MAYOR'S INTERNATIONAL BUSINESS PROGRAMME

LONDON & PARTNERS

ROUTES TO FINANCE

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BDO Benoy KPMG PA

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INTRODUCTION

High-growth firms in the UK saw record levels of equity investment during the first half of 2017.

Over £3 billion of funding was poured in – up some 74.7% on the previous half-year. The average deal was worth more than £5.5 million.

Different funding methods meet different requirements. Not every source will be suitable for every business.

David Bevan
BDO

Of course, equity investment is just one source of business finance: there are a number of funding mechanisms available to growing companies. But the equity figures illustrate a healthy appetite for providing capital to scalable business propositions. Sara French, head of the Mayor's International Business Programme, explains: "The businesses we have on the programme are well received by the investor community. Funders are keen to help our high-growth scale-ups - and to reap the financial rewards.

For government, the exponential growth that successful start-ups can achieve is a vital economic stimulus. Hence the introduction of tax incentives for investment in early-stage businesses in the UK, in the form of the EIS (Enterprise Investment Scheme) and SEIS (Seed Enterprise Investment Scheme).

Every firm must forge its own funding journey, in line with the development of the business. "There is no one-size-fits-all solution for financing a scale-up," says Kevin Smith, Chairman of KPMG's London Region.

David Bevan, Director of Corporate Finance at BDO, agrees: "Different funding methods meet different requirements. Not every source will be suitable for every business."

But as a rule, the funding journey will begin with a bootstrapping phase, then early seed funding. The later stages – the focus of this report – consist of rounds of debt and/or equity finance, eventually leading (in some cases at least) to exit. The good news is, your businesses should grow larger and stronger as it progresses through the financing lifecycle. As Yvonne Haizel of Mitsui & Co puts it, "success becomes likelier with each next funding round".

ABOUT THIS REPORT

Routes to Finance is brought to you by London & Partners, the Mayor of London's promotional agency. It looks primarily at the more mature end of the funding journey: late-stage financing and exit.

We draw on the expertise of the mentors and delivery partners on the Mayor's International Business Programme, which helps London's entrepreneurial businesses to accelerate their international growth.

For each of the funding mechanisms examined, we ask: what is it? Where does it fit in a business's development journey? What will investors be looking for? And what are the benefits and disadvantages?

We also present real-life case studies of founders on the Mayor's International Business Programme, who share their stories about securing finance. They give their thoughts on the experience, and offer advice for other entrepreneurs considering a similar route.

STEPS IN THE FUNDING JOURNEY

COMPANY FOUNDED

BOOTSTRAPPING

Ask yourself: is now the right time to expand? Are your business, and your senior team, ready to take on a foreign venture?

EARLY STAGE FINANCE

THE EQUITY ROUTE

SEED FUNDING

Early-stage funding invested in return for an equity stake. As with bootstrapping, seed finance may come from friends and family. But it generally involves more formal arrangements with angel investors, venture capital funds or crowdfunding platforms.

CROWD FUNDING

Typically early-stage funding, invested by a large number of individuals and institutions in return for equity, via a dedicated online platform.

DEBT FINANCE

Funds loaned in return for interest rather than equity, usually by financial institutions (mostly banks). Debt finance may convert to small amounts of equity once repaid.

- Venture debt
- Growth capital
- Recurring revenue lines
- Accounts recurring lines

ANGEL INVESTMENT

Finance from private individuals, usually given in exchange for equity, but sometimes loaned as convertible debt.

LATER STAGE FINANCE

SERIES A

SERIES B

SERIES C, D, & E

Successive rounds of significant, later-stage equity funding, aimed at accelerating the development of a business from start-up stage to maturity.

EXIT

M+A

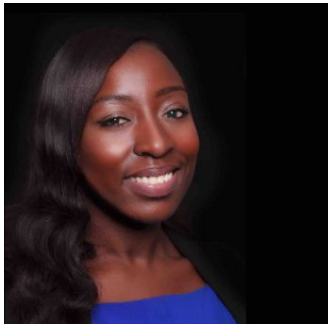
Selling a business to a larger concern, so as to access not just capital, but often new customers and markets.

IPO

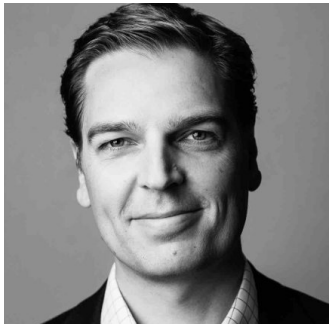
The first sale of shares in a business to the general public, conducted over a securities exchange.

MEET THE EXPERTS

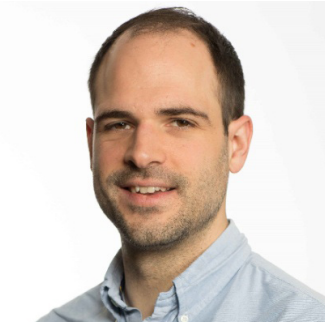
In this report, the Mayor's International Business Programme has drawn on expertise from across the London finance ecosystem. Meet our experts and programme mentors to the right, and on the following page.



Yvonne Haizel
Mitsui & Co



Jeppe Zink
Northzone



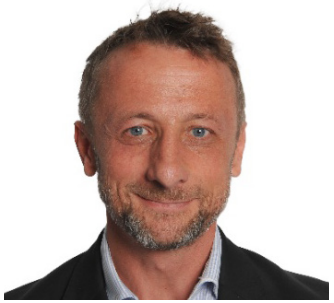
Andrew Parker
Silicon Valley Bank

John Cordrey
Foresight

James Clark
LSE

Kevin Smith
Chairman of KPMG's London Region

David Bevan
Corporate Finance Director, BDO



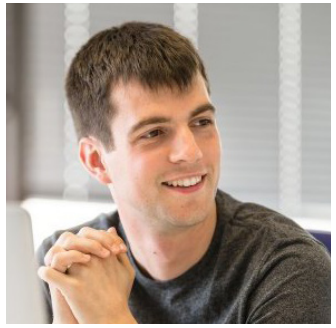
Jason Hill
Head of Challenger Banking at PA Consulting

MEET THE EXPERTS

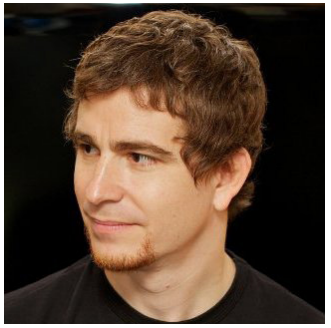
Mayor's International Business Programme Companies

There are more than 250 SMEs from across London being supported by the Mayor's Interntional Business Programme. We have featured a few in this report to illustrate the various types of funding available for SMEs. Meet the companies:

Estelle Lloyd
Azoomee
Co-founder



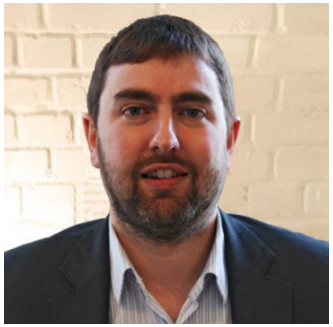
Simon Hay
Firefly Learning
Co-founder



Henrique Olifiers
Bossa Studios
Co-founder

Alain Falys
Yoyo Wallet
Co-founder & CEO

Sarah Kerruish
Antidote
Chief Patient Officer



Robert Timms
translate Plus
Co-Managing Director

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PRE-SERIES A FUNDING

As a scale-up looking to grow and with global expansion, potentially on the horizon, it's likely you'll have already received some funding, whether this be from bootstrapping, crowdfunding, seed investment or angel investment.

Azoomee, a company which joined the Mayor's International Business Programme in 2017, is a business making the transition from start-up to scale-up and you may well notice similarities between their funding journey and your own.

Having emerged from the earlier part of its finance journey, the company is now heading into the later stages.

PRE-SERIES A CASE STUDY: **AZOOMEE**

When it comes to business ideas, necessity is so often the mother of invention.

For Azoomee co-founder Estelle Lloyd, that necessity was a safe place for young children to begin embracing life online. "There wasn't a multimedia platform curated especially for children, where they could learn how to be online in complete safety," she says.

So in 2005, Azoomee was born. The subscription service offers thousands of video games and TV episodes for five to ten-year-olds. Content is chosen for its entertainment, educational and/or social and emotional learning value. There's also a series of BAFTA-nominated, NSPCC-approved tutorials for kids on how to operate safely online.

There are no group spaces – the instant messaging feature only connects kids once their parents accept an invitation. And there's no way for children to buy freemium content without their parents knowing.

The road to expansion

The platform took about 18 months to develop, and was initially available through the main app stores. Since then, Azoomee has developed revenue-sharing partnerships for tablet distribution with O2 and Argos, and is soon to launch an Amazon Prime channel.

As a result, its user base has increased exponentially, growing more than 330% in the ten months since December 2016.

Currently available in the UK, Azoomee has international expansion firmly in its sights for 2018. Its initial focus will be the Anglophone countries, where content won't need localisation; Scandinavia, where the audience is effectively English-speaking; and the Spanish-speaking world.

Estelle "couldn't believe" the help on offer when she discovered the Mayor's International Business Programme. She's since joined a trade mission to Silicon Valley, and received mentoring on pricing from KPMG. "That made us think completely differently about pricing," she enthuses.

> **The support from the programme has been absolutely fantastic. It's ideal for businesses making the transition from start-up to scale-up**
>
> Estelle Lloyd
> Co-founder, Azoomee

Angel approval

Azoomee isn't Estelle's first business. She and her co-founder have already started, grown and sold a tech company. That success was enough to persuade her angel investors to follow her into this endeavour.

"They had confidence in us," says Estelle, "and were happy to invest in a socially responsible venture."

As such, raising angel investment proved fairly straightforward this time around. Her angels then introduced her to additional funders.

Azoomee also attracted an environmentally friendly institutional investor, and raised £790,000 via Crowdcube (against a target of £450,000). Crowdfunding enabled Azoomee to market the product to an audience that includes many parents.

In all, the firm has secured £3.5 million of investment to date. The majority of this funding has been poured into developing the product and hiring tech talent. Azoomee is targeting a first major institutional funding round in 2018.

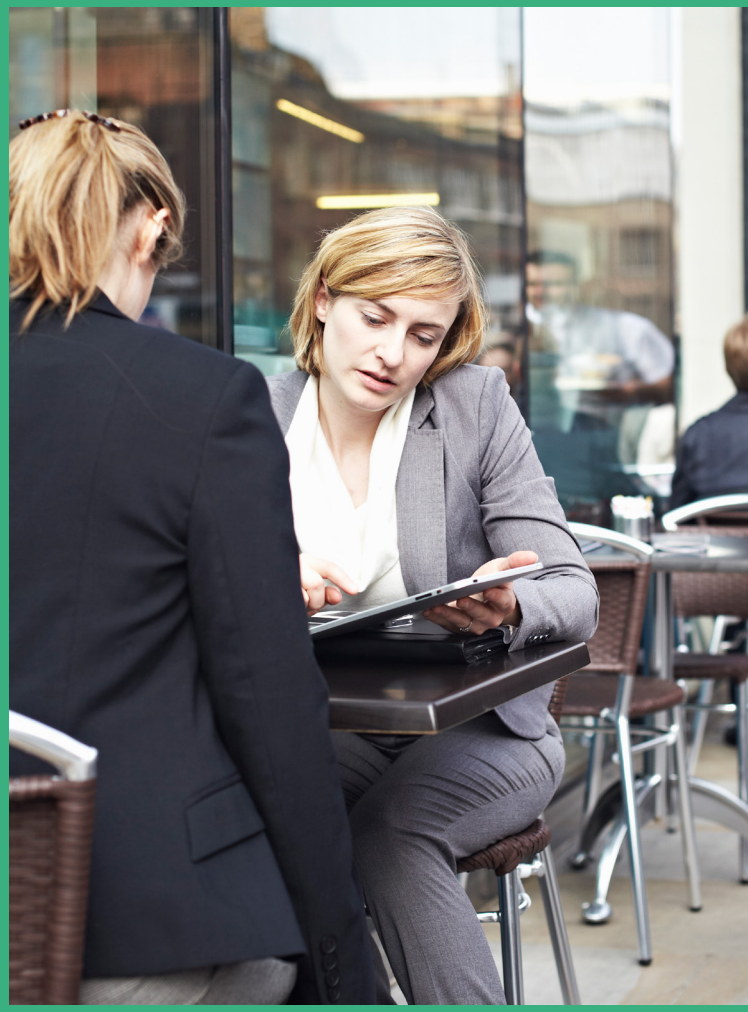
A positive climate

For Estelle, the key to successful fundraising is "finding a core network of investors that believe in you and your business." Once you've found that, life becomes easier.

Of course, the experience gained from the previous start-up helped Azoomee's founders. But that shouldn't discourage first-time entrepreneurs, affirms Estelle.

"Right now, the investment climate is favourable. There are many investors out there who are keen to put money into growing businesses."

Estelle Lloyd
Co-founder, Azoomee



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LATER-STAGE EQUITY FINANCE

There comes a time when a growing business has to "cease being a start-up, and become a scale-up," in the words of Yvonne Haizel of Mitsui & Co.

That's what the later funding rounds are for. They give firms a major cash injection, typically from venture capital (VC) funds, in exchange for a stake in the company. Investors will put several million pounds into the business, with the expectation that it will soon hit hyper-growth.

Later-stage funding is when business owners must come to terms with a significant dilution of ownership. "The more funding rounds you raise, the more new investors you acquire," explains Jeppe Zink, Partner at VC fund Northzone.

This can be a difficult emotional leap for founders, having worked every available hour to nurture their venture through its early development.

Later-stage finance rounds are known as the A series, B series, C series, etc. (or the A, B and C-round).

The amounts raised usually get bigger with each successive round. Kevin Smith of KPMG highlights the example of a British cybersecurity firm which recently raised an impressive £19 million at C-series stage.

For the purposes of this report, however, we'll concentrate on Series A and B.

Series A

What is it?

The clue's in the name. Series A funding is generally the first significant influx of VC funding into a business.

"A-rounds tend to be much larger than seed and angel rounds," explains Yvonne Haizel, who looks after EMEA tech sector investments for Mitsui & Co, a Japanese trading and investment company.

A series will generally involve a consortium of three to four investors, one of whom will lead the round. There are rarely more than five, as "too many cooks can spoil the broth at the A-series stage," says Yvonne.

> **You need a group that knows how to take the business to the next level, has a plan to get it there, and the skills to execute that plan.**
>
> Yvonna Haizel
> Mitsui & Co

Who is it for?

An A-round becomes a realistic prospect once a firm has determined a path to sustainable revenues – though it is unlikely to be generating profit at this stage.

"Series A funding is the first round geared at helping a firm reach profitability," says Yvonne. "It enables the firm to scale up its team, and step up its sales, marketing and customer acquisition activity."

What are the key criteria and terms?

A-series investors will want to know that a business has a core value proposition, and has found a product-to-market fit, according to Yvonne.

They tend to have another couple of key criteria – the first being a strong team. As Yvonne puts it: "You need a group that knows how to take the business to the next level, has a plan to get it there, and the skills to execute that plan."

The second is a path to exit. "Exit is a vital part of a business's value creation path," she says. "Investors will want to know what the founders have in mind."

The main negotiating point – after the amount to be invested – will be the equity stake. Investors will usually take around 20-40% of the equity in return for the funding.

"An A-series means a significant dilution of ownership," Yvonne explains. "That's the biggest change for entrepreneurs to adjust to. So it's important to strike the right balance.

"The equity stake must be big enough to attract investors, but it shouldn't dilute the founders' interest to an extent that will demotivate them. After all, it's down to them to drive the business forward."

What are the advantages and drawbacks?

A-round investors bring a great deal of strategic value to the businesses they invest in.

Mitsui & Co is a good example. The company invests across many industries, so can introduce firms to potential customers in the relevant sectors. “And we have very strong ties in Asia, so can help companies expand there,” Yvonne says.

“We also place seconded staff in some of the firms we invest in, to help them with important areas such as governance.”

However, an A-series can be the riskiest funding round. “The scale-up stage can be the most difficult, with the cash-burn rate having to be controlled,” warns Yvonne. “When a business is growing rapidly, there are always unexpected twists and turns.”

She emphasises the importance of getting the right investors to help the firm through.

“Entrepreneurs should look for investors they feel they can trust and partner with,” she advises. “The lead investor is particularly vital. It has to be someone you can work with when the going gets tough.”

Entrepreneurs should look for investors they feel they can trust and partner with

Yvonne Haizel
Mitsui & Co

SERIES A CASE STUDY: **FIREFLY LEARNING**

Educational software might not be everybody's idea of a schoolboy hobby. But that's how Firefly Learning started out.

Co-founders Simon Hay and Joe Mathewson continued to develop their idea through university and investment banking careers.

When schools began to show real interest in their product, Firefly Learning became a full-time venture in 2009. Its cloud-based, software-as-a-service educational resource allows teachers to set homework, track pupils' progress, provide feedback, and share learning resources with pupils and parents.

Today, the product serves about 500 schools and 400,000 pupils in 35 countries. In fact, a quarter of Firefly's business comes from abroad: mainly countries with a similar education system to the UK's, a large English-spoken student population, and/or plenty of international schools.

Kissing frogs

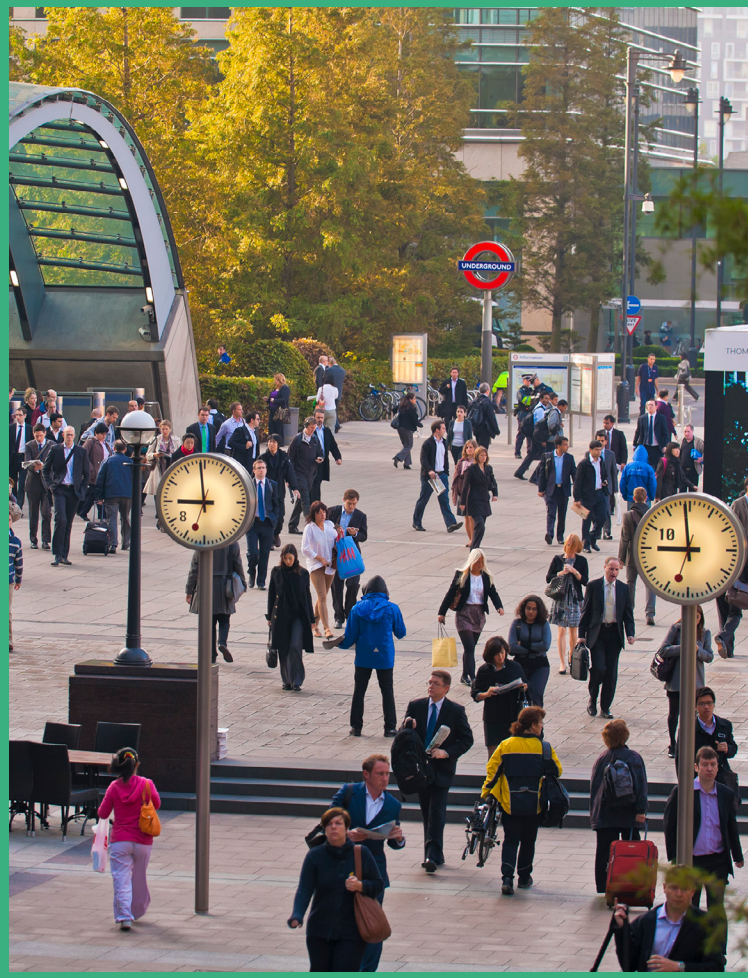
The firm's funding journey has moved quickly. Loans of around £1 million were all that separated the firm's bootstrapping phase from the largest ever ed tech A-round.

"We didn't need to take equity financing when we did our A-round," says Simon. "But with technology transforming how schools teach, we saw an opportunity to fast-forward our growth in the UK and abroad. It was time to scale up."

Firefly raised £4.5 million from BGF Ventures, who led the round, and growth capital investor Beringea.

But finding the right investor took a gruelling six months of conferences, tech industry events and introductory discussions.

"We were looking for patient investors, who shared our vision and values," Simon explains. "There's a lot of capital in London, and every investor has a different risk appetite, and different expectations of the terms and timescales. You have to kiss a lot of frogs!"



Going for growth

Firefly has ambitious plans for the funding, which include:

- continuing to develop the platform by intensifying R&D
- doubling the workforce to around 100 people
- increasing sales and marketing activity, to accelerate the growth of its user-base in the UK and abroad
- expanding its office and operations in Australia, its largest foreign market

Getting the right fit

Simon's advice when it comes to funding your business is to start the process early. "Looking for funding when you're running short of cash puts you in a weak negotiating position," he says.

It's also worth taking the time to understand the market, and to work out which investors are right for the stage your business is at, and for your particular funding needs.

"It all helps set realistic expectations about how much you can raise, who from, and on what terms," Simon explains.

Then once you've done your research, it's decision time: which investors are you going to go with?

"The most important factor in that decision is the fit," says Simon. "Make sure you can work with your investors for the next three to five years. Make sure they can bring the skills and knowledge to help your business grow.

"And make sure your interests are aligned. If they're looking for 200% growth, and you deliver 100%, there will be difficulties."

> **Looking for funding when you're running short of cash puts you in a weak negotiating position**
>
> Simon Hay
> Co-founder, Firefly Learning

SERIES A CASE STUDY: **BOSSA STUDIOS**

BAFTA-winning Bossa Studios doesn't just develop video games: it aims to disrupt every gaming segment it enters. Gaming website IGN described the studio's massively multi-player sandbox title, Worlds Adrift, as one of the most ambitious physics games ever.

The firm's player-base is global, and each game is of course localised for every market. But international expansion is still in its early stages at Bossa Studios. The firm is currently setting up an office in Seattle to access a wider pool of creative talent, and is weighing up a few European options.

The Mayor's International Business Programe is helping Bossa Studios to formulate – and expand – its thinking about which overseas markets to target, and the competitive advantages of different locations.

An unconventional funding journey

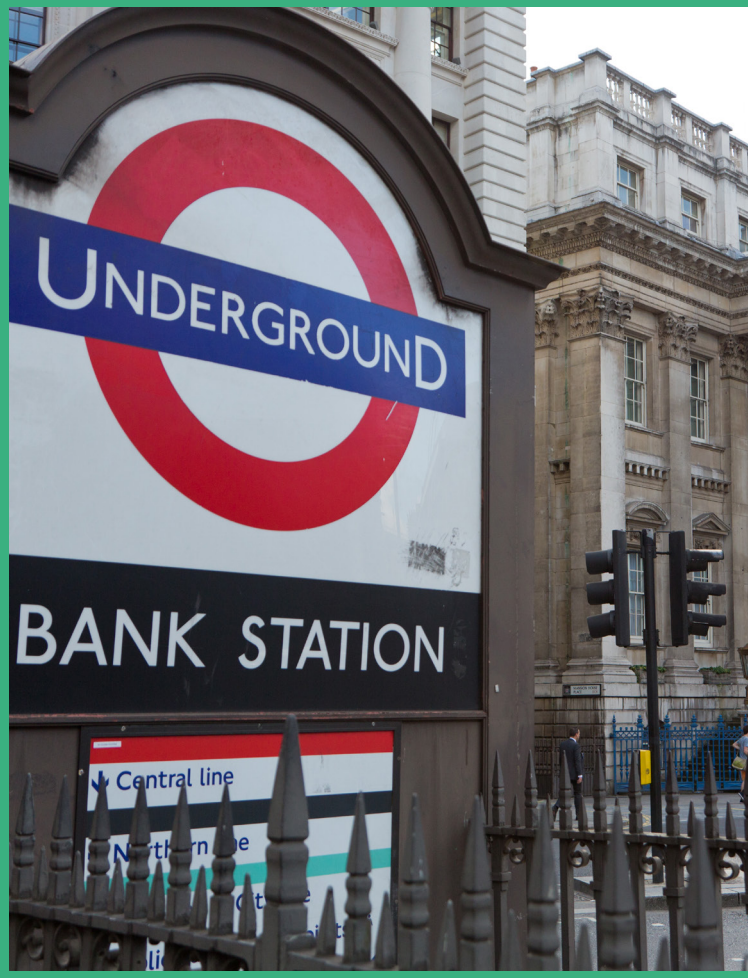
Like its approach to gaming, the firm's funding journey has been somewhat unorthodox.

It has already been through a management buy-out, after an early equity investor, Elizabeth Murdoch's production company Shine TV, merged with media giant Endemol.

After regaining its independence, the studio sought out new investment to help "reboot" the company.

"We were determined to maintain our position as a disruptor," says co-founder Henrique Olifiers. "We needed more strategic brains on the board to help us keep our competitive edge."

> **We needed more strategic brains on the board to help us keep our competitive edge.**
>
> Henrique Olifiers
> Co-founder, Bossa Studios



Position A

In a strong position to go to the investment community, the studio decided to pursue the A-round route.

"We didn't need to prove our viability," explains Henrique. "We'd been successful – and profitable – for a number of years, and our sustainability wasn't in question."

After putting together a carefully researched long-list, Bossa Studios met with about 40 potential investors to gauge their objectives, the value they were looking for in a business, and the potential to build on each other's strengths.

This led the company to a $10 million deal led by tech VC Atomico. Existing investor London Venture Partners remained involved.

"This is one of the most important business relationships you'll have, so do your due diligence.

Henrique Olifiers
Co-founder, Bossa Studios

Talent push

Henrique now has one overriding priority: talent. The aim is to grow the workforce from 55 employees to 100-plus.

This is still relatively small for a major game developer – the biggest employ several hundred. So it's important for Bossa Studios to attract what Henrique calls "really special talent".

"Our USP depends on having exceptional talent at all levels – from the strategic direction on the board to our creative developers," he explains.

Bossa Studios hasn't delayed in making a marquee hire. The firm recently recruited Chet Faliszek, one of the world's most renowned game visionaries.

Know your investors

Henrique believes the key to a successful A-series is to know your investors.

"This is one of the most important business relationships you'll have," he says. "So do your due diligence."

Start by researching the fund's investment portfolio and track record; ask around to find out more about the fund and individuals involved. You also need to think strategically about the skills and value each investor will bring.

Once you've made up your mind about who to approach, it's crunch time.

"You've got to make your pitch count," says Henrique. "It needs to be a well-crafted, concise summary of what makes your business a high-growth prospect. You don't have long to impress a potential investor, so work out how to get your vision across fast."

But remember, you also need evidence to support the growth story you're pitching.

"We're ambitious," says Henrique. "But our ambitions are grounded in reality, as we have the data to prove our forecasts."

Series B

What is it?

To state the obvious for a moment: series B funding follows the series A. It is used to finance a business as it reaches new goals and expands its growth.

Different firms have different levels of capital requirements at the series B stage. But it will typically generate between €10 million and €20 million euros, says Jeppe Zink of Northzone.

Who is it for?

Series B-funding is the scale-up round. It allows entrepreneurs to really accelerate growth, taking their venture to the international, or even global, stage.

Jeppe says that to attract series B investment, a company needs to have a product that's gaining traction in its market. The founders must be confident that within a relatively short time, it will be hitting the sorts of metrics that demonstrate hyper-growth.

> **Without real progress, new investors won't be tempted to put money in, while existing funders will be disgruntled if the valuation falls.**
>
> Jeppe Zink
> Northzone

What are the key criteria and terms?

The key to a successful B-round is to show investors substantial progress since series A.

"That's how you justify a higher valuation at the B-round," explains Jeppe. "Without real progress, new investors won't be tempted to put money in, while existing funders will be disgruntled if the valuation falls."

Other than that, investors judge businesses against similar criteria to those for earlier rounds.

Jeppe explains: "They will ask questions like: do we love the product? Now that it's in-market, do customers love it? Is it solving a genuine problem? How big is the potential market? And is the team high quality?"

The mathematics behind the investment is also important. "To write a €10 million cheque for 20% of the business, investors need to believe you can return close to ten times that amount to them in the future," Jeppe says.

"So if the business is worth €50 million at the B-round, your investors must be convinced that it will be worth €500 million someday. And that's before you add more investment further down the line."

In addition, Jeppe warns that the founders will need to be prepared for yet more dilution – a process that, as noted, begins at the A-series stage. "The founders will need to make sure they keep enough skin in the game to stay incentivised."

What are the advantages and drawbacks?

Series B finance helps the business to achieve the bullish growth it's been striving for, and shown the potential for, from day one.

But it can be a difficult time for a business.

"Hitting that growth curve isn't easy. It requires the company to professionalise," Jeppe says. "That can affect morale, and can be hard for entrepreneurs who've put their own stamp on their business."

However, your VC should be willing to support you through this challenging stage.

"At Northzone, we work hard to be a partner to our entrepreneurs," says Jeppe. "We offer strategic advice, market intelligence, help with planning and recruitment, and introductions to partners and potential customers."

VCs should also help businesses to access future funding rounds, according to Jeppe. "We're here to help make sure you're following the right process, meeting suitable investors, and pitching your business to them as effectively as possible."

Hitting that growth curve isn't easy. It requires the company to professionalise.

Jeppe Zink
Northzone

SERIES B CASE STUDY: **YOYO WALLET**

Yoyo Wallet's mission is to transform the retailer-customer relationship. Its mobile wallet combines secure mobile payments, automated loyalty and digital receipt collection.

With the Yoyo app, customers get a mobile payments and rewards experience in one, collecting points, stamps and vouchers as they spend. Transactions give retailers valuable basket data, with which they can analyse customer preferences and behaviour, and create more personalised loyalty and marketing campaigns.

Initially bootstrapped, Yoyo Wallet launched in 2013 to universities in the UK and Ireland, as well as several corporate clients, including Hilton and JP Morgan. The firm then secured two seed rounds, totalling around £2 million, from incubator Touchstone Innovations. An A-round worth £6 million followed, led by Touchstone.

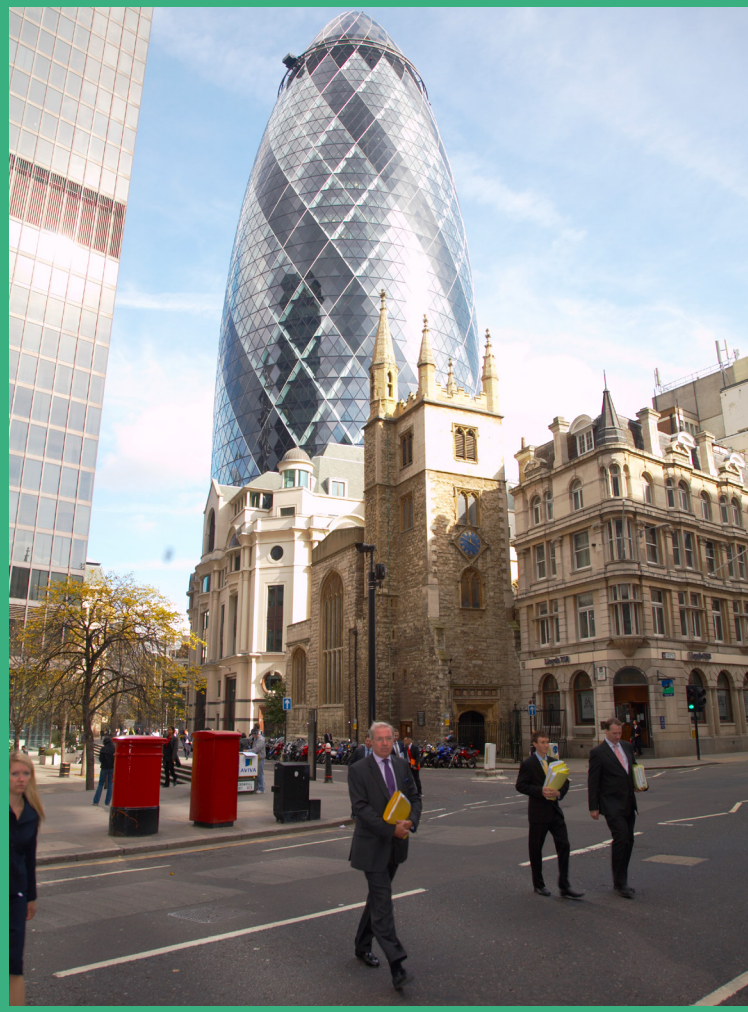
Co-founder Alain Falys takes up the story: "The A-round allowed us to really invest in the product, and give more focus to the loyalty data side of the business."

The next 18 months saw impressive growth, he continues. Yoyo went from 20 university clients to 70-plus; from a few dozen corporate accounts to over 200; and from a small high-street presence, to partnerships with the likes of Planet Organic, Harris + Hoole, and Caffè Nero. "We're proud to say the app processed its 10 millionth purchase in March 2017."

Revenues grew significantly as a result, providing the firm with the sustainable income to justify going for a B-series.

"You'll also have to convince them that your business is special. And the only way to do that is to get in front of them and tell them your story.

Alain Falys
Co-founder, Yoyo Wallet



Opportunities knock

A start-up usually has to put in enormous amounts of groundwork to find B-round funders. But in this case, the investors found Yoyo Wallet – not once, but twice.

As the firm was researching potential B-round investors, German retail and wholesale giant Metro Group made an approach.

"Yoyo's aim was always to expand beyond student and corporate environments to the high street," says Alain. "Metro Group saw that our solution could have a meaningful impact on a wide spectrum of retail businesses."

After high-level due diligence, Metro Group made a headline offer. And that's when renowned fund manager Neil Woodford CBE came knocking.

Woodford joined a Metro-led, £12 million B-series funding round. Touchstone Innovations and some of the firm's early angel investors remained involved.

Going for growth

Yoyo Wallet now has the finance to invest in further product development. To accelerate innovation and maintain its market-leading position, the company is hiring software engineering talent.

The series B funds will also be ploughed into sales and marketing, as it's "strategically paramount" to increase the firm's footprint in the retail sector.

International growth is on the agenda too. To date, foreign expansion has followed the international footprint of Yoyo Wallet's customers and investors. But now the firm is putting out feelers in multiple territories: Germany, Poland, Ireland, Singapore, Japan and the US.

The firm has already joined a trade mission to the US as part of the Mayor's International Business Programme, and Alain is excited about the potential growth that could come through the programme's global network. "For us, the value of programme is in that network," he says.

Choosing your moment

A B-round makes sense for start-ups once they've a degree of revenue traction and a proven business model, says Alain.

"The unit economics need to make sense," he explains. "It won't be enough to demonstrate user growth; investors will want to see monetisation of that user base.

"You'll also have to convince them that your business is special. And the only way to do that is to get in front of them and tell them your story."

> **Metro Group saw that our solution could have a meaningful impact on a wide spectrum of retail businesses.**
>
> Alain Falys
> Co-founder, Yoyo Wallet

LATER-STAGE EQUITY FINANCE CASE STUDY: **ANTIDOTE**

As any entrepreneur will tell you, a successful business needs to solve a genuine problem.

For Antidote, the problem couldn't be clearer: 80% of clinical trials suffer delays due to a lack of patients. The solution? A platform that taps into millions of potential patients.

By using machine learning, Antidote matches patients to trials with greater precision than has previously been possible. It currently reaches more than 195 online health communities.

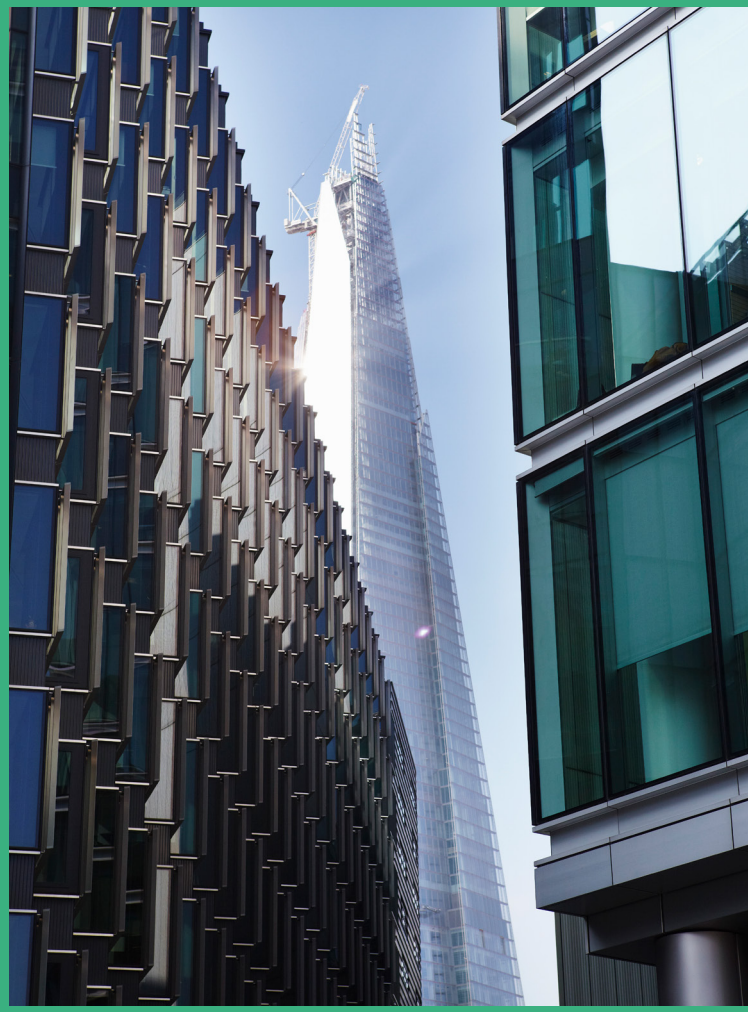
The platform has encountered strong demand in the US, where most of the firm's sales operations are based.

As a UK-based start-up doing most of its business in the US, Antidote has had "extraordinarily helpful" support from the Mayor's International Business Programme, says Chief Patient Officer Sarah Kerruish.

She explains: "The programme's Female Founders mission gave us fantastic exposure and invaluable contacts. Now, wherever we go, the people we speak to have heard of us."

To prove her point, former US Vice-President Joe Biden invited Antidote to be part of the Cancer Breakthroughs 2020 initiative programme's global network. "For us, the value of programme is in that network," he says.

> **The programme's Female Founders mission gave us fantastic exposure and invaluable contacts. Now, wherever we go, the people we speak to have heard of us.**
>
> Sarah Kerruish
> Chief Patient Officer, Antidote



A conventional journey

The firm's funding journey has so far been "conventional". The initial seed and subsequent venture rounds, including an A and B series, have totalled $15 million.

Most recently, Antidote secured a further $11 million in a round led by Merck Global Health Innovation Fund. Existing investors Smedvig Capital, Amadeus Capital and Octopus Ventures have remained involved, giving Antidote what Sarah calls "a huge vote of confidence".

In Merck, Antidote has found the perfect strategic investor for the business.

"They understand our space, and the issue we're addressing," says Sarah. "And they're adept at bringing together companies to create eco-systems to solve big problems. That's exactly what we're trying to do."

Antidote is using the latest funds for three key purposes. First, to expand the team, focusing on sales, marketing and engineering in particular. Second, to improve the way data from thousands of clinical trials is structured. And third, to keep the platform up to date with the changing nature of clinical trials in the age of precision medicine.

Think big

From Antidote's experience of venture funding rounds, Sarah has some bold advice for entrepreneurs.

"Don't be afraid to approach the big investors," she says. "And don't shy away from approaching the US investor community."

The recent successes of UK start-ups have made US investors take note, according to Sarah. "More and more British entrepreneurs are building the sort of scalable solutions that American venture capitalists are looking for.

"So be confident in what you've built, and go for it."

Don't be afraid to approach the big investors. And don't shy away from approaching the US investor community.

Sarah Kerruish
Chief Patient Officer, Antidote

A two-way process

Investors will scrutinise their target companies to the nth degree. But it's a two-way process, Sarah points out. Entrepreneurs need to know that their financiers will support them when the going gets tough.

"Do your due diligence on potential funders, just as they will on you," she advises. "Investors all have their own style and way of working with investees, so you need to be sure that they're right for your business."

She suggests getting reference checks on investors, and seeking advice from those who've been there and done it. "Talk to others who've completed the same funding rounds you're going through," she says. "You can learn a lot from their experiences."

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ALTERNATIVES TO EQUITY FINANCE

Broadly speaking, funding options for start-ups break down into two distinct categories: equity and debt.

Debt finance often comes in the form of bank loans, secured against the firm's assets. But start-ups may not yet have the necessary assets. In which case, there's a range of alternative debt options available, which we'll look at in more detail below.

Kevin Smith of KPMG explains: "Traditionally, debt has been difficult for early-stage businesses to secure. But more providers are now creating offerings for companies with less of a track record."

Taking on debt may be better suited to founders who aren't yet ready to give up ownership of their venture, in the view of Jason Hill, Head of Challenger Banking at PA Consulting.

"If you're reluctant to relinquish control, or dilute your holding in the business, then you might prefer to take on debt," he says.

BDO's David Bevan makes a similar point: "The decision comes down to whether the shareholders are willing to sacrifice equity in their business in exchange for cash, or take on debt to get the money upfront."

That's not to suggest that entrepreneurs face a stark choice between debt and equity.

The two forms of finance should "work hand in hand," according to Simon Hay, co-founder of educational technology platform Firefly Learning. "They're there to solve different problems," he says.

> **Venture debt isn't an alternative to equity – it's really there to complement an equity raise.**
>
> Andrew Parker
> Silicon Valley Bank

Debt finance and venture debt

What is it?

The term 'debt finance' generally refers to business loans: money lent to companies, usually by banks, with an interest rate and maturity date attached. These are typically secured against the company's assets – for example, its premises, trade debtors, intellectual property and/or cash flows.

Start-ups, however, may not yet have any such assets, and may not yet be generating cash. Fortunately, alternative debt financing options are tailored to the needs of fast-growth innovation businesses.

Institutions like Silicon Valley Bank specialise in lending to such companies, offering debt products such as venture debt, growth capital, recurring revenue lines and working capital.

Vice-President Andrew Parker explains the bank's approach: "When lending to a pre-profit business, we typically look at its growth, and therefore its ability to attract equity investors, or transition to profit, in the future."

Who is it for?

Silicon Valley Bank works with tech and innovation firms throughout their lifecycle, from pre-revenue through to IPO and beyond. As a rule, Andrew suggests that earlier-stage firms consider venture debt or growth capital when they're beginning to think about an equity round.

"Venture debt isn't an alternative to equity – it's really there to complement an equity raise," he explains. "It's an additional source of capital to allow a company to build value."

What are the key criteria and terms?

For lenders like Silicon Valley Bank, borrowers must be innovative, disruptive, high-growth ventures.

"We fund technology and innovation businesses that are disrupting a market, or creating an entirely new one," says Andrew. "That means having a unique and defensible proposition that can't easily be replicated."

According to Andrew, the main terms a business needs to consider when taking on debt are:

- The loan amount and period – how much you're borrowing, and for how long
- The total cost of the debt – the interest rate, plus any arrangement and/or early redemption fees
- The security – the assets against which the lender can claim should you default
- The warrant – the option for the lender to buy a small amount of equity in the company
- The covenants – the financial parameters the business borrowing the money must perform within (such parameters are a condition of some credit facilities)

> **Your lender should work with you to agree the right amount for the business, and the ideal balance between debt and equity.**
>
> Andrew Parker
> Silicon Valley Bank

What are the advantages and drawbacks?

Debt finance provides what Andrew calls a "cash runway", which a firm can use to grow its revenues – and therefore the valuation of the business.

The company may then use it to hire the necessary talent; develop and expand its products; run customer acquisition campaigns; enter new markets; and so on.

Another advantage is that unlike equity, debt brings about little or no dilution of ownership. Existing shareholders need give very few shares – if any – to the lender to raise the finance.

And as noted, debt is there to work alongside equity finance. Lenders will work collaboratively with shareholders. And like VCs, they should have networks of potential customers and suppliers, potential hires and future investors to bring to the table.

Companies should be mindful that the debt has to be repaid, however – and by a set date, Andrew cautions.

"Think carefully about how much you can borrow, and how much you can afford to repay. It's important to be prudent with debt financing. Don't be tempted to overburden the business – or yourself – just because it's available.

"Your lender should work with you to agree the right amount for the business, and the ideal balance between debt and equity."

And choose your lender carefully, says Andrew, by doing as much due diligence on them as they'll do on you.

"You'll want a provider with a track record of being patient, and of supporting businesses through thick and thin. After all, you're looking for a long-term partnership."

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EXIT

Not every founder starts a business intending to hand it over someday. But for many ambitious entrepreneurs, exit is often the end-game. Their ultimate aim is to cash in on the success of their venture. And as we saw in part 1, later-stage investors will often want to see a clear exit plan before putting money into a business.

There are two routes to business exit: sell the company to a larger organisation (acquisition), or float it on a stock exchange (IPO).

That said, neither acquisition nor IPO has to mean an immediate exit. The founding team may wish to remain on the board, to help steer the firm's future growth. In fact, investors may insist that they stay involved for a number of years.

In this section, we'll explore IPOs and acquisitions in more detail. Which strategy is right for your business? What will you need to do to persuade investors to buy? And what preparation is required to make the transaction happen?

M&A

What is it?

When it comes to mergers and acquisitions, we're more concerned with the 'A' than the 'M'. Start-ups are far more likely to be acquired by a larger organisation than form part of a merger of equals.

As a funding mechanism, being acquired opens up a larger pool of financial capital.

At the same time, it can also be a powerful growth strategy, as it should give you access to new customers and markets.

The firm making the acquisition may have a number of motivations. It might be looking to consolidate its supply chain, enter a new market itself, or drive synergies and exploit economies of scale.

Who is it for?

Being acquired can have a number of advantages for entrepreneurs, according to John Cordrey, Private Equity Investment Manager at Foresight Group.

"It can be good for businesses that are capital constrained, or where the founders want to de-risk and take some money off the table," he says. "It can also help reinvigorate growth, as well as providing the funding you need to invest in growth."

You'll want to consider how much equity to retain, John advises. "The acquirer is ultimately there to help you increase the overall equity value in the business. So it can be a great way to increase your personal equity value."

However, there's no golden rule for deciding when to put your business up for sale. It's very much sector-dependent.

A young tech company, for example, may have an innovation that's in hot demand, and find itself being snapped up at the pre-revenue stage. By contrast, a traditional engineering business would probably need at least £1 million EBITDA to appeal to a buyer – or ideally £2 million-plus.

It can be good for businesses that are capital constrained, or where the founders want to de-risk and take some money off the table.

John Cordrey
Foresight Group

Be upfront about whether you intend to stay on and help take the business to the next level. And whether you want to take all of your cash off the table, or defer some of the payout.

John Cordrey
Foresight Group

What are the key criteria and terms?

Potential buyers will want to see a credible growth plan, and will expect you to have established a second-tier management team.

"You'll need to be clear on your exit strategy too," says John. "That means being upfront about whether you intend to stay on and help take the business to the next level. And whether you want to take all of your cash off the table, or defer some of the payout."

There are plenty of other issues for founders looking to sell their firm, John points out.

You'll need to get a sense of the headline price your business can fetch; what synergies or value drivers there are for each prospective buyer; and what you could raise from alternate options, such as a bank, IPO, or a sale to a second tier of management.

Other questions to consider include:

- How much equity can you expect to retain if you stay on?
- Will you be offered options?
- How much cash will you receive on day one if exiting?
- Will there be an element of deferral – and for how long?
- How will your performance be measured when determining your payout?

With all this in mind, you need to do your research, John advises. "Then approach a select number of potential buyers, making sure you understand each one's potential motives to acquire your business.

"This creates competition, pushing up the price and giving you leverage when negotiating the equity and payoff terms."

What are the advantages and drawbacks?

As well as gaining access to capital, customers and markets, becoming part of a big, established organisation gives you more security. And if you don't want to remain in the business, it gives you a chance to exit.

Either way, you'll have the opportunity to cash out, and reap the rewards of all your hard work to date – particularly with a private equity purchase.

The obvious downside, of course, is that you'll lose day-to-day control of your 'baby'. But there are other pitfalls to be mindful of.

"You may encounter a culture clash, integration issues or conflicting objectives between the two companies," warns John. "Many a study has highlighted the number of M&A's that fail to deliver the expected value. So be sure to research your potential investors or acquirers carefully."

ACQUISITION CASE STUDY: **TRANSLATE PLUS**

Compared to many start-ups, translate plus has gone about things differently. And not entirely by choice. The language services provider – now one of the world's top 50 – was founded in 2008, when funding wasn't exactly in plentiful supply.

The two co-founders got their business off the ground with some fairly stringent bootstrapping. They paid themselves nothing for the first six months, living off their personal savings.

"We didn't go down the classic start-up route, taking on debt and developing the business to profitability over several years," says Co-Managing Director Robert Timms. "We made sure the firm was making money at the outset."

An international offering

Given the nature of its proposition, international growth has been a natural part of the firm's journey.

London-based, translate plus initially moved into Germany and Denmark, as the founders were familiar with these markets. By 2015, business had expanded to 50 countries.

Robert highlights how the Mayor's International Business Programme has been a key support to this aspect of the translate plus growth story. "For example, joining Sadiq Kahn's US trade mission was hugely beneficial," he says.

"We didn't go down the classic start-up route, taking on debt and developing the business to profitability over several years.

Robert Timms
Co-Managing Director, translate plus

The pivotal point

Re-investing profits kept the founders in complete control of the company for the first seven years. It wasn't until 2015 that they decided to seek funding – and decided to look for a buyer.

"The business reached a point where it was time for a transformative leap," Robert explains. "While for us as founders, it was time to de-risk, and gain some reward for our hard work."

While looking at various funding options, they discovered that cross-media marketing production company Prodigious – part of communications giant Publicis Groupe – wanted to add language and adaptation services to its offering.

"Being acquired by Prodigious was the ideal solution," Robert explains. "It had the ready-made global scale that could transform translate plus. Strategically, there was no overlap of services. And it offered the right level of de-risking, as an established and financially secure global business."

Acquisition

The two firms entered early discussions "to see if they were both serious," as Robert puts it, and to explore the cultural fit between them.

The conversations proved positive, and soon progressed to giving Prodigious a more detailed view of translate plus: its procedures, plans, forecasts, sales pipeline, and so on.

The next step was to negotiate high-level terms: the price and financial structure of the deal. Once these were agreed, the companies signed a Letter of Intent. Due diligence followed, then contracts were drawn up by lawyers, and signed by the directors of both firms. translate plus became part of Prodigious in July 2017.

The process was straightforward, but that doesn't mean it was easy. "It was nine months of incredibly hard work," Robert cautions. "Huge amounts of prep were required, and we still had to keep the business running.

"You must understand what's involved before going into an acquisition. Then ask yourself: are you ready for it?"

Scaling up

The plan is now to scale up the business, by capitalising on the significant international network that Prodigious has. With Asia-Pacific a key focus, translate plus has opened an office in Tokyo.

Looking back on the experience, Robert has two valuable pieces of advice for start-up founders considering selling their business.

"Sell when you want to, not when you have to," he says. "And know what you want from the acquisition.

"For example, is your aim to exit the business, or stay involved in growing it? The two scenarios will make for very different deals – and very different buyers."

Sell when you want to, not when you have to. And know what you want from the acquisition.

Robert Timms
Co-Managing Director, translate plus

IPO

What is it?

IPO stands for Initial Public Offering. Also called a flotation or stock market launch, it's the first time a firm's shares are made available to the public on a stock exchange. In the UK, that means the London Stock Exchange (LSE).

The LSE is actually two exchanges – the Main Market and Alternative Investment Market (AIM). The main market is divided into three segments: standard, premium and high-growth.

Who is it for?

"IPO is a way to secure significant investment when a business needs to make a step-change in its growth," says Jason Hill of PA Consulting.

It's often thought of as the domain of so-called unicorn businesses. But it's more attainable than you might think, according to James Clark, LSE's Head of Tech and Lifesciences, Primary Markets.

If it is your intention to float, you must be able to give investors confidence that your business will offer them long-term returns, James Clark stresses.

He also highlights the need to begin conversations with LSE as early as possible if you're targeting an IPO – as early as the seed stage.

"There are a lot of steps to go through, requiring a lot of preparation, so it's helpful to start considering what that means for your business when you have more time to plan. You'll need to understand the scale of the task, and be thinking about what to do, when."

What are the key criteria and terms?

A business must be on a healthy growth path to achieve IPO.

"You're looking at growth of between 10% and 60% annually, and sustainable revenues of at least £5 million a year," says James. "You don't need to be in the black yet – but you will need to demonstrate a clear path to profitability."

Conducting an IPO forces a business's owners to think very carefully about what they intend do with the money raised – more so than any other funding type.

"Investors will want to know what your growth strategy is, and how you will deliver it," explains James. "You're going to have to tell that story to the market to convince them to buy a stake in your firm."

IPO is a way to secure significant investment when a business needs to make a step-change in its grow

Jason Hill
PA Consulting

What are the advantages and drawbacks?

Once you're listed on an exchange, much of the hard work is done.

"The transition to public company is challenging, but raising finance will be much easier in the future," James says, "as you can keep going back to the market for more capital."

The listing process is onerous – with good reason. It takes a huge amount of work to make a firm operationally, financially and culturally fit for life as a public company.

Disclosure requirements, required to protect investors, will mean taking on auditors. And the make-up of your board and management must be right. "Some of your directors will need to know how to run public companies," James advises. "Investors will want to see that experience on the board."

Then there's the business valuation, followed by a 'roadshow', where the owners meet potential investors to try to drum up interest in their IPO. This is one of the final stages in the process of actually being listed on the exchange, which itself takes three to five months.

"Being listed is a fundamental cultural shift for a business," James affirms. "So it's worthwhile starting to prepare for it a good couple of years prior to IPO."

"The transition to public company is challenging, but raising finance will be much easier in the future.

James Clark
LSE

IN SUMMARY

Three key pieces of advice come through time and again in what our mentors and programme members tell us on the subject of raising finance:

1. Know the market

Research the investment community extensively before making any approaches. Ask around about potential investors to see what people think of them. "Talk to your network, find out what's worked for them," is the advice of Kevin Smith from KPMG.

2. Choose carefully

Having done your homework, be strategic about who you take money from. Be clear on what your investors bring to the table, over and above finance, that can help your business grow. "Your aim should be to find a strategic investor, ideally with experience of your sector, and in the regional markets you intend to target," says BDO's David Bevan.

Talk to your network, find out what's worked for them.

Kevin Smith
KPMG

3. Be prepared to work hard

Researching and meeting investors, developing and maintaining relationships, pitching your business, due diligence, negotiating terms... Raising money takes a lot of sweat and toil. "It's a critical decision, which will define the shape of your business in future years, as well as your control over it," PA Consulting's Jason Hill signals. So be ready to work at it.

And while doing all of this, you still need to keep the business on track. Each funding round will take you out of the business for many months, during which you're not working to keep the business on its growth trajectory.

Yet taking your eye off the ball will put you behind your plan – which could frustrate existing funders, and discourage future investors.

Such is the balance entrepreneurs must strike as they drive their businesses forward along their development and funding journeys. As Tony Hsieh, CEO of online fashion retailer Zappos, once said: "Chase the vision, not the money. The money will end up following you."

GET INVOLVED

The Mayor's International Business Programme supports the global growth ambitions of London's businesses. The 12-month programme includes mentoring, expert advice and real business opportunities for high-growth companies in the life sciences, technology and urban sectors.

For more information on the programme please visit **gotogrow.london**

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