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Venture Capital Keeps Flowing in Q1

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Venture capitalists are preparing their exit strategies.

That's one reason why VCs focused on fashion or the world of fashion technology have committed $150 million in follow-up investments since the beginning of the year. And while initial public offerings are the sexy exits that dreams are made of, the acquisitions front is where the action is at for most emerging firms that have garnered VC investments.

David Freschman, an early stage venture capitalist and cofounder and chief executive officer of fashion technology networking group FashInvest, said, "VCs are coming in for the Series B round to provide expansion capital. These funds are used right now for market expansion, customer acquisition and technology enhancements. Investors are looking to exit [their investment] through an acquisition."

According to Freschman, angels and early stage investors typically feed the Series A rounds. In Series B rounds, existing investors up their investment and bring in new partners because capital is necessary for an exit. That's because the still relatively young firms require more capital so they can continue building on their growth trajectory.

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Karen Griffith Gryga, managing partner at accelerator Dreamit Ventures, and cofounder and chairman of

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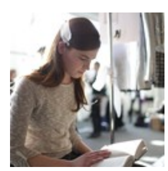
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FashInvest, said, “The basic venture capital model has always been about feeding the winners, and that’s even more so today than ever before. The first round investments are about derisking and proving the model. Every early stage venture capital firm has to be prepared with reserves in capital for follow-up investment because [one’s] portfolio wins when [one feeds] the winners.”

She said it’s really the second round investment decision that can be the hardest one to make: “Knowing when to stop investing in a portfolio company of yours is tough. It becomes like your child and it takes discipline to learn when to stop.”

At the WWD Digital Forum last month, Carly Rosenberg, vice president, e-commerce marketing for Ann Taylor and Loft, said “big data” is a 2013 trend for digital marketers. Rosenberg was referring to more personalized communications between retailers and their customers, but VCs also have their eye on operations that have substantial data assets.

Generally “big data” refers to technology platforms and applications that aggregate all kinds of unique information for different purposes.

Some of the firms that have raised another round of funding this year so far suggest that data analytics platforms are where many VCs are placing their bets. That shouldn’t be a surprise — CB Insights said Monday that firms in the big data sector have received $4.9 billion in funding since 2008.

According to Bruce Dunlevie, general partner of Benchmark Capital, which led the $18 million Series B funding for shopping analytics firm Euclid, “Physical retailers finally have an easy-to-implement, scalable solution for determining the effectiveness of their marketing and operations.”

Josh Goldman, general partner at Norwest Venture Partners, which led the latest $15 million Series B round for customer service metrics firm Stella Service, said, “The company’s proprietary data offering provides valuable, objective insight for measuring, benchmarking and improving customer service, and it has already proven to increase sales conversion for merchants.”

Other firms fueled in part by their use of social media platforms such as Julep and StyleHaul closed on new rounds of financing, while a concept such as Rent the Runway in a sector where there’s no other competitor has closed on a Series C round of funding.

So if these are the firms whose business model have passed investment muster from the VCs, what’s next?

Griffith Gryga said many firms are currently working with their portfolio companies on building a dual exit strategy. That’s why one often hears a company executive or investor stating that the emerging firm has “multiple exit options, with the potential for an initial public offering,” she said.

Still, exits in the industry are more often than not dominated by M&A activity. “There are two inflection points when it comes to exiting an investment. One point is early in the company’s development. These are the technological acquisitions we’ve seen more of in the past couple of years,” she said, explaining that these firms are at the life stage where it makes more sense to exit early, even though it may mean a smaller return on one’s investment.

The other inflection point is when a company shows there’s some momentum on the revenue development side. These are the firms that get acquired later, and sometimes go the IPO route.

The IPO route is rare, noted Freschman, who pointed out that the “costs of doing an IPO are extraordinarily expensive for small emerging companies. The regulatory issues connected with the Sarbanes-Oxley Act require millions just to get yourself in shape to go public.”

One notable exception could be Rent the Runway, the Web site for renting designer dresses and accessories. The company has closed on a $24.4 million Series C Funding round, and has raised thus far $55.4 million in the aggregate since launching in November 2009.

Scott Friend, managing director at Bain Capital Ventures, which has invested in several rounds of fund-raising for the rental firm, said, “Everyone is more bullish about its long-term prospects. Performance has been so good and the operating metrics keep improving.”

He explained that one benefit is that the model doesn’t have any competitors, but it does require a lot of

capital since it has to build from scratch the technology platforms tailored to the specific needs of the business.

"The only reason to invest in the system to improve the operations is because we all have conviction over the scope of this business opportunity," Friend said, explaining that "we see how consumers shop. We see how they interact with luxury and fashion. That's exciting for us."

While Friend acknowledges that one never knows for sure, he predicts that Rent the Runway will go the IPO route rather than an investor exit strategy via an acquisition.

According to CB Insights, last year 2,277 private technology firms were acquired globally, with acquirers paying a total of $46.8 billion for the deals where the acquisition price was disclosed. The majority of the acquirers, at 94 percent, were strategic buyers, such as Google and Facebook. As for acquisition price, CB's research said "more than 50 percent of deals are less than $50 million and more than 80 percent of the acquisitions are less than $200 million."

While a Google could be the dream exit for technology platform firms and those in the "big data" sector, fashion businesses could be the target of traditional retail companies, such as Nordstrom Inc.'s February 2011 acquisition of flash-sale site HauteLook Inc. in a stock deal valued at up to $270 million.

FUND-RAISING ROUNDS IN Q1

AMOUNT	COMPANY	WHAT THEY DO
$30M	LIVING PROOF	TECHNOLOGY-BASED BEAUTY COMPANY.
$24.4M	RENT THE RUNWAY	ONLINE DRESS AND ACCESSORIES RENTAL SITE.
$20M	FARFETCH.COM	E-COMMERCE SITE CONNECTING INDEPENDENT FASHION BOUTIQUES.
$17.3M	EUCLID	SHOPPER ANALYTICS FIRM FOR BRICK-AND-MORTAR RETAILERS.
$15M	STELLA SERVICE	CUSTOMER SERVICE METRICS FIRM FOR ONLINE RETAILERS.
$11M	FINDTHEBEST	DATA-DRIVEN COMPARISON PLATFORM.
$10.3M	JULEP	SOCIAL APPROACH TO MULTICHANNEL BEAUTY BRAND.
$10.1M	AHA LIFE	LUXURY SHOPPING SITE.
$6.5M	STYLEHAUL	ONLINE FASHION AND BEAUTY VIDEO COMMUNITY SITE.
$4.75M	STITCH FIX	PERSONAL STYLING SERVICE RELYING ON DATA ANALYTICS AND ALGORITHMS.

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