

Financing New Ventures

Course Syllabus (Summer 2019)*

Faculty	Administration
Professor Sandeep Dahiya	Esther Ziegler
Georgetown University	Tel: 061 207 33 42
Email: sd@georgetown.edu	Email: summerschool-wwz@unibas.ch

“This process of *Creative Destruction* is the essential fact about Capitalism. . . In other words, the problem that is usually being visualized is how capitalism administers *existing structure*, whereas the *relevant problem is how it creates and destroys them* . . . In capitalist reality as distinguished from its textbook picture, it is not [price] competition which counts, but competition from the *new technology, the new source of supply, and the new type of organization.*”

- Joseph Schumpeter, Renowned Economist
Capitalism, Socialism and Democracy (1950)

Course Description

Every year thousands of new ventures are started and a nearly equal number of existing businesses are closed down. Almost all of these ventures are single founder/employee type of ventures where the founder has neither the desire nor the possibility of creating a significantly large business organization. A small fraction of such ventures, however, hold the promise to grow into large businesses. In this course we will focus heavily on such *promising ventures* or “*startups*”. The reason for this focus is self-evident - business that are unlikely to grow fast have little or limited need for external financing-making such ventures somewhat irrelevant for a course titled *Financing New Ventures*. This course is designed to illustrate challenges faced

* This document was prepared by Professor Sandeep Dahiya and in preparing this syllabus, Professor Dahiya has drawn heavily on similar courses offered in other universities, especially those at Harvard Business School, Tufts University and at Princeton University. The suggestions and advice provided by professors Amar Bhide, Ramana Nanda, Joseph Lassiter, William Sahlman and Ed Zschau has been of tremendous help and their contribution is gratefully acknowledged.

by an entrepreneur in financing and growing a new firm. Exploiting a *promising opportunity* frequently requires an entrepreneur to marshal scarce resources, especially *external capital*. The course will focus almost exclusively on issues relevant to the *financing* of entrepreneurial ventures. We acknowledge that marshalling talent, customers, regulators and other stakeholders is equally and at times even more important than raising financing in many entrepreneurial ventures. However, given that this is a “Finance” course, the primary focus will be on challenges faced by entrepreneurs in securing adequate capital to launch *and* to grow their ventures.

We shall devote significant amount of time on understanding the role of *Venture Capital* (and to a lesser degree on Angel Investors) in financing new start-ups. The course requires and reinforces the skills needed to analyze a business with a strong emphasis on financing deal terms and valuation techniques. The course concludes by examining the harvesting of entrepreneurial ventures whereby the entrepreneur and the financiers realize the returns for their effort. The course will use a number of case studies based on startups or young firms.

Course Objectives:

Since the focus of the course is on *high potential* ventures, it is important to recognize the nature of the context in which entrepreneurs that start such ventures operate. Broadly, we can identify four critical characteristics of the environment faced by the founders of promising ventures. These are:

1. **Great Uncertainty:** The very nature of new undertakings implies that entrepreneurs face a tremendous range of uncertainty about technological feasibility of their product, the number of potential customers, and the availability of key resources such as talent and financing. **The course will provide theoretical and practical frameworks that Venture Capitalists and Angel Investors use to mitigate the challenge of financing high degree of uncertainty.**
2. **Rapid Growth:** The sheer level of uncertainty almost requires that the *expected* return for both the entrepreneur and the investors be high. This, in turn, can only come if the business is capable of growing extremely fast. The annual sales growth rate for a business that takes off can easily exceed 50%-100% per year. The pace of such growth forces entrepreneur to deal with the unique challenges of attracting people, assuring adequate supply and distribution of product or service, and developing an organizational infrastructure that keeps the wheels from coming off. A central issue is assuring that there is adequate financing available to launch and sustain such growth rates. **The course aims to illustrate the challenges of financing very high rates of growth and how these challenges may be met.**
3. **Radical Change:** Almost all high potential ventures unleash fundamental and radical change. The source of this change may be in product or process technology (e.g. Skype for telephony), or in distribution (Spotify for music distribution) or in a basic business model and type of organization (Amazon.com in retailing), or by creating new industries and markets (Google for online ads). It almost always involves moving from something that is known and familiar to something that is

only conceived in the mind. **The course will provide frameworks for valuing business with potential for great disruption.**

4. **Limited Resources:** Finally, most entrepreneurs operate with extremely limited resources especially tight financing. Given the tremendous uncertainty, investors will only commit in small incremental stages. Each stage must lead to reduction in uncertainty in order for investors to commit additional funds. A useful analogy is to think of a start-up venture as a series of experiments. You get enough money to carry out only one or two experiments - if the results are favorable you get more money to carry out another additional experiment or two. **The theme of attracting resources especially financing will be the leitmotif for the course.**

This context of Great Uncertainty, Rapid Growth, Radical Change, and Limited Resources has two implications that need to be considered. First, at a personal level, if you want to take the entrepreneurial career path you should be comfortable with all of these four characteristics. Not everyone can or wants to operate under conditions of huge ambiguity and limited resources. Pursuing radical change requires boundless faith in one's convictions against widespread skepticism. Rapid growth requires a pace and intensity of work which not everyone can or is willing to sustain. Secondly, these four factors make managing an entrepreneurial venture dramatically different from working in a large established company. For example, large companies almost always look for opportunities that "fit" their existing capabilities. Entrepreneurs consider most constraints as inconveniences to be overcome, not a reason to be restrained. In other words, entrepreneurs are "opportunity driven" while established businesses are "resource/capability driven."

To sum-up the course seeks to provide insights on the following issues:

- **What are the challenges of financing a new venture? How can these be addressed?**
- **Who provides capital to entrepreneurs? What do these investors expect?**
- **What are the key challenges in achieving growth of an entrepreneurial venture?**
- **How and when should a successful venture be sold to generate cash for the founder(s) and financiers?**

Pre-requisite Coursework:

None – It is recommended that you have a good grasp of financial statements and valuation techniques.

Required Materials (books, course packs, readings, other materials)

1. Course Packet (CP): All cases and background reading would be available on Harvard Business School Publishing (HBSP) Website. **I will provide the URL link and you have to register and pay for the course material directly to HBSP.**
2. You must also have a Financial Calculator and know how to use it.

Academic Integrity

All students are responsible for adhering to the guidelines for University of Basel.

Grading Components:

The grade structure of this course is geared towards helping you achieve the goals of the course. The evaluation philosophy is to provide you with constant feedback. You will have an opportunity to demonstrate your understanding of key concepts in every class session through class participation. You will also get multiple opportunities (Case discussions and polls, Quizz1, and a Final Exam) to show your problem solving skills. My hope is that this grading structure is constructive in that it allows you to act on specific areas that can impact your final grade.

Class Participation	20%
Case Polls (These are Google Polls due by 7:00 AM on date of class)	10%
In-Class Quiz	20%
In-Class Final Exam	50%

Expectations for the Class Participation

The expectations for this course are influenced by the fact that the course relies heavily on the use of case studies for course content and the case method teaching approach for classroom process. **Note that these expectations may differ sharply from those you have experienced with other courses at WWZ and UniBasel.** To get the maximum value out of this course (and to get a good grade), we expect you to be committed to the ``Three Ps" of student involvement in case discussions:

1. **Preparation:** Preparation for each class is critical, including careful reading of the assigned case and background materials, and rigorous analysis based on the assignment questions. I encourage preparation in study groups as a means for enriching the learning experience. I will assume that every student has prepared the day's assignment prior to class. For some sessions (including for the first session) you are required to complete an online survey related to the case. The deadline for completeing this survey is 7:00 AM of the day the case is scheduled to be discussed. (I use the data from your responses to shape the case discussion – so I need to have this data ahead of time).
2. **Presence:** In case method pedagogy, class attendance is critical to individual and collective learning. My expectation is that every student attends every class and arrives on time for each session. Since emergencies will arise on occasion, we expect that anyone who cannot attend class for any reason will contact me in advance, if at all possible. Prior notice is critical since I often plan to call on specific students in connection with particular cases/class sessions in the course. Absenteeism and lateness to class count heavily against the class participation grade since they adversely impact the learning of the section as a

whole.

3. **Participation:** Active and thoughtful class participation will be critical to your learning and the learning of your classmates. I typically cold call one student to start each class discussion and will cold call others throughout the discussion. Class participation accounts for a significant portion of the total grade in the course (20%). In evaluating class participation, I will consider both quality and frequency of contributions, with emphasis on the former. In assessing quality, I consider the following types of issues:

- Does the comment simply repeat facts from the case, or does it provide analysis that adds to our understanding of the case and its broader implications?
- Does the comment fit well into the flow of the discussion? Is it linked to the comments of others?
- Is the comment presented in a clear, compelling manner or is it confusing, repetitive or contradictory?
- Is the comment communicated well. Is there confidence in your voice and mannerisms?

In making my overall assessment of class participation, the overarching criterion is "how significantly does this student's participation contribute to the learning of the section as a whole?"

What if I get the "Wrong Answer"? Finance is a quantitative field and most cases will require extensive computations. That does not mean that each case has one RIGHT answer. Cases frequently provide limited or conflicting information just as in real life. As decision makers you would be expected to exercise judgement and make assumptions to get all the inputs for your estimation models. People will differ in making these judgement calls (as they should) and will reach different conclusions. Your class participation will NOT depend on **what number** you came up with - however it WILL depend critically on **how you got the number you got**. Of course not having a number at all would be taken as lack of preparation and a serious breach of expectations!

Expectations for the case polls

Each student must complete various online polls that are due by 7:00 AM on the day of the class. **YOU WILL NOT BE ABLE TO SUBMIT YOUR RESPONSES AFTER THIS CUT-OFF TIME. I expect that you will complete these polls based on your individual work and you should not discuss or share your responses with any other individual.** These polls require you to answer questions related to cases we will be discussing.

Expectations for in-class quizzes

The one quiz is scheduled for **Monday July 8th**.

Expectations for Final Exam

The final exam is a 1.5 hour in-class exam scheduled for **Monday, July 15th** .

Honor Code

You are encouraged to discuss cases and readings among yourselves as part of class preparation and review. However, all written assignments should reflect work on the part of the individual student. If you have discussed the assignment with other individuals, please indicate this by listing them individually in a footnote on the title page. **YOU MUST NOT SHARE YOUR SOLVED WORK WITH OTHER STUDENT.** Plagiarism is unacceptable and will be considered a grave breach of academic integrity.

Logistics: Contact Information, Textbooks, Course Calendar etc.

Key Information

You can access the course web site through the Summer School Program website.

Textbook and Course Packet

A Course reader would be available for purchase, which would include all the background reading and cases (details are provided below). I shall post the class notes and supporting excel files on Summer School Program's website for this course. You must also have a Financial Calculator and know how to use it.

The course will use Harvard Business School Publishing (HBSP) extensively. All cases needed for this course are available for purchase from Harvard Business School Publishing (HBSP) from the link provided above. The directions for purchasing the course pack are

1. You need to register on the site to create a user name if you do not already have one.
2. After you register, you MUST return to click on the link provided.

Coursepack link: <https://hbsp.harvard.edu/import/612404>

Reading and Case List

1. PunchTab inc (HBS Case 9-812-033)
2. Angels vs. Venture Capitalists*
3. Tire City (HBS Case 9-297-091)
4. Note on Working Capital*
5. Note on DCF Valuation*
6. Academic paper by Stanley Block on Discount for Private Companies*
7. The Basic Venture Capital Formula (HBS case 9-804-042)*
8. Outreach Networks: First Venture Round (UVA case #6569)
9. That Thing Venture Capitalists Do*
10. Convertible Notes in Seed Financing (HBS Case 9-813-017)
11. WebTracker (HBS Case 9-915-543)
12. inge watertechnologies, GmbH (HBS Case 9-812-002)
13. Snap Inc.'s IPO (HBS Case 9-218-006)

*Available for download at the course website. (ADAM)

Course Calendar

	Date	Topic	Background Reading	Case Assignment
1	Monday, July 1, 2019	Introduction to Financing New Ventures	Angels vs. Venture Capitalists	PunchTab inc (HBS Case 9-812-033)
2	Tuesday, July 2, 2019	Pro-Forma Forecasting	Note on Working Capital	Tire City (HBS Case 9-297-091)
3	Wednesday, July 3, 2019	Working Capital	The Basic Venture Capital Formula (HBS case 9-804-042)	Lecture on VC valuation method
4	Thursday, July 4, 2019	VC Valuation	That Thing Venture Capitalists Do	Outreach Networks: First Venture Round (UVA case #6569)
5	Monday, July 8, 2019	Convertible Notes, Preferred Stock	Convertible Notes in Seed Financing (HBS Case 9-813-017)	In-class Quiz Lecture
6	Tuesday, July 9, 2017	Deal Terms		WebTracker (HBS Case 9-915-543)
7	Wednesday, July 10, 2019	Harvesting – Trade Sale		inge watertechnologies, GmbH (HBS Case 9-812-002)
8	Thursday, July 11, 2019	Harvesting - IPO		Snap Inc.'s IPO (HBS Case 9-218-006)