

# **Article: What is Venture Capital?**

**By Len McDowall, Integral Capital Group**

Much confusion reigns over the term Venture Capital (VC) and the VC industry in Australia.

In simple terms, Venture Capital is capital invested by investors into a non-publicly listed business, in return for equity or shares in that entity.

Venture Capital investors are obviously then accepting a higher degree of risk ,as compared to banks and other financial institutions who loan funds typically against assets or collateral and in return are paid interest and eventually the return of their money over a set time period.

The term Venture Capital is often used interchangeably with the term Private Equity. Both of these terms cover all possible stages of investment, whether it be seed or start up funding, funding for expansion or funding associated with an acquisition, whether that be a Management Buy In (MBI) or Management Buy Out (MBO).

Venture Capital investors are equity investors who are seeking above average returns for the risk that they may lose their capital.

Private Equity firms involved in MBO's and MBI's have received much publicity over the last few years with spectacular results when they relist acquisitions that they made a few years before. Here the Private Equity Firms took advantage of weaker markets and leverage invested into ailing or underperforming companies, utilizing existing or new management teams to revitalize the businesses.

At the other end of the market ,technology based venture capital firms have struggled since the fall out of the technology sector in early 2000.Many are sitting on businesses that are struggling to grow.

Questions often on business owners minds are:-

- How would I go about obtaining venture capital funding?
- Am I big enough?
- Should I acquire another business?
- Should I sell?
- Should I go public?

These questions cannot be answered before establishing a clear strategy, and therefore it is important not to jump in or be swayed by what is happening in the public markets or in the media or with other businesses you are familiar with.

Each business is different, and the business owners and other stakeholders in the business will have their own set of expectations, needs, financial goals and personal objectives.

Should the strategy determine that an external investor should be brought into the business, then it is imperative that the business is made “investor ready”, in order to optimize the valuation for the business. Equally important, a list of criteria should be drawn up which clearly defines the type of investor required. Many businesses have suffered due to the involvement of an investor whose objectives were not aligned to those of the business.

The right type of investor should provide not only the injection of capital, but considerable potential value to a business in terms of resources, skills, contacts, experience etc.

Far too many businesses that were ill prepared rushed into public listing in the late 90's and consequently suffered. Most of these businesses would have been far better off with venture capital funding. Many more businesses find their eventual exit to be way of trade sale than public listing, and on most occasions significantly more value is realized.

Some companies undertake the capital raising process themselves. Some are successful, many are not. It is advisable to seek professional advice, as making the wrong move can either use up valuable time and resources, or worse still, create a negative perception in the market.

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### **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, 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 in 1990 which specialises in mergers and acquisitions, public floatation's and capital raisings.