

# Model Drivers & Forecasting

Dave Parker

[www.dkparker.com](http://www.dkparker.com)

@DaveParkerSEA



# Agenda

- ▣ Outcomes for the day:
  - ▣ Telling a financial story
  - ▣ Key metrics
  - ▣ Templates with Key Inputs
  - ▣ Common mistakes
  - ▣ Rolling up your sleeves

# About Dave

- 5X founder, Board Member, former SVP Programs at UP Global (Startup Weekend + Startup America)
  - Startup Next creator
  - Startup Week
- Author – "[Trajectory: Startup – Ideation to Product Market Fit](#)" shipping 3/2021
- 10 transactions – 8 sell side, 2 buy side now with [NextPath Advisors](#)

# Telling a Financial Story

- Finance is the language of business
- The story comes down to numbers, in cells on a spreadsheet, the model validates the story.
- Investors want to stress test the models and assumptions
- Models serve multiple purposes
  - Fundraising – pitch deck
  - Budgeting and forecasting – scalable revenue
  - Cashflow forecasting – runway

# The Model Supports the Deck

- ▣ The pitch deck provides a 3-5 year summary
  - ▣ You need to know the numbers
- ▣ The summary at a high level
  - ▣ Revenue, cost of revenue and gross margin (\$/%)
  - ▣ Operating expenses
  - ▣ Profitability and cashflow breakdown
  - ▣ Headcount
  - ▣ Key drivers (unit economics/customers)

# Financial Model Best Practices

- The success drivers (metrics, KPI's) are simple and easy to understand. Avoid complicated formulas
- The revenue categories map to one or more of the 14 models
- The five-year ramp is realistic (not \$100M)
- Cost of revenue is complete, so gross margin is correct:
  - Hosting, fulfillment, shipping
  - Labor (customer service)
  - Production costs

# Financial Model Best Practices

- Operating expenses are complete:
  - Expenses grouped by department (fixed vs. variable, cost of sales, etc)
  - Headcount – roles, compensation, benefits
  - Contractors – HR, Accounting, Engineering
  - Travel expense
  - Marketing – reflects go-to-market strategy
  - G&A – facilities, insurance, other operating expenses
- Investments are reasonable to estimate:
  - Intellectual property, equipment

# Financial Model Best Practices

- ▣ GAAP/Accrual based accounting
- ▣ Revenue recognition
- ▣ A great model answer the burning questions:
  - ▣ What are the business drivers?
  - ▣ When does cash flow breakeven occur?
  - ▣ How much investor capital is needed?
  - ▣ Will more than one round of funding be necessary?



# Forecast vs Actual

- ▣ Four dimensions of financial reporting:
  - ▣ Actuals – QuickBooks (accrual)
  - ▣ Operating Plan – Budget (roadmap for the quarter & year)
  - ▣ Forecasting
  - ▣ Variance analysis
    - ▣ Actual to plan
    - ▣ Actual to forecast

# Inputs

# Inputs

- ▣ Marketing
- ▣ Sales
- ▣ Pricing
- ▣ Product Roadmap
- ▣ Staffing

# Marketing/Sales

- ▣ Marketing Funnel is linked to but not in the model
- ▣ What channels
- ▣ When
- ▣ What outcomes
- ▣ Sales conversion metrics
  - ▣ Data comes from CRM
  - ▣ Forecast to actual

# Pricing/Product Roadmap

- ▣ What's the product pricing
- ▣ When do you release new features
- ▣ When are new products scheduled
- ▣ Are services included

# Staffing

- Key hires
  - Budget
  - When
- Time to recruit
- Cost to recruit

# Templates

# Revenue Models– Primary/Secondary

1. Fee for Service
2. Commerce
3. Subscription
4. Metered Service
5. Transaction Fee/Rental
6. Productize a Service
7. Combinations
8. Marketplace
9. Lead Generation
10. Gaming
11. Advertising/Search
12. New Media
13. Big Data
14. Licensing



# Top Templates

- Subscription
  - Recurring revenue, churn, ARR/MRR, LTV:CAC Ratio
- Transaction Fee/Rental (not booking topline revenue)
  - Avg transaction amount, % commission, # transactions/mo, LTV:CAC
- Productize a Service – people are required for some portion – most robust model, includes subscription
  - Split of revenue between product/services
- Marketplace –
  - Two funnels, buy/sell side, % fee, 2X LTV:CAC

# 3. Subscription

- ▣ Example: [Salesforce](#), [Box](#), [Spotify](#)
- ▣ Use: B2C & B2B
- ▣ Key Metrics
  - ▣ Average Revenue Per User (ARPU)
  - ▣ Conversion ratio – e.g. trial to purchase
  - ▣ Churn
- ▣ Challenges: MVP won't be enough to be Kick Ass Product
- ▣ Notes: Highest multiple, forecastable revenue

# 5. Transaction Fees/Rental

- ▣ Example: [99Designs](#), [KickStarter](#), [Elance](#), [Chugg](#)
- ▣ Use: B2C & B2B
- ▣ Key Metrics
  - ▣ Average transaction revenue
  - ▣ Fee % per transaction
  - ▣ Number of transactions
- ▣ Challenges: Margins are small (15%), need efficiency
- ▣ Notes: Don't start too low

# 6. Productize a Service

- Your offerings is generally complex and requires services to deploy
  - Gross margin on Services >35%
  - Product development comes with services
- Use: B2C & B2B
- Examples: Moz, service company convert to tools.
- Challenges – difficult to make the transition away from services

# 8. Marketplaces

- Example: [eBay](#), [Alibaba](#)
- Use: B2C & B2B
- Key Metrics
  - ▣ Average Transaction Amount
  - ▣ Number of Monthly Transactions
  - ▣ Commission %
- Challenges: two sided market places require you start with one side, value to seller & Product market fit (x2)
- Notes: critical mass or marketplace required

Inc 500 Data – Quiz: How much revenue to you need in three year to end up on the Inc 500 List?

# Inc 500 List

- ▣ Data from Top 10 over eight years
  - ▣ Avg \$50.64M
  - ▣ High Average \$147.78M
  - ▣ Low Average \$20.44
  - ▣ All from a baseline revenue of \$1M in first of three years

# Common Mistakes

- ❑ Complex and confusing assumptions - not on one tab
- ❑ Confusing model design
- ❑ Metrics and success factors not defined
- ❑ Overly aggressive revenue ramp
- ❑ Understanding expenses and cash needs (optimism)
- ❑ Key milestones not clearly outlined



# Corp Hygiene Note

- Museum Quality
  - Fully executed contracts
    - In OneHub, Drive, etc.
  - Offer letters, W-4, I-9, options, PIIA
  - Termination procedures
  - Contractor files – NDA, Inventions Agreements
  - Closed monthly books
  - Payroll and tax payments

# Templates

1. Choose a [template](#)
2. Familiarize yourself
3. Startup with Assumptions
4. Move to Compensation and people
5. Revenue next
6. Forecast