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# Valuation Basics

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## The Ambiguity of Valuation

- Valuation is not solely quantitative
- Entrepreneurs must learn valuation methods but be comfortable with ambiguity
- Valuation is “an illusion”, set more by market factors than by formulas
- What’s the price of your company?
- What someone is willing to pay for it?

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## A Willing Buyer and Willing Seller

- Apple Computer and Be, Inc.
- Apple (Amelio) approached Be to acquire it
- Be had revenues of $3 million and 40 employees (financed with $20 million of venture money)
- Apple - $100 MM; Be's counter - $250 MM.
- Never came to terms; Apple acquire NeXt
- 5 years later, Be acquired for $11 MM

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## Subjective Factors in Valuation

- Stage of business
- Management team
- Industry (or market)
- Reason for acquisition or sale
- Other factors
- Ultimately, cash flows drive valuation

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## Pre-money and Post-money Values

- Pre-money is the value placed on the company prior to the investment
- Post-money is the value after the investment
  - Computed as pre-money + amount invested
- Post-money determines how much the investor owns (or the entrepreneur has given up) as a result of the investment
- Post-money is often pre-money of the next round

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## Why Value Your Company?

- To determine its selling price
- To determine how much to give up for partnering
- To determine how much to give up for an investment

## How Much Equity Should You Give Up?

- Many entrepreneurs ‘unknowingly’ establish their company’s value
  - I want to raise $100,000.
  - I want to maintain ownership of 90%
  - Implied post-money valuation is $1,000,000
    - Entrepreneur retains 90%
    - A $100,000 investor gets 10%
    - $100,000 ÷ $1,000,000 = 10%
- Sophisticated investors may not agree on equity split or valuation

## Summary

- Valuations of companies, particularly early stage companies, is highly subjective
- It’s a negotiation process
- Understanding of terms is essential
- Other factors have big impact on ultimate valuation