

Fueling the naked city

By James Bowen

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There are eight million stories in the naked city, according to the narrator of a popular television crime drama of the late '50s and early '60s. Today there may be as many ideas swirling in the minds of our entrepreneurs, waiting for an injection of investor fuel. In 2005 the Canadian Venture Capital Association (cvca.ca) saw its members invest over \$1.8 billion in Canadian startups, with \$1.5 billion going to technology companies. In 2006 over \$260 million in investment fuel was added to Ottawa's high tech entrepreneurial engines.

Rod Bryden, president and CEO of **SC Stormont** and **Plasco Energy Group**, saw a shift in the investor model back in the '90s, when pension and other funds ballooned, some swelling to an unmanageable \$150-\$200 billion. These funds started passing the buck to smaller funds. About 5% made its way into the hands of venture capital companies looking to fuel early-stage companies. With the shuffle came specialization and entrepreneurs were left to find a VC focused on their particular market. And problems were compounded when technology and markets changed, putting entrepreneurs out of step – or a step ahead – of VCs whose purview had remained narrow.

The connection between risk and return, however, has remained the same over time, according to Bryden. Successful entrepreneurs have always understood risk, and know that a venture with less risk will meet with lower demands on returns by investors.

The natural rhythms of the market also drive changes in investor focus, according to the team at **Skypoint Capital** (**Peter Charbonneau**, **Andrew Katz**, **Leo Lax** and **Larry Perron**), thus making timing critical for startups.

They look at an industry, such as telecommunications, as a chain. End users are linked to providers, such as Bell, who are connected to equipment providers, like Nortel, who in turn are tied to software application providers. As each link in the chain develops or evolves, investment dollars shift from one link to another in a never ending loop. One sector's hand washes that of the other. When customer needs require more applications capacity, telecommunications companies then develop equipment that can accommodate those broader applications (think video over IP). Lax and Charbonneau point out that telecommunications capacity can easily handle current applications, creating a climate ripe for software companies to push ahead with next-generation functionality.

Ottawa's position as a centre of technological development is a growing concern – a local hot topic. Will that position soon be irrevocably altered, as an increasing number of companies outsource R&D to India and China? Are we not giving away our core competency? Will we not suffer a slow decline as a technology capital? Or, in the parlance of the Naked City, will we not become "marmalade on everybody's toast?"

Not so, according to Charbonneau, who says the rewards of bringing a product to market accrue largely to those who conceive of it and fund it, strengths, he figures, that will remain here for years to come. Lax says that Ottawa is brimming with ideas and that each one needs a local or North American entrepreneur to make it happen because only North Americans understand the North American market. Innovation and entrepreneurial ability are key; investment will go to where these two capabilities reside.

When looking at investment, angel investors should not be overlooked – though they commonly are, given their often low profile. **Irving Ebert** of the **Ottawa Angel Alliance** compares angel investors to the mysterious dark matter in the cosmos: unseen, omnipresent and vital. He believes that we need to bring angel investors into the light and study their success rates. Ebert has taken this message to the chair of the **Ontario Research and Innovation Council**, Ottawa tech luminary **Adam Chowaniec**,

Ottawa angels are beginning to move in a new direction, influenced by the ideas of the labour-sponsored funds and the highly successful Scottish approach. Scotland has a population of only five million and yet according to Ebert some \$70 million was invested by angels in local startups in response to a program of the national government that matched investment by qualified angels, a sharing of risk that increased the number of startups and resulted in an impressive average ROI of about 30%.

Ebert believes that angel investment could be stimulated by startups shifting from traditional exit strategies – IPO and acquisition – to exit via cash flow. According to local angel Mark Norton, exits through cash flow should be an equal

third option, if not the main one. He notes that too often an IPO or acquisition leads to yet another foreign (usually US) buyout, a woeful trend that reduces spin-offs and alienates, literally, R&D, skilled workers and sales/marketing talent.

Dave Scollon, manager of OCRI's **Ottawa Capital Network**, decries the lack of local funding, despite an abundance of innovation and diversification in sectors from telecom to software to life sciences; manufacturing to services to budding clean tech. This troubling picture is illustrative of the investment scene throughout Ontario: the inability of VCs to raise new funds. What should we do about it? Scollon would love to find the answer.

One try at an answer can be found in a twist now unraveling in the US venture capital community. Stateside VCs, such as Charles River Ventures, are lending money to early-stage companies on condition that they get options to invest in Series A round funding. Thus more early-stage companies receive funding for less dilution and VCs get their shares later, as well as the loans repaid.

Investment opportunity

Claude Haw of **Venture Coaches**, one of Ottawa's long-time venture capitalists, learned about investing in companies around Newbridge. Now he is focusing Venture Coaches on growing companies from "half-baked ideas" to "world-changing" enterprises. He says that in 2005, 9% of US venture capital went to clean tech while in Canada it was less than 1%.

As an emerging market for investor dollars, green tech is a difficult sell, Haw notes. One problem is that typically a green technology needs to be proven viable on a large scale to find funding. He believes that government should be doing more to encourage Canadian green ventures, helping them grow to a "large-scale" point where they can become a viable alternative to traditional oil and gas.

Thinking globally and acting locally, Haw has set out to build "world-changing" enterprises by investing at home. He recently joined the advisory committee of the newly created Ottawa Sustainability Fund, whose mandate is to give grants, gratis, to local projects that make a difference. Now is the time, Haw believes, to turn good deeds and clean technology ideas into money-making ventures.

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