How do you understand potential investors?

Why understand potential investors?
You will fail to raise capital if you:
1) Don't understand the investors needs.
2) Don't understand how the investors perceives how you meet their needs.
3) Don't understand how the investors perceive that you meet their needs better than others asking for capital.
4) Spend time on investors who will never invest with you rather than spending time on investors who have needs you might be able to meet.

Or, as Karen Kelly of K2 Performance Consulting told me, "Don't try to sell steak to vegetarians."

The overall process is to:
1) Document some hypotheses: What are the characteristics of a potential investor? What are their problems and needs?
2) Document your hypotheses in the business model canvas[1]. This framework ties together investors, their needs, your solution, and what's required to build your solution. Your business model canvas will change as your hypotheses change, are validated, or are invalidated.
3) Test the hypotheses by interviewing potential customers. These are not sales calls.
4) The interview process will either validate or disprove your hypotheses.
5) During the interview process you will likely revise some hypotheses, as well as set down some facts (i.e. validated hypotheses).

Key Hypothesis for the rest of this article:
Let's assume your target investor is the individual investor who makes decisions regarding some or all of their investable assets. There would be different needs if your target was: the Chief Investment Officer of family office; the financial advisor who makes investment decisions for clients; or an institution investing capital.

Why is a business model canvas critical?
Let's pick a simple example to illustrate:
1) You want to raise $10 million and you plan to do $25,000 asks from investor with investable assets of $3 -$5 million. You'll need have 400 investors. OR are you planning to do $1,000,000 asks from investors with investable assets of $100,000,000+? You'll need 10 investors.
2) Your channels, partners, resources, activities, etc. will be radically different for each of the above two examples.

A business model canvas will help you think this through.

What are some aspects of the target investor profile?
1) Age?
2) Gender?
3) Location?
4) Where born and where living now?
5) Current income and occupation?
6) Current net worth?
7) Part of a high net-worth family?
8) Supported by a family office, shared or dedicated to one family?
9) % of assets managed (i.e. investment decisions made) by third parties vs made directly by the investor
10) Associations membership e.g. Tiger 21 or Family Enterprise Xchange?
11) Yearly living expenses – e.g. some potential investors may have fractional jet ownership?
12) Future major expenses – this could range from several hundred thousand dollars to support a child in a foreign university, to a $100 million+ for their next yacht?
13) Do they have a documented investment thesis?
14) Do they have little time to manage their investments, are they devoting significant time to manage their investments?
15) What is their asset allocation mix? Specifically, what % of assets are they allocating to the asset class you are part of? Two examples: 1) You're a fintech company using AI to analyze home mortgage approvals. 2) You're an early stage Venture Capital fund investing in companies with women founders.

What are potential investor needs?

Investor needs can include social, emotional, and financial needs. These needs may include:

1) Being perceived by others as: a sophisticated investor, someone making a positive impact on society or a specific cause.
2) Having the satisfaction of knowing they are doing good.
3) Being actively involved and devoting time to managing their investment. They value the social interaction with other investors. They value being a coach or mentor to the CEO, being on the advisory board, or being on the board of directors.
4) This type of investment is a hobby.
5) They are seeking a xx% probability of achieving YY% cash-on-cash return within ZZ years?
6) They are seeking wealth transfer to their children and grandchildren.
7) IRR is of little interest.

What value will the investor provide to you and your company?

Investors can provide value in many ways. Some of the hypotheses in your business model canvas may include:

1) Providing capital both in the short- and long-term.
2) Enabling your capital raising by drawing upon their network of investors.
3) Providing access to their network of potential channels, partners, suppliers, customers, and employees.
4) Enabling your success based on the reputation of the investor.
5) Being a coach or advisor to you.
6) Serving on your advisory board or board of directors.

What are the dos and donts?

1) Do document and execute a structured process.
2) Do define your target investors and select potential investors who are representative. For example, if you are creating a venture capital fund which will focus on providing investor exits within 3 years, do not interview potential investors who seek a 20+ year exit in order to facilitate inter-generational wealth transfer.
3) Do face-to-face interviews. Video calls are a distant second best. Phone calls are a very distant third best. Don't do emails or surveys because those do not allow interactive dialogue and understanding.
4) Do get out and interview lots of investors. The absolute minimum number of investor interviews is 10. 50 interviews are a better number. You will have to contact many people to get the necessary interviews because most people will decline. They are strangers with busy lives.
5) Do ask potential investors if it's OK to record the interview for later analysis. If not, have a second person take detailed notes. Do not conduct a non-recorded interview by yourself.
6) Do document the criteria for assessing the answers. This will avoid confirmation bias, in which you'll ignore information which invalidates your hypotheses.
7) Do not interview friends, family, or those you have a personal connection with. You need brutal honesty, rather than hearing from people who do not want to hurt your feelings.
8) Do focus on the people who actually have the problem or need for which you are creating the solution.
9) Do create questions which require quantitative answers or specific descriptions. Don't ask for subjective or hypothetical feedback.
10) Do create questions which help you understand how investors think, and why they take the actions they do.
11) Do not talk about your company in your initial meeting.
12) Do not use or send a survey form. These tend to ask closed-ended questions, while you want open-ended responses to open-ended questions.
13) Do finish each interview with two questions: "Who else would you recommend I interview?", and "What should I have asked but did not ask?"
14) Do create a data collection form for each interview. This will contain things such as: the description of the investor profile, your open-ended questions, which hypotheses were confirmed and why, which hypotheses were invalidated and why, which hypotheses you gained no insight into and why, what changes you should make for the next interview (target customer profile, hypotheses, questions to ask).
15) Do review and update your business model canvas as you validate your hypotheses regarding target customers and their needs.

Other ways to understand investors:

1) Read research reports e.g. Tiger 21 reports.
2) Document and analyze sales calls on investors.
3) Interview your existing investors.

What are the challenges in interviewing potential customers?

1) The FEC (Founders, or Existing Companies), passionately believe they have created right solution. They believe there is no reason to interview potential investors. They are focused on building the solution and selling it. Their passion results in them being unable to listen to, and understand, what the investors are saying.
2) The FEC believe any sales and marketing problems can be fixed by changing the sales deck and changing the website.
3) The FEC are passionate they have the right solution. Hearing brutal feedback from potential investors requires founders who are self-confident, self-aware that they don't have all the answers, and have the ability to learn and adapt. I've observed many people who are not able to learn and adapt.
4) The FEC lack the personality and skills to contact a large number of strangers to setup and conduct interviews.
5) Doing interviews appears to be lack of progress. Building a solution is more fun and appears to be progress.

Conclusion

You will fail if your investors do not believe your solution addresses their individual key needs.

Footnotes:

[1] "What is a business model canvas?" The following is a link to my article http://koorandassociates.org/tools/what-is-a-business-model/