



Facebook effect' fuels Industry Ventures' new fund

Mary Kathleen Flynn July 11, 2011

Investor appetite for secondary stakes in venture capital-backed private technology startups continues to swell, with Industry Ventures LLC announcing on Monday, July 11, that it has closed its sixth and largest fund.

At \$400 million, the new fund, which provides liquidity alternatives for venture capital and technology growth equity investments, is considerably larger than the \$265 million fund the 11-year-old San Francisco firm closed in 2009.

The sector has since experienced the "Facebook effect," said firm founder and managing director Hans Swildens in an interview.

As startups such as Facebook Inc. stay private longer than they used to, founders, early investors and early employees are seeking liquidity long before a public debut. "It's commonplace for employees and angels and early VCs to sell shares for diversification and to take some money off the table," Swildens said. "That whole market is new.

"In addition to a handful of institutional investors such as Industry Ventures, the secondary market has spawned trading platforms, such as SecondMarket and SharesPost, that allow individual investors to buy and sell stakes in private companies, and also new funds that buy secondary stakes in private companies, such as GSV Capital Corp. and Keating Capital.

Another trend fueling the secondary market's growth is the shrinking of the venture capital industry. The number of VC firms that raised new funds hit a 16-year low in the second quarter, according to the National Venture Capital Association.

"As firms are shrinking or going out of business, we're providing follow-on capital or buying out their stakes," Swildens said.

Hard times for financial institutions have also given Industry Ventures and others opportunities to invest. Hedge funds, many of which have gone out of business or cast off illiquid assets, have proved fertile ground, as have bankrupt banks. Out of its previous fund, Industry Ventures picked up interests in nine VC firms from Washington Mutual Bank, which collapsed in 2008.

Moving forward, Swildens expects secondary-market investments to get more complicated. Traditionally in the secondary market "you buy equity in companies directly - you buy out a shareholder and put the stock certificate in your fund," Swildens explained. "But now, general partners are working with companies proactively to identify liquidity programs, and some require an investor like us to invest through another venture fund, like a side fund or a liquidity fund, so we can provide capital through an existing investor's fund."

He expects the trend to persist. "Investors are going to have to be more flexible with capital over the next couple of years," Swildens recommended.