bettereveryday.vc /what-kind-of-seed-round-should-your-raise-39d78ce68bac

What Kind of Seed Round Should You Raise?

rob go

8-10 minutes

Raising capital is really difficult, no matter what anyone says about the influx of early-stage dollars into the startup eco-system. I know very strong entrepreneurs that need to grind really hard to get seed rounds done, so I definitely don't want to take away from the challenge of doing that.

But in some cases, I find that entrepreneurs have more options around the timing and amount of their first raise than in the past. Choosing between the various options is particularly challenging with the increasing atomization of seed presenting a broader variety of paths. A few common questions I hear include:

1. Should I bootstrap or raise a pre-seed?
2. Should I raise a pre-seed or "proper seed"?
3. Should I raise a seed or jump straight to a series A?

Let me talk through each one and offer my thoughts.

There are many different definitions of pre-seed rounds. But here's my definition:

> A pre-seed is a round that is NOT likely to sustain you to a large ($7M+) Series A with significant traction. It is also likely a round that is <$1M in total size. This could come from an institutional fund, angels, or friends & family.

So, the decision for founders is often one of doing a pre-seed or bootstrapping. Usually, this is a founder who may be able to forgo salary and put in $0-$250K into this business, but rarely much more.

> **My general advice is to bootstrap as long as you are practically able**. Your cost of capital at this stage is as high as it will ever be, and it's tough to find a pre-seed investor that is really aligned with you at this stage.

I think your level of conviction about your business is somewhat related to your funding strategy. If you are in "I'm going to start a new company, I'm just not sure what" stage, definitely don't take outside capital.

If you are in "I have high conviction around a problem or area, but not sure about the right product" stage, I think things could go either way. But if you do raise money, make sure that you find pre-seed capital that is aligned with where you are. You want investors that really appreciate the level of risk that exists at this point. They know that at any point, you may actually decide that there isn't a good company to be built here, and completely change course or decided to give back the remaining dollars.

> At this point in the entrepreneurial journey, your time and optionality are probably more valuable than anything else.

You want investors who support you and understand this. They won't force you to artificially chase after a local maximum around your initial thesis or bang your head against a brick wall for several years if you think a different path is better.

If you are in the stage of having some early evidence around potential product/market fit and feel ready to commit several years of your life to your company and current direction, a pre-seed round could be a good idea. Again, remember that you are making a tradeoff between ownership and control vs. the speed, relationships, resources, and intellectual companionship you get from bringing along good pre-seed investors. Those are good things, but you will also have other opportunities to get those later when your equity is worth more.

I think of the pre-seed or large seed decision as one that trades off risk for dilution.

We are still largely in a place where **raising a pre-seed round (especially one from more price-sensitive institutional investors) will yield a fair bit of near-term dilution.** We are also in a world where larger seed funds are still pretty valuation sensitive. Chances are, if you raise a pre-seed, that level of dilution will hurt, and it won't get you so far along that the value of your next round with be super high.

The risk of raising a large seed early on is that if things go ok (but not great), you may be somewhat stuck. There, you aren't in a place where you can raise a strong Series A, your existing investors will have heartburn about giving you a few more million bucks to get further, and you may not be able to attract great investors even if you can raise a bit more money. Plus, after your big seed and seed extension, you've probably raised a level of capital that will make Series A investors question how efficient your business is, and the bar for your next round will be adjusted higher for the amount of time and capital it took for you to get there.

> You should raise a large seed when you feel like there is at least some signal of product-market fit, and that you can see a path with more capital (based on real data) to really strong metrics for a Series A.

Where I see founders get into trouble is when they raise a large seed before there is some product/market fit. In that scenario, most founders tend to increase their burn too much, take longer than expected to really get traction, and then need to raise more money before they have hit a meaningful value inflection point.

My other thought is that the quality of your investors does matter. You may be able to raise a larger seed from a weaker investor or from a syndicate that is poorly aligned with you, but then notice that the very best investors say no.

> Perhaps they are just wrong, which happens all the time. But perhaps they just need a bit more convincing to get there, and it makes sense to raise a bit less and prove out more to get a great investor alongside you.

Investors definitely don't make or break a company, but having an investor that isn't great can actually be a major drag. They should be avoided unless you are desperate.

I wrote a post on this previously, but some founders are in the fortunate position of deciding between raising a large seed vs. raising an even larger Series A.

In my opinion, you should only think about raising a large Series A if:

- **You have a strong lead that is doing the majority of the round, taking a board seat, and will treat you the same as a company that is further along and raised more money.** I've seen very few situations where a "syndicated" Series A works out. These are situations where a company raises a Series A level of funding, but from a broad set of investors with no one really treating the company like a full-scale investment. It's really easy to get lost or abandoned in that scenario.
- **You know the investor and really believe she will be committed for the long haul.** This shouldn't be an effort to "tag" an entrepreneur that they think has high potential and then back away or go radio silent if things go sideways. Remember, for some large funds, even a $5-$7M check is less than 1% of their fund's capital. You want to believe that the investor cares much more than you'd think from the % of their dollars that are at risk.
- **You are ready to for the "data to speak for itself" in the next round.** Even in today's environment, there is some selling to hopes and dreams in the Series A. The Series B is sold primarily on results, with even the hopes and dreams being dependent on data.
- **Your business is one where capital is a weapon, even in the early days.** It makes sense to go harder faster. My word of warning though is that founders often think that this is true when it actually is not. Often, raising more capital ahead of where a business really is creates more risk than it mitigates.
- **You are very confident that you are one of a tiny subset of founders that can take more money than is needed, not burn more money than necessary, and motivate your team to work with a laser focus like you have much less money in the bank.** Some founders do this well — David Cancel and Elias Torres from Drift effectively ran their company like they raised

$1M for the first year, even though they raised $15M. But chances are, you are not going to have the discipline to do this.

In nearly all other cases, I'd recommend *not* jumping straight to a Series A. As my friend Hunter Walk has been saying recently, seed is a phase. If your company is in the seed phase — you're still honing your PMF and growth engine — stick with seed fundraising. Doing something unnatural will hurt more than help in the long run.