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The investor and startup relationship goes both ways – you must woo each other

Investors have traditionally been seen as intimidating entities who entrepreneurs must dance for, cap in hand, to raise funds. But times have changed rapidly.

Dealroom data alone shows European startups raised €43.8B in H1 2021 – more than the €38.5B secured in the entirety of 2020 – which demonstrates that growing companies have many options to choose from, despite a tumultuous year.

Startups shouldn't get complacent though. Increased amounts of investment on the market means more startups competing for their share. Capital may be the holy grail, but entrepreneurs would do well to think long-term to ensure the investor they're courting has their best intentions at heart and will help them achieve their full potential.

On the market

Starting out, it's important that both the investor and 'investee' determine they're a good match. These parties are essentially embarking on a marriage; the only difference being that eventually you know that both parties will go their separate ways. The earlier the stage of the business, the longer that relationship will be, so it's important *that VCs* and portfolio companies have shared interests. Over time this relationship, like a marriage, will be tested to ensure alignment is maintained.

Before tying the knot, here are some matchmaking considerations for entrepreneurs:

Finding that spark

The relationship between portfolio company and investor should firstly begin with both parties understanding what the other is bringing to the table. In our experience, a short call to lay the groundwork and get to know each other is the most effective practice, rather than diving headfirst into a long, formal pitch.

This approach achieves two things. It allows the investor to inform the founder on how they operate and it provides the opportunity for the founder to detail what they want from their investor, both in terms of support and investment amount.

Long-term commitments

An all-too-often overlooked question a founder should ask an investor at the start of the relationship is "what type of return do you desire and when do you expect to see it?" In all the conversations we've had, companies typically fail to ask what we want as an investor.

Some VCs expect a 10x return, but if a founder wants to keep a company forever then that will require either incredibly significant scaling up or taking a lot of money out of the business to pay investors back. We have a very specific mandate for our fund and that's standard for all firms. Every investment has a target, so companies must be direct and ask upfront – even if it seems uncomfortable. Investors have a duty to be transparent, but entrepreneurs should be certain they're asking the right questions.

A bad date

Selecting the wrong investment can be one of the biggest downfalls for a portfolio company. Some lead investors may insist they get priority in follow-up funding without willingness to co-fund with others, purely on the basis that they will secure the most desirable tax returns with little regard to what is best for the business they're supposed to be helping.

In scenarios like this, founders must be bold. If they take a step back and think about just how time consuming it is to raise funding – which can be months in the making – it really makes no sense to rush into decisions if there are any red flags. Entrepreneurs shouldn't let themselves be bullied and it takes a great deal of courage to turn investment down. Investors can have a great deal of respect for those who put themselves and their business first.

Timing is everything

But how soon is too soon for investment? The best way is to work backwards. Founders should acknowledge there's a long process between starting as an early-stage company to becoming a high-growth business with defined scalable metrics – which is what VCs will want to see.

Timing is one piece of the puzzle. Another is about deciding where the money will be raised and the typical approach will be friends and family funding for an idea, building it out further, raising some more money to scale, and so the cycle continues. There's no such thing as too soon to raise money, but more a case of matching the stage of business to the most appropriate type of funding.

Happily ever after?

The obvious reason to go to an investor is to secure funding that will help business growth. However, founders should question VCs about what they can provide outside of investment. This is another way to ensure the right partner is being chosen for the journey.

In our case, we're an active fund. This means we're accessible, communicative and have regular monthly calls with portfolio companies to ensure they're on track with their objectives. This presents the chance for them to share any problems, which we can brainstorm through as a team, or provide proactive advice if we've witnessed similar challenges before.

The updates are powerful because we can determine a company's performance based on four key things – sales, product, cash flow and support requirements – helping accordingly. It's not about chastising entrepreneurs: this regular call lets the founder receive some external perspective from someone that isn't engrained in the day-to-day operations, allowing us to add value and achieve a better return.

Of course, on the flip side, some founders prefer a more hands-off and passive approach from VCs and would rather push for growth milestones alone without any additional support. There's nothing wrong with that; this approach will work for some but not others. In any case, it's important to recognise that investors can offer more than bank account top-ups if so desired.

The marriage between investor and investee can be a challenging one. However, when the right match is found, it can help establish a positive relationship that is both beneficial to the investor and the business.

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