BRANSTON

E-comm strategy & finance

Valuing non-public entities

Valuing non-public entities

- Outline
- 3 methods
- Working with management
- Case study exercise

Income

Assets

Markets & Transactions

Hybrids

Sum Of The Parts

Sense checks

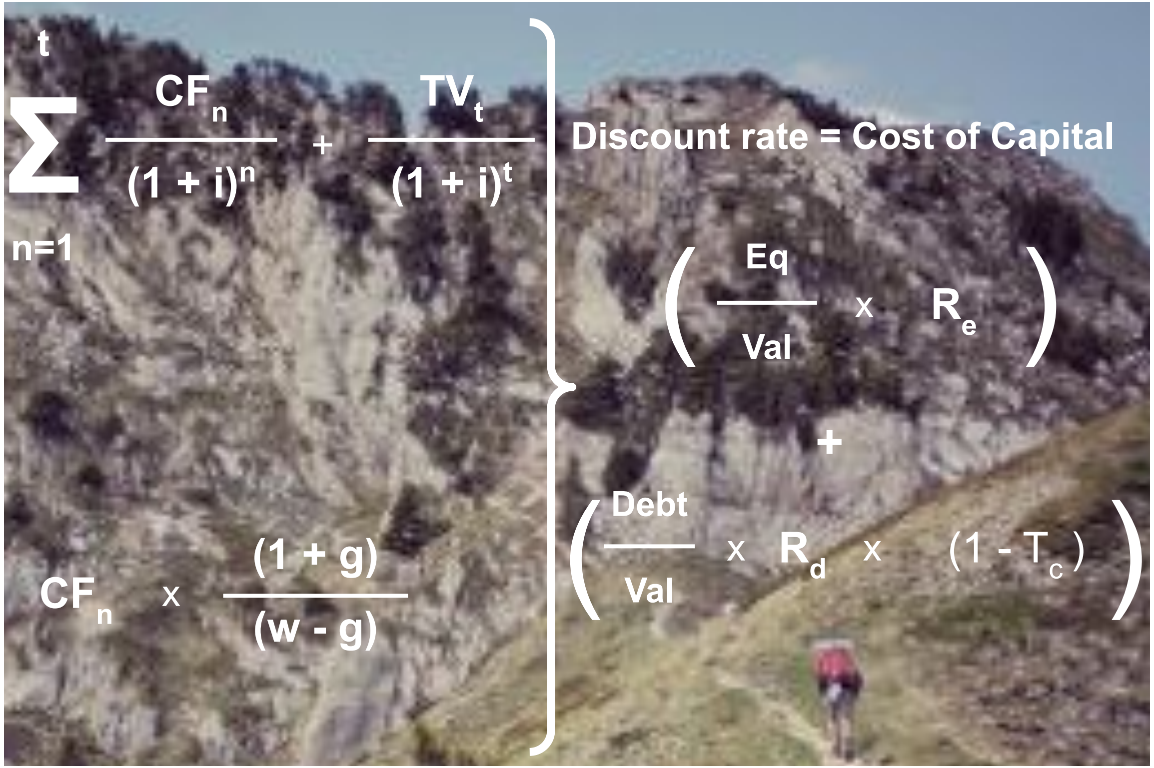
Programme outline

Trainee objectives	Adapt methodology for private company challenges	Engage appropriately with company management	Sense check the results
Content & Discussion	Critique of the 3 methods	Reflections on management engagement & ‘down rounds’	Worked case examples
Private company stereotype	Small Early stage High growth	Simple structure Few product lines	Low quality, short-term financial data
Student stereotype	Familiar with P & L, Balance Sheet, Cash Flow	Basic modelling and valuation skills	Focus is not valuation per se, rather how to apply to private companies

Income methods

Discounted Cash Flow

Early stage	Not yet at steady growth	Terminal value arbitrary yet large
Mature stage	Steady state growth	Unlikely for an emerging private business



$$\sum_{n=1}^{t} \frac{CF_n}{(1 + i)^n} + \frac{TV_t}{(1 + i)^t}$$

Discount rate = Cost of Capital

$$\left(\frac{Eq}{Val} \times R_e \right) + \left(\frac{Debt}{Val} \times R_d \times (1 - T_c) \right)$$

$$CF_n \times \frac{(1 + g)}{(w - g)}$$

Markets methods

Valuation multiples (public)

Revenue multiple

- Pre-profit OR Valued for customer contracts only
- Incentive to overspend on customer acquisition
- Total ? Core ? Recurring ?

Profit multiple

- If profitable
- Proxy (smoothed) for cash flow
- EBITDA ? PBT ? PAT ?

Business comparability is never perfect

Share price volatility …smooth it?

Precedent corporate transactions

Represent ative ?

- Transaction multiples highly cyclical
- Low transaction volumes during global share price weakness

Credible ?

- 100% comparability never occurs
- Arms length test

Lifecycle stage never matches comparators

Valuation premium for strong execution

Assets methods

Assets' saleable values

Relationship to business operations

No value for deploying the assets to generate profits

Premise of value:
going concern?
liquidation ?
collection of assets ?

Valuation evidence

Labour-intensive calculations
Can be arbitrary
Based on illiquid markets

Information businesses (e.g. e-commerce) have negligible assets

Work with management on contentious assumptions

Inputs	Modelling inputs: e.g. online customer acquisition & renewal rates	How achievable are revenue growth projections ?	Extra spending needed in order to reach scale?
Normalising	Longer projection period needed to reach steady state growth?	EBITDA as proxy for Cash Flow, to normalise Working Capital swings?	Multiples: how credible is the read-across from incumbents to innovative challengers ?
Fine tuning	Add in non-core assets and equity investments	Positioning net debt / cash Equity value - Net Cash = Enterprise Value counter-intuitive to a founder	Post-money = pre-money + invested equity

Down Rounds - Could valuations have been done better?

VC VALUATIONS

Norway's Oda loses unicorn status with new round

FORTUNE RANKINGS MAGAZINE NEWSLETTERS PODCASTS MORE

FINANCE · STRIPE

Why a Stripe down round would be a 'good startups, according to one VC

REUTERS® World Business Legal Markets Breakingviews Technology Investigations

Business

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Dreaded 'down rounds' shave billions off startup valuations

By Manya Saini

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Shein to close new funding round at lower valuation

Axios Pro Exclusive Content

Fintech Varo reportedly seeks funding at lower valuation

Lucinda Shen, author of Axios Pro: Fintech Deals

7 hours ago

Forbes

FORBES > INNOVATION > VENTURE CAPITAL

EDITORS' PICK

Cloud Startup OutSystems' $9.5 Billion Valuation Is Slashed In Half After New Funding Round

Interest rates impacting both costs and DCFs

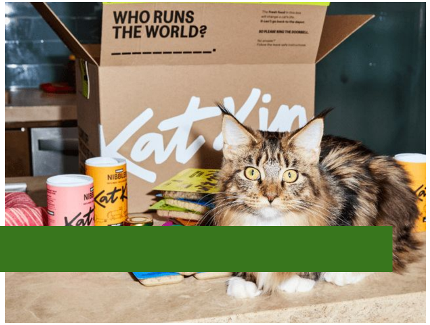
Public markets valuations falling too

Employee options' value loss

More valuation realism to remove stigma?

Case Study 1

Online pet food subscription business



Background	
Description	Manufacture & UK sale of pet food Direct to consumer; online only Monthly renewable subscriptions
Investors	Founders 3 venture capital funds 30 angel investors
Revenue	£10m annualised at December 2022
Capital intensity	High: manufacturing machinery; website
Age	2 years
Reason for valuation	Due diligence to attract new venture capital investors

Valuation	
Amount invested	£10m
Revenue projections	Subscription customer acquisition and retention rates
Cost projections	Unit economics of manufacturing, marketing & distribution Headcount investments to scale the business
Gross Margin	20%
EBITDA Margin	-10%
Debt	£4m venture debt facility, undrawn £3m equipment finance, drawn

- How will you forecast revenue?
- How will you forecast costs?
- What valuation method?
- What will you ask management?
- Cost of Capital
- Sense checks?

Case Study 2

Online gifting marketplace

Background		Valuation	
Description	Marketing and online sale of household goods Intermediary marketplace of 5,000 UK merchants Commissions charged to merchants; no inventory	**Revenue**	£60m annualised at December 2020
Investors	Founders 4 venture capital funds Widespread employee options	**Revenue projections**	Customer frequency and average order value Triangulated against: (i) Channel marketing return on spend (ii) Volume of products sold by active merchants
Amount invested	£220m	**Cost projections**	Online channel marketing Brand marketing Website development
Capital intensity	Low: website and app	**Gross Margin**	75%
Age	7 years	**EBITDA Margin**	10%
Reason for valuation	Venture Capital investors selling stakes to new investors Equity awards valuation report for HMRC	**Debt**	£3m credit facility, undrawn

How will you forecast revenue?

How will you forecast costs?

What valuation method?

What will you ask management?

Cost of Capital

Sense checks?