

**OUREA**  
CAPITAL ADVISORS

**Overview of equity fund raising  
& role of investment bankers**



## Huge amount of capital formation will be required especially in SMEs to sustain this growth

India needs to create 10-15 million jobs per year over the next decade to provide a gainful employment to its expanding young population

Innovation driven businesses crucial for such large – scale employment generation

Need of successful businesses that will help generate solutions in the sector of education, affordable health care, clean energy, waste management etc.

These high growth early stage companies will require early stage financing to become successful

### CHALLENGE

Financing deficiency will put the high growth companies at the risk of failure



# Large gap between the funding needs and available options for early stage ventures

## Financing options for an early stage company

### Funds from banks

- Excessive collateral driven instrument
- Stringent norms and mandatory past record requirement
- Rigid covenant structure which might hamper the growth of the company
- Difficult to avail for companies that create less tangible assets, are innovation driven and are promoted by first generation entrepreneurs

### Angel Investor / Venture Capital

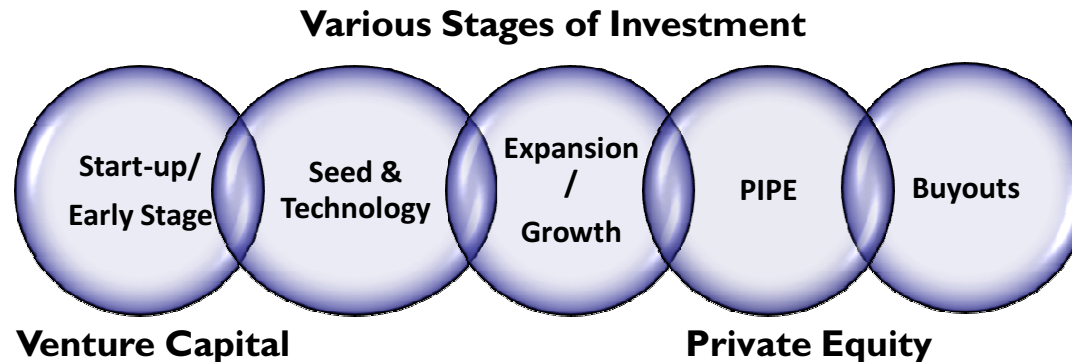
- Demand outstripping supply
- Trading away ownership of the company for funding
- Discomfort of the investors to deploy their capital in assets
- High level of controls from the investor due to stage and risk of the business
- Expectation mismatch
- Highest cost instrument

**SMEs struggling to raise “real” capital putting many businesses with high growth potential at risk**

# FUND RAISING

# Private Equity and Venture Capital- Concept

- Private equity is equity investment in high growth companies whether listed or unlisted
- Investments in private equity most often involve either
  - an investment of capital into an operating company or
  - the acquisition of an operating company (Buyout funds) or
  - purchase of shares of existing investors / promoters
- **Venture capital-** It is a broad subcategory of private equity that refers to equity investments made, typically in less mature companies, for the launch, early development, or expansion of a business.
- In India, private equity funds are active across sectors funding both listed and unlisted companies. Funding in listed companies is called PIPE (Private Investment in Public Enterprises)



# Why Venture Capital? Why Private equity?

## Startup / early Stage



Bank saying NO to loans and seed funding !!

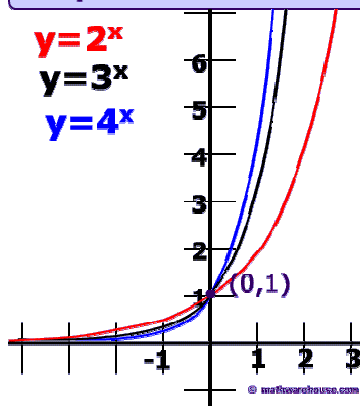
You have a new concept and friends and family do not believe the potential !! They say NO !

You have limited capital

## Growth Stage

But a venture capital fund takes a bet on you and your business model !

Graphs of three exponential functions



Industry in which you operate is growing at 15% but you wish to beat the growth rate!

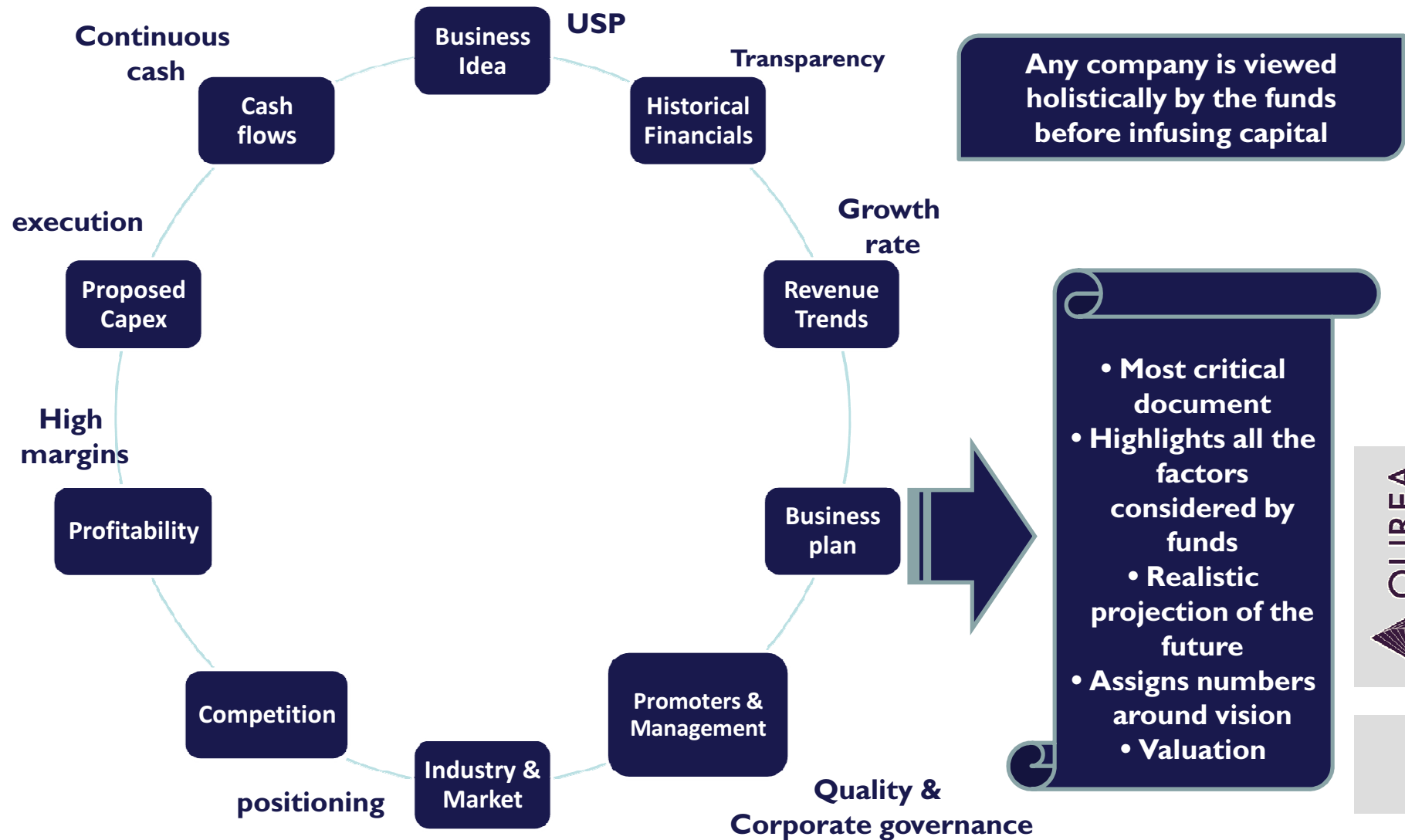
You wish to have growth in multiples and not in percentages

Company is fully leveraged and no room for additional bank funding!

You believe that your service / product can achieve the exponential growth and you have the right strategies in place!

A growth oriented private equity fund will fund the required growth and ride the upside !

# Key parameters considered by VC/PE



## Typical issues faced in private equity deals

- Business model – **Call of PE fund on the business**
- Valuation – **Both parties to agree on valuation**
- Agreement Terms – **Stringent terms if things don't work out as planned**
- Exit options – **Fund requiring immense clarity on exit**
- Confidence in promoter – **Will the promoter deliver?**
- Fear of private equity fund running the show – **Monitoring vis-à-vis micro management**



## Typical dilemma's faced by the management

### Growth v/s Dilution

PE leads to both growth and dilution – thus important to strike a balance between the two

### Control & interference

Fear of the management that the fund will exercise control and interference

### Valuation on future earnings

Structuring the investment on future earnings and profitability

### Investment Horizon

Investment Horizon typically ranges between 3 to 5 years – can extend upto 7 years. Exceptions are family houses

### Exit Options

IPO, Strategic Sale, Next round of larger fund

# Broad process of raising Private equity capital

## Pre infusion of money



- Business plan highlights markets, company, expansion plan
- Indepth financial model

- Fund carries out extensive research and business analysis
- Broad valuation parameters and commercials are agreed

- Term sheet highlights in principle agreement to key commercial terms
- External party appointed for financial due diligence
- Valuation adjustment post Due Diligence report
- Execution of shareholder agreement and closure

## Post infusion of money



- Create MIS systems and budgeting to formulate and track business numbers

- Private equity fund would monitor business numbers periodically on its own or through external party

- Key business parameters are taken up at Board for discussion

**VALUATION – MANAGEMENT’S  
DREAM OF ‘APPLE’ VALUE !**

## Valuation – what does industry players look for?

The process of determining the value of an asset or company

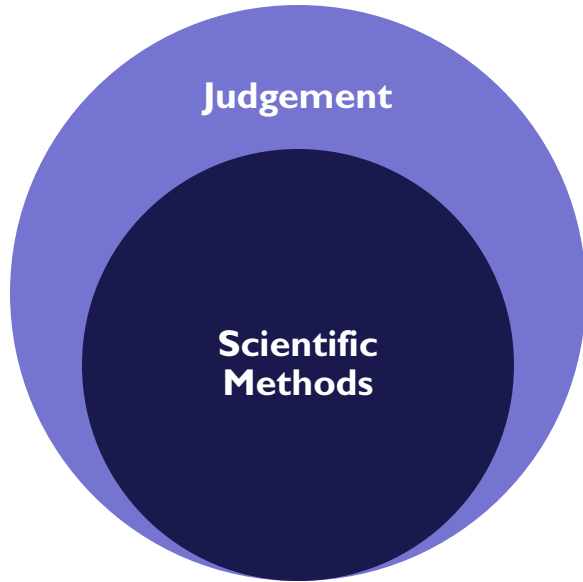
The act or process of assessing value or price; an appraisal.

Intrinsic value: The actual value of a security as opposed to its market price or book value

### How industry views it...

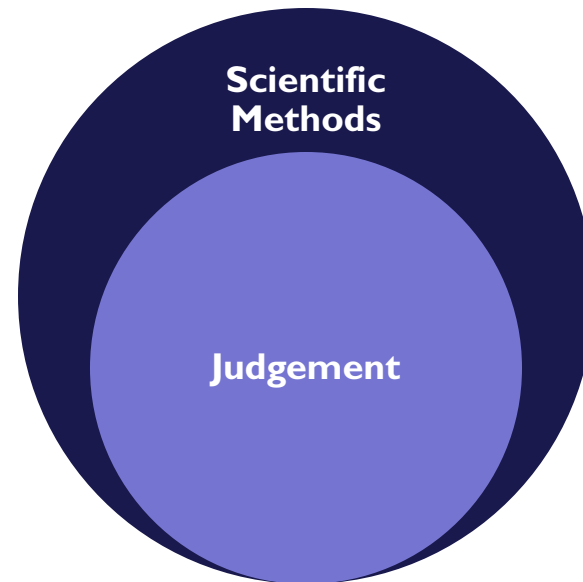
Perceived value for an asset or business which is agreeable to both seller and buyer at negotiated terms in the framework of valuation arrived and as on that particular market scenario

Its more of a science of judgement than a pure science!



Methods + judgement + Experience  
=  
VALUATION  
FRAMEWORK

Actually composition practiced in the industry !!



# Process of valuation

## Analysing the growth driver

- Both historical as well as future growth drivers (Macro and micro)
- Analysing the risk factors associated with growth

## Ascertaining quantifiable factors

- Revenues, EBITDA and PAT
- Market size, capacity and production

## Ascertaining intangibles

- Quality of management, manpower force
- Quality of customers and their contracts
- Vendor/supplier relationships
- Technology / Patent

## Building robust financial model

- 3 to 5 year indepth financial model
- Scenario analysis and sensitivity analysis

## Valuation – through Various methods

- Applying various valuation methods suitable to the industry & company

## Methods of valuation and their relevance

EV / EBITDA

Values the company based on true operational profit without considering any non cash charge

PRICE / EARNINGS

Values on EPS of the company. Attempts to factor the growth potential in net profits

PRICE / SALES

Values as multiple of revenues to capture high volume nature of business

DISCOUNTED  
CASHFLOW

Values the company on future cash flow earning capabilities

BOOK VALUE

Rarely used in growth oriented companies  
High weightage during liquidation

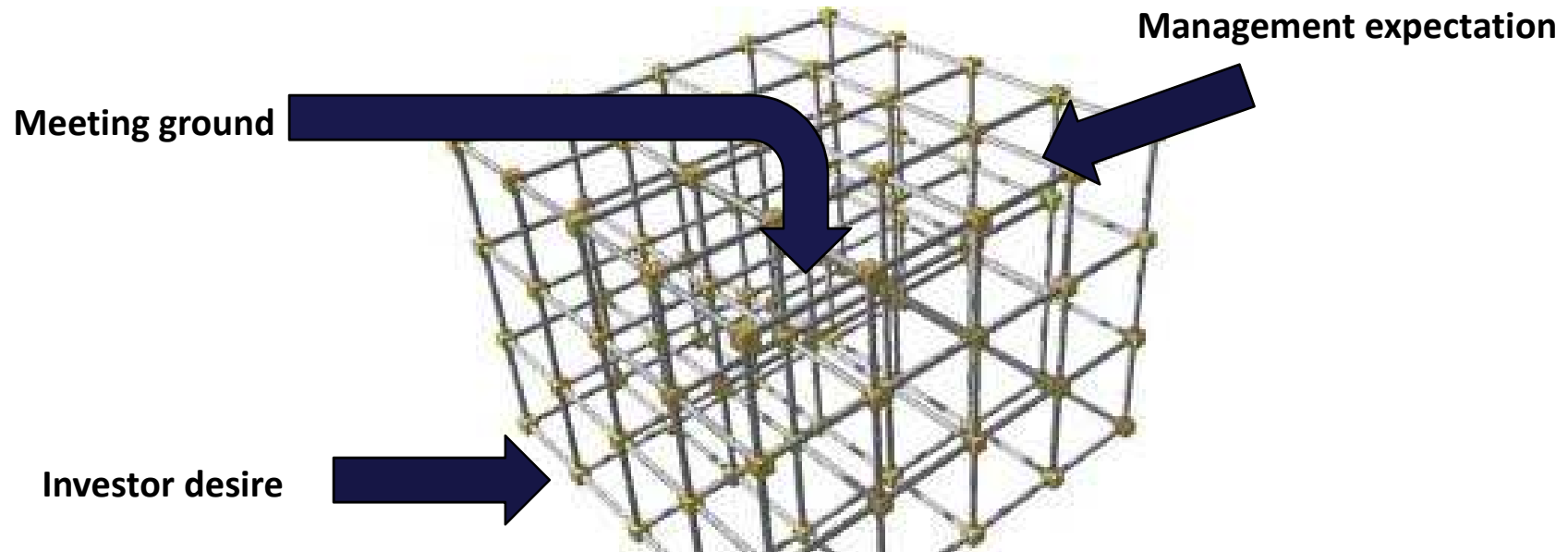
# What is the final valuation??

Common question – if multiple methods are used, what is that 1 exact value??

The answer is

**VALUATION DOES NOT GIVE 1 VALUE**

**IT PROVIDES BOUNDRIES AND FRAMEWORK FOR NEGOTIATIONS**





## What is genuinely expected from the investment banker

- Thorough understanding of the business
- Genuine hand holding and feedback on business
- Preparation of relevant fund raising documents
- Deep routed relationships with the funds
- Established credibility among the funding community
- High level of integrity – fees v/s interest of the client
- Balanced & pragmatic approach to negotiations
- Remaining engaged in the process

**THANK YOU**

**CA. SHRIRANG TAMBE**