

Course title: Creating Innovative Business Models

Lecture 7. Corporate venture

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Entrepreneurial Resources

- ▶ Most start-up funds come from an entrepreneur's personal resources, such as savings; however, there are other common sources of funding.
- ▶ One of the unique talents of entrepreneurs is finding the resources to launch a business. This requires understanding the differences between
 - short-term needs, those associated with activities not part of normal operations; and
 - long-term capital needs, relating to preparation for future growth.

BOOTSTRAPPING

- Most entrepreneurs get their businesses started by **bootstrapping**.
- **Bootstrapping**: operating a business as frugally as possible and cutting all unnecessary expenses, accomplished by borrowing, leasing, and partnering to acquire resources
- Bootstrapping involves:
 - hiring as few employees as possible
 - leasing anything you can
 - being creative

BOOTSTRAPPING

- Bootstrapping entrepreneurs can also ask suppliers to allow for longer payments terms, ask customers to pay in advance, or sell their accounts receivable to a **factor**.
- **factor**
- an agent who handles an entrepreneur's accounts receivable for a fee

Start-Up Money

- ▶ The main sources for start-up money for entrepreneurs include:
 - friends
 - family
 - others who believe in the entrepreneur
- ▶ These resources come in several forms, such as savings, credit cards, loans, and investments.

FINANCING THE START-UP

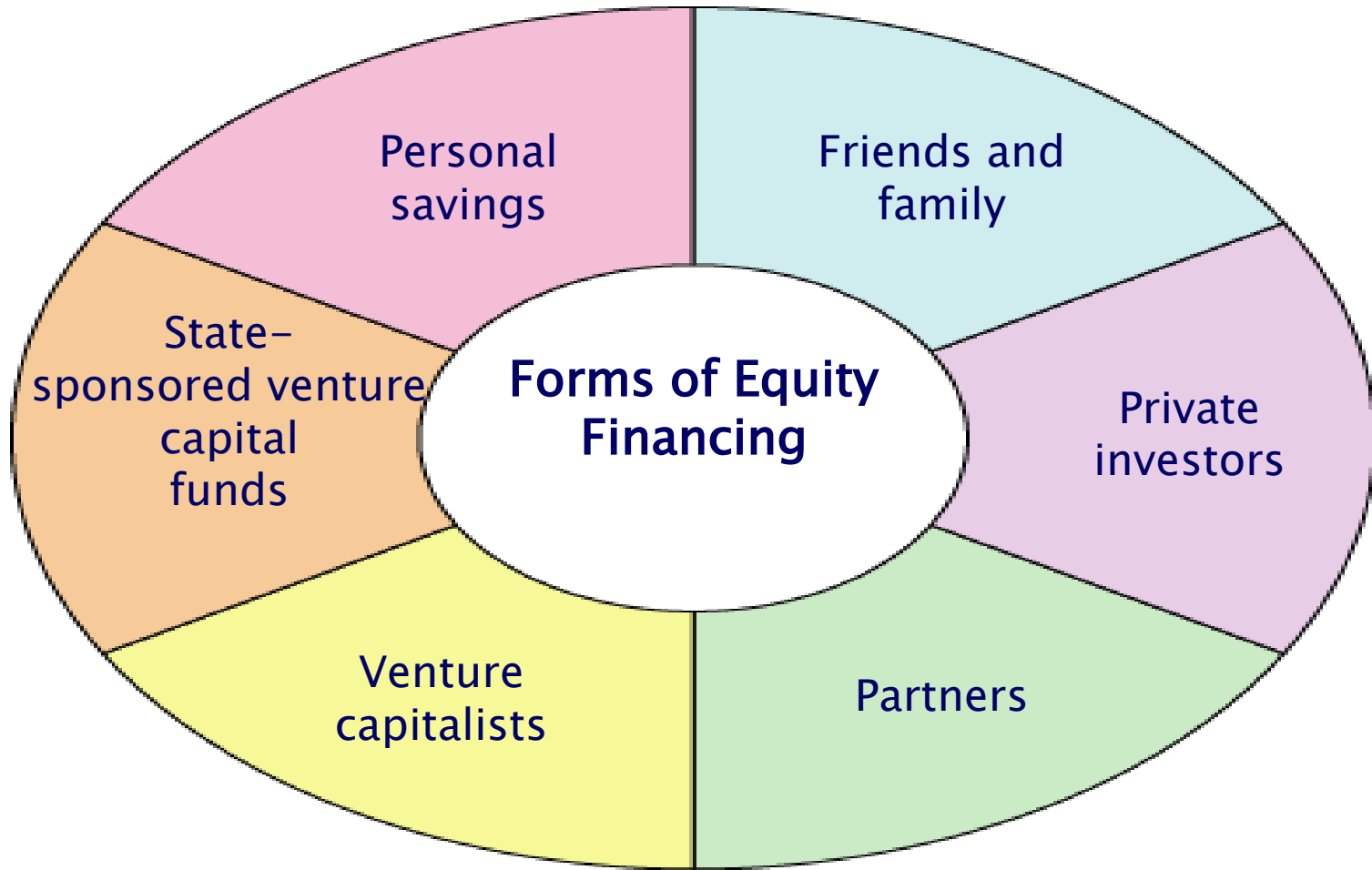
▶ Some sources of financing include:

- banks
- finance companies
- investment companies
- government grants

Sources of Equity Financing

- To obtain **equity capital** as a source of funding for a business, the owner must give **equity** to obtain the financing.
- **Equity:** an ownership in a business
- Equity funding is sometimes called **risk capital**.
- **risk capital:** money invested in companies where there is financial risk

Sources of Equity Financing



Sources of Equity Financing

- An **angel** often invests because of his or her belief in a business concept and the founding team.
- **Angel:** a private, nonprofessional investor, such as a friend, a relative, or a business associate, who funds start-up companies

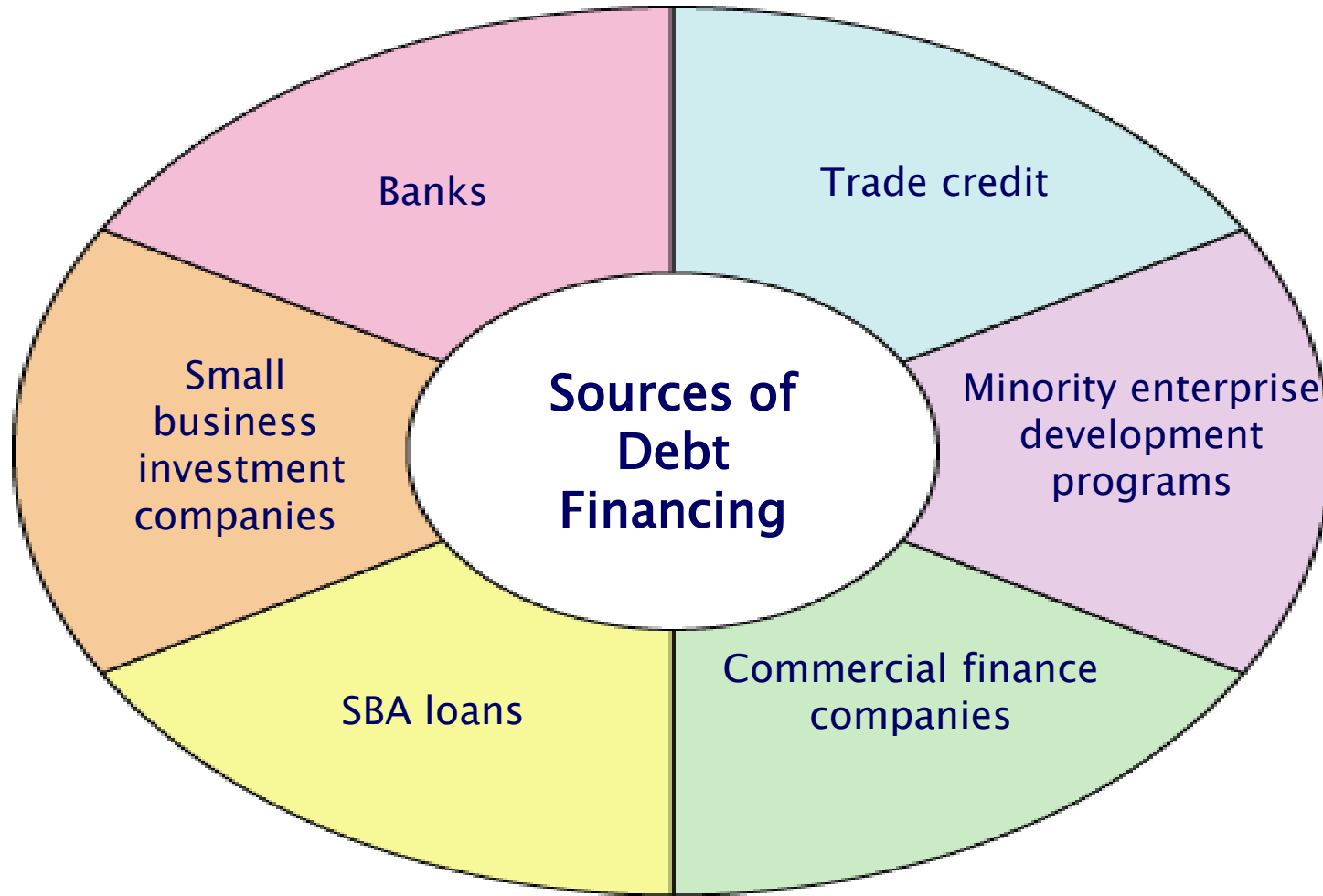
Sources of Equity Financing

- An existing business can use **venture capital** financing to raise large amounts of money to achieve its goals.
- **venture capital:** a source of equity financing for small businesses with exceptional growth potential and experienced senior management
- **Venture capitalists** often provide managerial and technical expertise to small businesses.
- **venture capitalists:** individual investors or investment firms that invest venture capital professionally (Shark Tank)

Sources of Debt Financing

- Sources of **debt capital** are far more numerous than sources of equity capital, but the entrepreneur must be certain the business can generate enough cash flow to repay the loan.
- **debt capital:** money raised by taking out loans, which must be repaid with interest

Sources of Debt Financing



Sources of Debt Financing

- Banks were once the primary source of **operating capital**, but today they are much more conservative in their lending practices.
- **operating capital**: money a business uses to support its operations in the short term
- An established business can usually get a **line of credit** from a bank, which it can borrow against.
- **line of credit**: an arrangement whereby a lender agrees to lend up to a specific amount of money at a certain interest rate for a specific period of time

Sources of Debt Financing

- Some businesses may seek **trade credit** from other companies in their industry as a form of debt financing.
- **trade credit:** credit one business grants to another business for the purchase of goods or services; a source of short-term

Financial Planning for Your Business

- ▶ Financial planning involves finding the right kind of financial resources at the right time in the right amount.
- ▶ Financial planning involves:
 - Identifying the stages of growth in your business
 - Identifying milestones that require resources
 - Identifying business advisers
 - Hiring an excellent management team

How to Obtain Financing

- To obtain financing, you must create **pro forma** financial statements to include in your business plan.
- **pro forma**: proposed or estimated financial statements based on predictions of how the actual operations of the business will turn out

What Venture Capitalists Expect

- ▶ Venture capitalists rarely invest in start-up companies, but when they do, they expect:
 - A tenfold return on their investment in five to seven years (for start-up companies)
 - A five- to seven-times return on their investment (for businesses in the growth stage)
 - A business with large market potential, growing at least 20% each year

What Private Investors Expect

- ▶ Private investors, or angels, expect:
 - businesses they understand
 - investing with like-minded investors
 - ten times their investment at the end of five years
 - a strong management team

What Bankers Expect

- Commercial lenders like banks rely on the five Cs to determine the acceptability of a business loan applicant:

Character

Capacity

Capitol

Collateral

Conditions

What Bankers Expect

- A bank must believe in the **character** of the entrepreneur,
- **Character:** a borrower's reputation for fair and ethical practices, including business experience, dealings with other businesses, and reputation in the community
- Banks consider the **capacity** of a business to pay its debts
- **Capacity:** the ability of a business to pay a loan in view of its income and obligations

What Bankers Expect

- Banks place a strong emphasis on whether a business has a financially stable **capital** structure.
- **Capital:** the net worth of a business, the amount by which its assets exceed its liabilities
- Banks are more likely to lend to businesses with valuable **collateral**.
- **Collateral:** security in the form of assets that a company pledges to a lender

What Bankers Expect

- Banks consider all the **conditions** in which the business operates.
- **Conditions:** the circumstances at the time of the loan request, including potential for growth, amount of competition, location, form of ownership, and insurance

Types of Growth Financing

- ▶ If your company has established a successful track record, there are other types of financing available, including:
 - venture capital (VC) companies
 - private placements
 - initial public offerings (IPOs)

venture capital (VC) companies

- If a VC firm is interested in funding your business and decides you have a sound business plan, it will begin **due diligence**.
- **due diligence**: the investigation and analysis a prudent investor does before making business decisions

PRIVATE PLACEMENT

Private placement is a way to raise capital by selling ownership interests in your private corporation or partnership.

- ▶ **private placement:** private offering or sale of securities directly to a limited number of institutional investors who meet certain suitability standards; ownership interests are called securities

Initial Public Offering (IPO)

- An **initial public offering (IPO)** is a popular way to raise a lot of money for growth since all proceeds go to the company.
- **initial public offering (IPO):** the sale of stock in a company on a public stock exchange
- The CEO of a company that has made an IPO is primarily responsible to the people who own the company **stock**.
- **Stock:** a type of security that signifies ownership in a corporation and represents a claim on part of the corporation's assets and earnings

Initial Public Offering (IPO)

- ▶ There are five steps to become a public company with stock for sale on a public exchange.
 1. Choose an underwriter or investment banker.
 2. Draw up a letter of intent.
 3. File a registration statement with the SEC.
 4. Announce the offering in the financial press.
 5. Do a road show.

Calculating Your Start-Up Capital Needs

You will need to calculate exactly how much money you will need to start or grow your business.

This requires estimating start-up costs, which include capital expenditures, working capital (operating costs), and contingency funds.

Start-Up Costs

- ▶ Start-up costs are those costs you incur before you start a business.

- ▶ Start-up costs may include:
 - furniture, fixtures, and equipment
 - promotion expenses and office supplies
 - fees and licenses

Operating Costs

- Operating costs, often referred to as **working capital**, cover the time between selling your product or service and receiving payment from the customer.
- **working capital:** the amount of cash needed to carry out the daily operations of a business; it ensures a positive cash flow after covering all operating expenses

Contingency Funds

- Since no one can predict the future, you should include a **contingency fund** in your start-up calculations.
- **contingency fund**: an extra amount of money that is saved and used only when absolutely necessary, such as for unforeseen business expenses

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