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Venture Capitalists Put Market before Product

By Trevor Loy, General Partner, Flywheel Ventures

When searching for investors, many entrepreneurs and inventors first present their product or technological innovation and then vaguely present the target market as “people who need this product.” But this isn’t how customers think when deciding whether to spend money.

Consumers start with a problem or “pain point” they desperately want to go away. They watch for anything that proposes to solve this problem. Discovering it, they decide whether it’s affordable or whether another product offers a better or cheaper solution. They might even decide they’re willing to live with the inconvenience if the solution is too costly.

The most successful venture capitalists first want to know how well the entrepreneur understands the target market’s problems. Only then do they want to hear about the solution.

Defining What Ails Us

The most compelling investment for a venture capitalist is one that has a meaningful number of potential customers with this same “pain point” and a strong desire to live without the pain. These potential customers must have the financial resources to buy the remedy, and they must be willing to pay more than what it costs the entrepreneur to make and market the product or service. These potential customers must be identifiable. They must be easy to contact, sell to and support. And there must be a way for them to express their delight with a product so that demand builds the way a virus spreads — exponentially. That’s the kind of rapid growth that attracts the attention and resources of a venture capitalist.

Fewer than 10 percent of entrepreneurs start by identifying a problem and then attempt to develop a product or solution that targets that opportunity. For this reason, I teach students in my entrepreneurial business classes to thoroughly analyze the market before they spend any time on a business plan. This approach forces students to describe all the elements of a compelling market opportunity from the customer’s perspective without proposing a possible solution. If it looks profitable to present a solution, that’s when the inventor needs to offer it.

Getting Their Minds Right

Entrepreneurs with science and engineering or manufacturing and operations backgrounds have an especially difficult time shifting to a mind-set that puts the priority on analyzing what a

customer would buy and not on the product. They often seem unable to embrace the idea of exploring a market opportunity unless they have already chosen a specific product or solution they want to bring to market. This subtle misjudgment of priorities drives most venture investing mistakes and might account for the poor performance of the industry in the past 10 years.

The product or service is essential, of course, but its conception should be driven by what will serve and delight customers by solving their problems and eliminating their pain. Most successful entrepreneurial teams can take the proper approach by adopting disciplined and efficient “customer development.” This involves seeing things from the customer’s perspective and constantly tweaking the product or solution until it holds the greatest and widest appeal.

Flywheel Ventures manages several funds, including the New Mexico Gap Fund, which invests up to \$200,000 in seed-stage business ideas. For more information, visit www.flywheelventures.com.

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