

This is the third in our Ask Adam series where venturing expert Adam Caper, managing director of Synchrony Venture Management, answers the industry's questions. To comment or ask further questions, anonymously if required, email: [jmawson@globalcorporateventuring.com](mailto:jmawson@globalcorporateventuring.com) and [adam\\_caper@synchronyvm.com](mailto:adam_caper@synchronyvm.com)

# Refilling the till without upsetting the apple cart



**Q** Our company has a goal for the total amount of cash it wants to tie up in its corporate venturing investments at any given time, and since we get most of our strategic value fairly early in the investment cycle, we would like to recycle that cash so we can pursue new strategic opportunities. Any ideas on how we might exit deals without taking a huge hit and disrupting our portfolio companies and syndicates?

**A** This question goes right to the heart of an innate conflict between CV investors and portfolio company partners – they invest for different reasons and with different time horizons.

The orthodox answer is a variant of “tough cookies” – once in a deal, all investors are expected to take the same ride. There are a couple of reasons for this. The first is the reciprocal of the validating effect of a CV investment – if a strategic is seen leaving the deal, it can be seen as a signal that things are not going well. The second is a bit of VC chauvinism – they (understandably) feel that if you want to play on their turf, you have to play by their rules.

But VC investors and early-stage company boards are starting to see the logic of allowing strategic investors to cycle in and out based on the strategic lifecycle rather than the longer investment one. For one thing, a disinterested strategic can be somewhat gangrenous to the body of the start-up, a dead limb better amputated than dragged around stinking up the joint. For another, there is an inherent liquidity premium in the trading of private company shares – that is, the seller has to accept a discounted price for his holdings, which represents a profit opportunity for someone. Third, there may be “room” for only one or two strategic investors, so why not recycle the shares once the relationship has created value and use them to do the next strategically relevant deal?

The solution lies in understanding both

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the potential problems that an early exit might create for your partners, as well as the advantages to them by figuring out a way to make it work.

For example, one of the major problems created by having an investor leave early is that it sends a loss-of-confidence signal to other stakeholders. But if the disengagement (either as an investor or a partner) is baked into the process at the outset, there is no disruption. It becomes a normal – perhaps even positive – developmental milestone. So make it part of the initial negotiation and explain the advantages to your partners. They will want some means of controlling the process (timing, the situation of the portfolio company and the identity of the buyer will all be important to them), but as long as they can ensure that the means and timing pose no threat, they will be willing to look at the benefits.

Still, an early exit is something of an unorthodox concept to sell, and getting buy-in requires understanding the concerns of the other side and anticipating them. Remember that regardless of equity ownership, there is likely to be continuing business between your firm and the start-up. Make sure the sale of equity does not affect that partnership. Anticipate a need on the part of the start-up's board to control who they allow into their ownership syndicate, so ask for nothing that would run foul of that need. Accept the liquidity you seek has value, and that value will most likely be expressed as a discount to the current share price (you will still make a financial return but will give up some of the upside to facilitate the transaction).

In general, as with all of my advice, put yourself in the other guy's shoes and figure out win-win solutions in advance. You may not get what you want – that is always a risk – but you will have a conversation in a way that fosters the relationship and sets a tone of understanding rather than triggering a “who the hell does this guy/gal think s/he is?” reaction. ■

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