Wary venture capitalists rein in investments

Net ventures top industry for VC cash

Jim Hopkins

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SAN FRANCISCO -- Skittish venture capitalists are still holding tight to their wallets.

Their first-quarter investments in start-ups and other young companies were down more than 50% from a year ago -- dramatically accelerating a trend that began in late 2000.

But despite the collapse of at least 435 dot-coms since January 2000, Internet ventures topped the list of new VC investments.

"The death of the Internet has been greatly exaggerated," says Jesse Reyes, vice president of research firm Venture Economics.

In reports out Wednesday:

* Investment falls. VCs, who invest on behalf of individuals and institutions, pumped $11.7 billion into 1,072 companies during the first quarter. That was down 56% from $26.7 billion in 1,751 companies in the same period last year, say Venture Economics and the National Venture Capital Association trade group.

Virtually all industries saw a drop, according to a separate report from PricewaterhouseCoopers and VentureOne. Only the industrial sector, which includes agriculture, showed an increase -- to $113.5 million from $59.6 million last year.

It was the second-consecutive quarter of falling investments and the smallest investment total since late 1998. The drop reflects investor angst after the tech-stock meltdown. Last year, VCs pumped $103 billion into young companies, up 67% from 1999.

Don't expect much change during the next 2 quarters, says John Taylor, vice president for research at Venture Economics. VCs are concentrating more on companies they've already invested in. And they continue hunting for bargains. Start-up valuations are down 30% to 40% from their peaks of the past 2 years, Taylor says.

Gary Little, a general partner with **Morgenthaler** Ventures in Silicon Valley's Menlo Park, says his firm invested in 14 companies during the first quarter and 13 during the fourth quarter of 2000. Many of the firms are in the optical and wireless industries. "Innovation doesn't stop just because the stock market dips," Little says.

Investors are attracted to companies with experienced management and a good track record, Little says.

* E-commerce attracts. In a boost for the Internet consumer market, online spending is expected to reach $65 billion by the end of 2001 -- up 45% from 2000, says a Shop.org study conducted by Boston Consulting Group. On Wall Street, the sector has seen a

rebound. USA TODAY's e-retail stock index is up 58% this year, but is still 67% off its November 1999 high.

VCs bet $3.1 billion on e-commerce and Internet content companies during the first quarter -- 27% of the total invested.

That's encouraging news for entrepreneurs such as Melinda Konopko, who co-founded Plum Party, an online party-supply retailer based in New York City.

Launched in 1999, the company was financed by Konopko and her partner, Risa Meyer. They are on the lookout for private investors, including VCs.

Konopko is convinced there's life in the business-to-consumer market, especially for companies that grow slowly and don't overspend. Citing the example of failed eToys, Konopko says, "These were people who were really providing a great service, but expanded in a way that didn't make sense."