



Cromwell Schmissey LLC

Information and Observations on State Venture Capital Programs

A Report for the U.S. Department of the Treasury and
Interested Parties in the State Small Business Credit Initiative

**All State Conference Call
Report Overview
March 27, 2013**

Report Purpose and Positioning

- The “Information and Observations” Report was written to serve as a discussion document with the following objectives:
 - 1. Provide a snapshot of SSBCI state VC programs to better understand:**
 - Geographic distribution of programs
 - Capital deployment models utilized
 - Investment stages targeted
 - Unique program qualifiers applied
 - 2. Encourage discussion and analysis on important topics:**
 - Geographic availability and accessibility of equity-based risk capital
 - The role(s) of government in capital markets and innovation ecosystems
 - The comprehensive features and benefits of SSBCI related to VC programs
 - Emerging best practice and “best principles” implications from SSBCI
 - Recommendations for path forward and improving industry standards

Salient Points

- **SSBCI is unique among federal capital formation initiatives.**
 - Allows flexibility for states to identify small business financing needs and design customized capital deployment models within a broad implementation framework, thereby providing:
 1. **Critical funding to stand up and/or strengthen state programs**
 2. **A meaningful demonstration of capital formation policy**
 3. **An active forum for program reviews and knowledge sharing**
- **State venture capital programs created or supported by SSBCI are diverse with respect to:**
 1. Capital deployment models
 2. Targeted stages of business development
 3. Application of different “qualifiers” for small business investment
- **Well-designed state venture capital programs can help address market inefficiencies and stimulate private investment.**

The Economic Development Challenge/Opportunity

- **State policymakers looking for more efficient and effective approaches to economic development.**
 - **SSBCI supports states acting as “laboratories of innovation”** for capital formation program experimentations;
 - **SSBCI can address market imperfections** by building small business investment capacity and “priming the pump” for private investment.
- **Leading states increasingly focus on innovation capacity building for a comprehensive economic development agenda:**
 1. **Research and development activity (public and private)**
 2. **Entrepreneurial ecosystem building**
 3. **Availability and accessibility of risk capital for small businesses**
- **However, venture capital is not efficiently deployed for optimal business development and economic development outcomes**
 - Over half of all venture capital is concentrated in two U.S. regions/states
 - Five states receive 88% of fund commitments and 74% of company investments



SSBCI VC Program Snapshot

Approximate
Amount Allocated to
VC = **\$400 million**

All but two state VC
programs are
focused on equity-
based investments

2/3 of capital is
focused on early-
stage companies

**Venture Capital
Deployment
Models:**

Direct Investment

Co-Investment

Fund-of-Funds

3rd Party Managed

Multiple Strategies

**Thirty Approved
State VC Programs**

Large Capital
Allocations to VC:

TX, FL, IN, TN, NY

Small Capital
Allocations to VC:

MN, KS, ME

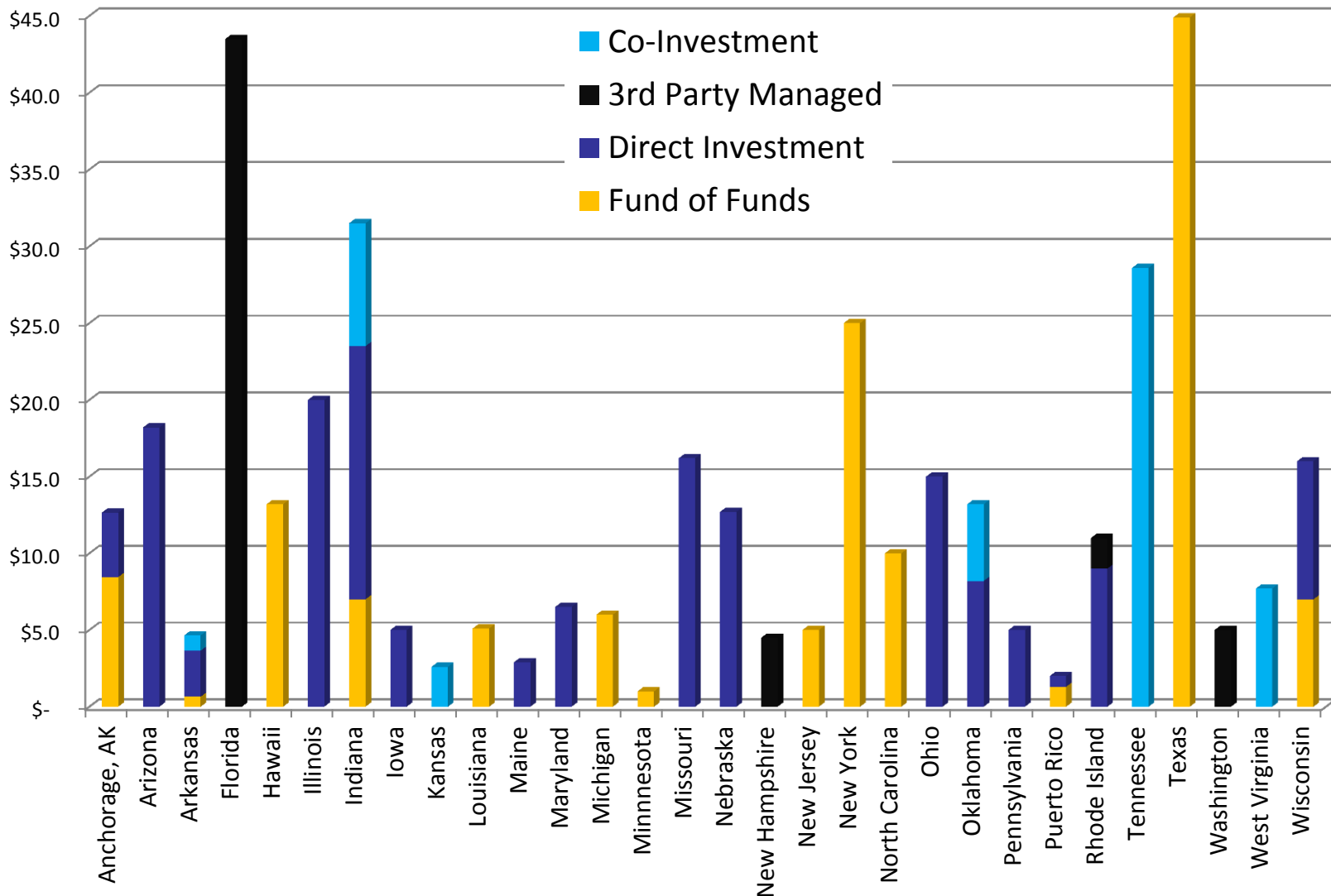


Venture Capital Deployment Models within SSBCI

- **Direct Investment Funds** – state serves as fund manager to actively network with entrepreneurs, source deal flow, performing due diligence, assist in the recruitment of co-investors and possibly set terms
- **Co-investment Funds** – state invests alongside private sector investors in deals meeting certain requirements, with state role focused on compliance rather than actively performing subjective evaluations
- **Fund-of-funds** – state invests capital in more than one VC fund as a limited partner; each fund manages the full processes of investing in high-potential small businesses while also complying with SSBCI program rules
- **3rd-party managed funds** – state contracts with a single external firm to manage the full investment process, with a single fund structure that may or may not commingle private funds

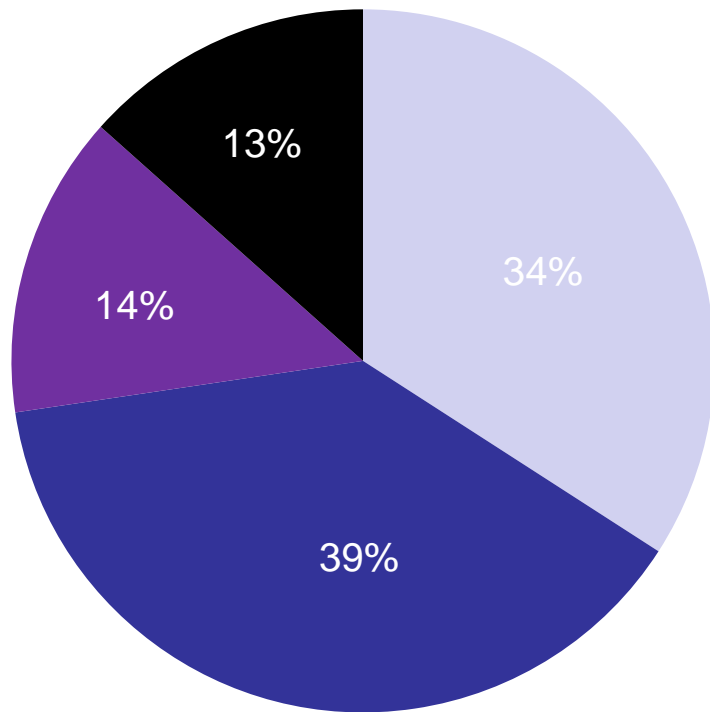


State VC Programs by Type of Investment & Amount



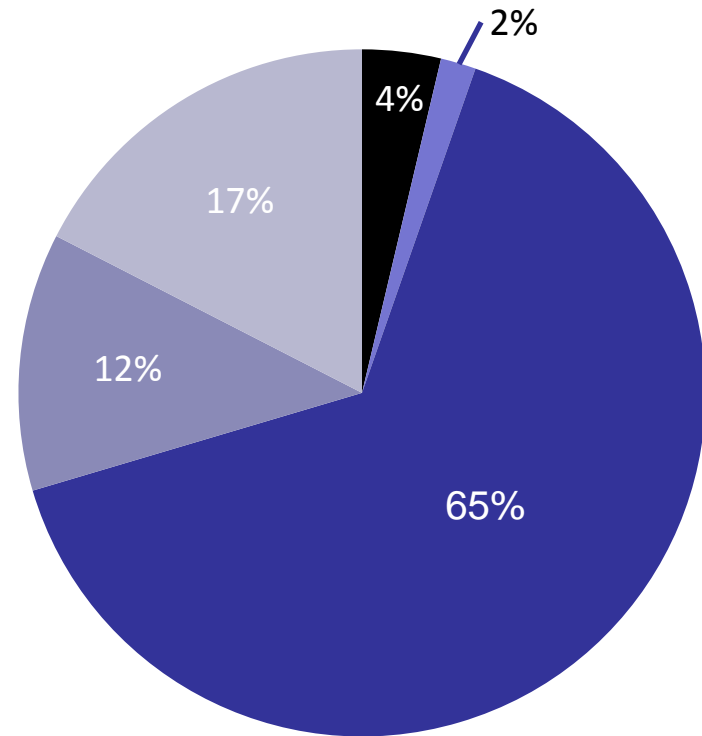
SSBCI Funding Allocations

By Capital Deployment Strategy



■ Fund of Funds ■ Direct Investment
■ 3rd Party Managed ■ Co-Investment Fund

By Stage of Investment



■ Any ■ Pre-Seed ■ Seed/Early
■ Growth ■ Mezz./Debt

Principles of Well-Designed State VC Programs

1. Understand the supply of and demand for venture capital.
2. Focus on capacity building with an ecosystem approach.
3. Create pathways to the next investment round.
4. Plan for the long-term and manage expectations.

Principles of Well-Designed State VC Programs

5. Specifically address the potential for conflicts of interest and political influence.
6. Attract the most capable leaders to manage resources.
7. Measure results accurately with defensible logic.
8. Align state economic development interests with the financial interests of fund managers and limited partner VC fund investors.

Report Recommendations

1. **Work with the industry of state VC programs to describe common challenges**, cull lessons learned and set forth emerging best practices.
2. **Review transaction-level data** to assess the performance of SSBCI VC programs over the program period.
3. Build on the foundation established by SSBCI to support state VC programs that operate on the **principles of a well-designed program**.
4. In future, **consider offering training** to improve relevant experience for state VC program managers.
5. Implement capital formation initiatives as part of a **comprehensive strategy for supporting entrepreneurial ecosystems** and foster regional innovation networks that improve such strategies.



SSBCI Venture Capital Programs Working Group

- Organized from discussions at the SSBCI conference in Chicago, primarily focused on direct-investment VC programs.
- Successfully coordinated communications with SSBCI staff on novel technical issues to help formulate a streamlined, optimal response
- **Next steps for Working Group?** Some suggestions...
 1. Form a steering group to identify key data points and performance metrics that participating states would voluntarily collect
 2. Accumulate success stories of SSBCI investments and impact
 3. Assist in a data collection process for better understanding existing or proposed state programs intended to stimulate risk capital investment in high-growth potential small businesses
 4. Facilitate match-making between state VC Program managers for improved information sharing and peer assistance

Request for Feedback

- Which of C/S's Principles (slide 9) are most relevant to the field? Which are most relevant to SSBCI?
- Would it be beneficial to the field for the SSBCI VC working group to advance one or more of these principles as a group in broad communications with policy leaders?
- Would it be beneficial to the industry for federal agencies to advance one or more of these principles in program related communications with states?
- Any other questions, comments, or suggestions?





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