Valuation Matrices

A Guide for Private Investors, both sophisticate investors and crowd investors, on valuing start-ups and early-stage businesses

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1 Introduction

One of the challenges in investing into early-stage ventures and startups is valuing the company. Since these Companies are not quoted on any stock-exchange and do not have any trading history upon which to such tools as price/earnings ratios are relevant, a balance needs to be struck between the optimistic projections from the entrepreneur and the caution required by investors in this risky asset class.

Having invested in over £100m into 200 early-stage companies, Envestors has come up with a guide to pricing early-stage investments.

2 Assumptions

The Valuation Matrix assumes the following:

- VALUATION: The figures displayed in Valuation Matrix are the PRE-money valuation of a Company i.e. the value of the company BEFORE any investment into that Company
- SALES: The sales assumptions are based upon ACTUAL sales for the previous three months. Owing to the unpredictability of financial projections it is safer to avoid basing a valuation on any future sales which are not contractually secured
- CASH INVESTMENT TO DATE: This figure represents the CASH investment into the Company which can be evidenced in the Balance Sheet. It does not refer to the opportunity cost of labour.

3 Valuation Matrix

	REVENUE Stage	Pre-revenue	Early Revenue	Growing Revenue	Maturing Revenue	Mature Revenue
	Range (ave of last 3 months ACTUAL)	Pre-revenue	Up to £50,000 pcm	£50,000 to £100,000 pcm	£100,000 to £200,000 pcm	Over £200,000 pcm
	Assumption (monthly revenue)	Pre-revenue	£25,000	£75,000	£150,000	£300,000
	Annualised Revenue	Pre-revenue	£300,000	£900,000	£1,800,000	£3,600,000
CASH investment to date	Assumption (CASH investment)					
Up to £50,000 (£25,000)	£25,000	**£350,000**	**£750,000**	**£1,500,000**	**£3,750,000**	**£7,500,000**
£50,000 to £200,000 (£125,000)	£125,000	**£625,000**	**£1,000,000**	**£2,000,000**	**£5,000,000**	**£10,000,000**
£200,000 to £1m (£600,000)	£500,000	**£1,250,000**	**£2,000,000**	**£3,000,000**	**£6,000,000**	**£12,000,000**
£1m to £2m (£1.5m)	£1,500,000	**£2,500,000**	**£4,000,000**	**£5,500,000**	**£10,000,000**	**£17,500,000**
Over £2m (£3m)	£3,000,000	**£5,000,000**	**£7,500,000**	**£10,000,000**	**£15,000,000**	**£25,000,000**

4 Sector variances

Certain factors may influence the valuation of Companies in certain sectors

- Technology platforms offering software as a service (SaaS). Companies which can demonstrate contracted regular recurring monthly revenue will be valued at 50% higher than the figures above.
- Medical devices. The risks and returns of medtech businesses are significantly higher with much depending upon the success of trials and gaining regulatory approvals.
- Social networks and marketplaces. Typically, high risk and dependent upon significant investment in marketing to build market share.
- Blockchain and distributed ledger. A specialist investment area where valuations can be higher than those stated above
- Technology products with strong Intellectual Property (IP). Potentially higher valuations.

5 Top Ten Tips for investors in early stage businesses

Most investors invest on “gut feel” on the strength of the management team and their product or service, but when doing so it is helpful to look out for the following hygiene factors:

1. Is there an Independent Board? Havign a Chair and at least one non-executive director (NED) entirely independent of the executive management team will help with corporate governance
2. Does the Balance Sheet make sense? Having a recent balance sheet, which has been signed off by the management team, will show the capital structure of the business for example if there are any Directors’ Loans or significant liabilities
3. Are the management team full time and solely and exclusively focussing upon the business? For very early stage businesses the Founder / Directors may need to supplement income elsewhere, but if taking on investment they need to be full-time and sign Service Agreements (Contracts of Employment) which covers issues such as non-compete, salary reviews, holiday entitlement etc.
4. Is this a genuine growth story rather than a survival story? A number of Companies seek equity investment when they are in trouble in terms of being insolvent. Investors should look at the balance sheet to identify negative Net Current Assets (excluding intangible assets).
5. Is there a simple organisation structure? Investors need to be clear as to which company they are investing in if there is more than one company in the group. They should be wary of over-complicated structures where the Directors are involved in
6. Is there a lawyer handling the investment legals? To ensure you receive your share certificates and any tax documents.
7. Are the tax documents up to date?
8. If making profits, are these profits a true reflection of the business? If the company is only making a profit as a result of the key Founders/Director(s) not taking a salary, then this needs to be taken into account (although great that the Founders/Directors are committed)
9. Has the team genuinely got an ambition to build and exit the business? As opposed to a lifestyle business providing them a comfortable income with no need to exit.
10. Are the interests of the Founder/Directors in line with those of the Investor? Probably the most important question for the investor and the Founder/ Director.

The above is an extract from the *Envestry™ Guide to Investing as a Business Angel* (24pp)

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