



VCs fear public market fallout

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Technology entrepreneurs and the venture capitalists who back their businesses tend to feel insulated from earthquakes that shake the public markets. Certainly, the lack of an initial public offering market and depressed M&A activity over the past several months have been worrisome, but venture capitalists tend to invest on a five- to seven-year time horizon, and one would hope that's a long way from the current troubled times.

Yet with the economic and financial problems having reached historic proportions, VCs acknowledged that the current crisis could indeed take a toll on private company finance by reducing available funding for startups and, as a consequence, stifling innovation.

"People are going to be more conservative," said venture capitalist Fred Wilson, whose New York-based **Union Square Ventures** backs microblogging firm **Twitter Inc.** and other Web. 2.0 startups. "There are times when people want to take risks and times when people don't want to take risks. Clearly, no one's going to want to take risks right now."

For the very youngest companies, the flow of capital could shrink significantly. This area of private investing has always been the riskiest, and angel investors who dabbled in backing young companies will pull back, said Chris Sacca, the former **Google Inc.** wireless chief who left the search giant earlier this year to focus full-time on early-stage investing.

"One thing we will see is the shakeout of many casual angels," he said. "The armchair investors who write checks to startups have been increasingly rare as they watch their public market portfolios dwindle and realize they don't have the stomach for early-stage high-risk deals."

Rodney Altman, a partner at **CMEA Ventures** in San Francisco, where he invests mostly in medical devices and biotech therapies, said the current environment is a "huge concern" for VCs, who face a double whammy of fewer exits and a need for larger asset allocations for portfolio companies that were taking longer to get to exit.

"We are actively looking at our portfolio right now and looking at how much we have reserved for each company," he said. "It would be irresponsible not to."

Yet some venture capitalists see a silver lining in the clouds over the U.S. economy. Drew Lipsher, a partner with New York-based **Greycroft LLC**, argued that most investors in private equity-oriented funds, including VC funds, are sophisticated and patient enough to wait out the current turmoil.

"They have a far longer-term horizon," he said. "Unless they have personal bankruptcy issues, they're not going to pull their money. They leave their money where it is and understand the long-term nature of these vehicles. In fact, they might put more of their money to work in venture capital and private equity."

For entrepreneurs, it will be more difficult to raise money, Wilson said, but not impossible.

"Good ideas are still going to get funded," he said.

Some startups that have received funding recently said they expected the worst but were surprised to find that the process was not as tough as feared.

"I've got to say it was refreshingly painless," said Yen Lee, founder and president of **UpTake Networks Inc.**, a Palo Alto, Calif.-based aggregator of travel information that announced a \$10 million Series B round of funding Wednesday, Sept. 17. "We didn't need to raise the money right when we did, but we had heard so many horror stories in the second quarter that we decided to raise the money now, and there were a number of firms that absolutely got the value proposition we're offering and the power of the business model."

Lisa Alderson, CEO of **CrossLoop Inc.**, a Monterey, Calif., maker of screen-sharing software used for tech support, said she also didn't have much trouble securing the \$6 million in Series B financing the company announced on Sept. 15.

"We had multiple term sheets and broad interest in our Series B, and it was fairly quick," Alderson said. "It was four months from the first pitch to our deal."

Lee and Alderson should consider themselves lucky they secured financing before the current debacle hit the nation's banking system, but others said it is just this kind of meltdown that creates opportunity. Theresa Lina Stevens, head of the Stanford Technology Ventures Program, which assists entrepreneurship at all levels of business, argued that the whole Web 2.0 phenomenon was essentially born in the ashes of the Web 1.0 bust.

"This can be a great time to start a business," she said. "When everything else is down, that is the time to start. The pressure is off, and you can still find early adopters, and you have more room for a learning curve, so that by the time the capital is available, you have something that is established and worthy of funding."

Sensing an opportunity to assist startups that may be having difficulty raising funds, Richard Singer co-founded a Web site, RaiseCapital.com Inc., that helps investors to connect with entrepreneurs. Singer said the site has seen a spike in activity in light of the weakness in the financial markets.

"Over the last two or three weeks, on the side of businesses looking for capital, we've seen a surge," Singer said. "We've also seen an increase in registered investors, but not as much as businesses looking for capital."