



Quick Guide to Early Stage Startup Funding

10 Key Funding Fundas

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Dear Readers,

Wishing you a Happy Dassera!

On this auspicious occasion, we are happy to present this “Quick Guide to Early Stage Startup Funding”. This brief presentation is primarily meant for founders of early stage startups who need practical guidance on key issues of funding. It is also meant for professionals like Chartered Accountants, Company Secretaries & Financial Advisors who are working with Startups.



We hope that you will find this short guide useful. Please feel free to write us at mdoffice@posiview.in or call at 8975761062 for further guidance.

At Posiview, we call this the #LanguageOfGrowth.

Happy & Productive Reading!

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1. What should be legal structure?



- ◇ What should be the Legal Entity:
 - ◇ Proprietorship: Not recommended
 - ◇ Partnership: Not recommended
 - ◇ Limited Liability Partnership: Ideal to start with
 - ◇ Pvt Ltd Company: LLP can be converted to Pvt Ltd Co.

2. Should you take Co-Founders?



- ◇ Should you take Co-Founders?
 - ◇ Positives:
 - ◇ Different Skillsets, Risk Reduces, Better Management
 - ◇ Negatives:
 - ◇ Relation between founders, Slow Decision Making
- ◇ How Many Co-founders
 - ◇ Depends on nature of business
 - ◇ 2-3 is ideal number

3. Should you raise an angel round?



- ◇ Yes, Its always a good idea to raise funding from angels i.e. friends, family and close network. It prepares you to pitch to investors and gives VC funds more confidence.
- ◇ After Friends & Family, if possible can raise funding from external professional investors
- ◇ Keep a minimum threshold per investor - ideally Rs 5 lacs
- ◇ If possible do not have a large number of investors for initial funding. Try and keep the number below 10-15 people.

4. What is the right time to raise investment?



- ◇ There is no right or wrong time as such for raising funding. You should raise the funding to meet your business targets.
- ◇ There is a challenge in raising funding at concept stage. Ideally the founder/s should put in their funding atleast till creating a Proof-of-Concept (PoC) or a Minimum Viable Product (MVP)
- ◇ Focus should be to fund business from customer revenues for as long as possible
- ◇ When there is a visibility of revenue or a monthly growing revenue number, its the ideal time to approach funds.

5. How are early stage startups valued?



- ◇ Valuation of early stage companies is more of an art than science
- ◇ Companies are typically valued on Discounted Cash Flow (DCF) method.
- ◇ However investors also use Comparable Company approach i.e. using ratios of other companies in the similar line which have got funded. Eg. companies in a particular industry may be generally valued at 2x of sales. So even if DCF valuation is much higher, the investor will value the company somewhere in this range.
- ◇ Intangibles such as quality of Promoters, No. of VCs interested in investing, potential of the sector in which company interested also play a role in deciding valuation.

6. Should you give ESOP/Sweat Equity to employees?



- ◇ It is a standard practice to issue ESOP / Sweat Equity to early employees. ESOPs are also issued after funding to attract the right talent.
- ◇ Sweat Equity can be given to some key members of founding team who are not promoters but have made invaluable contribution to the company
- ◇ You should note that all members of the founding team may not continue in long term; so evaluate and issue ESOPs accordingly
- ◇ As a standard practice 10% of company's share capital is reserved for ESOPs. If the company does not have an ESOP Plan, the VC Fund will mostly insist that a plan be created

7. What are the various round of funding?



- ◇ Founder's Capital : Own contribution of founders
- ◇ Friends & Family : Funding from people known to Founders
- ◇ Angel Round : Typically Upto Rs 2-5 crs. from Angel Investors, Angel Networks & Micro VCs
- ◇ Seed Round: Typically Rs 3-7 crs. from Super Angels & Seed Funds
- ◇ Pre-Series A: Typically Rs 5-15 crs. from Super Angels & VC Funds
- ◇ Series A : Rs 15-50 crs from VC Funds
- ◇ Series B & onwards : Depends on Company & VC Fund

8. What are returns & exit expectations of investors?



- ◇ Return expectations depend on type of investor. However the early stage investors expect returns in multiples of their investment. Individual investors typically sell their investment when the VC round takes places. The investment period of early stage investors is 2-3 years
- ◇ VC Funds invest for a 4-6 years period. Sometimes they can also dilute part of their stake or invest additional funds in the next round of investment.
- ◇ The preferred mode of exit of VC funds is next round of funding or IPO. Sometimes the company may also be acquired by another company.

9. What are the key points in an Investor Presentation?



- ◇ Two presentations should be made. One short Executive Summary of upto 10 slides and an Investor Memorandum of 25-40 slides
- ◇ The Executive Summary should contain details of the Market Opportunity, Problem/Solution, Product/Service & its USPs, Founders & Team, Go-To-Market Strategy, Competitive Landscape, Financial Summary, Investment & End Use.
- ◇ Financial Projections should be aggressive but backed up by assumptions that the founder/s should be able to justify
- ◇ Investor Memorandum can have explanation of each point mentioned above

10. What are the key factors that VC Funds look at?



- ◇ Quality of the Promoter is the most critical factor
- ◇ Size and growth of the Market in which the company exists
- ◇ Product / Service of the company - technology, quality, pricing
- ◇ Nature and stage of competitors and their products
- ◇ Amount of funding needed and where would that take the company
- ◇ Reasonability of Valuation



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