VALUATION: WHAT YOUR BUSINESS IS WORTH TO INVESTORS

Pre-money and post-money value explained, how investors estimate value at different stages, and how to talk about it.

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AT A GLANCE

- **Valuation** is what a business is agreed to be worth when someone invests. It decides how much ownership investors get for their money.
- **Pre-money valuation** is the value before new money comes in. **Post-money** is pre-money plus the new investment.
- Early valuations are more **negotiation than math**. Later ones lean on profits, revenue and comparable businesses.

Why it matters

The valuation decides how much of your company you give up. Too low, and you give away too much. Too high, and you may struggle to raise your next round. Understanding the basics helps you negotiate with confidence.

The basic math

Post-money valuation = Pre-money valuation + New investment

Investor's ownership = Investment ÷ Post-money valuation

EXAMPLE

An investor puts **$500,000** into Sofia's company at a **$2,000,000 pre-money** valuation. Post-money is **$2,500,000**. The investor owns $500,000 ÷ $2,500,000 = **20%**. Sofia and her co-founder own the other 80%.

How value is estimated

Stage or type	Common approach	What drives it
Very early startup	Negotiation, comparable deals, SAFE caps	Team, traction, market size, how much you're raising
Growing tech company	A multiple of revenue (often recurring revenue)	Growth rate, retention, margins
Profitable main-street business	A multiple of earnings	Steady profits, risk, owner dependence
Larger established company	Multiples of EBITDA and cash flow forecasts	Size, growth, stability, industry

Earnings multiples for small main-street businesses are often based on **seller's discretionary earnings (SDE)**: profit plus the owner's pay and certain one-time costs. Larger businesses are usually valued on **EBITDA** (your profit before taxes, interest, and accounting adjustments). Multiples vary widely by industry, size, risk and market conditions. See **X-03 How Businesses Are Valued When They're Sold**.

What raises or lowers value

Raises value	Lowers value
Steady, growing revenue	Uneven or shrinking sales
Recurring revenue and contracts	One-time sales
Strong margins	Thin margins
Many customers	One customer is most of your sales
A strong team	Everything depends on the founder
Clean books and contracts	Messy records
Hard-to-copy advantages	Easy to copy

Talking about valuation

1. **Know your numbers** and comparable deals in your industry.
2. **Start from how much you need**, then think about what share you're willing to give. Many early rounds sell 10% to 25% of the company.
3. **Don't anchor too high.** A valuation you can't grow into makes the next round painful.
4. **Look at the whole deal.** Terms can matter as much as the number. See **R-17 Reading a Term Sheet**.
5. **Get advice** from a mentor, lawyer or advisor who has done deals.

Common mistakes

- **Fixating on a big number** instead of good terms and good partners.
- **Mixing up pre-money and post-money.**
- **Using huge public-company multiples** for a small private business.
- **Ignoring dilution from future rounds.** See **R-16 Ownership and Dilution: The Cap Table Explained**.

Your checklist

- ☐ Decide how much you need and the share you're willing to sell
- ☐ Calculate pre-money and post-money for your target
- ☐ Research comparable deals or multiples for your industry
- ☐ List what raises and lowers your value, and fix what you can
- ☐ Get advice before agreeing to terms

Key words, explained

Word	What it means
Valuation	What a business is agreed to be worth.
Pre-money	Value before new investment.
Post-money	Value after new investment.
Multiple	A number used to estimate value from revenue or profit.
SDE	Seller's discretionary earnings: profit plus owner pay and certain add-backs.

Where to go next

- **R-16 Ownership and Dilution: The Cap Table Explained**
- **R-17 Reading a Term Sheet**
- **X-03 How Businesses Are Valued When They're Sold**

IMPORTANT
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