

The Journal of **PRIVATE EQUITY**

Strategies and Techniques for Venture Investing

VOLUME 5, NUMBER 1

WINTER 2001

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Since vibrant equities markets have stilled, and the events of September exert a sobering effect on many sectors of the economy, a look at what venture capital and private equity professionals are doing seems in order. This issue is devoted to a review of practices and ideas apart from the issues of stock market movements. We present articles concerned with running a venture capital or equity buy-out shop.

Our lead article examines what venture capitalists do day to day and how they learned their trade. For those of us speaking to groups not familiar with equity and venture capital, the most frequently asked question invariably concerns, "How can I become a Venture Capitalist?" Here, Fred Dotzler unravels the puzzle of where venture capitalists add value and how aspiring venture capitalists can acquire the skills necessary to do so.

Most venture capitalists sit on the boards of the companies they invest in. Anestis and Lindsey investigate many variables to explain when venture capitalists join boards and when they leave: the size of the IPO, the total financing for the company, the number of financing rounds, the number of pre-IPO investors, the size of the board, the geographical location of the company, and the industry. Do you think the rising equity markets in 1999 had an effect on these variables and on board composition? Their search for a "1999 effect" may surprise you.

In the race to find great ideas for new businesses, venture capital and equity capital partnerships have established new offices, in many cases outside of the United States. Dixit and Jayaraman investigate, through case studies of several large funds, the use of different models of growth. Each of the three models supports a different business style, and this article makes explicit the pros and cons of the organic growth, affiliate office, and specialized fund approaches.

Ever buy or sell a partnership interest? This is an appealing way to acquire or dispose of a non-public ownership share, but how do these transactions operate? Michael Smith takes us on a guided tour of the secondary private equity market. Wonder how much volume has flowed through the secondary market? Over \$2 billion in the year 2000. Would you like to see some recent large trans-

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actions, with both buyer and seller named? How about a list of secondary specialists? Or actual secondary fund performance numbers? That and much more is all here.

Private investment in a public company is a way for investment funds to bargain privately with a public company. Mark Anson illustrates the ins and outs of this procedure, one that grants unusual power to investors yet allows a (usually) struggling public company access to capital. What kinds of strings are attached to these investments? Many: for example, interest on convertible notes, warrant rights, conversion privileges (either fixed or adjustable), and of course registration rights. Remember, these private investments are not sellable on the public market until the new instruments are registered by the SEC. Sound a bit tricky to you? Read on to see where best to use this technique.

Our final article relates to LBO firms but applies quite directly to venture firms as well: The art, science and mystery of due diligence. Tom Kieren interviewed nearly one hundred managing directors in equity capital partnerships about their due diligence programs. How well planned were they? Were the deals financial or strategic in orientation? Who completes the due diligence? How are outside consultants selected? After the deals closed, how happy were the investors with their due diligence? These questions and many more concerning this vital step in the investment process are examined.

James E. Schrager
Editor