ENTREPRENUEUSHIP

Chp 12

Presentation: Informal Risk Capital, Venture Capital, And Going Public

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OUTLINE

- Financing the business and early stages finance.
- Three Risk-Capital markets.
- Characteristics of informal investor.
- Characteristics of Venture-Capital.
- Valuing your company & Ratio analysis and its types.
- Deal Structure & going public.
- On going public and after going public

Financing the business and early stages finance.

- **Financing the business** :Financing a business refers to obtaining funds to start, operate, or expand a company through sources like loans, investments, or personal savings.
- **Early-stage financing**: Funding provided to startups or new businesses to help them grow and develop initial products or services.

Seed capital: Initial funding used to develop a business idea or product before it generates revenue.

Startup financing: Funding provided to new businesses to help them launch and grow during their early stages.

- **Development financing**: Capital used to expand an established business, fund large projects, or scale operations.

Second stage: Funding for a business in its early growth phase, not yet profitable or generating strong cash flow.

Third stage: Capital for expanding a company with rapid sales growth that is breaking even or profitable but still private.

Fourth stage: Financing to prepare the company for going public through an IPO (Initial Public Offering).

Acquisition and Leveraged Buyout Financing

Acquisition: Taking ownership and control of another company.

Leveraged Buyout (LBO): Acquiring control of a company by borrowing funds to buy out current owners.

Going Private: Owners or managers buy all outstanding stock, turning the company into a private entity again.

Risk-Capital markets.

The **risk capital market** provides funding to high-risk, high-reward ventures, typically involving investments in startups or growing companies in exchange for equity.

Markets providing debt and equity to nonsecure financing situations

Three Risk-Capital markets.

Informal Risk-Capital Market: Comprises individual investors, often called angel investors, who personally fund startups in exchange for equity. This market is less formal and less regulated, focusing on early-stage companies needing seed capital.

Venture-Capital Market: Involves professional investment firms that pool funds to invest in high-growth potential startups. Venture capitalists provide significant capital and often take an active role in management to scale the business.

- Public-Equity Market: Allows companies to raise funds by selling shares to the general public through stock exchanges. This market provides access to large amounts of capital but requires adherence to strict regulatory and disclosure requirements

Private Equity Market

- The private equity market, also known as the enterprise capital market, provides funding for privately held ventures. It consists of individuals (angel investors), venture capital firms, and private equity funds. Angel investors, often accredited with high income or net worth, make the most deals, typically investing between $10,000 to $500,000. These investors are found through referrals from professionals like accountants or lawyers and often pool resources to reduce individual risk.

Informal Risk-Capital

- The informal risk-capital market consists of wealthy investors, known as business angels, who invest $10,000 to $500,000 in startups, particularly in early stages. These angel investors, often invisible and hard to find, provide significant funding in the U.S., contributing between $7 billion and $20 billion annually to around 30,000 firms. They tend to invest locally, with deals averaging $340,000.

Characteristics of informal investor.

Category	Details
Demographic Patterns and Relationships	
Education	Well educated, many with graduate degrees
Financing Location	Will finance firms anywhere, especially in the U.S.; most within one day's travel
Investor Role	Majority expect to play an active role in ventures
Membership	Many belong to angel clubs
Investment Record	
Investment Range	\$100,000 – \$500,000
Average Investment	\$340,000
Deals Per Year	1 to 2 deals annually
Venture Preference	
Stage of Firms	Start-ups or ventures less than 5 years old
Industry Interests	Manufacturing (industrial/commercial products, consumer products), energy, services, software

Characteristics of informal investor

Risk/Reward Expectations	
Capital Gain for Start-ups	10x median gain in 5 years
Capital Gain for Firms <1 year	6x median gain in 5 years
Capital Gain for Firms 1-5 years	5x median gain in 5 years
Capital Gain for Firms >5 years	3x median gain in 5 years
Reasons for Rejecting Proposals	
Risk/Return Ratio	Not adequate
Management Team	Inadequate
Business Interest	Not interested in proposed business area
Price Agreement	Unable to agree on price
Commitment	Principals not sufficiently committed
Familiarity	Unfamiliar with the area of business

Crowdfunding

- **Crowdfunding** is a method of raising funds for a project, business, or cause by collecting small amounts of money from a large number of people, typically through online platforms. Instead of seeking a large investment from a single source, crowdfunding allows individuals to contribute small amounts, which collectively meet the funding goal.

Example:

- One famous example is Kickstarter, where creators pitch their ideas, such as a new gadget or artistic project, and backers fund them in exchange for rewards like early access or special editions of the product.
- For instance, the Pebble Smartwatch was initially funded through crowdfunding on Kickstarter, raising over $10 million from thousands of backers.

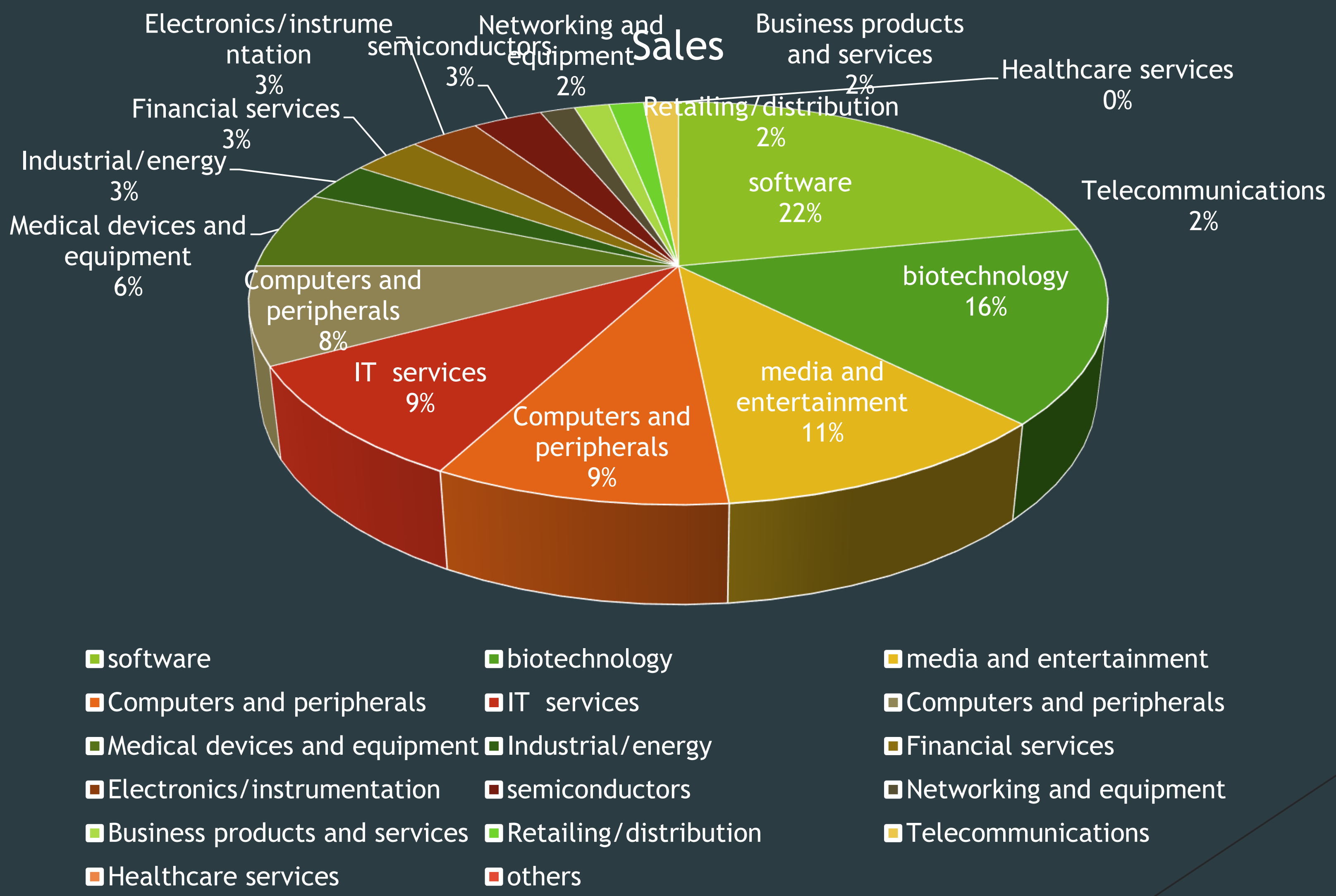
Venture capital

- **Venture capital** is a form of private equity financing where investors provide capital to early-stage or growing companies with high growth potential in exchange for equity (ownership) in the company.

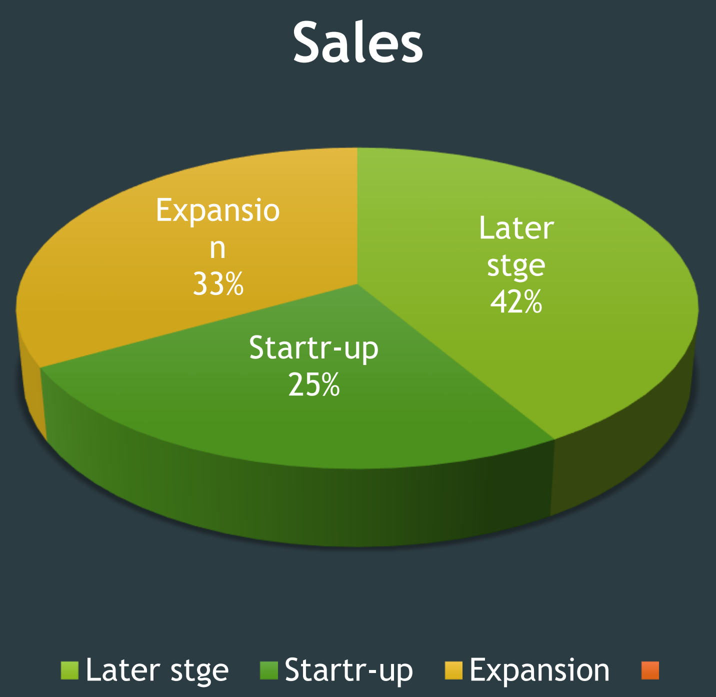
Example:

- Sequoia Capital invested in **Google** during its early stages, helping the company grow into a global tech giant.

Percentage of Venture Dollars Invested by Industry Sector (Q4 2014)



Percentage of Venture Dollars Invested by Stage (Q4 2014)



VC Investments Process

- Venture Capital Process refers to the steps venture capitalists follow to invest in early-stage or growing companies. Here's a breakdown of the typical stages:

1. Deal Sourcing:

- Venture capitalists identify potential startups or companies that fit their investment criteria through networks, referrals, or research.

2. Screening:

- The VC firm reviews the business plan, checks market potential, and assesses whether the company aligns with their investment focus.

3. Due Diligence:

- A thorough investigation of the company's financials, product, market opportunity, team, and legal structure is conducted to assess risk and growth potential.

4. Term Sheet:

- If due diligence is successful, the VC firm offers a term sheet outlining the investment amount, ownership stake, and conditions of the deal.

VC Investments process

5. Investment:

- Once the terms are agreed upon, the VC firm invests capital in exchange for equity. They also often provide mentorship and strategic guidance.
- 6. Post-Investment Involvement:
- VC firms actively work with the company to scale operations, help with strategic decisions, and prepare for an exit (e.g., an IPO or acquisition).

7. Exit:

- The VC firm exits the investment, typically after 5-10 years, either through an IPO (Initial Public Offering) or the company being acquired, aiming for a significant return on investment.

VC Investments by Region (Example Data):

- VC Investments by Region (Example Data):

Silicon Valley: $6.29 billion (43%)

- New England: $2.01 billion (14%)
- LA/Orange County: $1.22 billion (8%)
- NY Metro: $1.15 billion (8%)
- Southeast: $1.01 billion (7%)

These numbers highlight how Silicon Valley dominates venture capital investments in the U.S., with a significant percentage of VC funding going to startups in this region.