

## When Your Venture Guy Says Goodbye

As VC firms struggle to raise money, partners are leaving—and startups are being left in the lurch

By Eileen Gunn

Hubert Engelbrechten, CEO of Fremont (Calif.) semiconductor manufacturer GTronix, has helped raise \$40 million in venture capital for his company, including a \$10 million round led by Jafco Ventures in Palo Alto, Calif. Jafco partner Aaron Cheatham was instrumental in persuading his firm to invest in GTronix and became one of the company's board members. But in the fall of 2008, Cheatham dropped a bombshell: Jafco had become disenchanted with the semiconductor industry, and Cheatham would be leaving the firm to become a consultant.

For entrepreneurs, unexpected exits such as Cheatham's raise unnerving questions about the possibility of a replacement board member, access to the VC firm's network, and the availability of follow-on financing. Such departures are becoming more common as venture firms have trouble raising money or stop investing in certain industries.

"Quite a few of my clients have been told that a firm is no longer investing in their sector, so the partners who focus on it are leaving," says Josh Nathanson, a partner with Cleveland recruiter ON Search Partners. And with many portfolio companies struggling, venture firms are quicker to cut loose a partner who brings in problematic deals.

In 2008 the number of principals at VC firms shrank almost 16%, according to the National Venture Capital Assn. Mark Stevens, a partner at Mountain View (Calif.) law firm Fenwick & West, says the issue of departing directors "is one I've been dealing with more in the last 12 months, and I'm in a space that's pretty healthy—digital media." He continues: "With the disruption in the venture industry, it's only going to happen more."

That disruption has been severe. VC firms raised just \$1.7 billion in the second quarter of 2009. That was the smallest amount since 2003 and nowhere near the high of \$32.5 billion raised in the second quarter of 2000. And a survey by Deloitte Touche Tohmatsu found that 21% of firms are changing the sectors they fund. Entrepreneurs in semiconductors and electronics appear to be most vulnerable, as some 50% of venture capital firms plan to cut back there over the next three years. Other mature, cash-intensive industries, such as telecommunications and pharmaceuticals, are also being pinched.

At GTronix, Engelbrechten needed to make sure Jafco was still committed. "I knew we would need more funding to get us through the downturn," he says. He invited his new director, Nick Sturiale, to the company's offices for a briefing and tour and had him attend his first board meeting while Cheatham was still there. In the first quarter of 2009, with GTronix beginning to bring in revenues, Jafco led a \$7 million round of funding for the company.

But there are more difficult outcomes, too. Santa Clara (Calif.)-based Quellan, another of Cheatham's semiconductor companies, was acquired in August by Intersil ([ISIL](#)), a publicly traded semiconductor manufacturer. "I thought there would be additional [venture] financing, but it's too hard to build an independent company in sectors that are capital-intensive," says Cheatham. "This way the firm got something of a return." Quellan CEO Tony Stelliga says the sale was a tough call: "You're at a point where your technology risks are behind you, you have good prospects, customers, and market momentum," he says. On the other hand, "there's not much going on in the IPO market, so your exit is less certain. But that's what happens with startups."

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