WHITE PAPER

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MAXIMIZING EARLY STAGE FUNDING OPPORTUNITIES

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INTRODUCTION

Early stage to emerging growth stage companies are increasingly finding it difficult to raise funds despite the availability of potential investor sources such as angel funds, venture capital firms, crowdfunding websites, family offices, and services offered by emerging growth investment banks. The initial challenge is gaining access to the investment community. During these meetings, it is equally important for management teams to demonstrate an understanding of the funding process which includes proper positioning and information presentation in the format preferred by investors. Premium valuations and funding can be achieved by partnering with industry veterans that facilitate investor meetings and provide business/valuation expertise.

The Lay of the Land

"Simply put, the U.S. public capital markets are no longer hospitable to startups seeking capital to scale into the successful firms of tomorrow." *https://smallbiztrends.com/2016/07/innovation-act-small-business.html*
National Venture Capital Association President Bobby Franklin

With the number of IPOs down 50% from less than 20 years ago and many orphaned or low-trading stocks, it is no surprise startups and early stage companies are having difficulty raising capital. The vagaries of the public markets have trickled down to the private company financings arena as well. Funders who invest in private companies have established stricter parameters for investment consideration. Thus, it is crucial that companies seeking investment capital are "investment ready," lest they squander their limited opportunities to successfully attract investors. Moreover, the most successful startups understand the importance of relationship leverage by partnering with qualified industry veterans to gain access to capital and prepare for funding. For the purposes of this white paper, we focused on firms that provide funding from the angel stage through pre-IPO or sale stage. These include angel funds and investors, venture capital funds, family offices, and crowdfunding sites.

Funders

The **Angel Investor Market** is characterized by individual angels, an angel group, or syndication of angel groups that invest in companies from the seed to early stages. Many tend to be regional in focus; it is rare they invest in firms outside their region, although recent trends illustrate changes in this model. Valuations by region can vary as does the industry emphasis. In 2016, throughout the U.S., roughly half of all deals were in software or health care. Many funds perform due diligence with the intention of participating in follow-on financings, which reduces their failure rates.

According to the Center for Venture Research, the angel investor market in 2016 experienced a decrease in investment dollars and in deal size. Total investments in 2016 were $21.3 billion (down 13% from 2015) with nearly 300,000 active angel investors. A total of 64,380 entrepreneurial ventures received angel funding in 2016, with an average deal size of over $330,000. (This includes multiple or follow-on financings.) The Angel Resource Institute's 2016 report noted an average pre-money valuation of $3.7

million, down from $4.6 million last year. While the median funding was $127,000 by a single fund, the median size deal where groups co-invest was $950,000.

According to the National Venture Capital Association, there are 900 **Venture Capital Firms** with $333 billion in assets under management. During the first quarter of 2017, investors deployed $16.5 billion to 1,797 venture-backed startups --the fewest companies to receive investment since Q4 2011. Despite the slowdown, venture firms have plenty of cash to deploy. Following a record year for venture fundraising in 2016, investors raised $7.9 billion across 58 vehicles.

Angel and seed deals took the biggest hit in terms of the number of completed financings, with just 827 deals completed in the first quarter of 2017, down from 1,223 recorded in Q1 2016. In addition, the number of completed first financings fell to just 497 in the first quarter, the fewest in a single quarter in almost seven years. Investments into software and life sciences accounted for the majority of deal activity with more than 930 deals completed in Q1.

Title III of the JOBS Act established **Crowdfunding** provisions that allow early-stage businesses to offer and sell securities. Only Broker-dealers and registered funding portals are permitted to offer and sell securities on behalf of issuers to the investing public using crowdfunding. A May 2017 article in *VentureBeat* on crowdfunding offers a frank assessment of the market:

"Since Regulation Crowdfunding began on May 16 last year, 335 companies have filed offering documents with the Securities and Exchange Commission (SEC) to fundraise on securities-based crowdfunding platforms. Of those companies, 43 percent were funded, 30 percent failed, and the remainder are still open and trying to get funding. The total capital committed to date on these platforms is in excess of $40 million, with the average successful crowdfunding campaign raising around $282,000 from about 312 investors. The most recent quarter saw the greatest number of companies file with the SEC. This signals that issuers might finally be catching on to the opportunity that Regulation Crowdfunding holds." https://venturebeat.com/2017/05/16/equity-crowdfunding-is-1-year-old-today-wefunder-is-top-platform/

Family offices are private companies that manage investments and trusts for a single family. The company's financial capital is the family's own wealth, often accumulated over many family generations. There are as many as 5000 such entities in the U.S. alone and thousands more in Europe. Given lower rates of returns from certain types of alternative investments, the appetite for early stage private investments has increased in recent years, thereby making this segment a viable source of funding.

Finally, growth company **investment banks** may elect to become involved with or lead private placements with the intention of the first round leading to future rounds and perhaps an IPO or sale. Today, dozens of such firms exist in the U.S., many with long track records of success.

Not Ready For Prime Time

It is a very bitter pill for founders and management teams to swallow but *most firms are not "investment-ready."* In fact, they may not even be investment-capable. And they don't even know it.

The number one factor in the decision-making process for investors is confidence in management. If the founder has a history of building successful businesses, that history carries a great deal of weight for funders. Still, management must demonstrate not just a deep understanding of its business but industry knowledge (top-down and bottom-up) as well. Too much of an emphasis on one or the other may be viewed unfavorably.

Much like companies build their businesses that appeal to their target markets, founders must do the same with funders. This point is most often overlooked by companies new to the investing arena. In this scenario, investors could invest hundreds of thousands or millions of dollars. But, in order for that prospective investee company to even be considered for investment, the approach to this group must be different than presented to a typical customer. While a customer may consider competing products or services, funders may only invest in 2-5% of deals it reviews each year. Thus, management must put its best foot forward--the first time around.

The Hurdles

Business Plan: Founders may understand their business but too often the business plans are lacking the proper detail and information, and is in an incorrect format, which can be negatively viewed.

Business Model: Entrepreneurs occasionally live in a bubble and do not see holes or perhaps even opportunities in their business models. Collaboration with others can aid in building a strong model.

Forecasts: No one expects founders to be CFOs. However, producing realistic and defensible financial projections may be one of the most important aspects of investor presentations and successful funding. Another critical aspect of forecasts is the establishment of milestones which are used by funders to measure and judge management and the business model.

Valuation: Perhaps the biggest hurdle for entrepreneurs is valuation. Nearly all companies have an unrealistic view on valuation for their companies and can become intractable on this issue as well as ownership dilution, stonewalling the process or stopping it in its tracks.

Company-speak vs. Finance-speak: As noted above, it is critical that founders speak to funders in their language to exude confidence in their business and as good stewards of the investment funds. The process is not like the movie *Field of Dreams* (Build it and they will come.) Articulating the entrepreneurial story with the right positioning, appropriate materials, and being able to anticipate objections and have prepared responses are very real keys to success. Moreover, by providing information in the format in which the funders are accustomed, their due diligence efforts are easily managed and swiftly executed.

Once companies become investment-ready, the next hurdle is gaining A**ccess to Capital**. At the most basic level, it is not uncommon for company founders and management teams to struggle with access to capital. It is assumed that companies have already evolved from the *seed stage* and have raised the first funds from friends and family and may or may not have elected to take on conventional loans or convertible debt from a founder or friend of the firm. The next stage, which requires greater growth capital to meet its business model, may be more difficult to raise without proper contacts in the investing community. As a result, management teams find that they are spending as much if not more time trying to raise investment capital as they are running their companies. It is not uncommon that in order to close a deal quickly, companies accept funds from the wrong sources. Not all money is good money after all.

At this stage, most investors in an investee company are considered financial investors rather than strategic. Still, these investors should sit on the same side of the table as management, have a long term outlook, and ideally, be willing to increase their stakes as milestones as achieved. The wrong sources include investors that dictate potentially harmful terms or structures that may deter other investors from participating in subsequent rounds. Moreover, while the right sources include investors with a history of successes, wrong sources would only tout recent deal flow volume and sizes.

Don’t Go It Alone

The funding process is complex, lengthy, and competitive and startups have varying degrees of success. To maximize opportunities in successful fundraising, entrepreneurs need an advocate that can prepare them to become investment-ready and shepherd them through the process with the right funding sources. This advocate must have documented experience in the financial services industry with deep contacts and command respect from prospective investors. By working with firms that offer these and other qualities and services, funding at favorable valuations and with a swifter funding cycle can be achieved. Moreover, this partner will in turn aid in securing future funding commitments through the as milestones are met.

Entrepreneurs must also be able to differentiate from a true advocate that is not partnered with the company in a purely transaction-based relationship, but an aid and counsel to management throughout the lifecycle, as needed.

The Marble Arch Approach

Marble Arch Research principals have over 60 years of experience in the small company investment and investor relations industries. This experience includes structured transactions, external funding, strategic alliances, M&A counsel, investment management, public offerings, and investment research. Moreover, our relationships have resulted in $300 million in funding and investor awareness for public and private companies in the U.S. and around the world. Marble Arch clients benefit from our principals’ diverse backgrounds while working in senior positions for top tier investment firms including Prudential, Bear Stearns, and Piper Jaffray. Our success is based upon our deep understanding of relevant markets combined with strong, long-term relationships with strategic and institutional investors, along with key emerging growth investment banks.

Marble Arch offers unmatched full-service expertise, including:

- Business plans and business model guidance
- Financial forecasts
- Strategic consulting
- Valuation
- Investment reports and materials
- Data room management
- Investor roadshows and meetings

A Winning Model

The Marble Arch approach to assisting companies with their funding and investor awareness objectives typically consists of 4 stages.

Investment Prep:

This stage includes a review of and improvements to business plans, business models, and financial forecasts. The key is to developing a simple, compelling investment thesis and relatable to comparables, along with a financial model that is consistent with Wall Street expectations.

Investor Materials:

The second stage consists of most of the heavy lifting. In addition to arriving at a firm valuation or valuation range, we produce a 3rd party company research report with projected financials and comparables, along with present and future valuation estimates. We also aid in the production of corporate profiles investor decks and other relevant materials. A data room containing all necessary due diligence information is established and routinely updated. Providing access to this information and in this format can have a very positive effect on the funding consideration and reduce the funding cycle.

Investor Meetings:

After speaking with our contacts and sending the investment materials to prospective investors and investment banks to generate interest, Marble Arch sets up roadshows consisting of 1-1 meetings, dinner presentations (5-20 attendees), conference presentations, etc. Prior to the commencement of roadshow meetings, we routinely consult with management regarding presentations, provide coaching, and preparing founders to overcome identifiable objections. Following meetings, we follow-up with investors to answer questions, provide information, and to set up future calls/meetings.

Follow-On:

Given that it typically takes multiple meetings to secure interest and funding, we routinely follow up initial meetings with new ones every few months to provide prospective investors with updates. Moreover, we also update investor materials, including updates reports and decks. These updates are produced quarterly or at the least semi-annually, depending upon news flow and milestone achievements.

Conclusion

In order to successfully complete funding transactions, management teams must favorably differentiate themselves from the pack. Too often, by being unprepared, or by expecting unrealistic valuations, companies face significant hurdles in their funding objectives. Entrepreneurs who partner with industry veterans such as Marble Arch Research to serve as advocates and counsel can achieve greater success during this process.

Engagement with respected outside firms offers access to the right funders, exudes confidence in prospective investors, and aids in differentiation as compared with other deals under consideration. Moreover, such engagement can result in proper company/investment positioning, the understanding of the process from the investor perspective, and a tool to fast track due diligence by providing them with ongoing data room access.

Raising funds is an ongoing process but can be achieved with the right partner and the necessary preparation.

ABOUT MARBLE ARCH RESEARCH, INC.

Tracing our roots to 2008, Marble Arch Research, Inc. (MAR) is a leading investment research and advisory provider with a global reach. Headquartered in Atlanta, we also have offices in London, New York, and Baltimore. The Company is considered a pioneer in the production of Wall-Street quality sponsored research reports on privately-held, early stage companies, which are used to foster investor awareness and funding. Today, we combine these unique reports with critical advisory investor relations services which lead to targeted investor roadshows. Leveraging over 60 years of senior executive experience in emerging growth company corporate finance, research, sales, investment management, and investor relations, Marble Arch Research sets the stage for investor awareness and potential funding via conventional means and Reg A+ offerings.

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