The Entrepreneur Expectation Gap

Afore

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3 Tips For Resetting Expectations & Finding The Right VC For Your Startup Stage

There has been a shift beneath the feet of entrepreneurs seeking early stage venture funding. The problem is… no one told the founders. What was once Seed stage funding, today is more like Series A. Since we launched Afore two years ago, we've seen Seed stage round sizes and valuations spiral 3X and watch companies pound the pavement for up to 2.4 years before they are able to raise a Seed round.

So in an effort to fill the knowledge gaps for entrepreneurs and develop more successful connections and conversations with VCs, we are sharing 3 lessons from top venture capitalists including partners from **Pear VC**, **Sequoia Capital**, **Freestyle Capital**, and **Fika Ventures**.

Identify Your Startup Stage By Today's Standards

In venture as in life, there is no point in living in the past. As a founder you have to deal with the investment market in this very moment and size up your startup accordingly. Entrepreneurs need not seek out Seed funding in the wrong places and hit a wall. And VCs don't need to waste cycles on meetings that go nowhere. Let's go by the numbers and take a look at the changing winds for early stage venture.

In 2011 only 4% of companies raising a Seed round had revenue. In 2017 a whopping 51% of companies raising Seeds had revenue. That's a massive jump and is only trending higher. Seed stage investors demand significant traction and material revenue, they demand real product-market fit before they would invest. As we said earlier, Seeds these days are essentially A rounds.

> *Percentage of Seed companies with revenues; 4% in 2011 vs. 51% in 2017. Data from Wing VC.*

So be real about where your company is in the earliest cycles of startup gestation and growth. If you're generating revenue, you're likely ready for a Seed round. If you are still finding your footing, identifying the perfect customer and hone your product… Pre-Seed capital is going to make the most sense for your business.

Forget The Labels, Seek Out Your Best Partners

There's something to be said for following your gut, but the best instinctual reactions come from a backdrop of experience and ingrained knowledge. As more venture capital firms aim to uniquely differentiate their offering to entrepreneurs, it's critical to look past the labels and see through to the best partners that will be right for you and your stage of business.

At our inaugural Pre-Seed Summit, Freestyle Capital Partner Jenny Lefcourt recounted a recent round of startup fundraising she wanted to lead, but couldn't stay involved as the valuation began to soar via another VCs offer. Jenny, a founder herself, had a heart to heart with the entrepreneur, whose startup was pre-revenue, and took off her VC hat for the moment. Her and her team at Freestyle explained to the founder that it's about fit and partnership. She won the investment and helped shed light on what a great partner a VC can be. Jenny said, "You have to be really careful as a founder of where you get your money from. You want it to be the right check from the right person. So that they're thinking about you 24/7. Get the hardest, smartest working capital for your stage to extract the most value."

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Eva Ho, General Partner at Fika Ventures, shared that money from the wrong partner can be a massive risk for startups. She said, "There's so much capital that you could actually get Pre-Seed money from a large firm. We treat our Pre-Seed investments the same as we treat our Seed investment — it's not an option call. Outside of Sequoia and Lightspeed, who do Seed really well, a lot of the big firms now are just doing all stages and it's actually quite dangerous money. If you get it from the wrong people, who don't have the time to dedicate to growing you at the stage that you need to be grown at."

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It's also important to avoid falling into the trap of a misidentified round. Pejman Nozad, Founding Managing Partner at Pear VC, warned against investing based on previous check sizes and instead said to focus on stage of company development. Pejman said, "With so much capital in the market, the biggest effects are on the earliest stages and the biggest challenge I see is that we are mislabeling rounds for companies by the amount they are raising now or that they have raised." Pear's guiding philosophy is that every company goes from stage zero to one, and that check size will vary based on the individual case. He concluded, "There are two factors, one being users who love the product and second is how to create an efficient growth engine. It has nothing to do with the money that was raised already, it's about the stage."

So be mindful of finding the right partner for the right moment in your company's development. As an entrepreneur, you'll want to be armed with a VC ready to do battle to assist you in protecting and growing your startup.

Smaller Checks Can Make Better Sense

When it comes to taking on venture capital for your startup, don't be distracted by the size of the check. Sure, it's validating for what your building and ego-boosting for your overworked soul, but in the long run it may not be the best business decision for you and your employees.

Alfred Lin, Partner at Sequoia Capital and former COO/CFO at Zappos, discussed this at our Pre-Seed Summit. He said, "Don't be attracted to having large financings and large rounds. Those are vanity metrics — build your business for the long run. I think that's very important. The best companies are built with very little capital. Little capital can mean less dilution. Think about yourself as a shareholder of the company too and look at your level of ownership at every single round. It will diminish as you're taking more financing." So just because a check is big, doesn't mean it's smart money. Alfred noted that this doesn't mean you shouldn't raise at the level that your industry is raising, because sometimes it is a market share game, but concluded with "the most capital efficient company in your industry will do the best for shareholders — which is yourself, because you should be one of the largest shareholders in the company."

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Jenny Lefcourt said that the wrong valuation can shut down opportunities to find the best partners and grow the business in the right ways. A big check could feel good in the immediate, but can put founders in a negative position as they continue to socialize their valuation with potential future investors. She explained, "I have had founders who know they can get higher valuations. But they don't optimize for valuation — they optimize for getting the best partner and raising the right amount of money at a fair valuation. We want to work with founders who are long-term focused versus short-term focused."