Venture capital has enabled the United States to support its entrepreneurial talent and appetite by turning ideas and basic science into products and services that are the envy of the world. Venture capital funds and builds companies from the simplest form—perhaps just the entrepreneur and an idea expressed as a business plan—to freestanding, mature organizations.

Risk Capital for Business

Venture capital firms are professional, institutional managers of risk capital that enables and supports the most innovative and promising companies. This money funds new ideas that could not be financed with traditional bank financing, that threaten established products and services in a corporation, and that typically require five to eight years to be launched.

### Venture Capital Backed Companies
**Known for Innovative Technology and Products**
**2000 and 2006 Employment**

<table>
<thead>
<tr>
<th>Company</th>
<th>2000</th>
<th>2006</th>
<th># Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intel Corporation</td>
<td>86,100</td>
<td>103,200</td>
<td>17,100</td>
</tr>
<tr>
<td>Microsoft</td>
<td>39,100</td>
<td>71,000</td>
<td>31,900</td>
</tr>
<tr>
<td>Medtronic, Inc.</td>
<td>21,490</td>
<td>36,000</td>
<td>14,510</td>
</tr>
<tr>
<td>Apple Inc.</td>
<td>8,568</td>
<td>17,100</td>
<td>8,532</td>
</tr>
<tr>
<td>Google</td>
<td>—</td>
<td>10,600</td>
<td>10,600</td>
</tr>
</tbody>
</table>

*Source: Hoover’s*

Venture capital is quite unique as an institutional investor asset class. When an investment is made in a company, it is an equity investment in a company whose stock is essentially illiquid and worthless until a company matures five to eight
years down the road. Follow-on investment provides additional funding as the company grows. These “rounds,” typically occurring every year or two, are also equity investment, with the shares allocated among the investors and management team based on an agreed “valuation.” But, unless a company is acquired or goes public, there is little actual value. Venture capital is a long-term investment.

**Venture Capital Backed Companies**
**Known for Innovative Business Models**
**2000 and 2006 Employment**

<table>
<thead>
<tr>
<th>Company</th>
<th>2000</th>
<th>2006</th>
<th># Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Home Depot</td>
<td>201,000</td>
<td>345,000</td>
<td>144,000</td>
</tr>
<tr>
<td>Starbucks Corporation</td>
<td>47,000</td>
<td>116,700</td>
<td>69,700</td>
</tr>
<tr>
<td>Staples</td>
<td>49,993</td>
<td>68,500</td>
<td>18,507</td>
</tr>
<tr>
<td>Whole Foods Market, Inc.</td>
<td>18,500</td>
<td>38,600</td>
<td>20,100</td>
</tr>
<tr>
<td>PetSmart, Inc.</td>
<td>19,825</td>
<td>30,300</td>
<td>10,475</td>
</tr>
<tr>
<td>eBay</td>
<td>1,927</td>
<td>12,800</td>
<td>10,873</td>
</tr>
</tbody>
</table>

*Source: Hoover’s*

**More Than Money**

The U.S. venture industry provides the capital to create some of the most innovative and successful companies. But venture capital is more than money. Venture capital partners become actively engaged with a company, typically taking a board seat. With a startup, daily interaction with the management team is common. This limits the number of startups in which any one fund can invest. Few entrepreneurs approaching venture capital firms for money are aware that they essentially are asking for 1/6 of a person!

Yet that active engagement is critical to the success of the fledgling company. Many one- and two-person companies have received funding but no one- or two-person company has ever gone public! Along the way, talent must be recruited.

**What Entrepreneurs Are Really Asking For!**

An early stage venture capitalist sitting on six company boards has a huge workload.
and the company scaled up. Ask any venture capitalist who has had an ultra-
successful investment and he or she will tell you that the company that broke
through the gravity evolved from the original business plan concept with the
careful input of an experienced hand.

**Deal Flows — Where The Buys Are**

For every 100 business plans that come to a
venture capital firm for funding, usually only 10
or so get a serious look, and only one ends up
being funded. The venture capital firm looks at
the management team, the concept, the market-
place, fit to the fund’s objectives, the value-added
potential for the firm, and the capital needed
to build a successful business. A busy venture
capital professional’s most precious asset is time.
These days, a business concept needs to address
world markets, have superb scalability, be made
successful in a reasonable timeframe, and be
truly innovative. A concept that promises a 10
or 20 percent improvement on something that
already exists is not likely to get a close look.

Many technologies currently under development
by venture capital firms are truly disruptive
technologies that do not lend themselves to being
embraced by larger companies whose current
products could be cannibalized by this. Also,
with the increased emphasis on public company
quarterly results, many larger organizations tend
to reduce spending on research and development
and product development when things get tight.
Many talented teams have come to the venture
capital process when their projects were turned
down by their companies.

**Common Structure — Unique Results**

While the legal and economic structures used to create a venture capital fund
are similar to those used by other alternative investment asset classes, venture
capital itself is unique. Typically, a venture capital firm will create a Limited
Partnership with the investors as LPs and the firm itself as the General Partner.
Each “fund,” or portfolio, is a separate partnership. A new fund is established
when the venture capital firm obtains necessary commitments from its investors,
say $100 million. The money is taken from investors as the investments are made.
Typically, an initial funding of a company will cause the venture fund to reserve
three or four times that first investment for follow-on financing. Over the next
three to eight or so years, the venture firm works with the founding entrepreneur
to grow the company. The payoff comes after the company is acquired or goes
public. Although the investor has high hopes for any company getting funded,
only one in six ever goes public and one in three is acquired.
Venture capital is rare among asset classes in that success is truly shared. It is not driven by quick returns or transaction fees. Economic success occurs when the stock price increases above the purchase price. When a company is successful and has a strong public stock offering, or is acquired, the stock price of the company reflects its success. The entrepreneur benefits from appreciated stock and stock options. The rank and file employees throughout the organization historically also do well with their stock options. The venture capital fund and its investors split the capital gains per a pre-agreed formula. Many college endowments, pension funds, charities, individuals, and corporations have benefited far beyond the risk-adjusted returns of the public markets.

**What’s Ahead**

Much of venture capital’s success has come from the entrepreneurial spirit pervasive in the American culture, financial recognition of success, access to good science, and fair and open capital markets. It is dependent upon a good flow of science, motivated entrepreneurs, protection of intellectual property, and a skilled workforce.

The nascent deployment of venture capital in other countries is gated by a country’s or region’s cultural fit, tolerance for failure, services infrastructure that supports developing companies, intellectual property protection, efficient capital markets, and the willingness of big business to purchase from small companies.