

Confidential!

The framework of venture capital financing

Some insights for entrepreneurs

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Grazia Equity GmbH, November 2007

AGENDA

- Why should entrepreneurs be interested in Venture Capital?
- How can they secure Venture Capital?
- How should they structure a Venture Capital deal?

Dynamics of high-tech „new businesses“

Fast realisation of business potential but also necessary stamina

- creation and usage of viral effects
- winning of strong reference customers
- fast realisation of economies of scale
- sound financial base and reputation to survive setbacks

High capital requirements led to rise of Venture Capital

Window of opportunity

TIME

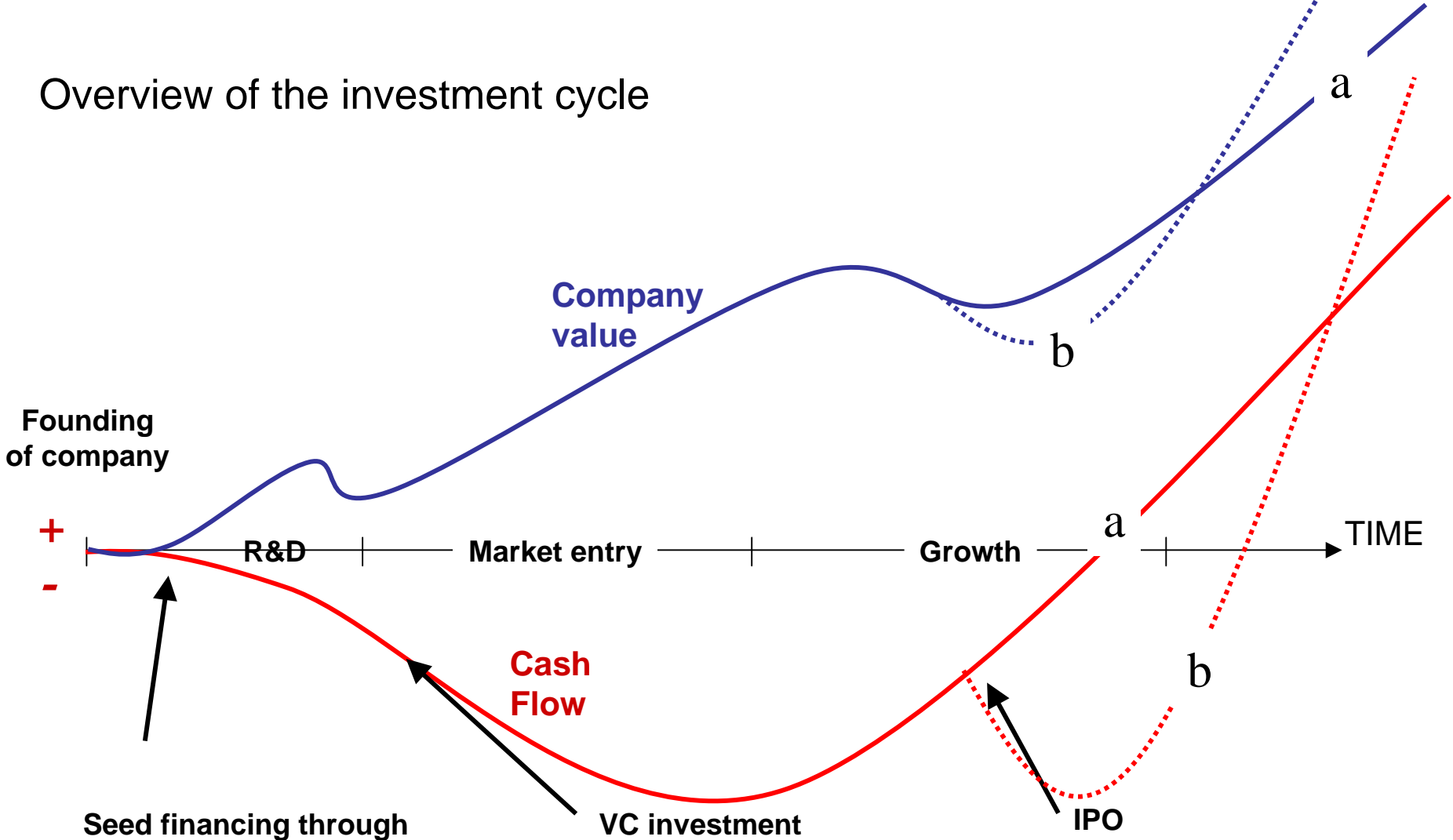
„To be too early“

- mindset of customers has to be changed
- technology is still immature
- bad economic climate

„To be too late“

- Catch-up of incumbents
- Frog-leaping of new entrants
- „Revolution“ of customer needs

Overview of the investment cycle



Seed financing through Business angels

- private investors with often relevant experience
- amounts range from 50 to 500k
- direct coaching of entrepreneurs and business development

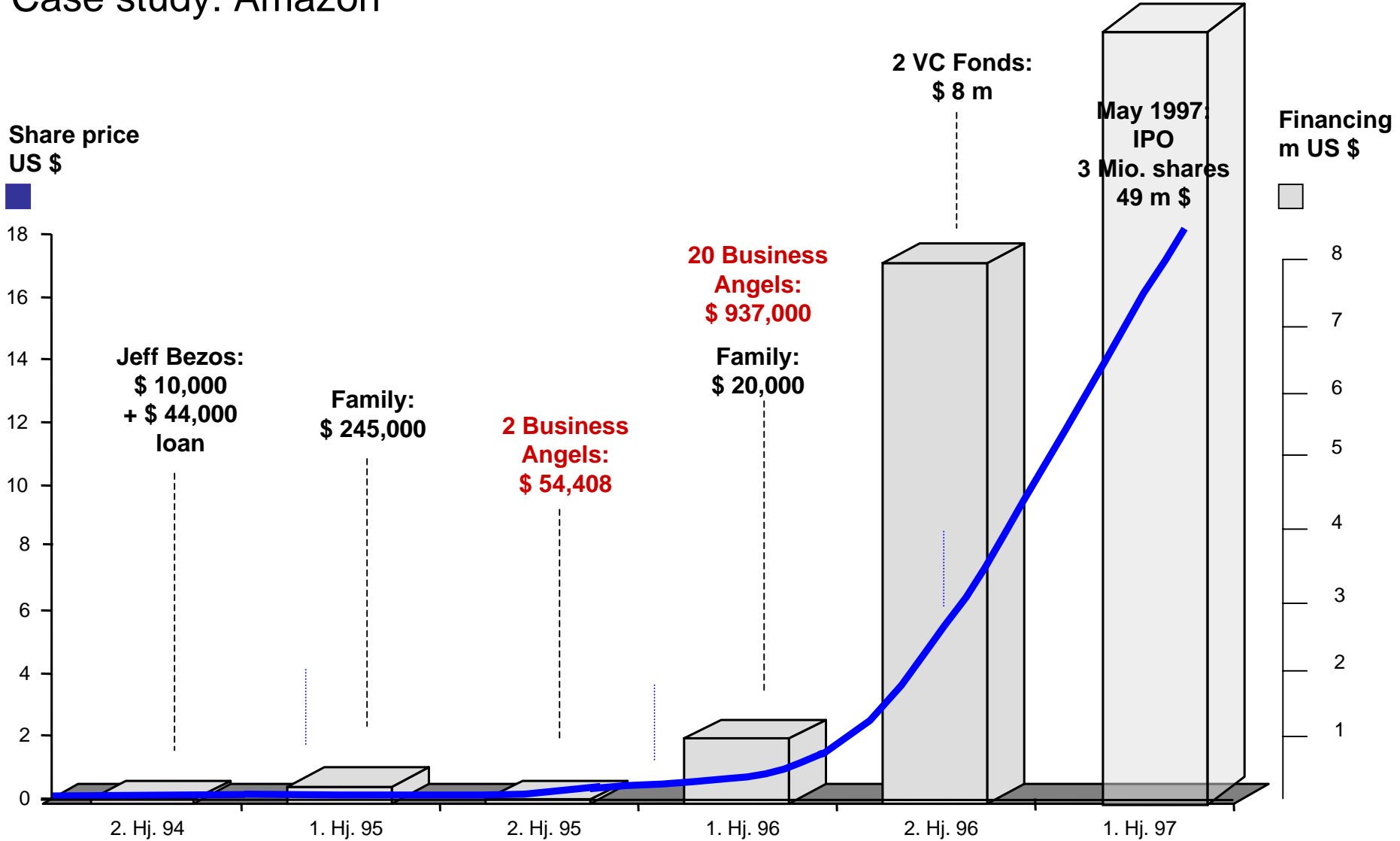
VC investment

- often institutional investors
- they need exit in 5 to 7 years
- Series A of 1-5 Mio €
- Series B of 5-15 Mio. €
- sometimes even Series C of > 20 Mio. €

IPO

- further accelerator
- additional funds with limited dilution
- significant reporting requirements

Case study: Amazon



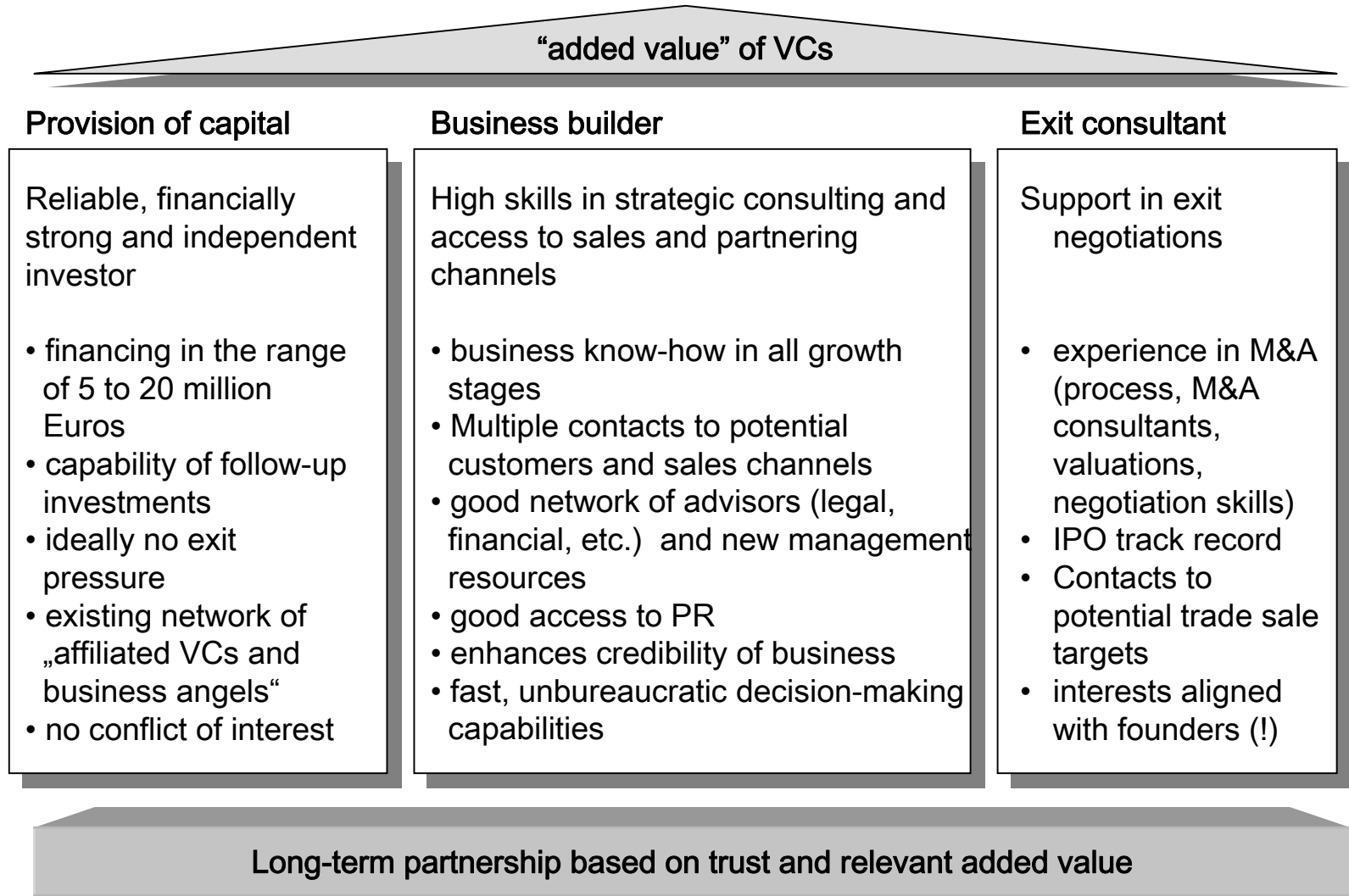
Market cap: 11/15/07: 22.3 m Euro

Source: David Amis/ H. Stevenson: *Winning Angels*

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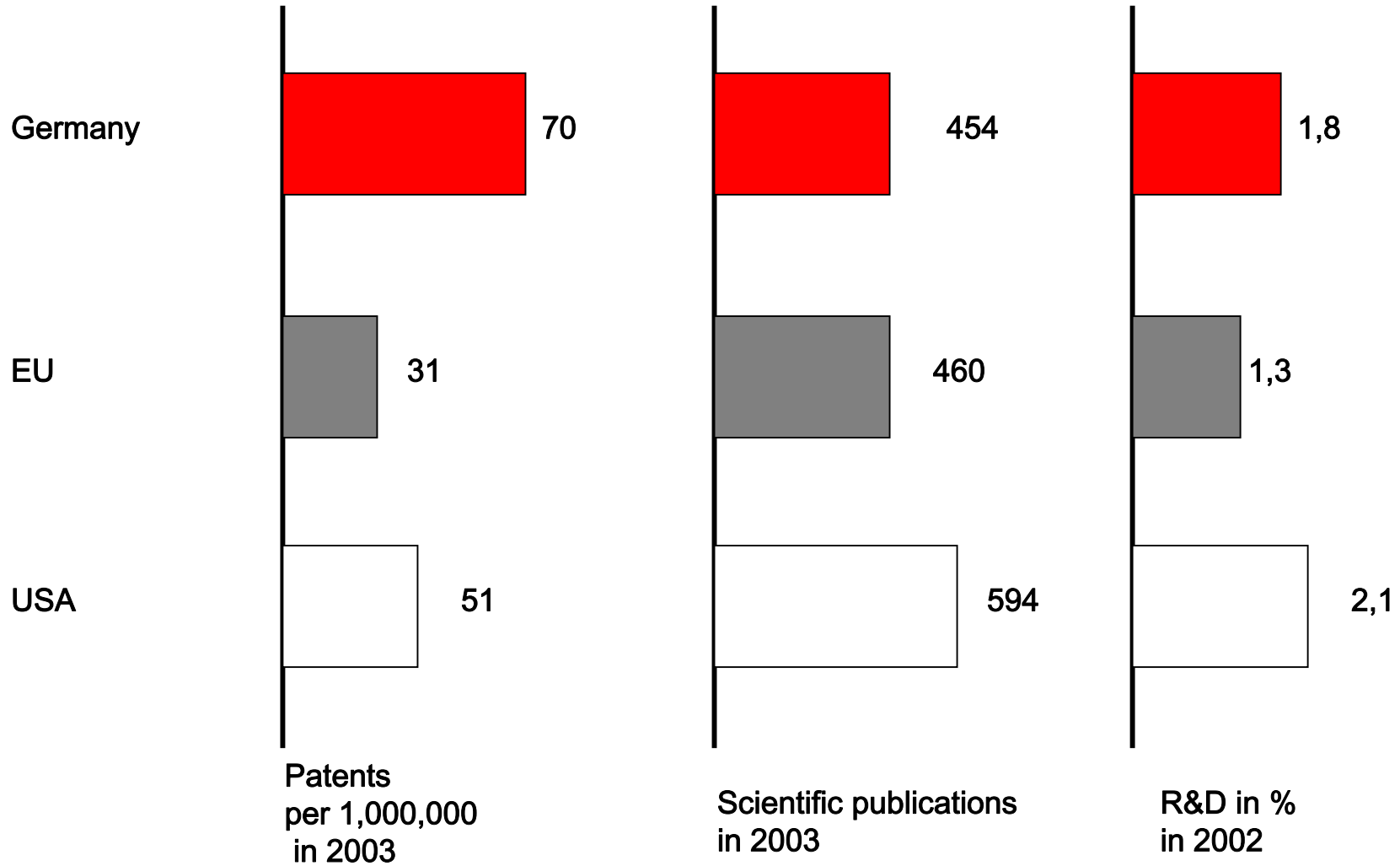
VCs should be a trustful partner and valuable consultant to entrepreneurs

VALUE PROPOSITION OF „VALUE ADD“ VCs

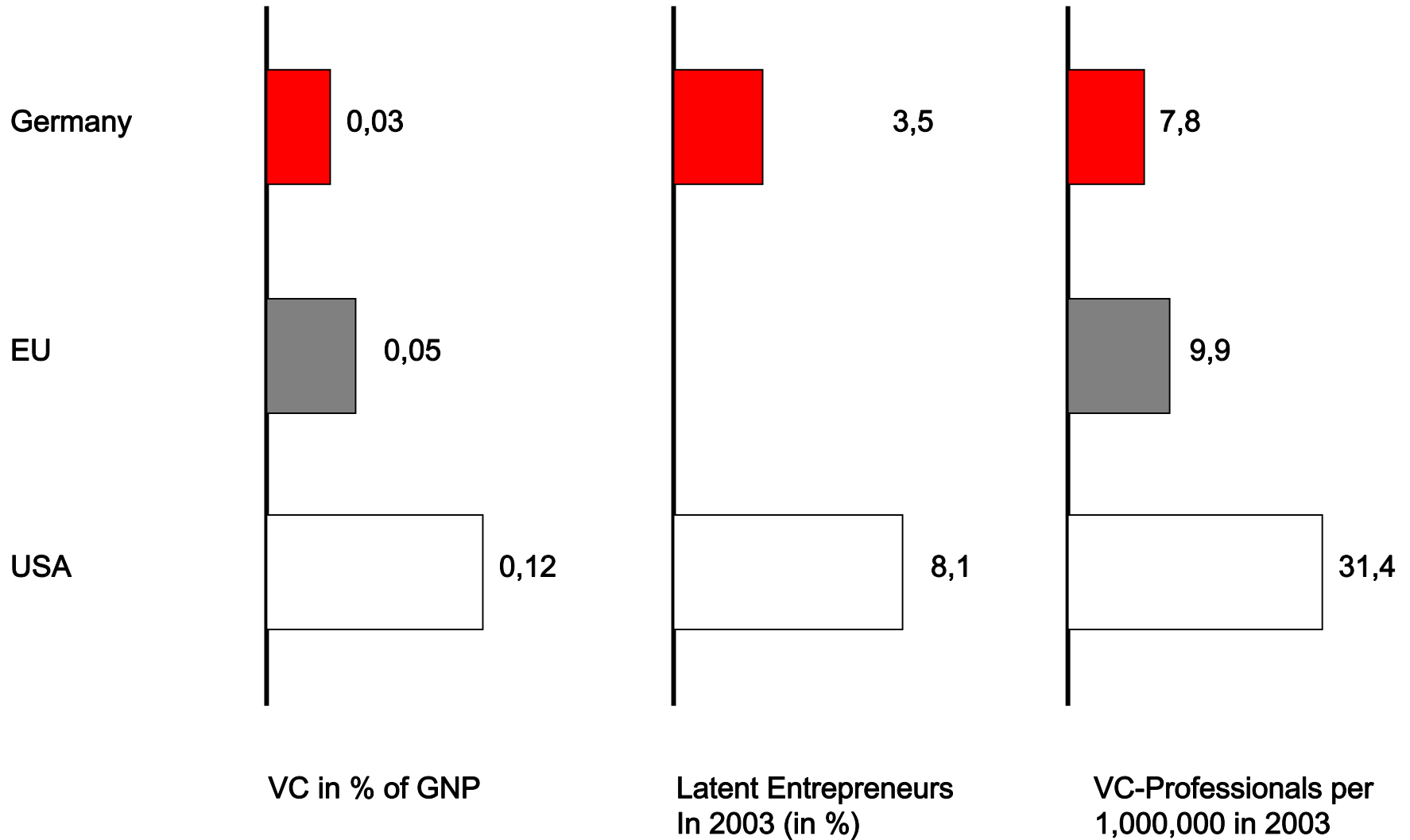


And does it work in Germany ?

GERMANY IS A LEADING TECHNOLOGY NATION...



... BUT NO START-UP NATION

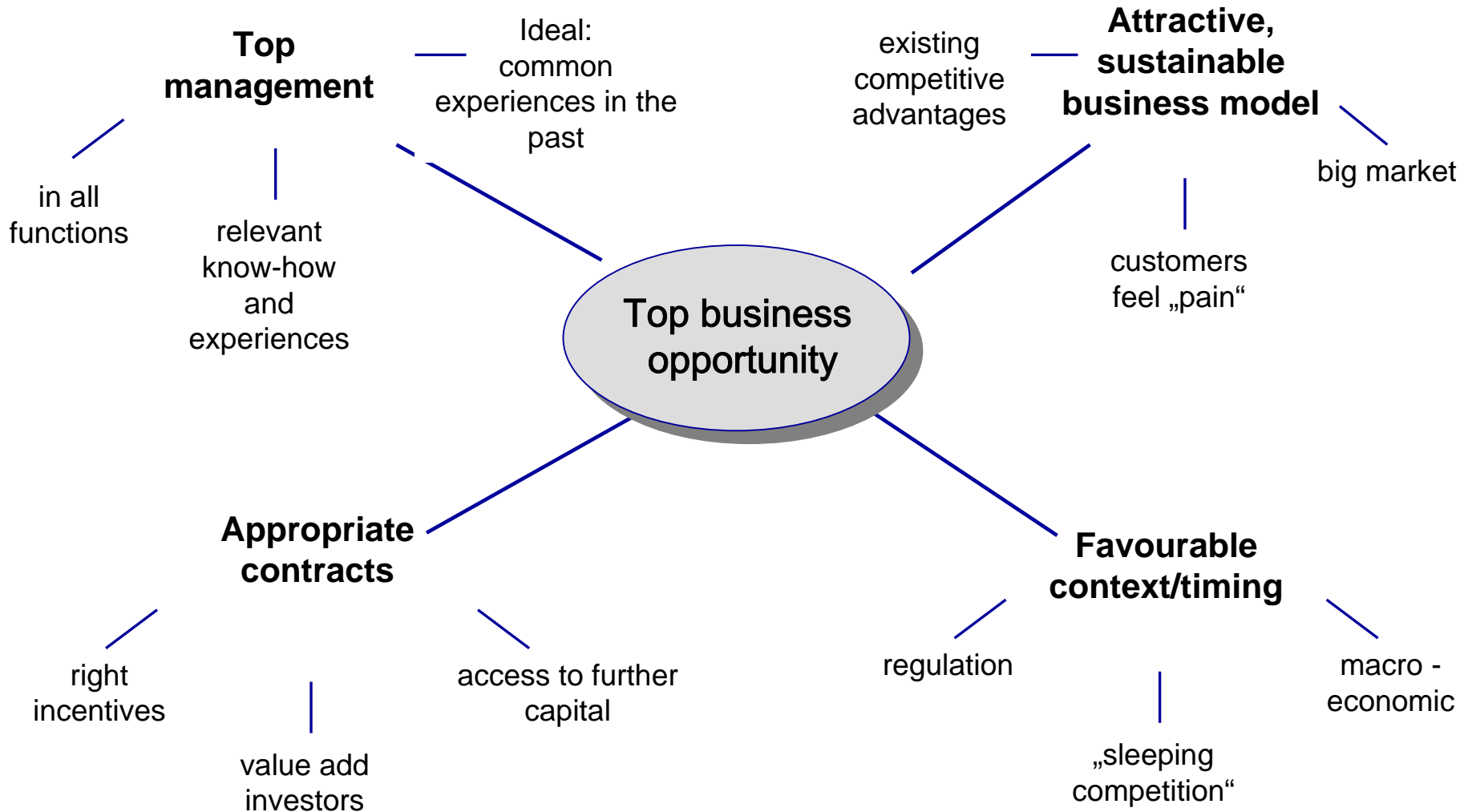


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Entrepreneurs should try to optimize the set-up of their business

CHARACTERISTICS OF TOP VC CASES

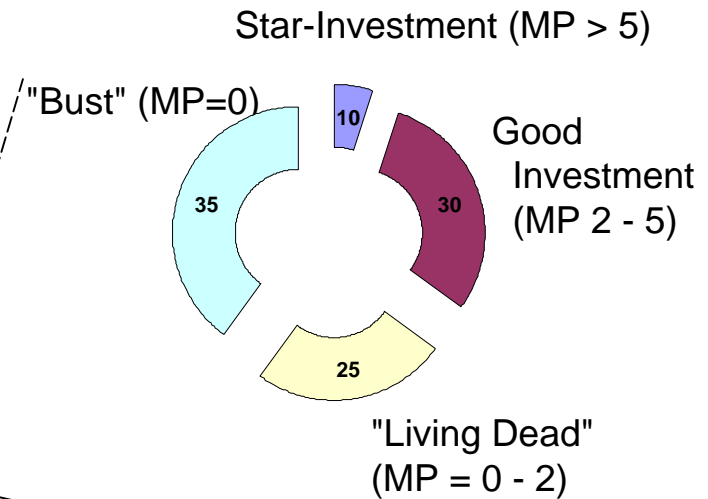
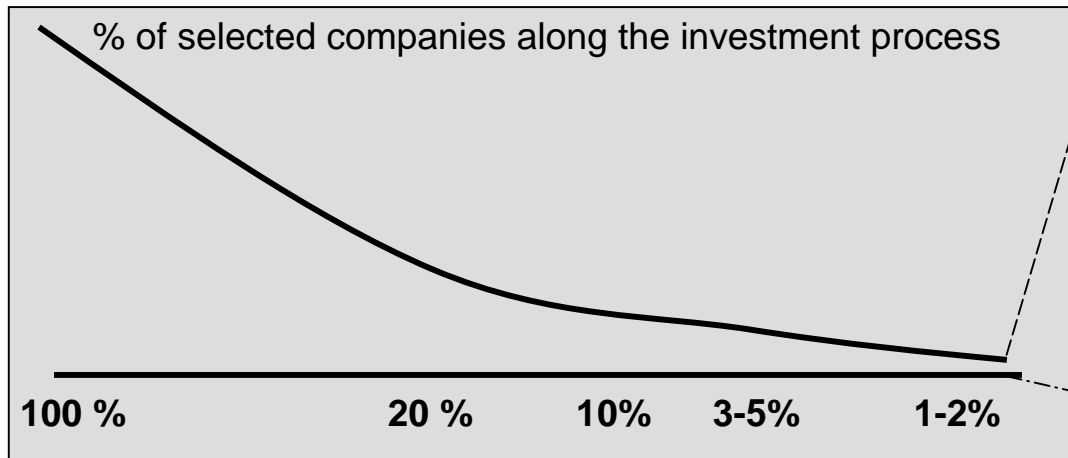


What does this exactly mean for entrepreneurial projects?

NECESSARY REQUIREMENTS FOR VC INVESTMENTS

- Relevant target market should amount to at least 300 to 500 m Euros.
- Company should make into the top 2 with a market share of at least 10%.
- Product/service offering should provide outstanding customer benefits, „twice as fast“, „half as expensive“ are statements that refer to the rule of thumb of „50% improvements (at least)“.
- The business model should be scalable resulting into high sustainable profitability. Scalability refers to increasing profit margins that can be achieved by decreasing customer acquisition cost, increasing purchasing power, viral effects („winner takes it all“).
- Management team must be outstanding (drive, enthusiasm, experience, networks, leadership, ethics, etc.) and almost complete (2 out of 3).
- Most VCs also like to see a „proof of concept“ and first revenues.

To put it into perspective...



- analyzing of BP and management
- belief in idea
- market check
- risk/return evaluation

- first „get-to-know“ meeting
- several follow-up meetings
- reference calls
- „engagement of specialists“
- financial and legal DD

- negotiations of terms
- drafting of contracts
- finding of co-investors
- closing

- controlling of progress
- strategic consulting
- business developm.
- decision-making within SVB

- identification of targets
- support with negotiations
- agreement on exit

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How can I structure a VC deal?

CONDITIONS AND TERMS OF VC INVESTMENT

VC terms

@Closing

- finding the „fair“ valuation
 - DCF ?
 - Multiples?
 - standards?
- warranties
 - extent?
 - cap?
 - minimum threshold ?
- conditions precedent
- no shop agreement, exclusivity
- fee sharing

Lifetime of investment

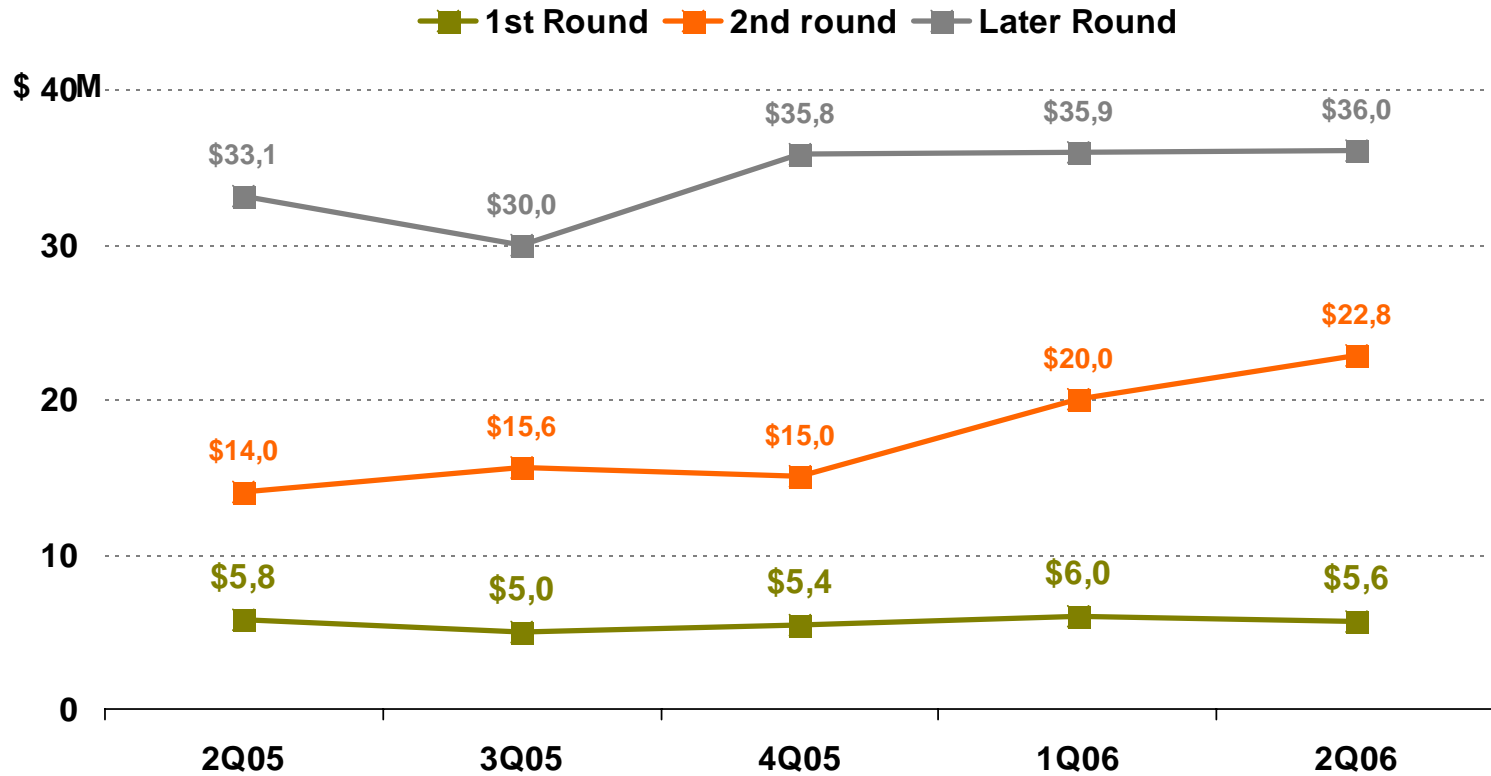
- information rights
- board representation
- veto-rights or matters requiring consent
- down-round protection
 - full-ratchet anti-dilution
 - weighted average anti-dilution
- vesting
- allocation of options

Exit provisions

- restrictions on sale
- right of first refusal
- drag-along agreement
- tag-along agreement, co-sale right
- redemption right
- liquidation preference

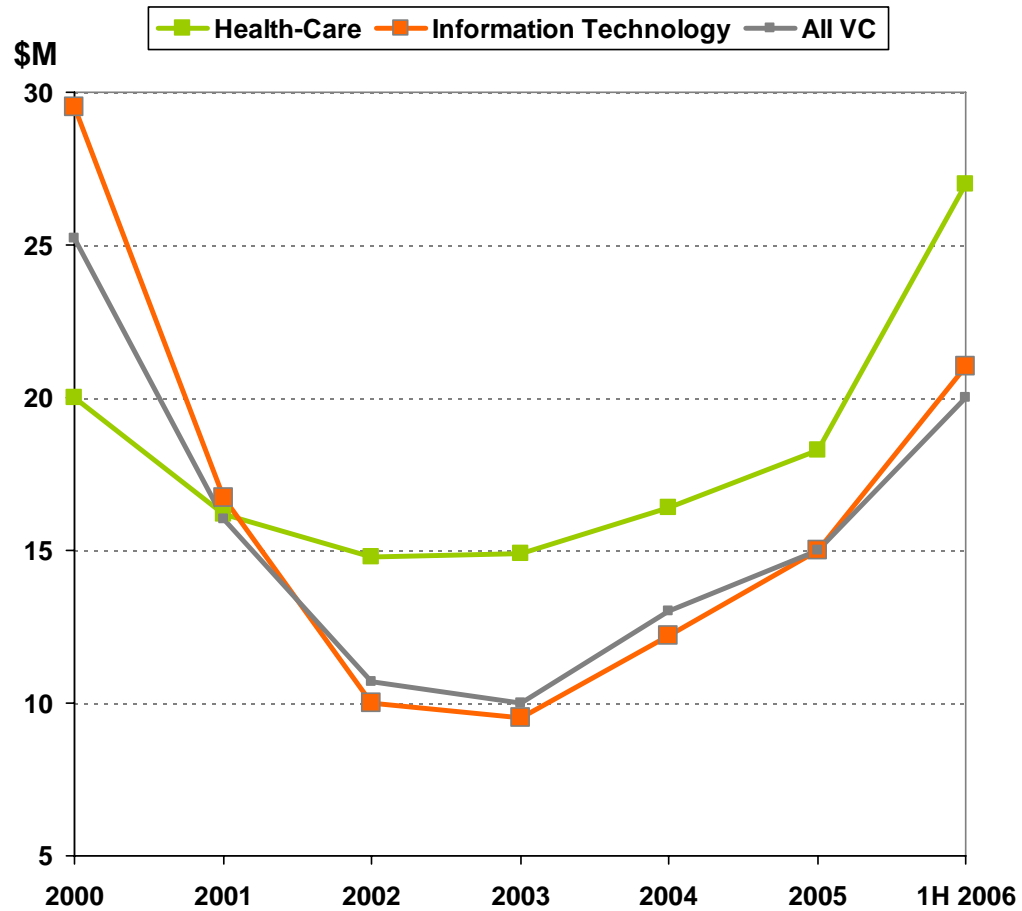
Trust and fairness as underlying principle to generate a „Win-Win Situation“

Median Pre-Money Valuation By Round Class (\$M) 2Q05-2Q06*



*U.S. venture-backed companies only. Source: Dow Jones VentureOne

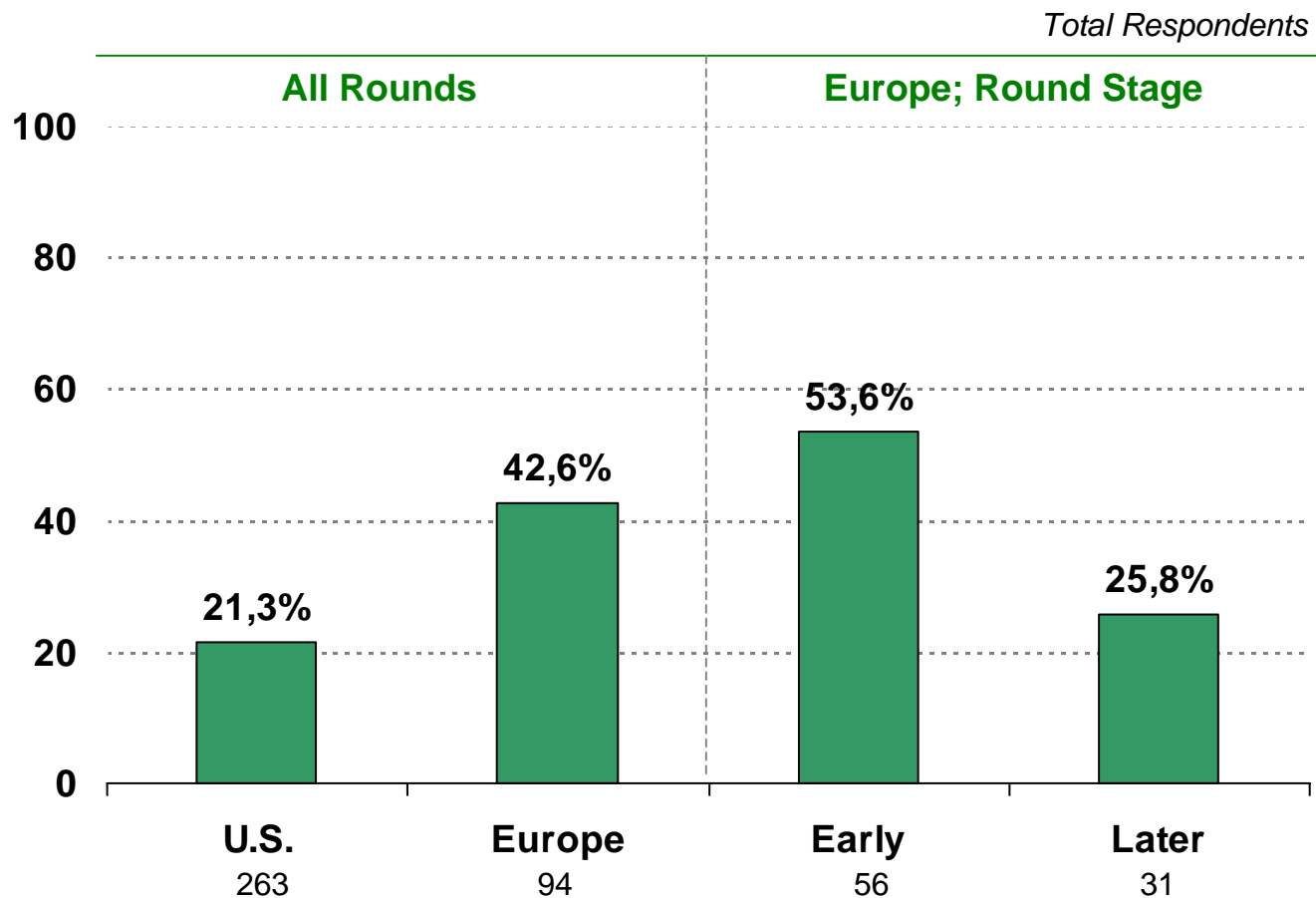
Median pre-money valuation by industry group (\$m) 200-1H 2006 (U.S. ventures-backed only)



Benchmark Percentages Of US Founders' Ownership After Round

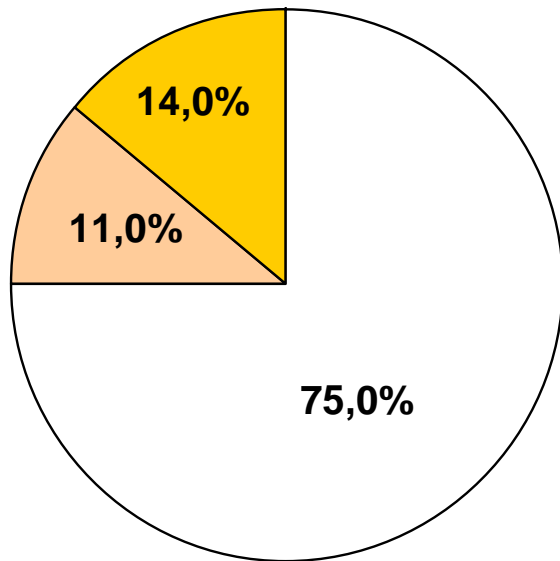
	1st	2nd	3rd & Later
Mean	35	16.3	12.1
Median	31.5	15	10
Minimum	4	0	10
Maximum	91.5	50	60
25th Percentile	20	9	4
75th Percentile	50.3	22	15
Total Respondents	98	66	79

U.S. & Europe: Capital raised paid to company in stages

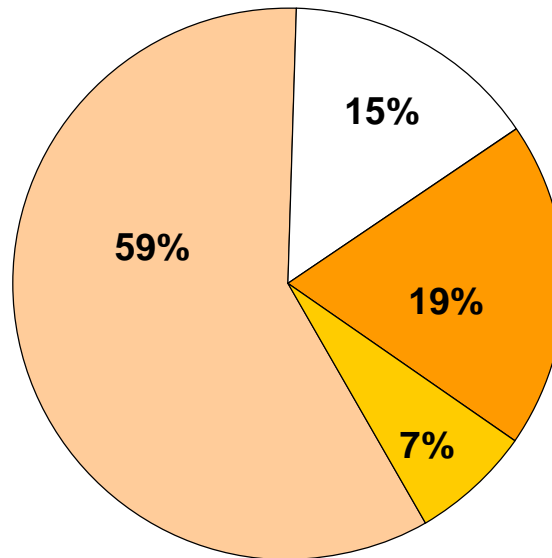


Who controlled the board? (100 respondents in %)

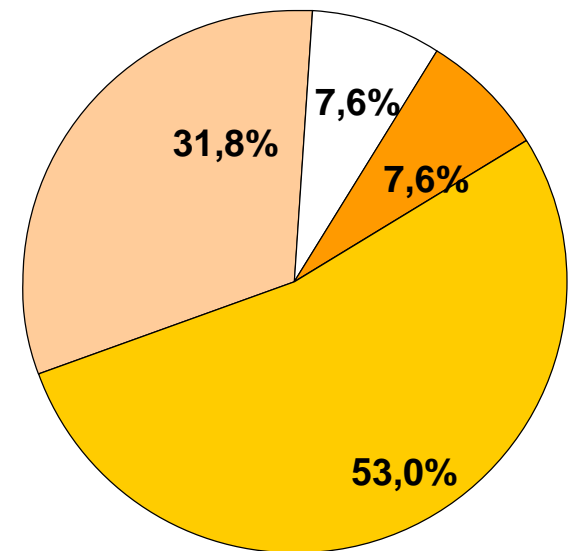
■ **Balanced Board** ■ **Current round Inverstors** ■ **Founders & Management** ■ **All Investors**



Before first round

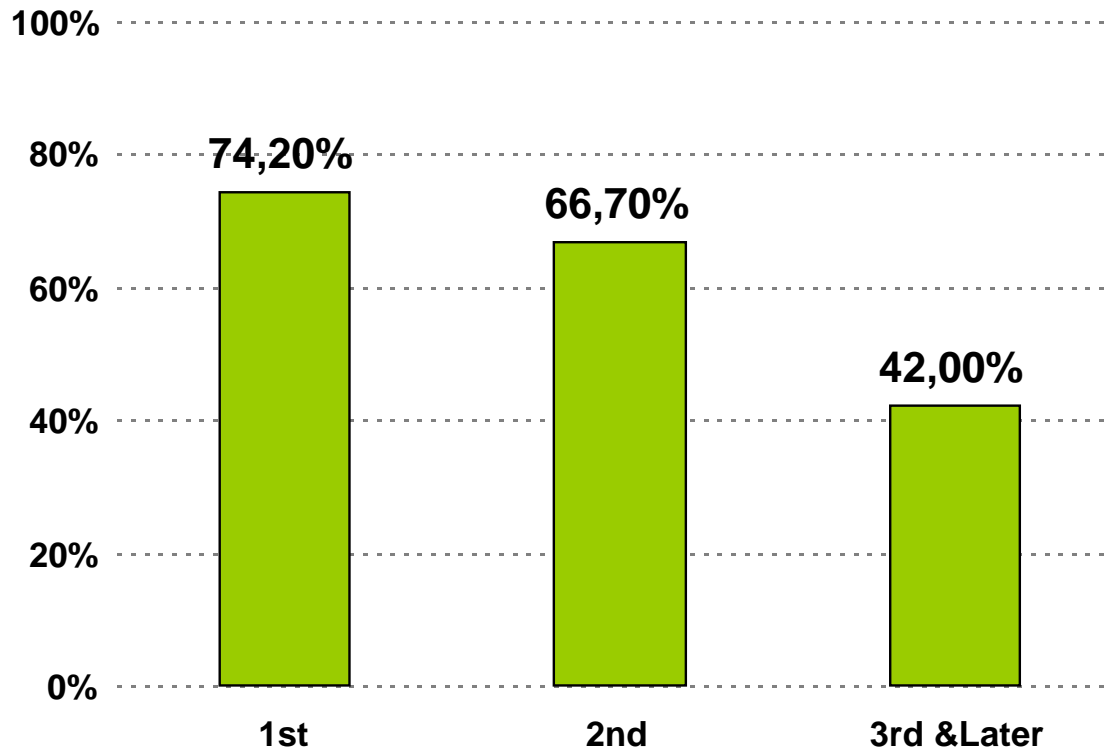


After first round

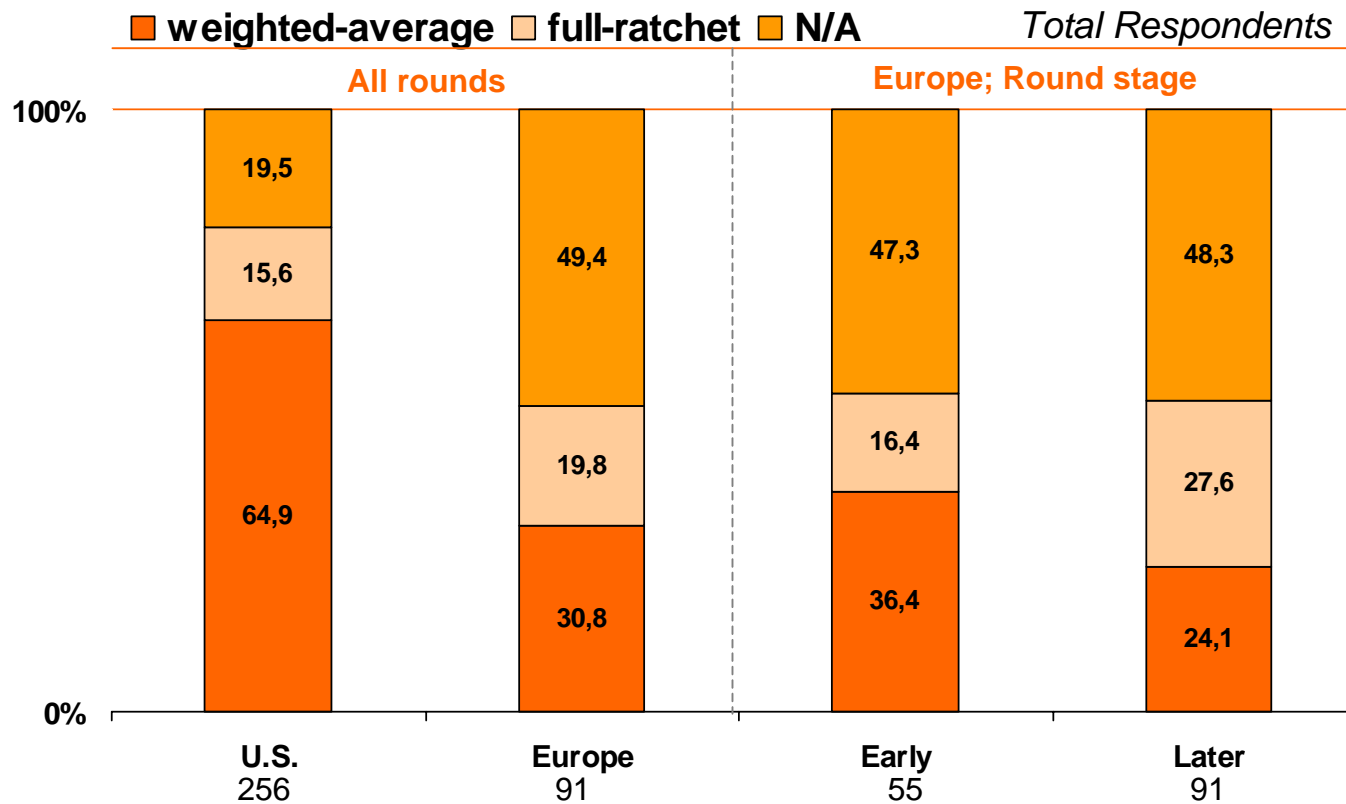


After second round

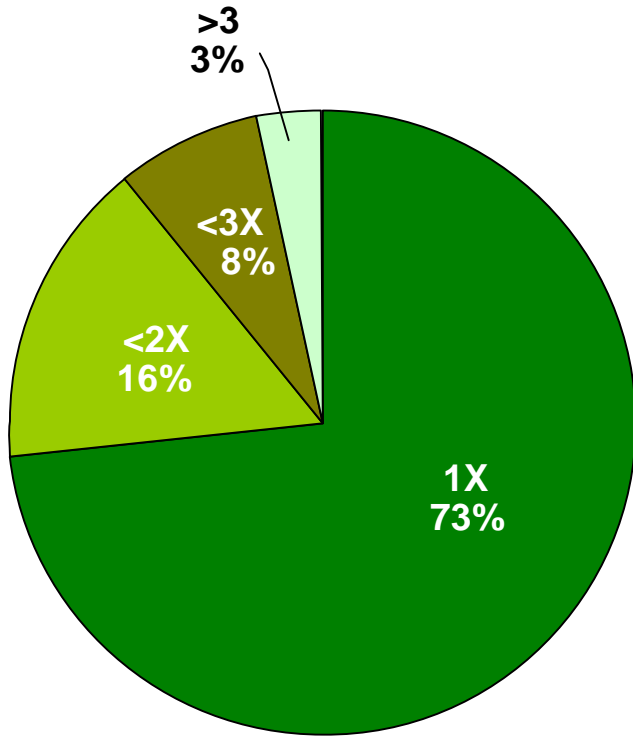
Investors who obtained affirmative voting control or veto rights over significant corporate transactions by round stage (in %)



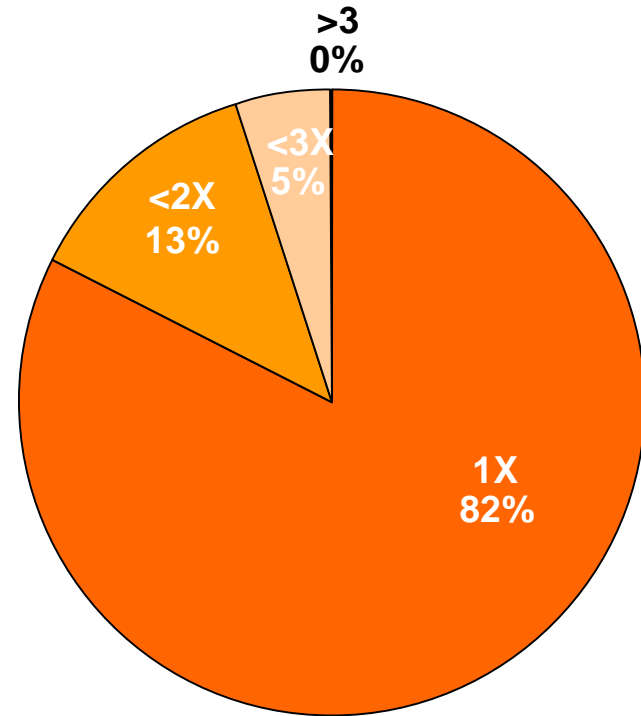
U.S. & Europe: dilution-protection provisions based on weighted-average or full-ratchet (in %)



Liquidation preference associated with preferred securities (in %)



4/04 – 3/05
Total
Respondents=157



4/05 – 6/06
Total
Respondents=157

Portfolio of Grazia Equity – November 2007

