Representative Lessons Learned by General Partners of Latin American and Caribbean Venture Capital Funds

The fund managers in emerging markets face a difficult task. Not only must they operate within an evolving marketplace, but they are also trying to create value in young companies. Often, the management teams are unaccustomed to active minority investors, and sometimes resist their recommendations. Should the management teams fail to perform, finding replacements can be difficult and time consuming. New investment teams may find that every move is scrutinized, not just by their limited partners and management teams but also by policy-makers who want to be sure that the program succeeds.

The following two accounts were written by general partners (GPs) active in the early stage investing sector. One is based in Brazil and the other in Uruguay. Their lessons learned demonstrate the evolution of a market and the process of discovery that the firms have experienced. Their lessons learned touch on all aspects of the venture capital cycle. In the deal origination process, teams mentioned the importance of hiring specialists to help understand the company’s management, technology, and market more deeply. Others expanded their due diligence conversations to include midlevel managers, not just the senior team. To improve company performance, the teams actively invested in management education, even to the point of recruiting mentors to provide individual coaching and, possibly invest as angels. Another firm sought to develop innovative investment securities that would balance the market’s state of evolution, particularly its uncertainty about classic venture capital valuation techniques, with the firm’s need for adequate risk compensation. These accounts also detail changes in the firm’s internal structure and processes in terms of communication and hiring as result of their experiences.

These accounts depict a vibrant venture capital landscape. To succeed, teams must be willing to experiment and pay careful attention to the results of their efforts, continuously revising their approach as the system around them changes.

We thank the teams who took part in this competition for their efforts and commend all of them. They represent a key part of the evolution of the venture capital ecosystem in Latin American and the Caribbean.
Lessons Learned: A change process case at CRP

CRP Companhia de Participações

INTRODUCTION

After 31 years, CRP has acquired a unique expertise in the Brazilian market. With nine funds under management, 69 investments and 41 divestments since 1981, CRP is the leader in terms of number of investments in the Brazilian Venture Capital and Private Equity industry. CRP has always taken a minority investment approach, based on a strong relationship with the entrepreneur/business owner. Year over year, CRP evolved its management process. Most of these innovations came out from lessons learned, as demonstrated in the four cases about experiences from our RSTec fund that will be highlighted in this article. At the end of the article, we will show how things changed internally in CRP in response to these lessons.

In 1999, CRP launched its third fund, RSTec with committed capital of US$4.4 million. This was a venture capital fund focused on startups, early stage and small innovative companies, in terms of both product innovation and management process innovation. The Fund’s investments were restricted to companies located in Rio Grande do Sul State, where CRP headquarters are located. The RSTec Fund invested in 15 companies (10 divested – 7 buybacks and 3 strategic sales; 4 write-offs; and 1 currently being divested). The portfolio was composed of 40% startup companies (no revenues), 47% early stage companies (revenues but no profits) and 13% small companies.

RSTEC: LESSONS LEARNED

Case 1 - A Software Developer

The investment was made in 2003. At that time, another venture capital firm already had a minority interest in the company. After three years of monitoring, CRP and the other shareholders wrote off the investment.

The Company was founded in 2003 to develop unique software tools for developing new software/systems programs and serving as a repository of knowledge about the data model, business rules, and systems frameworks. During the due diligence process, the product’s unique benefits (productivity and usability, among others) were verified by technical experts.
Thus, we saw an opportunity to invest in a company with an innovative product that filled a pronounced hole in the market and where its technology allowed full integration with other productivity tools then available in the market. In addition, the Company had a structured and experienced team that had led the project since the beginning. Moreover, the CEO’s international experience in the sector would be a valuable asset during the Company’s international expansion, one of the major goals of the investment thesis.

At the time of the investment, CRP was already monitoring the Company closely. The major efforts focused on mitigating the execution risk associated with the Company’s action plan, which lacked focus and consistency. The business plan was oriented to the development of the international market, where productivity tools for software/systems programming were widely accepted and demanded. This strategy would also accelerate the likelihood of a strategic sale in a relatively short period.

The facts, however, presented a different picture. Perceiving the difficulty of exporting to the international market, CRP tried, but struggled, to establish a more consistent shorter-term strategy for the Brazilian market. CRP also tried to establish a consistent commercial plan and to reduce operational expenses (structure and people) to keep financial resources at a comfortable level and maintain the business in the long run. CRP was relatively successful and the burn rate decreased drastically, which provided momentary financial stability for the Company. Unfortunately, these actions were not enough for the company to maintain the ideal capital structure in the long term. The sales performance lagged the original projections and the expenditures remained excessively high, due to:

a. the inability of the top executives, most of whom had come from large operations, to manage a small company;
b. the difficulty in making the product work, the need for an additional outsourcing team to do implementation, and the high level of customization and training necessary to help customers adopt it; and
c. the customers’ cultural barriers against adopting the tools. This was not anticipated in the business plan and required paradigm shifts in the minds of the users and changes in the customers’ internal management processes for success.

The major lessons learned in this investment case were:

i) The need to implement a more sophisticated due diligence process to understand the business deeply;
ii) The need to evaluate the top executives’ profiles and skills to run the business; and
iii) The need to calculate the right amount of capital needed, in order to guarantee the Company’s growth in the projected investment period.
Case 2 - A Web Service Company

The investment was made in 2002. By 2004, CRP had already divested the position.

Some years before the Fund’s investment, the Company had been founded as a distance learning website. Over the years, the Company expanded its business to the web services customization market and started developing websites and integrating databases with an exclusive focus on corporate solutions. During this strategic shift, the Company began developing applications and software programs for PDAs (Personal Digital Assistants) and smart phones, a fast-growing new global market.

During the due diligence process, the investors concluded that the technological aspects of the solution did not seem to be a critical issue for the Company’s success. On the other hand, the commercial ability of the entrepreneurs/executives was critical, as this skill would reduce the risk of accessing a new market. Commercial success would increase the likelihood that the Company would generate higher revenues in the short term, normally a period of fragile cash flow for any early stage company. Also, because the market was new, there were no dominant software companies operating in the PDA market (mobile solutions). The Company had excellent opportunities to become the leader in Brazil and leadership in that market would enhance its value to potential strategic buyers interested in consolidating the sector.

The development team mastered the programming technology for producing mobile applications for PDAs. The main product, sales force applications, was very versatile and could be applied in several different sectors/industries without requiring major customization.

After its investment, CRP started helping the Company to implement the best corporate practices available. The Board of Directors was established and an external auditing company was hired. CRP also encouraged the entrepreneurs to do yearly rounds of strategic planning in order to reassess the original business plan and maintain progress towards the best growth path.

Even with all of CRP’s efforts and support, the Company could not reach its goals due to the lack of an internal management process and the CEO’s excessive centralization of decision-making. Additionally, misalignments amongst the entrepreneurs, in terms of dedication and commitment to the Company’s project, had an adverse impact on the Company’s daily operations.

The business’s continuing weak performance and the lack of management controls increased the risk that CRP was assuming in terms of potential contingencies. In the face of a continued slump, CRP decided to divest because it did not believe the business would recover and it wanted to mitigate any potential contingent risk such as lingering labor issues or unpaid bills. The Fund sold its stake to one of the entrepreneurs for a symbolic value and took a negative return on the deal.
The major lessons learned in this investment case were:

i) The need to evaluate the top executives’ profiles and skills deeply;
ii) The need to assess the entrepreneurs’ relationship to detect potential conflicts and misalignment between them; and
iii) The need to improve the monitoring process, focusing on the investees’ main projects and the way they are being managed.

Case 3 - A Broadband Internet Provider

The investment was made in 2000. After approximately 2 years, CRP wrote it off.

The company resulted from a joint venture between a service company that did maintenance and implementation of cable networks and a communication technology provider of products and services. The deal was syndicated by three investment groups, led by CRP.

The company provided broadband Internet access through high frequency radio technology. The goal was to supply high-speed Internet at a competitive price and with innovative technology, in a fast growing market, in which the major competitors were rapidly taking positions but lacked a competitive solution, as their services were slower and more expensive.

The Company’s technological knowledge and market positioning in the Southern Region of Brazil represented a good opportunity to expand the business to the whole country and to become the major provider of broadband solutions. Due to its proprietary technology, the Company’s service reached constantly higher speeds and met the growing demand for very fast Internet connections. The company’s technology capabilities gave it a unique position in the Brazilian broadband market, attracting the attention of investors and potential strategic buyers and offering the Fund attractive divestment opportunities.

In the merged company, CRP and the other investors played a very important role as an element of balance between the two operations and their entrepreneurs. The two groups of entrepreneurs had different profiles, one more conservative and the other more aggressive, which created conflicts. CRP was called upon to resolve several conflicts between the managers. In addition, the Company had a “family” (nonprofessional) management approach, which created fragile processes and insufficient internal controls and communication between areas. CRP pushed the entrepreneurs to establish an organizational structure based on a professional CEO, who was not related to the controlling families. Furthermore, CRP led the discussions to change the commercial
strategy from a “retail” approach to a corporate approach. This shift added value to the business.

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<td>iv) The need to establish a controllership area to support the portfolio companies from the beginning of the investment.</td>
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Case 4 - A Machine Vision System Solution Provider

The investment was made in 1999. After nine years of active monitoring, the company was divested with a negative internal rate of return.

The company developed machine vision systems. These systems have several applications, all related to controlling processes (production, logistics, among others) that would be almost impossible to do manually. The main objective is to reach a zero failure rate in any of the processes.

Despite facing few competitors, the Company never managed to capture the available market opportunities. The market for machine vision solutions in Brazil was quite new. The few clients that were interested in the technology demanded custom systems, which were high-cost due to state-of-the-art technology requirements, and not necessarily applicable to other potential clients, which precluded economies of scale.

The Company was initially oriented towards finished products that could be commercialized in specific markets. This idea contravened the tailor-made model that was prevalent in the market. The goal was to gain scale and to increase the Company’s commercial focus. The entrepreneurs had strong technical backgrounds but little experience in commercialization. CRP coached them about commercialization and eventually hired a specific team for this task. CRP also helped the entrepreneurs to stay focused on the commercial viability of the products, rather than their technological aspects.

Despite all these efforts and strategies, the market grew more slowly than projected and the product adoption rate lagged expectations, due to cultural barriers and lack of resources for new capital expenditures. Furthermore, keeping highly skilled teams was a huge challenge because of the frustration caused by slow sales growth. The Company’s need for working capital was constant and high. Efforts to gain scale and reduce costs were thwarted by the clients’ demand for product customization. In the end, the Fund divested its stake to the majority shareholder in a buyback deal.
The major lessons learned in this investment case were:

i) The need to evaluate the market size and perspectives more deeply; and
ii) The need to improve the monitoring process, focusing on the investees’ main projects and their management process.

LESSONS LEARNED

The lessons learned made CRP rethink its investment approach and internal processes, in addition to its organizational structure. According to the limited partners, business owners, and others related to the segment, these changes were quite innovative in the context of the Brazilian Private Equity industry.

The first innovation involved having an organizational behavior psychologist produce a psychological and profile analysis of the business owners and key executives. This new process was extremely important in helping us understand the profile of the leading executives and in confirming their capabilities and alignment with the business goals. Additionally, this understanding allows the Fund to better understand the business owners and guarantee an alignment of interests with them during the investment years, which is very important for a successful divestment. The new analysis also covers other aspects of the portfolio companies such as: identifying the synergies among the team; understanding the companies’ culture; attesting to the quality of the management team; and understanding the succession and the innovation processes, among others.

Another innovation in the due diligence process was our new approach of hiring specialists in management processes and business strategy as consultants to analyze the main internal processes (production, administrative, commercial and financial), the business strategy, and the major internal projects. The objective is to check the alignment of the top executives in certain areas such as i) how to run the business, ii) future projects and iii) business perspectives. This new assessment helped us better understand the business plan, along with how to act and where to focus to develop the business efficiently.

The lessons learned also improved other aspects of the due diligence process, such as the assessment of the market and the competitive environment, the evaluation of the business’s internal processes and relations with the companies’ stakeholders, and also helped us develop a consistent business projection to get a better picture of the companies’ potential growth. CRP implemented a standard due diligence structure that considered the main issues to be analyzed in a company, including the valuation models, based on the best practices of the industry. CRP also started doing a pre due diligence analysis of the accounting, tax and legal aspects of the businesses during the appraising process.
Another important change happened in CRP’s internal structure: the firm moved from a model based on individuals to a model based on areas. Likewise, private equity and venture capital funds and operations were separated when CRP launched its first Private Equity Fund, CRP VII in 2010. The partners were divided by profile to manage the main areas of the investment process (prospection, due diligence, monitoring and divestig). The new management model was important to avoid problems that could arise in the investment cycle when one of the steps is more demanding than the others and also helped establish standards to give more consistency to all activities.

The monitoring process also changed to cover all business levels. CRP had always interacted with the investees on the strategic, governance, and shareholders levels, with great involvement in decision making. Starting in 1999, a new process was implemented to better monitor the investees at the management level. In 2006, CRP increased its efforts to follow the companies’ internal processes more closely. In 2012, CRP brought the monitoring process to another level and began giving direct advice to the investees’ operational areas on how to manage the fundamental projects in order to increase the success of the business plan. This new process is driven by the investees’ needs as defined by the board of directors. The CRP team goes to the investees to do a diagnosis.
and to help them to restructure those processes that are not running properly. This teamwork approach ensures the efficient execution of the main projects. CRP’s controllership area also started to have more effective control over the investees’ accounting and financial functions and tracked the results with specific indicators and regular meetings with the personnel in these departments.

**Figure 4. Monitoring Process Evolution**

Additionally, CRP improved the overall qualifications of its own team. Since 1999, when RSTec fund closed, 18 more professionals were added, reinforcing all internal areas. All areas are led by a senior partner who interacts closely with the team to make the processes flow efficiently. CRP’s back office area handles the financial and administrative issues of the funds and is also led by a partner. The entire company is managed by the CEO who was one of the founders of CRP.

**Figure 3. CRP Team Evolution**
CONCLUSIONS

All the innovative changes in CRP’s internal processes, team structure, and investment process have come from its experience in funds management, especially the experience derived from the growth and performance problems of small companies—problems that experience has shown exist in larger companies as well. CRP is getting superior results in many areas and is more prepared to lead new investments because of all the improvements that have been made, beginning with a better prepared team. CRP’s pioneering efforts in the Private Equity and Venture Capital industry in Brazil were, and still are, important differentiators in the market. More importantly, its experience in the innovation improvements affected in all its processes, have prepared CRP to avoid hurdles along the way.

The RSTec Fund results were an important example of the perseverance of CRP’s team. Against all odds (vintage 1999), the CRP team managed to recover many of its investments and delivered very good returns. The Fund received an award from IDB as the best Turnaround Fund in 2011 and is expected to return a multiple of 1.5 times invested capital. Since the RSTec Fund, CRP has closed seven more funds.
Lessons Learned: A Case Study at Prosperitas Capital Partners

INTRODUCTION

Prosperitas Capital Partners is a financial management company that has established the first Venture Capital Fund (UIVC-I - 2005), the first Seed Capital Fund (Fondo Emprender - 2007) and the first experiences of Angel investing in Uruguay.

The funding of early stage companies and venture capital activity in Uruguay has grown considerably since 2005, but there is still room for further development. In our 8+ years in early stage venture capital, we have learned how much hands-on work is needed to make a company succeed in our region. These years of experience made us identify three areas in which we, as a venture capital firm, need to reinforce our investment strategy and staff. These include:

1. Identify the risk of insufficient management skills/awareness required in each stage of development of an enterprise. This factor is necessary but not sufficient for a portfolio company’s success.
2. Choose entrepreneurs with energy, passion and—most importantly—openness to feedback that will accelerate the company’s growth. This factor complements the previous one.
3. As a venture capital firm, be prepared to provide financing structures and follow-up financing adapted to the state of development of the country’s entrepreneurial ecosystem.

*www.prosperitascp.com/*
THE LESSONS

1. First lesson learned: Lack of management skills and how we tried to supply them.

The number and quality of entrepreneurs is expanding in our country and success stories such as CEPA and PedidosYa.com are spreading not only throughout Uruguay but also all over Latin America. As is inevitable in venture capital, however, not every company has been a success.

In both of our funds, we have seen several cases of promising companies with an interesting business model and identified customers that did not ultimately prosper. Seeking to diagnose the reasons why these companies failed, we realized there are different risks at different stages of a company’s development, although risks related to lack of basic management skills appear in almost every case. Most of our local companies have shown vulnerability in terms of execution and management issues related to selling skills and basic financial planning. The reason is that entrepreneurs often lack basic business knowledge and therefore design a weak business model or establish an ineffective strategy to reach customers.

In 2005 when we launched our first fund, UIVC-I, we had not identified this risk. Moreover, we believed that we would probably change or reinforce the management team some years after we invested, at the time that we prepared the company for its next level. This assumed, of course, that there would be a basic management team available.

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*www.cepasafedrive.com*
*www.pedidosya.com/*
Instead we discovered that while financing became more available in Uruguay, developing management skills became the real growth bottleneck. There was no ecosystem that helped enterprises develop these skills; furthermore, UIVC-I was the first experience of active investing in Uruguay.

After investing in several companies with high potential but poor execution, we realized we needed to be involved in their management. In the case of UIVC-I, we implemented both monthly board meetings and weekly business counseling and coaching encounters to train the team on basic management skills. The aim of these sessions was to develop reporting discipline with KPI’s, create a human resource structure, and provide selling skills and techniques, among others.

CASE: CEPA Safe Drive specializes in road security, accident prevention and fleet management for domestic and multinational companies, and governments searching to optimize their automotive fleets (for small, medium or large vehicles). Founded in 1987 by a group of traffic safety engineers, technicians, and experts, the company was not capitalizing on the market’s high potential. In 2007, the company stopped growing altogether. This made the entrepreneurs seek external advice. First, CEPA became an Endeavor company, which helped management consider the importance of planning for growth. When the company started conversations with Prosperitas in 2008, it did not have a sales force or a commercial strategy. In 2009, UIVC-I invested in CEPA. Recognizing these shortcomings, two of the UIVC-I partners generated a fresh vision for the company’s future. An organizational restructuring created a solid management team with the skills to face the new challenges.

In 2007, when we launched the seed capital fund (Fondo Emprender) we knew we needed to work closely with the companies on management development. Our challenge involved how to do so without a considerable increase in operational expenses for our fund. Our first solution was mentoring. We assigned one of Prosperitas’ partners or someone in our close network that had related expertise along with an analyst to follow up each of the 20 start-ups in Fondo Emprender’s portfolio. The mentor and the entrepreneur met on a monthly basis to analyze the company and brainstorm new ideas to address challenges. After one year with this plan, however, we did not notice any significant changes in the companies’ performance. We discovered that in most cases, the entrepreneurs kept working in their old ways without regard to the advice received. There was a breakdown between the recommendations supplied once a month by the mentor and the actions that the entrepreneur had to take on a daily basis. Mentoring was not enough, we found. We needed to take a more pro-active approach with more frequent involvement in the execution to get results.
Despite the general poor results, though, some of the 20 companies did show improvement. Where companies realized that the mentor added value, they wanted more of his time, which led to his investment as an angel. Mentoring itself was not a big success, except in those cases where the mentor expected to eventually invest as an angel. The sense of belonging and contributing not only with time, but also having a stake in the business, made the big difference in the company’s early stages. Fondo Emprender’s team played a key role by matching the needs of the company with the mentor’s profile and facilitating the process by working with them in the investment agreement.

**CASE: PedidosYa.com** is a leading online food ordering service in Latin-America. The company provides a service that allows users to quickly find restaurants with home delivery and order food online. Ariel Burschtin, Ruben Soenke and Alvaro Garcia, three ORT University students, founded the company. It received a grant from Agencia Nacional de Innovación e Investigación (ANII) to develop a prototype with support from the University (providing only technical mentoring). After the platform’s development, the next challenge was commercial. The entrepreneurs managed to capture the attention of Kentucky Fried Chicken Chile, which became the first client. In October 2009, Fondo Emprender approved a non-guaranteed convertible loan to the company and placed Rodolfo Oppenheimer, one of the Prospectives partners, as the mentor. Rodolfo invested in the company in 2010. During his interactions with the company, he prepared it to receive an international round of financing and coached the team for every meeting that took place with the international investor. As of 2011, the company has raised two additional rounds of funding and is planning the third. It operates in six countries within Latin America: Uruguay, Argentina, Chile, Brazil, Colombia and Puerto Rico, and is currently working with more than 3,700 restaurants including major brands such as Burger King, Kentucky Fried Chicken, Denny’s, California Burritos, Benihana, Romero and Itame Sushi.

**CASE: Biogenesis** emerged in 2002 as the first Latin-American company to produce top quality temperature and oxygen saturation sensors, as well as electrocardiogram cables for medical use. In 2008, Fondo Emprender financed the company to achieve international certifications. In early 2010, Biogenesis had to decide whether to build a plant in Europe or Brazil. The decision involved a strategic analysis and Prospectives suggested that the company start working actively with a mentor. One of the entrepreneurs was reluctant to receive angel investment from the mentor due to a negative experience with a previous partner in a previous company. After some months working together, however, the entrepreneurs decided that the mentor was an asset and they wanted him more involved. By December 2010, the mentor invested in the company. As of 2012, Biogenesis exports to more than 28 countries and is finishing the plant in Brazil.
Some companies, though, required earlier support to capture the angel’s interest. Often, angel investors looked for the entrepreneur’s concept to achieve some basic traction before getting involved. Therefore, we recognized that we needed to take a further step and incorporate basic management skills as a service in a new financial instrument that could scale. We needed to add these skills to our staffing, as big private equity firms do. The question was how to provide a senior team advisory service without stressing the financial instrument or the target company.

2. **Second Lesson Learned: What did we do wrong after adding management skills?**

In several companies, adding management skills (with Prosperitas’ partners in the case of UIVC-I or mentors in the case of Fondo Emprender) did not generate the expected results. What happened in these cases? We determined that adding management skills was not a sufficient condition for success. We needed to rethink the overall profile of the entrepreneurs in.

**CASE: A Software company for SMF’s.** The company’s set of products aims to solve all the management needs for small enterprises, including accounting, reporting, and human resources. In 2007, UIVC-I invested in the company with the objective of scaling it throughout Latin America by entering each new market, consolidating it, and then moving on to the next one. Our principle directive to the entrepreneur was that the company needed to achieve basic traction in each market prior to accelerating growth. This recommendation was not heeded and the company was written off in 2011.

This second factor consists in identifying entrepreneurs with energy, passion and openness to feedback, with the added aptitude of being able to assess the most relevant advice received. Entrepreneurs who proactively listen and then seriously consider and analyze the advice received, are an additional necessary condition for reaching success. The key factor in a company’s success is not only the idea or the business model, but the team’s capacity to execute the plan relentlessly and make the necessary adjustments as needed. As the saying goes, “Ideas are cheap; execution dear.”
**CASE: A fishing-tech company**, which provides technology solutions to improve the fishing industry. A sea captain, who developed the first version of the product to simulate the trawls while fishing, founded the company in 2000. In 2008, Fondo Emprender approved a USD 50,000 non-guaranteed convertible-loan to help the fishing company update the software and start commercial activities. The main reason for approval was the product’s innovativeness and potential, although we knew we need to build a company around it. In 2009, the Uruguayan fishing company partnered with one of the world’s most recognized brands in professional fish finding equipment to develop software that simulated in 3D the behavior of the instruments while fishing. The partner was going to commercialize the product worldwide and share the revenue with the Uruguayan company. The entrepreneur and CEO did not know how to manage the relationship with the partner and the software’s development took longer than expected due to inefficient use of capital and human resources. Prosperitas’ team was deeply involved in trying to help the entrepreneur manage the company to fulfill the requirements of the agreement. After several problems between the entrepreneur and his staff, we suggested to hire a new CEO to end the development and be able to start the commercialization. The entrepreneur did not accept and after several disagreements with the partner, the Uruguayan entrepreneur ended up selling them the intellectual property that had been developed because he could not fulfill the agreement. This helped us to understand that a good product is not the key; it is the team that makes a good company.

**Third Lesson Learned:** A venture capital firm needs to provide financing structures and follow-up financing adapted to the country’s ecosystem.

The third factor reflects the evolution of the venture capital firm itself, as the entrepreneurs and the ecosystem develop. We are convinced that our financing instruments have to adapt to the development status of our region, as described below.

The experience of UIVC-I in 2005 showed that neither the entrepreneurs nor the ecosystem was ready to have valuations placed on a company. The majority of the companies in the UIVC-I pipeline were not familiar with the idea of valuation or investment conditions. Furthermore, there were no examples of venture capital investments in Uruguay. From Prosperitas’ side, this first fund helped us to understand and create an investment process adapted to our country’s maturity level. The concept and instrument of venture capital was innovative for our country and that resulted in a long investment process as we educated the entrepreneurs about the fundamentals of the asset class.
Based on that experience, when designing Fondo Emprender, we decided to change the investment instrument and provide seed capital up to USD 50,000, implemented as a standardized convertible loan. This instrument made the process quicker, reduced operational expenses per company, and was adapted to the 2007 market context.

The loan to equity conversion condition triggers when an angel invests and converts on the same terms and conditions as the new investor negotiated. This structure did not provide the capability to do follow-up financing to further leverage the angel’s investment.

In 2012, the reality is different. Angel investing is becoming more widespread and some acquisitions are starting to occur; therefore, we need to update our instrument for several reasons. First, Fondo Emprender did not monetize the risks it took in the early stages because we converted at the same conditions as the new investor, even though we nursed the company not only with money but also through mentoring. Secondly, when there was an exit without a previous investment round, we did not have an upside. Third, we couldn’t follow-up with investing in the most promising companies (e.g.: PedidosYa.com and Biogenesis). This is a new area of adjustment for the next financial instrument we are designing. The design of this new instrument will include the lessons learned from both funds and improve on them.

**CASE: CROVAT.** Since 2007 the company has been developing and promoting sites, blogs and communities on the Internet. Currently, it owns more than 20 blogs, has a staff of 25 and counts more than 10 MM unique visits to its blogs. It is managed by the founder/entrepreneur. Crovat provides an excellent case to explore the added value presented by the new kind of instrument we are considering. We also sought this entrepreneur’s to share his thoughts regarding strategy and organization. In this particularly case, when we invested in Crovat in 2011, our money was not really needed, but the entrepreneur was looking for mentoring and advice. Last January Crovat was contacted by a growing digital media company working in the U.S. Hispanic and Latin American markets and the acquisition occurred this summer. As Fondo Emprender’s instrument consists in a convertible loan and its conversion is triggered when an angel investor invested in the company, we did not share in the proceeds of this transaction—which would have been significant. Now we know a convertible loan needs to be more flexible and include other possible scenarios as conversion triggers (e.g. acquisition). Fortunately this entrepreneur is willing to show his recognition of our advisory role in this transaction and will pay Fondo Emprender a support fee as a percent of the transaction.
CONCLUSION

During these years, Prosperitas has begun a cultural change in Uruguay’s investment practices. Our experience shows that in early stage investing there is a need for investors and venture capital teams to work closely with entrepreneurs to supply not only business knowledge but also management skills. Among the lessons learned we can identify:

- As Peter Drucker mentioned in several of his books, “developing countries are not underdeveloped, they are undermanaged” and Uruguay is not an exception. We had to provide strong support for basic management skills from the beginning. A skillful management team can make all the difference by providing foundations through management and leadership (not providing “the fish”, but “the rod to fish”). The success cases in our portfolio are products or services that already exist worldwide and have wide competition. It is the relentless and focused capacity to execute and make the necessary adaptations into new business models that were the key factors for their successful growth.

- A good management team does not succeed on its own. The key factor in a company is not only the idea or the business model; it is the team’s capacity to execute. The personal characteristic shared by those teams who succeed is an open attitude toward receiving feedback and the capacity to discern and implement the appropriate portions of the advice received.

- A venture capital firm in this region should evolve to optimize on these opportunities. The firm’s venture manager must find innovative ways to inspire the companies and their management teams to make them highly profitable. Moreover, the firm must also be willing to evolve and adapt its financial instrument to keep pace with the changing venture market in such a way that aligns interests among all parties and reward the firm (and its limited partners) for the risks incurred. Prosperitas has been the only source of smart money in Uruguay and has to evolve this concept according to the entrepreneurs’ needs.

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