Finkel, Robert A. - The Masters of Private Equity and Venture Capital

McGraw-Hill, 2010, [Finance] Grade ★★★

In this book some of the real veterans of Private Equity and Venture Capital get to tell their own story – How did their career develop? Why did they make the choices they made and how did this form the sectors today? What lessons can they share (professional and in life)? The author Robert Finkel is the president and founder of a USD 190 million, Chicago based, PE-firm called Prism Capital. He got the inspiration for the book while arranging a number of panel discussions with seasoned VC-managers. With the book Finkel is *"seeking to expand my own interest in their accomplishments and channel it, in written form, into a kind of virtual classroom, one open to public viewing."* Self-improvement and sharing of financial wisdom – two worthy causes to write a book.

The structure of the book is simple: first an introduction by the author, then the two major parts of the book presenting one academic and five practitioners within first PE and then VC and finally a number of appendices with material from some of the practitioners ("Managing Director Selection Criteria" etc.). The arrangement lends itself perfectly to study the similarities and the differences of the two protagonists. Let's begin with what unites PE and VC. For a start they raise money, run funds with finite lives and then return the limited partners' money. This gives them "the advantage of a burning platform", i.e. a built in sense of urgency, a notion that time is money and an understanding of the alternative use of cash that is very conductive to driving change (and results). Both also view themselves as down to earth stewards of healthy business values, builders of enterprise value and champions of capitalism. That investors in public equity often are seen as politically correct hysterics is perhaps no surprise but I hadn't appreciated the tension that at times exist when it comes to hedge funds. HF:s are much too financially complex for the taste of those managing private capital and on top of that HF:s are the main competitors for the LP's money. In slightly different ways both VC and PE provide structure to the companies they invest in – governance is increased, strategies are sharpened and management is recruited. Another obvious similarity is the "2-and-20" fee structure.

The fee structure however illuminates one of the differences; AUM is much larger in PE than in VC and therefore while those working in the former can live happily on the management fee, the carry becomes relatively more important in VC. Even though they both, as stated above, bring structure the execution is very different. VC:s invest in the early stages and in hot new markets while PE invest in mature cash cows with potential for improvement. This means that while PE-owners at an early stage try to replace a CEO they don't have confidence in, VC-owners often coach an entrepreneur for longer and often only replaces him for a "professional manager" when the venture is brought to sufficient scale. The structure PE brings is focused on cost and capital efficiencies, repositioning often through M&A, accountability and cash flows, VC brings R&D prioritization, hiring skills, taking a product to market by adding sales competences and in general building a company with necessary systems. The outcome of an investment is more binary in VC than in PE and hence the risk is higher. This means that it's more common for VC's to co-invest and spread the risks, while this is mostly done in the very largest deals in PE. The difference in risk level also means that where leverage is a large part of the return PE generates, VC is equity-based only.

The masters presented in this book have been in business for 30, 40 or even 50 years and the stories they tell are those of how VC and PE started. One privilege of age is the ability to put things in perspective. However, at times the texts become memoirs rather than teachings of the tricks of trade. This makes the book likable but you don't learn as much as you could have.

Mats Larsson, January 8, 2014