CREATING A FINANCIAL BLUEPRINT

for Early Stage Startups

WHAT WE WILL COVER TODAY?

- Getting the basics right
- What should start-ups do to succeed?
- How can financial modelling help?

GETTING THE BASICS RIGHT

SPICE ROUTE FINANCE

THE CFO OFFICE PYRAMID

STRATEGY & GOVERNANCE

- Board Communication
- Strategic Research, Review & Benchmarking
- Dashboards & Performance Management

FINANCIAL PLANNING

- Business Plans Reviews
- Financial Projections & Cashflow Forecast
- Pricing, Sensitivity & Scenario Analysis

BUSINESS MODEL

- Business Plan, Business Model
- Unit Economics
- Working Capital Modeling

PROCESSES

- Month close process
- Inventory check and control
- Policies and procedures

FOUNDATION

- Compliances
- Book Keeping
- Audits

THE CFO OFFICE PYRAMID

WHERE DO YOU STAND CURRENTLY?

IDEA

- Research and assessment of **demand** in the market
- Research and understanding of direct and indirect **competition**
- Forecasting of development **cost** and product cost

MVP

- Validation or Revision of product **demand**
- Validation or Revision of **cost** assumption
- Primary assessment of **product** pricing

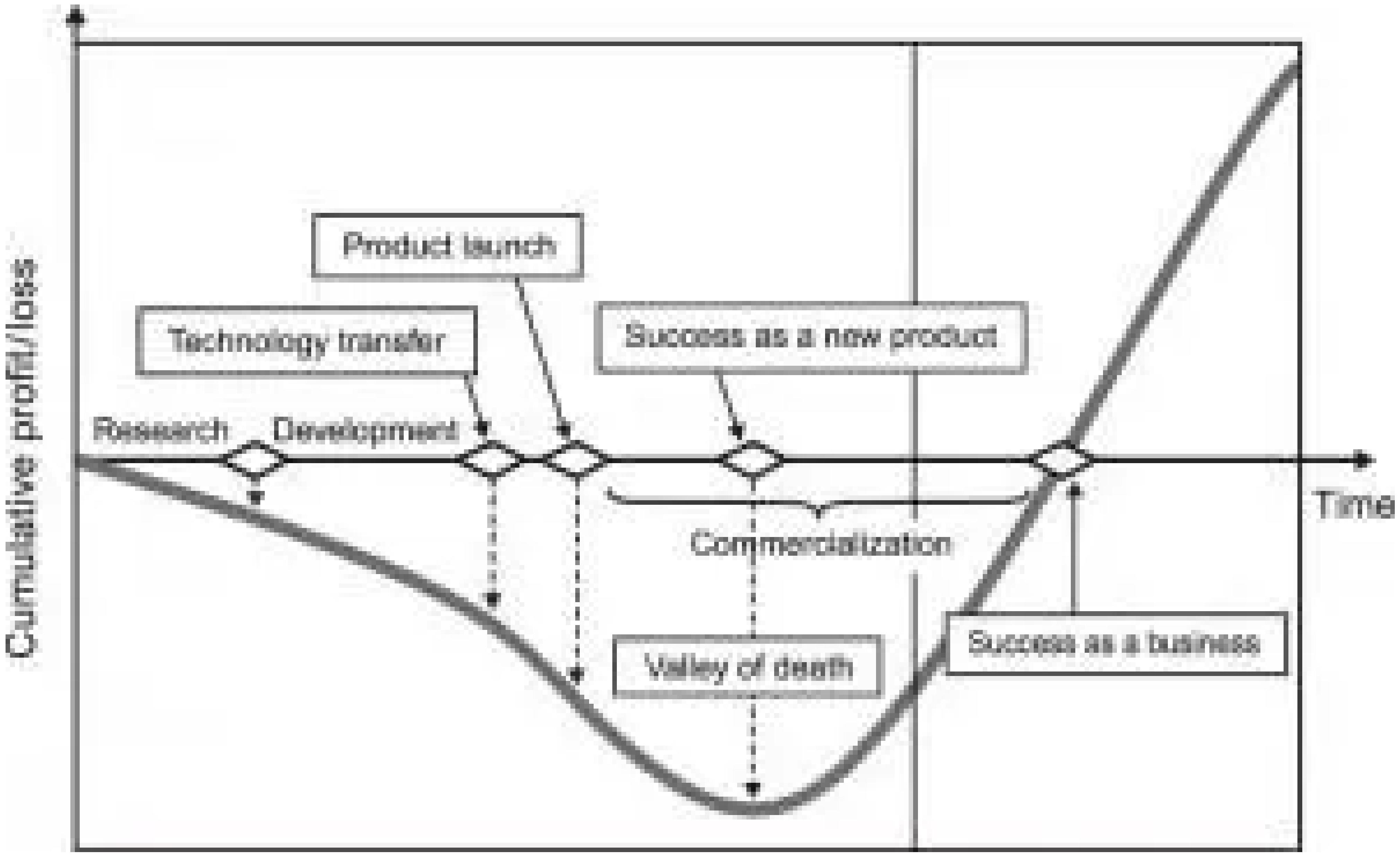
PILOT

- Testing and assessment of primary **pricing** and **monetization** models
- Assessment of **operational costs**

PMF

- Validation or Revision of **pricing** and **monetization** models
- Assessment and implementation of **pricing strategies**

EARLY START-UP LIFE CYCLE JOURNEY



- The startup life cycle journey represents the tumultuousness a startup has to experience in order to reach commercial success.
- A vast chunk of startups are unsuccessful in crossing the “valley of death”.
- In this section of the journey, a startup has already commercialized its product/service but is not able to make it profitable.
- Commercial success is obtained when a business is able to cover its direct costs, signaling improved unit economics.

SPICE ROUTE FINANCE

WHY START-UPS FAIL?

LACK OF CASH

OVERESTIMATED DEMAND

INABILITY TO COMPETE

PRICING/COST ISSUES

REGULATORY CHALLENGES

POOR BUSINESS MODEL

INAPPROPRIATE TEAM STRUCTURE

MISTIMED PIVOT

WHAT SHOULD START-UPS DO TO SUCCEED?

FOCUS ON BUSINESS MODEL

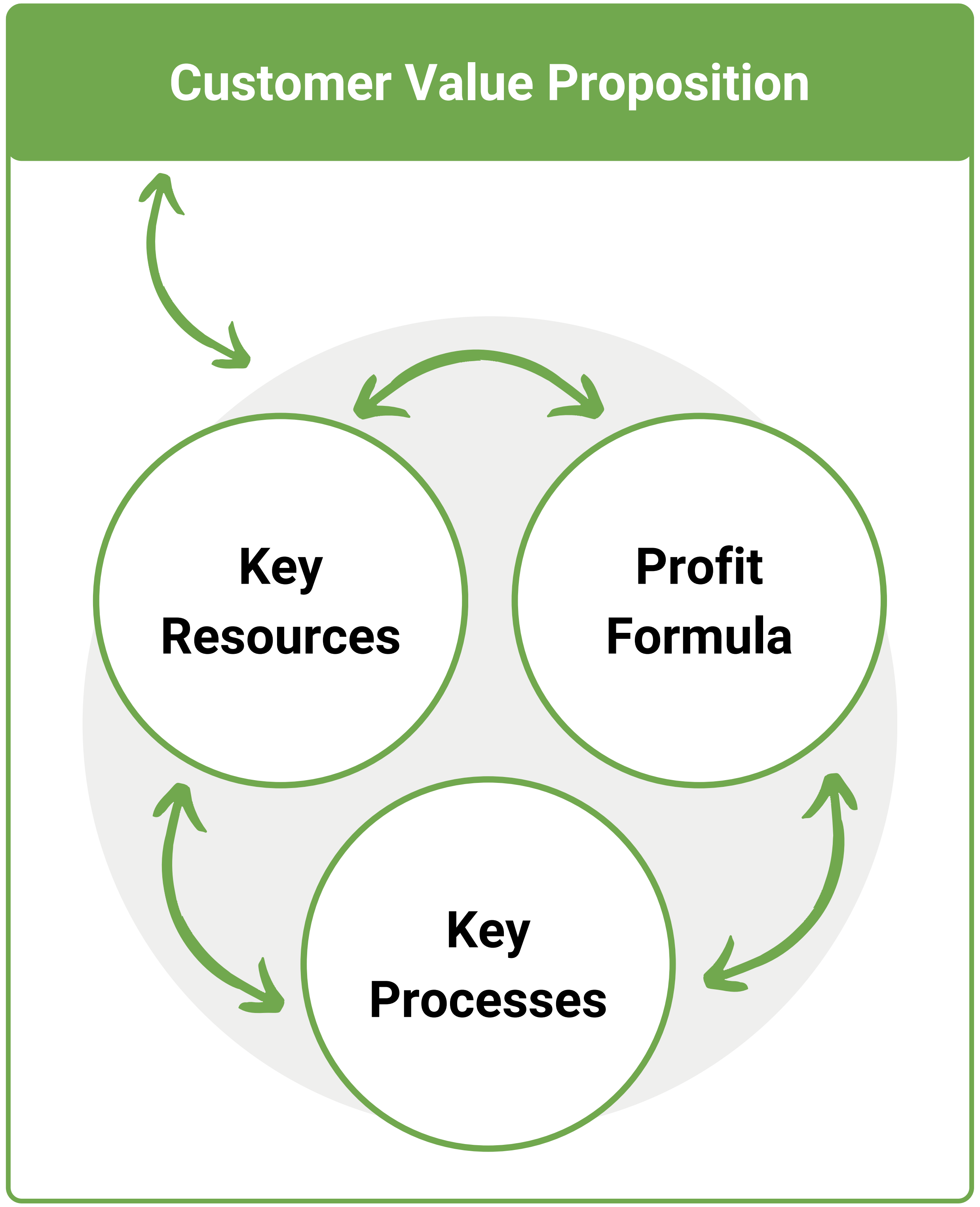
The following components make up a business model

Customer Value Proposition
What is the job you are doing for the customer?

Profit Formula
(Price x Volume) - Costs

Key Resources
Talent, capital assets, financing information, channels, tools

Key Processes
Processes, metrics and norms



Source: Harvard Business Review (2008)

SPICE ROUTE FINANCE

KEY DIFFERENCES

Business Strategy	Business Plan	Business Model

A business strategy sets out the purpose of your business, who it serves and what is the long term vision and mission. A strategy assesses and prioritizes options and then select the most advantageous. A business plan sets out how you will achieve your goals in detail, including the financial results. A business model explains how you are different to competitors and what gives you a strategic advantage.

Business Strategy	Business Plan	Business Model
What is your business? What is your purpose? Who is your customer? Analysis of business environment Competition and market gaps How can you compete?	What business are you in? What are your goals? How will you achieve them? What will be the financial benefit? What investment do you need?	Who is your customer segment(s)? What is your value offering? How will you reach your customers? What makes you hard to imitate? What resources do you need? How do you make money?

A 5 year Budget will have monthly plan for 1st year, Quarterly plan for 2nd and 3rd year, Yearly plan there after

IMPORTANCE OF MARKET RESEARCH FOR COMPANIES

Calculate TAM, SAM and SOM
This will help understand the potential future size of the company

Understand the customer problem and develop a value proposition
This sets the direction for future strategy and the product/service development process

Map out the customer journey and business process based on customer problems
Sets the foundation for how you expect customers to interact with your business

Validate processes and drive continuous refinement
Research will ensure that your business process is constantly improving

SPICE ROUTE FINANCE

IMPORTANCE OF SCALING FOR REVENUE MAKING COMPANIES?

Reach bigger and better markets

This can positively impact margins as it can help leverage pricing and volume

Achieve economies of scale

Helps lower cost per unit over time and achieve better margins and cash-flows.

Generate positive cash flows

Scale allows easier access to better working capital terms, access to capital markets and hence enables more efficient cash generation.

HAVE YOU ACHIEVED PMF?

- PMF (Product Market Fit) refers to a stage where a product or service has perfectly catered to a problem posed by the market.
- It's a highly subjective milestone that is very difficult tot achieve as problem statements keep evolving.
- Every industry will have a different way of defining the achievement of PMF.

INDICATORS OF PMF

Companies that experience growing ARR, MRR and have reduced their churn can be safely assumed to have reached PMF.

For companies without recurring revenues, a growing customer base and improving unit economics are signs of achieving PMF.

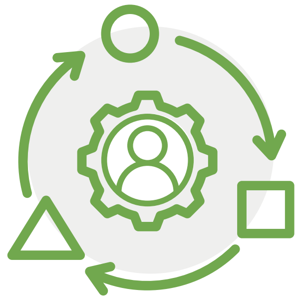
SPICE ROUTE
FINANCE

MAINTAINING PMF

- A firm's PMF status is not permanent.

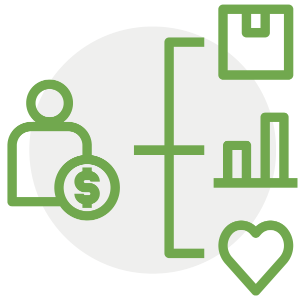
- Given the dynamic nature of the startup ecosystem, constant innovation and problem solving result in many startups losing their edge.

HOW TO MAINTAIN PMF?

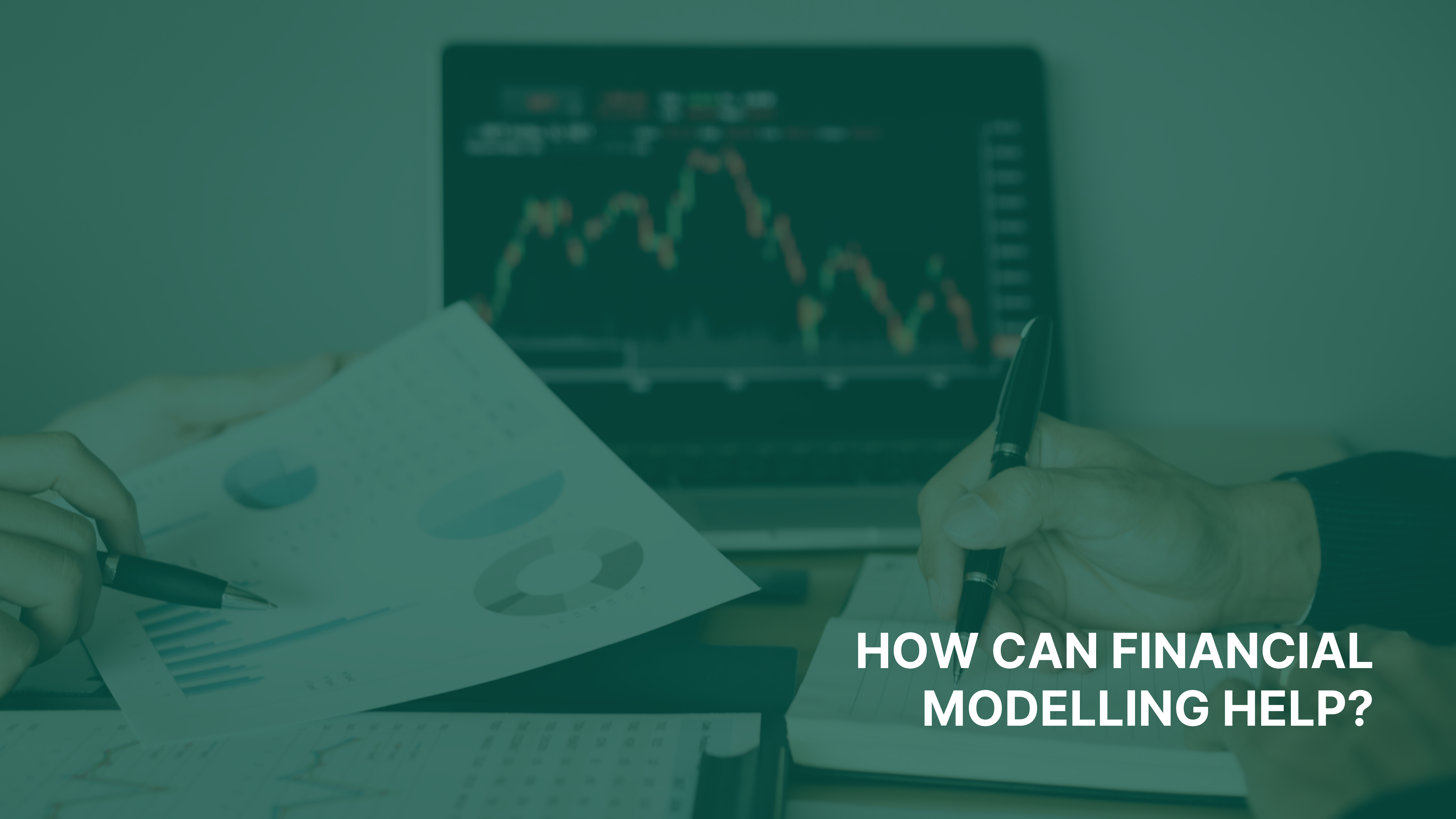


Have a customer centric business model

Spend time on R&D to create more efficient solutions



Constantly monitor the market to understand trends in customer behaviour



HOW CAN FINANCIAL MODELLING HELP?

WHAT IS FINANCIAL MODELLING?

A financial model quantifies the company's strategic vision.

It lays out a plan for future revenue growth, accounts for all the costs incurred and resources needed to achieve growth.

It relies on historical data to set a baseline and then forecasts future performance based on strategy.

- For companies with little to no operating history, financial data of competitors with operating history can be a good starting point.

- For companies with operating history, historical financial data of the company and along with financial data of competitors is a good starting point.

SPICE ROUTE
FINANCE

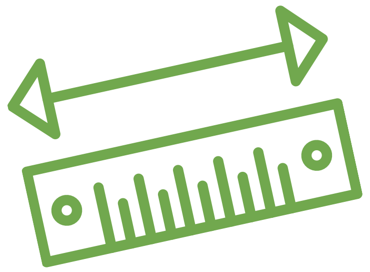
IMPORTANCE OF FINANCIAL MODELLING

EXERCISE FORESIGHT

- Can identify growth pattern and steps to be taken.
- Can also identify future issues and account for their effect on finances

UNDERSTAND RESOURCE REQUIREMENTS

- Growth requires resources, and models help identify how much would be needed



QUANTIFYING YOUR VISION

- Path to milestones is quantified.
- You can lay out the inputs you need to get to a said milestone.

INSPIRE INVESTOR CONFIDENCE

- Path to growth and profitability is visible to investor.
- Confidence is inspired by the numbers

TYPES OF FINANCIAL MODELS

TOP DOWN MODELS

1. Take a macro-to micro approach
2. Industry estimates are taken as starting point and inputs are narrowed down
3. TAM-SAM-SOM approach is a useful aid

BOTTOMS-UP MODEL

1. Approach is less dependent on external factors
2. It is an inside-out approach
3. Projections are based on main value drivers of business

A hybrid approach is the best approach

SPICE ROUTE FINANCE

KEY ELEMENTS OF A FINANCIAL MODEL

Revenue Plan/Buildup

- Sales Growth Modelling
- Growth of price and volume inflation
- Unit volume growth
- Market Size and Market Market Share
- Unit Market Size and Growth and impacts due to pricing of product / service
- Volume Capacity Approach : Relevant where revenue plan is linked to the capacity to produce
- Revenue Driven by investment in R&D and Marketing Spends
- Manpower Based Revenue plan with Tiered Pricing for each type
- Revenue Plan basis the produce/service roadmap

KEY ELEMENTS OF A FINANCIAL MODEL

Operational Overheads	Fixed Overheads	Marketing Cost	Manpower	CAPEX	Scale up Costs
• Skill development • QA • Training • Cloud costs • Staff welfare • R&R	• Management Salaries • Office Space • Professional Expenses • Legal help for	• Advertisement • PR • Events • Conferences • Research • Marketing Materials • SEO • Data analytics	• Linked to revenue • Linked to org structure • Annual appraisals • Market benchmarking for salaries • Span-based headcount planning • Stage based org structure planning • Tech setup	• IP development (stage-wise increase in CAPEX) • Plant setup (manufacturing) • App development (e-commerce, marketplace) • Technical architecture • IP (global vs India)	• Costs are dependent on the metric of scaling. • Metric of scaling is dependent upon the business model and the expansion strategy • Necessary to define responsibility metrics when scaling!

CASH BURN

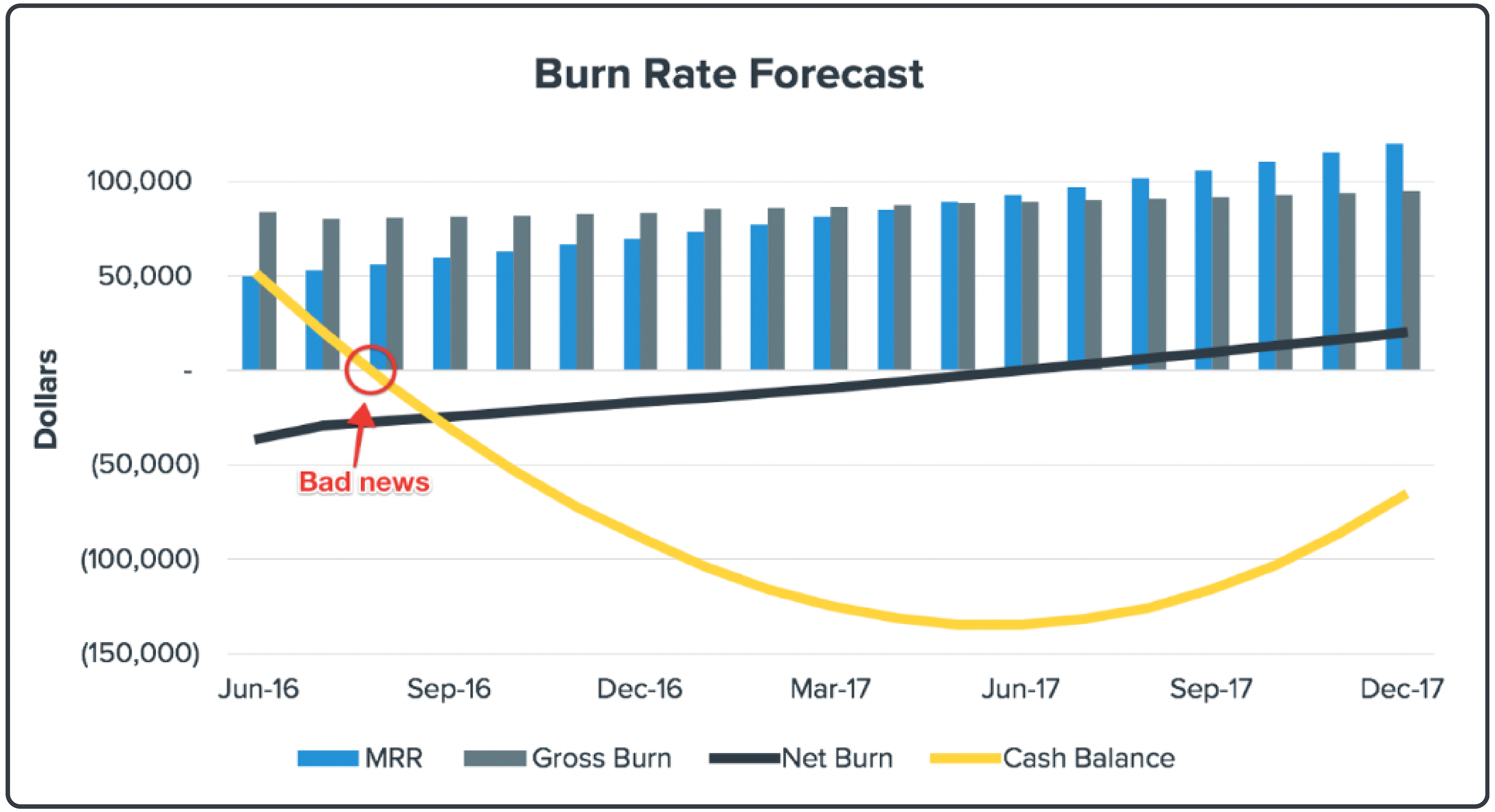
CALCULATING CASH BURN

Burn rate is the rate at which a company uses up its available cash.

Two types of cash burn rates:

Gross burn rate	Net burn rate
Total of all monthly expenses.	Gross burn rate - Income

As a measure of negative cash flow, burn rate is a crucial metric for understanding your startup's overall financial health.



Tracking cash burn is crucial for early stage companies as their survival is dependent on it.

CASH RUNWAY

CALCULATING RUNWAY

- Runway refers to how long a company can operate before they run out of cash,
- Typically measured in months.
- Runway = Total Available Cash/Net Burn Rate
- Runway is affected most by:

Receivables

Fundraising

- Burn Rates can be reduced with:

Layoffs and Downsizing

Decreasing Client Churn

RUNWAY CALCULATIONS

Operating Runway

$$= \frac{\text{Cash on hand}}{\text{Operating Cash Flow (OCF)}}$$

[avg. past 6 months]

Predicted Runway

$$= \frac{\text{Cash on hand}}{\text{Operating Cash Flow (OCF)}}$$

[avg. future 12 months]

Standard Runway

$$= \frac{\text{Cash on hand}}{\text{Change in cash}}$$

WHAT INVESTORS LOOK FOR IN A FINANCIAL MODEL?

1. Funding requirement
2. Utilization of funding
3. Margins (contribution, gross and EBITDA margins)
4. Cash burn and runway
5. Overall revenue growth rate
6. SBU/product wise revenue growth rate
7. Sales and marketing costs as % of revenue
8. R&D costs as a % of revenue
9. Unit economics

SPICE ROUTE FINANCE

HOW DO INVESTOR VALUE EARLY STAGE STARTUPS

1. Founding Team & Execution capabilities
2. Idea to monetization - Timeline
3. Traction from customer / Customer validation / Feedback loop
4. Your solution / Prototype / Agility to Change
5. Business Model & Size of Opportunity
6. How scalable is the distribution model
7. How strong are you in selling your product/service
8. How strong are the unit economics
9. Capital required over time

KNOW YOUR MENTORS

Sriram Chidambaram

Jai Vaidya

Education (Sriram Chidambaram)

CGMA from CIMA

Fellow Certified Management Accountant from the ICWAI

Qualified Company Secretary from the ICSI

EGMP from IIM-Bangalore

Experience

Founder and CEO at Spice Route Finance

VP of finance at E4E, a US based IT/ITeS multinational

Head of finance at MAS Holdings, one of the world's largest garment manufacturers.

Education (Jai Vaidya)

Passed all 3 levels of the CFA exams

ACCA Affiliate (passed all exams in 2 years)

PGDip in Econometrics from Monash University

Master of International Business from Monash University

sriram@spiceroutefinance.com | +91 9940392753 | http://calendly.com/spiceroutefinance | https://www.linkedin.com/in/sriramchidambaram/

WHAT DOES SPICE ROUTE FINANCE OFFER?

I

II

III

CFO Services

Our CFO office service, enables us to provide hands-on support for companies needing help in managing transactions, financial reporting and staying on top of unit economics

Advisory Services

Our advisory services bring strategic leadership to your finance function and is a key part of your top management till the time you need a new CFO.

Consulting

Our consulting services are short term engagements that ensure quick turnarounds and implementation of strategic initiatives.

OUR PRACTICE AREAS