Stanford eCorner

Where Does the Capital Come From?

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November 16, 2011

Video URL: http://ecorner.stanford.edu/videos/2842/Where-Does-the-Capital-Come-From

Venture capitalist Dana Mead explains the sources of his firm's funding, which include university endowments, foundations, funds, individual investors and limited partners. Mead also lays out how a venture capital firm is paid through management fees and a percentage of the "carry," or any returns beyond the initial investments.

Transcript

So whose money is this that we're investing? I mentioned in endowments, foundations and there's funds-of-funds, those are people that raise money and by their unique access are able to then invest those people's money into venture capital firms. There is also individual investors. So CEOs that have been very successful that we've worked that with historically, they're investors in our funds and then our - the partners themselves, all of us invest in our funds also. And those are called the limited partners of a fund and that's how it's made up. And every fund is a little bit different on the group that they have. We started with a much larger group of investors and over time, focused down on the smaller group. People ask sometimes, how are venture capitalists paid? Not different than private equity. We get a management fee on the money that we manage and then we also get part of the upside carry, so real simple. There is $100 million, the management fees are normally between 1.5% and 2.5% on that money, paid annually. So let's pick 2.5%.

So the firm would get $2.5 million a year on that $100 million. We would use that to pay people, run our business, do all our diligence et cetera. And then we get carry and carry normally ranges between 20% and 30%, what's that mean? That means once we've returned that $100 million to the LPs, anything we make on that, a venture capital firm will share 20% to 30% of that. So if we double that money, we would get 20% to 30% of that additional $100 million and that's the carry. So that's kind of the upside opportunity for venture capitalists.