# Article: Understanding Venture Capital

**By Investment Guru, Len McDowall**

Everyday we read about companies who have raised millions of dollars of capital to fund the growth and expansion of their business. The reality of raising these sorts of funds is much more complex than the newspapers make it out.

There are many different sources of capital – obtaining it depends on many factors. It also requires careful planning, the right advice and the right pitch. Whether you will get it or not also depends on what kind of business you have, what stage it is at, what industry it's in, how profitable it is, how much experience you have and how the overall market is tracking.

### What is Venture Capital?

The term Venture Capital means capital provided to fund a venture. Essentially venture capital and private equity mean the same thing. However there is a difference between Venture Capital and Private Equity firms. VC firms typically will look at more emerging business and industries and may get involved at an earlier stage. Private Equity firms typically like more traditional industries, and tend to like mature companies with consistent cashflows.

### What is a Business Angel?

"Angel" investors are individuals who like to get involved at the seed or start up stage of a business venture. They look for very high-growth companies that also have synergy with their own business skills or network. Capital invested can be as little as $10,000 and as much as $500,000 initially. Follow on rounds may be an option also. The Angel will typically look to get their hands dirty by taking a small role, going on the board, or acting as a business mentor.

### What is a liquidity event?

This is the event that gives the investor their money back. This is most commonly a trade sale or a public float. However, sometimes the investor may get bought out by another investor or by the original owner.

### Types of Capital Available

Below are some terms that are commonly used to describe the various stages of funding:-

**Seed** This is at the very beginning of a company's life, often before any profit or sales are achieved. Sometimes it's used to fund the formation of the venture and its necessary components in order to get it off the ground.

**Start-up** This is when the business has commenced trading but it is still in its infancy. A start up business is typically only six months or a year old.

**Expansion** The company has sales plus an established market in a particular segment or location (such as Sydney) and is now requiring funding so they can expand their operations further. Sometimes the company is growing very quickly and needs to scale up in order to meet market demand.

**Acquisition** The company is seeking to expand by purchasing other business that are similar or synergistic in nature. The company may not have the necessary funds to do this, which is where acquisition funding comes in.

**MBO/MBI** This stands for Management Buy Out or Management Buy In. It means exactly that. These are funds usually provided by a private equity firm or institutional bank which allow the existing management (MBO) or new management (MBI) to buy out the existing owners.

**Pre-IPO** The round of funding that precedes an IPO, usually between two months and up to two years. Funds are sought in order to fund an acquisition, expand or pay for listing costs. These deals are only usually available to professional investors, institutional investors or high net worth individuals because the amounts involved tend to be in the millions or tens of millions.

**IPO** This means Initial Public Offering and is when a company goes public on an exchange such as the ASX. This is done via a prospectus document and allows 'mum and dad' type investors to invest alongside the founders, major shareholders, professional investors and institutional investors. This is the most common way to raise large sums of money, such as $50m or $100m.



**About Len McDowall - Managing Director, Integral Capital Group Pty Ltd**

Len McDowall was previously inaugural Chairman and Managing Partner of Bird Cameron, Chartered Accountants, (now known as RMS Bird Cameron) which employed 1000 people in 50 offices in Australia and Hong Kong. Len McDowall who established Bird Cameron's mergers and acquisitions division, has extensive experience in all facets of financial management with a particular emphasis on structuring and negotiating joint ventures and capital raisings. Following his retirement from the accounting profession Len and his partners established the Integral Capital Group which specialises in mergers and acquisitions, public floatation's and capital raisings.