SalesSeek

Raising Funds

A one-stop-shop guide to the intricacies of approaching investors, raising capital yourself and best practice to get your Startup off the ground financially

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Introduction

Fundraising for startups follows a typical three-step process:

1. The company is initially bootstrapped by the founders themselves and what is often cynically called “Friends, Fools, and Family” - a reference to the combination of high risk and naive investors that can often spell trouble.

2. Once the company has started to show signs of life, the next step is typically one or more Angel rounds. Again, the naming implies a certain lack of hardhead headedness in evaluating investments.

3. Finally, having demonstrated traction, a company can look to institutional venture capital funds (VC) to bring on board significant investment as well as access to a financial ecosystem.

Each step requires a lot of work from the Founders to be successful, and probably the most important thing to consider is where you are and how you should approach on this funding cycle.

Generally, anything pre-revenue will restrict you to Friends and Family. We’ll drop the pejorative “Fools”, but it should be remembered that whilst “getting in early” can lead to amazing multiples, it also implies amazing risks. Many friends and family are investing not on the basis of a clear-eyed assessment of the business model, but rather because they are friends and family. It is beholden on the founders not to abuse this trust.

Some Angels might be interested in this stage, but it’s more likely they would want to see evidence of revenue first. Angels might sound like altruistic guardians, but in fact, the majority are professional investors. Whilst they may lack the capital reserves of VC firms, they will still be scouting a breadth of opportunities and will be looking to maximize their return whilst minimizing their risk. It would be a mistake to think of them in any way as being “easier” than larger VC firms.

Angel and Friends and Family rounds are usually called ‘seed rounds’, but once a company has repeatable revenue with solid metrics, it could then be in a position to approach VC firms, who would typically expect to invest in 3-5 rounds, deploying $10-$50M of capital and expecting to see a return somewhere between a 5 and 10 year horizon.

This three-step approach can often be short-circuited by repeat entrepreneurs, who have already delivered a successful project to the VCs. But for most new entrepreneurs it’s not practical to raise funds initially from the VCs.

But before examining the mechanics of raising funds, we should first ask a more basic question - should you raise funds?


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Pros and Cons of Fundraising

Pros and Cons of Fundraising

Why take funding?

There are two reasons, one good, one bad. First, the *good* reason:

Capital makes you successful (sometimes). Think of your Startup like a bicycle gear wheel or an hi-fi amplifier - you put a small input in, and get a larger output. You can buy lemons for $1 and turn it into $10 worth of lemonade. So why not put in $10 of lemons and get $100 of lemonade - etc? Don't have $10? Then get it from someone else in return for a share of the business. Well, the reason this is not always the right idea is that in order to raise funds, you have to in effect sell part of your company. In doing that, **you don't only forgo some of the profits, you also cede some control.** It's not unheard of for VCs to replace the original founder - in which case you would see precisely 0% of all that lemonade.

» *Photo Credit: Unsplash*

The second point is that **depending on your market, capital can have a different multiplying effect.** Software, for example, is capital intensive as it takes people to build something first before it can be sold. **Hardware can be even more capital intensive for the same reason..**

Tesla and SpaceX would be two good examples where you can't really play without significant investment. **Conversely service businesses (think accountants and lawyers) need almost no capital** - you can hire someone and sell out their time the same day. Indeed, it's a great way to build a software company without external capital by starting out as a services vendor, and then productizing your solution.

Fundraising is unusual in that the less you need it, the more people want to give you. 'Bootstrapping' is the best option to minimize dilution (selling off part of the company), control (the VC is now your boss), and distraction (fundraising takes a *lot* of time). Against this though must be balanced the reality of how much capital your solution/market requires.

This brings up another aspect, which is **network effects and critical mass.** You might consider a couple of scenarios - taking external funding and getting 1M users in 2 years, or bootstrapping to get those 1M users in 4 years. In this case, you should get funding - because your competitor will. Simply put, you don't have 4 years. If your market can be accelerated by funding, then **you need to take funding because your competition will.**

You can summarise the above with the saying **"capital is a competitive edge".** How much so for you determines how much capital you should get. VCs would love a hypothetical pitch "the first company to pump $1B of free storage into the market will become worth $20B". This is more or less the Dropbox proposition. VCs love this because that $1B entrance fee kills most competition. When all you have is a hammer, all the world looks like nails. All VCs have is money.

So that then is the good reason - capital makes you successful (with some caveats).

But what about the *bad* reason?

Sadly, founders sometimes dive into fundraising without every really asking themselves if they need it, and sometimes use it as **a proxy for success.**

To sum up, it's worth having a clear idea as to the importance of capital in your business to decide whether or not to pursue funding. **Your own goals also come into this.** Having funding makes some things easier, but other things harder - the decision is seldom a "no-brainer".

Do you get rich if you raise funds?

No. The money is the property of the company, not you. No one is going to give you $2M without some form of governance, which is why the VC will be joining the board, so you can't blow $1.9M on a second-hand business jet.

You could expect a salary, although if you are talking about $2M for finding, I would expect the CEO to take **a modest rather than market amount** - almost certainly sub-$150K.

You may have heard of what happened to Secret. Here they raised a much larger round - $25M in fact, and as part of this made what is called a **secondary sale** - the founders sold some of their own stock in exchange for money, so rather than the money going into the company it went into their pockets **- $3M a piece.**

One of the founders splashed out some of his $3M to buy a Ferrari. **Secret subsequently went bust. Let's just say the optics of this aren't great.**

The fact he bought a Ferrari is really irrelevant, but it's the detail that catches the eye. I'm reminded of the scene in Goodfellas - *"Don't buy anything. Don't get anything. Nothing big. Didn't you hear what I said? You're going to get us all f***in' pinched, that's why. What are you, stupid?"*

This is from the NY Times:

> *"But the news had broken that David Byttow and Chrys Bader, the founders of Secret, had sold part of their stake in the company for $6 million and that Mr. Byttow later bought a Ferrari. The founders did not initially tell the employees about the sale; instead, some of them found out on Secret.*
>
> *Although Mr. Byttow and Mr. Bader reassured workers at the meeting that they were dedicated to the company, it was a turning point, said people close to Secret, who spoke on condition of anonymity. It shook the confidence of some workers, they said: If the founders had taken money off the table, it could mean they were protecting themselves against Secret's failing."*

» *Photo Credit: Flickr*

Personally, I would hold the investors responsible. Surely if the founders are selling, doesn't that tell you something? Founders have to live, so I'm all for realistic salaries to paid, but giving them **a big early exit does not align their interests with the investors.** At best they spend more time thinking about sports cars rather than focusing on growing the business. At worst, they've already made their exit in their minds.

Bootstrapping and a lean startup approach

Bootstrapping and a lean startup approach

The lean startup approach is well known, and it does a couple of things:

1. It helps **take the pressure off getting funded.** The leaner you are, the more you can bootstrap. Less pressure on you to get funded typically translates to a better valuation. You want funders chasing you, not vice versa.

2. The mentality of **being very careful with money is something all investors cherish.** They say "spend it like your own money", but they don't mean go out and buy a Ferrari. Ironically the only time I fly Business is on my own dime. Every business trip I take it's Economy. I am not spending money like my own. Airlines really should rename their classes...

There is though something else to consider. Funds rely upon your business being able to consume capital and make it bigger. VCs have zero interest in an investment proposal for 10K turning into 10M since 10M does not move the needle, even if a 100000% increase looks attractive. There are not enough 10K opportunities like this, and they would not have the bandwidth to manage them even if they did exist. They need to be able to deploy 10M over the life of the company and turn that into at least 100M and preferably 1B. **VCs need companies that need capital,** and that can sometimes play against the lean startup philosophy. You don't see too many services companies get funded because they can't deliver the return on capital, even if they can become very successful businesses in their own right, and one of the most effective ways to bootstrap a company.

This means certainly take a lean startup approach, but preferably with a capital intensive product offering with a large market opportunity. What they like are cheap employees who live like monks with a very expensive product to develop.

How to bootstrap

1. Does your product/ market lend itself to bootstrapping?

There are a number of elements, but the first and most important one is, **"does your product/market lend itself to bootstrapping?"** Here is a counter-example - DropBox. Their business model is freemium - basically giving away free storage in order to compete with Google, Microsoft and Amazon. But someone has to pay for all that "free" storage. In Dropbox's case, this is their investors - to the tune of more than $1B. If you want to play in the "consumer cloud storage" market I would argue that then pretty much rules out bootstrapping, unless you are clever enough to figure out a way around this. But for many products and markets, cash is a competitive advantage - it's fundamentally why VCs exist.

More specifically, you need a business with a high gross profit - i.e. every transaction delivers profit, and delivers profit quickly. But one common mistake is to think only about profit. Surely a business that can extract 10% profit from each sale is better than one that can only extract 5%? Actually not if the second business can process more transactions. A business that can process 3 transactions at 5% profit in one day is better than a business that can only process 1 transaction at 10% profit.

2. Cashflow is king.

Cashflow is king. A good example of this is to use services/consulting revenue to help fund product development. This particular works well for Enterprise software companies - Tibco is one example that started out this way.

3. Team - can they work for no salary, instead taking stock?

The third major element is Team - **can they work for no salary,** instead taking stock? There are usually three types of people who can do this: 1/ students, who haven't yet learnt to spend money, 2/ part-timers, 3/ mid-life folks who have a cushion to support them. Obviously, "no salary" can mean "minimal salary" too. This is going to put more stress on the team (but more focus too), and so it will be even more important that all the team gets along. It can be hard to blend part-timers with full-timers too, but here's a test - can you get your first customer before you leave your day job? You should if at all possible.

4. No Investment.

The fourth point is **no investment.** This sounds a little counter-intuitive, so let me explain. By "investment" I mean some form of up-front expenditure, where the benefit is delayed into the future and has a certain risk associated with it. When bootstrapping you can't afford either delay or risk. We all hear stories of entrepreneurs mortgaging their house, and dark days when they just scraped payroll, but it is survivors' bias that we never hear the stories of loss, divorce, and suicide. Running a startup is the same as visiting the casino. Never, never, never, never, stake more than you can afford to lose. Don't fall for siren calls from investors saying how much they love their founders to have skin in the game and demonstrate commitment. They won't be the ones looking for a park bench to sleep on. They themselves explicitly play a portfolio game that expects the majority to lose.

Practically speaking, what does "no investment" mean? It means spending the minimum to show progress, to make a proof point. Here's an example. Everyone talks about MVP (Minimum Viable Product). I love Reid Hoffman's quote that "if you are not embarrassed by your MVP, then you shipped too late". This is true for all companies, however funded, but it's 10x true for bootstrapped companies. For me, the MVP should be built in powerpoint. Can I make a sale just on that? If not, why not? What would it take? If you think this is impossible - think again - all services contracts, for example, are fundamentally based on presentations. Always remember the adage "perfection is achieved not when there is nothing left to add, but when there is nothing less to be taken away". Break everything down into the smallest unit possible - make it work - recalibrate - try to get *some* revenue for this - continue.

5. Cut your expenses.

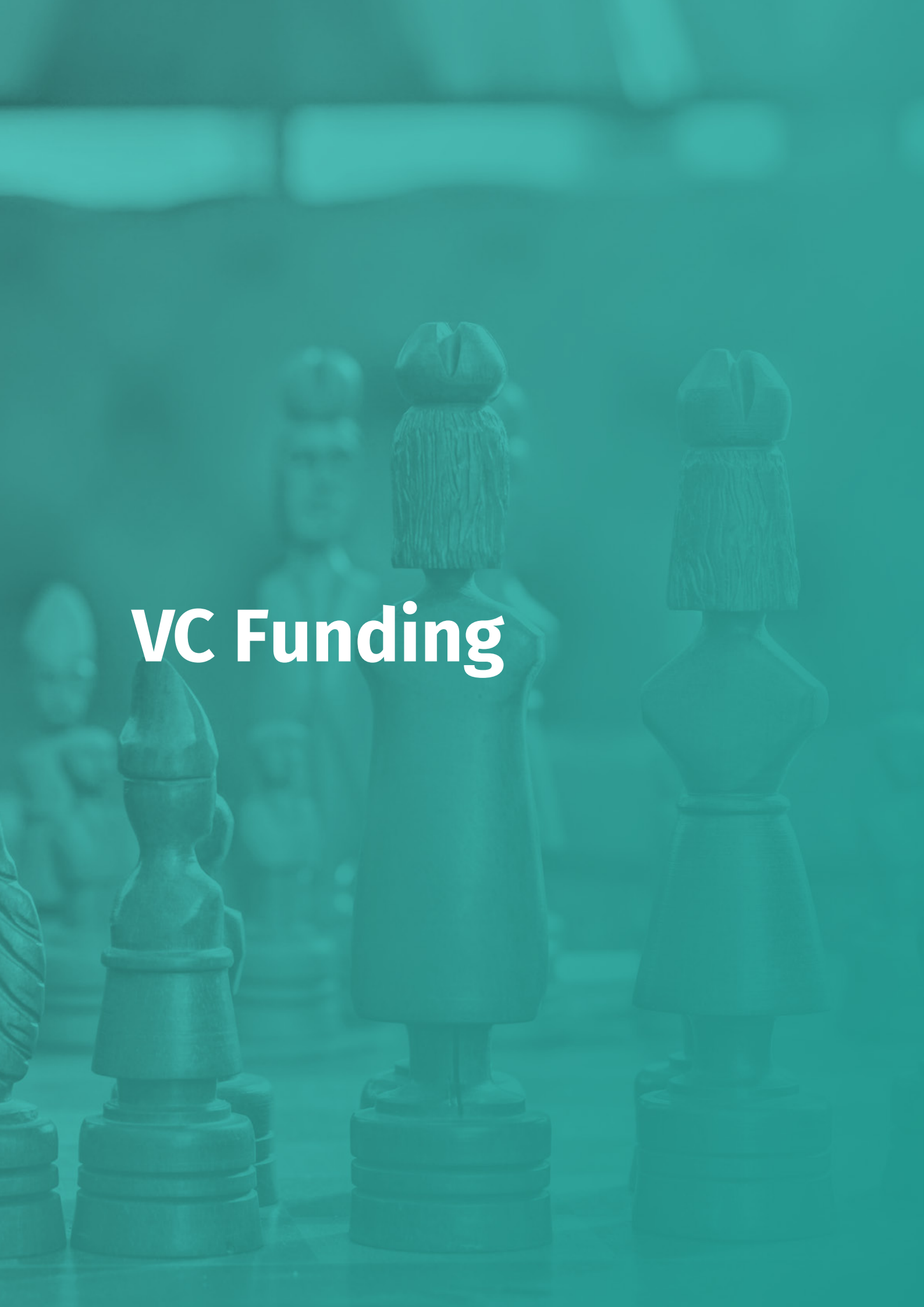
The final point is the obvious one - **cut your expenses.** Make do with second-hand. At SalesSeek we don't rent equipment for shows, we bought

our own kit (new, since it's a false economy to buy second hand computer kit with Moore's law), packed into second-hand Pelican cases bought for a fraction of the price. Always look everywhere how to save money. Do you need an office or just an address? Can you get an accountant to work for you on the cheap? Do you really want to spend $10K on that URL? Or do you think a silly made-up name like "Google" might work just as well for you?

This all sounds like hard work. And it is.

But it would be wrong to think to go the VC route is plain sailing either. You spend hours driving around Palo Alto and it's environs presenting to folks glued to their smartphones. Once you have investment you'll spend hours in interminable board meetings bringing them up to speed only. And finally, they will cut you with as much grace as a football club if you don't perform to the expectations built into the model. If you started up a business "to be your own boss", this is not it.

There is no "best way", but there may be an optimum route for you as a founder, and your product/market.



VC Funding

VC Funding

Traditionally VC funding has been issued in a number of groups - series A, B, C etc. I think series E is the highest level I've seen - by this stage the company has either successfully exited or failed. I don't think many people would want to invest in series F.

Prior to institutional funding, there will be a series of rounds. Friends and Family (although I think you should never take this), Angels/Seed. The reason I say never take friends and family is that they cannot afford to lose the money, which is the only sensible basis to invest in a startup. It's OK to risk your own livelihood, but not others.

One question you might have is why do VCs break funding into various rounds, rather than giving a company all they would need at the beginning to get to exit?

The answer is that companies want to raise money at the best valuation. The younger the company, the weaker the valuation, so you really want to borrow the "minimum". On the other side, VCs are fundamentally a portfolio business and want to spread risk. Rather than commit a large amount of capital at the beginning, when the risk of the company is high, they prefer to spread the risk over time (since they always have the option of not participating in further funding). So both the startup and the VC want to put in the minimum.

In an ideal world, you'd raise money every week, but that is clearly impractical given the overhead of raising finance, which typically takes 3-6 months. Practically speaking most people try to fund for at least 12, preferably 24, and often 36 months runway. There is another dynamic, which is VCs also don't want to give young companies too much money all at once as it tends to get wasted.

"Every time you take funding, you lost some % of the company."

Every time you take funding, you lost some % of the company. This affects control and also affects the value of your stock holding, as you have less stock. For example, let's imagine you invest in a pre-series A for $200K and get 10% of stock for that. Next, the company takes $4M in funding for series A in exchange for 50% of the company (a not untypical situation), the existing investors will have their shareholdings halved. So the original investment of 200K for 10%, means I now only have 5%. BUT the value of the shares post-funding would be $8M ($4M pre + $4M funding), which means they are worth 5% of 8M, or $400K -2x what was originally paid for the shares. This is an example of non-dilutive funding. "Dilutive" refers to the valuation, not the percentage (which always dilutes). Conversely, there could instead be a funding event of $2M in return for 66% of the

company. This would value the originally invested $200K at just $100K, half what was paid, and so a dilutive event.

Everyone is working to an exit, but the best way to get an exit is to not try. Focus on customers, revenue, growth, building a team, and keeping costs under control (in that order). Offers may or may not come, and they may or may not be worth considering. Bear in mind that acquiring companies will review twenty before acquiring one, so don't get your hopes up, and qualify them hard, since they may just be tire kicking.

If an exit does come, a number of things may come to light. In the VC funding, their shares will almost certainly have a liquidation preference, which means they at least get their money back (or some multiple) before the rest is shared out. This doesn't matter if you're successful, but in the event of a stalling company exiting for acquihire it's possible for the VC to walk away whole, and the initial investors with literally nothing. Avoid this type of exit.

The other aspect of an early exit is that is will be largely predicated on the strength of the team as opposed to the actual business. So the acquirer will want to lock in key team members by making the buy-out conditional on their employment over time. In other words, you don't get $10M now, but you get $10M earned out over 12-24 months (so if you leave half way through, you only get half the value).

Many early exits are distressed to some extent, regardless of how they are spun. StackMob got acquired by PayPal in 2013, who promptly shut the system down, after this rather more positive initial Page on readwrite.com

Recently we've seen a lot of very high valuations of unicorns, where the original investors have sold some of their own shares privately in a late stage round. This is almost always a much better deal for the sellers than the incoming investors.

Why would anyone want to sell pre-IPO shares in a hot high growth company? Exactly.

All Investors are not equal. How term sheets affect pricing

Various investor protections are becoming ever more common, as Square's IPO S-1 prospectus shows. There are several mechanisms that can come into play.

If you think about it, it's actually illogical. In principle the price should contain ALL the information there is about the value and risk of an enterprise. So rather than invest in a company at $10 with protections, it would be simpler to invest at $8 without any special protection?

The origin of this and the original form of protection was the **liquidation preference.** Insisted upon by VCs as a red-line, it means that a VC putting

in, say $5M at a pre of $10M, would get 33% of the shares, but in the event of any liquidation would first take out their original investment, then share the rest (sometimes they even claim a multiple of their original investment). The picture the VCs paint is one of two scenarios:

1. **Things go belly up.** No one gets anything.

2. **Things explode.** The company is sold for $200M, No one cares about the preference - it's a rounding error and we're all too rich to notice.

Of course, if that was all there is to it, then why do VCs care so much about it? Because in reality a very likely outcome is:

3. **Distress sale.** Some form of acquihire or asset sale. Here the company is sold for $5M . The original investors own 66% of the company, so it's not the end of the world. Maybe they get at least some of their money back? The founder's remortgage is still safe? NO. With a liquidation preference, the VC takes the first $5M - i.e. ALL of it! They get 100% of their money back and everyone else is left out in the cold.

The startup mantra is "death or glory", so no one wants to talk about the most likely outcome of simply returning injured. It's why it makes sense to co-invest with later VC rounds as you gain the value of the protections. Essentially **the terms are a form of non-transparent pricing.**

We've now started to see a **technical variation on the liquidation preference, which is a ratchet based on a future IPO price.** In this model, I invest at a price of $20, but if you IPO at less than, say, $25, then I get additional shares to make my profit still good. But those shares essentially dilute all the non-rachet holders.

Larger and larger pre-IPO rounds have pushed and been pulled by this. A lot of the recent Unicorn inflation is driven by a "don't bother about the risk, you're protected". To some extent, yes, but **this insurance is being paid for by the earlier investors.**

» *Photo Credit: Flickr*

How big of a problem is this? Some interesting research by Fenwick and West:

1. The **value of these preferential terms was an average of 33%** of the headline price.

2. In 2015, **50% of IPOs triggered these ratchets**, compared to only 4% in 2014.

Despite this, the cost to earlier shareholders so far has been minimal, but with everyone expecting a **substantial Unicorn reset this year,** the reality is that almost all of **this reset will fall upon the shoulders of the earlier investors**, and the late stage folks will be materially better off. That might cause a **backlash** to the popularity of these terms.

Cramming down the original Angels/early stage investors (founders almost always get additional stock granted, to large extent neutralizing the effect for them) sounds clever if you are the one doing the cramming, but too much of this risks putting the whole seed capital market at risk, and that helps no one.

Appealing to Investors

Appealing to Investors

What are investors looking for in a startup CEO?

Here are the five qualities I look for. I think a startup CEO needs passing grades in all of them.

1. Belief

Is there any shred of doubt in their mind they will succeed? If so, then pass. This is not a game for the faint-hearted.

2. Enthusiasm

A startup is not just for Christmas. This is a long haul. Do they have the emotional energy? Is their enthusiasm infectious? Do you come away from meeting with them with a smile on your face? Are they crazy enough to actually make this work?

3. Judgement

Everyone says ideas are nothing and execution is everything. Execution means making the right decision probably something like 20 times a day for 5 years or more. That's a tall order.

4. Trust

OK, so you're about to write a check for several million to this person - they are not going to run off with it are they?

5. Domain Expertise

There seems to be a common thread with a lot of recent high-profile startup failures where a "business" CEO ran what was a highly technical company. To give a counterexample, SalesForce has been successful at least in part because Marc Benioff is an extremely effective salesperson. Who better to run a sales software company?

I would argue all the traditional "MBA" qualities of leadership, interpersonal skills, organisational ability, analytical skills etc come a poor second to those above. It's not to say they are not useful, but primarily the purpose of a startup CEO is to get stuff done against seemingly insurmountable obstacles, and this is not really how the MBA crowd look at the world.

Startup CEO's don't just do their best. They do what it takes.

How do investors evaluate opportunities?

In my opinion, they are 35% interested in the market opportunity and 65% in the person who is going to make it happen.

» *Investors are 35% interested in the market opportunity and 65% in the person who is going to make it happen. Photo Credit : Flickr*

The market opportunity is partly the idea, but is mainly about market size, competitive dynamic, and the strength of your product in this sector.

The reason they are so focused on you as the principal is that the VC model is basically about hiring someone to go after a market. There is no point sweating about the details like a team, product, or value proposition since all of these *can* change, and in the typical startup all of these **do** change.

Changing a CEO means 5% of the company minimum plus a lot of disruption, so they would much rather get someone they think can do the the job from the start. Also there is the small matter of trusting someone not to run off/waste the money they give them.

Because no one has any idea which companies will succeed, VCs run a portfolio model where they bet on 20, expecting 1 or 2 to hit it out of the park to deliver high average returns.

Some VCs are more successful than others, but overall the basics of the model:

1. **Size of market opportunity**
2. **Strength of CEO**
3. **Spread of portfolio**

has proven to be an incredibly successful one. Angels often fall down on but can make a living if their own domain expertise helps them understand better. Many investors target certain sectors to leverage their expertise. Some funds/investors focus on cleantech. Others invest in alumni from certain universities, others invest in certain geospheres. This tends to be somewhat binary (either your business qualifies or not) depending on the structure of the fund.

4. **The Best**

Look at this from the Investor's perspective. They have limited amounts of both time and money, and so naturally pick "the best" investment from the ones on offer. They can't fund them all, even if they all "deserve" to be funded. Entrepreneurs sometimes look at their own business in absolute terms, but Investors are looking at in relative terms - it's basically a competition.

Things like detailed value proposition, team, IP etc are all important, but secondary to the above four points.

Those are the objective criteria, but in reality, it comes down to this:

Can you paint a compelling and credible picture of success. Do people's jaw drop when they see the demo? Do they send you emails at 3am the morning after your presentation as their brain has been working overtime on the potential your company has? Can you excite people?

How many advisors?

Rather than thinking of them as advisors, instead look at them as part-time workers. Maybe only an hour a week, but presumably adding value for that. With that in mind, key criteria are:

1. **What does the advisor do?** (e.g. PR advice).

2. **How do you engage the advisor?** Does your VP Marketing call her up directly? Do they come through you first?

3. **What is the time commitment?** Can they actually meet with a journalist and brief them on your behalf, or can they just set up the meeting? Or not even that, simply share their Rolodex?

4. **Is there any accountability or responsibility for this role?** Making a decision is easy when you don't have to suffer the consequences. Can we fire them if we don't get any PR?

A really bad way to look at an advisor is merely a "smart friend". Start-ups are a team, and you need people on the pitch moving the ball forwards. Fans shouting words of advice from the sidelines doesn't cut it.

There should always be concrete value, and this requires management effort to nurture and leverage. An important question would be "so how many of these remote, part-time, ill-defined staff can I manage?" The answer, of course, will be specific to your situation, but my intuition is that it's towards the 1-3 end of the scale, and anything above 5 looks odd.

I don't think there is any lower limit. Zero is a great number to have. Of course, this doesn't mean you don't take advice or seek it - just that you have not needed to formalise an advisor relationship - that's actually a plus.

What I would not do is to try and artificially boost the numbers of advisors thinking it makes your company look bigger or more important. I think very few investors are impressed with a list of advisors. People lend their names cheaply.

Advisors for fund raising

Whilst it's tempting to use paid advisors, and there is no shortage of people offering up their services, in reality, it makes little sense:

1. The entrepreneur is the domain expert. Whatever it is you're building, then your startup team know should know more about this (or at least have the confidence to think they know more about this) than anyone else.

2. Many startups work with **mentors and advisors.** These tend to be more experienced players in the same space as the startup. They can offer both advice and also intros to potential customers and investors.

Typically they'll do this for a modest equity stake (sub 1%) without salary. They may in some cases become board members too, but it's wise to keep the board as light as possible in the early days to avoid complications.

3. As soon as you start with external funding, a large part of the value proposition from the investor side is "**smart money**". Angels typically concentrate their investments in some narrow areas they have direct experience of. This is their edge, and of course, if they invest in you, then it's in their interests to help you as much as possible. Likewise, if you take VC money, you will gain access to some very experienced people as well as a broad network. It's usual for them to invite portfolio companies to help each other with some free "consulting" now and then - usually just a show and tell hour-long meeting, but valuable nevertheless to gain an outside perspective.

4. Google it. Or more precisely **Quora** it (not sure if that is a verb yet..). Here are some to get you started relevant to your questions about business plans etc.

All of the above differ from using a startup consultant in that they are all **long term relationships** and all lead to the internalisation of that knowledge inside your company building value.

I would countenance against hiring anyone "to arrange funding" for a fee as it's not necessary. You will need to be able to create and maintain a business plan, and manage forecasts as a core skill. It's not that hard - what's difficult in coming up with credible input numbers, and consultants can't help with that.

At later stages it may make sense to bring in specialist consultants to look at parts of the business, but generally, the principle is the same - if the work is important to the business, then it needs to be internalized.

Planning Fundraising

Planning Fundraising

Preparing for funding

To move things forward there are three things you need to do, none of which take funding:

1. **Technical Validation.** Can this thing actually be built? You say you are a self-taught programmer. That's fine, many people are. Can you do this yourself? If you can't then you need to rethink. Very few people would invest in a technically focused startup without a technical co-founder - you simply cannot outsource that for any amount of money.

2. **Market Validation.** At SalesSeek, we produced a short slide deck we circulated to 15 CEO's and VP Sales/Marketing (our target buyer) and asked them what they thought. You can do this yourself.

3. **Resource Plan.** People and money. How far can you get by yourself? Can you bootstrap part of this? The more you can do without external funding the better. What is a credible growth plan? All the time you are reducing risk, and making your company much more attractive to investors.

If you find yourself spending all day responding to orders and can't cope with customer demand, somehow the investors will find you...

When to raise and how much

"Raising money is hard work and a distraction for founders, so you don't want to be doing it constantly."

The **tradeoff is between money now at a low valuation, versus taking smaller amounts of money spread out at (hopefully) higher valuations**. Raising money is hard work and a distraction for founders, so you don't want to be doing it constantly. A funding round can take 3-6 months to close. So **12 months is really the minimum** you would want to plan for.

Conversely, you don't want to scoop up 5 years worth of funding all in one go now, since this will be at today's valuation. It makes more sense to raise half now, and half again at a higher valuation in the future. Practically speaking, **something like 2 years would be the maximum** you want to raise for. Because after 2 years, you ought to have increased the value of the company sufficiently that it doesn't make sense to raise more right now.

There is also another dynamic, which is that investors don't like to give too much money all at once to young companies as it tends to get spent too easily.

However, I think a better way to think about this is in terms of **key milestones.** Prior to profitability there are some :

KEY MILESTONES - PRIOR TO PROFITABILITY:

1. Minimum viable Product
2. First customer
3. Market validation (i.e. plurality of customers sufficient to say you have something)
4. Repeatable business model (i.e we spend X on lead gen and get Y revenue, like clockwork)
5. Profit

Each milestone successfully passed adds value to the company. Profit is but one of these, and if there is one thing I can confidently predict, it's that **you will be taking longer than your 2-year plan** to achieve that.

Instead, I would break this down to something more like "when can we get to First Customer", and try to fund for that (plus 50-100%). Remember VCs *need* follow-on funding in order to deploy their capital. I would not make profitability an explicit goal as it's too binary. Better make it something like "market validation" where you can paint a story and give yourself some wiggle room. Also, if profitability constrains your growth, in fact, you don't *want* early profitability - you should be concentrating on market share growth.

"Each milestone successfully passed adds value to the company."

The final point is that **everything has a value - even money.** So if the market is frothy and everyone wants in (e.g. 2014), then indulge them and help them lighten their wallets a little more by taking more funding than maybe you need. When money is cheap buy it. This gives you flexibility also to ride out contractions (e.g. 2016).

Should you pitch before or after you've built an MVP (minimum viable product)?

It depends on what your startup is attempting. You can think of two main types of risk with any new idea - 1/ technical risk: can this thing be built? 2/ market risk: will anyone buy it?

Any significant technical risk needs to be mitigated with at least a prototype. If you're proposing a cure for cancer, a pitch which went "we've got great people, and with your investment we're sure we'll find a cure" may not work well without a prototype demonstration of someone actually getting better. Conversely, if you're proposing a new way of consumer shopping, some market validation might be in order.

The majority of startups typically hold more market risk than technical risk, so the question is about getting market validation prior to a product. The trick here is Powerpoint - in the 90's it was a standing joke that Oracle always ran best on its primary platform - Powerpoint. Create a presentation and **get as much feedback from the market as possible.** You will no doubt learn a lot in this process too in terms of what your MVP (Minimum Viable Product) should be.

» *Photo Credit : Unsplash*

It's worth looking at this from the Angel's perspective - they have a (probably limited) choice of investment opportunities, including of course the ever-present "do nothing". You are basically in a competition with those other opportunities, so how much you need to show is dependent to some extent on how they look. It's worth investigating an Angel's existing investments and seeing how you stack up against them.

If the other opportunities have working prototypes and/or early revenue traction, then unless you can do likewise, you have a hurdle to overcome. If your value proposition and team are strong enough, and both technical and market risk are minimal, then it can certainly be done (indeed SalesSeek was initially funded like this), but obviously, everyone is trying to minimise risk. This will most clearly be seen not only in the invest/pass decision, but also in the valuation you get.

Fundraising Timeline

Here s a typical example of an initial fund raise with FFF followed by another seed stage institutional round.

FFF (Friends, Fools, and Family):

As an aside, I think it's worth stressing that "friends and family" investors are as a matter of principle a bad idea. What you should aim for are "professional acquaintance" investors who know your reputations, the market opportunity, and have a mature assessment of risk. They are actually more like Angels in that respect, albeit very tightly focussed on individuals/markets they personally know. That's not to say you cannot also count them as friends, just that that is not the basis for the investment.

For the first investment, all of these individuals should be aware of and track the whole initial company setup and conception. You could argue they are distant co-founders. You can use them heavily for advice in the design of the product and for validation of the value proposition.

Because of that, it's very difficult to allocate out specific time over and above what you would be doing anyway. In aggregate the time ou take from initial scope (a presentation circulated with the outline value proposition) to company formation might be some 3 months. In this period though, the activity is probably 50% for the founders.

I think the key here for FFF is to treat your initial investors not as investors per se, but as co-founders - let them see everything, warts and all. Prepare nothing "special" for them. In truth you are looking for people to say no, not yes, since that is far more valuable counsel. Their advice is key - the investment is really about binding them in.

Seed Stage:

This would be your first institutional funding from a VC focusing on early stage investments.

» *Photo Credit: Unsplash*

1. Investor Funnel. Create a shortlist of potential investors. Try to leverage any personal contacts you have and so easy to identify. Qualify aggressively on their ability to engage with a seed stage investment and also for competitive investments in their portfolio. You may find this knocks out quite a few. This will remain an ongoing activity.

2. Pitch Deck. You should already have slide sets covering most of this, so it only should take probably 2-3 man days effort, spread out over a couple of weeks to hone and tune. A bigger task is the financial model (5-year plan), but again since you should already have this, it will probably similarly be a 2-3 man day effort spread out over a couple of weeks. Again this is an ongoing task as you refine the value proposition.

3. Investor Meetings. A lot depends on locale. Silicon Valley is the obvious choice, but consider other places if you are looking for very modest amounts of capital so were able to satisfy this purely with regional based VC. There is a real advantage in having partners live just 10 minutes away from the office. This means any meeting time is just that with practically no travel time/expense to worry about. It's this dynamic that makes it worthwhile to be based in centers of VC activity such as London and (obviously even more so), the Bay Area. You will probably have to kiss a lot of frogs before finding your prince - 20-30 is not unusual, and many established juggernauts like SalesForce suffered early rejection from VCs. It's exactly the same reason and dynamic that J.K. Rowlings' Harry Potter manuscript was rejected.

Getting to term sheet stage probably will involve something like 4-6 hour long meetings over a one month period. Term negotiation should be rapid since there are a set of established norms that most VCs abide by, and unless you find yourself in a bidding war, you may not have much choice anyway.

4. Due Diligence. The big difference between institutional and FFF. Honestly, I tear my hair out over this. If at all possible get the lawyers to accept a shared document repository like Google Drive. The last thing you want is to have to print out every single open source license in full so that the lawyers can make a big binder. I don't know what they think they achieve with 50 copies of the MIT license - ultimately they still have to take your word for it that they are the right licenses... In a similar vein, try to get the lawyers to accept electronic signatures. Insisting on a (print-sign-fax) x (chase multiple times) will both prematurely age you and add weeks to the deal closing.

» *Photo Credit: Flickr*

This can take 4-6 weeks in elapsed and is probably a 50% load for the CEO, as well as requiring resource from your Head of Engineering and other individuals to pull together all manner of paperwork. This will be the biggest time sink for you. However, a lot of it can carry forward, so next time this should not be so time-consuming.

One final detail that might surprise you. Your startup will be footing the bill for their lawyers. And whilst you've been parsimonious using your brother-in-law, the VC's lawyers will be top drawer firms charging $10-25K and beyond. This grates, especially when you examine the lawyers' actual "value-add", but you just have to take a sharp intake of breath and move on...Because of that, it's very difficult to allocate out specific time over and above what you would be doing anyway. In aggregate, the time you take from initial scope (a presentation circulated with the outline value proposition) to company formation might be some 3 months. In this period, though, the activity is probably 50% for the founders.

I think the key here for FFF is to treat your initial investors, not as investors per se, but as co-founders - let them see everything, warts and all. Prepare nothing "special" for them. In truth, you are looking for people to say no, not yes since that is far more valuable counsel. Their advice is key - the investment is really about binding them in.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Getting Funding

Getting Funding

Setting Up Investor Meetings

If you can network into a VC, that's useful, but from all of my interactions, VCs absolutely do seriously look at all unsolicited pitches that come in. Many VC firms have submission forms on their websites for this very purpose. The pitch does have to work unaccompanied that does require marketing, presentation, and writing skills you may not have. Get help for that.

> *"A more important consideration is approaching the right VC, and within that, the right partner."*

A more important consideration is approaching the *right VC*, and within that, the right partner. I think you are far better off approaching a stranger investor who has complementary investments rather than one you know but has other interests.

The other angle is that truthfully you don't want meetings with VCs just for the sake of it. Considering how busy they are, it never ceases to surprise me how many meetings they take. Actually, it doesn't surprise me since what they are doing is gathering market intel. Even if they have no plan to invest in IdeaX, it's worth 30 minutes of their time finding out about ideaX if it's in some way related to their investment interests. You need to qualify out of these. Your problem is not getting a meeting with a VC, but rather getting funding.

Valuation

Typically at an early stage, there are no operating metrics to speak of, so *it all comes down to the story*. As a rule of thumb, you want to put together a credible business plan that within 5 years gets you to an MRR of something like $1.5M, which at a rough valuation metric of 60 MRR gets you to a magic figure of $100M. More/faster is better. However, probably more important than run-rate is growth rate. That is what will excite investors at all stages more than absolute revenues.

At an early stage there are three main things investors will look to in order to make a judgement:

1. **Market Opportunity.** What is your (credible) TAM (Total Addressable Market)? More is better. $1B is probably the entry level. How compelling is your value proposition? Do jaws drop when they see the demo? How big could this thing get?

2 **CEO/ Founding team quality.** The CEO is important as replacing a CEO can easily cost 5% of equity to attract a new one. And there is the little matter of can you trust this person with $1M+ cash. Investors can't monitor every little piece of their investment, so it comes down to them putting their trust in a CEO. The rest of the team is important for sure, but ultimately it is all about the CEO.

3 **Early traction.** Is it hot? Is social media screaming about this? Are downloads off the chart? Has the website gone offline due to the volume of traffic? Revenue is preferred, but in the absence of that, anything that shouts "hockey stick" is what people are looking for.

So how does all that emotion and hand-waving get translated into a valuation? One word: market.

Investors have a choice of investments, so they will weigh you against the other options they have available. Generally, even a small piece of the winner is worth a much bigger piece of a 2nd place company. This acts to drive up company valuations for the hottest at the expense of the also-rans. It's important to realise this is a competition, not an absolute value judgement. The reason Uber gets such an astronomical valuation is that it's the hottest ticket in town with lots of money chasing it - supply and demand.

» *Photo Credit : Flickr*

Since it is all about supply and demand, the best thing a company can do to increase its valuation is to make sure there is indeed a market with multiple investors to help set a reasonable price. You may not have that luxury, but it's definitely worth aiming for.

The final thought on valuation is that it may bounce back on you if you extract a really high valuation at an early stage. If indeed you can't fulfil expectations, you may be looking at future down rounds which bring their own complications. Better to leave a little fat on the table, and look to increase your valuation steadily with the rounds.

Workers, yes(even if part-time). Investors, yes. Advisors, no.

THE PITCH

There are many approaches, but all ultimately need to cover the same set of information. My own "formula" is:

1. Summary
2. Value Proposition: Problem
3. Value Proposition: Solution
4. Value Proposition: Competition
5. Market Opportunity: Size
6. Market Opportunity: Positioning
7. Market Opportunity: Go-To-Market (inc. Pricing)
8. Plan: Team
9. Plan: 3-5 year projections
10. Plan: Timeline (inc. close)

Ten sections doesn't mean only 10 slides, but you would not want to go above 20 slides.

In terms of the more specific question about market size and growth rates, this is difficult. The truth is no one knows how big a market is until you try it. There was no tablet market before iPad. Even in an established category is no guarantee of a market - nor a limit. But you need to put some kind of stake in the ground.

Predicting growth is of course obviously even harder (slide 9.). What I suggest is to also **present the actual growth rates of similar companies.** Whilst few private companies release revenue numbers, most will release user numbers, and knowing the pricing model you can at least estimate the revenue. Even without revenue, and particularly in your case as a social network, user growth alone is of interest. The other things to look at are the S-1s and other reports of "analogous" companies that IPO as they often detail their history. What this does though is to justify assumptions about hockey stick ramps etc. Even if your own plan is quite different, the base assumptions should carry forward.

Both of these points will certainly be a key concern of your investors, so you have to include them. It's largely on these factors that the decision to invest will be made - the other key criteria being what they think of you and the team from an execution standpoint.

Is it safe giving out your pitch to any investor?

Yes, in the sense that no harm will come from the Angel sharing your teaser with all and sundry (which BTW, they will). In fact the opposite, you will benefit.

It might help to give the perspective of someone who often receives this teaser forwarded from investors asking for my views.

Generally speaking, I will spend about an hour or so on a company. A distressing number of times I can't actually figure out in detail what the value proposition is, and a lot of my feedback will be to that effect. But if I say "I don't understand your terminology", then maybe, just maybe, others might have the same problem too.

But assuming I get past that stage, then my feedback will vary depending on my level of knowledge of the area. Sometimes feedback from someone outside can be interesting because of that. When you eat, breathe and sleep an idea continuously, some outside perspective can really help. Typically all of the feedback I give will get relayed by the Angel/VC back to the startup for them to factor in as they choose. Even if you ignore it, it's still a data-point worth having.

OK, so let's get to the heart of this. *Am I going to steal any good ideas I find? Absolutely.* In fact, every idea I've ever had came from somewhere else, either directly or indirectly. That's how ideas work.

I recently received a teaser for a company that I did not know about but fits into the market landscape of another idea I am working on. The result is that their name is now going to get propagated in front of a whole different set of investors as part of my market map. That can only help them. Oh, and I also told them about this other idea I'm working on, which again is at a minimum a data-point, if nothing else.

The worry about IP is misplaced. There is a well-trodden route if that is important - submit a patent. Here is a good resource to get started and see if this is applicable to you - Protecting Ideas: Can Ideas Be Protected or Patented? - IPWatchdog.com | Patents & Patent Law . The key point is that you must file before sharing if you think you will need this.

My final tip is to share what a security services person once told me on how to best to keep a secret - *"Never tell anyone"*. I guess that's why they get paid the big bucks. Of course, that means you won't be getting funded, but you need to make that determination as to which is more important to you.

You sometimes hear about bitter founders complaining others stole their ideas. The canonical example of our times is Facebook - At Last -- The Full Story Of How Facebook Was Founded But the reality is Facebook was as unoriginal idea as it gets. MySpace was already ahead. Going further in history back you had AOL hometown.

As Thomas Edison said, "Genius is 1% inspiration, 99% perspiration". It's why all investors agree it's all about execution, not ideas. If they think

your idea is so fantastic it's worth copying wholesale, then they will think you are the best people to execute. As others have said, no investors have ever taken a pitch idea and simply implemented with a different team. Investors are constrained on founders, not ideas.

What are some good examples of an app's competitive analysis report?

The key thing is that the analysis should not just cover the product, but also cover it's sales channels, marketing messages, key customers etc. It's also good to end the report with some actionable sound bites that can be used by sales/marketing to defeat them. I would structure such a report as follows:

THE APP'S COMPETITIVE ANALYSIS REPORT

1. Summary
2. Company/Product History/Profitability
3. Revenues/Market Share/Key customers
4. Market positioning (e.g. are they high-end and us low-end?)
5. Product Functionality - key strengths and weaknesses as compared to us
6. Future product plans (likely to be speculative)
7. Third party analysis/comments/press (e.g. consumer review sites, IT analysts)
8. Marketing (messaging, how much do they spend, what channels)
9. Proposed Product Development Strategy to counter (medium-long term)
10. Proposed Sales & Marketing Strategy to counter (short-medium term)
11. Conclusions - maybe an overall positioning matrix of all your competitors, a bit like Gartner's Magic Quadrant

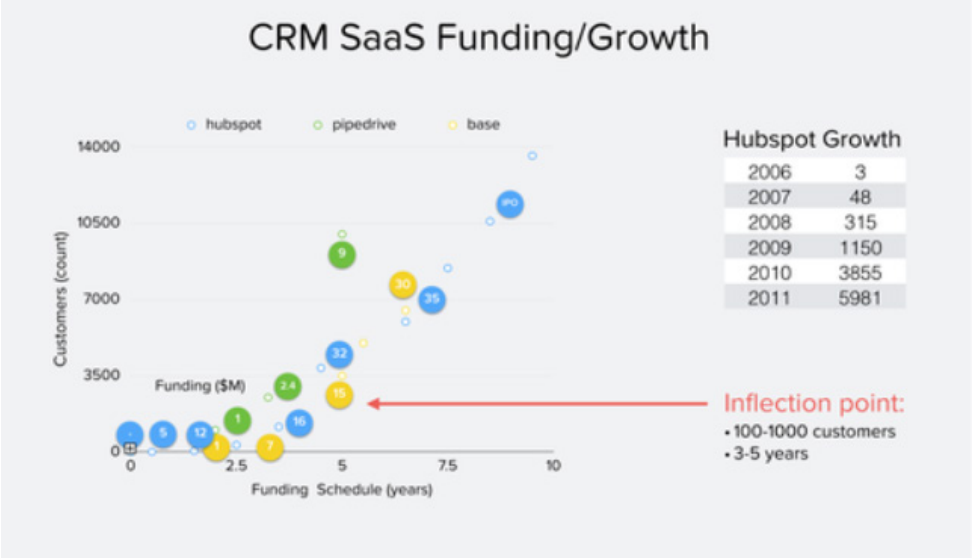
The Business Model

There are two main purposes in having a business model: 1. Illustrate the revenue ramp people looking for? 2. How can you justify these figures for your product and market?

An attractive end point for an investor, would be **a valuation of $100M within 5 years**, based on **a rough rule of thumb of 60 x MRR** (Monthly Recurring Revenue). Why not 5 x ARR (Annually Recurring Revenue)? Because the real number people are investing in is growth. All investments are based on a belief in future performance and for that growth is just as important as absolute numbers. I'm using the word "end-point" rather than exit since that may or may not happen then, but if you have a solid valuation, then everyone will still be happy.

Ultimately it's always about revenue - customer numbers are a proxy.

Assuming those figures, this means your revenue ramp from funding needs to reach out 5 years to an MRR of $1.7M. This won't be a straight line, but will instead be a compounding growth curve. The best way to understand what shape of curve to use is to look at similar companies to your own that have already gone this hump. Private companies seldom if ever give out revenue numbers but they often but user numbers out, especially with funding rounds. After a quick look at their pricing page is all it takes to then estimate their revenue. Here is an example pertinent to CRM looking at Hubspot, Base, and Pipedrive:



» *CRM SaaS Funding/Growth*

You'll note **there is always a hockey stick** caused be a critical mass of customers refining that product to get it "just right", and a critical mass of market awareness. That's the point when things take off. For large enterprise businesses, this is probably towards the 100 user end and for more consumer based businesses this is probably more towards the 1000 user end.

Use these ideas to build out a revenue and customer ramp that can be justified.

You can be as aggressive as you want, but it has to be realistic. Being unrealistic will sap investor confidence.

A key input to this is **pricing**. That's set by the market (which if you are creating a new market, may not yet exist), but in any event, assumptions here will have a critical impact on your revenue ramp. Those assumptions need to have defensible bases.

Perhaps the most important part of the justification is evaluating the potential market size. One approach I use is to **try multiple methods of estimating the market size** (slide 5.) For example I recently did this for a general productivity tool. I looked at three different models. One based on some fraction of MS Office revenue, another based on "what would a LinkedIn user likely be happy to pay for this" and finally, one based on some fraction of the SaaS market. All three models came in a range $2-5B, so it gave *some* confidence there might be a reasonable market here.

Finally, the forward plan needs to have **sensible costs** with it. The purpose of this is to make sure you can build a sustainable business that will not get swamped by cost of sale. This also brings in a key metric for SaaS companies CAC/LTV (Customer Acquisition Cost / Long Term Value). Clearly this needs to be positive, and preferably highly so. You can check out the many Quora answers around CAC/LTV for more info here. The costs need to support the business, so if when you have 1000 customers, does your model include sufficient support reps to manage that? And does the model contain sufficient rent for large enough premises for them? The model all needs to logically hang together.

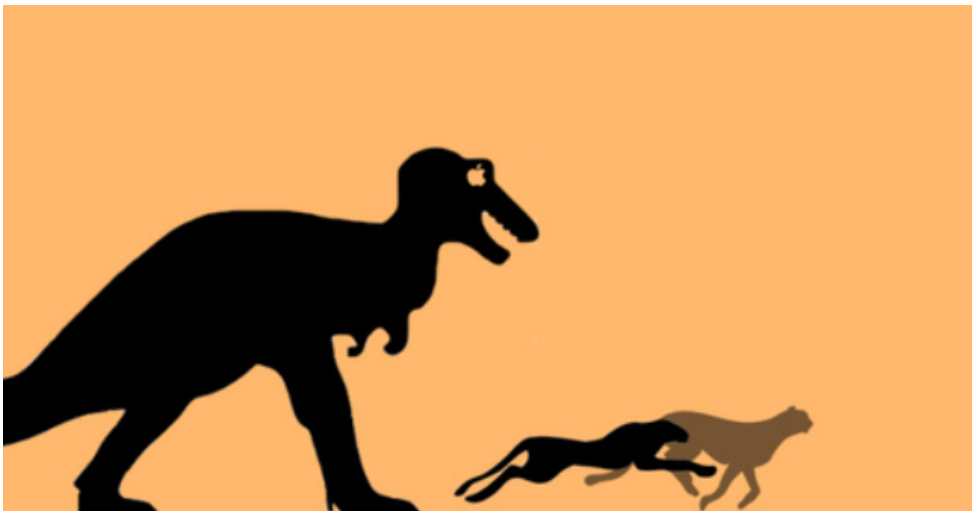
The aim is not to get to profitability as quickly as possible (although if you chose to bootstrap, it might be), but instead to grow as quickly as possible, running a loss that future funding rounds (1 every 18-30 months) top up. If this is a hot deal investors will *want* to be able to put more money in later. The granddaddy of SaaS, SalesForce, is still (2016) being run for growth rather than profit.

It's a great idea, but...Why Google/ Facebook/ Apple/ SalesForce (probably) won't steal your lunch money

It's the one question which always gets asked of a startup - why won't (*insert market leader here*) simply implement your great idea themselves, wiping you out in the process?

A reasonable enough question, given the billions of dollars and thousands of engineers available to them, as compared to the typical startup's resources.

It's worth outlining the reasons why in fact Goliath has fewer advantages than you might think as compared to David.



» *Goliath has fewer advantages than you might think as compared to David.*

1. Innovation is a Crap Shoot

“VCs invest in markets, and people (specifically CEO’s).”

No one *really* knows that your great idea is great. That’s only found out when the revenue comes in, and by that stage, you’re well on the way to becoming the next generation incumbent. VCs don’t invest in companies. VCs invest in markets, and people (specifically CEO’s). They understand that in a hot market, they have a shot at the unicorn which will become the market leader, and a very good chance of a 2nd to 5th place player that will deliver the returns needed to keep the limited partners in order. If the market is hot enough, you won’t lose your shirt even on the also-rans. Failures are buried, and history is rewritten to emphasise the foresight of picking the 1-2 mega hits which pay the returns and the 20-30 “failures” (and remember some may still be pretty successful by most people’s reckoning) simply forgotten.

It’s a portfolio business (the technical term for “crap shoot”), and one which most VCs only play with a fund size of $100-$500M. You can’t “just” invest $10M in Facebook circa 2004 and be done - it’s not that easy - you need to invest in a wide portfolio, and that takes serious amounts of money that even market leaders baulk at when trying to run their own innovation program.

This model also requires Darwinian culling - something VCs can do easily since all they have to do is simply stop returning calls when the cash runs out. It’s much harder for a large company psychologically or practically to fire an under-performing R&D team. Google is often quoted as a counter example, and certainly they end-of-life projects with impressive regularity, but even Google have shown far more patience with Google+ than any VC would. Large companies are like mammals with their young. VCs parent like fish, and whilst it’s cold-blooded (no pun intended), it’s more effective.

Large companies are not competing with one $5M startup, they are competing against a $B ecosystem, which is why so often it’s the startup that comes out on top. Large companies cannot run projects as portfolios like VCs can.

> *“Large Companies are Process-bound. Everyone can say no, and no one can say yes.”*

2. *Everybody is Loss-averse*

Nobody wants to cannibalize revenue. Start-ups don’t have any revenue, ergo, they don’t worry about cannibalization. It’s not easy to walk away from stable, predictable (even if declining) revenues. By comparison, this latest newfangled widget may or may not deliver in the market. Better to invest in an upgraded line of mainframes...

3. *Large Companies are Process-bound*

Everyone can say no, and no one can say yes. Or more charitably, there is a need to get “buy-in” from across the corporation, where “across” can be departments scattered over the globe. There is an inherent inertia, built around middle management more focused on managing their own pension trajectory. Upper management is often too distant from the market realities to identify up-and-comers. And people at the bottom just do as they are told. Or go and form their own startup...

4. *Large Companies need Large Projects*

All large companies fundamentally become conglomerates. When you are the market leader, the only place to grow is another market. If you are delivering several $B/quarter, then only large projects can move the needle. Sure, a startup growing at 100% pa looks impressive, but the additional $1M revenue would be just a rounding error.

Where large companies do focus in innovating is in the area of large capital intensive bets - think Google StreetView, something which would be hard for a startup to compete with.

This also impacts growth strategy. From the early 90’s Oracle stopped being a database company, transitioning to a full-suite enterprise IT provider today - hardware, software, and services. People often confuse the fact that SalesForce is the incumbent market leader in CRM with the belief that SalesForce is still a CRM company. Salesforce today is a Platform-as- a-Service company looking to expand out their footprint with big data and everything else. They want to be Oracle for Cloud. With 85% of IT spending coming from enterprise customers, Marc Benioff could not care less about smaller customers nor the CRM startups earning their stripes with them, any more than Oracle gives a monkey’s about MongoDB.

5. *Not Invented Here*

Google offered themselves to Excite in 1999 for the princely sum of $1M - but Excite pooh-poohed the idea since it was so simple to implement themselves. The funny thing is, they were right, but they just never got around to doing it. The rest, as they say, is history. Excite Turns Down Google Acquisition - In Photos: 6 Business Deal Disasters .

It’s hard as a big company product manager with access to hundreds of developers to accept they could have missed something a couple of geeks with barely a pot noodle between them have managed. So usually they don’t.

6. Large Companies aren't Large

Large companies have lots of departments. Each of which may or may not be that big. "*But they still have lots of resources*". Yes, but there are all doing things, and in terms of the actual skill sets needed, no, they don't.

I joined Sybase (1500 employees at the time) from IBM (300,000 employees) in the 90's and was surprised that up-and-coming Sybase (which only did databases) had twice the number of database focused staff than IBM (which did everything including project manage the delivery of military helicopters). I wasn't surprised then when joining the startup Illustra (< 80 staff) that we still had more web database expertise than Informix, Oracle and Sybase put together. Informix eventually coughed up $400M for Illustra.

7. Time is Money

Why, *on earth*, did Facebook not simply reproduce the 24 man-month effort that Instagram represented, rather than pay an eye-popping $1B???

It wasn't an acquihire for 13 staff. Nor was it really about market share, since almost every one of Instagram's 30M customers would already be using Facebook (845M at that time). And it certainly wasn't about acquiring revenue - Instagram had none, nada, zero, zilch, $0.00.

The reason was that Facebook was convinced that this was the future of photo-sharing and would put their own business at risk (since Facebook, reduced, is really about photos). For all the reasons outlined above, they knew that it would take at least 12 months to replicate that, and in that time there could have been a significant reversal of fortunes between the incumbent and the startup. Buying rather than building means additional revenue, but at levels commensurate with the acquiring company's existing sales and marketing channels - not the startup's. This can easily justify apparently silly revenue multiples since the comparison point is not what Instagram is currently doing, but rather what Facebook would be missing out on, were it not. With Facebook doing almost $3B in 3Q14, then paying just one month's revenue for Instagram now looks like a bargain given its importance to the Facebook value proposition.

Focus on the Customers, not the Competition

You can't reliably grow an oak tree by relying on just one acorn. You need a full tray of seedlings, thinning some out and nurturing the rest, and hopefully, at least one will turn out well. It's actually the entire premise of the VC model, and it's also the reason big companies don't typically stamp on startups, since they don't know which seedling will be the one to finally overtake them, and there are too many to snuff them all out.

Like all generalizations in business there are exceptions. Developing a feature for a market leader typically does not end well, but these should be clear to identify. The general rule, though, is clear. Few startups are actually at risk from the incumbents they seek to displace. The greater risk is does any part of the market actually want what you offer?

SalesSeek

www.salesseek.net