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FINANCE

The New Face Of Venture Capital

VC firms now prize dealmakers with experience -- not newly minted MBAs

It was like a rerun of the heady days of the late '90s. In March, more than 70 venture capitalists from around the U.S. were fighting for a piece of CipherTrust Inc., an e-mail security startup outside Atlanta. Partners from one well-heeled VC firm without an appointment even camped out in the company's lobby, hoping to buttonhole an exec. So when it came time to decide whose money to take and which investor to add to its board, CipherTrust could have chosen any number of veteran VCs. But it picked Asheem Chandna instead.

Asheem who? If the name doesn't ring a bell, you're forgiven. The 40-year-old had begun his career as a VC at San Mateo (Calif.)-based Greylock just six months earlier, after seven years as an executive at Check Point Software Technologies Ltd. (CHKP). He's one of a new breed of VCs who are arriving at the top firms after logging in years as high-tech execs, entrepreneurs, or apprentice VCs. "The days of bringing an investment-banking analyst into the firm have gone by the wayside," says Dave Barry, managing editor of *Dow Jones Private Equity Analyst*, an industry newsletter. Gone, too, are the newly minted MBA graduates who start as partners.

These VC newcomers are part of a sweeping turnover in venture-capital personnel. Just in the past year, Kleiner Perkins Caufield & Byers, Benchmark Capital, and Sevin Rosen Funds have revamped their partnerships. Since 2002, Battery Ventures, a star of the late-'90s telecom boom based near Boston, has shed four general partners and promoted four associates to replace them. Battery's crosstown rival, Charles River Ventures, has lost three partners and added four.

"THE 3 A.M. SWEATS"

Firms often change partners when they raise money for a new fund. But this year the game of musical chairs is playing faster than usual. Roughly half of all firms are soliciting funds, twice as many as usual, says Steve Baloff, a partner with Advanced Technology Ventures in Palo Alto, Calif. That's because firms waiting out the bear market began going back to investors last year when the stock market started to rise.

The turnover at established firms has also bred new competitors. Last year, Terry Garnett and

David Helfrich left Venrock Associates and ComVentures, respectively, to form Garnett & Helfrich Capital. As they raised their first fund, they found themselves competing with their former firms for two investors: Harvard and Stanford universities. In the end, each school invested with the new firm instead of the established ones, Garnett says. Harvard and Stanford declined to comment on their choice.

With so much money now chasing so few good deals, VC firms are seeking new partners who can bond with company founders. There's as much as $80 billion in uninvested venture capital available, yet the industry is on track to invest just $20 billion this year. "Because the business is tougher today, an individual's ability to identify with the entrepreneurs is very important," says Rick Frisbie, founder of Battery Ventures, which promoted an entrepreneur, Roger Lee, to partner in July.

Lee cut his teeth at Corio Inc. (CRIO), a computer-services provider he co-founded, before joining Battery in 2001. "I rely on my experience as an entrepreneur," he says. "I've paid payroll out of my back pocket, and I've had the 3 a.m. sweats." That background helped Lee cement his first deal at Battery. Together with partner Mark Sherman, Lee pursued an investment in security appliance maker Neoteris, which was raising $17.5 million last year. "Because [Roger] has been an entrepreneur, he can relate to you as an entrepreneur," says Krishna Kolluri, Neoteris' founder. Battery was the only new investor invited to contribute funds. Then, in December, NetScreen Technologies (JNPR) bought the company for $265 million.

Another newcomer at an established firm is Bill Tai, who joined Charles River to head its Silicon Valley office two years ago and exemplifies the new style of venture investing. In the wake of the technology-stock meltdown, Charles River decided to slash its $1.2 billion fund to $450 million and bid farewell to all but one partner at its California outpost. With a smaller investment pool, the firm needed someone who understood that less is more. "My model has always been to invest in three- or four-person teams" at low valuations, Tai says. "That was anachronistic in the bubble." Since joining Charles River, he has made five investments in wireless, software, and semiconductor startups valued at an average of $5.7 million each before he funded them. The startups' common theme: an ability to win customers without having to spend gobs of money.

At 42, Tai is an elder statesman among the new hires. Previously, at Institutional Venture Partners in Menlo Park, Calif., he funded chipmaker Transmeta Corp. (TMTA) of Santa Clara, Calif. The company had a spectacular initial public offering in 2000 -- rising 67% to close at $35 a share on its first day of trading -- but has since seen its shares fall below $2 apiece. The experience steeled him for his job at Charles River. "The firm was looking for someone who had experience throughout the cycles in venture capital, including the tougher prebubble era," Tai says. "They recognized that we may be back in that kind of environment for some time." Certainly the firms that succeed in this environment will be the ones that choose their next generation of leaders carefully.

By Justin Hibbard in San Mateo, Calif.