

Kleiner Perkins and
Sherpalo Ventures
made a wise decision



**ASSIGN
BUSTER**

Introduction to the case:

Founded in 1999, Zazzle. com Incorporation was established by Bobby and Jeff Beaver as an internet and catalogue retail company with ecommerce being their prominent way of reaching to the consumers (Swisher, K 2009). In 2005 Zazzle raised \$16 million dollars through venture capitalist funding from Kleiner Parkins and Sherpalo ventures. This funding was subject to severe criticisms and discussions in the society as journalists like Jason Ball raised apprehensions about such large investments being unreasonable for an internet based company.

Discussion Questions:

Do you think Kleiner Perkins and Sherpalo Ventures made a wise decision investing \$16 million in Zazzle? Five years from now, do you think that Zazzle will have disappointed or dazzled its investors? Why?

Zazzle from the start had a very profitable structure in terms of managing costs. As mentioned in the case itself (Barringer & Ireland, 2010), Zazzle followed the Dell model of maintaining low inventory costs, producing based on order and receiving payments prior to manufacturing (Hibbard 2005). It also paid its designers, artists and creators after it had received payment from its end consumers. Zazzle being such a low risk business venture made it an attractive proposition for the venture capitalists. Post the investment Zazzle grew leaps and bounds in terms of being recognized for its easy to use technology and also accounted for a profit of over \$20 million in 2006. In 2008 it acquired Goodstorm (Custom T-shirt Talk, 2008), which was another competing firm operating a similar kind of business. Such expansion and

profitability indicate the growth prospects of the business and the wise decision of the venture capitalists.

From being a small ecommerce based company in 1999 Zazzle grew as a major internet retailer in 2005. During this growth phase Zazzle managed to have tie ups with brands such as Warner Brothers, Coca Cola and Walt Disney (Swisher, 2009). It was also among the few who had the approval from U. S. Postal Service to make custom stamps. Zazzle introduced itself to Germany in 2009 (Piller, 2009) and has now expanded into Asia by launching itself into Japan in May, 2010 (Marketwire, 2010).

In addition to that it has impeccable records as on August, 2010 of monthly unique visitors exceeding 12 million, 140+ percent year-over-year traffic growth and number of members exceeding 5 million (Zazzle news). This step towards creating a global foot print surely assures high expected demands for the company and its ability to adapt and capitalise upon the opportunities that lie ahead if it. Based on the growing trends, the company is sure to create a market for itself and dazzle its investors.

Look at Table 10. 1 in the chapter, at the time that Zazzle raised venture capital funding, to what extent did it resemble the ideal candidate for venture-capital funding as stipulated by the materials in the table?

Zazzle maintained a low inventory cost model; produced goods based on order and received payments prior to manufacturing. It also paid its designers after it had received payment from its end consumers (Hibbard 2005). Zazzle being such a low risk business venture with strong cash flow and low leverage made it a lucrative proposition for the debt financing form <https://assignbuster.com/kleiner-perkins-and-sherpalo-ventures-made-a-wise-decision/>

of funding. In addition to the low cost model, Zazzle had an effective management along with healthy profitability scenario from beginning itself, which further indicates debt financing to be viable option of funding based on the table below.

Matching a New Venture's Characteristics with the Appropriate Form of Financing or Funding

Source: Table 10. 2, Barringer, R and Ireland, D 2010, Entrepreneurship: successfully launching new ventures

Evaluate Jason Ball's (the blogger) criticism of Kleiner Perkin's investment in Zazzle. Do you think Ball makes some good points or do you think his arguments are off base? Explain your answer.

Business Week, in its 15th April 2005 issue, highlighted the venture capital funding amounts of few companies such as Filmloop (\$6.5 million), BA Systems (\$880,000), Teneo Systems (\$4 million), Affinity Engines (\$400,000) and Zazzle. Com (\$16 million) (Hibbard, J 2005). All these were firms had their operations based on or through internet and ecommerce. The highest investment being made in a company which simply sells customised products over internet, could have been the reason for Jason Ball's bafflement.

The statement "From London perspective, it looks like they're partying like it's 1999 all over again in California" refers to the dot.com bubble which took place during 1998-2000. During this period there was a splurge of new companies in the internet industry with individuals speculating their prices to

<https://assignbuster.com/kleiner-perkins-and-sherpalo-ventures-made-a-wise-decision/>

go up and venture capitalists investing with little caution to create competitors in order to let the market decide the fate of each company's success and their investments. Jason Balls' comment is based on this scenario.

Based on the analysis of the kind of companies and investments that were made during that period, Jason's apprehension may seem valid initially as the profitability of such internet-based companies seem insignificant to be considered for a venture capital investment of amounts such as \$16 million. However, a detailed analysis and study of Zazzle's operations definitely make the investment viable for Perkin.

What do you think is Zazzle's exit strategy? How will Kleiner Perkin's and Sherpalo Ventures recoup their investment?

Timing and reason of exit is the most crucial part of any exit strategy as it determines the buyout / acquisition price. Reason of exit should ideally be when the company has grown rapidly and is unable to run it and finance its growth without the support of outside resources. In case of Zazzle, the company has been expanding at a constant growth rate and has undertaken necessary alliances and measures to ensure the progressive nature of business. It has also expanded into the global market and tasted success. For Zazzle to plan its exit strategy, it should evaluate its future plans and ensure the following factors exist during its exit period:

Impeccable records in order to become easily marketable (Kerr & Stahl 2007).

High profile to ensure good reputation amongst the market players such as vendors, consumers, competitors etc. as that adds value to the sale price.

Have important people assets in the company to create a greater market value

Maintain growth rate as companies with high growth rates are more preferable than companies with high profit growth. Similar is the case with Amazon.com whose stocks rose by 600% in 2001 even though it was reporting losses (Kerr & Stahl 2007). The investors know that high growth companies will eventually profit.

Innovative and technical competitive advantage coupled with unique selling proposition will ensure customer loyalty, which will help in increasing market value of the business (Kerr & Stahl 2007).

Any venture capitalist would have a target to recoup the investment made in the business. Kleiner Perkin's and Sherpalo Ventures too need to recoup the investment. Zazzle in the past 10 years has become a company which is valued at more than \$225 million and has been in the Top 50 of the World's Most Valuable Internet Start-ups (Silicon Alley Insider, 2009). Its growing potential is positive and so is its earning capacity. In order to recoup their investment Kleiner Perkin's and Sherpalo Ventures can adopt the following strategies based on their estimated time for recoupment:

Share in profits: The advantage of having a health inter personal relationship with the venture capitalist, forms of recoupment can be flexible based on

mutual understanding. Beavers and the venture capitalists could have an agreement over share in profits from the business on a periodic basis

Advertisement: Another form of recoupment for the venture capitalists could be the incomes from advertisements that could be placed on the zazzle website. This is similar to the Google model where every click on the advertisement generates a certain amount of income for the website owner. Since Zazzle is growing in its popularity, income from advertisement can be significantly used up for payment to its venture capitalists.

Conclusion

Since its inception Zazzle has managed to add value for its consumer needs and expand its horizons to ensure a global presence. Venture capital funding has proved to be fruitful for Zazzle to undertake growth and infrastructure reforms. Zazzle's performance projects a progressive future for the company before it actually decides to exit the market.