Master in Luxury Management
Entrepreneurship
Sources of Funding

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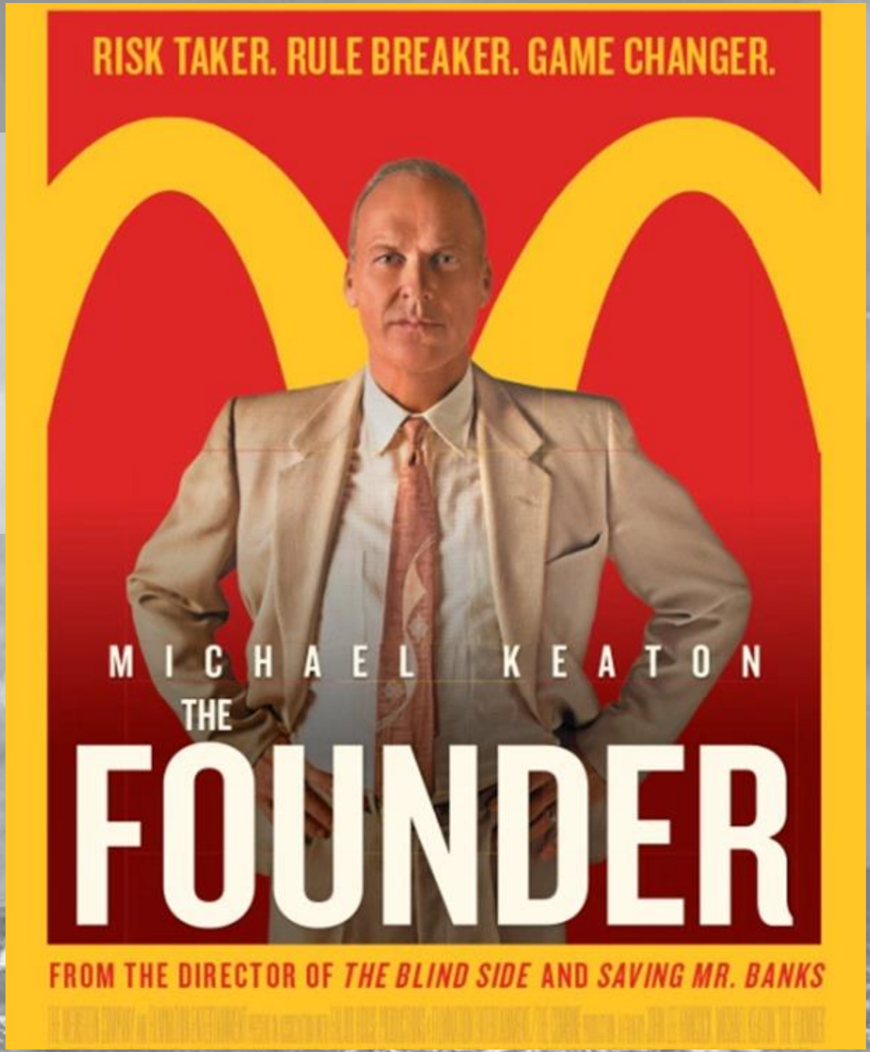
What have we learned until now?

- Timing of Business Idea
- Market of Business Idea
- Sustainability of Business Idea
- Financing of Business idea

Revenues, Finance, Control

- Find the right market
- Create a sustainable value architecture
- Find the appropriate business model



Why Most New Ventures Need Funding

Cash Flow Challenges

Inventory must be purchased, employees must be trained and paid, and advertising must be paid for before cash is generated from sales.

Capital Investments

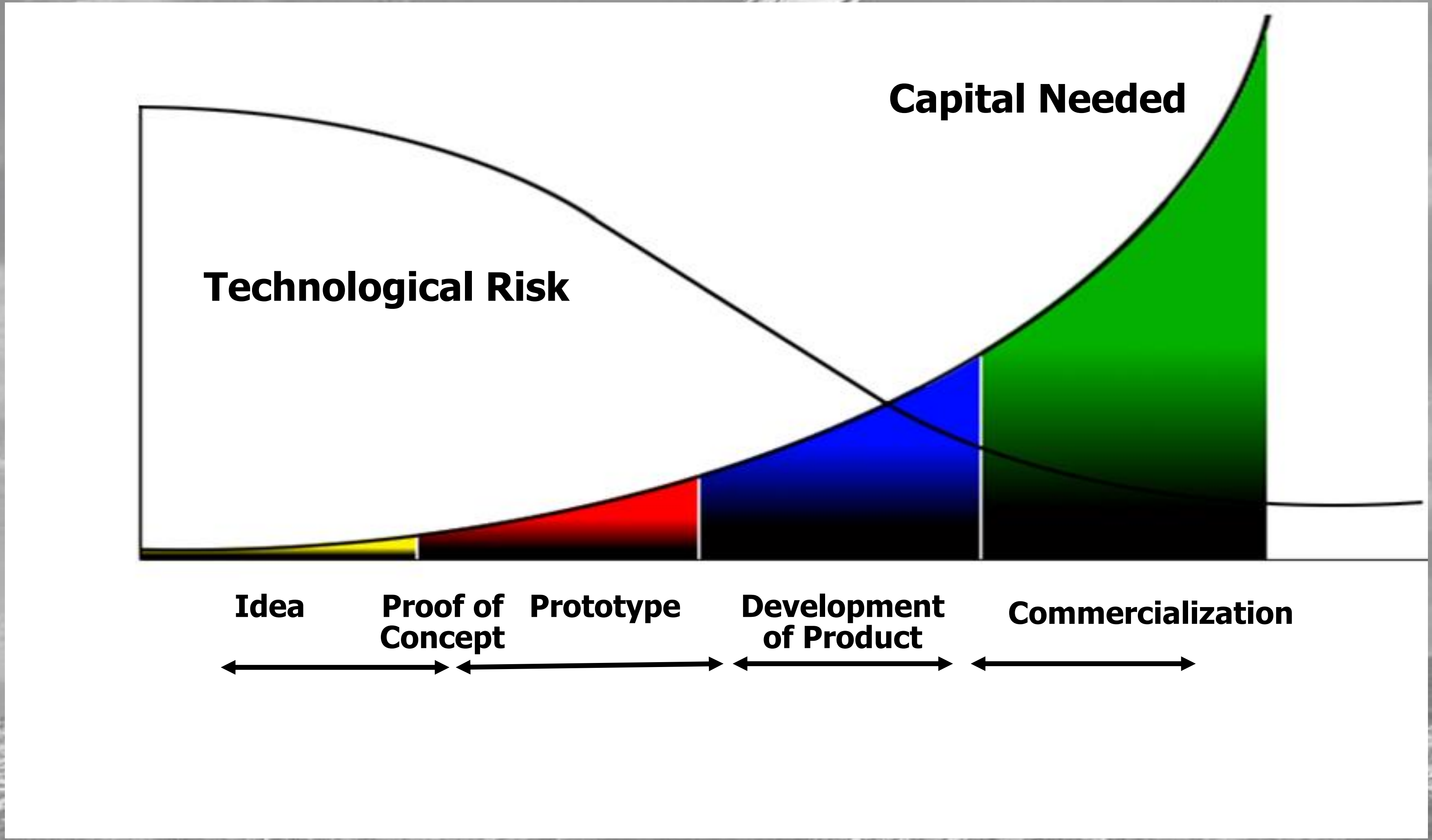
The cost of buying real estate, building facilities, and purchasing equipment typically exceeds a firm's ability to provide funds for these needs on its own.

Lengthy Product Development Cycles

Some products are under development for years before they generate earnings. The up-front costs often exceed a firm's ability to fund these activities on its own.

Why Most New Ventures Need Funding

Technological Risk and Capital Needed For High Growth Companies



Funding Sources (Pecking Order)

1. Personal Funds
2. Family and Friends
3. Bootstrapping
4. Government
5. Business Angels
6. Venture Capital
7. Partnering
8. Debt Financing
9. Crowdfunding
10. IPO

Personal Funds

- Most start up begin this way.
- Least expensive in terms of cost and control
- By showing that founders are prepared to take a personal financial risk, their personal commitment serves as a **signaling function** in face of imperfect information about the quality of the founders' venture projects
- Sources include:
    - Savings
    - Life insurance
    - Mortgage on a house or car

Family and Friends (1 of 2)

- Survey: 10% of business owners turn to family and friends for capital
- The resource inflow can be organized in many and diverse ways and often there will be no formal agreements regarding dividends and other terms and conditions (Shulman 1997).
- A formal agreement, however, will include:
  - Amount of money involved
  - Terms of the money
  - Rights and responsibilities of the investor
  - Steps to be taken when a business fails

Family and Friends (2 of 2)

Advantage

- Easy to obtain money
- More patient than other investors

Disadvantage

- Direct input into operations of a venture
- Tensions can develop between the participants

Bootstrapping (1 of 4)

Most entrepreneurs get their businesses started by **bootstrapping**.

bootstrapping operating a business as frugally as possible and cutting all unnecessary expenses.

Why bootstrapping?

Disadvantages of using outside capital

- Takes between three and six months to raise (if you are lucky)
- Decreases a firm's drive for sales and profits
- Increases the impulse to spend
- Decreases the company's flexibility
- May cause disruption and problems in the venture

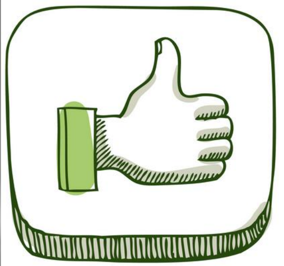
Bootstrapping (3 of 4)

Four basic rules for effective bootstrapping:

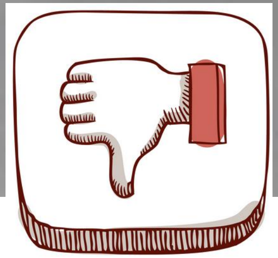
1. Overhead matters
2. Employee costs are the single biggest recurring cost
3. Reduce operating costs
4. Marketing matters, but know your customers and where they go for information

Examples of Bootstrapping Methods

Buying used instead of new equipment	Coordinating purchases with other businesses	Leasing equipment instead of buying
Obtaining payments in advance from customers	Minimizing personal expenses	Ask suppliers to allow for longer payments terms
Buying items cheaply but prudently via options such as eBay	Sharing office space or employees with other businesses	Hiring interns, part-time employees and freelancers



Bootstrapping



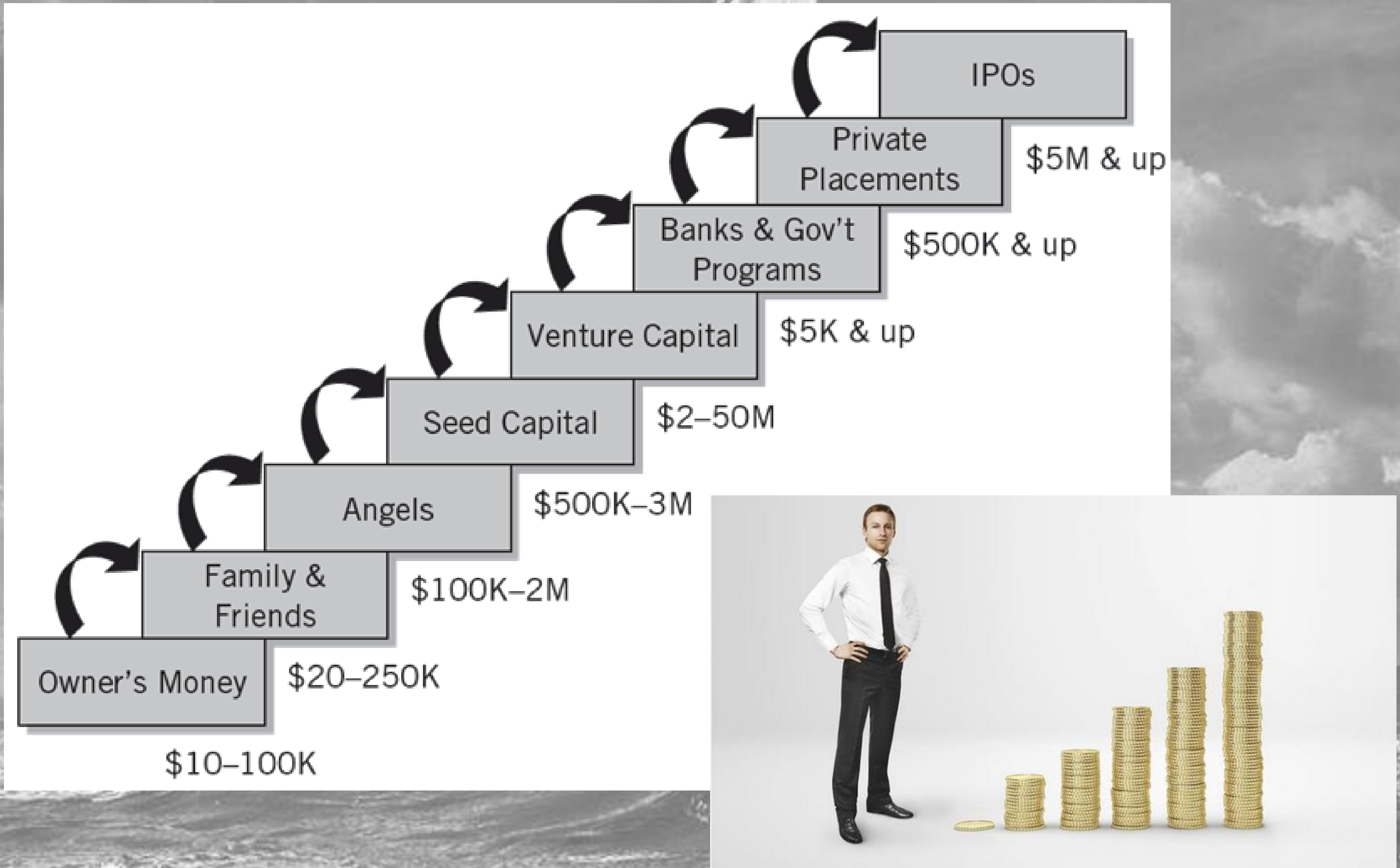
Pros	Cons
• Bootstrapped firms almost always spend cash more effectively than equity-financed ventures • Requires being close to customers, clearly identifying problems and solutions	• Resources for product development and market development constrained by cash flows • May miss big opportunities • May be left behind by competitors

A case history

Eventbrite

The Valorization Process

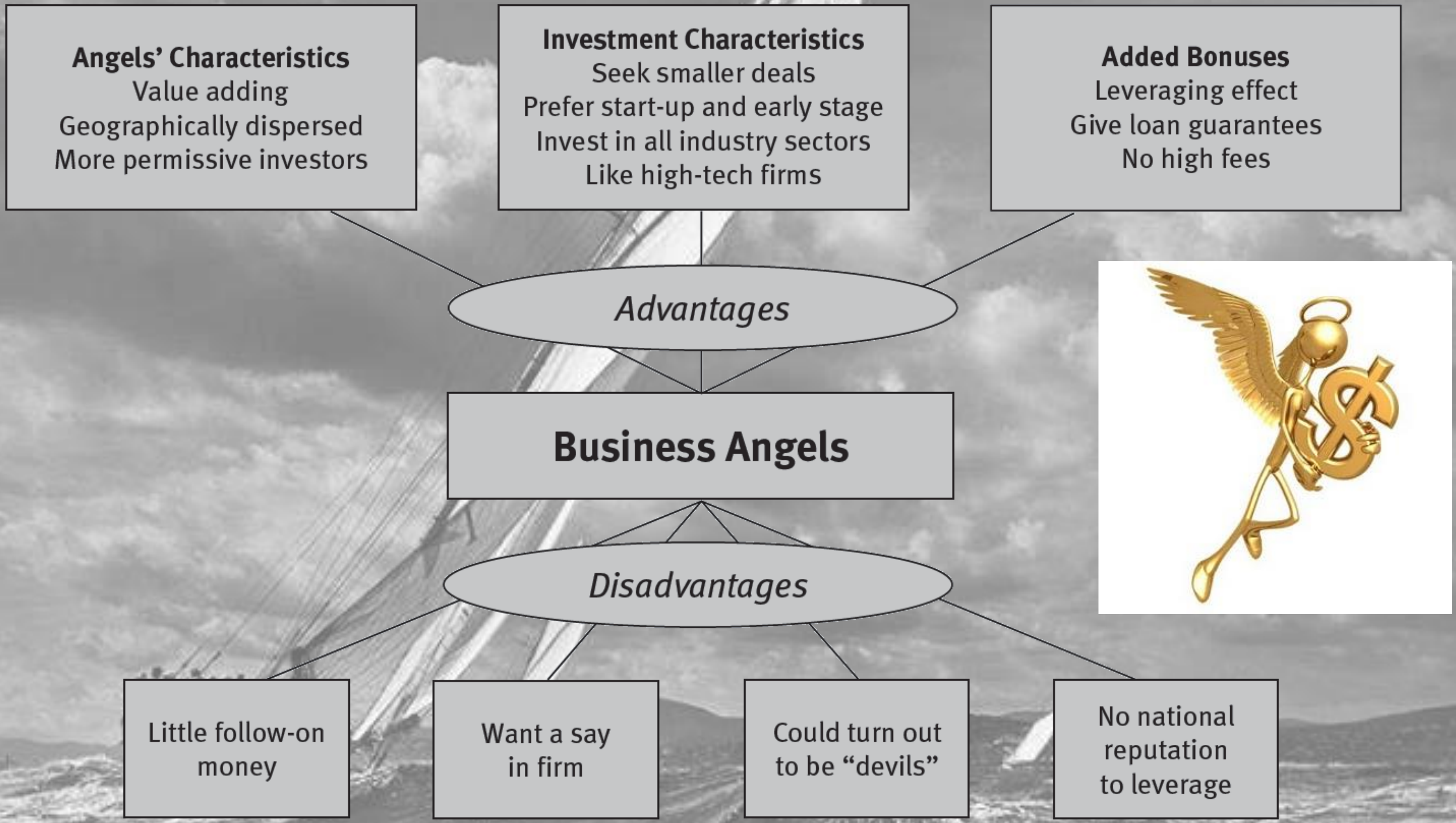
Typical Financing for High growth Firm



Business Angels

- Are private investors who invest in emerging business start-ups in exchange for equity stakes in the company
  - Ideal for companies that are too big for friends and family investors, but too small for VC companies
  - Most likely to finance start-ups with capital requirements in the $10,000 to $2 million range
- The prototypical business angel has high income and wealth, is well educated, has succeeded as an entrepreneur, and is interested in the start-up process.
- Most angels prefer to maintain a low profile so the key is **finding them!**

The Pros and Cons of Business Angel Investments



Source: Osnabrugge and Robinson, *Angel Investing* (2000),

Venture Capital

- VC is money that is invested by venture capital firms in start-ups and small businesses with exceptional growth potential.
    - Venture capital firms are limited partnerships of money managers who raise money in “funds” to invest in start-ups and growing firms.
    - The funds, or pool of money, are raised from wealthy individuals, pension plans, university endowments, foreign investors, and similar sources.
    - The investors who invest in venture capital funds are called limited partners.
    - The venture capitalists are called general partners.

Venture Capital

- Venture capital firms fund very few entrepreneurial firms in comparison to business angels.
  - Many entrepreneurs get discouraged when they are repeatedly rejected for venture capital funding, even though they may have an excellent business plan.
  - Venture capitalists are looking for the “home run” and so reject the majority of the proposals they consider.
  - Venture capitalists fund between 3,000 and 4,000 companies per year, compared to about 52,000 per year for business angels.

Venture Capital
More than just funding

- Advice and contacts
  - ➢ Provide management advice and access to valuable networks of contacts of suppliers, employees, customers, and other sources of capital
- Control
  - ➢ Entrepreneurs must give up a portion of their businesses in exchange for funding
    - Some VCs take an active role, others are passive investors

Venture capital + / -

Advantages	Disadvantages
Can raise substantial amounts	Venture capitalist requires a high rate of return
Business benefits from specialist investor support	Investment often supported by a high level of bank debt in business
Brings better discipline to business management & strategy	Not a long-term investment – venture capitalist will aim to sell within 5-7 years
Helps original business owners realise their investment	Loss of control – venture capitalist may take a majority share in company

tutor2u

Business Angels vs. 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

Source: Osnabrugge and Robinson, *Angel Investing* (2000)

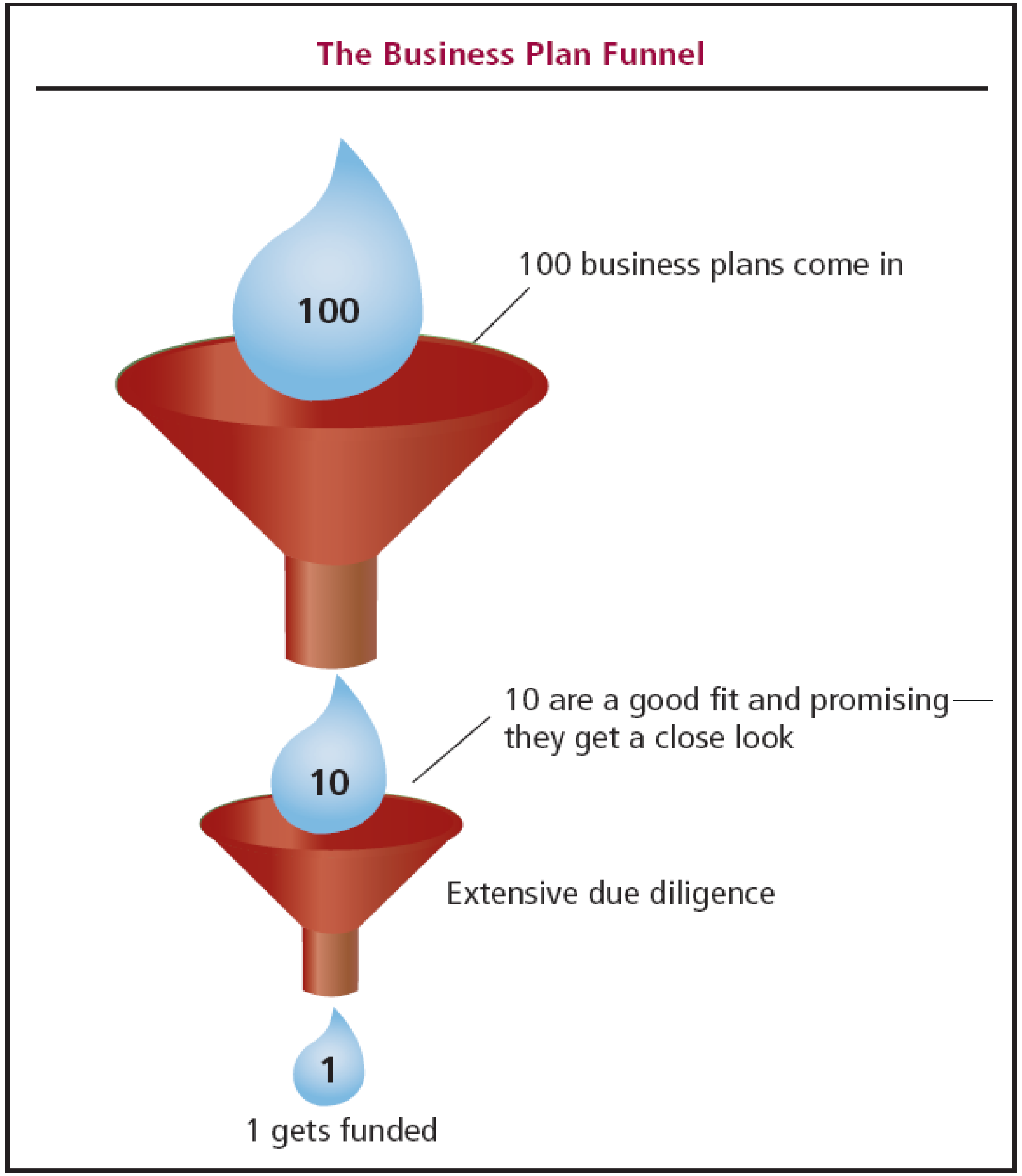


FIGURE 13.3

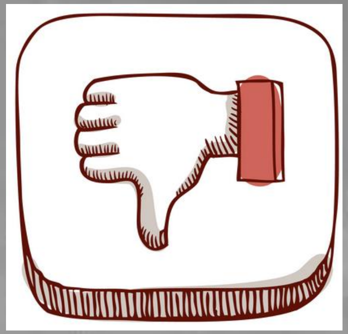
The Business Plan Funnel

Source: Venture Impact: The Economic Importance of Venture Backed Companies to the U.S. Economy, Fourth edition, National Venture Capital Association, 2007, p.10.

Partnering

- Capital can also be provided through relationships with customers, suppliers, rivals, etc.
- Partnership may take the form of joint ventures, licenses, distribution arrangements, cross ownership/support agreements.
- This is a longer-term, deal-specific approach, typically appropriate solely for the more mature business.

Partnering



Advantages

A business owner who partners with a compatible, strong partner can take advantage not only of their partner's sources of financing, but also their business acumen, employees, equipment and other resources such as complementary assets.

Disadvantages

- giving up personal control;
- diluting ownership;
- sharing profits.

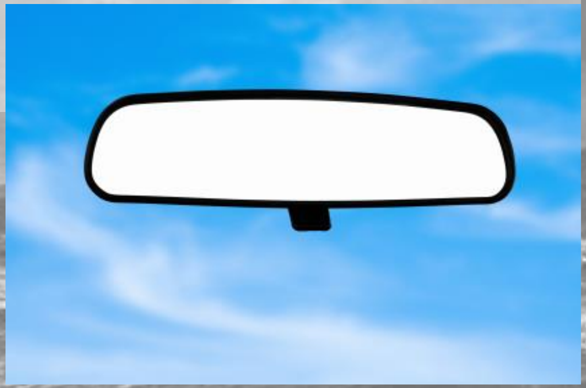
Debt Financing

- Banks provide 50% of the dollar value of loans to small businesses
- Reasons for borrowing:
  - ➢ Increasing the company’s workforce and/or inventory to boost sales
  - ➢ Gaining market share
  - ➢ Purchasing new equipment
  - ➢ Refinancing existing debt
  - ➢ Taking advantage of cash discounts
  - ➢ Buying the building in which the business is located
  - ➢ Establishing a relationship with a lender
  - ➢ Foreseeing a downturn in business

Two general types:
Conventional
and asset- based

Conventional bank loans (cash flow financing)

- Banks look primarily at a business' **income statement** to determine if it can generate sufficient **cash flow** in the future to service the debt.
- In this way, banks lend primarily based on what a business has done financially in the past, using this to gauge what it can realistically be expected to do in the future.
- It's what is called **"looking in the rear view mirror."**



Debt Financing: Asset-based loans

- Asset-based lending may be an alternative for startups that don’t qualify for a conventional bank loan
- Commercial finance asset-based lenders look at a business’ balance sheet and assets — primarily:
  - its accounts receivable
  - its inventory
  - its equipment
  - its real-estate\
  - **its property rights**

COLLATERAL

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.

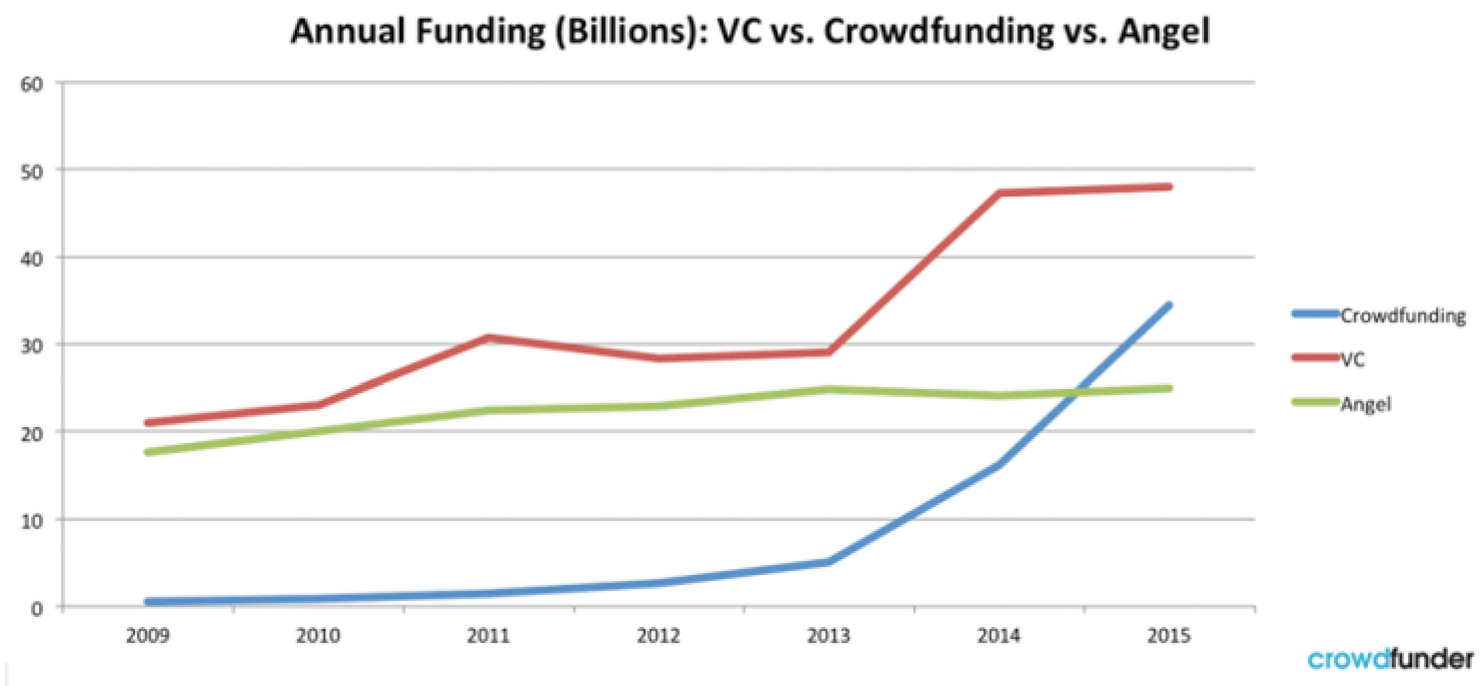
Crowdfunding

- **Crowdfunding** is the practice of funding a project or venture by raising monetary contributions (-- $10, $50, $100, maybe more) from a large number of people, typically via the Internet.
- This has all become possible in recent years thanks to a proliferation of websites that allow nonprofits, artists, musicians -- **and yes, startups**-- to raise money.
- Gained traction in the United States after the 2003 launch of ArtistShare, the first online crowdfunding platform.
- There is more than 1.000 of crowdfunding platforms around the world, with fundraising reaching billions of dollars annually.

Crowdfunding
Four types

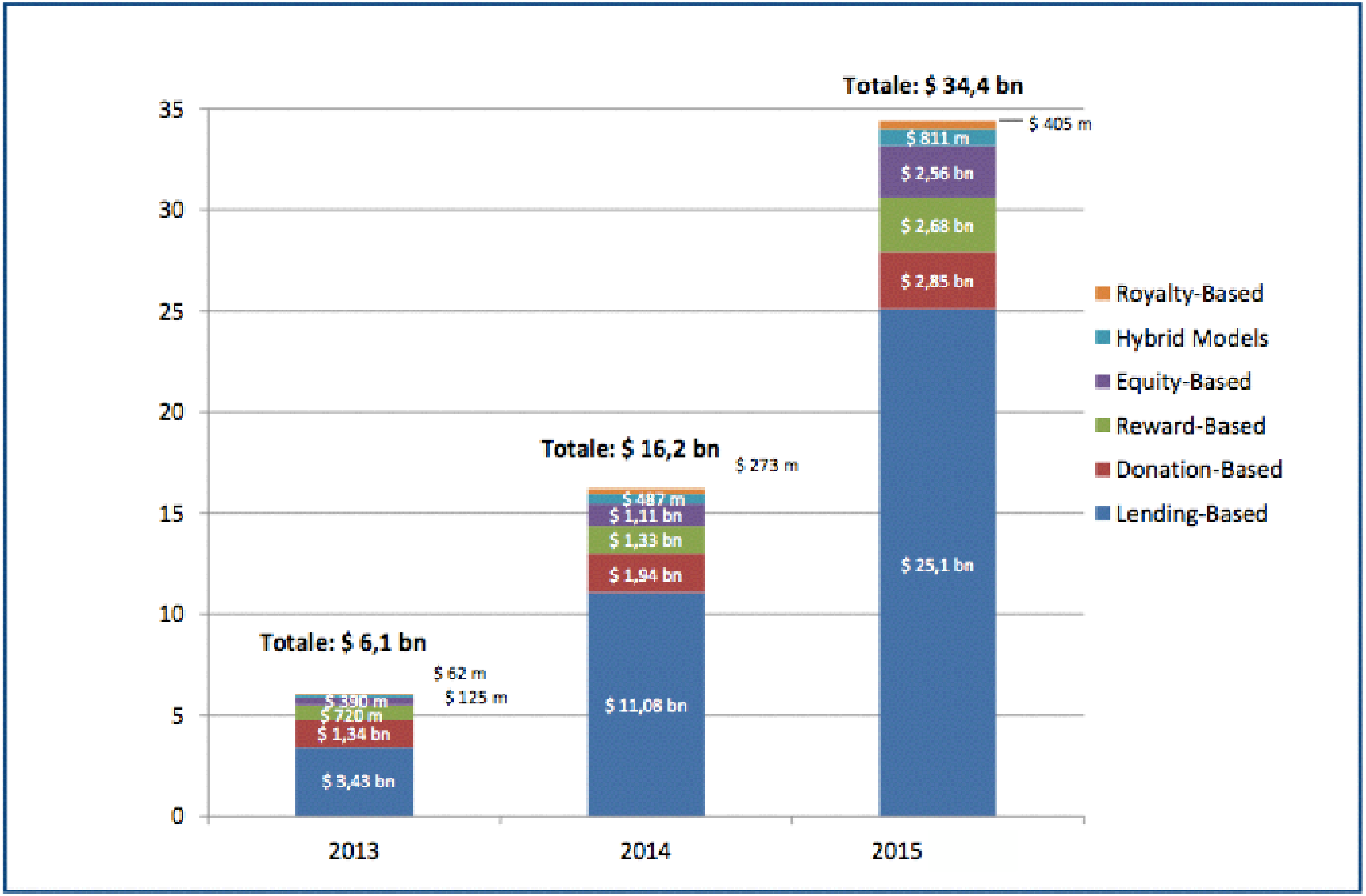
- **Donation-based:**
  - *Supporters make donations to your project and receive nothing in return (beyond the satisfaction of participating in your start-up).* (i.e. Migranodearena)
- **Rewards-based:**
  - *In exchange for a small amount of money, funders receive something. This is the perfect situation if you have a product to bring to market.* (i.e. Kickstarter, Goteo)
- **Debt-based crowdfunding:**
  - *A simple lending strategy where small amounts of money are repaid with interest (*Somolend*).*
- **Equity based:**
  - *By far the most complicated. Money is exchanged for a shareholder stake, which adds extra responsibility on the owner's (your) part.* (i.e. startupvalley.com, crowdcube.com, seedrs.com) https://www.seedrs.com/freeagent

- Crowdfunding surpassed Angel Investing in 2015, on trend to surpass Venture Capital in 2016



Note. Seems to rely on the Massolution report numbers above, which include P2P/Marketplace lending as a part of Crowdfunding.

Source: Chance Barnett, CEO of Crowdfunder.com, in a piece on Forbes.com



Totale: $ 34,4 bn
$ 405 m
$ 811 m
$ 2,56 bn
$ 2,68 bn
$ 2,85 bn
$ 25,1 bn
Totale: $ 16,2 bn
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$ 487 m
$ 1,11 bn
$ 1,33 bn
$ 1,94 bn
$ 11,08 bn
Totale: $ 6,1 bn
$ 62 m
$ 125 m
$ 390 m
$ 720 m
$ 1,34 bn
$ 3,43 bn
35
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20
15
10
5
0
2013
2014
2015
Royalty-Based
Hybrid Models
Equity-Based
Reward-Based
Donation-Based
Lending-Based

Crowdfunding, Finance, Storytelling

THE STARTUP STORY

- Vision/Mission
- Context
- Customers
- Rivals
- Timelines
- Knowledge
- Team
- Advisors/Investors
- Research
- Partners
- Messaging
- Assumptions

Got it… But does it REALLY help me to raise money??

Ok, but what does it mean exactly??

The Storytelling Canvas

Title:

Date:

Situation & Ambition

What is the current situation we're in?
What is its bigger context?
Who is involved?
What is our grand ambition?
What are our business objectives?

Resolution

How are we going to solve the challenge?
Why do we think this is the right solution?

Challenge

What's the biggest challenge we're facing?

Insight & Opportunity

What is the one thing that helps us overcome the challenge?

Epilogue & Appendix

What is the expected outcome?
What do we need to turn our strategy into action?

And now…the Pitch

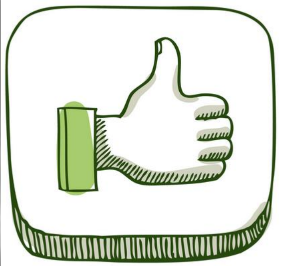
Initial Public Offerings (IPOs)

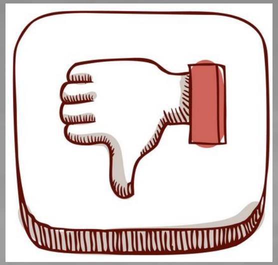
An **initial public offering (IPO)** is a popular way to raise a lot of money for growth since all proceeds go to the company.

- Is a way to raise equity capital to fund current and future operations.
- Raises a firm’s public profile, making it easier to attract high-quality customers and business partners
- Creates a form of currency that can be used to grow the company via acquisitions.

initial public offering (IPO): the sale of stock in a company on a public stock exchange

Initial Public Offering





Advantages

- Obtaining new equity capital for growth and survival.
- Enhancing valuation due to greater liquidity.
- Ease in raising additional capital.

Disadvantages

- Public exposure and potential loss of control.
- Loss of flexibility and increased duties to public stockholders and administrative burdens.
- Expenses involved ($700,000).
  - The Sarbanes-Oxley Act ↑
- Exasperating process.

The Dos and Don’ts of Raising Capital

DO

- **Sharpen Your Focus:**
- Know Who You Are Pitching To
- Try to Get a Referral Into the Investor or VC Firm
- Have a Good Advisory Board
- Have Good Legal Counsel
- Make Sure You Have a Handle on Your Secret Sauce
- Have a Great Business Plan & Executive Summary
- Line Up Your References
- Be Specific About Your Funding Requirements

The Dos and Don'ts of Raising Capital

DON'T

- Financial Projects with Unrealistic, Unfounded Assumptions:
  - *Crazy, Wild, Optimistic Revenue Numbers*
  - *Unrealistic Expenses*
  - *Underestimating the Total Size of Investment to Achieve Scale*
- Talking About Large, Generic Markets
- Focusing Only on Proprietary Technology
- Asking for NDAs
- Focusing Too Much on the Future at the Expense of the 12 Month Milestone
- Avoiding a Discussion of Your Competition or Actually Claiming Your Venture "Has No Competition"

Growth Stages and Funding Sources

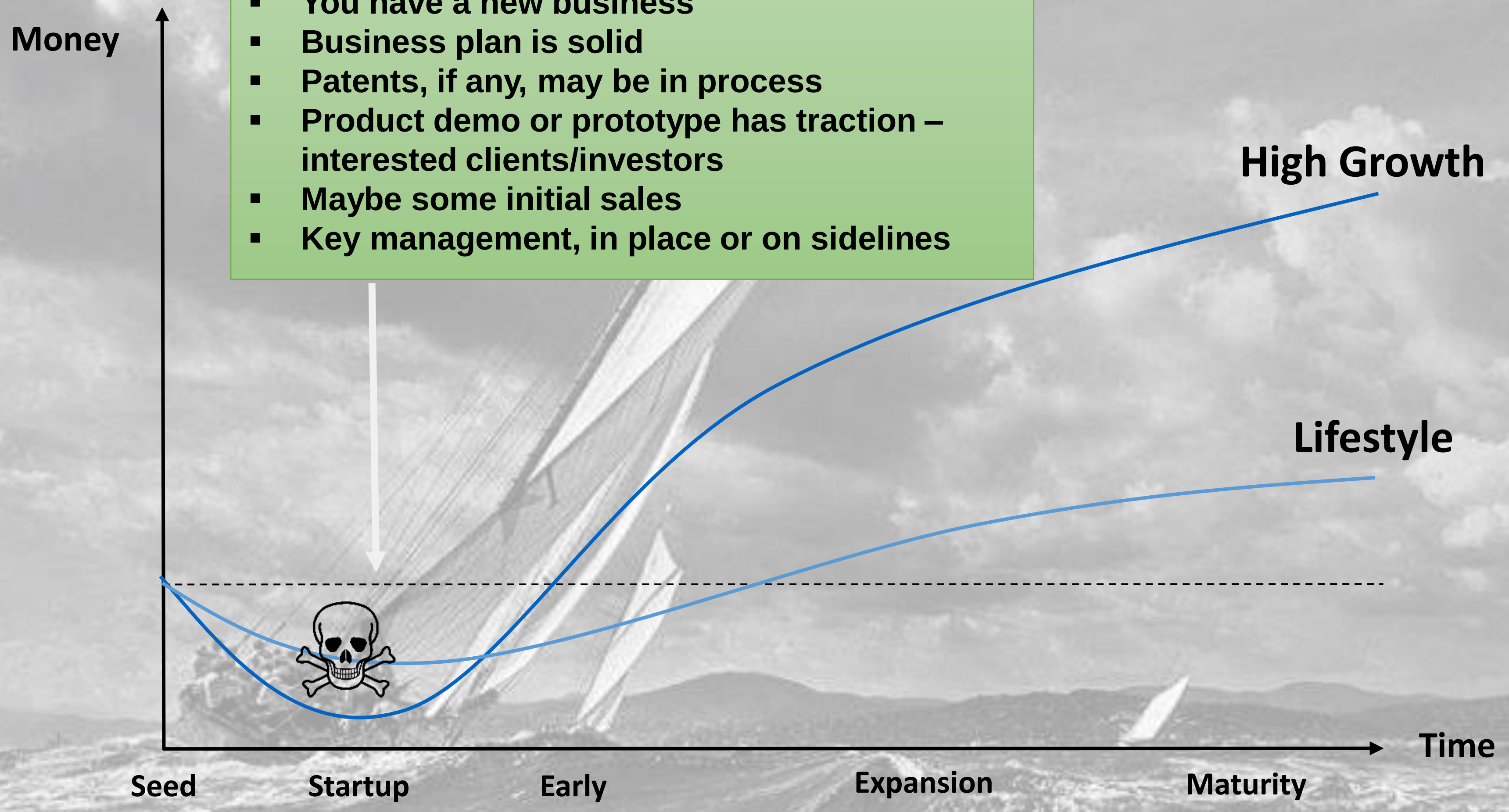
1. Seed Stage Financing

- You have an idea
- Writing the business plan
- Investigating the market
- Looking for people to join you
- Creating a prototype/demo of product or service
- Investigating patents

Growth Stages and Funding Sources

2. Startup

- You have a new business
- Business plan is solid
- Patents, if any, may be in process
- Product demo or prototype has traction – interested clients/investors
- Maybe some initial sales
- Key management, in place or on sidelines



The risks of the startup phase

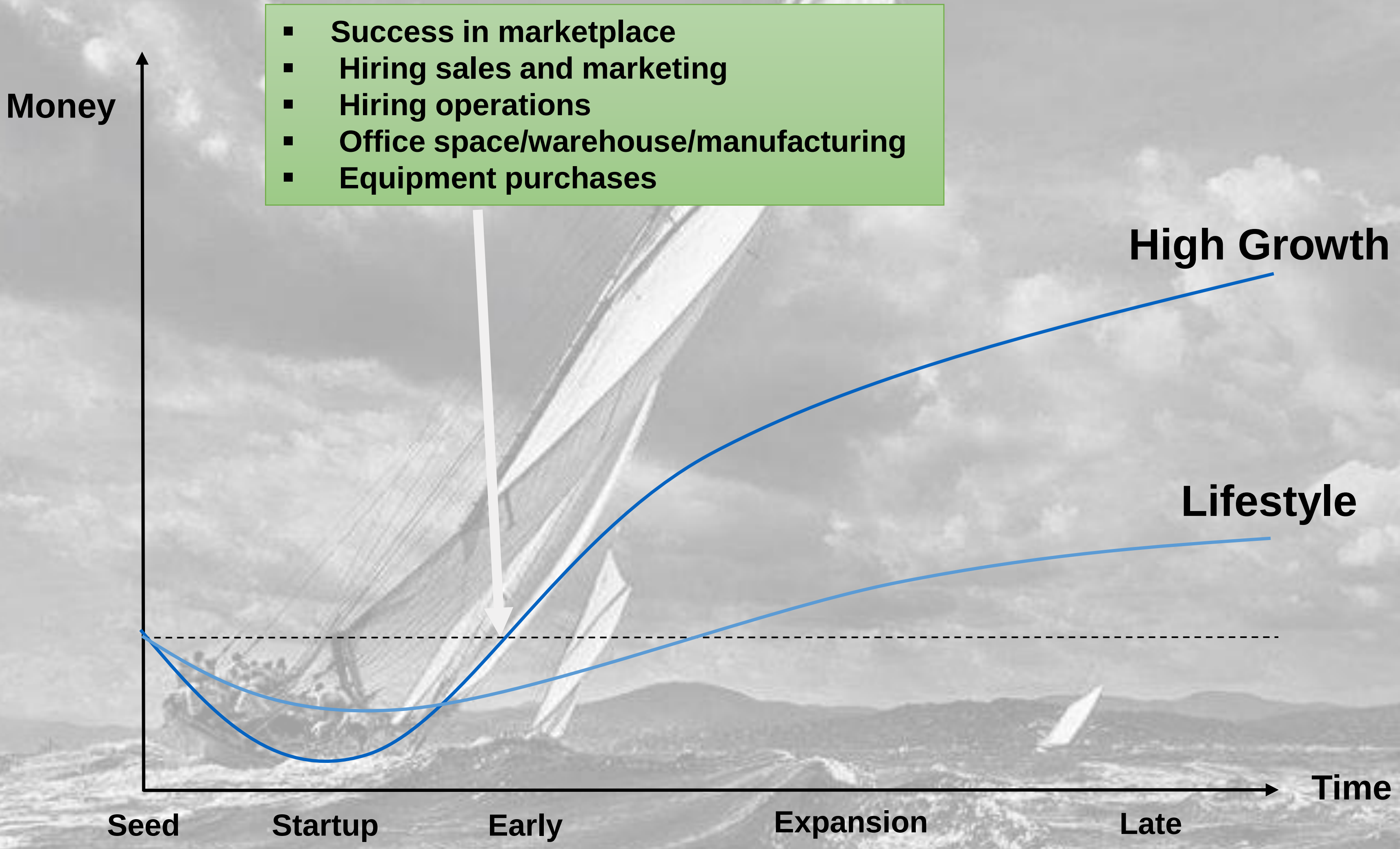
http://www.telegraph.co.uk/women/womens-business/11613924/Careers-advice-from-Upper-Street-shoes-CEO-Julia-Elliott-Brown.html

Julia's top 5 tips for Crowdfunding success

1. Make an emotionally engaging video – you have just a few minutes to get your audience to connect with your story and vision, so make it count; it will make or break whether they decide to view the rest of your pitch.
2. Set your target to 'just enough' – if you don't hit your funding objective, you get none of the money; better to set the target a little lower, and over-fund.
3. Run your campaign like a military operation – build a strong communication plan for all key stakeholders; your customers and business contacts could be your richest source of investment.
4. Get early support – secure early commitment from existing investors, and trusted contacts before you make your campaign live; seeing that others have already backed you gives the 'crowd' greater confidence.
5. Keep the faith – when it feels like your campaign is losing momentum, keep on asking people for commitment; it's often only in the last few weeks that campaigns gain velocity and hit target.

Growth Stages and Funding Sources

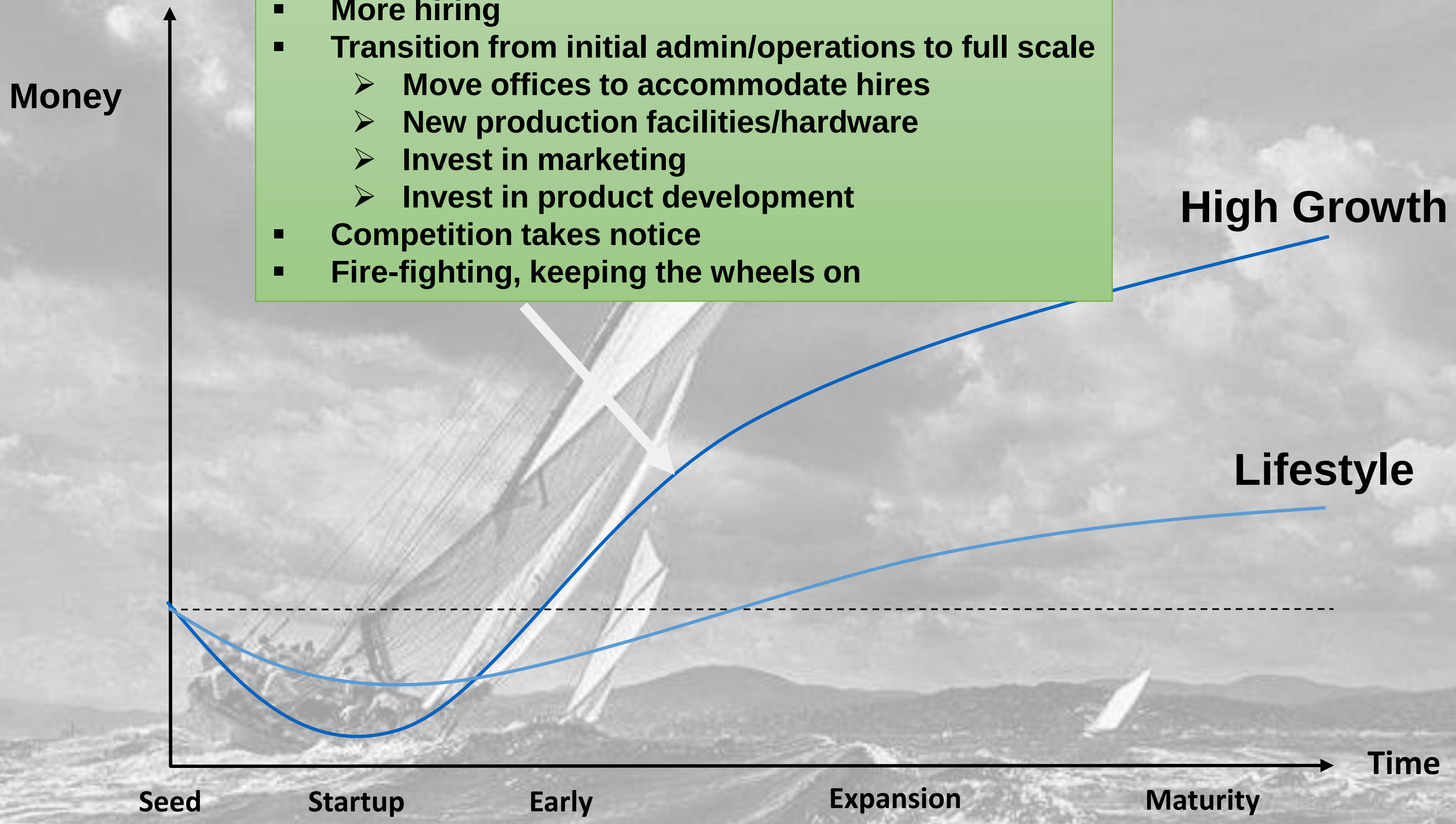
3. Early-Stage Financing



Growth Stages and Funding Sources

4. Expansion Stage

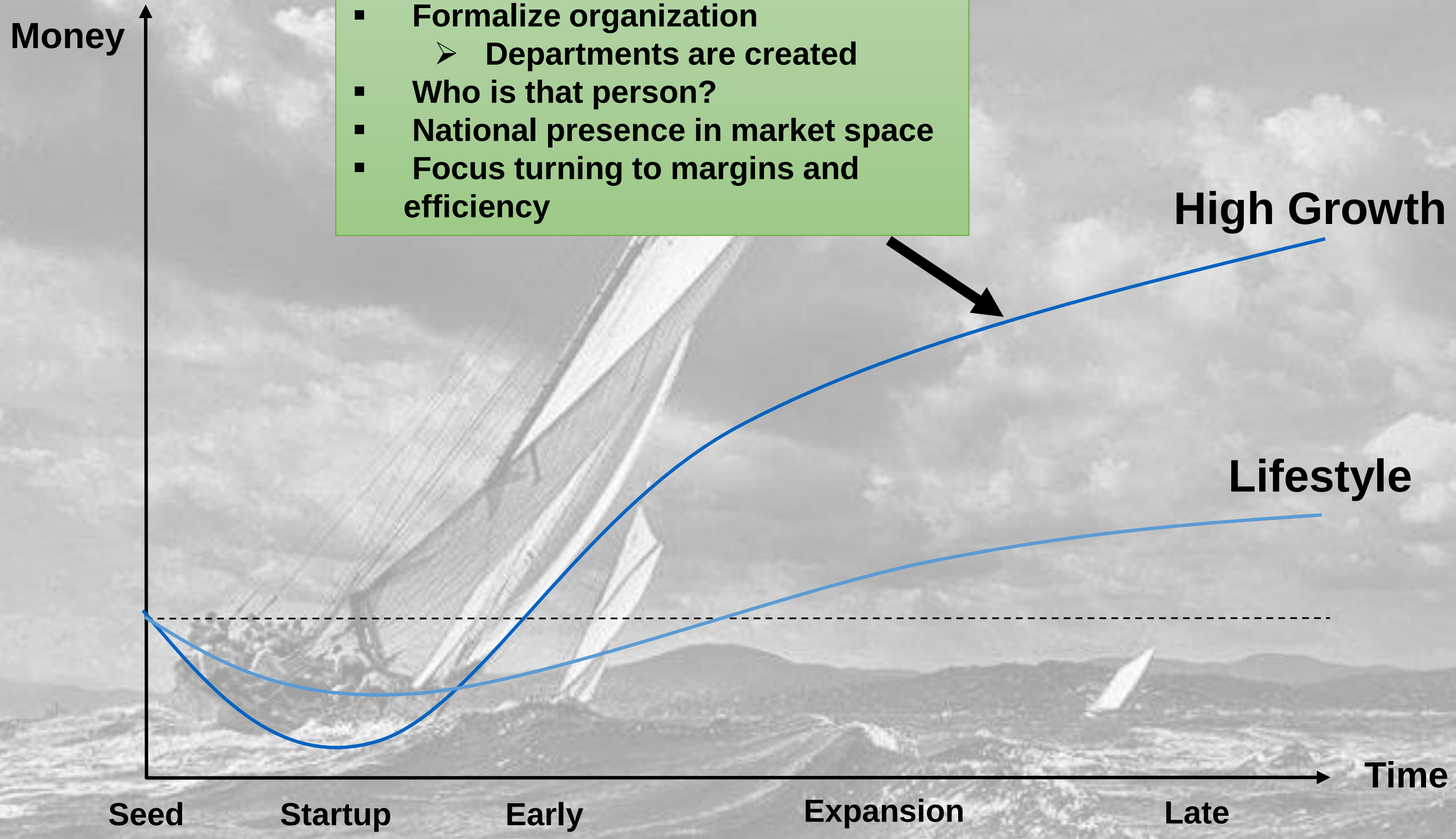
- Growing quickly
- More hiring
- Transition from initial admin/operations to full scale
  - Move offices to accommodate hires
  - New production facilities/hardware
  - Invest in marketing
  - Invest in product development
- Competition takes notice
- Fire-fighting, keeping the wheels on



Growth Stages and Funding Sources

5. Late-Stage Financing

- Continued growth
- Formalize organization
  - Departments are created
- Who is that person?
- National presence in market space
- Focus turning to margins and efficiency



Raising funds – Do’s and Don'ts

Do’s

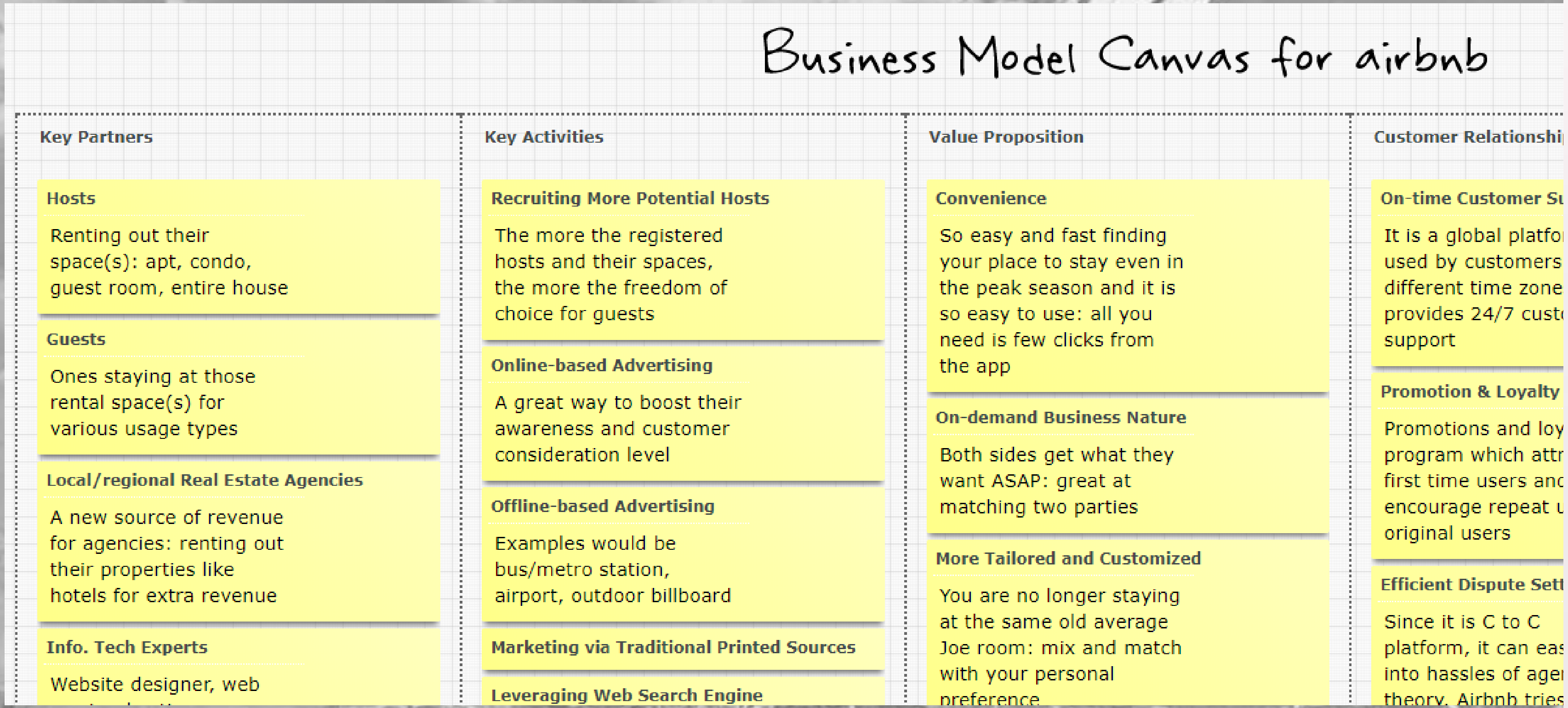
Know the field you are going to be in like the palm of your hand

- Don’t suffice with “I’ve spoken to potential customers who said they would buy as soon as it’s available”
- Don’t suffice with theoretical market researches
- Don’t hesitate to talk to competitors

Build and further your idea as much as you can – and more

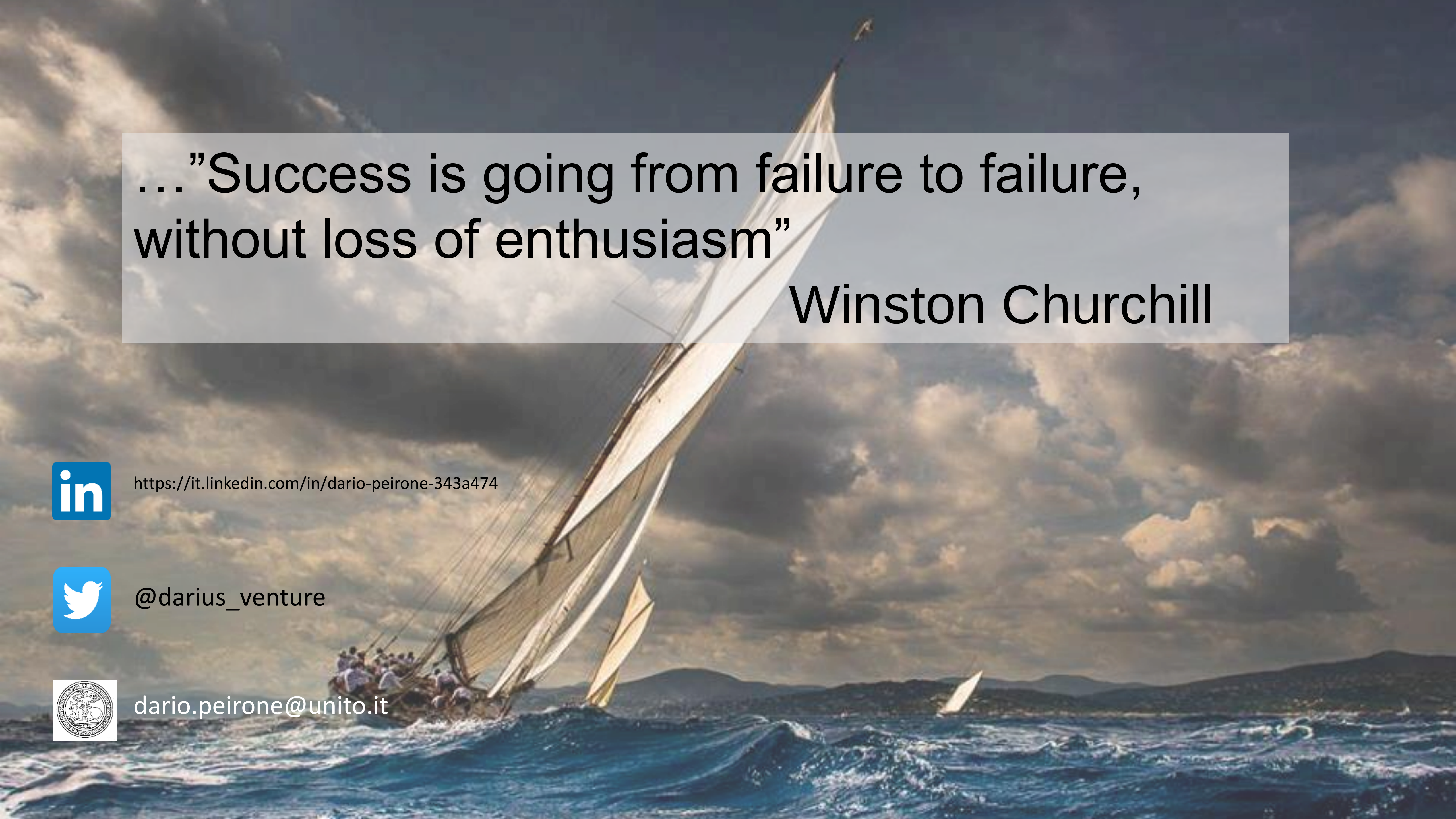
- Don’t say “as soon as I have the funds I start”
- Don’t say “as soon as I leave my job I start”
- Don’t WAIT (if you are not eager, why would the investor be?)

To Summarize….


Business Model Canvas for airbnb

Key Partners	Key Activities	Value Proposition	Customer Relationshi
Hosts Renting out their space(s): apt, condo, guest room, entire house	**Recruiting More Potential Hosts** The more the registered hosts and their spaces, the more the freedom of choice for guests	**Convenience** So easy and fast finding your place to stay even in the peak season and it is so easy to use: all you need is few clicks from the app	**On-time Customer Su** It is a global platfo used by customers different time zone provides 24/7 custo support
Guests Ones staying at those rental space(s) for various usage types	**Online-based Advertising** A great way to boost their awareness and customer consideration level	**On-demand Business Nature** Both sides get what they want ASAP: great at matching two parties	**Promotion & Loyalty** Promotions and loy program which attr first time users and encourage repeat u original users
Local/regional Real Estate Agencies A new source of revenue for agencies: renting out their properties like hotels for extra revenue	**Offline-based Advertising** Examples would be bus/metro station, airport, outdoor billboard	**More Tailored and Customized** You are no longer staying at the same old average Joe room: mix and match with your personal preference	**Efficient Dispute Sett** Since it is C to C platform, it can eas into hassles of agen theory. Airbnb tries
Info. Tech Experts Website designer, web	**Marketing via Traditional Printed Sources**		
	Leveraging Web Search Engine		

Creating Startups works like this….



…"Success is going from failure to failure, without loss of enthusiasm"

Winston Churchill

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