



THUNDERBIRD
SCHOOL OF GLOBAL MANAGEMENT

Financing the Venture

Russian Science Technology and Education Consortia (RUSTEC)

By

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Alternative Sources of Financing

Source of Financing	Length of Time		Cost				Control	
	Short-term	Long-term	Fixed Rate Debt	Floating Rate Debt	Percent of Profits	Equity	Covenants	Voting Rights
Self		X				X	X	X
Family and friends	X	X	X	X		X	X	X
Suppliers and trade credit	X				X			
Commercial Banks	X		X	X			X	
Private equity funds		X				X	X	X
Angels (private investors)		X		X		X	X	X
Venture capital		X	X			X	X	
Private equity placements						X	X	X
Public equity offerings					X	X		X
Government Programs		X						

Bank Loans

Bank Lending Decisions

- | | |
|--|---|
| <ul style="list-style-type: none">• Character• Capacity• Capital | <ul style="list-style-type: none">• Collateral• Conditions |
|--|---|

Types of Bank Loans

- | | |
|---|---|
| <ul style="list-style-type: none">• Accounts Receivable Loans• Equipment Loans• Inventory Loans• Real Estate Loans | <ul style="list-style-type: none">• Character Loans• Installment Loans• Long-term Loans• Straight Commercial Loans |
|---|---|

Private Equity Market (Enterprise Capital)

Individuals

- Individuals
- Angel Groups (networks)
- Angel Funds
- Family Offices
- Crowd Funding

Venture Capital Firms

- Private Venture Capital Firms
- Small-Business Investment Companies (SBIC)
- Industry Sponsored Venture Capital Firms
 - Banks and other financial institutions
 - Nonfinancial companies
- Geographically-Oriented Venture Capital Firms
- University Sponsored Venture Capital Firms

Private Equity Firms

- Limited Partners
- General Partners



Characteristics of Informal Investors

- Demographic Patterns and Relationship
 - Well-educated with many having graduate degrees
 - Will finance firms anywhere in the world
 - Most firms financed within one day's travel
 - Majority expect to play an active role in ventures financed
 - Have clusters of 9–12 other investors

Characteristics of Informal Investors *(cont.)*

- Investment Record
 - Range of investment: \$10,000–\$500,000
 - Average investment: \$175,000
 - One - two deals each year
 - Venture preference
 - Most financings in start-ups or ventures less than 5 years old
 - Most interest in financing:
 - Manufacturing—industrial/commercial products
 - Manufacturing—consumer products
 - Energy/natural resources
 - Services
 - Retail/wholesale trade

Characteristics of Informal Investors *(cont.)*

- Risk/Reward Expectations
 - Median 5-year capital gains of 10 times for start-ups
 - Median 5-year capital gains of 6 times for firms under one year old
 - Median 5-year capital gains of 5 times for firms 1–5 years old
 - Median 5-year capital gains of 3 times for established firms over 5 years old
- Reasons for Rejecting Proposals
 - Risk/return ratio not adequate
 - Inadequate management team
 - Not interested in proposed business area
 - Unable to agree on price
 - Principals not sufficiently committed
 - Unfamiliar with area of business

Types of Venture Capital Firms

Types of Venture Capital Firms

**Private
Venture
Capital Firms
(General
Partners and
Limited
Partners)**

**Small
Business
Investment
Company
(SBIC)**

Industry- Sponsored

- Banks and Other Financial Institutions
- Nonfinancial Companies

**Geographically
-Oriented**

**University-
Sponsored**



Venture Capitalists

- Evaluation Criterion
 - Strong management team
 - Unique opportunity
 - Appropriate return in terms of capital appreciation
- Evaluation Process
 - Initial screening
 - Initial agreement of terms
 - Due diligence (industry, market, players)
 - Go or no-go decisions
 - Document deal and close
 - Monitor deal

Venture Capitalists *(cont.)*

- Venture Portfolio Goal
 - 20% early stage—50–60% ROI
 - 40% development financing—40% ROI
 - 40% acquisitions and leverage buyouts—30% ROI
- Typical Venture Portfolio of 10 Deals
 - 4 belly-up
 - 3 walking wounded (or living dead)
 - 2 hits
 - 1 home run

Venture Capitalists *(cont.)*

- Factors in Pricing a Deal
 - Return
 - Amount of money needed now and later
 - Quality of deal
 - Quality of team
 - Amount entrepreneur is investing
 - Prospects of company in future
 - Upside potential
 - Downside potential
 - Form of investment—collateral
 - Liquidity
 - Exit avenues

Advantages and Disadvantages of Going Public

Advantages

- Obtaining capital with less dilution to founders
- Enhanced ability to borrow
- Enhanced ability to raise equity
- Liquidity and valuation
- Prestige
- Personal wealth

Disadvantages

- Expense
- Disclosure of information
- Pressures to maintain growth pattern
- Loss of control