FUNDING A TECH BUSINESS

ALL TECH START-UPS NEED SIGNIFICANT FUNDS TO INVEST IN PEOPLE AND DEVELOP THE IDEAS AND TECHNOLOGY NEEDED TO ACHIEVE THEIR VISION.

This essential capital can take a variety of forms, including loans, equity and other finance, depending on the stage the company is at in its lifecycle.

BOOTSTRAPPING

The beginning of the journey for most tech start-ups is the 'bootstrapping' phase. This is where the company is started with little capital and relies on personal savings, and possibly funding from friends and family. Many tech entrepreneurs continue to work full-time at this stage while they use savings to develop an idea or early stage technology into a proof of concept.

PROS

- Easy to access.
- Shows confidence in what you are doing to other future investors.
- You don't have to answer to anyone else.

CONS

- You bear the full risk.
- The capital you raise may not be sufficient to reach your goals or the necessary stage to obtain further funding.

FRIENDS & FAMILY/SEED CAPITAL

As the start-up develops, more options become available for funding, particularly as the company begins to demonstrate what might be possible in the real world. Investment at this stage often comes from friends, family or seed investors and can be equity or unsecured loans. While this is risk capital, you need to be mindful of how much equity is given away at this stage if you're using this option.

PROS

- Known to you and supportive so funds can usually be obtained quickly.
- They may be more accommodating if the business pivots or takes longer to achieve its goals than expected.
- Investment terms are usually more flexible than other sources of income, and they may accept lower returns.

CONS

- If the business fails, or returns are lower than anticipated, it can strain relationships.
- They may not have access to significant enough capital.
- Family and friends are not usually able to bring anything else to the table apart from their investment, unlike other types of investor.

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CROWDFUNDING

Crowdfunding can take a variety of forms but the two most common are equity-based or product-based, where the product is effectively paid for in advance. Crowdfunding is great for building a user base and for marketing a product as it can generate a large number of followers and brand advocates. It's not right for every tech start-up, but can bring many positive benefits in addition to money.

PROS

- Makes your start-up more visible to the outside world.
- Can generate significant interest and help to increase your user-base and build brand advocates.
- A good way to test your product and demonstrate user acceptance.

CONS

- You will have to deal with multiple shareholders.
- Fund raises are often complex and time-consuming.
- Not a suitable choice for all tech businesses.

EQUITY FUNDING/ANGEL INVESTORS

Investors will take an equity stake in start-up businesses in exchange for their cash. This investment will be at a value (of the company) but can often be at a discount given the risk at the time of investing and the uncertainty of successful return. Angel investors can often be useful mentors and through their networks make valuable introductions to other similar companies, entrepreneurs and other investors.

Every angel investor has a different appetite for investment and risk and usually invests between £10,000 and £500,000, either individually or in a syndicate.

Equity raises at this level allow investors to take advantage of the UK government tax incentives offered by the Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS).

PROS

- Investors can obtain tax reliefs for investing in qualifying companies which encourages them to invest.
- Angels are often experienced entrepreneurs who can guide and mentor you as well as opening up other opportunities via their networks and acting as ambassadors.
- Angels are more flexible than venture capitalists so agreeing investment can be easier.

CONS

- Equity is given away in exchange for funds.
- Angels rarely follow on investments due to the high-risk nature of angel investing.

GRANTS/PROGRAMS

These are often available for early to mid-stage companies, although they tend to be for businesses operating in specific geographical areas or sectors. The process to obtain grants can be very long and the uncertainty usually makes them additional finance rather than a primary source of funding.

PROS

- Gives the business exposure which could attract other investors and customers.
- A number of programs give favourable loans which either wouldn't normally be available or carry a lower interest rate.

CONS

- Applying for grants can be very time-consuming and may distract you from the business.
- Programs all have their own criteria and agendas so aren't appropriate for all start-up tech businesses.

VENTURE CAPITAL FUNDING

Venture capital is start-up or growth equity capital or loan capital provided by specialised financial institutions or finance houses. These venture capitalists are looking to invest in high growth tech companies that need capital to expand quickly.

Funding is usually in stages, or series. Series A will normally follow successful seed funding and proof that the business is viable and has developed a track record or significant user base. The amount invested is usually between £3m-10m. Series B funding focuses on building the business through people, advertising and marketing. Companies can expect to raise between £5m-15m at this stage, with Series C funding following afterwards if this is successful.

PROS

- Provides significant growth capital which allows your company to expand to its next stage of growth.
- Gives you access to experienced professionals with resources and networks, including partners and future investors, to help you grow.
- Investment from a VC adds instant credibility to your business.

CONS

- Usually set very demanding targets and you can lose equity if these are not met.
- Focus can quickly shift to how the business can ultimately be sold as VC firms have a defined window of investment.
- It may be challenging to keep control of your business.

INCUBATORS AND ACCELERATORS

Incubators and accelerators can also sometimes provide limited capital and often they provide support, workspace and mentors to start-up businesses. However, founders should be aware that there can also be costs associated with joining these types of programmes.

PROS

- Backed and supported by experienced start-up professionals that will often support your business with limited capital, space, introductions and opportunities.
- Involves working with a similar tech start-up so you can benefit from collaborating with companies in the same position as your own.
- Can provide credibility when going out to raise future investment.

CONS

- Some incubators take a significant equity stake.
- Thorough research is essential as there are significant differences between the programs in both quality and the value they add.

TO DISCUSS ANY QUESTIONS OR ISSUES YOU MAY HAVE AROUND FUNDING YOUR TECH BUSINESS, PLEASE CONTACT

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