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Founder-Investor Fit

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10-12 minutes

Welcome to issue #11 of *next big thing*.

This is the third in a series about trends in the venture capital industry.

My last two essays, on solo capitalists and agglomerators vs. specialists, touch on key aspects of the current ecosystem.

But what will drive the evolution of the industry in the future?

Founder-investor fit, which happens when the desires of founders match the products of investors, is one important factor.

At its core, venture capital is a people-driven business.

As venture capitalists, we search for extraordinary founders to invest in, and our investment decisions often come down to our judgment of those founders as people. Most venture capitalists operate in partnerships, which are made up of people, and the dynamics between those individuals drive decision-making within firms. And for founders, the selection of which investors to work with sometimes rests on which people they want to be in business with for many years. "You can't fire your investor" as the truism goes.

So it naturally follows that the right lens with which to analyze the future of the industry is the "people" lens. *Founder-investor fit* is a concept I've long thought about, and one that I think provides an important framing for viewing the future of venture capital.

As venture firms grapple with key topics such as diversity, generational transition, the tension between individuals' brands and the firm's brand, and how all these factors play into partnership dynamics and fundraising, *founder-investor fit* deserves to be at the center of the conversation.

Founder-Investor Fit

The decision for a founder to take an investment from a venture capital firm, and the decision for a venture capital firm to invest in a founder, hinges on *founder-investor fit*. Once a venture firm has decided to make an investment, their ability to win over the founder rests on finding *founder-investor fit.* And the key question becomes: does the firm's product match the founder's needs?

How do founders choose their investors? Some care about the best deal terms: the largest round size at the highest valuation with the lowest dilution. Others care most about speed of the investment decision. Some care most about the brand of the firm. Some gravitate more towards agglomerator firms, and others more towards specialists. Others care more about the brand of the individual partner leading the investment. Still others care less about the brand, but more about how exactly the firm or the individual will help their business be successful. Some founders are looking for specific expertise - help in hiring, for example, or a former founder, or someone with deep experience in their business model or sector, as their lead investor. Other founders want a stage-focused investor to match their stage of business. Many founders' decisions rest on references, on the investor's reputation, and on better understanding how the investor has acted in the past during good and bad times. If the new investor is taking a board seat, the decision can rest on who the founder wants as their board member, based on some of the above factors. Finally, for some founders it comes down purely to the relationship built with the investor, and who they want to spend a lot of time with as they continue to grow the business.

Given the many potential desires of founders, answering how to find *founder-investor fit* is key for every venture firm and every venture capitalist as they think through their strategy.

Venture Firm Strategy

Beyond the focus on sectors or on stages, the key strategic decisions within a venture firm are about the people. Whom to hire? Whom to promote? Whom to retire? How is the partnership structured? Who gets to make which decisions? And many more.

Diversity across gender, race, age, socioeconomic background, and other vectors, is one of the hot-button topics influencing venture firm strategy today. Though the majority of venture firms still don't have a female partner, more women than ever became VC partners in 2019. And 2019 was also a historic year for female-founded companies, with more funding, and more female-founded unicorns than ever before. More recently, the national conversation on racial inequality and the Black Lives Matter movement has shone a light on the lack of Black VCs and Black-founded venture-backed companies. "Make the hire, send the wire" has become a rallying cry across the industry.

Generational transition is another issue that many firms are grappling with. Several factors - the decade-long bull market, many investors who have been active since the dot-com crash starting to enter retirement ages, and the new crop of younger, more diverse investors in partnerships - make this a unique moment for firms to think through transition. Benchmark and Sequoia are two of the very few venture firms that have successfully navigated multiple generational transitions. A handful of newer firms, such as First Round, Upfront, and USV, have publicly discussed the subject, as have limited partners such as Top Tier. The news that Bill Gurley is stepping back in Benchmark's new fund is one public example, but there are many more firms thinking through generational transition in 2020, with younger investors ready to take on leadership roles.

Brand - at the firm level, and at the individual partner level - is a very important area of decision-making. Andreessen Horowitz launched as a new firm just over a decade ago, and changed the content marketing landscape in venture capital. In addition to every partner actively blogging, the firm hired a content-focused team, including WIRED editor Michael Copeland and mobile analyst Benedict Evans. Firms such as Decibel, First Round, NFX, and Unusual Ventures also produce content at the firm level, but a lot of the brand-building in venture capital happens at the individual level. Twitter, blogs, newsletters, podcasts, and video content have enabled individual investors to build their brands and to try to rise above the noise in the industry. Though everyone is trying to differentiate themselves in an increasingly crowded industry of agglomerators and specialists, there can be tension between a firm's brand and an individual partner's brand, for they may not be 100% aligned. And some firms' brands are synonymous with an individual, which can make it challenging for others in the partnership to succeed.

Diversity, generational transition, and brand all put pressure on partnership dynamics at venture firms. The best partnerships are those that are aligned on principles and values, but have lots of differences and complementary skillsets. Unfortunately, that's a magical combination that is rare to have in a partnership, and that's part of what leads to difficult decisions, and to constant change in our industry. Transparency and scrutiny of venture firms is also higher than ever in today's world, and news travels faster. In the past month alone, news came out that Alexis Ohanian is leaving Initialized, the venture firm he co-founded. First Round is hiring a new partner, and opening up the process. Base10 Partners, Plexo Capital, Illumen Capital, and Precursor Ventures have launched a new effort, the VC Diversity Pledge. With venture firm strategy and decision-making more out in the open, founders can utilize this information to hone in on which investors they want to work with.

There’s a lot more to unpack here. How does the structure of partnerships and investment committees factor into strategy? Is that something that founders care about? And how does strategy impact culture, and the ability to attract and retain the best talent? Ilya Sukhar and others responded to my last essay with perspectives on how the working environment can be very different at agglomerators vs. specialists. Finally, firms’ differing strategies to find *founder-invest fit* most come to light in a competitive financing when founders have to choose between strong options. This piece by Alex Konrad describes the “two-way race between two firms, Andreessen Horowitz and Benchmark, to secure the investment in Clubhouse.” It seems that ultimately the a16z network, as well as perhaps the deal terms, helped steer the Clubhouse founders in their favor. But you can certainly envision different founders with a different set of preferences going in the opposite direction.

The Decade Ahead

Founder-investor fit can serve as a north star for firms to navigate the decade ahead.

If you believe that more diverse founders will want to take investment from more diverse investors, then adding diversity to the partnership can help find *founder-investor fit*. If a new generation of partners as leaders can better steer the firm towards *founder-investor fit*, then decision-making around generational transition can be smoother. Brand resources can be tipped in favor of the firm or of the individual partners depending on which feels more authentic, brings founders in, and wins them over.

Of course, this all requires buy in from the firm's limited partners, and requires effort on the part of general partners to be self-aware about strengths and weaknesses, and to adapt.

But this matters, because focusing on *founder-investor fit* can lead to a competitive advantage for venture capital firms over time. Craig Thomas, a director at Investure, which is a limited partner in several venture funds, states:

> In my view, venture is an iterated game where firm brands compound and the only future-proof strategy is to have a partnership or brand that appeals to the broadest group of founders at any given point. That makes diversity, brand, partnership structure, and generational transfer key inputs into finding and attracting, and accessing, the best founders.

The firms that thrive over the next decade will understand *founder-investor fit*, especially in the context of these key trends. The firms that don't will be challenged.

And the new firms that get started today with an intentioned strategy as it relates to *founder-investor fit* may just become the next big thing in the venture capital industry.

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I started *next big thing* to share unfiltered thoughts. I'd love your feedback, questions, and comments!

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