ENET

Understanding Term Sheets and Valuation

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Bill McCullen
LaunchCapital
Director, Boston Office
Outline

• Introduction to LaunchCapital

• Valuation Methodology

• Valuation Considerations for Early Stage Companies
LaunchCapital Overview

- Established in February ‘08 to address the early stage funding gap
  - Large VCs focused on later stage and bigger deals
  - At that time, the gap was acute on the East coast as few institutional investors specialized in seed stage
  - Over 60 investments in 3 years

- Great time for investing in capital efficient businesses
  - Cost of starting a business had dropped
  - Opens the door to successful investments at lower value exits

- Goal to diversify across several parameters
  - Geography – 3 offices open in Spring/Summer ‘08
  - Industry – industry agnostic, focus on the business model
  - Deal type – from pre-seed/tech transfer to small Series A, lead or follow, level of activity

- Typical investment in $50k to $250k range
Changing Landscape - Explosion of Seed Funds in 2H09 and 2010

New Seed VCs by Location
Since Jan 2009

- Other: 6
- NYC: 19
- SF: 21
- MA: 3

New Seed VCs by Industry
Since 2009

- Other: 6
- Agnostic: 9
- Energy: 3
- Technology: 31

Plus:

- Emergence of Angel List (1000 angel investors)
- Larger VCs also syndicating seed rounds (KPCB, CRV, Greylock, Sequoia, Accel, GC, etc.)
Valuation Methodology

• It all depends on the stage of investment

• Late-Stage is heavy on data – Quantitative

• Early stage is highly subjective – Qualitative
Valuation Methodology – Late Stage

• Comparable Company Valuation
  – Publicly traded or known private
  – Multiple based – sales, EBITDA or perhaps UMV or other users data
  – Challenge – finding true comparable companies (markets, business model, stage/growth rate etc.)

• Comparable Transaction Valuation
  – Again, multiple based
  – Challenge - Finding relevant data
    • Valuation not revealed for many private transactions
    • Things changes in 2008-2009

• Discounted Cash Flow
  – One data point with sensitivity
  – Challenge - Assumption driven (growth rate, discount rate, etc.)
Valuation Methodology – Early Stage

• Often Pre-revenue or even Pre-product

• Very Subjective with influence from
  – Team – have they done it before, successful exit?
  – Traction – is the product done?, any early customer traction
  – Market – size, competitive position, barriers to entry
  – IP – absolute necessity for some businesses (e.g. life sciences, medical devices), less important for others
  – Future capital needs

• Largest Influencer is the team
  – Early stage start-up with first time entrepreneur is a price taker
  – Experienced entrepreneurs often have more pricing power
Valuation - Considerations

• Pure Valuation (e.g. pre-money) is One Consideration

• More Important is Post Money Ownership Stake
  – Pre-Money is one component
  – Equally important is how much does one raise
  – Need at least 12 months plus some cushion and a sense of key milestones to be reached with the round

• To Maximize Ownership
  – Bootstrap as long as possible to demonstrate traction in the market
  – Look for non-dilutive sources of capital
  – Create demand for your deal
Valuation - Conclusion

• Valuation Methodology Varies with Stage

• Early Stage Valuation is Qualitative

• In the End, Valuation is Less Important than Finding the Right Investor
  – Compatible
  – Relevant Industry Experience
  – Deep Network that you can leverage