



Main Street VCs

A new breed of venture capital, coming soon to a town near you.

From: [Inc. Magazine, December 2004](#) | Page 40

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Moving his wife and three young kids from a sleepy beach town in central Florida to California certainly wasn't something Jim Proctor planned on doing last winter. But when a respected Silicon Valley venture capital firm offered him a term sheet and told him to start packing, he dutifully began hunting for a new house on the West Coast. Proctor, the co-founder and CEO of WiDeFi, a technology concern in Melbourne, Fla., didn't have much of a choice. While his company boasted a promising product -- a device that extends the range of various wireless devices -- it also had the wrong address. "If you're a responsible officer and you have an opportunity like that, you just can't put your personal interests first," he says. "There were other investors to consider."

After finding a new house and office space near Silicon Valley, Proctor, 37, was close to making the cross-country trek when one of those very investors made him an amazing offer. In July of 2003, Inflexion Partners -- an upstart VC fund founded in Gainesville, Fla., in 2002 -- had contributed to WiDeFi's first round of financing, which totaled \$1.6 million. But the fledgling outfit didn't have deep enough pockets to pony up for a second round. Instead, Inflexion's general partners lined up a deal with two larger VC firms, Aurora Funds of Durham, N.C., and Axiom Venture Partners of Hartford, Conn., which agreed to commit more than \$6 million. Even better? Proctor and his business could stay in Florida, where the competition for talent and other resources, like office space and housing, is a lot less intense.

Such a coup would have been unthinkable until recently. Florida isn't exactly known as the place to be for venture capital. Just last year, in fact, fewer than 60 VC deals, totaling \$230 million, were made in the Sunshine State (the nation's fourth largest, based on population), according to a recent survey by PricewaterhouseCoopers, the National Venture Capital Association, and research company Venture Economics. During the same period, on the other hand, more than 1,000 deals, worth \$7.7 billion, were made in California, mostly involving VC funds and companies located in Silicon Valley.

Therein lies the the problem for companies like WiDeFi. Most venture capitalists prefer to be within an hour's drive of their investments, and most of them are clustered in areas like Silicon Valley and the suburbs of Boston. "There's a good supply of companies in

Silicon Valley and a trip [to Florida] still takes an entire day," says Dan Rua, Inflexion's general partner. "From a VC's perspective, it's just one more hurdle for a company like WiDeFi to overcome."

But that's beginning to change. During the past year or two, enterprising VC firms have been setting up shop in locales as far-flung as Bozeman, Mont., and Las Cruces, N. Mex., hoping to tap into unmet demand from start-ups that have top-notch ideas and products but lack early-stage capital. This new generation of venture capitalists consists mainly of young financiers who cut their teeth at big firms and are now eager to sink them into emerging markets, usually near universities like, say, the University of Florida in Gainesville.

Matt Harris, for one, worked at Boston behemoth Bain Capital before founding Village Ventures in Williamstown, Mass., in 2002. Harris's outfit, like many new venture capital firms, focuses on companies in regions that are shunned by traditional funds, like western Massachusetts. Other things remain the same. Just like the big outfits in Silicon Valley and Boston, small-town VCs focus on industries that boast high margins, in particular technology. Village Ventures, for instance, invests in companies in the technology and life science fields. And, while these young upstarts may be less formal than their predecessors, they still have high standards. In other words, business owners looking to score financing from one should come armed with a solid business plan and a top-notch management team.

The new breed of venture capitalists, however, tends to have a much softer touch than their traditional counterparts. That's a major selling point for entrepreneurs like WiDeFi's Proctor. "In Silicon Valley, the VCs seem to take an all-or-nothing approach, so the company is either 100% successful" or not successful at all, Proctor says. "They tend to be much less entrepreneur-centered." The deal Proctor struck with Inflexion enables him to stick to his original growth strategy and expand more slowly than a Silicon Valley firm might expect. Like the patient coach of a promising farm team, firms like Inflexion are prepared to guide companies every step of the way until they hit the big time. "These types of deals take a lot of work and a lot of focus, and a lot of VC firms aren't interested in that kind of nitty-gritty work," notes Harris, of Village Ventures.

Of course, Harris and his peers aren't targeting out-of-the-way businesses out of the goodness of their hearts. Financiers willing to venture beyond Silicon Valley tend to be rewarded with superior returns, since companies located off the beaten path usually garner lower valuations. In other words, investors get more bang for the buck. Small-town venture capitalists are also getting a boost from various federal and state economic development programs. In an effort to prevent homegrown start-ups from moving on once they mature, government officials in "have-not" areas are experimenting with using public financing from state pension funds and similar sources to help finance regional VCs. A new fund called the Rural Oklahoma Capital Alliance, for instance, plans to raise \$10 million in private capital, then leverage it with money set aside for rural areas by the U.S. Small Business Administration. The fund's director, Ray Wheatley, calculates that Oklahoma companies represent \$50 million in venture capital demand. But just three

businesses based there received venture capital investment in 2003, according to the PricewaterhouseCoopers survey. "The chance of getting VC from Sand Hill Road for these deals is probably next to none," he says.

Still, there are disadvantages that small-business owners need to consider before tapping a regional venture capital fund. Most of the funds are made up of less than \$50 million, making it difficult for them to provide financing down the road, when entrepreneurs need bigger chunks of money. Instead, they focus on seed funding and smaller deals, usually worth about \$1 million. That said, there's a good chance the hometown funds could broker a third-party deal with more substantial venture funds, as Inflexion did for WiDeFi.

Harris, for his part, leverages his industry connections to link up local businesses with bigger players, like his former employer Bain Capital. Those firms, in turn, are much more likely to consider investing in a far-off company if there's already an investor on hand to oversee operations. In exchange, the middleman usually receives a percentage of the returns. "Most VC firms won't do a local deal without a local VC holding their hand," notes Mark Heesen, president of the National Venture Capital Association. "They need local eyes and ears."

Finding a local VC firm is more art than science. Because there is no clearinghouse for them, your best bet is to stay plugged in to the local business community. It also pays to periodically check out the National Association of Seed and Venture Funds, which lists new members on its website (www.nasvf.org).

Back in Florida, Proctor's company is thriving, thanks in large part to the second round of venture funding it received last March. WiDeFi, which now has 12 employees, recently scored a major contract with the U.S. military. Sure, Proctor admits, there were times this past summer when he wished he had moved. Three of the four hurricanes that hit Florida affected him and his employees. Still, he says, it's good to be home. 📍