

U.S. Venture Capital and European Technology

Proven Success in New Fertile Ground

By Steve Clearman, General Partner, Geocapital Partners

Despite the perception that it is prohibitively difficult for U.S. venture capitalists to successfully back early-stage deals across the Atlantic, Europe is proving fertile ground for young, innovative information technology companies needing capital in industries that have defied the traditional boundaries of regional or national markets.

Private equity in Europe historically has translated into late-stage and buyout transactions, with the most-cited caveats against venture capital investing there being a lack of liquidity, weak management teams, few role models, less advanced technology and even cultural differences. Of the ECU 14.5 billion capital deployed in Europe in 1998, just 11.4% went to seed and start-up deals, according to the most recent statistics published by the European Private Equity and Venture Capital Association. The prior year, just 7.4% of ECU 9.7 billion found its way to the youngest companies.

While the percentage is improving slightly, the low level of activity still speaks to a painful lack of capital for early-stage deals. The supply of interesting entrepreneurial opportunities, however, is growing rapidly in Europe, as the elements for an entrepreneurial environment are increasingly evident. Geocapital Partners stands as one of the few American venture capital firms with a successful track record of taking advantage of this growth in early-stage European companies, particularly when it comes to technology.

Behind, but Gaining Ground

An investor in European technology companies must be aware that the overall region is

still about a year and a half behind the U.S. when it comes to daily computer usage. Internet penetration, for example, varies considerably from country to country, with Scandinavia trailing the U.S. by a year, the United Kingdom and Germany by a year and a half, and France, Spain and Italy needing about two years to catch up.

A U.S. venture capital firm with experience in building Internet-related companies at home over the last few years will find itself in great demand among European entrepreneurs who want to benefit from the lessons learned.

Geocapital Partners' expertise in technology investing carried over across the Atlantic when backing StepStone, the leading European online jobs search company. While the company's founders had a number of venture firms eager to make an investment, Geocapital Partners stood out because we had closed two similar deals in the U.S. — HomeStore.com and AutoWeb.com — in 1997. All were examples of a migration from traditional print classified advertising to the Web, and our prior experience played directly into the founders' final choice for a financial partner. At the time of Geocapital Partners' investment last year, StepStone was the most popular Web recruitment site in Scandinavia, and now it ranks as the leading site in all of Europe. In March 2000, StepStone completed its initial public

offering and is one of the premiere public Internet companies in Europe.

In helping StepStone achieve that success, Geocapital Partners relied on its experience on the ground and led recruiting efforts across Europe to find a chief executive, vice president of marketing, chief technology officer and chief financial officer who would all lead the company in its rapid expansion. Geocapital Partners also introduced them to and advised them on three acquisitions, initiated and led a renaming and rebranding of the company, and advised on strategic marketing deals, including online agreements with portals throughout Europe.

Venture Capital, American-Style

The experience and perspective that seasoned American VCs bring to a European technology deal at times can be considered more valuable than cash. While there are

top-notch European venture firms also looking to put capital to work, most of them are Euro-centric, without any manpower in the U.S. to help these young European companies eventually migrate to the American marketplace. In addition, they do not have the benefit of running similar businesses in the U.S.

European entrepreneurs know that venture capitalists here are supportive, long-term partners who position companies and their prod-

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ucts for exponential growth. European entrepreneurs dream of replicating an American IPO success story — and many are seeking success in the U.S. financial markets while also looking to distribute their products or services in the States.

Part of a U.S. strategy involves being able to help these companies recruit appropriate management teams in the States, and part entails being able to open doors to commercial and financial relationships.

U.S. venture firms are far more involved with the underwriters and the institutional investors in the Nasdaq market than European firms. In the U.S., IPOs offer both a market for financing and a promise for liquidity. Nasdaq is unquestionably the market with long-term liquidity for investors in IT related businesses. Although some European stock markets, such as Germany's Neuer Markt, are steaming with hot valuations, they are unproven in terms of the liquidity they provide.

The ability of U.S. venture firms to introduce European companies to the American market is a distinct advantage. Geocapital Partners has learned that operating as one integrated team from the U.S. and Europe enables us to provide a unique selling proposition to European entrepreneurs. Increasingly, we also find that American entrepreneurs favor the transatlantic position as well because they benefit by broadening their potential market, and that in turn benefits investors with the potential for larger profits.

Speaking Their Language

Another way the U.S.-Europe dynamic works in favor of American venture capital firms is that European entrepreneurs, especially those involved in technology, tend to look long-term and are eager to forge relationships beyond their national borders.

In the past, U.S. investors in low-tech European industries have been daunted, both culturally and physically, by the lack of a local partner on the ground. Cultural and language differences were considered weighty barriers in the past and meant that local success was possible only with local partners.

Most technology entrepreneurs from around the world, however, seem to share a

common, modern-day approach to business, one that is more freethinking, cross-cultural and global-minded. In addition, English has been accepted as a universal language in the technology space. Combined, these make entrepreneurs very comfortable when working with U.S. venture capitalists.

With an increasing number of European entrepreneurs seeking U.S. venture capital, it is also increasingly important to stay focused on sectors where there is existing expertise, as well as perceived future growth.

Continental Europe, for example, has produced some major winners in application software systems that make large enterprises run. In this space, Germany has produced Software AG, one of the largest stand-alone application companies in the world, and the Netherlands has Baan. It is reasonable to expect other major European companies to emerge in applications software.

providers and the opportunity to back such companies. Europe is also generating many innovative young companies that are providing technology for these alternative communication providers, which also opens doors for investors.

Geocapital Partners is a U.S. venture capital firm with a track record, strong financial commitment and presence in Europe. Investment opportunities in Europe are becoming more interesting, and because we have been able to leverage our existing expertise overseas, more U.S. firms are bound to follow.

About Geocapital Partners

Geocapital Partners has an office of eight investment professionals and administrative staff based in London, from which the firm supports investments throughout Western Europe. We have completed deals in the U.K., Norway, Sweden, France, Italy, Ireland and Spain. Several of these deals were in software companies

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The leading wireless equipment manufacturer is Nokia, which along with Ericsson, represents two of the three largest wireless handset manufacturers in the world that are headquartered in Europe. Since Europe leads the world in wireless technology and usage, Geocapital Partners also anticipates major innovations in this sector to come from there.

E-services, those businesses that provide strategy, planning and implementation of e-commerce solutions for all kinds of enterprises, represents another area of tremendous growth in Europe, as do other business-to-business Internet companies. Again, e-commerce is another sector where Europe is a little behind the U.S., so these are small companies that have great possibilities of becoming major contenders as they grow.

Further, deregulation of the communications industry in Europe has created a large number of alternative communication services

catering to global markets, and some were in Internet companies addressing the pan-European market. As a portfolio, our European activities have been extremely profitable.

As we proactively source deals, not only do European entrepreneurs welcome our calls but we find we are often the first U.S. firm to have contacted them.

It is true that the competitive landscape in Europe is changing, as there is a rapid flow of money into the region, but we still find that our position as a U.S. venture capital firm in the European market gives Geocapital Partners a strong, competitive edge.

Geocapital Partners manages over \$500 million and makes investments ranging from \$5 million to \$25 million. In addition to our staff in London, the firm has U.S. offices with a 20-member professional and support team located in Fort Lee, N.J., directly across the Hudson River from New York City.