FRANCE DIGITALE

Bootstrapping vs Fundraising

Bonus: a comprehensive guide to understand Venture Capital

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Are you sure **you** need **investors**?

Are you sure **investors** need **you**?

France Digitale is
the alliance of the best entrepreneurs & investors
to create more
world-class digital champions in France.

We lobby to make a startup-friendlier environment and
make awesome events

Interested in being part of this amazing community? Drop
us an email: willy@francedigitale.org
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Part 1. How does fundraising work?

"For [VC-Backed] startups,
escape velocity has to do
with becoming the dominant
vendor and growing indefinitely."

— David Cummings

Who will fund you?

Startups don't get money from bankers (lending), only from shareholders (equity)

Banks won't lend money to finance projects with no short term revenue generation

So let's focus on **shareholders**

(Equity = long-term financing needs in uncertain corporate investment)

that's you

PS: there are lots of subsidies in France, from 50K to 500K. Go and look for it (warning: it's very time consuming)

Who are the shareholders for each step?

Pre-seed	Seed	Series A & B	Serie C+	M&A IPO
<100K	100K-1.5M	500K-5M		
Savings Love Money (F&F) Grants	Venture Capitalists Love Money (F&F) Business Angels Angel Funds Wealth managers	Venture Capitalists Angel Funds Wealth managers Corporate funds	Venture Capitalists Growth funds	*Shareholders*

Rule of thumb: each round you give around 20-30% of your remaining capital, except in pre-seed when you give around 5-10%

Who are the shareholders for each step?

Pre–seed
<100K

Savings
Love Money (F&F)
Grants

Seed
100K-1.5M

Venture Capitalists
Love Money (F&F)
Business Angels
Angel Funds
Wealth managers

Series A & B
500K-5M

Venture Capitalists
Angel Funds
Wealth managers
Corporate funds

Serie C+

Venture Capitalists
Growth funds

M&A
IPO

Shareholders

If you raise funds in tech, it will most likely be sooner or later with venture capitalists

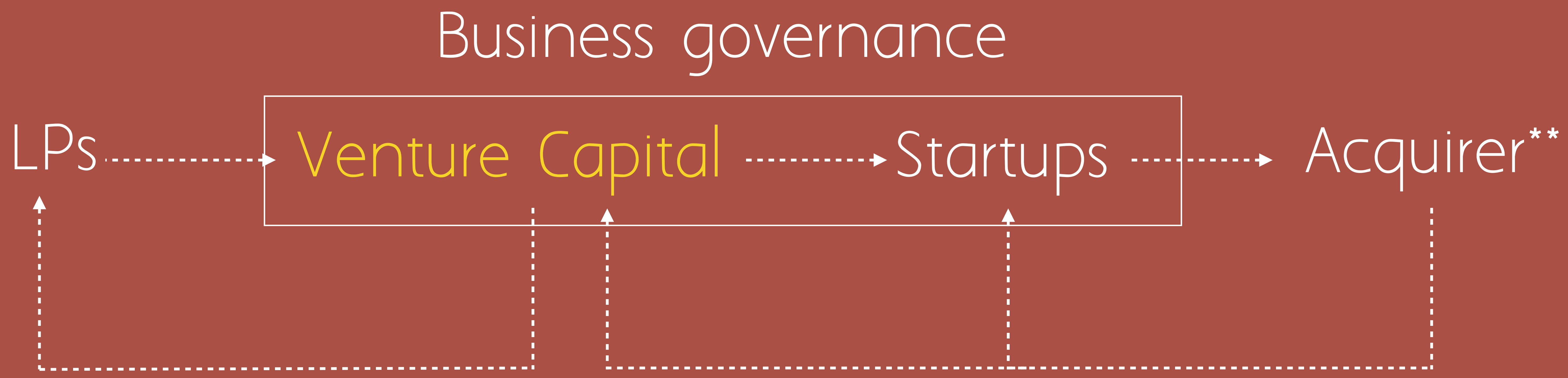
You'll certainly work with VCs.

Do you really know them?

Behind each VC there is at least one LP*

VCs also raise funds and need to be profitable

& when VCs fund your startup, they also risk their own money (between 1% and 3% of the total fund)



when you raise, you add two constraints:
sell your company within 5-8 yrs (1) at a bigger price than your last valuation (2)

---------- financial flow

*Limited Partners **M&A/IPO

When do VCs earn money?

The objective of a startup is to grow the business and its value as fast as possible to realize the greatest ROI possible on exit

So all the profits get reinvested rather than paying dividend

Shareholders get paid ONLY when they sell the company

QUICK TEST

2 questions about venture capital

1 What should be the minimum return per startup?

eg: if you say **x1.5** it means that you have to earn €3M if you have invested €2M

1 What should be the minimum return per startup?

Answer: **x2.25**

Do you wanna know why?

Please refer to Annex at the end of the presentation, it's a bit technical

② What are the key factors for an exit?

eg: the startup was a member of France Digitale

2 What are the key factors for an exit?

Answers

Growth
it's the only real focus of an entrepreneur

Visibility
from the mass market and from the key players

Barrier to entry
IP, distribution, partnership, technology...

Profitability
especially if you look for a financial exit (LBO/MBO/IPO),

People -> Process
the right organization to keep scaling the business

3 What are the differences between FCPI & FCPR?

	FCPI	FCPR
Category	Retail investment fund	Institutional investment fund
Funded by	Tax-incentivized individual investors*	Limited Partners (institutional)
Investment period	30 months	36 to 48 months
Investment criteria	Innovative* companies in Europe	Defined by the GP
Maturity	5 to 7 years	7 to 10 years
Size	Between 10M€ to 30M€	Between 30M€ to 200M€
Management Fees	around 3,5% / year	2% /year
Raising period	Every year (following the fiscal calendar)	No rule (usually when the investment period of the previous fund is finished)

*Individual investors benifiting from a tax incentive : immediate 18% IR tax credit / immediate 50% ISF tax credit

What does a VC expect from a startup?

"The best shot is a very large market with big companies where nothing disruptive happened for 5+ years"

— Stéphanie Deslestre, Qapa

Venture capitalists look at the same things*

* but they don't see things the same way

The criteria of investment for VCs:

team + opportunity + business model

1 Team = risk of execution

the most important criteria by far

Best format:

2-3 founders
with complementary skills,
experience in the field,
good learning pace,
connexions within the industry,
(or a community already built).

Super bonus: recommendation from a VC/BA or entrepreneur
Mega bonus: you already sold one company before
Ultra Bonus: you already sold one company before with a multiple of x2.25+

2 Opportunity = vision+promise

make them want to know more. work on your brand.

Problem/solution

(problem/solution -> be very specific & convincing about the problem)

Timing

(the later you enter a market the less risky but also the more expensive - don't be too early though)

Market size

(you have to be ambitious & disrupt a huge market)

Competitors

(you are not the best, you do things differently and that's a better way to do it and you execute it well. Focus on your competitive advantages.)

Joker: exit easy to spot (big players + recent M&As)

(or IPO if you want to rock the world)

3 Business Model = smart & wise

show them you know your job & you're creative

Value proposition

(not the technology but the product/service for the client)

Clients

(you'd better really know them)

Competitive Advantage

(distribution, technology, partnership...)

Distribution

(growth hacking plan)

Joker: you've got wonderful traction

(if it seems very risky you'd better have some good figures)

Valuation 101

Valuation: the basics

Pre-money

value of the company + goodwill

\+ funding

Post-money

\+ stock options

Post-money fully diluted

Valuation: illustration

valorisation = 10M€

fundraise = 5M€

10% stock option

Pre-money	10M€
Post-money	15M€
Post-money fully diluted*	16.67M€*

Capitalisation	Pre	Post	Post FD
Historic shareholders	100%	66%	60%
New shareholders		33%	30%
Stock options			10%

* it's like you have only (1-% stock options) of the company, since the stock options will dilute the overall shares
Valorisation Post FD = post-money/(1-% stock option)

Looking for advanced lessons about valuation?
Check Khan Academy

All stocks are not made equal

Preferred stocks & main associated rights

1. Rights of capital protection

1.1. Right of pre-emption

Right to acquire stocks that are sold before it can be offered to any other person or entity.
Also called "first option to buy".

1.2. Right of anti-dilution

In common and preferred stock, the right of a shareholder to maintain the same percentage of ownership in a company, should the company issue more stock. The anti-dilution clause can also indicates the right of a shareholder to purchase more shares in a new round of financing at the offering price up to his/her previous percentage of ownership.

* if an investor have 20% of the company for 700K€ in seed, and anticipates a future need of financing of 10M€, he will allocates 2M€ (or more) to maintain 20% of the company.

Preferred stocks & main associated rights

2. Political Rights

2.1. Right to board representation

2.2. Vote of strategic decisions
Acquisition, budget, dividends.. can be vetoed

Preferred stocks & main associated rights

3. Financial Rights

3.1. Liquidation preference

Specify which investors get paid first and how much they get paid in the event of a liquidation event such as the sale of the company. Liquidation preference helps protect venture capitalists from losing money by making sure they get their initial investments back before other parties. eg: the first 5% pro rata for all shareholders, then to financial shareholders till the level of their investment, then the rest pro rata for all shareholders

3.2. Ratchet

Correction of the pricing for the next round if the shares are at lower price. Two possibilites: full ratchet = the initial shares are priced at the level of ones from the new round ; weighted average ratchet = initial shares are priced at the level of the weighted average price paid during the different rounds

More about preferred stocks & main associated rights (french)

The 2Ps: prediction-process

Investing in VC is not really an exact science*

A glance at the anti-portfolio of Bessemer Venture Partner

Apollo Computer

(acquired by Hewlett Packard) BVP's Felda Hardymon was offered a small position in the company's last private round, and waved it away: too small a position, he thought, at too high a price. In less than a year it was worth 17x.

"Stamps? Coins? Comic books? You've GOT to be kidding," thought Cowan. "No-brainer pass."

Incredibly, BVP passed on Federal Express seven times.

BVP had the opportunity to invest in pre-IPO secondary stock in Apple at a $60M valuation. BVP's Neill Brownstein called it "outrageously expensive."

David Cowan passed on the Series A round. Rookie team, regulatory nightmare, and, 4 years later, a $1.5 billion acquisition by eBay.

Cowan's college friend rented her garage to Sergey and Larry for their first year. In 1999 and 2000 she tried to introduce Cowan to "these two really smart Stanford students writing a search engine". Students? A new search engine? In the most important moment ever for Bessemer's anti-portfolio, Cowan asked her, "How can I get out of this house without going anywhere near your garage?"

StrataCom

(acquired by Cisco) Felda Hardymon: "[Sierra's] Pete Wendell asked if I'd like to look at Stratacom, which was doing a 'fast packet switch.' I gave him a blank stare."

BVP's Pete Bancroft never quite settled on terms with Bob Noyce, who instead took venture financing from a guy named Arthur Rock.

Prediction: chances to fundraise with a VC in France are pretty low

* dealflow of around 1000-1500 startups/year for a reputed VC fund (between 500 & 2000 depending of the scope & the attractiveness of the fund). 5-10 deals closed/year

** around 4000 startups/year seeking fund. Around 200 fundraise in the whole ecosystem.

The Process

Executive Summary → Dealflow instruction
analyst

try to avoid this step by meeting them
before you need funds (chances almost x2)

40% OUT

Weekly investment committee
full team

90% OUT

Business Plan

First meeting
analyst + partner
Slideshow

85% OUT

Instruction
2 partners/1 partner-1 analyst
focus on specific points, "friendly" due diligence

40% OUT

/!\ due diligence

Negotiation
at least one partner
Everything you got

>10% OUT

Party
everyone cool
Champaign

chance of raising: 100*(1-40%)*(1-90%)*(1-85%)*(1-40%)*(1-10%)=0,48%

The relationship AFTER the raise

What they will ask you:
- reporting (revenue each month or quarter)
- an action plan
- validate the P&L and the main decisions

What you should ask them:
read this wonderful article

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* or send us an email: willy@francedigitale.org

Part 2. Should you raise funds?

yes, this is just an option

99designs®

GoPro®
Be a HERO.™

github
SOCIAL CODING

ROVIO

APPSUMO

DELL™

What do they have in common?

They bootstrapped.

You can make an incredible startup
without raising funds.

No money = great constraint to look for efficiency
Money is a painkiller.

Founded in 2008 - 3 cofounders.
1 kept working full time during the early days,
the 2 other made freelancing on the side.

* Github

Founded in 2010 - 3 cofounders.

Build the MVP with $60 (open source + outsourcer)

First test on Reddit : 200 deals of pro accounts at imgur.com 50% discount

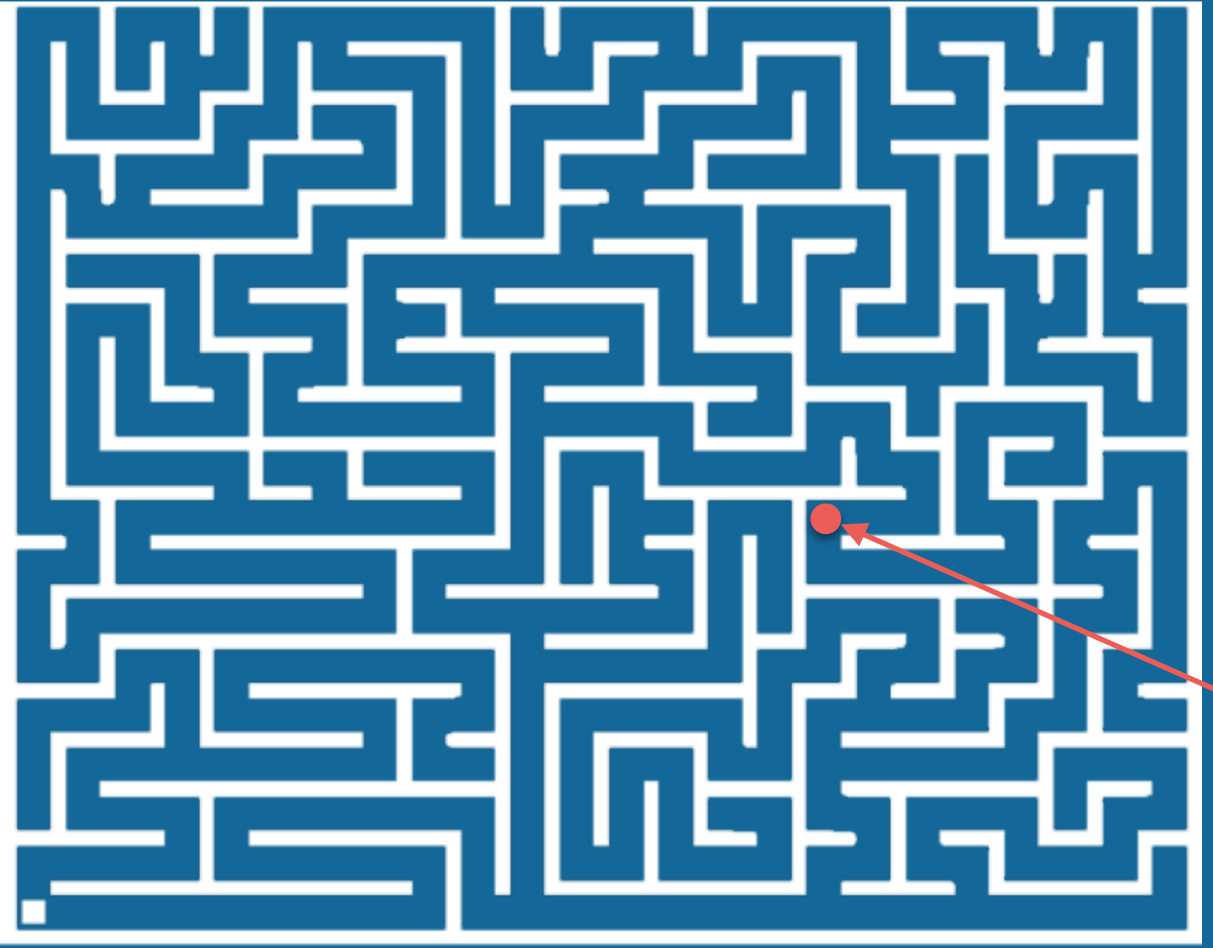
Then rebuilt the site & sold 500 productivity bundles on Lifehackers. POC + cashflows.

* AppSumo

Yes, this is possible*.
So when should you raise fund?

* also in France, look at MyLittleParis, HumanCoders, Adopteunmec, Wisembly, Capital Koala, Appgratis (at least for a long time), etc.

The next slide could hurt your aesthetic sensibility.



you are here

Do you want to grow very fast to disrupt a market?

NO → DON'T RAISE!

YES ↓

Do you have significant upfront investment to test your market?

YES → RAISE!

NO ↓

Can you grow your business as you wish with your revenue stream before burning all your cash?

YES → DON'T RAISE!

NO ↓

Do you charge man days to your clients?

YES → C'mon, close more deals. (you don't sale enough to raise)

NO ↓

Do you want to keep the control of your business

YES → You're in trouble

NO ←

Is your market small?

NO ← RAISE!

YES ↑

Either you can find a way to generate enough revenue or your dead

What should you remember?

What should you remember?

Not raising is not failing.
Raising is not succeeding.

By the way...
Github raised funds eventually.
So did 99designs

raising funds is not a one time decision

What does bootstrapping mean?

in practice

Bootstrapping = lower velocity

Escape velocity, in physics, is basically the speed needed to break free from gravity.
For a bootstrapper it might only be the freedom to pay the bills.

Your growth can be linear.

If you have 10 new clients every month and if your retention is great.
that makes 120 clients per year. That can be more than sufficient

Distribution can be smaller

If you need a few thousand customers and not millions,
you can use any channel that is ROI positive. Even if it doesn't scale.

Acquisition & retention can be manual

You can email yourself your power customers and get to know (or at least talk to) most of your clients, sooner or later.

Conclusion for PG

"Avoid investors till you decide to raise money, and then when you do, talk to them all in parallel, prioritized by expected value, and accept offers greedily. That's fundraising in one sentence. Don't introduce complicated optimizations, and don't let investors introduce complications either.

Fundraising is not what will make you successful. It's just a means to an end. Your primary goal should be to get it over with and get back to what will make you successful—making things and talking to users—and the path I've described will for most startups be the surest way to that destination.

Be good, take care of yourselves, and don't leave the path."

- Paul Graham

Credit

Infos of bootstrapped companies in Quora

Discussion with lots of investors, especially **Marie Ekeland**, **Xavier Lazarus**, **Samantha Jerusalmy** & **Sebastien Derhy** (Elaia Partners), **Emanuele Levi** (360 Capital Partner), **Nicolas Celier** (Alven Capital), **Jean-David Chamboredon** (ISAI) & **Vladimir Bolze** (Fa Diese), Jérôme Masurel (50 Partners)

Discussion with **Frederic Mazzella** (BlaBlaCar)

Discussion with **Oussama Ammar** (The Family) and his wonderful workshops (in french: fundraising & valorisation)
Workshop France Digitale + Girls in Tech about "Financing Seed"
Presentation (in french) from **Christophe Raynaud** (ISAI)
Article of Paul Graham

Special thanks to Mathieu Daix, Taro Ugen & Emmanuelle Coulon, my dear colleagues that helped me to improve this presentation
Slides 27-28, 31-32 were made by Marie Ekeland (Elaia Partners)
Slides 63-65 were made by Emanuele Levi (360° Capital Partner)
Slide 19 were made by Barbara Belvisi (PiedElephant)

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Annex

THE DARK SIDE OF THE PRESENTATION

Corporate finance 101: hurdle rate & IRR

you can skip this slide, only for math lovers

€100M with a hurdle rate: 7%* (6 year average holding period positive return) -> €150M minimum

Target IRR of fund investors (the LP) 10-15%*net of carried interest -> around €225M to stay in business

* average in the venture capital market

Let's explain why you need a x2.25 on average without math (1/2)

20 startups in the portfolio

€4M of funding per startup

valuation x2

Below 2X they actually "lose money" (20x4x2=160 < 225)

target size for the fund

3X is a positive contributor to fund objectif (20x4x3= 240 > 225)

5X & 10X are needed to compensate bad investments

Let's explain why you need a x2.25 on average without math (2/2)

1 blockbuster: 20x = 80m

1 Star: 10x = 40m

2 Successes: 5x = 2x20m = 40m

4 Average: 2-3x = 4x10m = 40m

6 Bad investments: 0,5x-2x = 20m

6 Write-offs

→ €220M, net IRR to investors 12%*

On any given investment, x10 must be possible.

*including 20-25m of carried interests (for 12 years of work)