Yao Huang of Divison One Capital

Speaker1: [00:00:04] This is the Investor Connect podcast program. I'm Hall Martin. I'm the host of the show in which we interview angel investors, venture capital, family offices, private equity, and many other investors for early stage and growth companies. I hope you enjoy this episode. Investor Connect is a 501 C three nonprofit dedicated to the education of investors and startups for fundraising. Please consider donating $100 to the program to help others in their investor and entrepreneur journey. You can find the Donate button on the Investor Connect org website.

Speaker2: [00:00:44] Well, hello, this is Hall Martin with Investor Connect. Today we're here with Yao Huang of Division One Capital. Division one Capital. Is there a purchase order receivables purchasing fund that makes capital available to minority and women owned businesses so they can grow and realize their potential? Yeah. Thank you for joining us.

Speaker3: [00:01:01] Yes. Pleasure.

Speaker2: [00:01:02] Great. So where are you calling from today?

Speaker3: [00:01:05] I am in Chicago. Great.

Speaker2: [00:01:08] Good. So let's start off with your background. What were you doing before joining Division one Capital.

Speaker3: [00:01:14] Two decades of tech and venture building companies to invest in them and special place in my heart for the underdog.

Speaker2: [00:01:22] That's great. So what excites you right now?

Speaker3: [00:01:25] Making capital available to as many people as possible, especially those that may have been biased from venture for banks creating new sources besides equity based financing. So there's a whole back story as to how this all started.

Speaker2: [00:01:44] Great. Well, before we get into that, let's tell me more about your advice for people investing in startups. You see a lot of people investing out there. What do you tell them to do before they write that check?

Speaker3: [00:01:55] Not have a lot of years and startups. This fund isn't necessarily for startups per say. We can get into that later, but investing in startups in general. I looked at a founder who looked at, well, these days it's fairly simple to get product at least minimum viable product up and running so you can get some traction. One customer, two customers, especially if it's enterprise or get a couple hundred, if it's consumer something moving to prove that this is going somewhere defensible. Ip If you have that just the roadmap experience, I think it's not as hard as it used to be because a lot of the technical infrastructures there and that's getting more and more scalable these days. I find a lot of it to do with the business.

Speaker2: [00:02:46] Right. On the other side of that table. What's your advice for founders? What do you tell them to do before they go out to raise funding?

Speaker3: [00:02:53] Get some customers, generate some revenues. Some of them talk about size. Picture on your deck. And honestly, if you're fundraising, you should have talked to those investors in the beginning. Just socializing without asking for money. Keeping them abreast, showing them what's happening so that when it's time to pull the trigger, they already know. And it's much easier than starting from scratch at the moment that you are ready. So it's kind of like making friends before you're ready to raise.

Speaker2: [00:03:23] Great. Well, let's go back to that history behind Division one Capital, behind your current fund and how you came to it. What was the backstory there?

Speaker3: [00:03:33] So again, I've been in venture for a long time and it's not capital that's meant for everyone. It's meant for about 2% of companies. So there's 98% that this kind of money doesn't touch. But this kind of money, this venture money is very sexy. It's in movies. It's in books you read about in articles everywhere. It's all over the Internet. Wow. You're really famous. You're a founder that got funded, which doesn't mean anything, means that you owe a lot of money later. And traditional businesses, which used to have some, I guess, story to support, has fallen by the wayside to tech companies. And this whole story of Facebook and

Zuckerberg and all those types. And there are groups like women that have been biased or underserved and I mean of venture capitals, entire all assets combined, all funds combined, only 2% go to women. And similar stats for minorities. That number hasn't changed. In fact, it's declined as a reason. And so there's a lot of people working for that, starting more funds that make capital available, more LPs extending to first time partners that are women or minority. But that's still that number isn't changing. And I would like to see some movement that opens up availability to more people. That's not going to happen in my lifetime. If they double, this will go to 4%, double that, go to 8%. So that doesn't really make much of a difference. And I like to do something. So we spend a lot of time looking at where where we can place capital. And the other end of it would be debt. If you look at that, well, there's banks out there. Banks don't really lend to a lot of minority and women things that don't look the same. There's a lot of biases, a lot of research behind that.

Speaker3: [00:05:24] And so they look at businesses. What makes it less risky? Well, if you have big accounts like corporate accounts, like government accounts, you get a contract from one of them. It really defines your business. In fact, they're usually large seven figure contracts, eight figure, nine figure contracts. It's game changing and they're pretty solid. There's a nice mode around. It's difficult to get. And they do a lot of diligence, meaning the companies are established, they're able to service those contracts, deliver whether it be product or service. And I'm like, Wow, that's really good. Why don't we look at companies that have some of these contracts? And the least riskiest among those two buckets are government contracts. So we spend a lot of time looking at companies with government contracts. Turns out the government takes a long time to pay to be a month, three months, upwards of nine, 12 months before they'll pay the bill. So now you're fronting big cash flow there. Those kind of starts as a purchase order. Once you win the contract purchase order, banks lend against that. So now you have another problem for these founders or these company founders, and they're not always an AI tech company. Yes, there are software, there's I.T., but there's also janitorial, there's construction, there's lawn care service, there's everything, and not a lot of time or mindspace. Space is spent thinking about these kind of companies. And there's so many of them across the United States. So we spend a lot of time thinking about who we want to help, where we want to go, partnering up with different cities. One of the reasons I'm here in Chicago and trying to make it as fair as possible to get capital out there.

Speaker2: [00:07:08] So she has a limited partner. Make a return on this type of investment.

Speaker3: [00:07:14] Like most do this profits and in this case, there's profit sharing. So I don't want to go into term sheets on this video, but they're interested. We have a whole set right there. But it's quarterly returns versus waiting adventure. You wait till seven years after exits happen. This is something that actually can happen much faster.

Speaker2: [00:07:39] Right. Okay. So they're taking a portion of the profit from the project and like, venture where we sell the business and then we all divide up the returns that come from selling to businesses.

Speaker3: [00:07:49] In finance. We buy the receivables on a discount, so we wait for the the payer to pay. When that happens, we have fees associated with that and that over time, over a fund of $100 million, that's up.

Speaker2: [00:08:06] And so so what are the challenges in putting this fund together? On the investment side, what challenges have you encountered and how did you overcome them?

Speaker3: [00:08:15] Investment side, not so much, mainly because this kind of fund is not driven by the stock market. So right now we're going into recession. Everyone's all scared. This is not touched by that. This is stable, regular returns. We've limited the risk by working with the government. And there are risks associated with this as there is with anything but not from receiving of capital. We've been pretty fortunate there. But if you're talking about risks and making these investments, the biggest one would be that the government doesn't pay. For what? Because you didn't complete the task. And then we have risk mitigators for that as well. But there's there's ways to balance all the components of this. This is actually, in fact, one of the oldest forms of capital. Been around for hundreds of years. It's not very sexy, but it's still an area that hasn't grown very much because it's mostly private money. Most funds are 30 million lower, not very large. They tend to be very niche. They're not well understood by founders. They don't really go out. And it's not easy to find these. It's still based on paper. If there's a lot of just old traditional ness to it that I think we'd like to overcome for everyone.

Speaker2: [00:09:36] Great for the women started that you're supporting. How do they benefit from this?

Speaker3: [00:09:43] We are giving preference to women founders and minority based founders. So. Where you could not borrow from a bank where capital is not available to you in other ways. This is go get a piece of business and we'll help you out.

Speaker2: [00:10:02] That's great. So you've got this running in many cities. How is it going so far?

Speaker3: [00:10:08] Great. I mean, cities love it because it's aligned to their minority and women initiatives. City of Chicago, for example, is trying to hit a 26% minority. Vanderpool trying to hit a 2% women vendor pool. In order to do that. These businesses need to be able to carry the cash flow. If cities are taking a long time to pay, those businesses are fronting the salaries, benefits, expenses. And not everyone can do that. And so they need organizations like ours to help float until the bill comes. Right.

Speaker2: [00:10:46] And after government contracts, what would be the next one in line that you would go after?

Speaker3: [00:10:51] Working with city and states right now. The next one would be federal. We're also finding a way to help nonprofits that get grants. Same problem. In some cases, these nonprofits don't get the funding until after they complete the requirements. So let's say the nonprofits helping to feed the poor, you have to feed them first before they'll get the grant, which is very. Not intuitive, but. They can't get bank loans for that. We're working on a website open for that as well.

Speaker2: [00:11:25] Great. Well, you're doing some fantastic work there in the last few minutes that we have. What else should we cover that we haven't?

Speaker3: [00:11:31] I'm we're super excited about this. If there's interest in participating as an investor or if you have cities that want to get involved, we're happy to. We have capital that can extend up to $75 million per city. As as long as there's interest and for. Owners, founders, companies, small and medium sized or more open here.

Speaker2: [00:11:59] That's great. So how best for listeners to get back in touch with you?

Speaker3: [00:12:03] Pretty accessible. There's a website division one capital dot com you can email us from there and I think you have some email addresses to share as well.

Speaker2: [00:12:11] That's great. We'll put that in the show notes. Want to thank you for joining us today and hope to have you back for a follow up soon.

Speaker3: [00:12:16] Sure. Thanks.

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