As a start-up entrepreneur, you still have enough funding options

Right product and realistic projection of cash flow and customers can attract funding even as investors hesitate to write cheques in the current environment

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The Securities and Exchange Board of India (Sebi) recently warned investors about the legality of crowdfunding. "Electronic platforms facilitating fundraising on digital platforms are neither authorised nor recognised under any law governing the securities market," said the Sebi note. According to the market watchdog, such platforms, open to all investors registered on these, amount to a contravention of the Securities Contracts (Regulation) Act and the Companies Act. It has also asked some companies to stop on-boarding of new investors.

Entrepreneurs, who are always seeking investors, will feel a little hard done by Sebi's warning. But, there are other reasons as well. Venture capital funds and angel investors who were willing to fund start-ups are asking more questions before signing on the dotted line. According to Paula Mariwala, co-president, Stanford Angels & Entrepreneurs India, funding is becoming more rational. "It is not that it is not available but it's not as easy as before. In that context, entrepreneurs need a solid plan. While early-stage investors do understand that there may not be revenue or many customers to begin with, they (investors) look for a clear path to a sound and sustainable business model and a path to profitability," she explains.

Raising additional cash has become more difficult now because many investors still haven't got an opportunity for exit. This kind of rethink on additional deployment resulting in temporary slowdown is typical after a long cycle of massive inflows, says Bharat Banka, former head of a private equity fund and FideliMent Ventures founder. "Investors will fund ventures but they will ask founders to tighten the business," he says.

Hence, it is important to generate cash flows and have some paying

customers, says Mariwala.

Need to have Vs nice to have: It is easier to get funding if you are addressing a key problem. "In good times, all kinds of companies get funds. But, if you sell a problem-solving solution, you will always have a market, even if the economy is bad. It is a toss-up between 'nice to have' and 'need to have'. If you create a 'need to have' product, customers will be willing to pay for it upfront. But, if it is a 'nice to have' product, the customer will take his own sweet time to pay," says Arun Natarajan, founder and CEO of Venture Intelligence, a data and analytics firm. If you have worked in an industry for a long time, you can identify the gaps that exist and address that.

Business plan with visibility of profitability: In addition to a good idea, you also need a solid business model and some path to profitability. If not, at least a visibility of what is required to reach profitability. "Founders should have a clear idea of how they will generate and exactly how much money is required. It cannot be an infinite amount," says Mariwala. She cites the example of a start-up in the fintech sector. While their product was good, the investor was not willing to put money in immediately. The founders were asked to explain how customers would adopt the product. They were asked to do a pilot project and come back with a revenue model on how much money would take them where.

"The investors waited for them to come back with more details on how they would execute and how they will reach scale. The founders were asked to list who the customers were, how they would reach them and why customers would change to this product," she says.

Raise limited funds: Investors may prefer to give money in tranches similar to the slab-based payment for property. So, entrepreneurs must make their business plan accordingly, says Banka. "If your venture does not require tons of money at the beginning, don't take it just because it is available. Your business should not be dependent on when funding comes because then, there is nothing for you to do," he explains.

Competition and cash flows: With investors tightening their purse strings, they might ask entrepreneurs for data points on a month-on-month progress of the venture. Entrepreneurs are also expected to think of all possible competitors – online, offline, foreign and even your customers' apathy to your product, Natarajan adds. If there is no cash flow, then you have to prepare for a very large funding. "In today's context, cash flow is very important. Understand where the cash is coming from and where it is going. Investors will look at that. Have a plan in place for generating revenue if you don't get funding. This could be by offering services while waiting for your own product to get funded," says Mariwala.

Have a balance sheet ready: While it may not be possible to have a balance sheet from day one, you must have the ability to project how the business will work on a three to five years' time. "The venture capitalist will ask for a projection for at least 18 months, if not three years. So, have a working knowledge of the financials or hire a chartered accountant," says Natarajan.

Entrepreneurs must have their Registrar of Companies filings and legal documents in place. If you have to make payments to vendors or have other loans, disclose all this in a transparent manner. Most investors do understand that there is no real financial data to see, but compliance is becoming very rigorous.

Options for start-up entrepreneurs

Investors enter at various stages, depending on the stage of the company and amount needed

Angel investors: For amounts up to ₹2 crore, you can approach angel investors. They can be anyone: friends, family, college alumni network, professionals in your industry, etc. Many angel funds co-invest with the founders while some could insist on the first round of funding from the founder.

Seed funding: For funds between ₹2 crore and ₹10 crore, you can approach seed funds.

Venture capital funds: For funds above ₹10 crore, you can approach venture capital funds.

Loans: Traditional bank funding for start-ups in India is difficult,as it is targeted at companies, which have assets that can be offered as collateral. But, there is a new hybrid product called venture-debt. These are essentially non-banking financial companies which invest into the debt and term loan after the venture capitalist has backed the venture. You don't need to dilute equity right away. The terms are similar to those of a bank but they will get a little more equity.

Crowdfunding: Despite Sebi's spanner, experts believe crowdfunding will continue. Areas such as high-end cutting-edge technological products or art-like non-mainstream movies can attract this type of funding because a number of passionate investors may want to see the product exist and are willing to pay to create it.

Government grants: One can also take a collateral-free loan up to ₹1 crore under the Credit Guarantee Fund for micro-and small enterprises, a scheme of Sidbi and the ministry of small and medium enterprises.