VentureKit Radio #1: How to Fundraise with Brendan Baker

https://www.venturekit.com/baker

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Mark Goldenson: Welcome to the first VentureKit podcast. I'm Mark Goldenson. VentureKit is a new blog that publishes free startup guides to help entrepreneurs get things done. I started VentureKit because I'm a four-time founder and I felt how hard it is to find actionable startup advice. I've talked with hundreds of founders who say a lot of advice today is bullshit. It's often too abstract, irrelevant or just plain wrong.

Mark Goldenson: I want to bring you startup advice from domain experts that's detailed and actionable. No bullshit. I plan to bring you checklists, decision trees, pros and cons, guidelines, exceptions, the nuances that define good execution. It's a hard goal, but I think it's an important one.

Mark Goldenson: Our first podcast is about how to fundraise. I interviewed Brendan Baker, who was Dealflow Manager and 2nd employee at AngelList. He reviewed over 8,000 deals and helped hundreds of startups raise funding. Brendan also worked at Greylock, a top venture capital firm that invested early in Facebook, LinkedIn and Airbnb. He most recently started Fabric, which he describes as a coworking community for quietly awesome people.

Mark Goldenson: I've had my own experience with fundraising, raising $27 million across three startups. The most recent was Breakthrough, an online therapy startup that signed over 30 health insurers and covered 10 million people before being acquired.

Mark Goldenson: My talk with Brendan covers how to contact potential investors, create a fundraising narrative, run a pitch meeting and close investors. This podcast assumes that raising capital is right for you and that you know roughly how much to raise, neither of which is a given. We'll cover financial modeling in the future to help you determine the right amount to raise.

Mark Goldenson: One disclaimer - this is my first podcast and I'm getting over a cold, so I apologize for all the kinks. Hopefully, we will work these out over time. Let's get started on how to fundraise with Brendan Baker.

Mark Goldenson: I started by asking Brendan about finding investors. How do you decide which ones to target?

Brendan Baker: I think there's a bad way and a good way. I think they bad way is to ask people, "Can you think of any investors that would be interested in my company?" What you don't realize when you're asking somebody that is that it's actually a pretty difficult cognitive problem to match your specific stage and focus and progress as a company with an investor who may be interested. I can use myself as an example, because I get asked this all the time. I don't know how many investors I know. Maybe 20, 30, 50, something like that. But, invariably, when somebody asks that, I'll come up with like three names, because that's all I can do. So, that's the bad way.

Brendan Baker: I think the better way is to do the work beforehand. Come up with a set of targets, and put that in front of people. It's much, much easier for people to react to information than to create it. If you build your lead list, start putting it in front of people who can help you.

Brendan Baker: Now, if you have 200 names, don't put 200 names in front of them, but put 20 or 30 or 50 and ask them. Who do you like here as an investor? Who do you not like as an investor? Would you grade them one, two or three? Then ask them as well, "Do you have a relationship with that investor, and how strong is that relationship?"

Brendan Baker: When you get that information, don't use it right away. Just collect that from the people that can help you around you, and then when it's time to target them, go through the most, the strongest paths to reach those people, and do it sort of as a batch process.

Mark Goldenson: You can create your target list through AngelList, Crunchbase and just googling. Focus on investors who invest at your stage, in your market, and have invested in the last three to six months. Some firms will have a public presence, but be conserving funds or entirely tapped out. Also, be aware that some firms say they invest in the earlier stages, but actually rarely do. They say this to get early looks at you and will waste your time. Do the upfront research to prevent that. Next, how many investors should you target for a seed round, and how long does fundraising take?

Brendan Baker: A seed round or an angel round is a little bit different, because you just have to pitch a lot more people to raise a half million or a million or whatever it is.

You're probably going to have to pitch 50, 100 at the earliest stages, you're probably going to have to pitch 100 plus people, 150 maybe even. That just could take a long time. If it goes incredibly right and you're really efficient about stacking your meetings, it could happen in three, four weeks. Not the whole process, but like actually getting to commits. But, often it will take longer and in a tough environment or first time entrepreneurs, it's going to take months.

Mark Goldenson: How do you decide which investors to approach first? Do you start with your safety school investors, the ones that you'll accept but are not that thrilled about? The second tier that you'd be excited about, but maybe not the most excited about, or do you go right for your first tier, the ones you really want most?

Brendan Baker: Do not go for the first tier first. Don't go pitching Sequoia first. Look, the caveat is if anyone is really close to the effort, you know, they've known you for a long time, advisors who want to invest money, you know, get the money from them. But, I think we're talking about investors that you don't know. I particularly like just ranking one, two and three, because I think this is pretty easy. I wouldn't take a ton of time to do it, but who would be your first choice, who would be your second choice and who would be your third choice. These should be relatively large groups each.

Brendan Baker: I like pitching the second choice investors first in the process. I like doing that because, you know, in spite of practicing, your pitch is going to suck at the beginning. It's just a, you know, a fact of nature. So, with a rough pitch, you don't want to be wasting that on your top choices.

Brendan Baker: The second reason I like pitching the second ones first is that the company is going to look very different with a couple hundred thousand dollars in the door than it will when it's, you know, about to go broke, which is the start of every fundraising process it seems. So, when you go to your first choice investors, which will be next, you might have money converted from the second choice folks, and that's going to help convert your top choice investors. I would say the third choice, the last, I mean, they are truly your safeties if everything goes wrong, but ideally, you'd rather that they're not in the company.

Mark Goldenson: I see founders approaching fundraising serially sometimes, where they do one investor a week and then the process tends to drag along. So, I think a parallel process works better, but how many investors do you think typically a founder should be talking to at the same time, and related to that, should there be a start and an end date that is communicated to investors, or should it be more open-ended?

Brendan Baker: Like, serializing a fundraising process is a disaster. It's going to be a disaster emotionally, because it's just going to drag on a long time. Every week with one investor potential. You know, rejection from that is just going to be catastrophic, and it's going to be, from a perception point of your company, it's also going to be a disaster. It's going to feel like you're in the market for a long time, that it's not working, et cetera, and that there's no energy around that fundraiser.

Brendan Baker: So, you want to do it in parallel and you want to jam it as concentrated as you can. You want your calendar to be stacked with pitch meetings for a smaller number of weeks. I don't know what the upper limit of that is. It really depends on how superhuman the founder is, whether you're doing phone pitches, whether you're in a place like Silicon Valley, where you can meet four or five people a day if you're really crazy, but you really want to be pitching multiple investors per week for sure and hopefully even more.

Mark Goldenson: Next, Brendan talked about what success rate you should target for investor pitches.

Brendan Baker: It's hard to get a rule of thumb because it varies a lot, but I usually think if you're converting 10% of your pitches to money, that is acceptable. You're doing okay. If you're not converting, you know, if you're converting a lot less than that, there's something wrong. Figure it out and then go back out. Don't just keep pitching.

Mark Goldenson: I heard someone at YC describe this as when you are raising and it's not going well, the horrible sucking sound of sucking through a straw and there's no liquid in the glass. That's when you know to stop and maybe build on your metrics before you go out again.

Brendan Baker: I think it's always going to feel like that, or it's like often going to feel like that at some point in the process, but if it's constantly feel like that, yeah, 100% there's something going wrong.

Mark Goldenson: In my experience, a small percentage of companies are clear yeses, many are clear nos, and the rest are in a big, gray middle. I asked Brendan how he estimates the fundability of pitches he saw at AngelList.

Brendan Baker: Well, it totally depends on the type and stage of investor, but I usually go back to my AngelList experience. That was 8,000 different pitches. It was clear that about 5%, maybe 10, but I think 5 were just obvious yeses. We're going to help these people raise money. We're going to spend time, et cetera. I would say probably 50% to 60% in that case were obvious nos. You know, it's an open platform. There's a lot of stuff that comes in that is not super credible. Then, you're stuck with this 30% or 40% where you have to make decisions around. That's the tough stuff. That's where you spend 80% or 90% of your time trying to make decisions around.

Brendan Baker: In a later stage venture context, I think it depends on new firms, but that's probably a smaller window. That's probably 10 or 20 or 30% are kind of difficult. They may be, "I take one more meeting," difficult, or they may be, "I really struggled with this decision over two weeks," difficult. But, that's the reality of where most entrepreneurs are. They're credible enough. They probably can raise the money if they tell a great story, if they manage a process well, if they get through it, if there's a little bit of luck for sure. But, it's not a slam dunk, and this describes a lot of entrepreneurs who fail, that you don't hear about. They could have done it maybe, if things broke right.

Brendan Baker: It also describes a lot of the ones that succeeded. When you see a headline on TechCrunch or something like that, you know, ex-founder raises $30 million, it might have been really tough for them. We just don't know. It seems that every single company has at least one round that is really difficult, if they live for long enough. Every single fancy name has been through this, so it's almost universal, I've found.

Mark Goldenson: Next, we talked about creating your fundraising narrative. What defines a great narrative?

Brendan Baker: Any good founder is going to be able to come in and describe the execution of their company and the details. They're probably also going to be able to describe what the vision for that company is, and what they want it to be in 5 years, 10 years and the impact that they want it to have in the world. Very, very few of them are great about describing how the world is changing and how that vision fits in with how the world is changing. The best entrepreneurs, when they get up to that level, they really start to speak to investors, because that's where investors live.

Mark Goldenson: An analogy about this that I love is the Idea Maze, coined by Balaji Srinivasan, Andreessen Horowitz. To quote Balaji, "A good idea means a bird's eye view of the maze. Understanding all the permutations of the idea and the branching of the decision tree, gaming things out to the end of each scenario. Anyone can point out the entrance to the maze, but few can think through all the branches." If you can verbally and then graphically diagram a decision tree with many alternatives, explaining why your particular plan to navigate the maze is superior to the ten past companies that fell into pits and 20 current competitors lost in the maze, you'll have gone a long way towards proving that you actually have a good idea that others did not and do not have.

Mark Goldenson: This is where a historical perspective in market research is key. A strong new plan for navigating the idea maze usually requires an obsession with the market, a unique insight from deep thought others did not see, a hidden door. Sometimes, you can get past a particular Minotaur and enter a new market, but only after you've gained treasure in another area of the maze, like Google going after email, after it made money on search.

Mark Goldenson: Sometimes the maze itself shows over time, and new doors open as technologies arrive, like Pandora on the iPhone. Sometimes there are pits that are uncrossable for you, but are crossable for another, like Webvan failed, but Amazon, Walmart and Safeway have the distribution muscle to succeed. Sometimes, there are pitfalls that are only apparent when one company has reached scale, problems which require entering the maze at the very beginning with a new weapon. Google PageRank was inspired in part by AltaVista's problems set scale, problems that were not apparent in 1991.

Mark Goldenson: A bad founder is just running to the entrance of say, the movies, music, file sharing, P to P maze, without any sense for the history of the industry, the players in the maze, the casualties of the past, and the technologies that are likely to move walls."

Mark Goldenson: Every market has its own maze, and no one has a perfect view of it. You can learn the maze through history, theory and experience. This is critical for creating and effective fundraising narrative. Show you know the maze better than anyone, and you can tell a compelling story about why you will find the treasure.

Brendan Baker: Totally. The most exciting way that comes across is like, there's an aha moment, or an entrepreneur teaches you something that you didn't know, and you see it, and you sort of say, "Shit, you're right. That is a window. That is really exciting. I didn't know that before." Not a lot of people will know what you know, and that's a great place to be starting a pitch.

Mark Goldenson: Right. Michael Seibel from YC calls this the unique insight, and he's always looking for, what is the unique insight that this startup, this founder has and no one else does?

Brendan Baker: One of the things that you reminded me of, as you said that, I emphatically agree. It's really important to be specific in your pitching. It's important to be specific in your framing of what you're doing, but also, as you're saying Mark, how you're getting to market, how you're getting to these large groups of people or companies, being specific I think is scary. It's scary for a lot of founders, especially early on because if you stay vague and general, you can't be called out. You can't be challenged, but you also don't excite people and, like you're saying, you don't demonstrate any unique insight, or unique knowledge about the problem. So, I challenge founders to be as specific as they can about what they're doing and how they're getting there. It feels risky, but you've got to put yourself out there in that way.

Mark Goldenson: Founders are often especially wrong about their market size. They cite market sizes of the super broad market they're in, like the $200 billion market for mental health care, instead of the smaller slice they're actually serving, like the $1 billion market for online therapy. Be as narrow as you can while still targeting a roughly $1 billion market. You'll show discipline and credibility and reduce the number of direct competitors. Brendan talks about competition from the investor view.

Brendan Baker: You know, one of the things that founders don't get to see is all the other pitches that investor has see in the last week or month or year. They're not going to see that they've been pitched by 30 other companies that are roughly in that large, what did you say, $100 billion health care market. You need to differentiate and you need to be unique, so it's by zooming in to that $1 billion opportunity that maybe spans into a couple adjacent opportunities, that you become one of five to consider, or one of three to consider, instead of one of 100 to consider.

Mark Goldenson: Right. I know founders then worry about, well, are we just going to be limited by that one market, but I think in a lot of markets, the right strategy is to get in and dominate a field of it, an inch of it, a segment and then that often gives you the opportunity to expand horizontally or across the value chain.

Brendan Baker: You can communicate that too. That's exactly right. You can start by saying, "Here's where we're starting and here's where we're going," and 90% of the pitch is talking about where you're starting in that initial market, and you can then end the pitch with 10% or maybe, you know, seed it at the beginning with, "Ultimately, we're going to this bigger place than this first market, but we get there through the first market." That works well because you combine a sense of focus with a bigger vision that can be exciting down the road.

Mark Goldenson: Right. Amazon started in books, and Facebook in colleges, eBay in collectibles, and now they dominate much broader categories.

Brendan Baker: Although, if Bezos has been going and saying, "We're going to start with books and we're going to end with fundamental hosting and storage layers on the internet," he would have been kicked out immediately in those pitches.

Mark Goldenson: Yeah. I saw this image recently of him back in '95, '96, and the caption was something like, "I'd like to sell you some books." Now, it's 2017 and he has this badass jacket and you imagine explosions happening behind him and the caption is, "I'm going to buy fucking everything."

Brendan Baker: Yeah, that's confidence. He's earned his confidence, I guess.

Mark Goldenson: Next, once you've drafted your pitch, how do you get good feedback on refining it?

Brendan Baker: I would assemble a group of, I don't know, 5, 10 or 15 people around you. You call them your "team", who can help you through this part of the process. Pitch them, and have them give you feedback. Now, who you choose to pitch here matters a lot. You want people who know their shit, people who want you to succeed, and people who are unafraid, obviously, of giving you clear, candid, sometimes very difficult feedback. The best group that fits into these three categories are other entrepreneurs who are a step or two ahead in the process. So, find a dozen other entrepreneurs and pitch them.

Brendan Baker: When you do that, there's one structured way that I like to help them give you great feedback. I would give each one of them a piece of paper. I would get them to draw a line down the center of it, a vertical line, and put E on one side and H on the other. E stands for excitement. H stands for hesitation.

Brendan Baker: The reason you do this is you want to help them surface the things that they find exciting about the narrative that you have, and the things that are tripping them up. The things that cause hesitation. So, an exciting thing could be the market could be incredibly interesting. Either you're talking about an obviously interesting huge market, or you're teaching or opening their eyes to something that they didn't see before. That could be very exciting. A hesitation might be, is this the perfect team composition. You can't change that when you're going out to pitch in the near term, but you know you want to be able to speak to that and allay fears and hesitations of investors.

Brendan Baker: So, if you do this with 10 people, you'll collect, you'll start to see the same things that people get excited about and the same things that people are hesitating about in your pitch. Then, you can sort of work that into the pitch in a better way. Address the hesitations and make sure the exciting things are up at the front, super clear.

Mark Goldenson: Now, if you don't know five to 10 founders to help you with this, you can find them. Get intros to founders you admire, go to high-quality meet-ups, even cold contact if necessary. Founders usually welcome new connections and having a strong network of fellow founders will help you a lot, personally and professionally.

Mark Goldenson: Moving to creating a pitch deck, I asked Brendan what mistakes he most often sees in them.

Brendan Baker: The first one is a general one. It looks like a menu or just a sequence of slides. This is the problem, and this is the solution, and this is the product, and this is the market, and this is the team. Those pitches suck, and they work a lot less than you would like. So, this is why we talked about a narrative. A narrative is incredibly important to build in a cohesive way.

Brendan Baker: One of the interesting things that I saw at AngelList, in the early days, long before it was a platform, it was just a Wufoo forum, and we had a bunch of fields. In screening hundreds and ultimately thousands of these, you learn to look at different parts of that application as indicators of whether a company was serious.

Brendan Baker: One of the things that I loved was looking, you know for a while, we had a question that was something like, "What is your distribution strategy? How are you going to reach people?" Probably 90% or more of answers, maybe even 95% or more, said something along the lines of, "Our product is going to be fucking great." Right? Maybe they use words like viral. I saw so many times, "Our product is inherently viral." We will just build this amazing thing and it will get out into the world and people will come crashing through the door. Anybody who is listening to this podcast probably knows that's fiction and it doesn't work that way if you're not Pinterest.

Brendan Baker: So, I looked at that specific field as an indicator of how sophisticated those founders were, and the ones who came back and said, "Oh, here's the three steps for distribution, how we get in front of people," I actually cared a little bit less about what was in that answer, but that they had some depth of answer there.

Mark Goldenson: Brendan is highlighting that investors often care more about your thought process than your initial decisions. They expect that early on, you'll make a lot of pivots. How you test hypotheses, collect feedback and adjust quickly is key. Brendan talked more about what founders get wrong with pitch decks.

Brendan Baker: The thing that they get wrong all the time is that they bury the lead. So, there's probably one or two or three, maybe things that are incredibly compelling about any individual company. There aren't twelve, right? In the worst cases, you'll find something incredible as the fifth bullet point on the eleventh slide, and you just want to scream at the person, "Why is this not on the first slide or second slide or third slide?"

Brendan Baker: Now, those strong things could be anything, right? It could be the traction or speed of progress for this company could be phenomenal. Make sure that is somewhere in the first three slides or sixty seconds if possible in the pitch. It could be this team is amazing and perfectly suited to tackle this problem. It's going to be different for every company, but you need to figure out what the really exciting things are in the pitch and get them up at the front.

Mark Goldenson: Brendan is right, and a sad reason is that investors typically have short attention spans. Hook them in the first few minutes to try to overcome that. We next talked about how to convey one of a pitch's most important elements - traction.

Brendan Baker: You have to first understand what traction is, which is your story of momentum told though evidence of market demand. So, it needs to be a story that is compelling. It can't just be a bunch of charts. It has to be evidence-based, and it has to be about demand. So, let's please not use testimonials or press. That is not traction.

Brendan Baker: The reality is that, especially the early stages before everything is figured out, I think a lot of founders feel really bashful about their traction, because they look at the headlines and they see that so and so company is at millions and millions of users or whatever. The reality is that describes almost every early stage company who is still trying to figure it out. So, you have to dig a little bit deeper. We're not going to be able to solve this on a podcast. I find this is something that can be done pretty effectively if I would with companies for 20 minutes or 30 minutes and we sort of poke around at what's happening.

Brendan Baker: But, there's a hierarchy, so you want to think about revenues. If you have any, use them at the beginning of the earliest stages especially, because it might feel super bashful to say, "Well, we have $10,000 in revenues." It might feel like a small number, but most early stage companies don't have any, so it's kind of a differentiator. You want to talk about top line, other sort of numbers of customers, clients, or users.

Brendan Baker: But, I think the really rich stuff at the early stage is around engagement and how people are using a product or a service, how crazy they are. Can you define who the crazies are? Like, active users are people who open the app three times a week and do X action. That's 40% of our user base is active users, and they are crazy. They do this and they do that and they do the other thing, and look how much they love it.

Brendan Baker: So, a lot of what can overcome a deficit of top line traction at the early stages is just talking about what's happening and how people love it, but expressed through numbers, and expressed through very quantified evidence of that love for their product.

Mark Goldenson: Right, especially if you can paint a credible picture that, even if the initial numbers are small, there are all of these other people that have not been reached yet, who are just like them and the funding is going toward reaching them.

Brendan Baker: Totally. There are ways that you can communicate that too. Maybe there's a waiting list. Maybe there's, if it's more of a team-based enterprise product, you're starting to see how it's spreading between teams and a company or it's spreading from company to company, and there's early indications of that, so you're absolutely right, that those early metrics around how stuff might spread, even if it's really faint, can be pretty interesting.

Mark Goldenson: Translating all of this into a pitch deck is a big task. So, I published a detailed guide with 60 examples on how to create each common slide. You can find the guide at venturekit.com/pitchdeck. I also recommend Brendan's post about story boarding, which you can find by googling Brendan Baker story boarding.

Mark Goldenson: So, you have your pitch deck and you've scheduled pitch meetings. How should you deliver the pitch? Since investors seem to like bold founders, should you amp up that boldness? Maybe even be brash?

Brendan Baker: I feel very strongly about this, because certainly in Silicon Valley, we really value one or two standard assertive, fairly masculine types of confidence, right? People who are staring these daggers of confidence through our wall, through the wall. Those people tend to succeed in fundraising, probably disproportionately to the actual quality of the companies.

Brendan Baker: So, I'm a little bit more subdued. I'm a Canadian. I tend to over apologize and caveat. I can be confident. I have my own type, but it's not the super brash Silicon Valley confidence. I think it can look even different when you don't look like our stereotype founder. You don't come from the same place. Maybe it's that you're not Caucasian or you're not male or you're not 20 something. Maybe it's different than that. So, I'm really interested in figuring out where everybody's unique confidence comes from. That's a personal thing for everybody.

Brendan Baker: I can tell you how I get it in these situations. Usually, I always believe in the problem I'm trying to solve, even if I don't know how I'm going to get there. So, when I'm challenged on something, I can usually go back to, "Well, fuck, I really think this is important. I really think the world is changing in this way. I really think there's an opportunity and I really think it's going to be solved by us or somebody else in the next 10 years." Usually I can use that as confidence fuel on myself. I think everybody will have a different answer, and it's important to figure out where your particular version of confidence comes from. It probably doesn't hurt of have some pump up music that you throw on the headphones in the parking lot as well.

Mark Goldenson: Next, we talked about hard questions. How should you handle them? Especially when you don't know the answer.

Brendan Baker: You know, one of my favorite investors and people in the industry is John Lilly and I've been in a bunch of pitches with him and he's really intelligent and he really thinks carefully. Sometimes when he is really engaged with a pitch, the questions are challenging. Sometimes that comes off well. Sometimes it doesn't, but from his point of view, it's really coming from a good, engaged, supportive place, but they're hard questions. You want hard questions as a founder. It means that people give a shit.

Mark Goldenson: Right.

Brendan Baker: The worst thing is that an investor doesn't give a shit.

Mark Goldenson: Right. Then also, when those questions get hard, I see founders who make up answers or strain their credibility, where it seems like admitting you don't know is a better approach, but when is it wrong to say you don't know?

Brendan Baker: I mean, it always feels difficult to admit that you don't know. We've all been in a pitch or in front of a class or something like that where we don't know the answer. I give founders a lot of points for saying they don't know, but then having something intelligent to say afterwards.

Brendan Baker: This usually means, "Well, I don't know, but here's how I think about this problem." If they can go into it on one or two levels of depth, and tell me how they're going to figure that out or how they're going to discover that in the future. I mean, an early-stage company is a collection of unresolved questions and admitting that's the case can be powerful. But, you want to know that they're thoughtful behind that, and that can work really well.

Mark Goldenson: Throughout the pitch, it's critical to maintain your credibility. Professional investors hear grandiose pitches every day, so they have very sensitive bullshit detectors. Think of your credibility as a pane of glass. Every lie, inaccuracy, or even exaggeration you tell cracks the glass, and it takes only a few of those for your credibility to break, so admit what you don't know, do not overstate, definitely do not lie. Err on the side of credibility. Investors are deciding whether to invest serious money and time into you and they will only do that if they trust you.

Brendan Baker: I'll say one more thing is I think it is terrifying for entrepreneurs to be challenged, especially dismissively or aggressively about what they're doing, because let's be honest, I mean, most companies are just expressions of their founders. There's something that was not created before that they brought into the world that is deeply, deeply personal and there's a bunch of people who are dismissively saying, "This is shit," which is essentially saying that you are shit and you don't deserve to exist in the world. So, that is pretty tough existentially, and I think that happens under the surface with founders a lot.

Mark Goldenson: Next, how do you know when it's not working versus you just haven't met the right investors yet?

Brendan Baker: You know, if you're hitting real subject matter experts, like people who know your area of the world really well, we talked about this before, right. If they're asking really good questions, very specific questions and they're engaging, if those people aren't investing money then you definitely have a problem.

Brendan Baker: It doesn't mean that you're not going to be able to raise from investors have more sort of widespread or horizontal world views or don't know your area quite as well, but if you pitch 10 people and they're asking excellent, deep questions about what you're doing and you're not raising from them, that's a pretty big indication.

Mark Goldenson: Let's say you've pitched a set of investors and some of them are interested, but haven't yet committed. How do you close them?

Brendan Baker: This is incredibly hard because many investors are creatures of FOMO, so they'll try to buy as much time as they can to collect more information and make a decision that is probably pretty hard, until they're going to run out of time and they'll act incredibly quickly.

Brendan Baker: So, you'll see founders try to create forcing functions in different ways. Usually that means there's an end date. You need to make your decision by X day. The round is closing, or this portion of the round is closing or the price is going to go up in a month or something like that. I'm generally in favor of setting those forcing functions because how else are you going to force someone to make a decision. But, you just, it's a little bit of a delicate dance and you'll just have to know that people are going to blow past those somewhat arbitrary end points pretty regularly and then you have to think about what you're going to do.

Mark Goldenson: A key tool in closing seed investors is offering better terms for committing early. You can do this if you structure your round with a safe or a convertible note. I won't dive into the legalese here, but look up Y Combinator's primer on safes to learn how you can change two specific terms - evaluation cap and the discount rate - to incentivize some investors to commit early and get the rest to be in or out. Just be sure to track all your shareholders and their future potential ownership in different scenarios. You can ask your lawyer to do this or use a more affordable tool like Carta or Capshare. This will help you avoid sticker shock around dilution.

Mark Goldenson: Next, how do you know what's a fair valuation?

Mark Goldenson: So, let's say you've got now a term sheet. A question I hear founders talk about, and I've thought about myself is, how to know whether it's fair. How would you answer that?

Brendan Baker: What the fuck does fair have to do with anything? This is a market. I mean, I'm not trying to be insensitive. I just want people to understand that it's not a reflection of their inherent value. They're just in a market for startup shares and they're competing against another 99 startups for that investor's time.

Brendan Baker: The term sheet is going to come down to, you know, the excitement of the investor, the conviction that investor has, the sense of scarcity if they're competing with other investors, the timing. Like we said, AI, it was a great time to raise around AI startups probably one, two, three years ago. So, they all had more fair term sheets at that time regardless of how good the companies were.

Brendan Baker: So, I don't think fair matters. I think understanding the market is very important, getting data points about the market. Also, understanding the intricacies of a term sheet and which terms are important to you. Which are commonly accepted? Which ones are egregious? You can do this by having a good lawyer that knows the market. You can also have a couple of advisors who have been through this before and help you get into the weeds of a term sheet, but there's not such thing as fair.

Mark Goldenson: I think you're underscoring the difference between price and value that we founders can think the company is worth a certain amount, probably more than most would say, but ultimately if investors are going to pay only half for the right of putting in money, then that is the current market value until we find something otherwise. I've felt this with domain names where you can think a certain domain name is worth $5,000 and the guy who owns it is saying it's worth $50,000, and if you can find one crazy person in the world who will pay $50,000, it's worth $50,000.

Brendan Baker: Absolutely.

Mark Goldenson: Finally, I asked Brendan about his current project, Fabric.

Brendan Baker: Yeah, we call Fabric a work community for quietly awesome people. We want to be kind of the anti WeWork. I think it's incredibly lonely to build something or it's lonely to work remotely or it's lonely to work as an independent consultant. I felt this in my last sort of side project company where it ended because I felt isolated and alone, so Fabric is about figuring out how, when we leave traditional work environments, we don't lose all of the benefits of a traditional work environment, like the relationships with people, the value of other people, some of the systems, so of the sharing of goals. We're figuring a lot of this stuff out, but it's community first, and it's space second, and it's been that way since we started out of my apartment about a year and a half ago.

Mark Goldenson: If you want to learn more about Fabric, go to workwithfabric.com. Sincere thanks to Brendan Baker for being so generous with his time. If you're a startup looking for an advisor, I highly recommend him. That's a wrap on our first podcast. I hope you've enjoyed it. Subscribe to future podcasts and read more guides at venturekit.com and reach me at mark@venturekit.com.