

MS&E 272: Course Wrap-Up

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Finance

- The study of the allocation of scarce resources
- Simple rules:
 - More cash is preferred to less cash
 - Cash sooner is preferred to cash later
 - Less risky cash is preferred to more risky cash
 - Don't run out of cash

Entrepreneurship

- Working Definition:
 - The relentless pursuit of opportunity without regard to tangible resources currently controlled
- A complete process from identification to harvesting
- A way of managing

Management Approach

- Opportunity driven vs resource driven
- Revolutionary vs evolutionary commitment
- Multi-staged vs single-staged commitment
- Use & rent resources vs own and control
- Flat organizations vs formal hierarchy
- Value created vs resources controlled
compensation

Structural Model

- Critical elements:
 - people
 - opportunity
 - context
 - deal
- Concept of “Fit”
- Concept of dynamic “Fit” management

Important Skills

- Resume reading
- Financial statement analysis
- Proforma modeling
- Industry and competitive analysis
- Opportunity analysis
- Valuation
- Deals
- Negotiation
- “Fit” analysis and management

Essential Questions

- Who is the customer?
- How do they make decisions?
- What risks do they perceive?
- What benefits?
- What is the potential profit margin?
- How much capital is required to support sales?
- What is the lifetime value of a customer?
- Is this a large or a small NPV project?
- Who else can ask these questions and respond to the opportunity?

Spotting Opportunity

- Customer
- Supplier
- Employee
- “Knowing and being known”
- Getting in the “game”

Valuation Tools

- Cash Flow Models
 - Free cash flow @ WACC
- Price-to-Earnings (P/E) Ratios
 - Fundamental determinants
 - Comparables
- Venture Capital Method
 - Success scenario
 - Carving up the terminal pie
 - Discount rate factors
 - Future dilution

Limitations of the Tools

- Theory problems
- Estimation problems
- Bias
- Intractability
- What's a comparable?

Valuation via Questions

- A discount rate vs a range of reasonable discount rates
- Common sense and benchmarks (e.g., junk bond rate)
- Tradeoffs between different elements (e.g., profitability and growth rate)
- What would the present value be for a competitor?
- IRR--how wrong could I be?

More Questions

- What if same outcome, but two years late?
- What if need twice as much capital?
- What if terminal value is different?
- What is the upside potential?

Lessons on Financing Ventures

- From whom you raise capital is often more important than the terms
- Running out of cash is disastrous
- Maximizing the price at each stage of a venture is not a sensible objective
- Preserving options is essential
- Think of the amount of equity you raise in terms of buying insurance
- Raising cash is best viewed as buying time
- Price is not the same as value
- Horse race between fear and greed

Attitudinal Objectives

- Anything is possible
- Myth debunking
- Success and failure
- Kinds of failure
- Luck
- Timing
- Acknowledging lack of knowledge

Attitudinal Objectives (cont'd)

- Proper role of analysis
- Arrogance vs confidence
- Cynicism vs skepticism
- Criticizing vs fixing
- Risk avoidance vs risk management
- Common sense
- Logic
- Learning/investing

On Goals

I don't make pictures just to make money. I make money to make more pictures.

Walt Disney

Some Rules

- Don't maximize short-term anything
- Time cannot be replaced
- Subscription businesses are great
- Don't run out of cash
- Family is all that matters