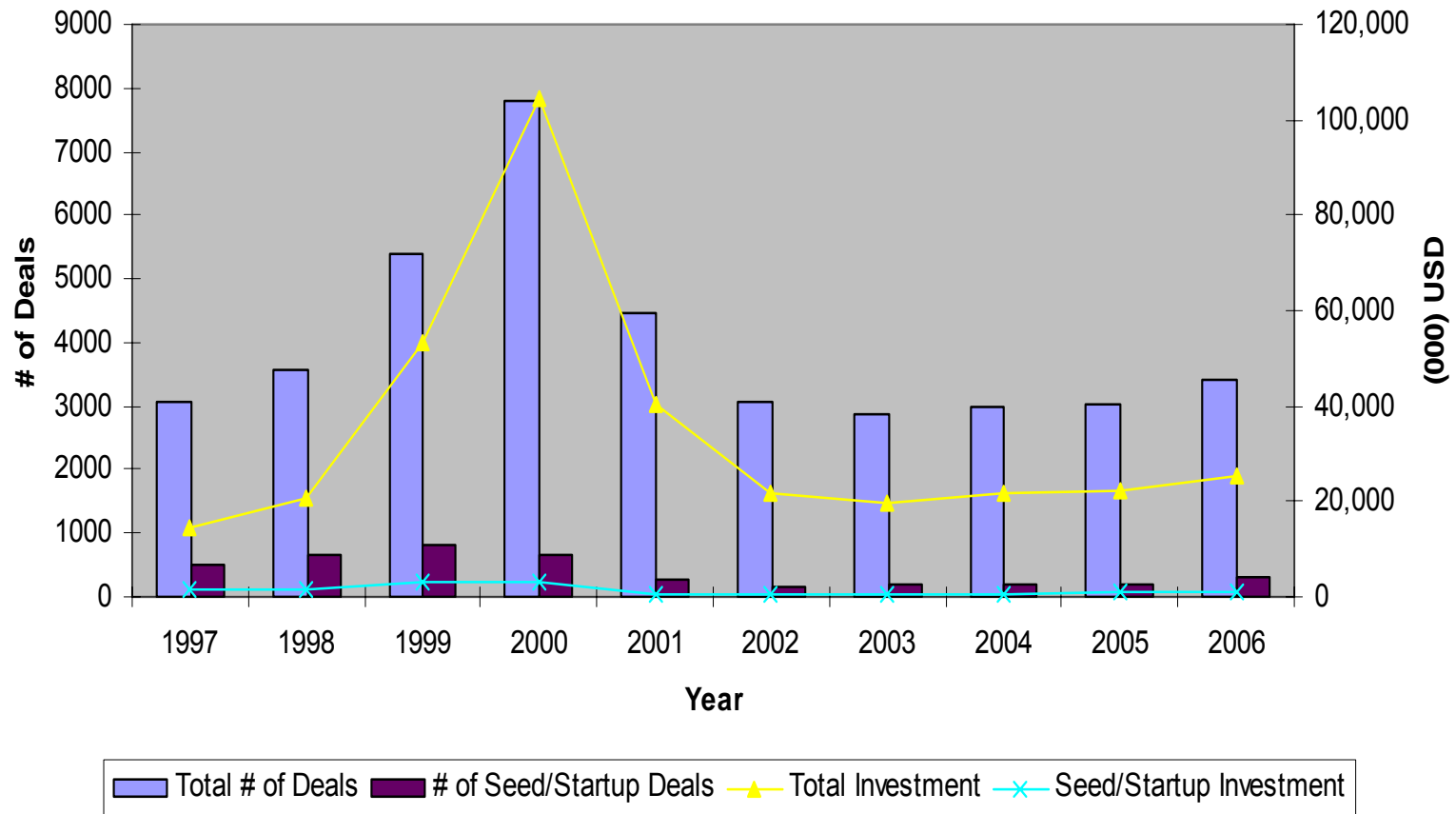


Classification of Companies



Why not Venture Capital

It's not Seed/Startup Capital



THE ARTHUR M. BLANK
 CENTER FOR ENTREPRENEURSHIP
 AT BABSON COLLEGE

Source: VentureXpert

Self-Funding by U.S. Entrepreneurs



- Entrepreneurs themselves provide 67.9% of the capital for their new ventures.
- Total capital needed to start a new venture is \$62,594.
- Entrepreneurs provide \$42,501.
- External informal investors provide \$20,093.



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Expected versus Actual Sources of Capital

Entrepreneur's Expected Sources of Financing (All GEM Nations)	
Sources of Funding	Percent of Entrepreneurs
Close Family	32.9%
Other Relative	14.5%
Work Colleague	14.7%
Friend or Neighbor	15.3%
Stranger	7.3%
Bank or Other Financial Institutions	42.2%
Government Programs	19.7%
Other	12.3%

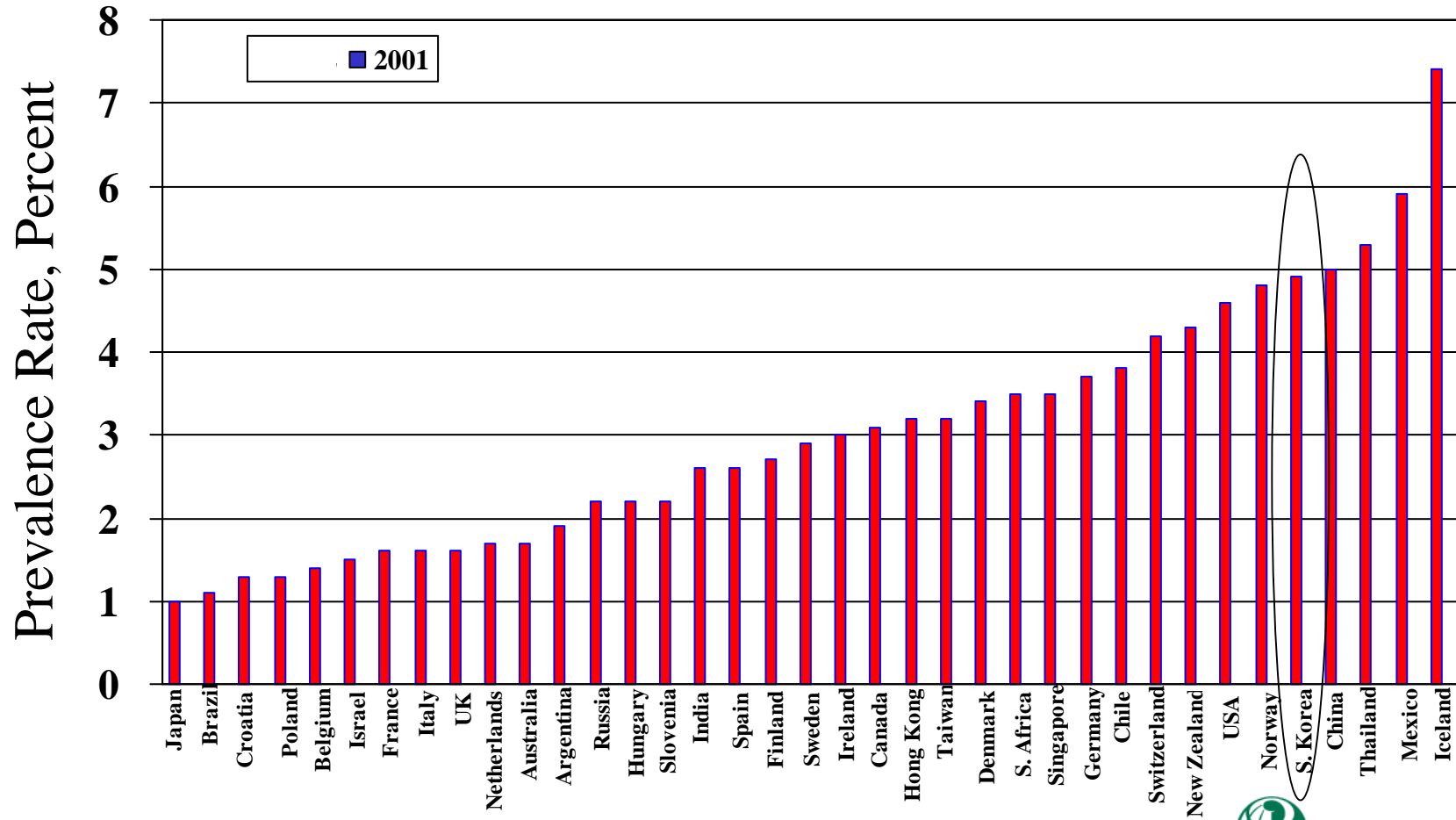
Total is more than 100% as entrepreneurs cited multiple sources.

Relationship of Informal Investor to Entrepreneur (All GEM Nations)	
Sources of Funding	Percent Total
Close Family	48.9%
Other Relative	8.4%
Work Colleague	7.7%
Friend or Neighbor	26.4%
Stranger	5.8%
Other	2.7%
Total	100.0%

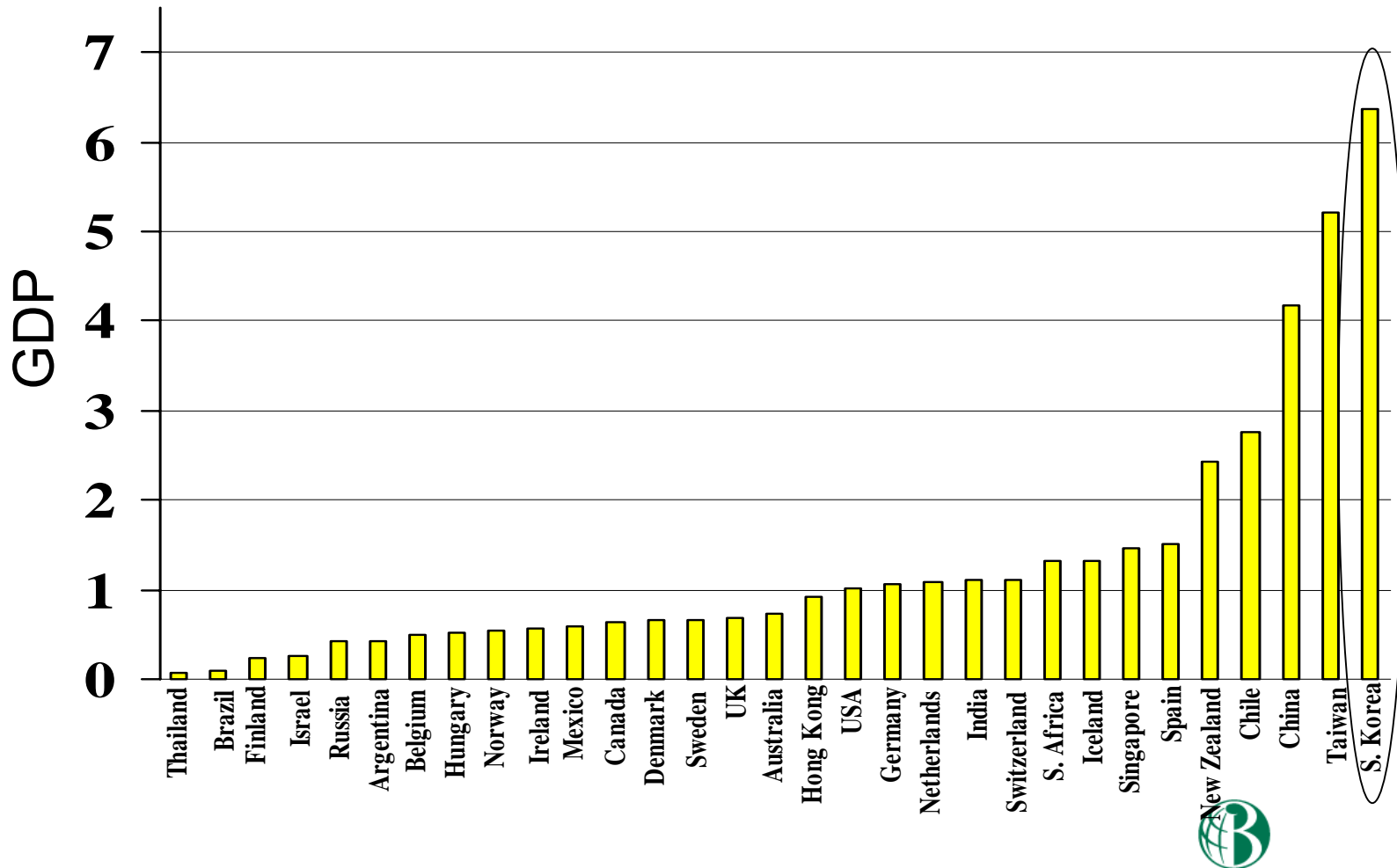


THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Informal Investor Prevalence Rate



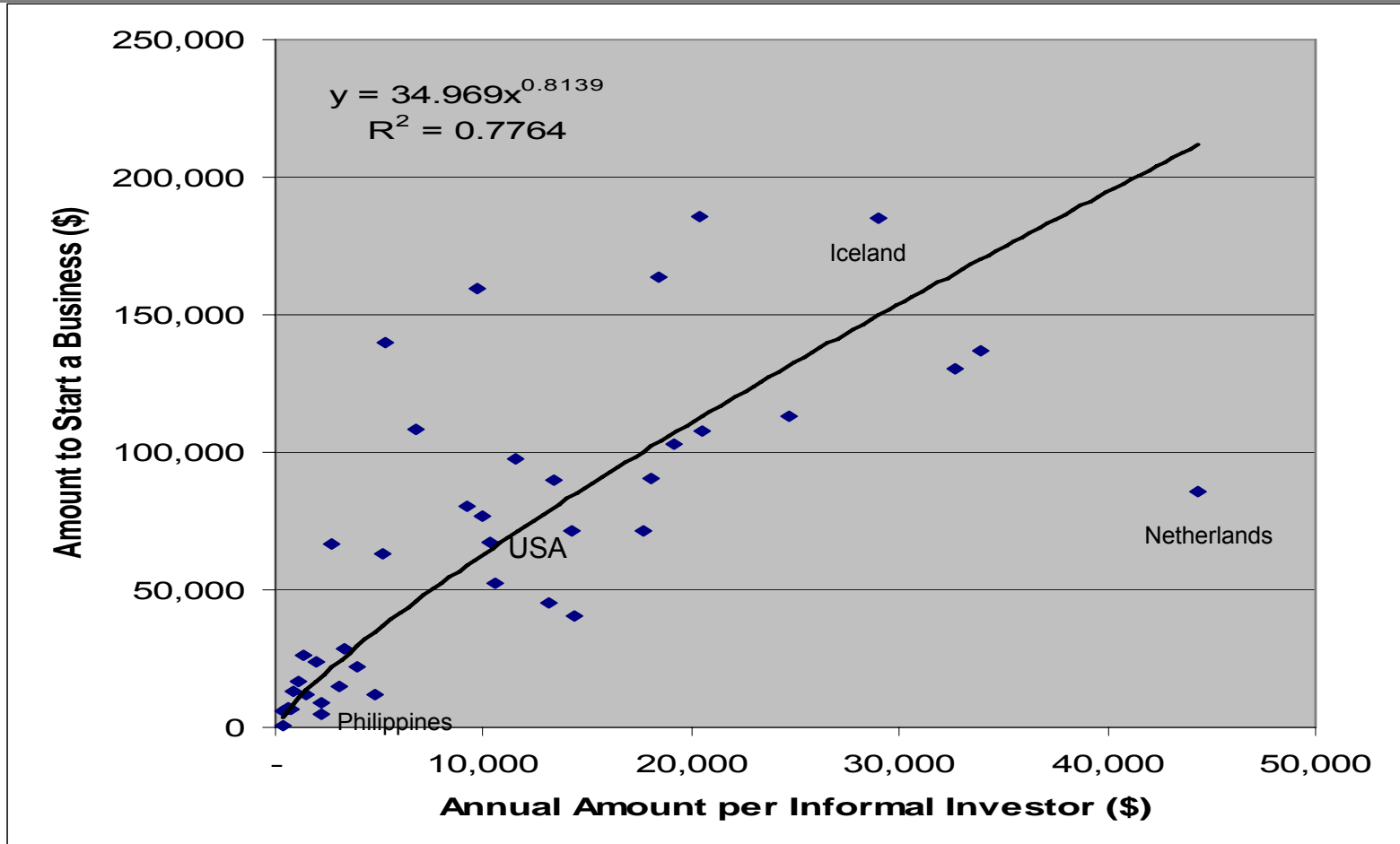
Informal investment as percent of GDP



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

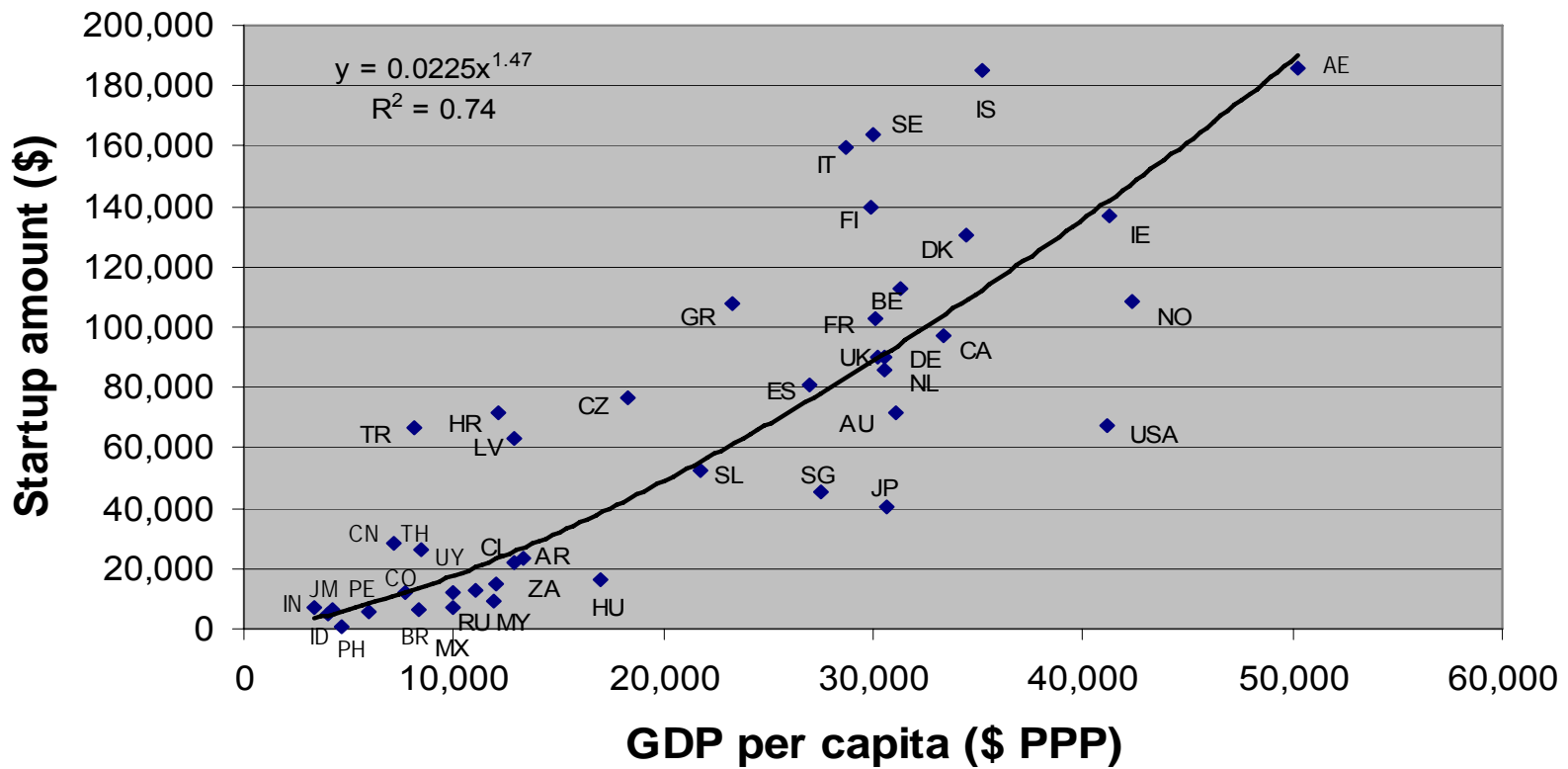
Classic venture capital comprises investments in seed, early, startup, and expansion stage companies.
Bygrave and Zacharakis ©

Startup Amount vs Annual Amount per Informal Investor

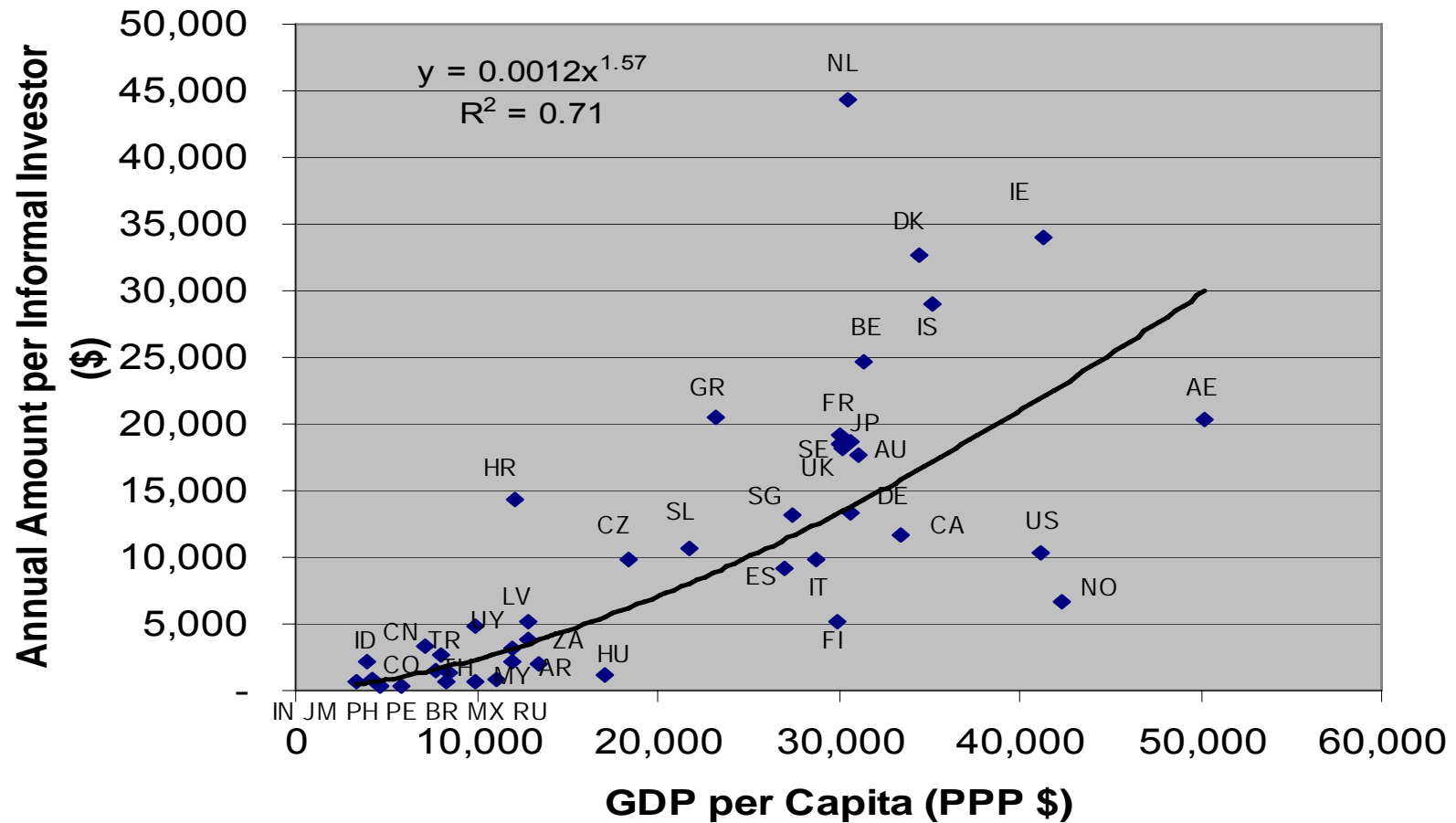


THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

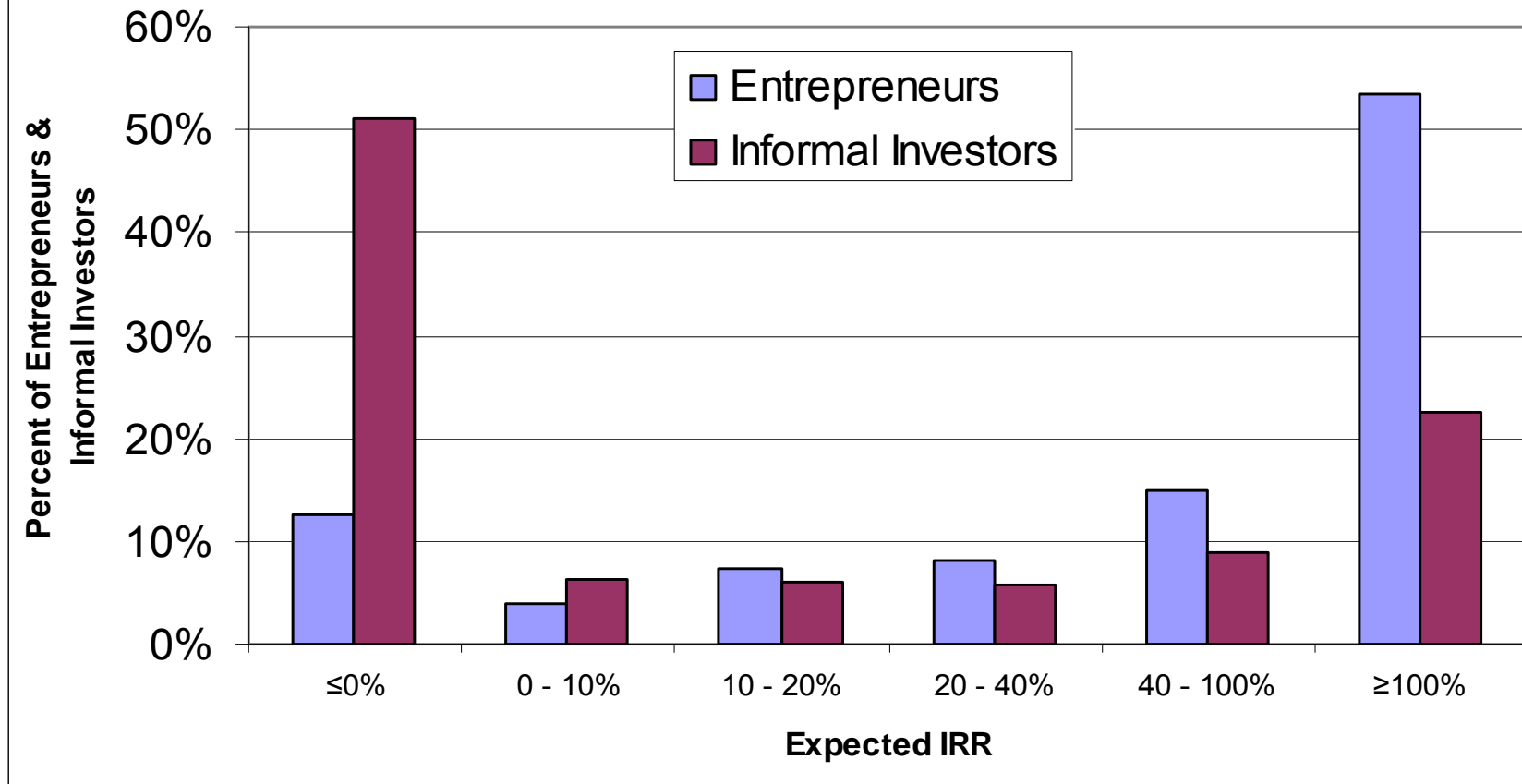
Amount of Startup Money vs GDP



Annual Amount per Informal Investor vs GDP



Expected IRR for Entrepreneurs & Informal Investors



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Maximum Return

Stage	Expected Annual ROR%	Holding Period
Seed and Start-up	50-100+	~10+years
1st Stage	40-60	5-10
2nd Stage	30-40	4-7
Expansion and Bridge	20-30	3-5
LBOs	30-50	3-5
Turnarounds	50+	3-5



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Driving Forces Impacting VC

- **Worldwide Savings Glut***
 - \$11 trillion worldwide in 2005
 - Chinese savings increasing and spreading worldwide
 - Corporations not distributing excess cash
 - Housing bubbles in Spain, US and elsewhere
- **VC Driving Forces**
 - Larger Funds
 - More Funds
 - Move to International Markets
 - Follower/Herd Mentality

• Too Much Money; A global savings glut is good for growth -- but risks are mounting.
Rich Miller, Jack Ewing, Stanley Reed, Laura Cohn, Frederik Balfour and David Henry.
Business Week 3942 (July 11, 2005): p58.



Key Questions

- **How is worldwide glut impacting VC today and into the future?**
- **Where is VC money going?**
 - **Geographic**
 - **Stage**
 - **Industry**
- **Where should it go?**
- **What pressures are building?**
 - **Too much money chasing too few deals**
 - **Valuations heating back up**



Venture Capital Across The World

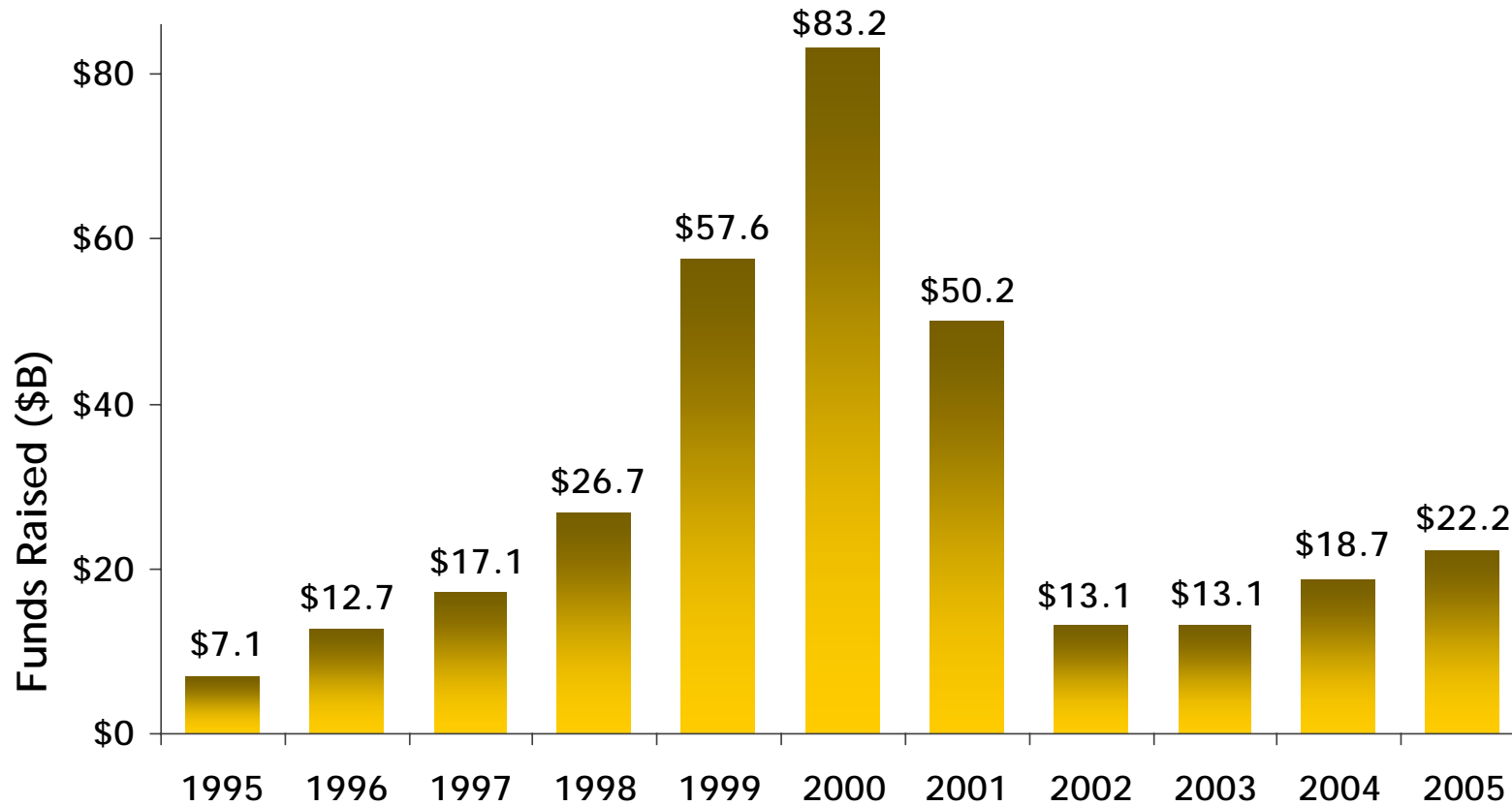
- **\$53.8B worldwide in 2006**
 - **\$41B in US**
 - **\$8.3B in Europe**
 - **\$2.8B in Asia**

Source: VentureXpert.



Fundraising is Picking Back Up

Commitments to Venture Capital Funds



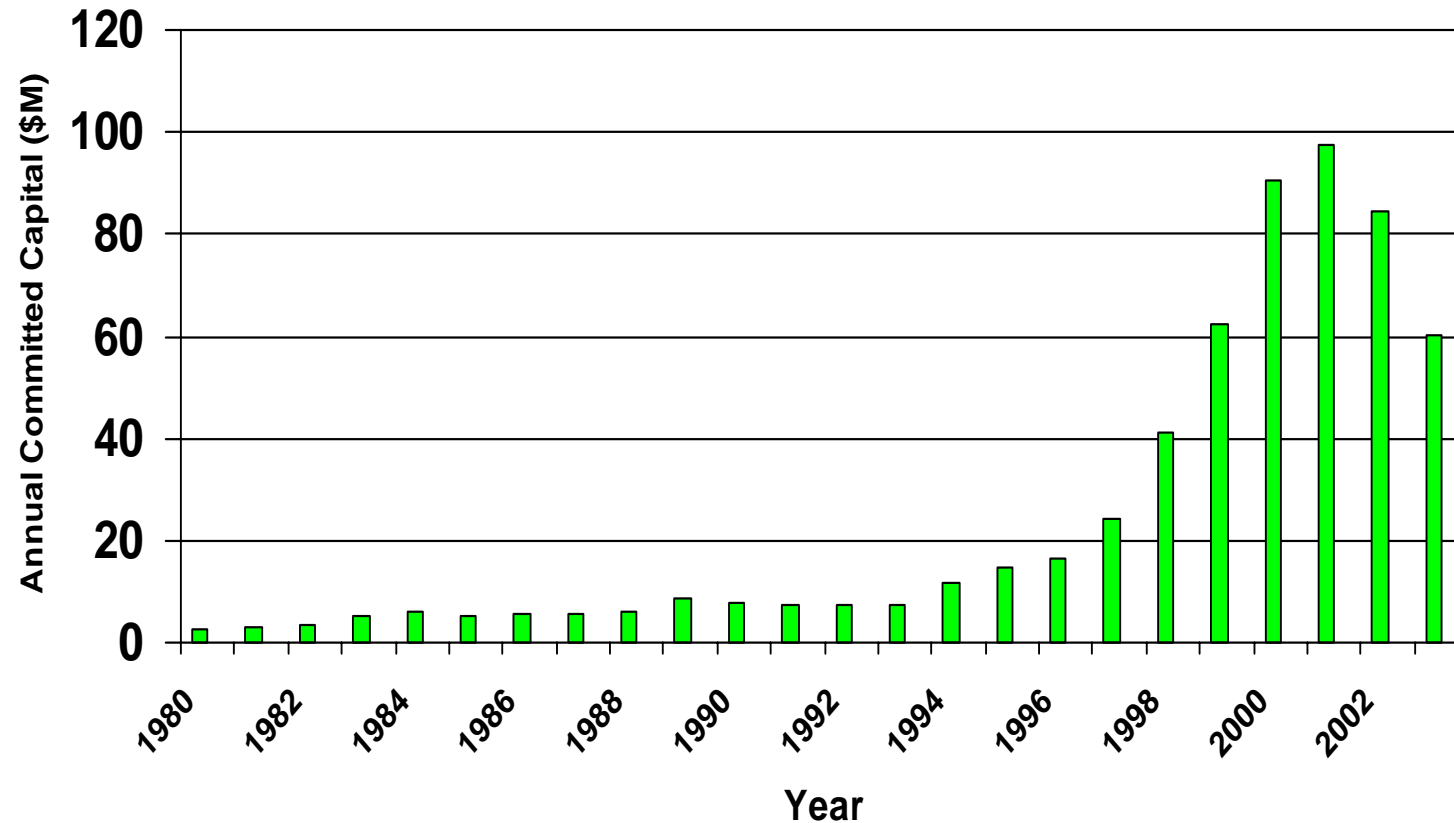
Source: Dow Jones: Venture Source.

Bygrave and Zacharakis ©



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Although Overhang is Stabilizing



Reyes, J. (2004) **Private Equity Performance 2004: The Coming Shakeout.**



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Industry Dynamics

	1997	2003	2005
No of Firms/Funds	515/885	1027/1954	1714/4157
Professionals	4,914	10,833	11,138
Total Cap Mgt	\$64.6 B	\$251.4 B	\$406.8B
Avg Firm Size	\$13m/professional \$135.3 M	\$23m/professional \$245.7 M	\$36m/professional \$237M
Avg Fund Size	\$94.0 M	\$103.5	\$98M
First time funds	61	38	27
Largest Fund	\$1,158. M	\$1,100 M	\$1,250M

Reyes, J. (2004) Private Equity Performance 2004: The Coming Shakeout.

2005 data from VentureXpert.

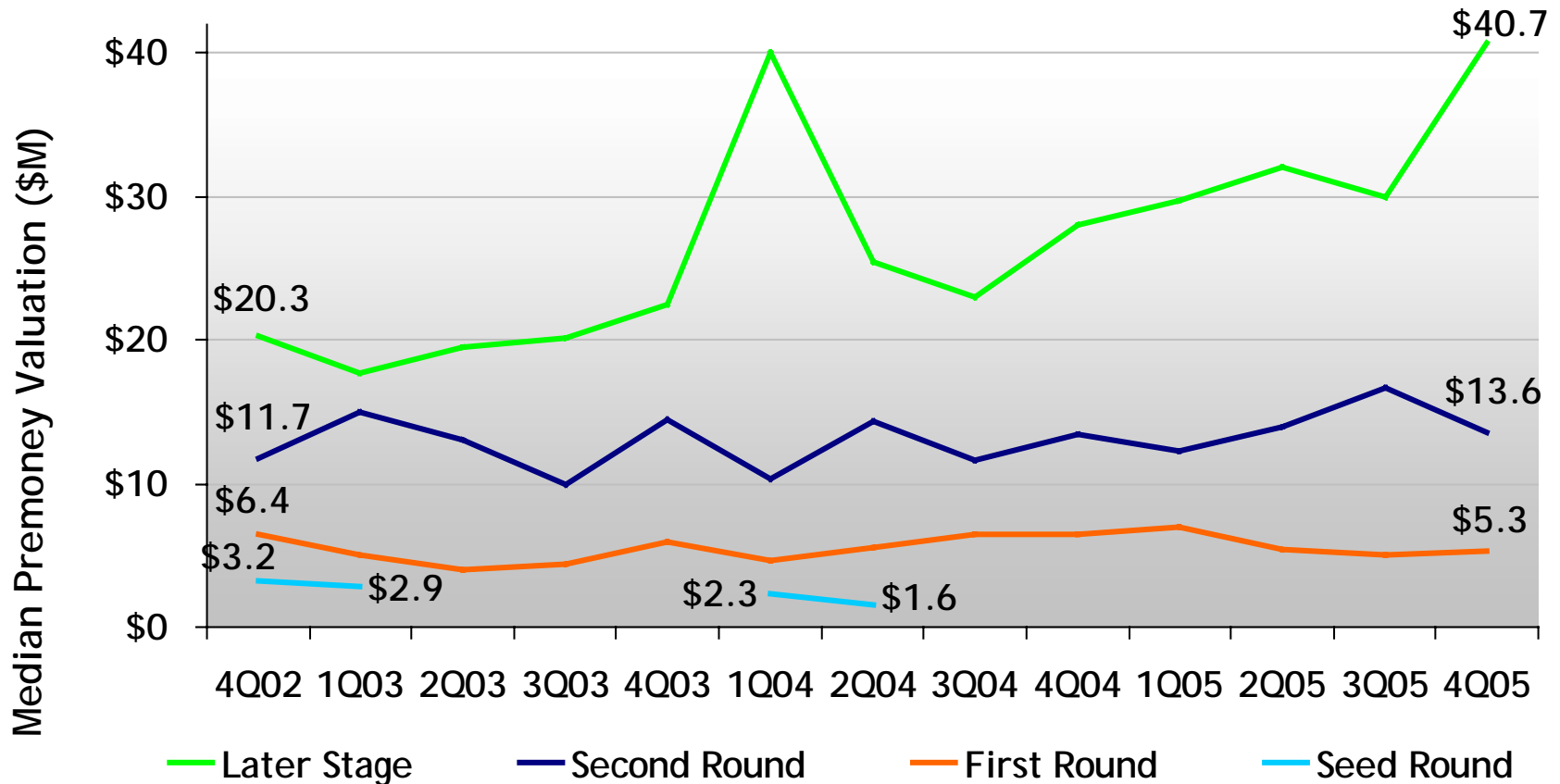
Bygrave and Zacharakis ©



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Later Stage Valuations Skyrocket

Median Premoney Valuations by Round Class (All Industries)



Source: Dow Jones: Venture Source.

Bygrave and Zacharakis ©



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

Thompson Financials'
 US Private Equity Performance Index
 Investment Horizon through 12/31/05

Fund Type	1 Yr	3 Yr	5 Yr	10 Yr	20 Yr
Seed/Early Stage VC	8.3	3.1	-10.9	41.5	20.4
Balanced VC	24.3	11.7	-3.5	18.9	14.6
Later Stage VC	6.9	8.6	-4.1	11.3	13.5
All Venture	15.6	7.5	-6.8	23.7	16.5
NASDAQ	5.2	14.2	-2.2	7.7	12.4
S&P	6.3	10.1	-1.1	7.3	11.0



THE ARTHUR M. BLANK
 CENTER FOR ENTREPRENEURSHIP
 AT BABSON COLLEGE

Returns By Percentile

Cumulative IRR as of 12/31/2005		Venture Capital				
Sample size : 1164						
Percentile Group	Overall	Seed	Early	Balanced	Later	
70.00th percentile	13.43	10.63	13.71	13.49	13.39	
60.00th percentile	8.62	8.46	7.25	9.17	9.52	
50.00th percentile	4.36	3.94	2.58	5.56	5.04	
40.00th percentile	0.78	1.73	-1.4	2.56	1.49	
30.00th percentile	-1.81	-0.99	-6.53	0	-0.57	
20.00th percentile	-7.28	-6.51	-11.13	-3.3	-2.75	
10.00th percentile	-14.75	-9.77	-19.37	-11.23	-10.05	
0.00th percentile	-100	-31.45	-47.88	-35.45	-100	

Source: VentureXpert



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

IMPLICATIONS

- **Capital overhang is working through.**
- **Size of VC firms continues to grow**
 - \$ outpace partners
 - Later-stage (lower risk?) deals
- **Remain focused on high-tech**
 - Investing larger amounts at later rounds, tech has most potential to achieve returns
- **Less co-investing/syndication**
 - Need to put more money into each deal
 - Lowers learning and network reach
- **Valuations Heat Up**
 - Hurts returns
 - Increases risk



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

A MOVE TO NEW MARKETS

- **50% of US VCs expect to invest globally by 2010**
 - Following the entrepreneurs (many US trained)
- **China and India are hot markets**
 - 20% of US VCs plan to invest in China
 - 18% plan to invest in India
- **Investing Strategy**
 - Co-invest with local investors (42%)
 - Strategic alliances with local VC firms (39%)
 - Open new office with local talent (30%)
 - Transfer partners (10%)

VC Outlook 2010: A Brave, Global World *Mark Jensen and Mark Heesen*. [Venture Capital Journal](#). Wellesley Hills: [Aug 1, 2005](#). pg. 1



THE ARTHUR M. BLANK
CENTER FOR ENTREPRENEURSHIP
AT BABSON COLLEGE

What Does it Mean?

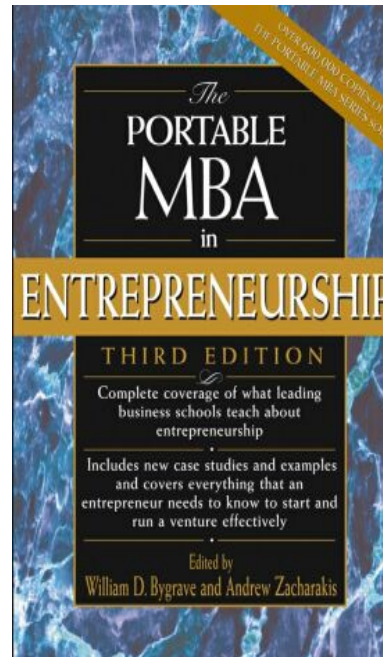
- **Search for better deals?**
 - **Breeder for Technology**
 - **Energy**
 - **Water**
 - **Developing Economies**
 - **Later, larger absorptive capacity deals**
- **Who fills in that larger, increasing gap?**
 - **Angels, FFFF, Bootstrapping**



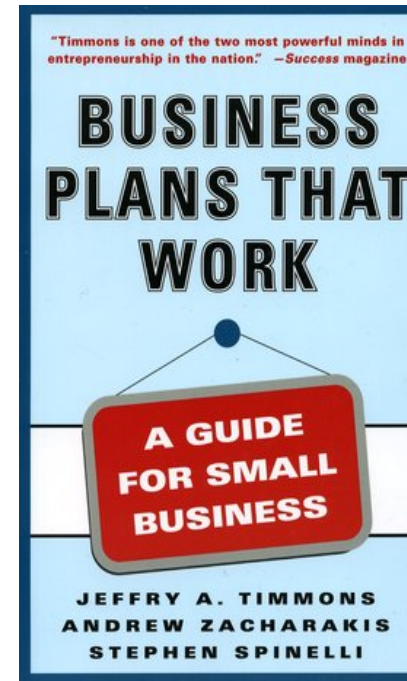
For those wanting more...



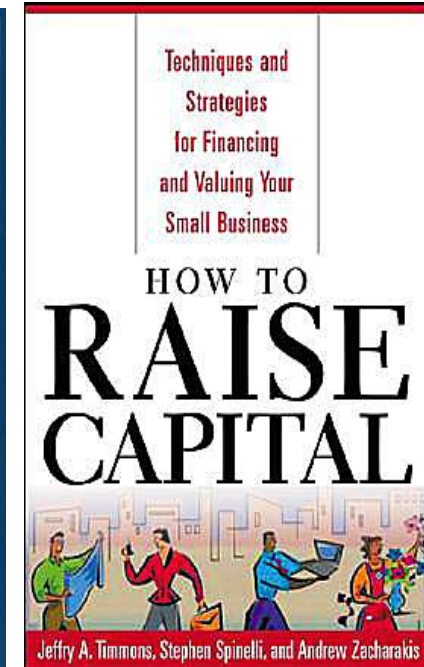
Bygrave & Zacharakis
(2007) *Entrepreneurship*



Bygrave &
Zacharakis (2004)
*The Portable MBA in
Entrepreneurship*



Timmons, Zacharakis &
Spinelli (2004) *Business
Plans that Work.*



Timmons, Spinelli &
Zacharakis (2005) *How
to Raise Capital*

