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How to Snag the Strategic Investor

Venture-capital firms and corporate investors each pump cash into startups, but their goals are likely to be very different

What is it that professional investors want from young companies? The highest possible return on investment, we are told. But that oversimplifies the matter, because the fact is that professional investors are driven by their own individual agendas -- ones that may not be readily apparent to entrepreneurs.

It is often said that the most important challenge faced by any business owner is understanding his or her customers, which is true enough -- so far as it goes. But entrepreneurs must also understand the complex factors, influences, and priorities that motivate their distributors, wholesalers, retailers, and other links in the marketing chain moving products through to customers. Entrepreneurs also must adjust the incentives they provide to make sure all parties' needs are in harmony.

THE CORPORATE VIEW. The agendas driving professional investors also vary widely. Begin with strategic investors, which are typically large corporations, and have much different agendas than those of venture-capital investors. Thus, entrepreneurs must adjust the investment pitches they make to each if they are going to stand a chance of winning funding. In this article, I will examine the corporate investor's perspective, and in my next column, the venture capitalists' outlook.

Corporations that invest in young companies typically do so through a venture arm established for that purpose. These units are staffed by professionals trained in the ways of the venture-capital world, but their view of that mission differs from those of counterparts in venture-capital firms -- and it is a much different perspective than entrepreneurs often imagine. Simply put, they must report to a corporate hierarchy whose goals are reflected in its investment strategy.

Entrepreneurs seeking investment funds from corporate investors tend to view them as huge bureaucracies that want to invest in nimble young companies providing the latest in technology or marketing. The entrepreneurs' biggest worry is that the corporate investor will somehow steal the new technology. Meanwhile, the opportunity many entrepreneurs see is the possibility that corporate investors will eventually buy out their startups. This view of corporate investors colors the entrepreneurs' approach to obtaining investment backing. They tend to focus on legal issues -- protecting their intellectual property, establishing guidelines around the corporate right of first refusal on possible acquisition, setting up terms for technology licensing, and so forth.

DIFFERENT PERSPECTIVE. The corporate venture investor's view may be much different, however. Corporate investors may be less interested in gaining access to a particular technology than they are in tapping the entrepreneur's envision. Also worth noting is the change that has taken place since the late 1990s, when there was a high probability that corporations would acquire the companies in which they invested. These days, that is less likely to be the case.

So what is it that the corporations want? Typically, it is something more subtle than what entrepreneurs suppose -- to take possession, one way or another, of their ideas and technologies. The corporations want most of all a window on the future of a particular industry, and they figure that a young company with leading-edge products or services is going to provide the best view of those emerging horizons. In addition, the corporations assume that the young company's management is likely to include the leading thinkers and doers -- people, in other words, who are in contact with other brightest lights of their industry.

Corporate investors want to join the clique, as it were, to which leading-edge entrepreneurs belong.



Gabor Garai

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