Venture Capital Management: Opportunity and Challenges for Entrepreneurs

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Abstract:

Present study is based on venture capital management and explained how its modern tool for women empowerment. Venture capital is a type of funding for a new or growing business. It usually comes from venture capital firms that specialize in building high risk financial portfolios. With venture capital, the venture capital firm gives funding to the startup company inexchange for equity in the startup. This is most commonly found in high growth technology industries like biotech and software. A person who deals in venture capital is a venture capitalist, and usually works for a venture capital firm. The firm typically has one or more investment portfolios that are owned by a limited partnership. The venture capitalist is often a general partner in the portfolio, and individual investors or other institutions particularly university endowments and pension funds are limited partners in the limited partnership. This paper includes, meaning, method, features of venture capital investments, financing, methods of venture capital the funding process, advantages of venture capital, disadvantages of venture capital, exit route, venture capital funding, venture capital vs loans, venture capital vs angel investing and seed financing, venture capital vs crowd funding. Keywords: Angel, Investment, Capital, Equity and Start up Background: Venture Capital has emerged as a new one.

Introduction:

Background- Venture Capital has emerged as a new financial method of financing during the 20th century. Venture capital is the capital provided by firms of professionals who invest alongside management in young, rapidly growing or changing companies that have the potential for high growth. Venture capital is a form of equity financing especially designed for funding high risk and high reward projects. It is a private or institutional investment made into early-stage / start-up companies (new ventures). As defined, ventures involve risk (having uncertain outcome) in the expectation of a sizeable gain. Venture Capital is money invested in businesses that are small; or exist only as an initiative, but have huge potential to grow. The people who invest this money are called venture capitalists (VCs). The venture capital investment is made when a venture capitalist buys shares of such a company and becomes a financial partner in the business. Venture Capital investment is also referred to risk capital or patient risk capital, as it includes the risk of losing the money if the venture doesn't succeed and takes medium to long term period for the investments to fructify. Venture Capital typically comes from institutional investors and high net worth individuals and is pooled together by dedicated investment firms. It is the money provided by an outside investor to finance a new, growing, or troubled business. The venture capitalist provides the funding knowing that there’s a significant risk associated with the company’s future profits and cash flow.
Capital is invested in exchange for an equity stake in the business rather than given as a loan. Venture Capital is the most suitable option for funding a costly capital source for companies and most for businesses having large up-front capital requirements which have no other cheap alternatives. Software and other intellectual property are generally the most common cases whose value is unproven. That is why; Venture capital funding is most widespread in the fast-growing technology and biotechnology fields. Capital budgeting and capital structures are associated with investment decisions while working capital management is the functional area of finance. It involves the relationship between a firm’s short term assets and its short term liabilities like managing inventories, accounts receivable and payable, and cash (Gitman, 2005; Babu & Chalam 2014.

Features of Venture Capital investments

- High Risk
- Lack of Liquidity
- Long term horizon
- Equity participation and capital gains
- Venture capital investments are made in innovative projects
- Suppliers of venture capital participate in the management of the company

Methods of Venture capital financing

- Equity
- Participating debentures
- Conditional loan

The Funding Process:

Approaching a Venture Capital for funding as a Company. The venture capital funding processtypically involves four phases in the company's development:

- Idea generation
- Start-up
- Ramp up
- Exit

Step 1: Idea generation and submission of the Business Plan: The initial step in approaching aVenture Capital is to submit a business plan. The plan should include the Jutabelow points:

There should be an executive summary of the business proposal Description of the opportunity and the market potential and size Review on the existing and expected competitive scenario Detailed financial projections

Details of the management of the company

There is detailed analysis done of the submitted plan, by the Venture Capital to decide whetherto take up the project or no.

Step 2: Introductory Meeting: Once the preliminary study is done by the VC and they find the project as per their preferences, there is a one-to-one meeting that is called for discussing the project in detail. After the meeting the VC finally decides whether or not to move forward to thedue diligence stage of the process.

Step 3: Due Diligence: The due diligence phase varies depending upon the nature of the business proposal. This process involves solving of queries related to customer references, product and business strategy evaluations, management interviews, and other such exchangesof information during this time period.

Step 4: Term Sheets and Funding: If the due diligence phase is satisfactory, the VC offers a termsheet, which is a non-binding document explaining the basic terms and conditions of the investment agreement. The term sheet is generally negotiable and must be agreed upon by all parties, after which on completion of legal documents and legal due diligence, funds are made available.

Types of Venture Capital funding:

The various types of venture capital are classified as per their applications at various stages of a business. The three principal types of venture capital are early stage financing, expansion financing and acquisition/buyout financing. The venture capital funding procedure gets complete in six stages of financing corresponding to the periods of a company's development

Seed money: Low level financing for proving and fructifying a new idea

Start-up: New firms needing funds for expenses related with marketing and productdevelopment

First-Round: Manufacturing and early sales funding

Second-Round: Operational capital given for early stage companies which are selling products,but not returning a profit

Third-Round: Also known as Mezzanine financing, this is the money for expanding a newlybeneficial company

Fourth-Round: Also called bridge financing, 4th round is proposed for financing the "goingpublic" process

***A)* Early Stage Financing:** Early stage financing has three sub divisions seed financing, start upfinancing and first stage financing.

Seed financing is defined as a small amount that an entrepreneur receives for the purpose ofbeing eligible for a start up loan.

Start up financing is given to companies for the purpose of finishing the development ofproducts and services.

First Stage financing: Companies that have spent all their starting capital and need finance forbeginning business activities at the full-scale are the major beneficiaries of the

***B)* First Stage Financing:** Expansion Financing: Expansion financing may be categorized into second-stage financing, bridge financing and third stage financing or mezzanine financing.

***C)* Second-stage financing:** is provided to companies for the purpose of beginning their expansion. It is also known as mezzanine financing. It is provided for the purpose of assisting a particular company to expand in a major way. Bridge financing may be provided as a short term interest only finance option as well as a form of monetary assistance to companies that employthe initial public offers as a major business strategy.

***D)* Acquisition or Buyout Financing**: Acquisition or buyout financing is categorized into acquisition finance and management or leveraged buyout financing. Acquisition financing assists a company to acquire certain parts or an entire company. Management or leveraged buyout financing helps a particular management group to obtain a particular product of anothercompany.

Advantages of Venture Capital

They bring wealth and expertise to the companyLarge sum of equity

finance can be provided

The business does not stand the obligation to repay the money

In addition to capital, it provides valuable information, resources, technical assistance to makea business successful

Disadvantages of Venture Capital

As the investors become part owners, the autonomy and control of the founder is lost

It is a lengthy and complex process It is an uncertain

form of financing

Benefit from such financing can be realized in long run only

Exit route: There are various exit options for Venture Capital to cash out their investment:IPO

Promoter buyback Mergers and

Acquisitions

Sale to other strategic investor Examples of venture

capital funding

Kohlberg Kravis & Roberts (KKR), one of the top-tier alternative investment asset managers in the world, has entered into a definitive agreement to invest USD150 million (Rs 962crore) in Mumbai-based listed polyester maker JBF Industries Ltd. The firm will acquire 20% stake in JBF Industries and will also invest in zero-coupon compulsorily convertible preference shares with 14.5% voting rights in its Singapore-based wholly owned subsidiary JBF Global Pte Ltd. The funding provided by KKR will help JBF complete the ongoing projects.

Pepperfry.com, India's largest furniture e-marketplace, has raised USD100 million in a fresh round of funding led by Goldman Sachs and Zodius Technology Fund. Pepperfry will use the funds to expand its footprint in Tier III and Tier IV cities by adding to its growing fleet of deliveryvehicles. It will also open new distribution centres and expand its carpenter and assembly service network. This is the largest quantum of investment raised by a sector focused e- commerce player in India.

Comparison of VCM:

Venture Capital vs Loans: Although loans and venture capital are both common methods for funding businesses, venture capital is very different from a loan. With a loan, a lender gives company money, and the company has a contractual obligation to pay back that amount plus interest over some period of time. Sometimes the loan is backed by assets (like equipment or inventory) or receivables. In the case of many small businesses, the loan is backed by a personal guarantee from the business owner. This backing allows the lender to recoup some of its investment in case the lendee defaults (fails to make payments). With venture capital, the startup company issues private shares in exchange for money. The venture capitalists partnership fund actually becomes a partial owner of the startup.

Additionally, venture capital is usually only used with high growth industries, where risk is much higher. In these cases, there are little or no assets to back the loan in the event of default so the likelihood of obtaining a loan is much lower, and the potential payouts must be drasticallyhigher to result in a successful investment.

Venture Capital vs Angel Investing & Seed Financing: The primary differences between VC vs seed & angel investing are timing in the company's lifecycle, monetary size, and deal structure.Timing, Venture capital is typically not used for extremely early funding. Instead, these rounds are often called "Series AA," or "Pre-A" rounds, and include funding from friends & family, angel investors, and seed stage financing syndicates and firms. Venture capital firms usually get involved at the Series A round and after (all happening after the AA or Pre-A rounds). Although both VC and seed/angel investing are high risk investments, seed & angel investing usually happen in the earliest stages of a startup when the risk is ultra-high.

Funding Amounts. Venture capital also usually starts with companies that are slightly more mature (although not necessarily profitable), with higher valuations, and higher funding amounts. Funding amounts in angel & seed investing typically range from a couple thousand USD through to one million USD, while venture capital is usually millions, tens of

millions, or even hundreds of millions of dollars.

Deal Structure. Angel investing also frequently uses different deal structures than VC, although this is primarily to reduce legal costs, cut transaction overhead, and rapidly accelerate the rate at which the startup and angel investor can agree on terms. Some of these alternative structures include convertible notes and SAFEs ("simple agreement for future equity"). Unlike venture capital, convertible notes and SAFEs don't actually transfer equity in the company to the investor until a later date, and in the case of failed start ups, sometimes not even at all.

Venture Capital vs Crowd funding: The primary difference between venture capital and crowd funding is simply equity. Venture capitalists acquire equity in the startup. Crowd funders do not. Instead, crowd funding is much more like a high-risk pre-order platform, where there's a reasonable probability that the startup may fail to deliver the pre-order.Who Has Control of the Company When a VC Investor Is Involved? - VC financing is a poor choice for entrepreneurs who wish to retain control of their business. In exchange for providing funding most VC firms obtain majority voting rights by having the majority of the shares (or a preferred class of shares that are senior to common shares), as well as special veto rights. VC investments are often structured so that in the case of a share sale the VC investors have priority rights in terms of compensation. How Hard Is It to Get Venture Capital Funding for a Business?: Unfortunately the vast majority of businesses do not qualify for venture capital funding. VC firms are very choosy about the businesses they invest in - according to the U.S. Small Business Administration less than .1% of businesses are funded by venture capital. Of the few that are able to obtain VC funding, almost all are firms that are past the startup stage and can demonstrate a viable product or service. The vast majority of new business seed money still comes from the business owner themselves or from angel investors.

Conclusion:

Considering the high risk involved in the venture capital investments complimenting the high returns expected, one should do a thorough study of the project being considered, weighing the risk return ratio expected. One needs to do the homework both on the Venture Capital being targeted and on the business requirements. Startup or growth equity capital or loan capital provided by private investors (the venture capitalists) or specialized financial institutions (development finance houses or venture capital firms). Venture capital isa type of funding for a new or growing business. It usually comes from venture capital firms that specialize in building high risk financial portfolios. With venture capital, the venture capital firm gives funding to the startup company in exchange for equity in the startup. This is most commonly found in high growth technology industries like biotech and software. A person who deals in venture capital isa venture capitalist, and usually works for a venture capital firm. The firm typically has one or more investment portfolios that are owned by a limited partnership. The venture capitalist is often a general partner in the portfolio, and individual investors or other institutions particularly university endowments and pension funds are limited partners in the limited partnership.

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