

# Tales of the Venture Specialists



September 16, 2005  
(Excerpt by Joshua Jaffe)  
-- While traditional venture capital firms diversify their capital across stages and sectors, the new funds are much more narrowly focused. These new specialists are drilling even deeper into information technology.

Partners at these firms and other specialist firms profiled later in this story argue that these investment niches offer plenty of different targets and claim that their industry focus furnishes them with a competitive advantage over generalists that lack industry expertise or deal flow in a particular area. And they do have their champions within the venture industry.

"This matches with the maturity of the market," says Paul Frankel, a lecturer at Stanford University who is raising a Sausalito, Calif.-based subordinated debt fund called Ecosa Capital that will concentrate on sustainable businesses. "It's tougher to find the best deals, so firms are becoming more highly specialized."

The danger, of course, is what happens when the markets these new firms are focused on experience an inevitable down cycle or simply don't pan out at all. Internet-only funds such as Internet Capital Group Inc. of Wayne, Pa., were shattered when a disproportionate number of their portfolio companies had to close. And wireless-focused funds such as Argo Global Capital of London found out the downside of a narrow sector focus during the telecommunications boom and were forced to fine-tune their investment focus last year.

Yet even if they achieve success, their long-term viability is open to question, since the very segment they set out to exploit may change so dramatically over the life of their funds that their investment model (or the business models of their portfolio companies) no longer makes any sense. How events in any given sector unfold are obviously unknowable, but a look at the different funds now operating may offer some glimpse of

possible directions. Also bear in mind that perhaps the key to the VC specialists' success may be to use their niche areas as a marketing tool to raise money and attract the best entrepreneurs but then interpret their mandate as widely as possible to diversify their portfolio.

Another older specialty firm is Blueprint Ventures. Managing partner Bart Schachter says the South San Francisco, California-based firm's strategy is to work with corporations to spin out their assets when the unit is still at a pre-revenue stage. Since closing its first fund in 1999, Blueprint has worked with companies such as Microsoft Corp. and NEC Corp. and completed 13 intellectual property-based spinouts with the \$200 million it has raised in two funds.

With the sale of portfolio company Sarvega Inc., a Chicago-based XML Web security startup, to Intel Corp. in August, Schachter believes his strategy provides Blueprint with a higher success rate than other

venture capital firms.

"Ten percent of VC-

backed startups succeed, whereas 60% of corporate IP spinouts do," he says, pointing to the reduced capital and technology risk as well as to the ability to receive immediate customer feedback.

He cites Covad Communications Group Inc., a digital subscriber line services company that Intel spun out when Schachter was at the microprocessing giant, as an example of the potential for Internet protocol-based corporate spinouts. Others include Xerox Corp.'s Palo Alto Research Center Inc. spinouts Adobe Systems Inc., 3Com Corp. and PlaceWare. Intel Capital veteran Schachter adds that it's possible to get top-notch technology out of corporations by focusing on their non core assets. "The stuff may be good, just not core," he says. "If Microsoft comes to us with an operating system, we're going to be suspicious."

