SNS COLLEGE OF ENGINEERING

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DEPARTMENT OF MANAGEMENT STUDIES

COURSE NAME : FINANCIAL SOURCING MANAGEMENT

II YEAR /III SEMESTER

Unit 1 – Startup Valuation

Recall

❖ Business Plan
❖ Components of Business Plan

Topic

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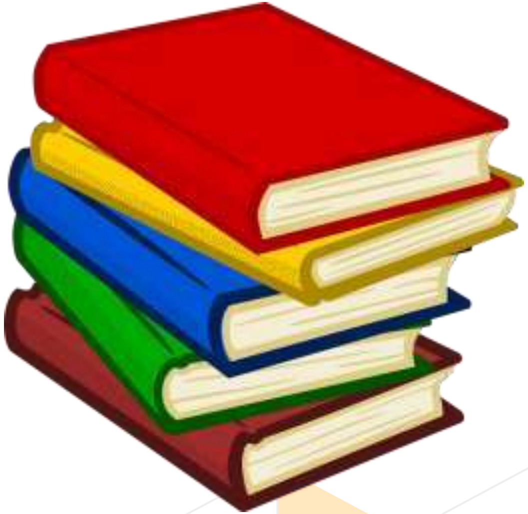
Lets Focus on

Start-up Valuation



Startup valuation

Startup valuation are the ways in which a startup business owner can work out the value of their company during the pre-revenue stage of their lifespan

Several startup valuation methods are available for use by financial analysts.

How much does it worth?

A startup have enough capital to fully develop its underlying idea or concept. A startup without money is destined to fail

You need money for marketing, office space, prototype development, to hire staff, for inventory and a dozen

Estimating the value of your startup is the only way you'll be able to pitch your idea to an investor whose first question will be: *How much does it worth?*

Methods of Startup Valuation

1. Venture Capital Method
2. Berkus Method
3. Cost-to-Duplicate Method
4. Discounted Cash Flow Model (DCF)
5. Comparables Method
6. Book Value Method

Venture Capital Method

A startup valuation that employs a forecasted terminal value for the startup and an expected return from the investor (often stated as 10X, 8X, and so on), to determine pre-money and post-money valuations.

Pre-Money Valuation = Post Money Valuation — Invested Capital

Let's say an investor values your startup at a terminal value of $1,000,000 and he wants a 20X return on his $10,000 investment. In this case, your Post-Money valuation would be $50,000. And, according to the Venture Capital Method, the Pre-Money Valuation would be:

Pre-Money = $50,000 — $10,000 = $40,000

Berkus Method

A straightforward method that values startups based on five key aspects.
Qualitative element to be considered
Sound Idea
Prototype
High-Quality Management Team
Strategic Relationships
Product Rollout or Sales Made **$500,000 each.**

For each feature the startup possesses in full, the valuation should go up by $500,000. Nevertheless, depending on the degree in which each element is developed the investor could reduce the value of the item to say $400,000 or $250,000, to determine the final value.

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Cost-to-Duplicate Method

This startup valuation main goal is to determine how much it would cost to start the same business from scratch.

The cost-to-duplicate method is a very realistic approach that puts into question the competitive advantages of a startup.

If the cost of duplicating the startup is very low, then its value will be next to nothing. In turn, if it is costly, then the value of the startup will increase as the difficulty increases.

Discounted Cash Flow Model (DCF)

A technical tool employed by financial analysts to determine the value of a business by estimating its future cash flows, discounting them at a certain discount rate to obtain their present value.

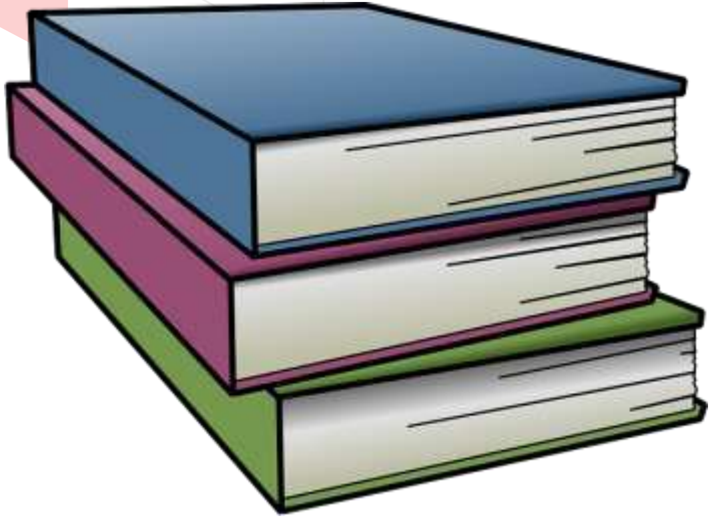
Given the fact that this method relies heavily on assumptions that require some historical data to be performed, it is not the most widely employed to value startups.

Comparables Method

This approach employs referential information and numbers from other similar transactions to estimate the value of a startup.

Let’s say that a similar app to the one developed by the startup was recently valued by a venture capital firm at $5,000,000 and the app had 100,000 active subscribers/users. This means that the company was valued at $50 per user. An investor could use this benchmark to value a startup with a similar app.

Book Value Method



This method is based solely on the net worth of the company. i.e. the tangible assets of the company. This doesn't take into account any form of growth or revenue, and is usually only applied when a startup is going out of business.

Right method for your stage

Each of these startup valuation models can be more useful for some stages than others and you need to determine in which stage you are in before you pick the method that is best suited for you. Here's a list of the three common stages of startups:

- **Seed Stage**
- **Round A Stage**
- **Round B Stage**

Seed stages

This is the earliest stages for any startups. At this point, there's usually no revenue, no assets, no team, no business. Just an idea and the willingness to move forward. At this point, the Berkus Method or even the Venture Capital Valuation Method may be the most recommended for you.

Round A Stage

Your startup is now a solid idea on the move. You probably have a prototype by now or you have already made some sales. At this point, you can rely on more technical methods such as the Cost-to-Duplicate method or yes, the Venture Capital Method again.

Round B Stage

At this point what you need is money to expand and continue growing. The business model is already proven and your revenue-generation potential can be assessed. These methods include the DCF Model.

Assessment

For each feature the startup possesses in full, the valuation should go up by $500,000. Nevertheless, depending on the degree in which each element is developed the investor could reduce the value of the item to say $400,000 or $250,000, to determine the final value.

.Explain this Method

Summary

These methods or frameworks is important because startup companies lack reliable past performance and predictable future performance that most established businesses use to estimate their value so having a way to guess a valuation.