How to raise venture capital and private equity funding – a guide for entrepreneurs
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1. Introduction

A venture capital or private equity investment refers to an investment in a company by a professional investor, usually in exchange for a portion of the company’s shares. A venture capital investment is a great way to accelerate a company’s growth. The benefits of venture capital and private equity investments lie in professional knowledge of growth as well as the expertise and contacts an investor can bring in. The aim of private equity investors is to raise the value of the company through the company’s success, so that this rise in value benefits all stakeholders. Growth built with investors is also in the entrepreneur’s interest: it makes the company more valuable.

Both startups and established growth companies can raise venture capital or private equity funding. It is important for the entrepreneurs and owners to not only understand what type of an investment is the most suitable for their company, but also what type of an investment is possible from the investor’s point of view. The aim of this guide is to help you find the right partner to guide you either at the start of your path or further on the road to growth. The guide provides information on what types of venture capital and private equity investors there are, how they look for potential companies to invest in, how the investment is made, what the cooperation with these investors is like, what type of added value venture capital and private equity investors bring to the company, and how the investor can eventually exit the investment.

The guide describes factors that investors normally pay close attention to in the investment phase. It is recommended that you go ahead and look for investments, even if some parts outlined in this guide seem unfamiliar. Perhaps the most important part of a successful venture capital or private equity investment is a growth-hungry and knowledgeable management team in the target company. Many growth stories actually differ from the typical formula of making investments.
Startup
In this guide, a startup refers to a young, innovative company that usually strives for fast, international growth with a scalable business model.

Growth company
In this guide, a growth company refers to a company with not only established business and turnover, but also with potential for future growth. The company’s turnover can range from a few million euros to hundreds of millions of euros.

The amount invested into Finnish companies in the past five years by private equity and venture capital investors

4,000,000,000 €*
Five Steps to Securing Venture Capital or Private Equity Funding

1. Determine whether your company is suitable for investment

Finnish venture capital and private equity investors focus on accelerating the growth of their portfolio companies. Therefore, companies generally need to have the necessary prerequisites for growth. Some of the signs investors typically look for are clear growth potential, a diverse and committed team and management as well as a favorable market situation. Other potential reasons to search for venture capital or private equity are a generational transfer, a need to change ownership structure or large investment requirements. Signs that can deter an investor can for example be a low growth rate, weak financial viability, a difficult market situation, misaligned vision or an owner’s unwillingness to share decision-making power.

2. Find the right investor

Venture capital and private equity investors can be roughly divided into two groups by the types of investments they make. They either invest in startups or more established growth companies. In the case of startups, investors typically make majority investments. While minority investments are an option also with growth companies, in these cases, majority investments are more common. The determining factor is the need of the investee company and its owners. Investors can also specialize in a certain industry or company size, depending on the investment thesis of the fund they manage. When it comes to venture capital or private equity investments, personal chemistry is the key. While the role of the investor in the company’s operations varies, a good, effective and confidential relationship is always a vital part of a successful investment.

3. Understand the investor’s investment thesis

Venture capital and private equity investors invest in portfolio companies through vehicles called funds. The funds are typically raised from big institutional investors and aim to make a profit by exiting the investments after a certain period of time. When establishing a fund, venture capital and private equity investors agree on investment criteria with the fund’s investors. A wide range of criteria are used, such as the companies’ geographical location, industry, size, stage, role in a value chain, technology, financial viability and desired investment size, ownership share as well as return and exit potential. From a company’s point of view, it is important to form connections with the type of investors who focus on their type of companies.

4. Prepare your company’s growth path

Investors help your company grow, but even during the application phase, it is important to make sure future growth is both credible and promising. In addition, for many growth companies, private equity investment can come into question if their growth strategy includes acquiring a company, a large investment or another similar situation. Private equity investors are happy to help with growth and strategy discussions and will often bring in their own ideas, contacts and potential acquisition targets. In any case, the owners, management and staff should all be prepared to put in the necessary work to achieve the growth targets. Startup companies should also carefully prepare a pitch to present their idea, team and market potential to investors.

5. Fundraising is also sparring

Don’t be afraid to get in touch with venture capital and private equity investors – even if initial contact does not lead to an investment, you will still gain essential guidance for taking your company further.

GROWTH STORIES
Examples of cooperation between companies and venture capital and private equity investors can be found on the FVCA’s website (www.fvca.fi/in-english). The website also includes a search engine that can be used for finding suitable investors for specific kinds of companies.
2. Venture Capital and Private Equity

2.1 Is venture capital or private equity the right option for you?

2.11 Startup companies

Startup companies usually aim for fast growth. Startups are often not profitable to start out with, as they are still in the phase of building their product and looking for the product-market fit. Therefore, they often raise external funding from venture capital investors to sustain themselves. In making these investments, the investors become minority owners of the portfolio companies. Venture capital investors strive to increase the value of their portfolio companies by working actively with the teams and then exiting the investments via acquisitions or initial public offerings (IPOs).

Do you want to build an international growth story?

Venture capital investors that focus on investing in startups aim to find companies with international growth potential. The entrepreneur must be motivated and capable of building international growth.

Can you commit to the company for as long as ten years?

The growth stories of startups can be long and demanding. That is why entrepreneurs or teams looking to raise venture capital must be committed to working for a single company from 5 to 7 years. Using energy on other companies simultaneously is usually not an option.

Are you looking to enter a growing market?

Strong growth often requires that the targeted market is a growing one. The
market must also be suitable for scalable business models that enable the startup to grow internationally.

**Are you ready to give up part of your stake?**

In exchange for their investment, a venture capital investor receives equity in the company. If more rounds of financing are required, the entrepreneur’s own equity stake in a company will gradually decrease – that is, dilute. Oftentimes, later investment rounds will be bigger and the company will also be valued at a higher level. In these cases, the absolute value of the entrepreneur’s share will in fact increase, even if the entrepreneur owns a smaller cut of the company.

**Are you willing to cooperate?**

In addition to giving up a cut of the cake, the entrepreneur must be ready to develop the company in cooperation with the investor. Venture capital investors regularly work with their portfolio companies on product development, go-to-market and on raising follow-on funding, sometimes even on a weekly basis.

**Are you ready to sell the entire company in 5-10 years?**

The entrepreneur’s equity stake will decrease with each investment, and when the venture capital investor exits the company, the entrepreneur might also end up selling his or her shares. One should even be prepared to sell the entire company, in case the new owner requires this. However, the entrepreneur often remains working for the company and may even be required to do so in the terms of the acquisition. In case of an IPO, the entrepreneur usually retains partial ownership of the company.

**2.12 Growth companies**

Private equity investors fund and support the growth of more established growth companies. In these cases, most of the investment sum is paid to the old owners (the sellers), and the rest is invested in funding the growth of the company. In Finland, most investments in growth companies are majority investments, but there are also several investors who focus on making minority investments in established growth companies.

**The company must have cash flow**

Private equity investors investing in growth companies look for companies that already have cash flow. Investors look for positive cash flow and existing business, market position and organization. Private equity investors typically also take out loans for corporate restructuring. The cash flow must enable loan repayment.

**Sufficient turnover**

Private equity investors are interested in growth companies that are already substantial in size. Finnish investors accustomed to making larger investments are typically interested in companies with a turnover of at least 10 million euros, but they can also look into smaller companies. In these cases, there usually are possibilities of consolidation or corporate restructuring in the industry. For investors that focus on making smaller investments, a turnover of 2 million euros is the lower limit.
Clear growth potential
Finnish private equity investors usually want to help their portfolio companies grow in value by increasing their turnover and profitability. The target companies should have a solid basis in terms of, for example, management, organization, expertise, production and competitiveness that enables the increase in turnover and positive development in financial performance. The position of the company in the value chain must also enable growth. Sometimes, the company itself will not be a growth company, but by merging two or more companies the investor can build an interesting growth path and open up new development trends. Private equity investors can also be interested in lower-growth companies with a relatively safe market status and strong cash flow.

Interesting industry
Private equity investors normally attempt to invest in growing industries. Industry’s cyclical and its growth possibilities through internationalization also affect the investor’s interest. The more the industry has to offer in terms of growth and positive value development, the more interested the investor is.

Management and key individuals must be capable of creating growth
The company must either have a capable management team to guide it towards growth, or it must have the possibility of recruiting the necessary talents after the investment. The company’s management must have the right amount of vision and drive to build growth.

Are you willing to give up your stake or to broaden the ownership base?
A private equity investor will often buy the majority of the company. There are, however, investors that are also interested in minority ownership. In a majority investment case, the seller can retain a portion of the ownership or the seller can be required to invest a part of their purchase price back into the company. This is especially common in cases where the seller opts to remain working for the company. If the management team has not been an owner of the company, the entry of a private equity investor will often lead to a rearrangement of partnerships. The company is typically sold on to the next buyer after 3 to 7 years. The new owner will then redefine the management team’s incentive and commitment schemes according to its own strategy.
2.2. Reasons to look for venture capital or private equity investment

Venture capital or private equity investment offers many advantages when compared to other forms of funding. An investment does not only mean money, but also expertise, contacts and partnership. The investor will benefit from the success of the company: thus the entrepreneur, the management and the investor all have the same interests at heart. The goal of the investment is to increase the company’s value through growth, which will end up benefiting all owners.

Increasing the value

During the investment, the entrepreneur or seller usually gives up some of his or her ownership in the company. In five years, after growth built together with the investor, the remaining ownership can be worth more than the original stake in the company.

Splitting the risk

Investment by a venture capital or private equity investor is usually done in a form of equity financing. Compared to a bank loan, an equity investment has weaker terms in the case of bankruptcy from an investor’s point of view. In principle, the investment will not be repaid to the investor during the investment period. This means that the investor shares the business and ownership risk with the entrepreneur and management. Investors stand to profit from the investment only if the value of the company grows, and this success is measured in the exit phase.

Faster growth than with cash flow financing

Growing with cash flow is slow and for companies striving for fast growth, it can even be impossible. In the case of growing industries, there are usually many companies vying for a shot in the same markets. Companies that are able to accelerate their growth and invest in the future with the help of external funding can gain a definite advantage that only continues to grow year by year. This is how markets can slip away from companies that may, for example, have the best technological solution, but not enough funding to grow while operating at a loss.

Expertise and contacts

With the help of venture capital and private equity investors, companies gain access to vast amounts of expertise from different fields and industries. Investors have generally invested in a large group of growth companies. Through this, they have experience and knowhow of the pitfalls and shortcuts of growth. From this familiar group of companies, it is easy to look for good operational models, practices and benchmarks for various things such as scaling to different markets. Startups often need 3 to 4 rounds of financing to accelerate their growth, and experienced venture capital investors can help their portfolio companies raise these follow-on financing rounds. Private equity investors can then again support their portfolio companies with additional financing when needed, for example in cases of larger acquisitions.

Funding for change

A private equity investment in a growth company usually requires that there is an internal desire for change within the company. Say, a large company wants to withdraw from a type of business that is profitable, but not at its core. An entrepreneur wants to grow and scale a company, but needs additional resources and expertise. A public actor wants to privatize an establishment. A company’s owners recognize a need for restructuring. An entrepreneur wishes to retire in the coming years. These are just examples of situations where venture capital or private equity investment can be a natural solution.

Fulfilling dreams

An investment by a venture capital or private equity investor can bring about the fulfillment of an entrepreneur’s dreams. Investors bring in added resources and expertise that can help the company grow larger and more valuable than without external funding – often faster than its peers.

Allocating wealth

An established growth company may be very profitable even before the investment. Through a private equity investment, an entrepreneur receives a significant portion of the company’s value as cash (or even the whole value of the company, if the arrangement does not include an investment back into the company). This can help in diversification of the entrepreneur’s wealth, as a smaller portion of his or her assets will be tied to a single company. For the owners of startups, a venture capital investment can reduce the need for other forms of funding and therefore lower personal risk.
Goal-oriented board work

A venture capital or private equity investor often brings along a professional governance model to the board of directors. As many entrepreneurs may not pay too much attention to board work in the earliest stages, investors can help establish good governance principles. This is also a prerequisite for later acquisitions or IPOs.

2.3 Why wouldn’t you be the best fit for venture capital or private equity investment?

You only want money

A private equity or venture capital investor brings in not only money, but also expertise. The entrepreneur must be ready to work with the investor. In exchange for capital, the investor will demand decision-making power over the company: the more they have invested and own, the more say they would like to have.

You don’t want to give up ownership

The advantages of venture capital and private equity investments are equity financing and partnership. In order to reap these benefits, the company must be run in cooperation with the investor. Ownership will also be divided between the entrepreneur and the investors.

Contradicting incentives

Patents and other rights pertaining to the business model should be in ownership of the company that is seeking funding.

Inadequate growth opportunities

In order to interest investors, startup companies must both target international markets and have potential for growing fast enough. A startup operating on a national level does not usually offer adequate growth opportunities. Established growth companies can operate in a domestic market, but they must be able to show sufficient growth potential or otherwise meet the investor’s criteria.

You have multiple projects

An entrepreneur must be willing to work in the investee company. An investor will not want to commit themselves to a team that divides their time and energy between multiple companies and jobs.
3. Finding funding

Many companies are seeking for funding. Especially in the startup scene the amount of eager companies far outnumbers the capital available. Since not all discussions with venture capital and private equity investors lead to an investment, it is essential to prepare well for your negotiations.

3.1 What do investors look for in a company?

3.1.1 Startups

An investment decision of a venture capital investor is a sum of many parts. Before you attempt to raise funding, think through how the following things are solved in your company.

Do you have a technological advantage?

Growing markets are also often competitive. Patents that support your business plan or innovations that bring a sustainable advantage to your company can help convince investors.

Does your team have the right expertise?

Venture capital investors put a lot of emphasis on the team. In addition to the current lineup, investors are interested in the company’s ability to recruit leading talent. Investors expect companies to understand the strengths and development needs of their current team, along with how to build their team up. Key personnel must be kept committed to the team with contracts and financial incentives.

Is the company in the right phase?

Timing, the size of the investment and the developmental stage of the company play a huge role in the investment decision. Venture capital investors often choose a specific stage and investment size they focus on. Investors investing in startups typically seek for a 10-30 percent stake of the company.

Is the business model scalable and is there proof of international demand?

While a startup does not need to be profitable at the time of investment, they generally do need to have proof of demand and interest, a working business model and even proven success in internationalization. A scalable business model is a prerequisite for internationalization. The company must be able to display their sales pipeline: how many possible clients it has, how those prospects can be reached, how they will convert into clients and whether their product or service is able to retain clients. An investor looking for scalable growth will also be interested in hearing about customer acquisition costs in terms of time and other resources.
Solid contracts
Startups grow quickly, so their documentation is typically not at the same level as that of established companies. Relevant contracts do, however, need to be in place. For example, shareholders’ agreements must be established and any intellectual property rights need to be owned by the company itself. Contracts of employment must also state that employee patents belong to the company.

Estimate of required funding
Startups typically raise multiple rounds of funding. Venture capital and private equity investors are interested in a clear estimate of how much future funding is needed to achieve later stages of growth.

3.12 Growth Companies
When investing in an established growth company, a private equity investor will typically evaluate the company in light of achieved financial results. The investor will already mentor and assess the company in the research phase, which is called due diligence. That is why negotiating with an investor can develop the company further, even if discussions do not lead to an investment.

Management and the management team
A private equity investor must believe in the skills, motivation and vision of the company’s management and management team. Oftentimes, investors will only invest in a company whose management will commit to becoming an owner.

Strong company culture
For a private equity investor to help a company achieve growth, the company must have a solid company culture. A strong company culture is especially emphasized in situations where an investor merges two or more companies.

Indication of growth
The company’s management, strategy and numbers must showcase potential for growth and value increase. If the company has not grown without the help of external funding, it is not self-evident that an investment would help. However, sometimes an investment by a private equity investor can be the crucial factor that leads to a path of growth. This can happen through an acquisition, investment, development project or simply through refined strategy. On the other hand, investors can also be interested in lower-growth companies with a steady market position and strong cash flow.

Plausible growth strategy
The company and its management must have both a desire for and a plausible vision of future growth. Most times, a private equity investor will help clarify growth plans and refine targets, all the while bringing in their own ideas and past experiences.

A close review of the company
In addition to reviewing the management, investors will assess the company’s strategy, industry, business, customers, and place in the value chain as well as their contracts and an estimate of the company’s valuation. Refining the company’s strategy and business model is also a part of this process.
3.2 Find the right investor

When it comes to securing venture capital or private equity funding, working actively comes a long way. Finding the right investor is an important part of the process.

Understand how the investor operates

Venture capital and private equity investors typically raise their funds from large, institutional investors. When establishing the fund, venture capital and private equity investors agree on investment criteria with their fund’s investors. Therefore, when seeking funding, it is best to focus efforts on investors whose criteria match your company’s situation the best. Venture capital and private equity investors are also called high-risk investors to reflect the sizeable risk they undertake when making an investment. Consequently, expected returns must be high.

Investment size

Venture capital investors invest in startups that don’t necessarily yet have turnover. In the earliest stages of development, the rounds of financing range typically between 200,000 to 500,000 euros in size. In further stages, the rounds can be worth millions of euros and investors also require proof of demand, a working business model and evidence of the team’s capability to achieve international growth.

Juha Tukiainen, MB Rahastot

“I should always ask the investor’s former portfolio companies about what the cooperation with the investor was like. More often than not, venture capital and private equity investors will be glad to give the contact details of former portfolio companies as references”

Industry

Some investors – especially venture capital investors that specialize in startups – focus on a certain industry or business model. Identifying the right investor will not only help in securing the investment, but also in bringing the right kind of expertise to your company.

Investors specializing in growth companies usually operate on a wider basis, with no focus on a certain industry.

The role of the investor in finding funding

The further along a company is, the more likely it is that more than one investors will join in on a round of financing. Even then, one of investors will take the lead. This investor is referred to as the lead investor. They will be in charge of running the round, will play an active role in the company’s operations and will want a seat on its board. Other investors typically take part in a multi-investor syndicate, but with no interest in board membership. Therefore, if your case requires a lead investor, it is advisable to first focus on finding one.

History

Getting acquainted with an investor’s past investments will help shed light on what kinds of growth stories the investor has previously built, what industries they have been successful in, and how well they have cooperated with the owners and management of former investee companies.

Management

The company’s management will work very closely with the investor. Naturally, personal chemistry plays a big part.

Ways of operating

Venture capital and private equity investors have their own ways of operating when making investments and developing companies. It is important to make sure that these ways feel right. Different variables include ways of analyzing the company, building growth strategies and working with the board. Some of the funds will appoint their own employee as a chairman of the company’s board, while others use an outside chairman. In any case, the
board usually has outside members with industry-specific experience.

### 3.3 Contacting venture capital or private equity investors

#### 3.3.1 Startups

In Finland, there are a limited number of venture capital investors who invest in startups. Companies and investors are brought together, for example, in different types of events. Even so, the best way to find an investor may be contacting them directly. When trying to catch the attention of an investor, utilizing your contacts is vital. Does your own company or network have any kind of connections to investors or their portfolio companies? References and introductions are often more convincing than a cold call.

#### 3.3.2 Growth companies

Investment processes can begin in three different ways.

**The entrepreneur or company gets in touch**

The company can be expecting a significant change, for example the entrepreneur’s retirement, internationalization, an acquisition or a larger investment in the future. In these cases, the entrepreneur or company can directly contact potential private equity investors. Investors themselves encourage these initiatives.

**An advisor calls for bids**

Growth companies can use investment banks as advisors to help them find the right private equity investor. In these cases, the advisor acts as the active party, working to find the right investors, negotiating with them and possibly setting up an auction of the company. Sometimes these situations can be challenging, as the company’s management will not get as much of a chance to form a deep, confidential bond directly with the investors.

**An investor identifies an interesting target**

Venture capital and private equity investors are constantly on the lookout working to find the right investors, negotiating with them and possibly setting up an auction of the company. Sometimes these situations can be challenging, as the company’s management will not get as much of a chance to form a deep, confidential bond directly with the investors.

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**“An entrepreneur should always consider what type of investment would be the best fit for them. A majority investment means more immediate capital, but a minority investment allows a larger stake of the company for the entrepreneur.”**

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**Markus Einiö, Juuri Partners**

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**“Pick up the phone and call. It won’t cost you a cent. Investors will be happy to meet with you if your case sounds at all interesting. Even if the meeting does not lead to an investment, you will get free sparring to develop your company further.”**

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**Pia Kåll, CapMan**

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You can find information on almost all the Finnish venture capital and private equity investors on the FVCA’s website. The website also includes a search engine that can be used to find the most suitable investors for your company.

www.fvca.fi/in-english
The price is important, but there are other things that matter as well. Investments come hand in hand with a wide range of emotions. It is important to build trust between the investor and entrepreneur. If trust isn’t gained, neither party will want to move forward. If trust is gained, the valuation may be adjusted.

Pia Kåll, CapMan for exceptional companies with growth potential.

3.4 Prepare the right kind of presentation

The significance of a company’s presentation varies greatly according to the developmental stage they are at. When it comes to startups, pitching – or presenting the company to investors – is often emphasized.

For growth companies, it is not always necessary to put as much time into the presentation: investors specializing in growth companies often have prior knowledge of the companies and will also have access to public information on their history. Nevertheless, it is good to consider how to best present your case so that the company and its business potential will be depicted the right way. This is especially important if investors do not know your company well beforehand. You should ensure that essential information and views on how to develop your company are presented well in your phone call or presentation.

Early-stage pitching

Most often, pitching means presenting a company to a large group of people – for example at an event. A pitch normally lasts a few minutes. It is important that the presentation is exciting and makes the investor want to learn more about the company. To achieve this, the presentation must stand out, market the company, and represent its vision well. It is also essential to share key facts pertaining to the company and its idea: what problem the company solves and how, potential market size, business model and why this specific team is the right one to fulfill the vision.

Presenting to venture capital or private equity investors

Making an inspirational pitch is not enough when the entrepreneur is put face-to-face with an investor. In these situations, it is best to carefully prepare a well-polished presentation that not only answers any questions the investor may have, but also displays a deep understanding of the company’s industry. In addition to basic information like the team, financial figures and market situation, the presentation should cover market potential and growth opportunities.

3.5 The timing of the investment

The timetable for the investment will depend on the size and stage of the company as well as negotiations and the extensiveness of due diligence, which is a process of thoroughly analyzing the company.

In early-stage investments, the fastest rate that an investment can be realized is typically around two months from the first meeting. In these cases, the investment is usually around 100,000 euros in size. Due diligence will be lighter than with larger investments. In these smaller investments, venture capital investors will usually go through at least:

» Market potential
» The product and related technologies
» The team’s key individuals, expertise and commitment
» Terms of the investment

A funding round or structure of over a million euros in size will generally take longer, since investors will want to take a closer look at the company.
The financing round can include multiple investors, some of which can be international actors. The investor will typically interview the company’s customers, take a look at international references, analyze key individuals’ expertise and prepare a more detailed shareholders’ agreement than with smaller investments. The shareholders’ agreement will regulate the rights and obligations of the company’s partners. For these reasons, the investment can only be carried out in about 3 to 4 months after the process begins.

3.6 Defining the valuation

3.61 Startups

For all parties involved, a key matter in any investment decision is the price of the company, commonly referred to as valuation. When it comes to startups, valuation and the size of the financing round are connected, as venture capital investors will typically want a minority share of the company, usually around 10 to 30 percent. Hence, if the round is million euros in size, the valuation of the company is generally between 3 to 10 million euros.

The following factors affect the price:

- **Market potential**: How big of a success can the company be?
- **Proof of demand**: The better and sharper the proof of product demand is, the more it will raise the company’s price, as it decreases the investor’s risk.
- **Patents**: Patents are important since they can serve as a competitive advantage for the company.
- **Stage of the company**: A company that is further along will pose a smaller risk to the investor. Accordingly, the price will be higher.

3.62 Growth companies

A growth entrepreneur looking for a majority investment will sell some of their stocks in the investment process. This is why defining the price is an important part of the investment decision.

- **The company’s growth potential**: Private equity investors estimate how big of a growth it can build together with the company’s management team in 4 to 5 years. An investor may also buy a company for its strong cash flow, even if huge growth opportunities are not on the horizon. Subsequently, the valuation will be lower.
- **Industry**: In fast-growing, low-cyclical industries, company prices will often be higher than in static or cyclical industries.
- **Financial situation**: Strong, positive cash flow will usually raise the price.
- **Industry position**: Private equity investors are interested in the company’s position in the value chain. Market share is also a key factor.
- **Management and culture**: During a growth period, the role of the company’s culture is emphasized. A strong culture usually makes the company more prepared for growth. This is indicated in the price as well, as an experienced, skilled management team will have a positive effect on the valuation.
4. Working with the Investor

4.1 Making an investment

The investor will want to make sure that cooperation with the company will run smoothly. This is why management is usually kept committed to the company by taking them into account in a distribution of shares. Sometimes shares will be offered to other personnel as well. The shareholders’ agreement is a vital contract at the very center of this ownership.

A shareholders’ agreement will usually outline at least the following terms:

» Commitment to the company
» Management of the company and decision-making in important decisions
» Exit conditions
» Non-compete clauses
» Ownership of patents

4.11 Startups

After the investment decision has been made, the whole investment sum will not usually be transferred directly into the company’s account. The venture capital investor will want to make sure the funding will be used to direct the company in the right direction. This is why the financing is often provided in trenches that are paid out gradually for the company, when some set milestones are reached.

Startups will generally require several rounds of financing before the venture capital investor is ready to exit the investment. Other investors may also come in during later financing rounds.

The valuation of the company will typically increase and the size of the rounds will grow. When it comes to startup companies, venture capital investors usually invest 10–30 percent of the company’s value. Therefore, the original investors’ and founders’ stake will dilute, or decrease in size, when the company raises new rounds of financing in further stages. Nevertheless, venture capital investors also aim that at least 20–30 percent of the company is still owned by the original founders or entrepreneurs at the exit point.

4.12 Growth companies

In the case of growth companies, often a holding company established by the private equity investor buys the entire target company. On the other hand, a minority investment is usually made straight into the company. If the private equity investor finds that the seller’s role in the target company is es-
sential, they will build incentives for the seller to continue working for it. In these cases, the seller will invest a part of the sales price back into the holding company. The conditions of the investment may be the same or even better than that of the investor. Even if the investor and seller opt to look for a new CEO, the seller may still continue as a significant owner. The most important objective is to make sure the company’s operational management stays just as motivated to develop the company further than before the arrangement.

4.2 Investor’s activities in the company

A venture capital or private equity investor will start building a growth strategy for the company in order to increase its value. All actions undertaken will happen with this objective in mind. For early-stage companies, the guidance can be very concrete and take place on a daily basis, whereas in cases of more established companies strategic guidance is often emphasized. A growth strategy is typically built for 3 to 7 years, or in other words, for one strategic growth phase.

Refining the strategy

During the investment process, the investor will go through the company’s strategy and, if need be, make changes to it in cooperation with the company’s management and other owners. The strategy will be finalized at the beginning of the investment process, yet it can be revised later during the investment period.

Validating the organization’s ability to grow

To start out, the private equity investor will make sure the organization has what is needed to carry out the strategy. The investor can also help with necessary recruitments so as to ensure the company has the required expertise.

Bringing reporting up to par

The company may not have a clear and coherent reporting system. This is vital to the investor: achieved results are constantly monitored to ensure the company is moving in the right direction. Clear reporting relationships also enhance the quality of company’s administration and management.

Evaluating acquisitions

While organic growth often plays a leading role, growth can also be accelerated through acquisitions. Acquisitions can be made at any point of the investment period, but significant effort is usually put into analyzing competitors and other potential acquisition targets at the beginning of the investment period. If need be, an investor can make an additional investment into the company to finance the acquisitions.

A seat on the board

An active venture capital or private equity investor will normally want a seat on the board. In general, a venture capital or private equity investment will increase the importance of the board and diversify its members’ range of expertise.

4.3 The length of the investment

Venture capital and private equity investors typically exit the investment after 3 to 7 years, which is roughly the equivalent of one strategic growth phase. The exact length of the investment period will be determined by the market situation as well as the company’s development and increase in value.
4.4 Exiting

A successful venture capital or private equity investment always ends in an exit, a detachment from the company. Exiting is the investor’s way of making a profit on their investment. Instead of trying to make a profit with dividends or other forms of revenue, venture capital and private equity investors aim to increase the company’s value. There are many ways of exiting, the most common of which are an acquisition or an IPO (initial public offering).

Acquisition

In an acquisition, a company is sold to another company, a new private equity investor or to management. A company coming into ownership may merge the original company into their own organization or develop it further on its own. A new private equity investor is often larger and more focused on the next growth phase. It is also possible that the original entrepreneur, seller or the company’s management purchases the company for themselves.

In an acquisition, all shares are usually sold. The buyer will attempt to keep key individuals committed to the company through new incentives. Sometimes, the purchase price can be paid out gradually over a longer period of time, based on future financial performance.

Initial Public Offering

In an initial public offering, or IPO, the stocks of the company are offered to the public. In addition to selling old stocks, the company can raise new capital by issuing new shares.

The private equity investor and other owners are usually unable to completely detach from the company during the IPO. This is referred to as a “lock-up.” A complete exit will happen through several phases over a longer period of time. An IPO will usually signify a new phase of growth for the company.

The prevalence of IPOs is partially dependent on the market situation. In Finland, IPOs were relatively rare in the 2000s, but in recent years the market has started to pick up. Even so, it is still relatively rare to see a startup IPO in Finland.