Chapter 4: Financing & Managing Venture

TE IT – Entrepreneurship and E-business

Leena Ladge
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Chapter 4: Financing & Managing Venture

1. Entrepreneurship; Robert Hisrich, Michael Peters; Tata McGraw Hill Publication
2. Entrepreneurship: New venture creation by David Holt, Prentice Hall of India Pvt. Ltd.

Lecture No 20:

Financial Ventures, Financial Stages, Sources of Finance, Criteria for evaluating Capital-process.

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Learning Objectives:

- Study the fundamentals of Venture Capital.
- Discuss the benefits of Venture Capital Financing.
- Discuss the stages of Financing.
- Study the market for venture capital and to review venture capitalists' evaluation criteria for new ventures.
- To examine the existing informal risk-capital market ("angel capital").

Introduction

https://startup.law/wp-content/uploads/2018/02/venture-capital-funding.jpg

Venture Capital

Venture

- A project which is new and possibly dangerous, because you cannot be sure that it will succeed

Capital

- an amount of money that you use to start a business or to put in a bank, etc. so that you earn more money (interest) on it

Venture Capital

- A capital invested in a project in which there is a substantial element of risk, typically a new or expanding business.

Importance of Venture capital financing

- **Promotes Entrepreneurs**
- **Promotes Products**
- **Encourages customers**
- **Brings out latent talent**
- **Promotes exports**
- **As Catalyst**
- **Creates more employment opportunities**
- **Brings financial viability**

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Importance of Venture capital financing

- **Helps technological growth**
- **Helps sick companies**
- **Helps development of Backward areas**
- **Helps growth of economy**
- **Manage unavoidable risks**

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Venture Capitalists

Are valuable and powerful source of equity funding for new ventures that provide:

- Capital for start-ups and expansion
- Market research and strategy
- Management-consulting, audits and evaluation
- Contacts—customers, suppliers, and businesspeople
- Assistance in negotiating technical agreements
- Help in establishing management and accounting controls
- Help in employee recruitment and employee agreements
- Help in risk management and with insurance programs
- Counseling and guidance in complying with government regulations

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Startup Funding

- **Dfgdfh**
- **Fhf**
- **H**

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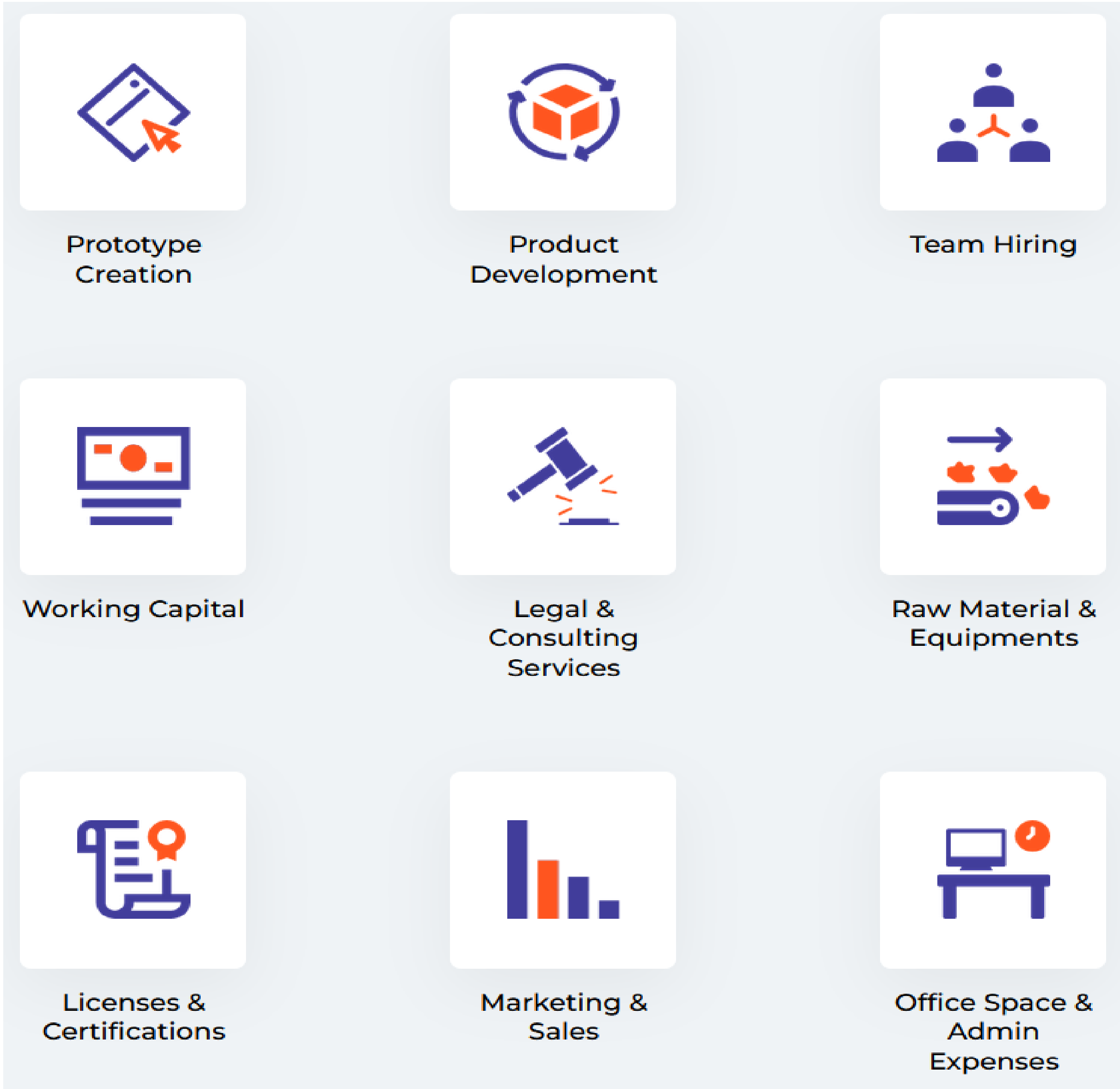
Why funding is required by Startups?



https://www.startupindia.gov.in/content/sih/en/funding.html

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Types of Startup Funding

Working Capital	Equity Financing	Debt Financing	Grants
Brief	Equity financing involves selling a portion of a company's equity in return for capital.	Debt financing involves the borrowing of money and paying it back with interest.	A grant is an award, usually financial, given by an entity to a company to facilitate a goal or incentivize performance.
Nature	There is no component of repayment of the invested funds.	Invested Funds to be repaid within a stipulated time frame with interest	There is no component of repayment of the invested funds
Risk	Financer: There is no guarantee against his investment. Startup: Startups need to give up a portion of their ownership to shareholders.	Financer: The lender has no control over the business's operations. Startup: You may need to provide a business asset as collateral.	Financer: There is a risk of the startup not meeting the goal or objective for which the grant has been provided. Startup: There is a risk of the startup not receiving a portion of the grant due to several reasons.

https://www.startupindia.gov.in/content/sih/en/funding.html

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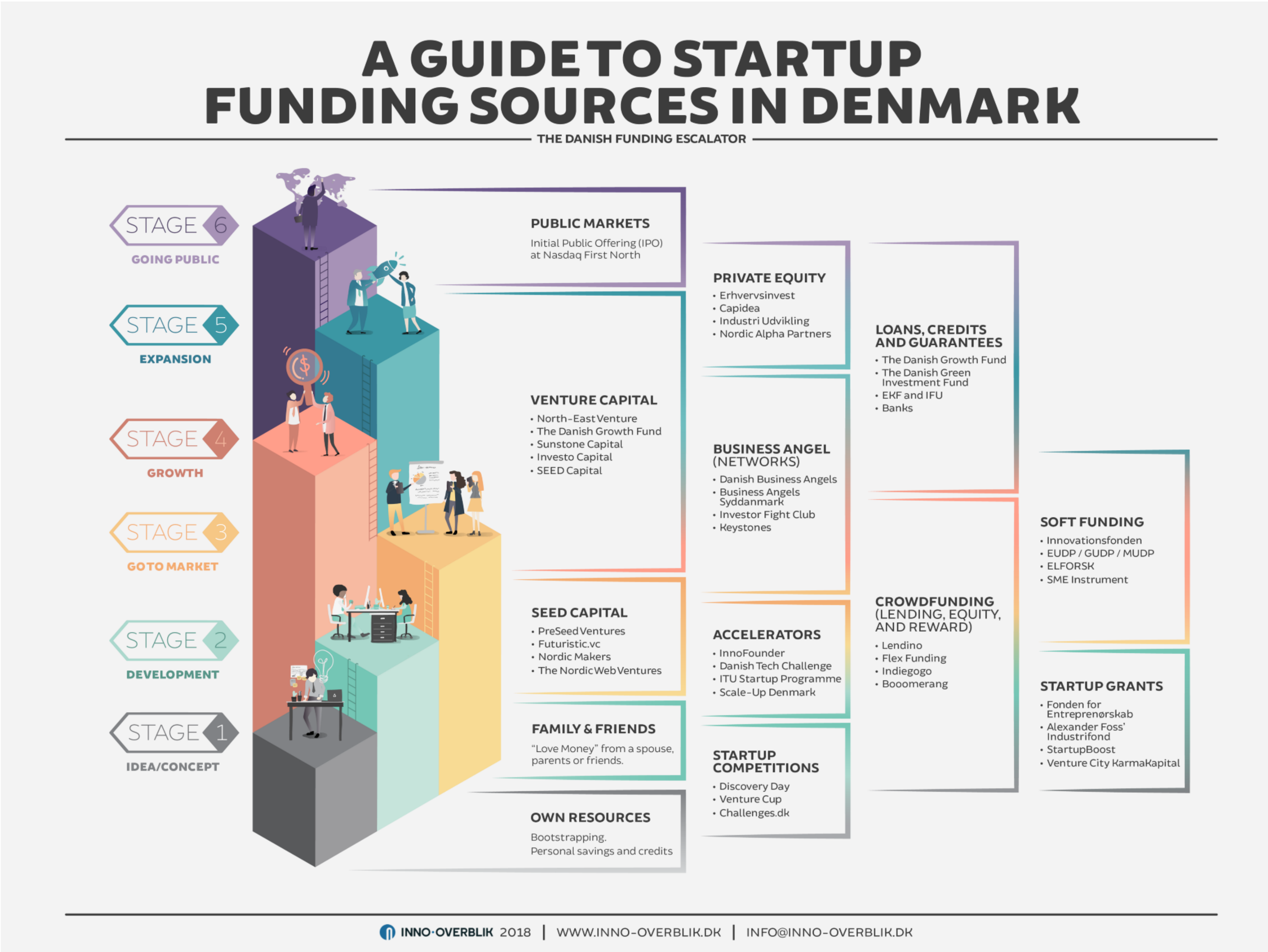

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Debt Versus Equity

Debt Financing

- Secured financing of a new venture that involves a payback of the funds plus a fee (interest for the use of the money).

Equity Financing

- Involves the sale (exchange) of some of the ownership interest in the venture in return for an unsecured investment in the firm.

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Debt Financing

Commercial Banks

- Make 1-5 year intermediate-term loans secured by collateral (receivables, inventories, or other assets).
- Questions in securing a loan:
  - ✓ What do you plan to do with the money?
  - ✓ How much do you need?
  - ✓ When do you need it?
  - ✓ How long will you need it?
  - ✓ How will you repay the loan?

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Debt Financing

Advantages

- No relinquishment of ownership is required.
- More borrowing allows for potentially greater return on equity.
- During periods of low interest rates, the opportunity cost is justified since the cost of borrowing is low.

Disadvantages

- Regular (monthly) interest payments are required.
- Continual cash-flow problems can be intensified because of payback responsibility.
- Heavy use of debt can inhibit growth and development.

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Common Debt Sources

	Business Type Financed		Financing Term		
Debt Source	Start-Up Firm	Existing Firm	Short Term	Intermediate Term	Long Term
Trade credit	Yes	Yes	Yes	No	No
Commercial banks	Sometimes, but only if strong capital or collateral exists	Yes	Frequently	Sometimes	Seldom
Finance companies	Seldom	Yes	Most frequent	Yes	Seldom
Factors	Seldom	Yes	Most frequent	Seldom	No
Leasing companies	Seldom	Yes	No	Most frequent	Occasionally
Mutual savings banks and savings-and-loan associations	Seldom	Real estate ventures only	No	No	Real estate ventures only
Insurance companies	Rarely	Yes	No	No	Yes

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Other Debt Sources

Trade Credit

- Credit given by suppliers who sell goods on account.

Accounts Receivable Financing

- Short-term financing that involves either the pledge of receivables as collateral for a loan or the sale of receivables at a discounted value (factoring).

Finance Companies

- Asset-based lenders that lend money against assets such as receivables, inventory, and equipment.

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Other Debt Sources

Equity Instruments

Give investors a share of the ownership.

- ***Loan with warrants*** provide the investor with the right to buy stock at a fixed price at some future date.
- ***Convertible debentures*** are unsecured loans that can be converted into stock.
- ***Preferred stock*** is equity that gives investors a preferred place among the creditors in the event the venture is dissolved.
- ***Common stock*** is the most basic form of ownership and is often are sold through public or private offerings.

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Equity Financing

Equity Financing

- Money invested in the venture with no legal obligation for entrepreneurs to repay the principal amount or pay interest on it.
- Funding sources: public offering and private placement

Public Offering

- "Going public" refers to a corporation's raising capital through the sale of securities on the stock markets.
- Initial Public Offerings (IPOs): new issues of common stock.

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Equity Financing

Public Offering

Advantages

- Size of capital amount
- Liquidity
- Value
- Image

Disadvantages

- Costs
- Disclosure
- Requirements
- Shareholder pressure

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Lecture No 20:

Financial Stages, Sources of Finance, Criteria for evaluating Capital-process

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Learning Objectives:

- Discuss the stages of Financing.
- Study the market for venture capital and to review venture capitalists' evaluation criteria for new ventures.
- To examine the existing informal risk-capital market ("angel capital").

Entrepreneurial Thought

- **Flipkart Story**

Private Placements

Regulation D

- Securities and Exchange Commission (SEC) regulations for reports and statements required when selling stock to private parties—friends, employees, customers, relatives, and professionals.
- Defines four separate exemptions, which are based on the amount of money being raised:
  - ✓ Rule 504a: placements of less than $500,000
  - ✓ Rule 504: placements up to $1,000,000
  - ✓ Rule 505: placements of up to $5 million
  - ✓ Rule 506: placements in excess of $5 million

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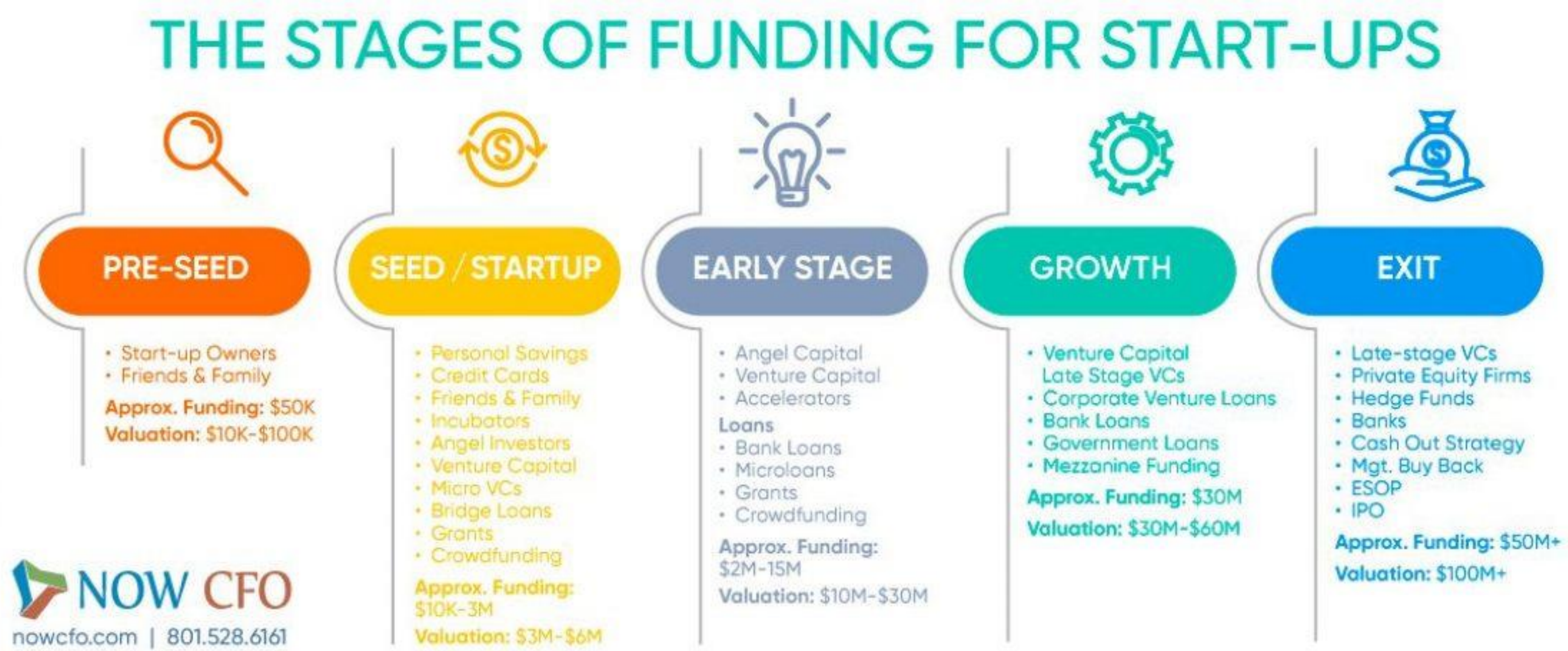
Stages of Funding



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Private Placements

Accredited Purchaser

- Regulation D uses the term "accredited purchaser." Included in this category are the following:
  - Institutional investors such as banks, insurance companies, venture capital firms.
  - Any person who buys at least $150,000 of the offered security and whose net worth, including that of his or her spouse, is at least 5 times the purchase price.
  - Any person who, together with his or her spouse, has a net worth in excess of $1 million at the time of purchase.

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Investors

"Sophisticated" Investors

- Wealthy individuals who invest regularly in new and early- and late-stage ventures and are knowledgeable about the technical and commercial opportunities and risks of the business in which they invest.

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Lecture No 24:

Criteria for evaluating Capital-process, Informal Risk Capital, Business Angel Investments, Management of venture

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Learning Objectives:

- Study the market for venture capital and to review venture capitalists' evaluation criteria for new ventures.
- To examine the existing informal risk-capital market ("angel capital").
- Discuss the meaning of Management and Venture Management.
- Study the levels of Management.
- Learn the functions of Management.

Venture Capital

- About venture capital

Dispelling Venture Capital Myths

Myth1: Venture capital firms want to own control of your company and tell you how to run the business.

Myth 2: Venture capitalists are satisfied with a reasonable return on investment.

Myth 3: Venture capitalists are quick to invest.

Myth 4: Venture capitalists are interested in backing new ideas or high-technology inventions—management is a secondary consideration.

Myth 5: Venture capitalists need only basic summary information before they make an investment.

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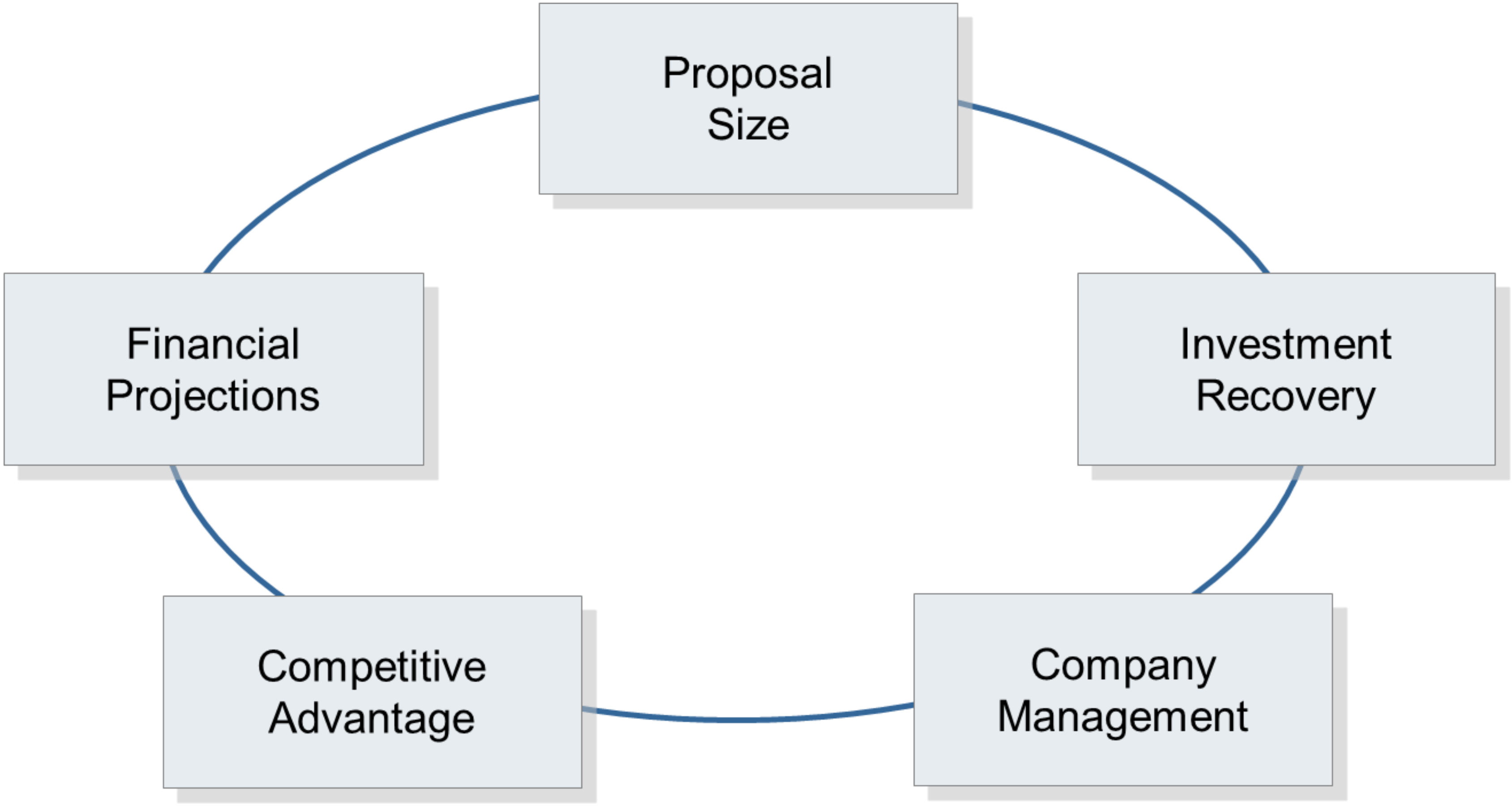
Venture Capitalists and Business Plans



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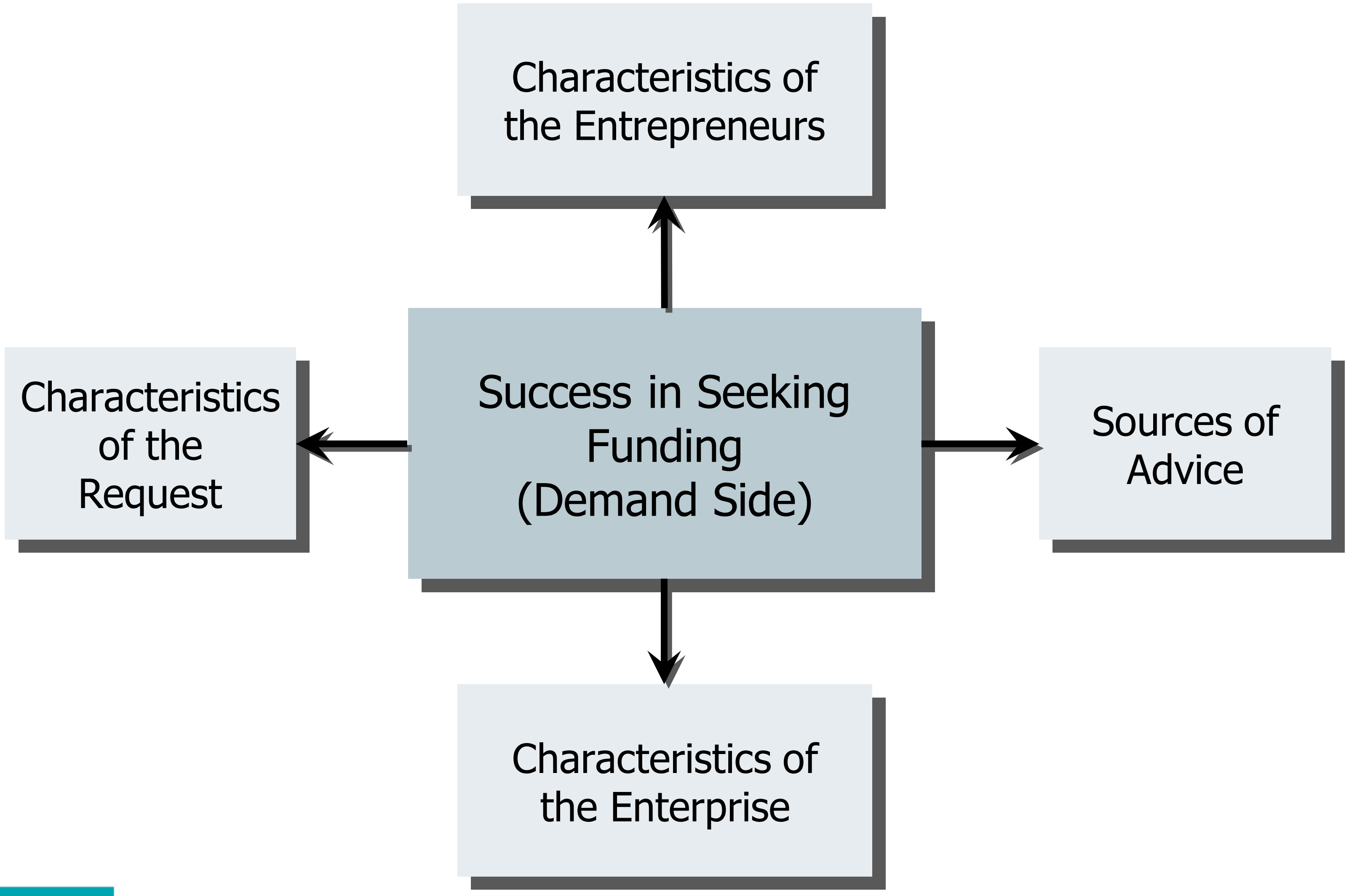
Factors in Successful Funding of Ventures



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Returns on Investment Typically Sought by Venture Capitalists

Stage Of Business	Expected Annual Return on Investment	Expected Increase on Initial Investment
Start-up business (idea stage)	60% +	10–15 × investment
First-stage financing (new business)	40%–60%	6–12 × investment
Second-stage financing (development stage)	30%–50%	4–8 × investment
Third-stage financing (expansion stage)	25%–40%	3–6 × investment
Turnaround situation	50% +	8–15 × investment

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Factors in Venture Capitalists' Evaluation Process

Attribute	Level	Definition
Timing of entry	Pioneer	Enters a new industry first
	Late follower	Enters an industry late in the industry's stage of development
Key success factor stability	High	Requirements necessary for success will not change radically during industry development
	Low	Requirements necessary for success will change radically during industry development
Educational capability	High	Considerable resources and skills available to overcome market ignorance through education
	Low	Few resources or skills available to overcome market ignorance through education
Lead time	Long	An extended period of monopoly for the first entrant prior to competitors entering the industry
	Short	A minimal period of monopoly for the first entrant prior to competitors entering this industry

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Factors in Venture Capitalists' Evaluation Process

Attribute	Level	Definition
Competitive rivalry	High	Intense competition among industry members during industry development
	Low	Little competition among industry members during industry development
Entry wedge mimicry	High	Considerable imitation of the mechanisms used by other firms to enter this, or any other, industry—for example, a franchisee
	Low	Minimal imitation of the mechanisms used by other firms to enter this, or any other, industry—for example, introducing a new product
Scope	Broad	A firm that spreads its resources across a wide spectrum of the market—for example, many segments of the market
	Narrow	A firm that concentrates on intensively exploiting a small segment of the market—for example, targeting a niche
Industry-related competence	High	Venturer has considerable experience and knowledge with the industry being entered or a related industry
	Low	Venturer has minimal experience and knowledge with the industry being entered or related industry

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Criteria for Evaluating New-Venture Proposals

- **Major Categories of Venture Capitalist Screening Criteria:**
  - ✓ Entrepreneur's personality
  - ✓ Entrepreneur's experience
  - ✓ Product or service characteristics
  - ✓ Market characteristics
  - ✓ Financial considerations
  - ✓ Nature of the venture team

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Ten Criteria Most Frequently Rated Essential in New-Venture

Criterion	Percentage
Capable of sustained intense effort	64
Thoroughly familiar with market	62
At least ten times return in five to ten years	50
Demonstrated leadership in past	50
Evaluates and reacts to risk well	48
Investment can be made liquid	44
Significant market growth	43
Track record relevant to venture	37
Articulates venture well	31
Proprietary protection	29

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Venture Capitalists’ Screening Criteria

Venture Capital Firm Requirements

- Must fit within lending guidelines of venture firm for stage and size of investment
- Proposed business must be within geographic area of interest
- Prefer proposals recommended by someone known to venture capitalist
- Proposed industry must be kind of industry invested in by venture firm

Nature of the Proposed Business

- Projected growth should be relatively large within five years of investment

Economic Environment of Proposed Industry

- Industry must be capable of long-term growth and profitability
- Economic environment should be favorable to a new entrant

Proposed Business Strategy

- Selection of distribution channel(s) must be feasible
- Product must demonstrate defendable competitive position

Financial Information on the Proposed Business

- Financial projections should be realistic

Proposal Characteristics

- Must have full information
- Should be a reasonable length, be easy to scan, have an executive summary, and be professionally presented
- Proposal must contain a balanced presentation
- Use graphics and large print to emphasize key points

Entrepreneur/Team Characteristics

- Must have relevant experience
- Should have a balanced management team in place
- Management must be willing to work with venture partners
- Entrepreneur who has successfully started previous business given special consideration

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Venture Capitalist Evaluation Process

- **Stage 1: Initial Screening**
  - ✓ This is a quick review of the basic venture to see if it meets the venture capitalist's particular interests.
- **Stage 2: Evaluation of the Business Plan**
  - ✓ This is where a detailed reading of the plan is done in order to evaluate the factors mentioned earlier.
- **Stage 3: Oral Presentation**
  - ✓ The entrepreneur verbally presents the plan to the venture capitalist.
- **Stage 4: Final Evaluation**
  - ✓ After analyzing the plan and visiting with suppliers, customers, consultants, and others, the venture capitalist makes a final decision.

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Informal Risk Capital

Business Angel Financing

- Wealthy individuals in the United States are looking for investment opportunities.
  - ✓ They are referred to as “business angels” or informal risk capitalists.

Types of Angel Investors

- Corporate angels
- Entrepreneurial angels
- Enthusiast angles
- Micromanagement angels
- Professional angels

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Main Differences Between Business Angels and Venture Capitalists

Main Differences	Business Angels	Venture Capitalists
Personal	Entrepreneurs	Investors
Firms funded	Small, early-stage	Large, mature
Due diligence done	Minimal	Extensive
Location of investment	Of concern	Not important
Contract used	Simple	Comprehensive
Monitoring after investment	Active, hands-on	Strategic
Exiting the firm	Of lesser concern	Highly important
Rate of return	Of lesser concern	Highly important

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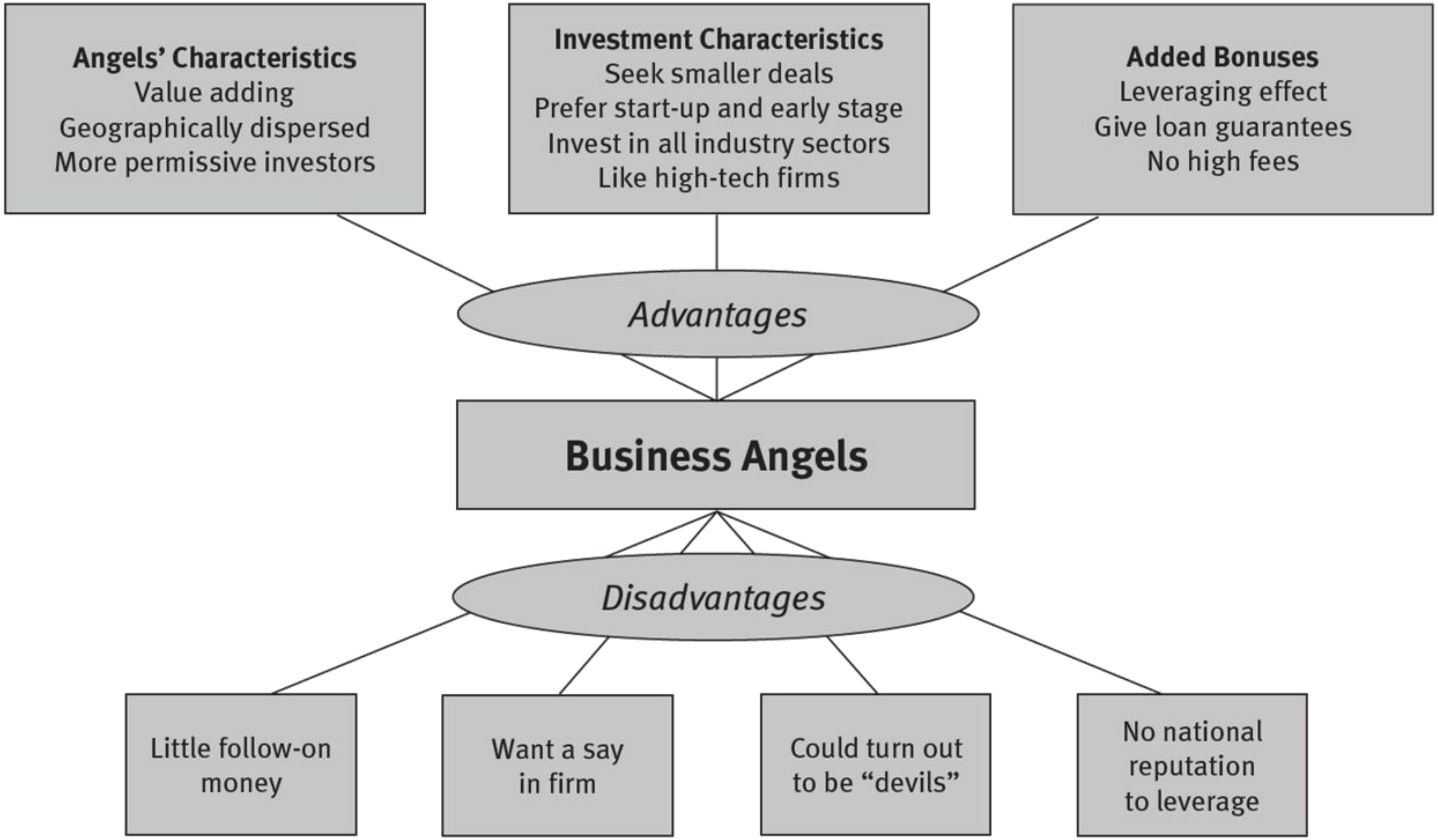
The Pros and Cons of Business Angel Investments



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Management

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Management

- Organization and coordination of the activities of an enterprise in accordance with certain policies and in achievement of clearly defined objectives.
- Management is often included as a factor of production along with machines, materials, and money.

Levels of Management

Top-level managers

- The following skills are needed at the top managerial level.
  - ✓ Broadening their understanding of how factors such as competition, world economies, politics, and social trends influence the effectiveness of the organization.

Levels of Management

Middle-level managers

- Typically consist of general managers, branch managers, department managers.
- They are mainly responsible to the top management for the functioning of their department.
- They devote more time to organizational and directional functions.

Levels of Management

Middle-level managers

- Some of their functions are as follows:
  - ✓ Designing and implementing effective group and intergroup work and information systems.
  - ✓ Defining and monitoring group-level performance indicators.
  - ✓ Diagnosing and resolving problems within and among work groups.
  - ✓ Designing and implementing reward systems that support cooperative behaviour.

Levels of Management

First-level managers

- Typically consist of supervisors, section officers, foreman, etc.
- They focus more on the controlling and direction of management functions
  - ✓ Assign tasks and jobs to employees, guide and supervise employees on day-to-day activities, look after the quantity and quality of the production of the company, make recommendations, suggestions, and communicate employee problems to the higher level above, etc.
  - ✓ Basic supervision, Motivation, Career planning, Performance feedback.

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Definitions of Management by great Management Scholars

- A 'Management Is a distinct process consisting of planning, organising, actuating and controlling; utilising in each both science and art, and followed in order to accomplish pre-determined objectives.” - George R Terry
- "Management is the art of getting things done through others and with formally organised groups.” - Harold Koontz

Definitions of Management by great Management Scholars

- "Management may be defined as the process by means of which the purpose and objectives of a particular human group are determined, clarified and effectuated" - Peter Ferdinand Drucker
- "Management is the art of knowing what you want to do and then seeing that they do it in the best and the cheapest may."- Frederick Winslow Taylor

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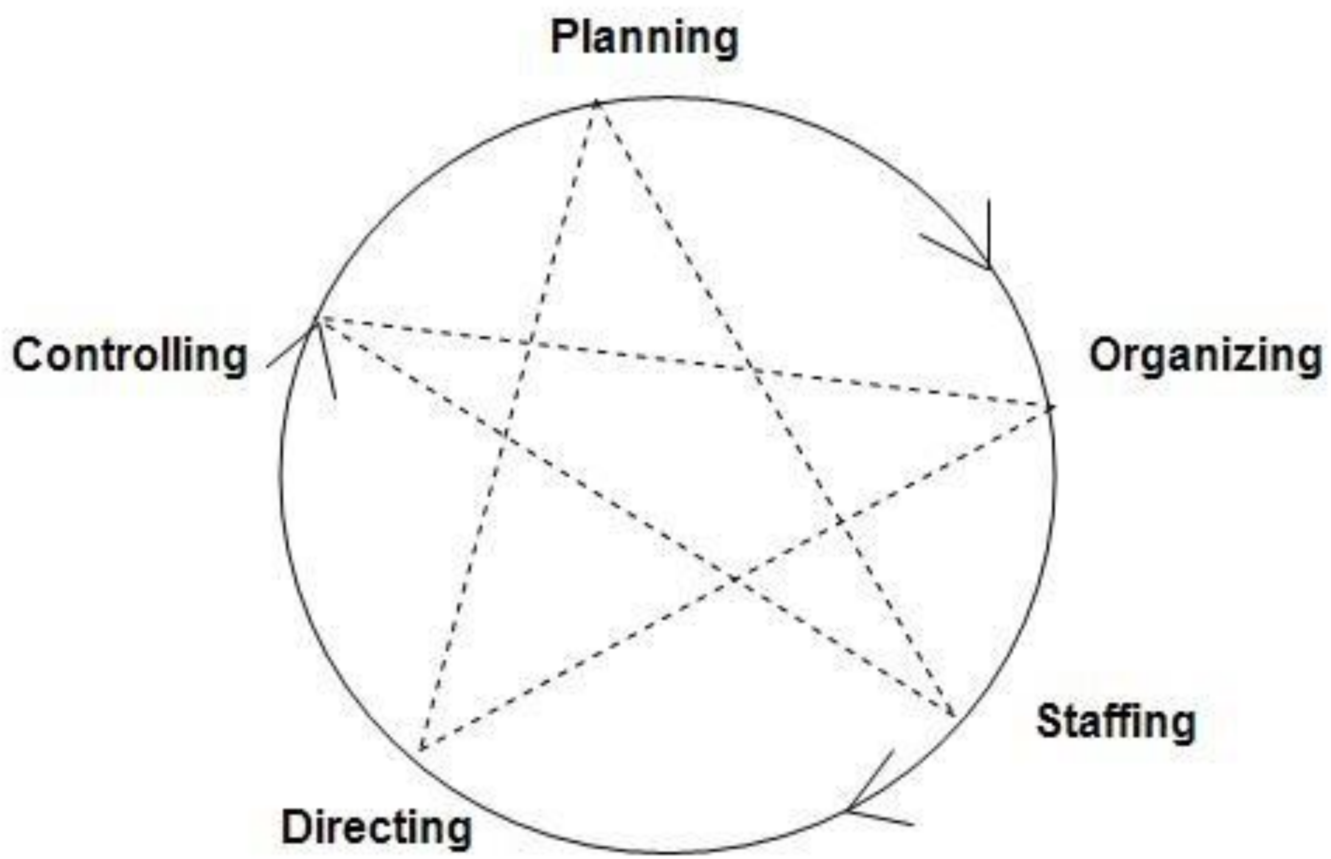
Venture Management

- Venture management is a business management practice that focuses on being both innovative and challenging in the realm of introducing what could be a completely new product or entering a promising newly emerging market.

Functions of Management



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Functions of Management

Planning

- It is the basic function of management.
- It deals with chalking out a future course of action & deciding in advance the most appropriate course of actions for achievement of pre-determined goals.
- A plan is a future course of actions. It is an exercise in problem solving & decision making.
- Planning is necessary to ensure proper utilization of human & non-human resources.
- It is all pervasive, it is an intellectual activity and it also helps in avoiding confusion, uncertainties, risks, wastages etc.

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Functions of Management

Organizing

- It is the process of bringing together physical, financial and human resources and developing productive relationship amongst them for achievement of organizational goals.
- Organizing as a process involves:
  - ✓ Identification of activities.
  - ✓ Classification of grouping of activities.
  - ✓ Assignment of duties.
  - ✓ Delegation of authority and creation of responsibility.
  - ✓ Coordinating authority and responsibility relationships.

Functions of Management

Staffing

- It is the function of manning the organization structure and keeping it manned. The main purpose o staffing is to put right man on right job. Staffing involves:
  - ✓ Manpower Planning (estimating man power in terms of searching, choose the person and giving the right place).
  - ✓ Recruitment, selection & placement.
  - ✓ Training & development.
  - ✓ Remuneration.
  - ✓ Performance appraisal.
  - ✓ Promotions & transfer.

Functions of Management

Directing

- It actuates the organizational methods to work efficiently for achievement of organizational purposes.
- Direction is that inert-personnel aspect of management which deals directly with influencing, guiding, supervising, motivating sub-ordinate for the achievement of organizational goals.

Functions of Management

Directing

- Direction has following elements::
  - ✓ Supervision
  - ✓ Motivation
  - ✓ Leadership
  - ✓ Communication
  - ✓ Supervision
  - ✓ Motivation
  - ✓ Leadership
  - ✓ Communications

Functions of Management

Controlling

- It implies measurement of accomplishment against the standards and correction of deviation if any to ensure achievement of organizational goals.
- The purpose of controlling is to ensure that everything occurs in conformities with the standards.
- Controlling is the measurement & correction of performance activities of subordinates in order to make sure that the enterprise objectives and plans desired to obtain them as being accomplished.

Functions of Management

Controlling

- It has following steps:
  - ✓ Establishment of standard performance.
  - ✓ Measurement of actual performance.
  - ✓ Comparison of actual performance with the standards and finding out deviation if any.
  - ✓ Corrective action.

Lecture No 24:

Scientific Management , Introduction to Human Resource management

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Learning Objectives:

- Discuss the objectives of Management.
- Study the concepts of Scientific Management.
- Learn the concepts and functions of Human Resource Management.

Objectives of Management

- **Getting Maximum Results with Minimum Efforts**
- **Increasing the Efficiency of factors of Production**
- **Maximum Prosperity for Employer & Employees**
- **Human betterment & Social Justice**

Scientific Management

Development of Current Management theories

- Ideas of formal management can be traced to the 1700s.
- The most significant developments in management theory emerged in the 20th century.
- Many theorists of this period, who tried to understand how best to conduct business and developed Managerial practices.
- Frederick Winslow Taylor, started the Scientific Management movement. He and his associates were the first to study the work process scientifically. In 1909, Taylor published "The Principles of Scientific Management."

Scientific Management

- **Ford and Taylor's Scientific Management**

Four Principles of Scientific Management

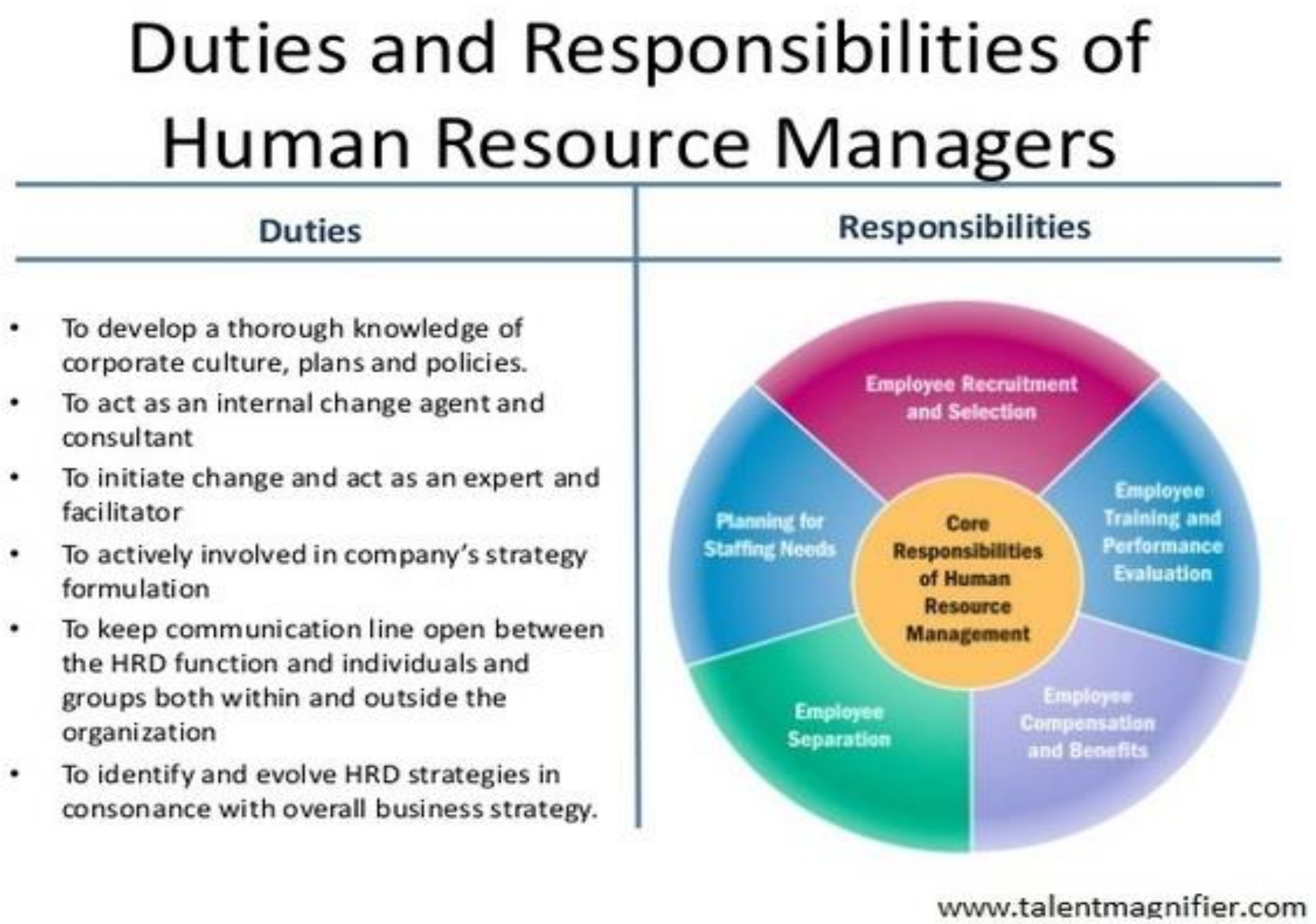
- Taylor's four principles are as follows:

1. Replace working by "rule of thumb," or simple habit and common sense, and instead use the scientific method to study work and determine the most efficient way to perform specific tasks.
2. Rather than simply assign workers to just any job, match workers to their jobs based on capability and motivation, and train them to work at maximum efficiency.
3. Monitor worker performance, and provide instructions and supervision to ensure that they're using the most efficient ways of working.
4. Allocate the work between managers and workers so that the managers spend their time planning and training, allowing the workers to perform their tasks efficiently.

Human Resource Management (HRM)

- Human resource (HR) departments in many organizations use many tools/methods outside their organizations (recruiting) and inside their organizations (employee development).

Human Resource Management (HRM)



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Human Resource Management (HRM)

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Human Resource Management (HRM)-Functions

1. Recruiting

- Both recruiters and job seekers are moving to online social networks as recruiting platforms.
- Enterprise recruiters are scanning online social networks, blogs, and other social resources to identify and find information about potential employees.
- Job seekers have a good chance that they will be seen by recruiters.
- So, it is important that both active and passive job seekers maintain online profiles that accurately reflect their background and skills.
- It also provides some tips to assist you in a job search.

Human Resource Management (HRM)- Functions

2. Onboarding

- Onboarding is how new employees acquire the necessary knowledge, skills, and behaviors to become effective members of the organization.
- Through the use of social media, new hires can learn what to expect in their first few days on the job and find answers to common questions.
- Because they are available inside the company's firewall, these social communities can provide detailed information about corporate policies, as well as giving employees the opportunity to complete necessary forms online.
- These communities also provide introductory training, such as workplace safety information and how to use enterprise applications.

Human Resource Management (HRM)-Functions

3. Employee Development

- The best strategy to enable, encourage, and promote employee development is to build relationships with employees.
- Many HR professionals use enterprise social tools such as Chatter , Yammer, and Tibbr to tap into the wisdom of every employee.
- These tools help connect employees to work efficiently across organizations and to collaborate on sales opportunities, campaigns, and projects.
- They help companies simplify workflows and capture new ideas, enable HR managers to find subject matter experts within the organization.

Human Resource Management (HRM)

3. Employee Development

- As HR managers can better motivate employees, thereby helping them become more engaged and excited about their work.
- Employees can then be better rewarded for their expertise.
- Another area of employee development is training. A large percentage of the time and expense of employee education and learning management can be minimized by utilizing e-learning and interactive social learning tools.

Thank You!

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