



Outside Venture Firms Fill Local Funding Holes

BY RICHARD CLOUGH
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John Tomich, co-founder of Onestop Internet Inc. in Rancho Dominguez, recently reached out to a local venture capital firm to secure funding for his information technology startup. His phone rang shortly thereafter with an investment offer.

But he was surprised that it came from a different firm – one headquartered on the other side of the country. Even stranger, he had never even contacted the firm. Somehow, word had gotten out.

It's a story that is all too familiar among local startups: An entrepreneur with a bright future spins his wheels while trying to raise local capital, only to be saved by an outside firm.

"The (venture) firms in L.A. are so boutique that they can't cover as much territory," said Tomich, himself a former senior associate at Shelter Capital Partners, an L.A. venture capital firm.

Los Angeles is home to many of the nation's most promising tech startups, but the vast majority of them have to look elsewhere for funding.

Despite a handful of viable venture capital firms, including Shelter and Clearstone Venture Partners, L.A. venture funding has long trailed Silicon Valley in large part because local venture capitalists have had little success in forming a cohesive industry.

But with the recent relocation of a venture firm to Los Angeles and the opening of branch offices by a number of large Silicon Valley firms, many in the industry say that more attention than ever is being focused on developing L.A.'s venture capital community.

Nearly \$200 million in venture capital was invested in Los Angeles County startups in the first two quarters of 2009, according to the quarterly MoneyTree Report by PricewaterhouseCoopers LLP and the National Venture Capital Association. That's a mere one-sixth of the \$1.2 billion invested in Silicon Valley startups in the same period, though it still places Los Angeles among the country's largest beneficiaries of venture funding.

However, less than 10 percent of the money invested in local tech startups actually comes from L.A. venture capital firms, according to research conducted by Momentum Venture Management, a Pasadena-based firm that helps emerging companies develop their businesses. Instead, many new companies still have to reach out to firms hundreds or even thousands of miles away, such as those clustered on Silicon Valley's famed Sand Hill Road.

"It's ironic," said Andy Wilson, managing partner of Momentum. "We have this huge population base, yet there's probably more venture capital on a single floor in a single building on Sand Hill Road than there

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is in all of Southern California.”

Unlike Silicon Valley, where the venture center is in a concentrated geographic area, in Los Angeles it’s so spread out that it has been difficult to create any semblance of a venture capital industry, Wilson said.

“There’s never been any synergy,” he said. “We have the sprawling geography and I think this is another manifestation of that. We are trying to pull together pockets of resources that are so diffuse.”

Flush with cash

It’s not that Los Angeles doesn’t have the money: The county is home to more millionaire households than any other in the country.

As a result, Southern California has a historically vibrant network of so-called angel investors – individuals who fund new startups. Tech Coast Angels, which invests exclusively in Southern California companies, is the largest angel investor network in the United States.

But the group isn’t flying as high as it once did: Its investments dropped more than 10 percent in 2008 from the previous year.

Nonlocal firms have stepped into the void, sending scouts and opening satellite offices in the region. In some cases, such as the phone call to Onestop Internet’s Tomich, outside firms are simply reaching out unprompted to promising startups.

Onestop Internet received \$13.3 million in the second quarter from Bessemer Venture Partners, based in Larchmont, N.Y.

Greg Gilman, chief executive and co-founder of RxVantage Inc. in Santa Monica, said local venture firms, though few in number, are typically well managed and can identify strong companies.

“There are some really top-tier firms,” Gilman said. “There are some excellent firms down here, just not as many of them as one would hope.”

RxVantage, which develops medical software, recently secured funding from two venture firms – \$500,000 from Slater Technology Fund in Providence, R.I., and an undisclosed investment from a local firm.

There are some bright spots in the local venture industry.

Venture capital firm DFJ Frontier, which closed a \$55 million fund in April, recently moved its headquarters from Sacramento to Sherman Oaks because the partners said they see tremendous opportunity in local companies.

Co-founder David Cremin said the best deal flow is now coming out of the Southern California region.

“We’re really excited about deals we’ve done locally,” he said.

Cremin, who has been involved in the local venture industry since 1998, said Los Angeles has much more of a venture community than it ever did in the past. Each month, he meets with more than a dozen regional venture capital firms in an atmosphere he described as “very interactive and very, very collegial – that’s the way Silicon Valley got started.”

Cremin said he expects new venture capital firms to crop up in Los Angeles in the coming years because there are plenty of promising companies and as they get attention, venture money will follow.

“We have to prove the companies are worthy of the kind of venture capital that can fuel explosive growth,” he said.