Chapter 5: Risk and Return

Venture Capitalists

Tong Minh Phuong
MA5N0202
Content:

1. Definition of venture capital
2. Example of venture capital
3. Venture capitalists’ expectation
4. Trend in venture capital
1. What is venture capital

- Venture capital is a form of **private equity** in which capital is raised in **private markets** as opposed to the public markets.

- Venture capital is usually invested in start-up and small companies that are believed to have long term and rapid growth potential.
  - For start up and small businesses, sometimes it’s hard to access capital markets (stock market), venture capital is an essential source of money.

- The riskiness of venture deals demand generous returns on capital.
About three-quarters of venture-backed firms in the U.S. don't return investors' capital. Many company backed by venture capital fail, but when they win, they win big.

Youtube’s sale to Google for 1.65 billion in 2006
Skype’s sale to Ebay for 2.6 billion in 2006
Google, Genertech and Apple were originally funded by venture capital.
3. Venture capitalists’ expectation

Venture capitalists are generally wealthy investors seeking exceptional returns, investment banks, venture capital firms and other institutions.

“If the capital markets return 8% on average, then venture capital has to earn a substantial premium over that. So you will need to have expected returns of 20% to 25% and actual returns of 17 – 18%” (David Mathias – managing partner of Carlyle Group)
4. Trend in venture capital today

Firms are likely attractive to venture capitalists today:

- Environmentally friendly
- Health care
- Medical research
How can the venture capitalists capitalized on their investment?

- Venture capitalists take on the risk of financing risky start-ups in exchange for equity – an ownership stake – in the companies they invest in. They usually get a say in company decisions. If the company they invested develops, venture capitalists expect to earn big money from dividends and the increase in stock’s price.

- In order to make the decision on the company funded, venture capitalists analysis business plan proposed by companies seeking for venture capital, evaluate risk and earning potential of new businesses.
Thank You