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A New Approach to Venture Capital: How BDC is Building a New Generation of Entrepreneurs

Jerome Nycz, Executive Vice-President, Subordinate Financing and Venture Capital, BDC

In his introduction, Jeffrey Crelinsten noted that much had happened since Nycz had spoken at this conference several years earlier. “We’ve witnessed dramatic changes in the Canadian venture capital scene,” said Crelinsten. “The federal government wants to revitalize our VC ecosystem, and Jerome’s team at BDC has been tasked with that initiative.”

Nycz began by noting that the capital and other resources for turning ideas into businesses have become highly accessible. “Entrepreneurship is becoming truly democratized,” he said, noting that young people who have witnessed the ravages of corporate downsizing are highly motivated to take matters into their own hands.

“They see value in creating their own company and being in greater control of their destiny,” he observed. “We need to encourage this and help people see entrepreneurship as a desirable profession.”

He added that there is a wider interest than just helping individual entrepreneurs. “We now have the data to show that venture capital makes a difference, a big difference,” he said. Such support builds higher levels of sales growth and employment, greater investment in R&D, and a longer life for these firms. The effects are therefore felt across the entire economy.

BDC, a crown corporation that operates as a commercial bank, was established specifically to serve this need. As an example of who the bank helps, Nycz singled out D-Wave, based in Burnaby BC. This firm has been developing a quantum computer called The Infinity Machine, which can take on some daunting computational challenges. BDC was one of the first investors in D-Wave, more than a decade ago, and the company has been thriving ever since; it currently ranks fourth in “patent power”, behind giants such as IBM, HP, and Fujitsu. Part of the goal is ensuring that the company succeeds in ways that keep it and its expertise in Canada. Nor is D-Wave alone in gauging such success, Nycz noted; BDC has worked with other dynamic firms such as fuel cell leader Ballard, the science communication enterprise CREO, and social networking innovators such as Layer 7.

Nycz acknowledged that the venture capital market in Canada has been rocky over the last decade, which has had a very chilling effect on entrepreneurs, especially in the high-tech sector. The downturn was not part of a cycle, but a structural change that called for a re-evaluation of how BDC went about its business. When the bank did the analysis, it found that Canada had the fundamentals, including talented, ambitious individuals conducting world-class research. At the same time, the country has a shortage of serial entrepreneurs, the experienced managers who can tap into global networks. In addition, the investments that were being made tended to be small, so that entrepreneurs had to spend much of their time chasing money, rather than building up their firms.

BDC established three funds to address these shortcomings for companies in the fields of health, IT, and clean technology. Each of these well-capitalized funds was set up to operate privately, so as to demonstrate how the right ingredients lead to success in this asset class. Nycz pointed to Monteris Medical, a Winnipeg firm that is refining a non-invasive technique for eliminating brain tumours with laser beams, as an example of a firm funded from the health fund.

Nycz explained that BDC has also invested less in external VC funds, in order to build up the available scale of their direct funding to companies. At the same time, they developed a strategy for supporting start-ups by bringing in other funds to companies that are breaking ground in a new area, including some highly specialized funds designed to target specific opportunities.

BDC also supports accelerators, such as Vancouver's GrowLab, which are designed to serve as boot camps to cultivate entrepreneurial skills in a real-time, high pressure environment. Hundreds of applicants vie for a handful of positions, where they will get several months of direct mentoring, some $30,000 in direct funding, and opportunities such as travel to Silicon Valley. "It's messy, but full of energy and creativity," he said. "It's not unusual to find 20 people huddled in a room at 2 a.m., eating pizza and working on their apps."

Graduates of this accelerator are also eligible for $150,000 from BDC, which essentially purchases equity in the new firm. "It's a fast-paced, secure environment, where these young entrepreneurs can test new ideas, fail fast, and lose as little money as possible," he said. "They can learn from their mistakes and bounce back to start again. We back them, we mentor them, we encourage them, we connect them with angel investors and potential clients, so they can take their company to the next level."

BDC has partnered with six accelerators like GrowLab across Canada, all of them working in IT. This program has had 1,500 candidates and 100 graduates, 74 of who subsequently received formal financial support from BDC. That support comes to $11 million, which has been doubled through leverage with private capital.

"I've seen them; I've met with them; it's really exciting," said Nycz, who also divulged that the federal government has now asked BDC to invest another $100 million in the similar ways over the next two years. "Through these accelerators, we're seeing a new crop of entrepreneurs, who are not afraid to pivot the company when things don't go according to plan. This is a generation of socially committed entrepreneurs who are open to advice and mentorship. It makes me hopeful about Canada's future."

Nycz referred to the federal government's Venture Capital Action Plan (VCAP), representing some $400 million in new investment, which is being deployed with the help of BDC. Some $50 million will go to new, high-performing funds, while the rest will recapitalize existing private-sector funds. "The goal is to stimulate the market and get more money flowing to commercialize new ideas being developed by Canadian companies," he said, noting that the program creates

incentives for private sector investments by first putting public funds into these enterprises, but also allowing private funds to leave the enterprise first. “The investment time frame is compressed, and the return as a function of time is higher,” he said.

Nycz added that three of these funds have already completed their first closings, including more than $200 million in commitments from corporate and provincial and federal government sources. The impact of this activity can already be seen, with VC investment in Canada climbing by 31% in 2013, the highest level seen since 2007.

“A stagnant venture capital sector is bad for Canada,” he concluded. “It’s bad for innovation and it’s bad for entrepreneurs. I’m excited about this new way of doing things. The industry isn’t perfect yet, but we’re seeing real light at the end of the tunnel. Collectively, we’re building a new generation of entrepreneurs that will carry Canada well into the first half of this century.”

A questioner asked how BDC was co-ordinating business planning and tracking, which are essential to growth, and how the success of these enterprises would be measured. Nycz listed several concrete indicators that would be used to assess firms, such as their ability to attract outside funding, key customers, and to refine their products. In this way, BDC tracks the performance of the enterprise, such as whether its product is moving forward and finding customers, as well as monitoring the investment company, to ensure that they are meeting their own milestones. This information is then reviewed in a board setting, with corrective action being taken when necessary.

As a follow-up, the questioner asked if this reporting would be transparent. Nycz confirmed that these records are public. “We’ve got an established reporting mechanism reporting back to the departments of finance and industry, outlining the firm’s performance and the underlying performance of the portfolio companies,” he said, adding that all of this is detailed in BDC’s annual report.

Ron Freedman asked what the projected rate of return is expected to be. Nycz recalled that in 2010 the VC industry’s rate of return was -6%, with BDC doing slightly better at -5%. Now many of the firms and funds are starting to break even, as well as gaining greater traction in their respective markets. More significantly, they want their funds to become large enough to allow for sustained reinvestment in more rounds of financing. In this respect, he said, graduates from accelerators are at a distinct advantage, insofar as they are more ready to receive support from outside investors.

A final questioner asked for examples of enterprises beyond the ICT sector. Nycz acknowledged that ICT is attractive because relatively modest investments can generate significant returns fairly quickly. Having honed their investment strategies in this area, he said, BDC is expanding its activities to life science and energy, which will require larger pools of investment to help such enterprises succeed.