



# Entrepreneurial Finance

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Giorgio Valentinuz

Contents refer to:

©2011, *Smith J.K., Smith R.L., Bliss R.T., Entrepreneurial Finance. Strategy, valuation & deal structure*; Stanford University Press

# Goals

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- The aim of the course is to present the concepts of applied corporate finance in a situation of launching a business, based on innovation. In this case, models and tools that are normally used for companies with a history behind (and often listed on stock markets) may not be applied in the same way
- The business plan is the document in which strategic decisions (regarding either assets side or liabilities side) are translated into financial figures useful for evaluation
- The theme of the evaluation of a private owned company is developed in practice from entrepreneurs' perspective so as investors' (private equity funds, business angels,...) perspective



# Learning Objectives

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- How new venture finance and corporate finance differ
- Which financing choices are feasible and why
- Tailoring the business plan to its purpose
- How real options relate decision trees to important milestones
- How milestones and real options relate to strategy and the value of an opportunity
- The basics of financial modeling and assessing the cash needs of a venture
- Value new venture opportunities using standard valuation methods
- The entrepreneur's point of view on value creation



# Contents

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- **Getting Started**
  - Introduction (Ch. 1)
  - New Venture Financing: Considerations and Choices (Ch. 2)
- **Financial Aspects of Strategic Planning**
  - New Venture Strategy and Real Options (Ch. 4)
  - Developing Business Strategy Using Simulation (Ch. 5)
- **Financial Forecasting and Assessing Financial Needs**
  - Methods of Financial Forecasting (Ch. 6)
  - Methods of Financial Forecasting: Integrated Financial Modeling (Ch. 7)
  - Assessing Financial Needs (Ch. 8)
- **Valuation**
  - Foundations of New Venture Valuation (Ch. 9)
  - Valuation in Practice (Ch. 10)
  - The Entrepreneur's Perspective on Value (Ch. 11)



# Learning materials

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- Smith Janet Kiholm, Smith Richard L., Bliss Richard T., *Entrepreneurial Finance. Strategy, valuation & deal structure*. Stanford Economics and Finance, Stanford University Press, 2011
- Lecturer's slides
- Cases on [www.sup.org/entrepreneurialfinance](http://www.sup.org/entrepreneurialfinance)



# Lessons and office schedule

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## Lessons

- Monday 16.00 – 19.00
- Tuesday 16.00 – 19.00

## Office hours

- Monday 15.00 – 16.00  
19.00 – 19.45
- Tuesday 15.00 – 16.00  
19.00 – 19.45



# Calendar

- Lessons  
From 29 September  
To 16 December
  - Lessons  
From 29 September  
To 16 December
  - Lessons  
From 29 September  
To 16 December
- Lessons
    - 29/09 2<sup>h</sup>
    - 30/09 3<sup>h</sup>
    - 06/10 3<sup>h</sup>
    - 07/10 3<sup>h</sup>
    - 13/10 3<sup>h</sup>
    - 14/10 3<sup>h</sup>
    - 20/10 3<sup>h</sup>
    - 21/10 3<sup>h</sup>
    - 27/10 3<sup>h</sup>
    - 28/10 3<sup>h</sup>
    - 04/11 3<sup>h</sup>
  - Lessons
    - 10/11 3<sup>h</sup>
    - 11/11 3<sup>h</sup>
    - 17/11 3<sup>h</sup>
    - 18/11 3<sup>h</sup>
    - 24/11 3<sup>h</sup>
    - 25/12 3<sup>h</sup>
    - 01/12 3<sup>h</sup>
    - 02/12 3<sup>h</sup>
    - 09/12 3<sup>h</sup>
    - 15/12 3<sup>h</sup>
    - 16/12 3<sup>h</sup>
- No lesson
    - 20/10 ???
    - 21/10 ???
    - 03/11 Holiday
    - 17/11 ???
    - 18/11 ???
    - 08/12 Holiday



# Exams

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- Winter session (from 07/01 to 13/02)
  - 07 / 01 / 2015
  - 26 / 01 / 2015
  - 09 / 02 / 2015
- Summer session (from 25/05 to 04/07)
  - 26 / 05 / 2015
  - 16 / 06 / 2015
  - 30 / 06 / 2015
  - 27 / 07 / 2015
- Autumn session (from 31/08 to 18/09)
  - 01 / 09 / 2015
  - 15 / 09 / 2015





# Exams

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- ORAL exam
- AVERAGE DURATION: around 20 minutes
- CONTENTS: all the program



# What you can find on the website?

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- End-of chapter questions and problems
- Interactive cases, including spreadsheets where useful
- Technical appendices
  - Reviews of basic statistics, time value, and option basics
  - Business plans and using integrated financial statements
- All figures from the book
  - Excel figures are downloadable as spreadsheets
  - Excel templates can be modified for other uses
- *Venture.SIM* simulation software can be downloaded
  - Includes a short tutorial that also covers some basic Excel
- Glossary of entrepreneurial finance terms
- A list of useful websites



# General lessons from corporate finance

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- Present value
- Opportunity cost of capital
- Market efficiency
- The “Law of one price”
- Portfolio theory
- Capital structure irrelevance
- Separation of financing and investment decisions
- Value additivity



## Where corporate finance ends – entrepreneurial finance begins

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- Investment and financing decisions are interdependent
- Ability to diversify risk affects investment value
- Outside investors may be actively involved in a venture
- Information (and beliefs) of parties are very different
- Incentives of parties are much different
- New ventures are portfolios of real options
- The importance of harvesting to realize a return
- Maximizing value for the entrepreneur is different from maximizing shareholder value



# Onesole Shoes Pitching

## OneSole - Shark Tank Business Plan Pitch Video

Watch the OneSole entrepreneur pitch her business plan to potential investors.



# Start up: a definition

(Italian Ministry for Economic Development)

- Sono detenute direttamente e almeno al 51% da persone fisiche, anche in termini di diritti di voto;
- Svolgono attività di impresa da non più di 48 mesi;
- Non hanno fatturato – ovvero hanno un fatturato, così come risultante dall'ultimo bilancio approvato, non superiore ai 5 milioni di euro;
- Non distribuiscono utili;
- Hanno quale oggetto sociale lo sviluppo di prodotti o servizi innovativi, ad alto valore tecnologico;
- Si avvalgono di una contabilità trasparente che non prevede l'uso di una cassa contanti, fatte salve le spese legate ai rimborsi



# Entrepreneurial finance

- It concerns financial decision making by entrepreneurs who are undertaking new ventures
- Joseph Schumpeter (1934) viewed the entrepreneur as actively seeking out opportunities to innovate. For him the entrepreneur is the driver of economic progress, continuously seeking to disturb the status quo in a quest for profits from deliberate and risky efforts to combine society's resources in valuable ways that are not yet perceived by others
- Peter Drucker (1985) describes entrepreneurs as individuals who “create something new, something different; they change or transmute values”



# Entrepreneurial finance

- Today, entrepreneurship is most often described as the research of opportunities to combine and redistribute resources, without regard to current ownership or control of those resources
- Innovation is very important but is not enough to guarantee a reward for the entrepreneur. To be successful, an entrepreneur needs to maintain a clear focus on how strategic choices and implementation decisions are likely to affect rewards
- “Good ideas and good products are a dime a dozen. Good execution and good management – in a word, good people – are rare” (Rock, 1992)





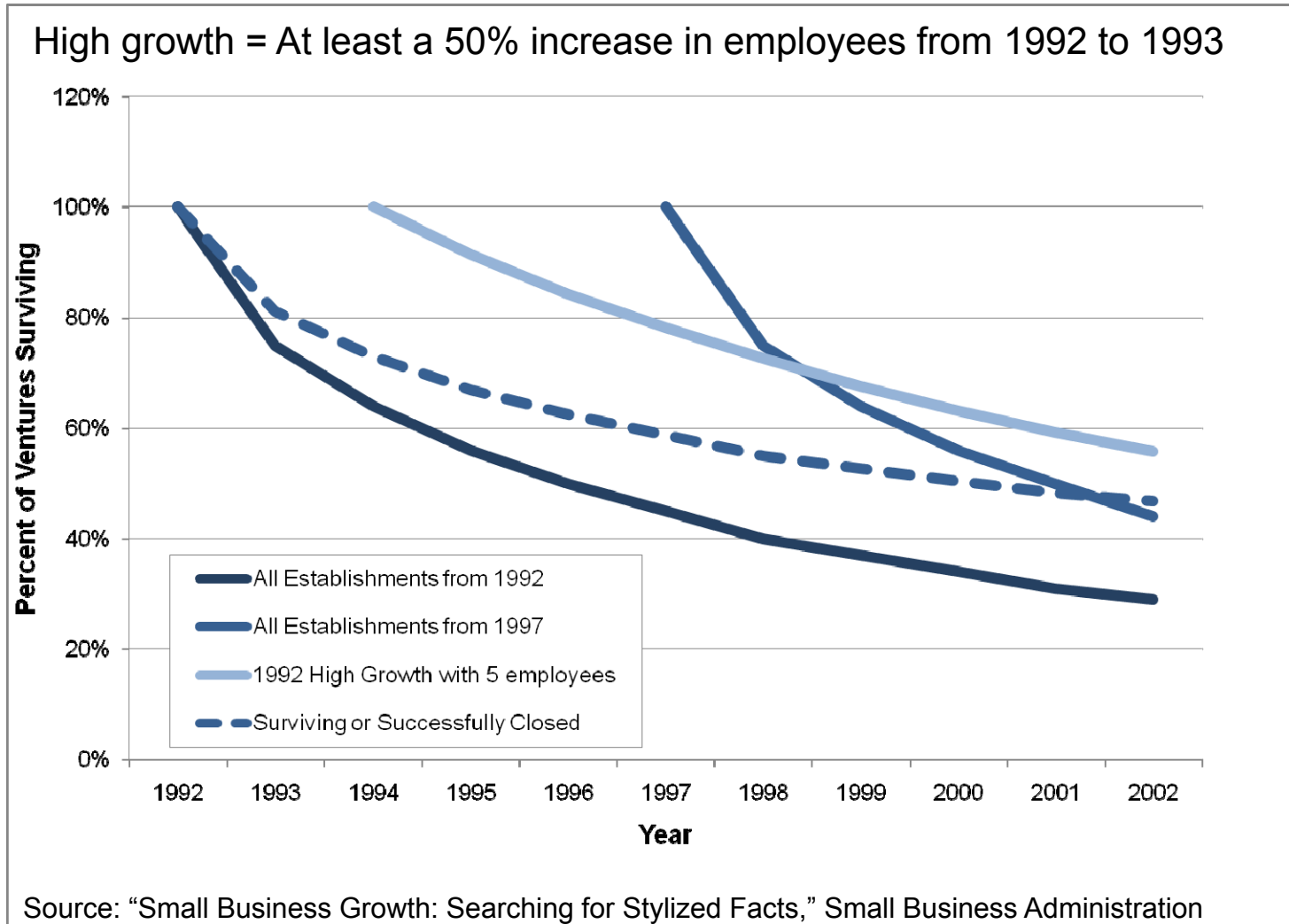
# Entrepreneurship is Multidimensional

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- The entrepreneur must:
  - perceive an opportunity to create value by redeploying society's resources
  - devise a strategy for marshaling control of necessary resources
  - implement a plan of action to cause the change
  - harvest the rewards that accrue from the innovation



# New venture survival rates



Source: "Small Business Growth: Searching for Stylized Facts," Small Business Administration Working Paper, 2007, prepared by Brian Headd and Bruce Kirchoff



# New venture survival rates

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- 50% of new ventures survive at least four years and 30% at least ten years
- “High growth” firms have a better survival record; 72% survive at least four years
- One-third of non-surviving entrepreneurs still considered their venture a success
- From 2000 to 2007 an average of 904.900 new business were created per year in the US. The average number of business terminations during the same period was 744.100 (around 83%)
- The number terminated with a financial loss to creditors via bankruptcy, however, is only 4,5% of all terminations

