MassEcon
Location is everything.

Venture Capital Roudtable Executive Summary – October 28, 2010
Nutter McClennen & Fish, 155 Seaport Boulevard, Boston MA

Anchors:

Name	Position	Representing
Alex Glovsky	Partner	Nutter McClennen & Fish
John Harthorne	Founder & CEO	MassChallenge
Jon Karlen	General Partner	Flybridge Capital Partners
Jack McCullough	Client Relations Director	KPMG

Anchors Opening Remarks:

Alex Glovsky began the session by noting that though venture activity has weakened in recent years, there is still activity in the marketplace. From the legal perspective, he has seen the economic downturn hit the venture community as much locally as nationally and worldwide. The industry has since bounced back to show some recovery in the pace of venture investment from Q1 2009 to date. In Q2 2010, $518 million was invested in early stage startups in MA. These gains come in the wake of more judicious practices of VC firms; volatility and retrenchment are increasingly evident in the venture experience for entrepreneurs. Venture firms are taking a far more conservative approach than many of the companies they have been interested in. He sees innovation continuing at a strong pace but the spark for that innovation, in the form of capital, is in transition.

Jon Karlen noted the hardships felt throughout the industry as the venture capital firms gained less than they invested in 2010 for the first time since 2003; the venture community has shrunk in both the number of professionals and amount of activity. This decline in activity was caused by excessive risk taken on by venture capitalists in the dot com era resulting in excessive losses. VC professionals have adopted a prudent approach in selecting startup companies, maintaining a risk averse strategy. At the same time, Jon highlighted that VC is cyclical and VC firms and startups alike are becoming more accustomed to conservative yet effective investments. As a testament to this theory, angel investors have become more prominent in recent venture activity, a reflection that companies are requiring less capital to get off the ground. Jon reminded the attendees that Massachusetts remains one of the most popular states to start a business citing the state's exceptional research capabilities and university talent.

John Harthorne stressed that VC firms value a company that can boast a degree of consumer interest in its product or service. In his experience with 110 startups at MassChallenge, consumer product and retail startups achieved heightened success by highlighting a tangible consumer base interested in their product. Furthermore, the key to creating a successful consumer product is to maximize personalization while retaining a manageable cost level. Regarding the increasingly evident risk averse practices of VC firms, tier funding is a useful tool; more positive results have derived from multiple levels of funding requiring startups to demonstrate continuous improvement throughout the inception and growth of the company. He concluded by mentioning the growing popularity of shared goods in the marketplace. Companies like Zipcar and Relay Rides (car sharing) continue to grow as consumers increasingly value companies with sustainable initiatives.

Jack McCullough viewed the decrease in VC funding in a positive light since many companies – when capital was plentiful - received funding from overanxious firms who failed to conduct the necessary due diligence. Jack used the analogy that though VC firms are getting less at bats, the batting averages in the industry are much higher, which significantly benefits the economy in the long term. In Jack's view, the increased investment by angels could harm the economy as some of these investors lack the broad knowledge base of VC firms and tend to give money without conducting proper research. He agreed with Mr. Harthorne that increased accountability is evident in the industry, as funded companies are required to produce results after the first round of capital to gain the second round. Venture capitalists are becoming skeptical of articulate entrepreneurs focusing on expectations rather than quantitative business and consumer facts.

<u>Q&A</u>:

Q – As many successful Massachusetts startups tend to move out of state (e.g., Facebook) , how can we keep these companies in state for the long term?
A – Jack McCullough: Educate entrepreneurs of the benefits of staying in Massachusetts; boast about the Commonwealth's many advantages.

John Harthorne: Though capital is scarce at the moment, sell entrepreneurs on the other inexpensive resources readily available in the state like office space. Because the economy will realize an upswing in the near future, the time to capitalize on low rates and start a business is now.

Jon Karlen: Human capital in Massachusetts is among the best in the country. Young entrepreneurs have the whimsical idea that bringing their company out west will result in a million dollar check over lunch with an executive. The California culture emits a "dreaming vibe" that draws young companies out of Massachusetts and we need to replicate that here.

Alex Glovsky: Nurturing the young entrepreneurs is important; the more we give to them, the more they will give back to us and consequently, stay here. Donating time and making friends enhances the probability of companies doing business in MA.

Greg Hoffmeister: Within the last year and a half, a huge change is evident in the early stage ecosystem of young people with organizations like Bostinnovation, Greenhorn Connect, and DART Boston. These organizations are gathering to promote innovation in Massachusetts more now than ever before. Had these organizations been here when Facebook was created, the company may have been more prone to stay.

Bill Rurode: Massachusetts has a great opportunity going forward because it retains the most important part of business development, knowledge. Though manufacturing is increasingly outsourced from overseas, the base of knowledge in Massachusetts ensures that successful companies will continue to grow in state for years to come.

Q – Is Massachusetts well-positioned for the solar/green sector?
A – Jack McCullough: Domestically, Massachusetts is well suited to become a leader in the industry. The government is certainly doing its part to support the industry through subsidies and tax credits. We have to be really patient as consumers and companies begin to accept new clean energy alternatives. Robust revenues and profits in the industry may be five or six years down the road, which is a long time for investors looking to make a profit.

Jon Karlen: Big ideas in clean energy are coming out of university labs in the state. A combination of technology from universities, government policies and venture capital result in a hotbed for green technology in the state. The largest issue facing these companies involves the ability to produce at a sustainable price. Plenty of innovative ideas exist in the clean tech sector but the majority of companies will struggle to keep production costs low, especially as government subsidies run out in the future.

John Harthorne: Massachusetts is good at R&D which is the hard part of the equation. If the state continues to excel in R&D, other elements of the green initiatives should fall into place. Also, 40% of the population is within a seven hour drive from Boston; a huge percentage of the consumers in the country are very local, representing a huge opportunity for these green companies to market their product.

Ryan Weber: The R&D will stay local with a lot of these companies but MA is geographically challenged to house manufacturing. These clean tech companies need ample light, water, land etc. and some of these resources are more easily obtainable in the Texas, New Mexico and Arizona.

Q –What will it take to bring companies to Boston's innovation district?
A – Matt Harvey: We are seeing more of a trend of companies moving back to urban settings like Cambridge or downtown as opposed to moving out to the suburbs. The current public transportation infrastructure in Massachusetts creates a challenge for companies to move out to the suburbs.

Greg Hoffmeister: Companies like to be around other companies with similar practices, so it is important to have a company to "lead the pack" and generate interest from other companies to the area.

John Harthorne: The MassChallenge initiative will help spark interest in the area as a multitude of startup companies were housed in the seaport area as part of the competition. The technological ecosystem coupled with exceptional law firms in the area make for the ideal environment to develop startup companies.

Greg Hoffmeister: Companies like to be around other distinguished companies; we need pioneers and leaders to inhabit the area to set an example. Cheap rent and low cost financing is imperative as new companies don't want to be spending valuable VC dollars on office space.

Q – What is the state's/MassEcon's role in helping young companies stay and grow here?

A – Jon Karlen: The goal is to help these companies access all the resources necessary to get started. Publicizing these companies provides legitimacy, capital allows companies the financial freedom to accomplish goals, and oversight and guidance ensures that young entrepreneurs will avoid common mistakes.

John Harthorne: Although gaining funding from the state for MassChallenge in such a tough economy was originally thought to be one of the hardest endeavors for the organization, state officials were surprisingly open to funding our initiatives, proving the state's support for young companies. Also, organizations like MassEcon make it easier for MassChallenge to procure young entrepreneurs to the state. When MassChallenge first began, we utilized MassEcon's website for statistics concerning the economic condition of the state.

Q – Should Massachusetts stay a startup economy or focus on retaining successful companies?
A – Ed Walsh: There is nothing wrong with R&D and brainpower staying in Massachusetts, but as technology moves along, the number of companies in state decreases.

Lowell Richards: The labor force for manufacturing is well below what is needed for growth companies to maintain their manufacturing operations in state. More laborers and space is needed for sustained growth which draws companies to larger states with excess land. We should be targeting companies that want manufacturing to remain in close proximity to R&D. We shouldn't be discouraged by companies leaving the state because not all companies are a good fit to remain in MA, we should concentrate on retaining the companies that are a good for the region.

Jack McCullough: Massachusetts startups tend to get bought up quickly in the state by large companies with operations across the country and internationally. Because these large companies make early offers that these small startups can't refuse, the startup's employees and operations are relocated to different regions at the discretion of the distinguished company.

Susan Houston: It doesn't need to be an either-or proposition in terms of being a start-up economy vs. keeping large companies here. We have a diverse economy in a compact, well-connected state. We want to keep companies here through all stages of their life cycle, and demonstrate that a company can get its start in Cambridge and expand in other regions.

Attendees

David Begelfer	NAIOP MA
Rimi Chakraborty	T3 Advisors
Matt Harvey	CresaPartners
Greg Hoffmeister	T3 Advisors
Annamarie Kersten	MA Office of Business Development
William Luster	North Shore Alliance for Economic Development
Kevin Quinn	Dacon Corporation
Lowell Richards	Massport
Bill Rurode	RBS Citizens, N.A.
Art Robert	MA Office of Business Development
Michael Scott	Nutter McClennen & Fish
Edward Walsh	Mira Development
Ryan Weber	Thompson Hennessey & Partners

MassEcon Staff

Susan Houston
Mary Duggan
Derek DeAndrade