

Venture Capital Guide

2024



In this Guide

What is venture capital?	3
The investment process	9
Exit strategies	22
How to win venture capital	27
Trend report	33
About Hamilton Locke	37



What is Venture Capital?

What is Venture Capital?

Overview

What is Venture Capital?

Described in basic terms, Venture Capital ("VC") involves the investing in early-stage high-growth companies that are developing new and innovative technologies and systems. Venture capitalists usually take equity (minority share) in the company and provide capital, commercialisation and strategic skills and insight.

VC is often referred to as "patient capital" because rather than an immediate return to the investor through regular payments of principal and interest, the investor has to wait for its return through long-term capital appreciation, realised only after the sale of their shares in the company by way of an IPO or trade sale (typically between 3 and 5 years after the investment).

Key characteristics of a VC investment

- typically have higher risk/return profiles;
- new marketing ideas, innovative technology and new product application potential;
- products which have passed through the early prototype stage and are adequately protected by patents, copyright or confidentiality arrangements;
- businesses with the potential to mature within a few years to the point of an IPO or trade sale;
- opportunities for the venture capitalist to contribute beyond the capital investment;
- high-quality executives and employees who are energetic, focused and professional; and
- a significant, although not necessarily controlling, participation by the venture capitalist in the company's management.

What is Venture Capital?

Forms of venture capital



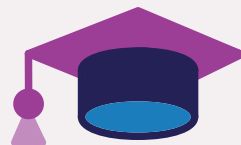
Institutional venture capital

Involves a fund manager, who raises funds (typically from high-net-worth individuals and superannuation funds) to invest in a diverse portfolio of companies, often with an industry focus.



Corporate venture capital

Established corporations making VC investments either via an independent arm of its business or a dedicated corporate division.



University funds

Most universities have dedicated commercialisation divisions to assist students to take their research to the market.



Government funds

Australian federal and state governments have created dedicated venture capital funds which invest for both commercial and public interest objectives.

What is Venture Capital?

Traditional debt vs VC finance

Form of investment

Investor's source of return

Return on investment

Protection for investor

Risk

Considerations for investor

Time before investor generates income

Means of exit for investor

Traditional debt finance

The company borrows money which it must repay later, with interest

Interest

5 – 10% per annum

Mortgage and security taken over the assets of the company

Low (as secured assets can be sold if company defaults)

Adequacy of collateral

Usually 1 month (interest payments)

Loan repayment

VC finance

In return for funds, the investor receives a percentage stake in the capital of the company

Growth in the value of the investor's shares

An internal rate of return (IRR) of 35 – 40%

Seats on the company's board, preferential shareholder rights, put/call options

High (usual profile for VC is high risk for high return)

Management team and market potential of company

Typically 2 – 6 years

IPO or trade sale

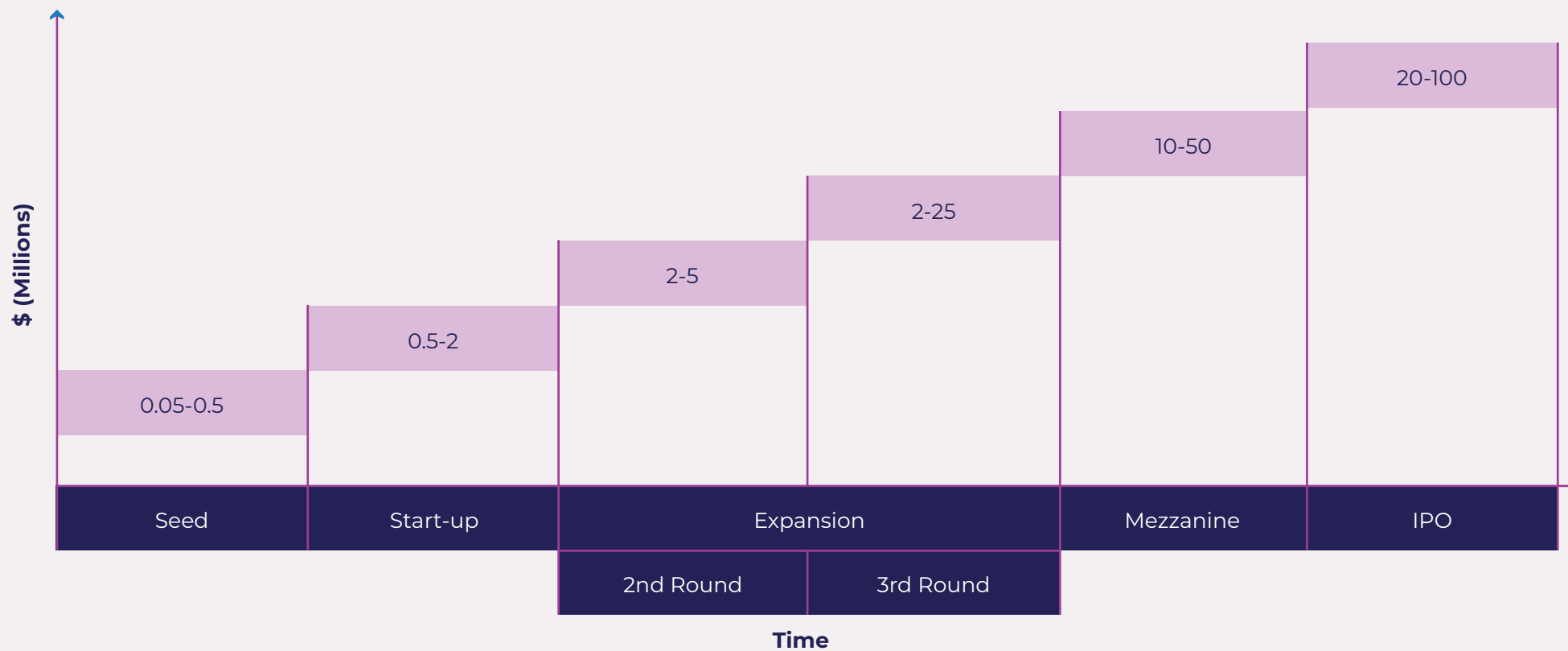
What is Venture Capital?

Risk and returns

Stage		Summary	Risk/Return Ratio	Funding Needed
Stage 1	Seed	Business idea or concept with product offering still in development.	Highly speculative and funding may be in small amounts for an as-yet and unproven concept.	\$50,000 to \$500,000
Stage 2	Start-up	Also known as “Angel Round”. The concept or product has been developed and patented.	Considered the riskiest stage for investors as the company requires large amount of capital but has no reliable indicators of its future success.	\$500,000 to \$2 million
Stage 3	Expansion	Also known as “Second Round” and also may comprise multiple rounds.	Company is fully set up and is building a financial track record. Funding required to expand existing operations and marketing capacity.	\$2 million to \$10 million or more.
Stage 4	Mezzanine	Also known as “pre-IPO funding”. Allows a company to prepare an IPO.	Mezzanine investors are usually just providing experience and funds to “dress up” a company for listing.	\$10 million to \$50 million or more.

What is Venture Capital?

Lifecycle & funding



The Investment Process

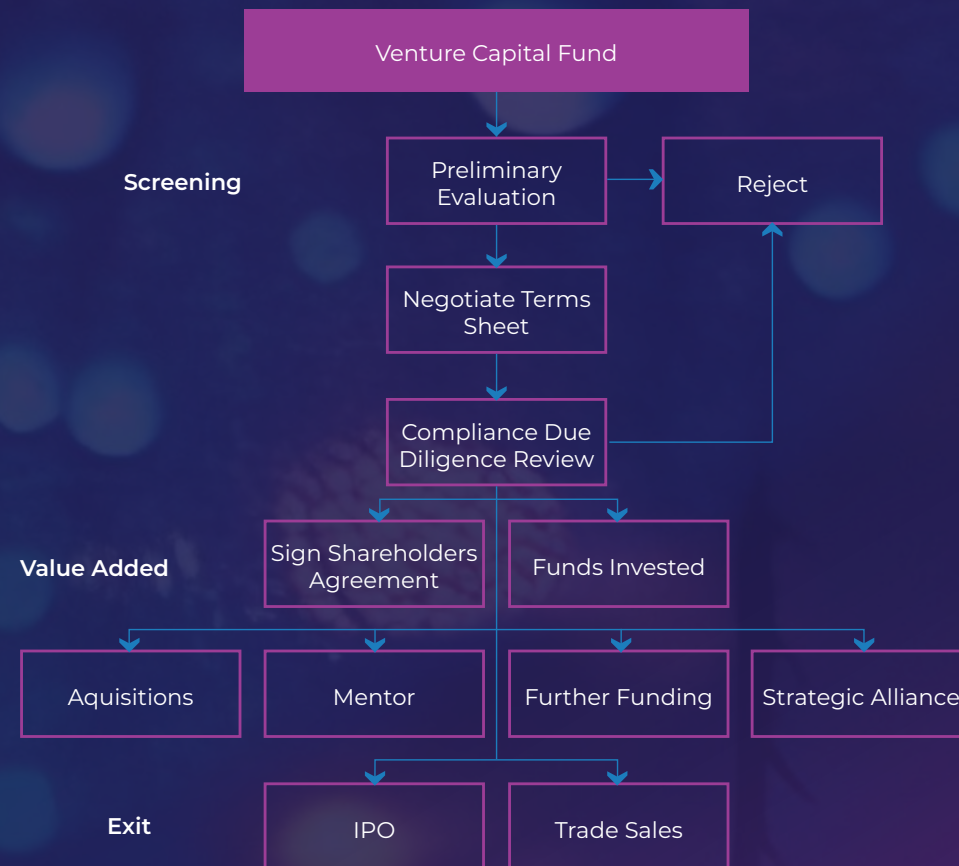
The Investment Process

Overview

Selection of the right type of investment is a very important decision for both entrepreneurs and venture capitalists. And the investment process, a complex one for both.

“60% of a watermelon,
is better than 100% of a grape”

Mark Cuban



The Investment Process

Overview

Entrepreneur	Entrepreneur Preparation / Screening
Step 1: Prepare a business plan Process Involvement: The business plan should clearly identify the entrepreneur's business opportunity and strategy, by comprehensively and professionally setting out: • key facts about the business; • business activities; • financial plan; • industry and competition; • customers and target market; and • how resources will be used to achieve business objectives.	Step 2: Selecting suitable venture capital funds Process Involvement: An entrepreneur/company should consider: 1. investment preferences of the various funds; 2. quality of the relationship between the management team & investors; 3. the funds' track records; 4. ability of the fund to provide future funding; and 5. value that the investor can add through industry experience, contact networks and expertise in start-up financing.

Entrepreneur Preparation		Screening		Screening/Negotiation		Neg/Value Added	Value Added	Value Added/Exit
1. Prepare a business plan	2. Selecting suitable venture capital funds	3. Submit business plan	4. Prelim evaluation & negotiating valuation	5. Negotiate Terms Sheet	6. Due Diligence Investigations by Investor	7. Negotiate & execute formal investment docs	8. Funds Invested	9. Exit

The Investment Process

Overview

Screening

Step 3:

Submit business plan

Process Involvement:

Sending unsolicited business plans is usually not a good strategy. The best approach is to be introduced by a third party who has an existing relationship with the funds.

Screening

Step 4:

Preliminary evaluation and negotiating valuation

Process Involvement:

Once the investor has looked at the business plan, there will be preliminary discussions and interviews to determine whether the company is suitable.

Whilst agreeing on the valuation is important, other factors including restrictions placed on the Founder's shares, should be considered.

Entrepreneur Preparation		Screening		Screening/Negotiation		Neg/Value Added	Value Added	Value Added/Exit
1. Prepare a business plan	2. Selecting suitable venture capital funds	3. Submit business plan	4. Prelim evaluation & negotiating valuation	5. Negotiate Terms Sheet	6. Due Diligence Investigations by Investor	7. Negotiate & execute formal investment docs	8. Funds Invested	9. Exit

The Investment Process

Overview

Screening / Negotiation	Screening / Negotiation
Step 5: Negotiate terms sheet Process Involvement: The terms sheet sets out the basic framework for the deal. Typically, the issues to be resolved at this stage include: • form of the investment; • protections to be given to the investors; • rights of the investors to appoint board representatives; • pre-emptive rights; and • exit strategies. The terms sheet also typically grants the investor an exclusivity period in which to conduct its due diligence inquiries.	Step 6: Due diligence investigations by investor Process Involvement: Once the terms sheet is signed, the investor will proceed with due diligence. This involves a detailed examination of the company to assess the feasibility of the business.

Entrepreneur Preparation		Screening		Screening/Negotiation		Neg/Value Added	Value Added	Value Added/Exit
1. Prepare a business plan	2. Selecting suitable venture capital funds	3. Submit business plan	4. Prelim evaluation & negotiating valuation	5. Negotiate Terms Sheet	6. Due Diligence Investigations by Investor	7. Negotiate & execute formal investment docs	8. Funds Invested	9. Exit

The Investment Process

Overview

Negotiation / Value Added by Investor to Business	Value Added by Investor to Business	Value Added by Investor / Exit
Step 7: Negotiate and execute formal investment documentation Process Involvement: Upon completion of due diligence investigations, parties will prepare and execute formal documentation.	Step 8: Funds invested Process Involvement: An investor can usually provide (in addition to the funding required by the business): • knowledge, skills and contacts for acquisitions; • mentoring; • further funding at a later stage; • strategic alliances; and • industry know-how and contacts.	Step 9: Exit Process Involvement: Typically by IPO or trade sale. Investor usually can provide at this stage: • knowledge and assistance to dress-up for IPO; and • further funding.

Entrepreneur Preparation		Screening		Screening/Negotiation		Neg/Value Added	Value Added	Value Added/Exit
1. Prepare a business plan	2. Selecting suitable venture capital funds	3. Submit business plan	4. Prelim evaluation & negotiating valuation	5. Negotiate Terms Sheet	6. Due Diligence Investigations by Investor	7. Negotiate & execute formal investment docs	8. Funds Invested	9. Exit

The Investment Process

Selecting suitable funds

Most venture capitalists prefer business plans to be limited to no more than 15 to 20 pages, and should set out:

1. Executive Summary:

maximum 2 pages summarising the essence of the plan.

2. Table of Contents:

tool for the reader to navigate through the plan.

3. Background on the Company:

brief history and description of the nature of the business, industry and future direction of the business.

4. Product/Service:

description of product / service and the unique qualities and stage of product life cycle.

5. Market Analysis:

industry size (domestic and international) and growth rates, competitors, market share, customers, barriers to entry, barriers to growth, distribution channels, target segments and competitive advantages.

6. Marketing:

how the product will be marketed, overseas market access issues, pricing plans, sales force, strategies for different markets, distribution channels and how these compare with competitors.

7. Manufacturing:

description of production process, details of production costs including resources required, capacity and suppliers.



The Investment Process continued...

8. Research and Development:

status of development of the product.

9. Management:

profiles of key personnel, organisation chart and any additional staff planned and expected remuneration.

10. Risk Factors:

to company, market and the industry.

11. Financials:

summary of past and projected performance.

12. Funds Required:

amount of funds, use of funds, capital structure and ownership before and after financing.

13. Company Matters:

directors, shareholders, bankers, auditors, lawyers and other advisors.

14. Appendices:

project brochures, statutory accounts, detailed projections (previous 3 years), resumes, market studies or articles.



The Investment Process

Selecting suitable funds

It is recommended that the company prepares a short list of suitable funds and requests a copy of their publications to assist in considering the following:

1. INVESTMENT PREFERENCES	A company should look at the investment preferences of various VC funds, such as: • particular stages of investment; • amount of investment; • industry sectors; and • geographical location.
2. COMMUNICATION	As the investment and relationship will typically last a number of years and involve close negotiations and discussions, it is important that the fund selected is one with which the company can build a strong and open relationship.
3. EXPERIENCE	What other companies in the industry has the VC fund invested in, and their track record?
4. FUTURE FUNDING	Does the VC fund have capacity to provide further rounds of funding or introduce the company to offshore finance markets?
5. VALUE ADDED SERVICES	Does the VC fund offer any: • industry specific knowledge; • financial and strategic planning; • recruitment of key personnel; • acquisition identification; and • access to international markets and technology.
6. AIC	The Australian Investment Council (AIC) (formerly the Australian Private Equity and Venture Capital Association Limited) has adopted an industry Code of Conduct which established a minimum set of principles that its members must observe. It recommended that the VC fund be a member of the AIC.
7. OTHER INVESTORS	It is usual that the company will require further funding. It is also usual for VC firms to co-invest in a deal. Companies should consider whether the venture capitalist would be willing to work alongside other investors.

The Investment Process

Submitting a business plan

A good approach is for a company to speak to:

- an associate who may have obtained VC financing previously;
- government laboratories and institutions;
- other entities that licence technology to venture-backed companies;
- accountants, lawyers and bankers who advise VC funds or venture-backed companies;
- superannuation fund managers;
- universities; and
- other entities involved in innovation and venture capital.



The VC Fund will undertake a preliminary evaluation of the merits of your proposal, in particular:

- experience of the management team;
- potential for exit;
- profitability of the business;
- outlook for industry;
- competitiveness of the product/services;
- barriers to entry; and
- viable business model.



Once the investor has reviewed the business plan, there will be preliminary discussions and interviews to determine the suitability of the investment.

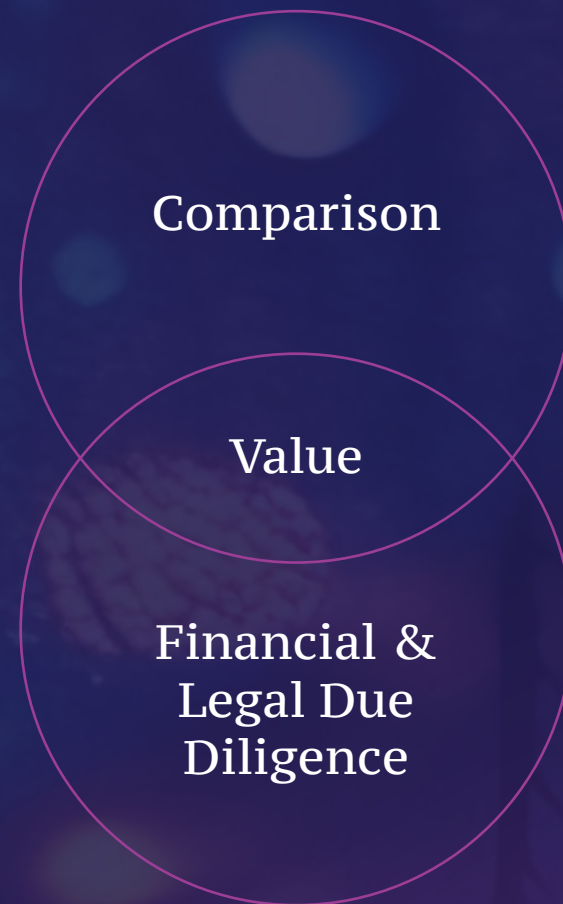
The Investment Process

Valuation

Valuation of the business

Negotiating valuations is usually one of the most difficult issues in VC financing, this is intensified further in the case of a start-up without any operating history.

Venture capitalists will often use other deals by other companies in the industry and information about comparable companies that have used VC financing, in assessing management's projections. They will typically want any projections and valuations from management to be supported by financial and legal due diligence and based on verifiable assumptions.



The Investment Process

The term sheets

The framework for the investment will be set out in a terms sheet which records the parties understanding of the key issues and governs the investment until such time as the parties negotiate the detailed legal agreements.

During the negotiation of a terms sheet, companies should bear in mind that it is likely that they will need subsequent rounds of financing, and any future venture capitalists will typically want the same or similar rights as those granted to early-round investors.

1. Form Of Investment Consideration

Consideration for the investment may take the form of ordinary shares, preference shares or convertible notes. Venture capitalists generally want preference shares as they confer additional protection without leveraging the balance sheet. Rights attached to preference shares include:

- preferential right to dividends;
- preferential right on a liquidation or winding up of the company; and
- right to convert preference shares into ordinary shares at any time. Note that many seed round investments sub \$1 million in value are now often conducted via a Simple Agreement for Future Equity (SAFE). This is a form of convertible note that is tax equity and which converts in the future to shares when the relevant company conducts a priced capital raise, often at a discount to the share price implied by that raise.

2. Size Of Investment And Tranches

Venture capitalists may wish to make their investment in stages or tranches with each tranche conditional upon the company achieving certain milestones.

3. Appointment Of Directors

Venture capitalists will want some oversight and control over the progress of their investment. In order to do this, they will seek to appoint a certain number of directors to the board and tailor the company matters which must be considered by the Board.

4. Protection Against Dilution

There are two types of anti-dilution protection:

- (i) Restructures: protection against share dividends, share splits, reverse splits, and similar recapitalisation occurring by adjusting the conversion price of preference shares to ensure that the number of ordinary shares issued on conversion represents the same percentage of ownership.
- (ii) Prior protection: if the company issues shares at a discount to shares bought by an investor, the conversion price is adjusted to ensure the number of ordinary shares issued on conversion represents the same percentage of ownership.

The Investment Process continued...

5. Redemption

Venture capitalists may seek the right to force the company to realise the value of the investment at some point in the future by requiring the company to buy back or redeem their shares if an IPO or trade sale has not occurred by a certain date.

6. Facilitation Of Sale Of All Issued Shares

Venture Capitalists may also require a “drag along” clause which compels all shareholders to sell their shares if more than a specified percentage of shareholders (usually 75%) accept a third party offer.

7. Standstill For Founding Shareholders

Venture capitalists may also require that the founding shareholders agree to standstill provision which prevent them from selling their shares in the company for a period of time.

8. Executive Service Agreements

Venture capitalists may require that key executives sign appropriate executive service agreements.

9. Information Rights

Venture capitalists may want the right to receive certain information to allow them to comply with the reporting obligations of their investment vehicle (such as an Early Stage Venture Capital Limited Partnership (ESVCLP)), such as monthly financial statements, annual audited financial statements, and the annual budget and business plan approved by the board.

10. Intellectual Property Rights Of The Company

Venture capitalists may want assurance that the company has sole legal and beneficial ownership of the intellectual property rights.

11. Pre-Emptive Rights

Venture capitalists may require a pre-emptive right to invest in future issues of shares in preference to a third party.

12. Exit Strategy For Investors

Venture capitalists are driven by the need to realise the value of their investment and may seek to impose a provision enabling them to force a trade sale or IPO if such an event has not occurred within 3 - 4 years of the investment.

13. Additional Management Members

Venture capitalists may require the company to recruit additional executives to the management team.

14. Exclusivity Period

Venture capitalists may seek a period of exclusivity after the signing of the terms sheet, typically 30 to 60 days, where the venture capitalist has the right but not the obligation to invest, and the company is restricted from engaging in negotiations with other potential investors.

The Investment Process

Due diligence

The detailed examination of the company will run in parallel with the terms sheet negotiations. The venture capitalist and its lawyers will typically undertake due diligence on the following:

1. Corporate

Review of the company's:

- corporate structure including subsidiaries;
- business names;
- constituent documents; and
- shares issued and debt securities convertible into shares.

2. Assets

Review of what assets the company owns, including:

- real property;
- intellectual property; and
- contractual rights and intangibles,

and who owns the assets and any mortgages or charges over them.

3. Intellectual Property

Verification of the company's ownership of the intellectual property.

4. Financial Statements

Extensive review of financial statements and accounts of the company will be conducted to assess the past performance and future prospects of the business.

5. Material Contracts

Review of the company's key contractual relationships with suppliers and customers, key employees, strategic alliances, licensing agreements and other material contracts.

6. Employees

Review of the company's:

- standard employment agreements;
- relationships with key employees;
- employee option plans;
- modern award compliance and employee / contractor classifications; and
- history of any disputes (if any).

7. Litigation

Searches undertaken and review of any actual or threatened litigation or dispute which the company has been involved in.

The Investment Process

Legal documentation

Although actual legal documentation and agreements vary in relation to the subject deal to be done, in most deals the following documents and agreements are standard:



Subscription agreement

Sets out the subscription details such as:

- number of shares;
- price of shares;
- number of tranches;
- dates of subscriptions;
- warranties about the company;
- rights attaching to shares; and
- any conditions which have to be satisfied before the investment is made.



Intellectual Property Acknowledgement Deed

Acknowledgement and confirmation by other parties that they have no rights in any intellectual property which they developed and assign all such creations and property (if applicable) to the company.



Shareholders agreement

Sets out the ongoing relationship between the shareholders and the company as agreed in the terms sheet.



Executive service agreements

Sets out the terms of “key” employees ongoing relationship with the company, including remuneration and bonus entitlements. It is usual that these terms will have confidentiality and restraint obligations which apply to key employees during their service as well as post-employment.

Many seed round investments are now made via an instrument known as SAFE. First developed by the Silicon Valley based fund and incubator, Y Combinator, a SAFE is a form of convertible note that is tax equity (and hence an eligible investment for the most common form of VC fund entity in Australia, an ESVCLP) and which converts in the future to shares when the relevant company conducts a priced capital raise, often at a discount to the share price implied by that raise.

The key benefit of a SAFE is that it allows very early stage businesses to raise capital with minimal documentation and no valuation and allows such matters as shareholders agreement terms and initial valuation to be determined at the time when the company is ready to conduct its first priced capital raise.

Exit Strategies

Exit Strategies

Overview

VC investment is considered “**exit-driven**” as venture capitalists are motivated by the need to realise their investment. In terms of this realisation, there are 3 main strategies: IPO, trade sale or redemption of the investor’s shares by the company.

1
IPO

2
Trade
Sale

3
Redemption

“Every company needs an exit strategy and an exit plan. Ideally, the exit strategy should be agreed upon by the founders before the first dollar of investment goes into the company.”

Basil Peters

Exit Strategies

IPO

An Initial Public Offering (IPO) is, as the name suggests, the very first sale of the company's shares to the public by listing them on a public stock exchange such as the Australian Securities Exchange (ASX) or the National Association of Securities Dealers Automated Quotations (NASDAQ) (an American stock exchange).

An IPO has historically been the favoured exit strategy for venture capitalists and founding shareholders because generally the shareholders in the company can realise their investment and potentially receive very high returns on their original investment.

Any potential high returns should always be measured against the time and expense usually incurred in the IPO process (which is highly regulated and scrutinised) and in ensuring the company's ongoing compliance with ASX Listing Rule requirements after the IPO.

In more recent times, economic conditions and market sentiment relating to inflation and interest rates has meant founders and investors have had to take a more flexible approach to exit strategies, including trade sales, secondary sale transactions, holding for longer and, for funds, continuation vehicles.



A guide to the IPO process (the IPO Roadmap) has been prepared by Hamilton Locke and can be accessed [here](#)

> [Hamilton Locke IPO Roadmap 2022](#). The IPO Roadmap 2022 provides practical and up-to-date guidance on the decision to list, choosing your team, preparation, due diligence and disclosure, the offer and the listing.

Exit Strategies

Trade Sale

The IPO exit process is expensive and time-consuming but offers potential for a very high return. A trade sale, by contrast, may not offer the same return, but will generally involve less expense, effort and risk.

In recent years, trade sales have become increasingly popular with both founders and potential buyers (including VCs). This has coincided with increasing returns being offered in certain industries, particularly tech, the ability to exit (or acquire) more rapidly, and the variety of deal structures available.

Trade sales can be structured in a variety of different ways to allow for:

- founders to have a clean break, or to have continued involvement in the business for a set period;
- upfront consideration or deferred consideration (e.g. in the form of scrip, retained equity with options for the buyer to purchase these at future milestones, earn outs, or deferred cash payments).

This variety of structures allows for founders and VCs to mitigate risk, for example, by bridging the valuation expectations of both parties with part of the sale proceeds being contingent on the financial performance of the business over a two or three year period.



Hamilton Locke have analysed the deal trends and negotiation points in M&A transactions in Australia in our M&A Deal Data Report 2023 which can be accessed here

> [Hamilton Locke M&A Deal Data Report 2023](#)

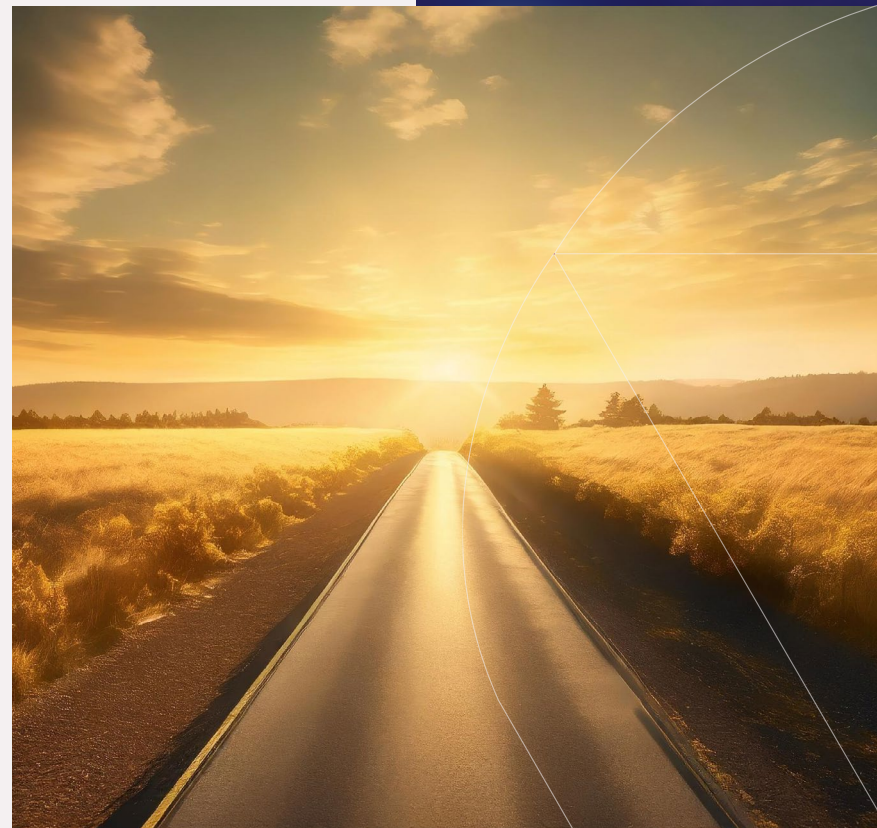
Exit Strategies

Redemption

A company can buy back the venture capitalist's shares at a previously specified price or rate of return. The triggers for a redemption by either the company or the venture capitalist will be contained in the shareholders agreement. Note that this option may not be open to VC funds that are ESVCLPs as they are constrained by strict eligibility rules on the terms of their investments.

Like a trade sale, the potential for return on original investment is not as high as an IPO exit and significantly, the return would be capped at an upper limit based on the previously specified price or rate of return. A company should always consider any redemption rights sought by a venture capitalist and whether the inclusion (and the terms of) that right may hamper the company's ability to raise funds in the future.

Future investors, whether equity or debt, will have concerns about whether their investment is being used to pay out earlier investors rather than grow the business.





How to Win Venture Capital

How to Win Venture Capital?

Overview

Many entrepreneurs mistakenly believe that having an outstanding concept and management team is enough to secure venture capital investment. However, venture capitalists see outstanding concepts backed by good management teams every day, and they may have hundreds of proposals and business plans on their desks at any one time.

As noted previously in this guide, much of a company's success will have to do with pinpointing and targeting the ideal VC investment fund and customising the pitch to this fund.



How to Win Venture Capital

Key characteristics

Generally venture capitalists will look for the following characteristics in an investment target:

Superior business: the company's product should have a large potential market with high growth prospects, and be a product which is easily differentiated from its competitors. The market should have barriers to entry so that the company's strategic position is defensible.

Quality and depth of management: it is said that venture capitalists will, like seasoned punters, "bet the jockey, not the horse". A company should assemble a balanced team of professionals and management with the all-round experience to accomplish the objectives set out in its business plan.

Corporate structure: a venture capitalist will look for a clean corporate structure, rather than having a widely diversified shareholding and also clear distinction between company's assets and those assets still held by founding shareholders.

Intellectual property: an investor will want to ensure that the company has clear and indisputable rights and ownership of the intellectual property prior to investing funds in the company.

Investment structure: the investment structure must allow the investor to generate high returns which justify the risk of the investment, often by providing an easy exit strategy where reasonably permissible.

Typical process of elimination by venture capitalists



How to Win Venture Capital

Australia's venture capital investment program

The Australian government supports innovation and productivity growth through its venture capital tax concession program, under which tax relief is granted to subsidise investment in venture capital. The tax concessions are only available to investors and managers of certain investment vehicles established under the oversight of the Department of Industry, Science and Resources (ISR), known as venture capital limited partnerships (VCLPs) and early stage venture capital limited partnerships (ESVCLPs). A list of VCLPs is available [here](#) and ESVCLPs is available [here](#).

Certain eligibility requirements apply to receive these tax concessions. Some of these requirements relate to the types of businesses that VCLPs and ESVCLPs can invest in and the form that the investment may take. Others relate to the structure of the partnerships themselves, however these are not discussed in this Guide. If the investment that you are offering does not meet these requirements, you will be generally unable to receive investment from a VCLP or ESVCLP. VCLPs or ESVCLPs may only invest in your business, if your business and the investment meets the requirements set out on the following page.



REQUIREMENTS THAT APPLY TO BOTH VCLPS AND ESCVLPS

- VCLPs and ESVCLPs may generally only invest in “eligible venture capital investments” or “permitted loans”.
- **Eligible venture capital investments** are investments in companies or unit trusts that:
 - are at risk;
 - are the acquisition of:
 - shares or units;
 - options to acquire shares or units; or
 - convertible notes (other than convertible notes that are debt interests);
 - are located in Australia (subject to certain exceptions), which is defined as having at least 50% of assets and staff being located in Australia for at least the first 12 months of the investment;
 - have a predominant activity that is not property development or land ownership, finance*, insurance*, construction, or passive investments*. When working out what a business’s predominant activity is, the VC fund must assess whether eligible activities account for more than 75% of the business assets, employees, or income;
 - has a total asset value which is less than the thresholds set out below;
 - do not use the investment to invest in another entity, subject to certain criteria;
 - are made and disposed of while the partnership is registered as a VCLP or ESVCLP; and
 - are held for at least 12 months.
- **Permitted loan investments** means debt investments that accompany an eligible venture capital investment of at least 10% of the investee business, or is a loan made for less than 6 months.

*An activity that relates to developing technology for use in these activities, is ancillary or incidental to developing such technology, or has been found to be a novel application of technology by the ISR will not be excluded by the predominant activity tests.

VCLP REQUIREMENTS

- VCLP may only make investments in an investee that:
 - has a total asset value before the investment is made of ≤ \$250 million;
 - is not listed, or is de-listed within 12 months after investment.

ESVCLP REQUIREMENTS

- Investments made by the partnership must be consistent with the partnership’s approved investment plan, which may limit the type of businesses that the partnership may invest in.
- ESVCLPs must generally only acquire newly issued shares or units, options or convertible notes of an investee. If an investment involves the purchase of pre-owned investments from existing investors, certain additional restrictions apply.
- Subject to certain exceptions, an ESVCLP may only invest in an investee that:
 - is a business in an early stage of development;
 - has a total asset value before the investment is made of ≤ \$50 million;
 - has a registered auditor; and
 - is not listed on a stock exchange at the time of investment.

Conclusion

Venture capital is considered the muscle behind innovation because it involves more than just the provision of financial accommodation to a company.

Venture capitalists specialise in different industries, growth stages and risk profiles, where they can add value in specialist skills and mentoring which best fit the company's needs.

Companies should consider whether it is VC that they are seeking. As outlined in this guide, VC firms will tend to work throughout the life cycles of a company and are very much involved in the operational structure. Venture capitalists have a strategic role in the company and will likely seek to have a clear involvement with the company in order to stay close to their investment and to ensure that they are able to contribute to major decisions that could impact their returns in the long run.

However, a company should seek to understand the value a venture capitalist brings by doing its due diligence in order to really understand if a venture capitalist is going to add value in addition to capital, and whether the expertise of the venture capitalist is synonymous with the requirements of the company.

The risks for both the company and the venture capitalist is tremendously high and despite the televised portrayal of a smooth and swift process, it is a long and complex transaction. Given the risks and complexity of the deal, it is critical that companies are aware of the issues raised in this guide and assess the impact those issues may have on the future of the business.





Trend Report

Trend Report

The rise of venture debt

Venture debt lending has long been a feature of the US venture financing landscape but is belatedly starting to feature in Australia with the recent launch of two Australian based venture debt shops. Venture debt involves the provision of debt finance to typically later stage start-up companies that is used as equity round replacements or for milestone financing, working capital or M&A activity.

Venture debt will be appropriate for later stage start-ups that are producing revenue and for enterprises that require funding through the growth phase of their development but are not yet able to obtain finance from traditional lenders.

Term loans and convertible notes are often the instruments by which the debt is provided. Warrants may also be granted to the financier to provide potential equity upside as a sweetener for the financier accepting higher levels of risk by lending to an early stage company.

The optimal time for a business to raise funds is often immediately following the achievement of a key milestone that increases a company's valuation, resulting in less equity dilution for the same amount of capital raised. Venture debt can extend the cash runway of a start-up company to its next valuation driver, thereby giving the company space to increase in value in the meantime. A subsequent equity round can then be raised at a higher valuation. Management, employees and investors can all benefit from less dilution and investors can benefit from less cash required to maintain their ownership position.



Hamilton Locke have prepared a **venture debt handbook** providing a practical step-by-step guide on all aspects of venture debt investments, which can be accessed [here](#)

Trend Report

VC investment

Following a significant spike in VC activity in 2021 and 2022, where capital raised, number of deals, and the value of deals globally was the significantly higher than ever recorded, VC investment in 2023 was close to the pre-covid levels of 2019.

In 2023, Australian venture capital saw 413 deals (down 21% on 2022), \$3.5 billion in funding (down 54% on 2022).

Falling valuations: In Australia (following the global trend), valuations at all deal stages are expected to continue to fall, with later-stage transactions the most impacted:

- **Seed:** investors estimate, on average, a fall in valuations from peak pricing of 33%;
- **Series A and B:** investors estimate, on average, a fall in valuations from peak pricing of 41; and
- **Series C onwards:** investors estimate, on average, a fall in valuations from peak pricing of 47%.

Industry focus: The myth is that venture capitalists invest in good people and good ideas. The reality is that venture capitalists invest in good industries. In Australia, emerging areas that have continued to attract VC investment include artificial intelligence technology (AI) and machine- learning driven automation and technology. This trend is consistent with the utility and demand for AI and automation technology across various businesses and different industries as well as governments.

Changing focus: With a drop in funding from 2022 to 2023, founders have shifted their focus away from reliance on (or expectations of) VC capital. Founders have needed to work particularly hard to avoid down rounds (raising at a lower valuation than previous investments), by implementing cost cutting programs or avoiding equity raises in favour of bridging finance.

“Startups will continue to attract investment in emerging areas such as AI, cleantech, healthtech and defencetech”

Amanda Price
- Head of KPMG High Growth Ventures

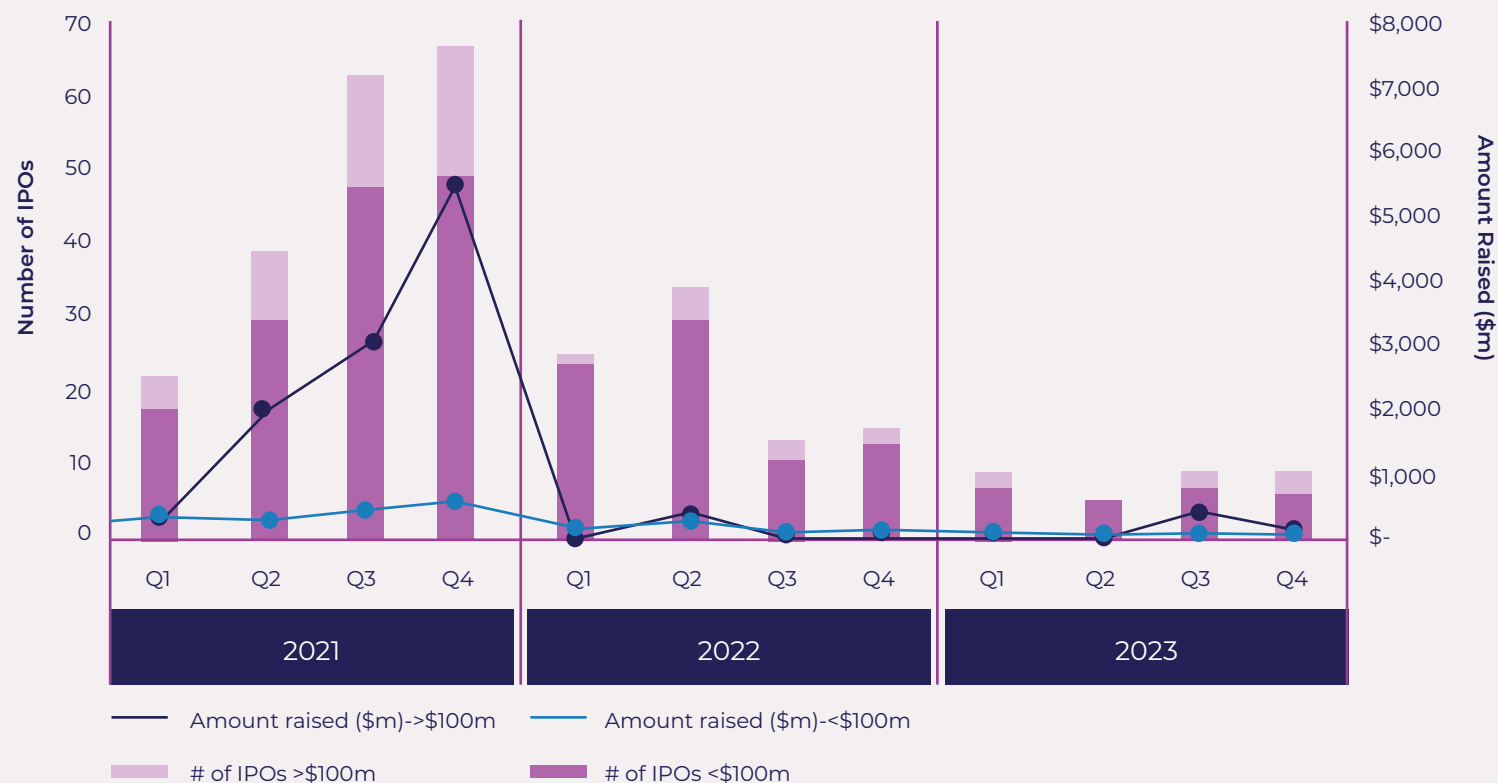
Trend Report

IPO exit activity

It is not surprising given tough economic conditions over the past few years that the number and value of IPOs in Australia has materially declined.

The decline in the Australian market (specifically from Q4 2021 to Q1 2022, and again to Q1 2023) has been reported to be largely a result of interest rate increases and global political and economic uncertainties, with far less large cap listings taking place.

Activity by Quarter



Source: <https://h1b.com.au/2024-ipo-watch-australia-report/>



About Hamilton Locke

Who we are

Hamilton Locke is an award-winning team of lawyers advising forward-thinking businesses and innovators on their most pressing challenges.

Courageous thinking. Collaborative structures. Culture at the fore. These are the qualities that enable us to provide today's most innovative companies with practical advice that moves the dial. From complex transactions to industry-first challenges, we strike the right balance of out-of-the-box thinking and accountability to our clients.

Our nimble structure empowers our team to focus wholly on outcomes. With top-tier lawyers operating across multiple jurisdictions, we bring the best people together to solve a problem and deliver creative and cohesive solutions.

We don't sit on the fence. We put people first. And we do the best work of our lives. It's a breath of fresh air that we believe our clients deserve.

Our corporate team has been recognised in:

Chambers
AND PARTNERS

The
LEGAL
500

IFLR1000 **Best Lawyers**



Great humans (and lawyers).

With over 60 partners and 200 lawyers from all walks of life, we work with authenticity and purpose to deliver efficient and effective advice.



Accessible and practical.

We're here for the long haul. Our advice has your business in mind, so you can easily implement it into your operations.



Local teams, global connection.

We have offices in Sydney, Melbourne, Brisbane, Perth, Newcastle and New Zealand, as well as business networks in the US, UK, and APAC – allowing us to meet your needs, no matter where you are.



Intersection of expertise.

Our teams blend deep sector knowledge with extensive legal experience and an entrepreneurial lens to provide bespoke advice on projects and deals.



Full service, in every sense.

The weight of an award-winning international team, with direct access to top-tier partners. It's the best of both worlds – and how it should be.

Key Contacts and Contributors

Corporate/M&A



Cristin McCoy
Partner
[+61 497 093 763](tel:+61497093763)



Jo Ruitenbergh
Partner
[+61 427 182 390](tel:+61427182390)



Peter Williams
Partner
[+61 421 878 817](tel:+61421878817)



Guy Sanderson
Partner
[+61 413 214 223](tel:+61413214223)



Zane O'Neill
Lawyer
[+61 2 8072 8271](tel:+61280728271)



Venture Debt



Zina Edwards
Partner
[+61 468 992 183](tel:+61468992183)



Lauren Cloete
Partner
[+61 426 591 125](tel:+61426591125)



Funds



Erik Setio
Partner
[+61 434 651 167](tel:+61434651167)



Nick Huett
Senior Associate
[+61 3 8676 7735](tel:+61386767735)



Hamilton Locke has extensive experience and continues to have a strong presence in the VC space. Additional details on our Corporate team and is available [here](#)

Initiatives



Australian Growth Company Awards

The Australian Growth Company Awards were launched in 2012 by Hamilton Locke's managing partner Nick Humphrey to celebrate excellence of high-growth Australian companies. The awards recognise companies that demonstrate high rates of sustainable growth, as well as innovation, integrity and contribution to community.

The awards are proudly co-sponsored by Hamilton Locke, Source, ASX, Findex, MA Financial Group, Ansarada, 2020 Exchange and Willis Towers Watson, as well as media partner, MergerMarket.

[Read more](#)


Technology Scale-up Awards

The Technology Scale-up Awards celebrate disruptive Australian technology businesses that demonstrate high rates of growth and industry-leading innovations, while making a significant impact in their industry sectors.

The awards are proudly co-sponsored by Hamilton Locke, Source, Tank Stream Labs, Ansarada and S2S Summit.

[Read more](#)


Taste of Australia

Taste of Australia is specifically designed for foreign investors and their advisers, and provides a high-level look at the current issues facing deal makers in Australia.

In this edition, we discuss:

- M&A and Capital Markets Update
- ASIC focuses on 'greenwashing'
- Merger control update
- Foreign investment
- Real Estate
- Construction
- Cyber Security and Privacy
- Artificial Intelligence
- Battery Metal Investment
- Agribusiness

[Read more](#)


Takeover Roadmap

From the takeover threshold to acquisition structures, pre-bid arrangements and defensive tactics, takeovers in Australia are highly regulated by legislation and by policy guidance from regulators.

If you're planning a takeover, it's critical to be on the front foot to minimise delays and ensure a smooth process for all involved – which is why we've prepared The Takeover Roadmap.

Whether you're embarking on a new acquisition or in the midst of one, this guide is your companion for navigating the complex world of takeovers in 2024.

[Read more](#)


Hamilton Locke M&A Deal Data Report

The M&A Deal Data Report is a survey of deal trends in Australia across a range of metrics including warranty caps, earn-outs and purchase price adjustments.

[Read more](#)


Raising Capital Guide

Hamilton Locke's Raising Capital Guide summarises the key components of each of the main secondary capital raising options available in the Australian public market.

This guide is specifically designed to assist market participants and the management team of ASX listed entities to understand the capital raising options available to them, and to set out some of the key considerations for determining the most appropriate capital raising method in a particular circumstance.

[Read more](#)


Hamilton Lock IPO Roadmap

The Hamilton Locke IPO Roadmap is a plain- English, easy to follow reference guide with step-by- step advice for businesses. It provides practical and up-to-date guidance on the decision to list, choosing your team, preparation, due diligence and disclosure, the offer and listing.

[Read more](#)


Mergers and Acquisitions

Mergers and Acquisitions, written by Nick Humphrey, is a plain English reference guide mergers and acquisitions and buyouts with step-by-step advice on the key legal, tax and structuring issues when implementing transactions.

This comprehensive text also includes chapters on equity funding, IPOs, distressed buyouts and preparing for exit.

Published by Wolters Kluwer, it can be ordered online:

[Order here](#)

Thank you.



SYDNEY

Australia Square
Level 42, 264 George Street
Sydney, NSW 2000

BRISBANE

Riverside Centre
Level 19, 123 Eagle Street
Brisbane, QLD 4000

NEWCASTLE

Level 3
21 Bolton Street
Newcastle, NSW 2300

MELBOURNE

Level 33, Suite 1
360 Collins Street
Melbourne, VIC 3000

PERTH

Central Park, Level 48,
152-158 St Georges Terrace
Perth, WA 6000

AUCKLAND

Vero Centre
Level 35, 48 Shortland Street
Auckland, 1010 New Zealand

hamiltonlocke.com.au

Disclaimer: Hamilton Locke Australia is operated by Hamilton Locke Pty Ltd (ACN 621 047 247) (Hamilton Locke Australia).

Hamilton Locke New Zealand is operated by Hamilton Locke (NZ) Limited (Company No. 8463155) (Hamilton Locke NZ).

Refer to our [disclaimers](#) page for more information.

