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VENTURE CAPITAL

Austin Ventures raises record fund for Southwest

Georgie Raik-Allen
Redherring.com
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Austin Ventures has raised the biggest-ever early-stage venture fund focused on the Southwest United States. Over the past five years, the region's high-tech industry has matured, allowing the venture firm that helped nurture that growth to share the rewards.

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The Austin, Texas-based venture capital firm announced last week that it secured \$825 million for its seventh fund, about \$500 million more than it raised for its sixth fund last year. According to general partner John Thornton, the firm needed to raise a large fund to

keep up with growing investment opportunities in the region.

Austin Ventures estimates \$85 million in venture capital was invested in Austin-based IT companies in 1996 and \$250 million was invested in 1998. The firm expects investment to grow to \$700 million this year. Austin Ventures invests about one-half of its capital in Austin and the other half throughout the rest of the Southwest.

As the biggest early-stage investor in town, Austin Ventures is taking credit for an increase in entrepreneurial activity. "We have been doing very

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early-stage investing for six to eight years, and that work is just now starting to bear fruit in terms of lucrative exits and expansion rounds," Mr. Thornton says.

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RISING STAR

As the Texas tech sector matures, it's producing an abundance of successful role models for new entrepreneurs and a more experienced talent pool for early-stage companies. Mr. Thornton says the region has a labor shortage problem similar to Silicon Valley's. "Attracting top talent is our biggest challenge, just like our friends on the coast," he says.

According to Venture Economics, the new Austin Ventures fund makes it the third-largest early-stage VC firm in the U.S. Oak Investment Partners is the largest, with \$2.7 billion under management, followed by New Enterprise Associates with \$2.3 billion and Austin Ventures with \$1.6 billion.

As venture funds continue to grow, firms are spending more money on deals and looking increasingly at expansion rounds they normally couldn't afford. Austin Ventures's new fund will give the firm more participation in late-stage deals.

According to Mr. Thornton, the trend can be dangerous. "All institutional firms with funds over \$500 million are vulnerable to walking away from the most lucrative investing -- very early-stage and seed deals," he says. Mr. Thornton admits that Austin Ventures is not as well-positioned to serve "two people with a great idea" as it once was.

To address that potential problem, the firm spun-off AV Labs, a \$60 million fund that focuses specifically on early-stage deals. "We're attempting to reinvent the early venture firms," Mr. Thornton says.

AV Labs has offices and management that are separate from its parent, but it shares an "economic interest." Austin Ventures will be given an opportunity to invest in later-stage rounds of AV Labs's portfolio companies. The spin-off fund already invested in secret startups Mediaprise, Web Taggers, and

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SETTING ITSELF APART

Austin Ventures focuses on five areas: communications, semiconductors, applications and infrastructure, business-to-consumer (B2C) electronic commerce, and business-to-business (B2B) e-commerce.

According to Mr. Thornton, the firm differentiates itself by employing a large group of investment professionals. The firm has 22 investors, each with expertise in one of the five investment areas. By contrast, many firms like to increase capital under management without increasing partners, so they don't have to share profits.

Austin Ventures claims it offers its portfolio companies local connections and accessibility that better-known Silicon Valley or Boston-based firms don't provide. Success stories for Austin Ventures include seed investments in Tivoli Systems, an early-stage deal in Vignette (Nasdaq: VIGN), and lead investment in Metasolv (Nasdaq: MSLV).

According to Mr. Thornton, the biggest mistake he's seen is entrepreneurs having so much access to capital that they get cocky and assume they know what consumers want. "Entrepreneurs are in a big hurry and not going through the rigorous process of validating their business ideas at a very early stage," he says. "That's what AV Labs has been set up to do."

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