STARTUP SCHOOL

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An Introduction to Venture Creation
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- 1993- BS Computer Science, KU
- 1994 - 2001 - San Francisco, First Dot-Com Wave
- 2010 - MBA @ UCLA
- Current - CTO @ Zuma Ventures
- Current - Investment Committee at UCLA Venture Capital Fund
Y COMBINATOR IS A VENTURE FUND

- Paul Graham and Sam Altman profit if Y Combinator does well
- Venture funds must have unicorns
- Therefore, they MUST invest in “hyper growth” companies
- What’s wrong with a “small” $100M valuation?
# Financial Reward & Impact

<table>
<thead>
<tr>
<th>A Real Company</th>
<th>Valuation</th>
<th>Employee #100’s Upside (10bp)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dropbox</td>
<td>$10B</td>
<td>$10M</td>
</tr>
<tr>
<td>Facebook</td>
<td>$200B</td>
<td>$200M</td>
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<table>
<thead>
<tr>
<th>Your First Company</th>
<th>Theoretical Valuation</th>
<th>Founder’s Upside (10%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>“Uber for Pet Sitting”</td>
<td>$100M</td>
<td>$10M</td>
</tr>
<tr>
<td>“Uber for Space Travel”</td>
<td>$2B</td>
<td>$200M</td>
</tr>
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1. IDEA
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- The Idea comes first
- The company should feel like an important mission
- Why now?
MISSION-ORIENTED COMPANIES

• You yourself will be dedicated to them. If you don’t love what you’re doing, you’ll give up.

• It’s easier to hire and motivate others on the team.

• People outside the company are more willing to help.
GOOD IDEAS LOOK BAD

- 13th Search Engine - Google
- 10th Social Network - Facebook
- Web-Based Email - MightyMail (sold for $35M cash, six months after founding)
- Plenty of Fish
FIRST TO MARKET?

- You can be late to market, just close the market.
WHY NOW?
WHAT IS SPECIAL ABOUT THIS TIMING?

Why wouldn’t this company succeed two years ago, and why it will be too late in two years.
GROWING MARKETS

- Both Sam Altman and Paul Graham talk about growing markets
- Look for macroeconomic trends that will help the company grow
- A rising tide lifts all boats
THE GREAT RECESSION BEGAT

- AirBNB
- Uber
- TaskRabbit
- DogVacay
- etc.
IDEALAB: BILL GROSS

THE SINGLE BIGGEST REASON STARTUPS SUCCEED

March 2015, TED Talk
Idealab Founded Over 100 Companies in Last 20 Years
5 Essential Elements that Lead to Success

- Ideas
- Team
- Business Model
- Funding
- Timing
Top 5 Factors in Success Across More Than 200 Companies

- Timing: 42%
- Team / Execution: 32%
- Idea “Truth” Outlier: 28%
- Business Model: 24%
- Funding: 14%

For more talks visit TED.com
DERIVATIVE COMPANIES

• “The Uber of X”

• Both Sam Altman and Paul Graham argue that these are bad ideas, but consider:

  • AirBNB for Dogs
  
  • Raised $47M in venture funding
  
  • Employs 100-250 people
A FEW GUIDELINES

• Find a small, UNDERSERVED market, where you can get a monopoly, then quickly expand

• Search for people or companies that have significant problems

• These problems are not served by any existing incumbents

• Example: payday lenders and the underbanked

• Example: Realty Mogul
2. PRODUCT
WHAT IS A PRODUCT?

- SOLVES A SIGNIFICANT PROBLEM
- FOR A LARGE AUDIENCE
- THAT IS WILLING TO PAY (VIA SOME CURRENCY)
- BETTER THAN THE CURRENT SOLUTIONS
EXAMPLES OF PRODUCTS

• Facebook
• Google
• Tinder
• Zappos
• Bachelor Degree in Computer Science
BUILDING A GREAT PRODUCT

- Build something users love
- Great products win
- Fanatical users
- User feedback loop
- Metrics: Focus on Growth
Start Here
GREAT PRODUCTS

• Users who love products tell their friends
• This causes organic growth
• This lowers customer acquisition cost
• Which makes the unit economics of your company better.
PRODUCTS SOLVE PROBLEMS

• What problems do the following products solve?
• Google
• Facebook
• What is your current favorite product?
• What unsolved problems do you have?
User feedback
- What do they like?
- What would they pay for?
- What would make them recommend it?

Show it to users

Product Decisions

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ASK YOUR USERS

- Ask them what they like and don’t like.
- Watch them use it.
- Ask them what they would pay for.
- Ask them if they’d be really bummered if your company went away.
- Ask them if they’d recommend the product to their friends (net promoter score).
THE BEST COMPANIES HAVE THE TIGHTEST FEEDBACK LOOPS
CASE STUDY: FLYING YAK
3. TEAM
TEAM SELECTION

• Find people smarter than you
• Find founders you have a pre-existing relationship with
• The correct number is 2-3, not 4, not 1
• Hire slowly, fire fast.
• Maintain n-1, where n is the team size you *think* you need
FOUR PERSONALITY TYPES

• Entrepreneur - the company visionary
• Producer - makes things happen
• Integrator - the team gel that holds it together
• Administrator (adds systems and procedures)
COMMON FOUNDER PATTERNS

• Hacker / Hustler
• Tech / Product / Sales

• Core team should *not* include
  • CFO, Accounting, Customer Service, PR
EQUITY SPLIT

- Have this conversation early
- Everybody has graduated vesting
  - 4 year vest with 1 year cliff
BOARD MEMBERS

- Previous company-building expertise.
- Strategic management experience.
- Technical or industry experience.
- Reputation and valuable network.
- An intimate understanding of the customers and markets.
BOARD MEMBERS

- Somebody with a golden rolodex that can bring you relationships, and by association, sales.

- Potential board members:
  - CEO of ideal biggest customer
  - CEO of biggest partner
  - CEO of potential acquirer
  - CEO of financial partner (ie, Angel, VC, P/E firm)
4. EXECUTION
CEO RESPONSIBILITIES

- Set the Vision
- Raise Money
- Evangelize
- Hire and Manage
- Make sure the entire company executes
GOALS

1. User Growth
2. User Retention
3. Features that Improve 1 & 2
GROWING A STARTUP

• Growing a Startup = the methodical removal of risk from the company

• The value of a startup is directly related to the amount of risk remaining

• Each round of funding should be used to eliminate another type (or 2) of risk
STAGES OF A COMPANY

- **Startup**
  - Validate Value Hypothesis
  - Validate Growth Hypothesis
- **Efficiency**
  - Improve Unit Economics
- **Growth / Scale**
  - Capture Market Share
  - Remain Unprofitable
- **Mature**
  - Defend Market Share
  - Reap Profits
- **Decline**
  - Declining Profits
  - Low Investment
Lifecycle of a venture

- **Firm Formation**
  - Research Grants
  - Development Grants (eg SBIR)
- **Stage of Venture Development**
  - Basic Research
  - Applied Research
  - Proof of Concept
  - Target Market
  - Business Plan
  - Working Prototypes
  - Founding Team
  - Engineering Prototypes
  - Supplier Contracts
  - Production Prototypes
  - Distribution Contracts
  - Revenue Growth

**Funding**
- **Net Cash Flow**
- **Early Stage Venture Capital** ($500k-$2M+)
- **Venture Capital** ($2M-$50M)
- **Private Equity, Project Financing** ($2M-$50M)
- **IPO, Merger, or Acquisition** ($25M+)

- **“Valley of Death”**
STAGES OF A COMPANY

Customer discovery → Customer validation → Customer creation → Company building

Search

Pivot

Execution

Steve Blank - The Start-up Owners Manual
OPERATING METRICS

• Revenue / Revenue Growth
• Burn Rate
• Customer Acquisition Cost (CAC)
• Customer Lifetime Value (LTV)
• Active Users (30 day)
• Retention / Churn
• Viral Coefficient
FUNDRAISING

![Startup Financing Cycle Diagram]

- Angels, FFF
- Seed Capital
- Early Stage
- Break even
- Valley of Death
- IPO
- Mezzanine
- 1st
- 2nd
- 3rd
- Later Stage
- VCs, Acquisitions/Mergers & Strategic Alliances
- Secondary Offerings
- Public Market
WHY GROWTH CAPITAL?

- CAC = The Cost to Acquire a Customer
- CLV = The Lifetime Value of a Customer

It might take several months to recoup the CAC, which means the more aggressive one’s customer acquisition, the greater the loss.