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Rock Center for Entrepreneurship

Fundraising Essentials

OVERVIEW

Raising capital is hard and complicated. Founders often struggle to raise capital, because they view it as a nuisance and aren't adequately prepared. But through careful preparation, founders can be better positioned to raise capital. The key elements of a blueprint for success include honing an awesome pitch, developing a well-thought-out financial model, determining how much capital to raise, targeting the right investors, and smartly executing the funding strategy. Securing funding requires commitment and focus, and for intense, short periods (of perhaps four to eight weeks) needs to be a full-time job.

5 KEY TAKEAWAYS

1. To raise capital, you need a great pitch.

For an early-stage company, a great pitch is about communicating a compelling story and vision. An investor will want to know "Why you?" and "Why now?" They will want to see that you understand the market and the competitive dynamics. A great pitch is delivered through a pitch deck at a meeting, though a growing trend is to provide a short video ahead of the meeting.

> **Pro tip:** People want to invest in big visions about the future. Your pitch needs to communicate the opportunity you see, your vision, and why you and your team can achieve this vision.

2. A prerequisite for raising capital is a clear, realistic financial model.

Founders rarely get excited about financial models. But a financial model isn't just something to do for investors; it is something that founders need to have for themselves to run the business. A financial model provides an actual plan that the founders execute. The plan lays out assumptions and identifies growth levers. In presenting the financial model to potential investors, founders need to make the model clear and need to be intimately familiar with all aspects of it.

> **Pro tip:** Incorporate all elements of the business in the financial model. Make the model realistic, tangible, and clear . . . and know the model inside and out.

3. Founders must have clarity on how much capital they want to raise at a certain point.

Often, founders describe wanting to raise a certain amount of capital in order to hire engineers or fund marketing. But investors don't want to fund expenses or a company's burn rate; they want to fund a company to enable it to achieve certain milestones.

Founders need to view themselves at point A and think about what milestones the company will achieve at point B, when the company will need more funding. These milestones might include the company's financial run rate, the number of customers acquired, or other measures of progress.

> **Pro tip:** Don't think of the amount of capital you need in terms of expenses to be incurred; think about the amount of capital you will need in order to achieve a set of milestones that show the company is on the path to creating significant value.

4. Founders need to think carefully about finding the right investors.

To target the right investors, founders need to understand the different types of investors (see next page).

In addition to the different types of investors, identifying the right investors includes finding investors that fit with your strategy, match with your desired check size, have capital to invest, invest frequently, are interested in your space, and have backed similar companies.

Just as investors ask questions to founders, founders should ask the following questions to investors:

- How big is your check?
- How many investments do you do per year? When was you last investment?
- Are you interested in my company? (Drive investors to make a clear decision.)
- What is your process? What are the next steps?

> **Pro tip:** By focusing on the right investors, and not being distracted by the wrong investors, you will save time and increase your chances of success.

Investor Type/Characteristics	How to Research Them
Angels: Invest $10k to $50k ▪ Easiest target at early stage ▪ Price sensitive, want to be in early ▪ Target professional angels, not occasional angels ▪ 2-4 meetings to get to a decision ▪ They rely on gut, little due diligence or research	▪ Read LinkedIn and AngelList profiles ▪ Understand investment history and areas of interest ▪ Look for similar investments
Micro VCs: Invest $100k-$1M ▪ Ownership sensitive, want 8%-10% ▪ Systematic; often have a vertical focus or thesis ▪ Typically 4-6 meetings ▪ Do systematic research and references	▪ Same as Angels plus understand the focus of different partners at firm
VCs: Fund size of $100M+ ▪ Startups should AVOID VCs unless they have a seed program ▪ They want to get to know you to monitor you—but you don't have time for VCs	▪ See if they have a seed program; if not don't engage with VCs until later funding rounds

5. The key aspects of the fundraising strategy are largely the same but some elements differ based on the amount of money being raised.

Regardless of the amount of being raised, getting the first commit is really hard. Rounds accelerate after they are half full, and the price is typically set halfway through. Initial commits are smaller and later commits are larger, and—because investors have a herd mentality—a round gains momentum near the end.

For financing of $300,000 to $750,000:

- Go after angels and start with friends and family
- The first commit is key
- For the first half, focus on small checks ($25k-$50k)
- For the second half, focus on larger checks
- Leverage commits for introductions
- After a few commits, it's a numbers game

For larger financings of $1M to $3M:

- Start with smaller checks from angels
- After early commits, engage Micro VCs—and look for a lead
- The lead is a $500k-$1M check that will set the terms
- Once you get a lead, the round should come together

To manage the process, create an investor pipeline of investors who are a good fit.

For each investor, determine WHY they are a good fit. Categorize potential investors as:

- Wave A: Less desirable—practice with them to refine your pitch
- Wave B: Main targets
- Wave C: Backups

Treat each wave as a sales funnel. Treat fundraising as a full-time job. With proper preparation, commitment, and focus, raising capital should take four to eight weeks.

> **Pro tip:** The key in fundraising is getting the first commit, which communicates to other investors there is interest. Make it easy for the first commit by allowing a "soft commit" who can back out later.

ADDITIONAL RESOURCES

- See Alex's blog Startup Hacks
- Recommended reading: Venture Deals by Brad Feld

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Iskold currently serves as a coach and a VC in Residence at the Arthur Rock Center for Entrepreneurship at the Harvard Business School. He previously taught an award-winning undergraduate computer science class at NYU. He holds a B.S. in Math with Honors from Lehigh University and M.S. in Computer Science from NYU.

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