VC vs PE Investments in SaaS

WITH DAVE KELLOGG

Dave Kellogg is a technology executive, investor, advisor, and blogger. He is an Executive-in-Residence (EIR) at Balderton Capital (London) and principal of his own eponymous consulting business. Previously, he held CEO positions at Host Analytics and MarkLogic and, prior to that, was SVP/GM of Service Cloud at Salesforce and CMO at Business Objects. Dave has worked in varied capacities with companies including Bluecore, GainSight, MongoDB, Pigment, Recorded Future, and Tableau. Dave previously sat on the boards of Alation, Aster Data, Granular, Nuxeo, and Profisee.

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Aznaur Midov (AM): Dave, thank you for being on the podcast. Regular listeners already know you, but could you please say a few words about yourself for the first time listeners?

Dave Kellogg (DK): Great to be here. My name is Dave Kellogg. I'm currently running a consulting business and sitting on boards. I'm on three boards right now, Alation, Nuxeo, and Profisee. Two are VC-backed, and one is PE-backed. Previously, I was CEO of Host Analytics which we took from $8 million in ARR to $50 million in ARR and sold to a PE firm two years ago.

Prior to that, I was General Manager and SVP at Salesforce, I ran a company called MarkLogic from zero to $80 million, and I also was Chief Marketing Officer at Business Objects as we grew from $30 million to $1 billion. In addition to the three boards, I was on two other boards – one was Aster Data systems, which we sold to Teradata, and Granular, which we sold to DuPont.

AM: So, the theme of this episode is the comparison of Venture Capital (VC) and Private Equity (PE) investments in SaaS companies. Throughout your career, you mostly worked with VC funds, but you also had experience working with PE firms as well, right?

DK: Yeah. I think Private Equity has become a more significant part of the software and SaaS world. And I have been increasingly exposed to it as a result. I think their role in the industry has changed a lot over the past 20 years. I'd say I'm certainly not an expert on the PE side, but I've definitely been exposed through fundraising, through selling Host Analytics, and through my board involvement.

AM: One of the exit strategies for SaaS companies is exceedingly selling to PE funds. Why would VC sell the company they invested into a PE fund instead of continuing to grow it?

DK: In some ways, we need almost to go all the way back to the internet bubble to answer that question. Before 2000, software companies went public at around $30 million in revenue. Versant, where I worked, went public at $30 million. Business Objects went public at $30 million. My first employer, Ingres, was trying to go public at around $40 million, but then the stock market crash happened, so that's delayed, and we got bigger. But the bar for going public was tiny by today's standards.

In my mind, it was a result of the excesses of the dot.com bubble we were in, but what I consider to be personally a massive overcompensation to where if you looked at the average SaaS IPO last year, their median trailing 12-month revenue, or median implied ARR of approximately $200 million. These are big companies by historical standards. By the way, I almost joke there's a reason the stock options vest over four years because it used to take four to six years to go public. Now, it takes 12 - 13 years.

This has created the need and the opportunity for all these additional rounds of funding. An IPO itself used to be a $100 million round. I think I saw a $100 million B or C round the other day. So, the C round is the new IPO. And it makes sense. These are $300 million companies are also raising about $300 million in capital to get there. In the old days, you might raise $20, $30, and then raise $100 in IPO. And by the way, you'd never spend it because you were not supposed to lose money back in those days. It was kind of a crazy time, whereas now, people are much more interested in investing for growth.

The other big difference, I would say, is the quality of the revenue today is much higher. A $250 million SaaS company has a $250 million recurring revenue stream, whereas a $30 million perpetual, one-shot licensed company with a $30 million revenue stream. Many people will divide that by either two or three to make it equivalent, right? So you have companies that are much bigger and stronger.

That's created this whole need for additional types of financing. In the old days, PE firms were known for buying broken companies at fire-sale prices and trying to turn them around. In some ways, back in the day, CA Technologies was almost like a public PE firm. My first employer Ingres, I think, sold at 0.7x revenue to CA. They used to buy broken software companies and then jack up the maintenance. It was kind of a harbinger of PE.
And then independent PE firms did that for a living for a long time and had a bad reputation as a result. It was like, "Oh, you got bought by a PE firm; something must have gone terribly wrong. Why didn't you go public?" But remember, you could go public at $30 million, and now it's a long road to be public. You need to be able to raise $300 million to grow to roughly $250 million in revenue, which may take 13 years. That's created the opportunity for what they call “growth equity financing,” rather than mezzanine financing or all these additional rounds.

Why would a VC firm sell to a PE owner? I gave you the big backdrop, and maybe the answer is obvious given that backdrop, but the explicit answer to the question is, because you've got a company that is nowhere near going public, and you are coming up on the end of your fund life. Let's say you founded the fund in 2010; it's now 2020, you had a company that had a good start, then got in trouble, say it's $40 million in ARR today, breakeven, growing at 20%. Well, your fund is coming to an end. This thing is not going to go public anytime soon. And you know compounding 1.2% from $40 million is going to be a long, long time before it could ever go public.

So how do you get this thing liquid? And the answer is you can either sell it to a strategic, or you now have this whole new class of buyers, who would be interested in buying that company, either to grow it and sell it to somebody else. I'd say the typical standalone PE business model is to buy it today, at 50/50 debt versus equity, and sell it in four to six years for 2x-3x what you paid for it. That's it. That's the default play.

There are variations on it, where you do a roll-up buying a lot of small companies, or you buy a platform, one big company, and then you buy a bunch of little ones. But the basic math is still the same – you're trying to get a return that's equivalent to 2x-3x over four to six years on a 50/50 basis of equity and debt. So that's why they would sell because there's nothing else to do with it.

And they need to get liquidity at some point. Sometimes entrepreneurs forget that these are financial investors, and they are in it for a return. VCs can be amazingly patient, but they need to get liquidity at some point.

Your next question was: how are they different in my experience. As somebody who spent their time mostly on the VC side and now getting exposed to the PE world, what are some differences? And I'll answer first from an operational perspective, and then maybe we can go back and talk about investment. But from an operational perspective, I think there are a number of differences. One is they bring a lot of best practices. The other is you have different board dynamics. Let's start with those two.

The first thing about PE firms is they are big into best practices. They may have an internal consulting arm, and these people will show up for free and help you optimize your business. I would dare say that, philosophically, some PE firms say, "Hey, that's helpful. It's available for free. You can use it." Some would say, "they're showing up on Tuesday ."And you're going to be using it as you don't have a choice.

I think the thing they have in common is they all care a lot about best practices, from hiring to having your own interview methodology, to SaaS metrics, to how they approach market research, how you do the team building at the executive level, how you make strategy, you know, your Go-To-Market model, where they're going to show up with experts who will share different dials of voluntariness, their best practices with you.

To be honest, I think it's a great idea. The notion that "Hey, we're buying a lot of software companies, we can pattern-match across them, share best practices, and build a team of experts to be our staff experts in certain areas" is a great idea. It is rare on the VC side, although Andreessen Horowitz had a little bit of that when they had Mark Cranney as kind of the sales partner and Jeff Stump as the people partner. But I don't know how much they do it today. But in the PE world, it's a standard thing.

The other thing that's different in a PE firm operationally is board dynamics: a VC board is basically a cat-herding exercise from a CEO's perspective. You've got one guy who invested at 10 cents a share six years ago; you've got the guy who did the last round, who invested at $5 a share two months ago; their interests are not really aligned. They all have different expectations. They probably underwrote different financial plans. They all have lots of opinions because they're all-powerful people. It can be tough for the CFO if they don't happen to agree on what to do. And if you have beers with SaaS company CEOs, you'll definitely hear, "Oh, gosh, some board members want to go this way. And some want to go that way. It's all, you know, kind of hard." That doesn't happen on a PE board.

I would say, on VC boards, there tends to be an alpha male. And unfortunately, it usually is a male, but we'll call it the alpha person. But one or sometimes two alphas on the board usually emerge who will drive it. Usually, that alpha role kind of helps the CEO herd the cats; often, it's the A round investor because they have the longest history with the company and are kind of the biggest risk-taker. But not always. I've seen companies where it's actually the A round and the E round investor, and they sort of partner together and say, "We'll be the alphas leading the board."

You can see that dynamic organically emerge on a VC board. But on the PE board, there is a general partner/investing partner at the PE firm who sponsored the investment. That would be the de facto alpha board member. There might be two or three other people from the PE firm on the board as well, but they tend to be principles or VPs - usually, there are not multiple partners. And you may have some independents as well. The independents may have helped the firm with diligence – they may have been part of the transaction, and help the firm decide whether or not to buy the company so they have some continuity, and they get asked on the board.

By the way, if you're selling to a PE firm, and some experts are helping them, they might well be on your board in six months. So be nice. So the overall dynamic is just super different, and for a first-time CEO, it can be very challenging. Well, both situations are challenging. If you are a first-time CEO, who's climbed the corporate ladder (not a 27-year-old), you are used to working for a boss. And one of the hardest things about switching to CEO is you don't have a boss, right? You have a board, and it's a committee, and it doesn't have one mind. And if you treat them like a boss, you will make them nervous. They want you to run the company, and they're there to kind of be a sounding board to you.

On the PE side, there's a far greater risk of just treating that general partner like a boss. And I'm pretty sure some of them like to be treated that way. And again, you need to be careful because, in a VC board, it's harder to get confused because you have five people saying five different things like, "OK, I don't have one boss." In the PE world, you've got three people who aren't talking, the general partner who made the investment who talks a lot, and maybe an independent or two that don't talk that much––it's very easy to start treating that person like "the boss" rather than a board member. And that's a situation I think you need to watch. Because in the end, even if they don't want you to treat them like a boss, they want you to run the company and use them as a sounding board.

The last operational difference I remembered is the model. When you raise money from VCs, you show them a three-year financial model. Everybody knows it's a little inflated, and everybody discounts it. So you get into this game of like, "should it be 20% more aggressive than we think because they're going to discount it 20%, so you have this kind of game theory of numbers inflation. But that happens in a VC round. Everybody kind of knows it, and nobody really says it. And rare is the CEO stupid enough, and I have seen this happen, where literally after raising round, they're like, "Oh, that was a garbage plan, the real plan is this," which is a huge mistake, by the way. Provided you don't make that egregious mistake, if you just say, "Gosh, we're having trouble hitting the plan that we showed you in the financing round because we didn't hire some salespeople or something went wrong." That's kind of the norm. Some companies actually get ahead of their plan. I'm not saying that doesn't happen either. But I would say the general pattern in VC is you put out an optimistic plan.

And then, in my mind, I hate to put it in black and white fashion, but it's kind of forgotten about. You're just like, "OK, just tell me about the plan going forward. What can we sell this year? What can we sell next quarter?" They're not kind of whipping out the plan and looking at it and saying, "Well two years ago, you promised you'd be this big." That just, in my experience, doesn't happen.

On the PE side, it does. It's a huge difference. So I remember one time I was working with a PE company, and I had this kind of "the only quarter that matters is this quarter" mindset. You know, "Hey, what are you going to do this quarter? What's coming next? And everything else is in the past; who cares?" And a PE partner basically said, "Well, you know, we underwrote a model that said you were going to sell this much this year. And if you're behind last quarter, we expect you to catch that up."

And I'd never in 25 years on the VC side heard that. I was frankly shocked. I was like, "Catch up to what?" And they're like, "We underwrote a model." And that – those were the words that made it light up in my head: "Oh, you think about this differently." The VCs use the operating plan, in my opinion, to try and figure out valuation, how much they are willing to pay, and how aggressively they're going to hire salespeople to grow. It's kind of a compass pointing you in the right direction. Whereas this notion that "we underwrote a model, and we need you to hit that model, and if you're behind, you need to catch up," I think is much more of a PE creation.

And look, as soon as that light bulb went off, it started to make sense because VC is fundamentally a hits business. I think we've talked about this before, but if you take your average top-tier VC fund and yank out the top two investments, the IRR will fall from 36% to 12%, not worth the risk premium and the lack of liquidity, right? On the PE side, it doesn't work that way. VCs are elephant hunters, whereas PEs are rabbit or deer hunters, right? If you want to switch to baseball, the baseball metaphor is that you know VCs are kind of grand slams. They're looking for the big home run grand slam hits. Whereas PEs just want a lot of doubles. They'll take a single, but they can't take a strikeout because they're not offsetting the strikeouts with home runs. When you realize that, it kind of explains everything.

AM: How do you think this affects the initial due diligence of PE and VC funds?

DK: It's another great question. We talked about how PEs are different on the kind of operational side, like once you're working with one, but what's it like before you work with one? I think the management level qualitative diligence feels very much the same. They ask about the team, they ask about the business, and they ask about the technology and sustainable advantage. All those things feel pretty familiar.

I think the difference is that PE firms have more staff than VC firms. I mean, Andreessen would be an exception because they have a pretty big staff to help them with investments. But a lot of even top-tier VC firms are just a handful of general partners and a couple of junior folks, and that's it. These are not large organizations. And on the PE side, they tend to be. There are a lot of people, like principals and vice presidents, trying to work their way up to make a general partner.

And consequently, on the PE side, they do a lot more legwork and a lot more depth. The two biggest differences I've seen – one, they'll tend to recalculate all your numbers. One time with PE firms I got, they said, “don't bother telling me your CAC ratio, your LTV to CAC, we're going to calculate it ourselves.” Like, we don't care how you calculate it.

And I think on VC, that's different. VC will say, "OK, so you say your CAC is 1.3? What's included? What's excluded?" They will ask you how you calculate it, and you need to explain whether you put customer success in your CAC or not. And if you have reasonable answers, you can kind of spin your numbers or talk about your numbers. And in the PE side, I mean, this is maybe extreme, but it's like, "No, we've got our way of looking at things, we're going to have the MBAs grind it out, and we'll tell you what your CAC is. Thanks very much."

The other thing I'd say that I've seen PE firms do is hiring other firms. I think Ernst & Young has a division called Parthenon that is used in the PE world where they'll do some level of diligence themselves, but even business level diligence, such as number crunching. Like, "We've got this company. It's doing OK. Does it have segments of its customer base that it's ignoring that are really profitable? And they've never figured it out."

And I don't see VC people doing that. It's kind of not their business. They're trying to invest in healthy, growing businesses anyway. They're just trying to get a piece of the rising star, whereas PEs, in general, are trying to improve the operational performance of the business. And one of the best ways to do that is to find something that's working and being ignored. And you can hire people like Parthenon to do that for you. And they do, in my opinion, very high-quality work. I've seen some of these reports, and I was like, "Wow! This is good."

I think bigger firms may do it with their own staff. But smaller firms may hire a third-party market research and analysis firm. The other thing they'll do, by the way, is they'll actually do their own market research on you. You're going to show up and say, "Our customers love us. Do you want to talk to five customers?" And on the PE side, they're going to say, "We already did. In fact, we talked to 20."

AM: What about the company's strategy discussion? Do both VCs and PEs have the same type of due diligence and same discussions with management?

DK: I think there's probably one difference I've seen. I like to make things black and white to make them clear, and reality has a lot of shades of gray. So with that disclaimer, I think the philosophy of a VC is "I am your partner and will help you build your business." I think the philosophy of a PE is, "I am going to buy this business, it's going to be my business, and we're going to use our playbook to make it worth money."

There are growth stage PEs that look more like VCs, so you have a crossover in the middle. But I think the fundamental thing is that the VC wants to be your business partner, helping you build your business. And the PE is an owner, and it's their business, and they want to hire staff to build their business for them. I think, by the way, stock options are a fascinating contrast case between VC and PE. We'll come back to due diligence in a minute. But this demonstrates the point to me.

People ask, "Can you make money as an operating executive in the PE world? Can you only make big money in the VC world?" The answer is you make a lot of money in the PE world. But the difference is, in the VC land, stock options are like, "Hey, we're going to vest them over four years, we're going to try and give you a way to own them," which is tricky these days, maybe we'll do a 10-year tail or something. But the idea is if you come and join the company and work, we want to give you some shares for your contribution. If you leave, you can keep those shares. And that's OK, because it's a small world, and life is long, and we all want to be friends. That's kind of the VC's "how can I be helpful" sort of perspective on it.

The PE perspective is you make money only if and when I make money. That doesn't mean you can't make money – they'll give you significant stakes. I think PEs also concentrate the equity in the top management more so than the VC. The VCs are a little more democratic, "Hey, everybody, from the CEO to the receptionist, should have some shares." I think the PE is like, "No, let's give the top 20% of company shares because we want the people in charge to have a lot of skin in the game."

And back to my other comment of

“you make money if, only if, and when we make money “– PE firms typically have buybacks on the share options. They might say your options vest at liquidity so that they could do the vesting schedule. It says when we sell the company for more than 2.5x times what we paid for it, you vest. Or, maybe you'll vest over five years, not four, which is another PE thing. But there is time-based vesting; we have a buyback right on it if you leave early.

They really expect you to sign up for the tour of duty, do the tour of duty and be successful. And if you do it, you'll make a lot of money, assuming you are one of those top-end people. I think it reflects the difference. And these are the small things, but they're not so small, right? Go work in a PE firm for three years, get in a fight with your boss, quit, and discover you have no equity. That's not a small thing.

I am going over these examples to show the big picture and tie it all together. So, now, let's go back to due diligence. I think the difference is the VC is trying to be a responsible steward of the limited partners' money. They invest money on behalf of LPs, so they need to make sure they've done due diligence to make a responsible investing process. So they vet the team, vet the numbers, and look at things. If you were thinking of it as buying a house, they are doing a housing inspection to ensure there weren't any problems they didn't see.

The PE perspective is different because, in some ways, VCs make money on the sell, while PEs make money on the buy. A friend of mine was on a car lot in Florida, and he was like 60, and he worked a lot. He taught me that in a used car business, you make money on the buy. A 2004 Ford Taurus or Honda Accord are worth what they are worth in the market. You can't change that. But you can change how much you pay for it. You make money on the buy. That's how you get companies selling at 0.7x revenue. And certainly, old-school PE was that way.

But even modern PE still know they make money on the buy. Because they're not shooting for a 10x or a 100x or a 1000x as these guys sometimes get on the VC side; they're shooting for 3x or 5x. And when you're shooting for 3x or 5x, you can't make mistakes, first, as we've talked about, hence the best practices blah, blah, blah. But gosh, if I could buy it for 80 instead of 100 and I'm going to sell it for 240, I just got a materially better IRR. So that's the difference.

And the buzzword for this is "re-trading," and it was a word I hadn't heard in all of the 25 years working with VCs. I then ended up in PE land, where you'd hear it. It's a word with a negative connotation. The idea is you re-traded the deal, say, "Hey, Aznaur, I'll buy your house for $1 million. Then comes the inspection. I think a VC, if they came back and found a bunch of stuff that needed to be done, they'd say, "I don't want to buy the house anymore." The PE will come back and say, "I'll buy the house for $800K because there's $200K repair work to do."

And that's the difference. For the VC, it was like, "Hey, I thought this is a great house and a great neighborhood, and it's not, so no thanks." I don't think VCs re-trade deals because they're not trying to make money on the buy. But the PE will tend to see that as a "Hey, I still want this thing. It didn't totally invalidate my hypothesis. But I'm not going to pay as much for it because you kind of warranted in some way that something wasn't wrong that I found wrong. And therefore, I'm going to take the opportunity to re-trade it."

You know, particularly old school PE people might even kind of invent reasons to re-trade it. This is sometimes why PE people get a bad name because certain firms may actually make up things or just say, "Hey, there's a chip in the paint over there," that doesn't actually matter, and no one ever said there wasn't. But they'll come back and really start niggling about little things that they didn't care about just to knock down the price. And that deserves a negative connotation in that case. But in the other case, I'm not sure. Would you rather have a deal destroyed? Or would you rather have a deal at a lower price reflected the fact that, "Oh, gosh, you know, the roof needs replacing, and that costs $100K."

AM: This was an excellent summary. Was there anything we missed regarding the difference in approaches of VC and PE funds?

DK: The thing I think we missed would just be the numbers because I haven't had time to research them. But the odds of selling your company to a PE firm are probably, what, 10 times the odds of going public? And 5 times the odds of selling to a strategic? This is the new exit in Silicon

Valley. Why is it the new exit? Because the IPO bar has been raised from $30 million to $300 million, and the IPO timeframe has gone from 4 to 13-14 years. And that has changed everything.

In my mind, people don't talk about that enough because everyone is, you know, "Hey, we're going to go public; are we shooting for an IPO. Is a strategic going to swoop down and buy us for some amazing multiple?" I mean, those things happen. It's great when they do. But if you just want to play the odds, right, almost by stage – if you get to $30 million, what are your odds of going public versus getting bought by a PE? People tend to say, "Oh, if we get the $30 million, we can get anywhere." I say, "Not true. A lot of bad stuff can happen between $30 and $300 million."

AM: I've seen both generalist PE and VC funds with software being just one of the several areas they invest in, and software specialist funds that only focus in well, software. Which one of them would you prefer to sell to?

DK: Well, I guess there are two scenarios. And this is an important part of selling a company to a PE firm. Do you and your team want to stick around? And did they want you to stick around? And those are independent variables. For example, in my last company, my mission was to get it sold. When VCs hired me, the job was to get them liquid. They were old funds, and they'd been in the investment for a while. So to me, my mission was to get the thing liquid, and when I got it liquid, I was done. And I had no interest in staying on despite liking the new owners. They're great people, but it just wasn't – what I was there for.

Whereas on the other hand, sometimes the founder loves the business, wants to keep growing the business, and just needs a – what one banker called it – a shareholder rotation. It is a great euphemism where we want to rotate out the old shareholders, rotate some new shareholders and start over. And in those cases, you may want to stick around, and they may want you to stick around. I think that's really the first answer to the question because if you don't want to stick around, frankly, as a manager with fiduciary responsibility, you should want to sell to the highest bidder, right?

I know there are other considerations, who's going to take care of the employees, who are going to take care of the customers, etc. But you have to remember, as I would say, when you buy the house, you can paint it purple, if you want to – It's your house. When you sell it to somebody, they can do and will do what they want to do. And if what they want to do is align with what you want to do, and you want to stick around and do it, and they want you to stick around and do it, then it really starts to matter who you're selling to.

And, by the way, there's a lot of game theory about whether or not you want to stick around. I'd say be very careful – if a PE firm asks you if you're willing to stick around or want to stick around, say no at your own peril. From a game theory viewpoint, I believe there's only one correct answer to that question: "If you guys want me to, I'm in. I love the business, the customers, and the market, and if you don't want to, that's fine."

And by the way, if you're a VC-backed company, the VCs on your board is not going to let you sell to somebody at a lower price just because they have a growth thesis versus the EBITDA thesis – they have a fiduciary responsibility. They can't say, "Oh, we want it to be nice to the employees, so we sold it for $20 million less." That doesn't work.

So, all other things being equal, I personally would rather sell to a SaaS specialist because I think they're going to be able to help you more, they're going to know more, and you'll have a better network of fellow portfolio company CEOs to kind of share ideas with. But to me, who you sell to in the end is going to be a function of the process you use to sell a company and who comes up with the most money.

Maybe they'll be in the situation where two offers are close enough that it doesn't really matter which one you pick, in which case the factor that starts to weigh it is a certainty of the deal. Someone who's offering a little less did a lot more diligence and a lot more homework than this person who still has some things to check out. And what are they going to find? And will they re-trade? How do they behave during the process? Who do we actually trust to do this deal?

And by the way, this is how some PE firms win. They're good citizens of the process. They come in deliberately on the low side. Why? Because they make money on the buy, right? And if I can shave off $5 – $10 million on the price, because we've been good the whole time, we've hit every deadline, we followed your process, while the other guys have been trying to disrupt your process. And therefore, even though we don't have the highest dollar offer, we have the highest certainty to close because, by the way, if you go with the other guys, we're going to shut down our project.

And this, I believe, is a bluff. But if I were them, I'd say, "If you don't take our offer now and take somebody else's offer, we're going to shut down our process and go on to the next deal." I never lived through that, so I don't know how that plays out. But my hunch is it's a bluff, a scary bluff. Because if you think the other person doesn't have certainty of close, now you've lost your bird in the hand and your bird in the bush. And when your job is to make money for investors, that's a pretty scary proposition.

AM: Can you name a few software-focused PE funds off the top of your head?

DK: Before I answer this, if someone in the audience is actually thinking about selling their company, and you're thinking of selling it to PE, I would strongly advise you to get a banker because there are more of these firms than you could possibly imagine. Literally, in the warm-up to this call, Aznaur and I were talking, and I knew of a firm that he hadn't heard of, and they're managing $5 billion in assets. And this happens all the time. He's like, "Who are they? Never heard of them, and they have $5 billion?" So there are a lot of these firms out there.

Everyone is familiar with the big names on the growth equity side, Thoma Bravo, Insight Partners, and Vista Equity; those are some big names that I think everybody knows. I think there's a – you know, people like Accel-KKR. There are scores and scores of others. So don't just think you can only sell to one of the big names. Some guys specialize in mid-market like Riverside, where I have some friends, or ParkerGale, where I'm on a board. Some people specialize in really, really big stuff like you're going to meet people whose minimum check size is $300 million. Often your company is not worth their minimum check size because they're managing that much money.

So it's very important to have somebody to help guide you. Some of the other big names Warburg Pincus, Summit Partners, and the guys at Silver Lake, are obviously huge. There is Sumeru Equity, which is a spinoff of Silver Lake. I've worked with those guys. There are a lot of people out there. And I think the answer is that if you're going to sell the PE, you really need a banker for two reasons.

One, to navigate this process for you. Those PE firms buy companies for a living. It's their job. They're very good at it. And if you're doing it for the first time, that's inherently unfair. The other issue is that you need a tour guide because I could name 25 other PE firms with different flavors and sizes. And you need somebody to help you figure out who is worth talking to, who buys companies in your space, who has a reputation for just throwing an early offer out and then not really being interested, who throws out a high offer, but they're known to re-trade the offers. All these things are reasons why you need a banker.

Look, you can just Google top PE firms and apologies to any friends who I've missed at the dozens of PE firms I work with. But it's a big, big world. And the real message for the audience is it's a far bigger world than you know of. When I sold my last company, we had 60 people on the shortlist, which doesn't sound like a shortlist. But there was a long list of every firm you could talk to. And I think we mailed out 60 CIMs (Confidential Information Memorandum), and we got 10 LOIs. These are the kind of numbers you're talking about. And I don't think that was an extensive process. I think it was a fairly typical process. And the bankers swear to god that this was not “spray and pray.” Like, we're just "I'll give everybody a book." And he's like, "No, no, we're going to look at which people get a book and which don't, and we're going to be thoughtful about this. But we really think there are 60 firms who have a viable interest in buying this business."

The other thing I'd say is, don't forget, a lot of VC firms are kind of crossed over. The VCs don't necessarily like giving away all the downstream equity to growth PE, right? In some ways, if I were a VC, I might view them as parasites. So a lot of them have created their own growth funds. In the early days, I think they worked with their own preferred growth stage VCs. And then I think the bigger ones certainly have created their own growth funds. And the reason they're separate, by the way, which may not be obvious to people, is they need to have different expectations for the limited partners.

A classic, you know, Sequoia numbered funds, Sequoia 12, Sequoia 20, whatever they're up to now, that fund is an early-stage fund aiming at swing for the fences, home run investments, and long timeframes to liquidity. Whereas a growth fund is looking to double or triple its money maybe in four to five years.

AM: Dave, thank you very much for this fantastic interview.