Chapter 13:

How to contact investors

We have reached the point when the startup is ready to initiate contact and dialogue with potential investors. At this point it's important to understand how to go about that initial contact and to know what materials investors expect to see.

A common mistake is for entrepreneurs to send their 50-page business plan to 30-something investors and then sit back waiting for them to call and invite them to pitch. But before you send out any material, you need to get the trust of a potential investor. They get hundreds, if not thousands, of contact requests a year. Every entrepreneur thinks they have the best idea or they wouldn't be doing it. But why should a busy, time-strapped investor speak to you? What's in it for them?

In this chapter you will learn how to approach potential investors, and why you shouldn't send them a business plan.

Rule number 1 – Don't write a business plan!

Many entrepreneurs believe they should write a long and well-articulated business plan, setting out in detail all their future plans, and that the business plan is key to funding.

Wrong. If you send a long business plan to a professional investor I can guarantee they won't read it – and for three reasons:

1. It's too long
2. It's full of irrelevant details
3. It's out of date

1. Too long

Investors won't allocate time to read a 50-page business plan, especially not early in the process when they're mainly looking to weed out unsuitable opportunities. They get so many opportunities that they must be able to evaluate yours in three or four pages. If you send them a long business plan, they might read the first five pages to see if it has an executive summary and they won't read the rest.

Danish venture capitalist Nikolaj Nyholm works as a partner in Sunstone Capital. I once asked him what he does when an unsolicited, long business plan is emailed to him. He said, 'It will most likely rot to death in my inbox.'

2. Irrelevant details

A business plan is often full of irrelevant information. When you write it, you're caught up in explaining a lot of details about the future – many of these are of limited interest and value to a potential investor. When you try to estimate your rental costs in three years, or whether in five years you'll go into other territories like Germany before Spain, you will lose them. They know the plan will change many times before then.

What investors are looking for are specific elements of the business model: the problem you're solving, how you're solving it, who your customers are, the team, etc. They don't want to play the needle in the haystack game, trying to locate those five or 10 useful pages among dozens.

3. Outdated

The problem with a lengthy and detailed plan, with graphs of your cost of business and your market penetration guesstimates for year five, is that it's outdated as soon as you press the print button. Perhaps you assume that your customers will pay €10 and they'll be in Europe, and then you launch and find out that the customers won't pay €10 and they come from Asia. That changes the entire plan, revenues, costs and how you market your product.

Key note: A business plan is seen as a negative signal

If I see a hundred page business plan from a founder, I think, 'They're sitting and spending three months in the basement making this perfect plan instead of going out and talking to customers or making the product.' That says something about how they think about entrepreneurship and how to get started. Perhaps they have their reasons for doing so, but to me it signals that their priorities are off.

Just ask the founders of some of the most successful startups what their initial business idea was, and you'll find it was very different from the business they are running now. Investors know that and therefore won't spend hours reading your lengthy plan.

Key note: What to do instead of creating a long business plan

You need to focus on two things instead of creating a formal business plan:

1. **Process.** You need an agile process, getting you from your idea to closer to a real business. I recommend reading books like *The Lean Startup* and *Running Lean*. By reading these books you can learn to apply important concepts for agile development, like minimum viable product, build-measure-learn, and business model canvas/lean canvas.
2. **Material.** Read Chapter 13 for the material you should develop and use in communication with your potential investors – this doesn't include a business plan!

Should you ever make plan for internal use?

Should you write a business plan just for internal use? Most serial entrepreneurs acknowledge that there's real value in planning and thinking about the future, in thinking about what they really want to achieve and how they want to solve a problem. Winston Churchill famously said, '*Plans are of little importance, but planning is essential.*'

The value for me and most serial entrepreneurs is not the business plan as a document, but rather the process of making it. You and your co-founder(s) will learn a lot from discussing the really important subjects about the business; the where, what, how, who, why, and when. What you find will have important implications both for your business and for your funding strategy.

Planning and strategizing is essential for determining and aligning you and your team to where you want to go. The question is: what is the best process for you internally to get that alignment? Is that a business plan or is it a different kind of process? My opinion (which is echoed by many investors and serial entrepreneurs) is that you need a more agile process and documentation than the classic business plan approach offers.

Key note: What do you do if an investor asks you to send a business plan?

Some investors will *ask* for business plan. If this is the case, you should decode what they're asking for. The investor doesn't want a hundred page Word document; what they want is to understand your business. Your investor slide-deck and budget should be linked and are normally enough for an investor to decide to take the next step with you. If they ask for more, you should ask the investor what specific information they would like to see. Then you can update your investor slide-deck accordingly. You might find all the investors you approach ask for the same five or 10 extra pages. If so, add them to your main slide-deck and this will become your business plan.

Rule number 2 – Trust is the most important factor

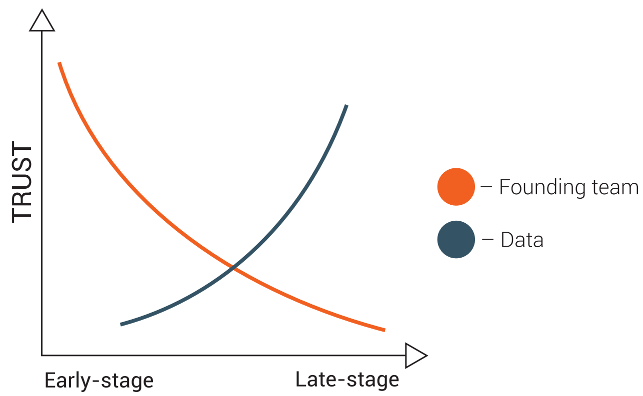
I know I'm repeating myself, but it's important: trust is the most important factor.

For any investor to invest in a startup, they need to have a lot of trust given the scary statistics on how many startups fail. You can even divide this trust into two things the investor must believe in: trust in the business opportunity (that the problem you are trying to solve is real, that the market is big enough etc.), and trust in your team (that you have what it takes to deliver on the opportunity).

But there is a big difference between early- and late-stage startups when it comes to how trust is generated.

If you're a late stage startup, you have a product, users, paying customers and revenue, and a team that have delivered the above. What this means is you have a lot of historic data, that is both quantitative and qualitative, to support your claims. You are able to provide credible answers to tough questions like: *What is the cost of getting a customer? How much are they willing to pay?* and *How big is the market?* Real data beats every scenario analysis there is. If you have customers paying, that is proof – and proof generates trust. Of course, they still have to have trust in you and the team, but it's relatively easy to convince investors about the business because you have real data.

Early-stage is about trusting you, later-stage is about trusting your data



But what about an early-stage startup? You might have a beta version of the product, maybe you have some users, but you probably don't have paying customers yet. You've hopefully convinced a few people to join you, but it's likely to be an incomplete team. You have very little performance data; it's all about the future. You're saying, 'I *think* there's a big market; I *think* my customer would pay for this cool product if I made it.'

Key note: Focus on you and not the market

For later stage investing, even if the investor doesn't trust you, the figures don't lie, and investors put their trust in the data, but in early-stage investing, it is even more about trust in you.

Early-stage startups should of course explain the business and market opportunity, but it's really 80 per cent about you and 20 per cent about the business.

VC explains: Personal trust is local

Arne Tonning is partner at the venture capital fund Alliance Venture and explains why startups need to understand that early-stage financing is local:

The probability of investment is inversely proportional to the distance between the founder(s) and investor.

Early-stage investment is still a local business to the extent that it's more likely an investor is located close to the founder(s)/startups. For early-stage investments, relationships and access to references on a personal level is a critical factor for de-risking a case for investors in the absence of the clear business metrics that are more present in later stages. Your credibility as a founder is highly dependent on your personal network: where you worked, where you studied, etc. This is hard to replicate for someone 'alien'.

While it's difficult, factors such as relocating, building common networks, or at least having a very specific expertise in common with an investor may help reduce the perceived distance between a founder and an investor, thus making an investment more likely. This can take time. The quickest way to gain 'locality' quickly is by going through the best accelerator programs. However, fundraising closer to home is in my view more likely to be a successful path for most startups at the starting point.

How do you get investors to trust you?

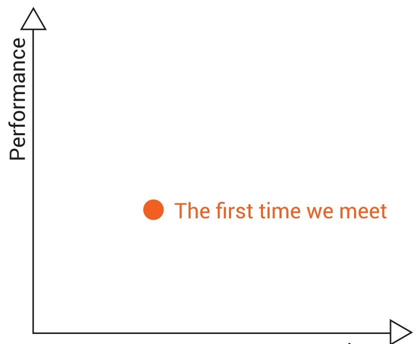
If it's all about trust, how do you get early-stage investors to trust you? There are two different types of investors: those you already know, and the rest. Perhaps you have an acquaintance, or friends and family, who know you and have the means to invest in you. Great, they know you and therefore trust you (and, if they don't trust you, perhaps you should look in the mirror).

Most startups will have to go beyond their personal network and approach investors they don't know at some point. When they do, they will need to build trust.

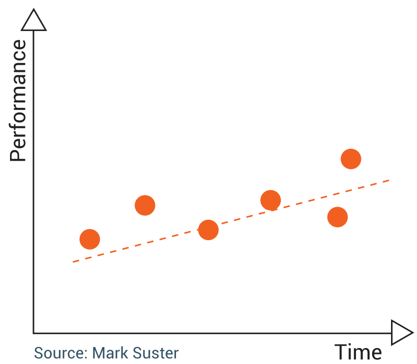
The key point here is that trust is built over time. You're unlikely to trust a person you have met for half an hour. This explains why you can't expect to get the money on the same day you meet a potential investor – there's no personal trust. Even if they think you're cool, feel you have what it takes, and you have a great business, the chance you'll get money the same day or the day after you meet is tiny.

We discussed earlier that the process televised on the show *Dragon's Den/Shark Tank* is fake. It's a theatre where you pitch in front of five investors, they discuss what you've said and then say, 'OK, we'll invest two hundred thousand euros'. In reality this never happens.

Entrepreneur turned venture capitalist, Mark Suster, from Both Sides of The Table, said, *I don't invest in a dot, I invest in a line.*



Source: Mark Suster



Source: Mark Suster

Imagine yourself as a dot on a graph with performance on the y versus time on the x. Even if your performance at a given time is good, investors want to see a line so they can see you at different points in time. Investors look at entrepreneurs they heard about six months ago who had great plans for the future, and when they meet six months later they may see they're still not quite there yet but the line is going in the right direction.

As Lars Andersen, General Partner in SEED Capital, explains:

The most common mistake startups make in relation to contacting VCs is that they make contact too late. Seriously, it's about sticking your neck out there. Your product doesn't have to be perfect. Build a minimum viable product, use it to learn about your customers, and start contacting VCs. We might say that it's still too early, but that doesn't mean never. The now successful wine scanner app, Vivino, had a first product that was absolute crap, but they gave us something to work from. This creates a paradox for many startups.

You should not count on VC money too early since in reality they invest rather late in the process, but you need to begin building relationships with them early on. They need time to get to know you before they invest their money – just make sure you don't waste too much time on coffee with VC partners!

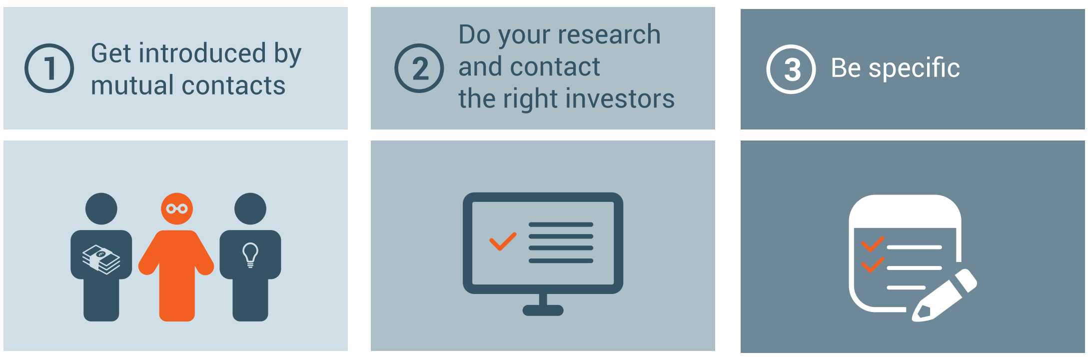
Key note: Build relationships with investors ahead of time!

What does this mean to startups? You have to build relationships with potential investors before you need the money – you shouldn't wait until you have everything in place. Create relationships now.

How do you build relationships with potential investors?

There are three important points to keep in mind when reaching out to investors:

How to contact potential investors



Get introduced by mutual contacts

Investors are generally short of time, but opportunity rich. They have lots of opportunities presented to them, but little time to evaluate them. They have to prioritise – it's like a business sales funnel. Out of the thousands of entrepreneurs who knock on their door each year, they might invest in one to five. They'll spend a lot of time with those selected entrepreneurs. As an early-stage investor, they have to be careful not to take two or three hundred down the sales funnel because they can't go into depth with that number. They need to say yes or no quickly, find the 30 or 50 to take to the next stage (a meeting), and then find the one to five they want to invest in.

Even if they wanted to, they can't meet everyone who contacts them, so they have to say no to a lot of requests. So, although they're not just deleting emails without reading them, they might spend just 10 seconds on each message. Ten seconds!

Advice from former VC: The biggest mistake from startups when contacting VCs

Søren Jessen Nielsen (former general partner of two venture capital funds).

The biggest mistake made by entrepreneurs when searching for venture capital is to send unsolicited emails to a given VC fund. A VC partner rarely spends that much time on such emails, simply because there are so many startups contacting them. A given VC partner might have over 500 companies contacting them a year, so saying no early in the process is a way to manage their time. They may skim the email, but are unlikely to spend too much time on it and the chance of it leading to a meeting is very low. Compare this to a case in which the partner is introduced to the startup via a mutual contact; the partner will evaluate this request in much more detail. Ideally, it will come from an experienced/known business angel, and in the dream scenario the business angel will indicate they are interested in investing in the startup.

You should avoid spending time on cold-emailing VC partners, and instead spend your time on building relationships with people who can introduce you to the right partners!

In 2015, I reached out to a number of potential investors (venture capital funds) in Silicon Valley for one of my ventures. Despite only contacting investors who were active in the specific subfield, it was almost impossible to book meetings, or even get feedback on emails, from most of the funds I contacted. But when I was introduced via a mutual contact to the same partners in the same funds, almost all of them responded instantly, resulting in lots of investment meetings. Why? Because they took the time to read my email and take it seriously as it was now associated with a trusted contact.

Key note: You need introductions!

If you want to get in contact with an investor, it's crucial to get introduced by a mutual contact, someone who can vouch for you and who knows the investor well enough to make the introduction count. The person making the introduction is saying: 'I trust them; take it from here.' It's basic business sense: your mutual contact is establishing trust for the investor to take you seriously.

Below is an example of an introductory email I used when I wanted to get in contact with a US-based venture fund. I connected them via a good friend of mine who already knew the partner at the specific venture fund and was in a position to make an introduction.

From: **Dan Eisenhardt** [redacted]
Date: 2015-05-27 21:26 GMT+02:00
Subject: Intro to Sepior
To: [redacted]
Cc [redacted]

Hi [redacted]

Hope things are going well at [redacted]!

I want to introduce Nicolaj H Nielsen, who is a Danish serial entrepreneur and also one of the first investors in Recon Instruments. He is co-founder of Sepior, that is a startup working in the cloud encryption space. Sepior is currently headquuarted in Denmark, where it has received seed funding, but is now investigating a potential move of HQ to US (but keep R&D in Denmark). Nicolaj is looking for the right point of entry into [redacted] since Sepior might be a right fit for either [redacted] directly or for the dedicated [redacted] fund you have created. Nicolaj and the CTO of Sepior will be in Bay area next week.

Please find attached a brief intro deck on Sepior.

Best regards,

Dan

Dan Eisenhardt
President & CEO

recon INSTRUMENTS

Join groups, ask for referrals, look for venture capitalists online and then ask your networks for referrals. Don't cold call. They probably invest in less than one per cent of the companies they look at so you need to get a foot in the door.

You need to find contacts to introduce you to the right partners in the right funds in your country. That's not to say they'll invest straight away, but you'll gain their initial trust. Then you need to build on that trust and show you have a cool team, you know what you're doing, you have a product that is much better, a business model that is scalable, and the market you are building is big.

Do your research and contact the right investors

Though you may not need funding right now, you shouldn't spend time contacting investors that are likely wrong for you – and you shouldn't waste their time either. You need to find investors who are relevant and who invest in:

If you're an early-stage startup and barely off the ground, you shouldn't contact investors who normally invest hundreds of millions of euros. Those hundred million euros implies they invest very late, and your startup is therefore not relevant to them – neither now, or 12 months from now.

When you've done your research and located a relevant investor, find a mutual contact who can introduce you to them. A good reason you should focus on relevant investors alone is because you will need an introduction. Imagine I'm a mutual contact and you ask me to introduce you to an investor. If I later find out your startup isn't relevant to that investor, I will end up looking bad for having introduced you.

Be specific

You've found a particular investor who you'd like to talk to and ask for advice because you want money at some point in the future and therefore want to start building a relationship now. You need to be very specific in your request for a meeting. Remember, investors get many requests for such meetings every day.

Business angel: Don't just ask for coffee!

Tommy Andersen, a tech entrepreneur and business angel, explains:

The biggest mistake startups make when pitching to me is saying, 'Let's have a coffee' without even telling me why. I have a busy daily routine and meet a lot of startups and founders all the time. Therefore, pitch me with a clear call-to-action and a clear message why we should meet for that special coffee. Just asking for a meet-up to hear about the world's greatest idea doesn't do the trick.

When you contact an investor you have to be specific about why the investor should take time out to meet you. Is it because you need the money now? Is it because you need some kind of advice? Maybe your questions can be answered by a phone call? Even when investors reduce the thousands of requests to a few hundred that seem relevant, that's still a lot of meetings. Make the investor's life easier by being specific.

When I get contacted by people who aren't specific, I write back and tell them to call me. That way, I achieve two things: it's much more time efficient for me because in a 10 minute call I can give some useful advice, and more than 50 per cent never call which maybe even more important. If an entrepreneur doesn't have the guts to call a potential investor or adviser when asked to do so, that's a firm indication they don't have what it takes to succeed.

Take-away points

Don't write a long business plan for investors. It will most likely not be read because it's too detailed at this point and will be full of irrelevant information based on very high level assumptions and outdated as soon as you hit 'send'. Three to four pages should be enough to say everything they need to know.

Investing in early-stage startups is all about trust; particularly personal trust in you and your team. Ideally you know the person already, otherwise use your contacts to get a great introduction to the right investors who are in the right market.

Building trust is essential, and takes time to build. Therefore reach out to the potential investors ahead of time and not at the last minute!

