Pre- and Post-Money Value

Pre-money value refers to the equity value of a company prior a share capital increase, whilst post-money value already includes outside financing. Therefore, pre- and post-money value represent perspectives differing in their respective timing (pre- and post-transaction).

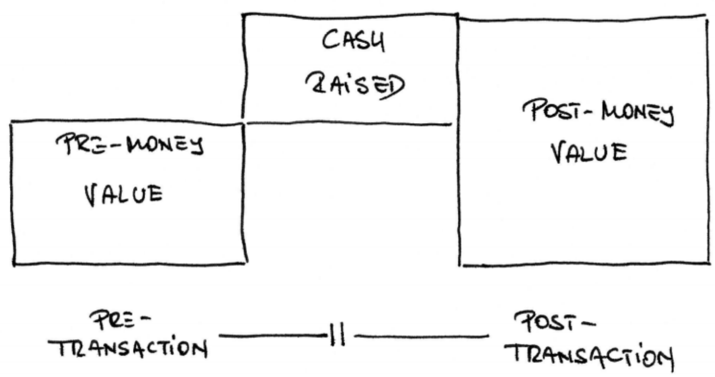
If reference is made to the topic of valuation in the course of an intended share capital increase (e.g. IPO), then in most instances a firm´s pre-money value is meant. Thereby, the value of a firm´s equity is determined from the perspective of prior to the intended transaction.

However, in the course of discussing a startup´s funding round with venture capital funds, frequently also a cross-reference to a firm´s post-money value may be made. Whereby such makes sense, because the actual cash put into a startup is the essential basis for the implementation of a business plan: A different amount of funding would most likely result in a very different strategy or justifiable growth momentum. – Besides, during the discussion of funding rounds of startups, also psychology and anchoring does play a role: Whilst an investor may prefer pointing towards the relative "lower" pre-money value as point of reference, not least for psychological, tactical reasons, the founder consortium may stick to the relative "higher" post-money value. - Such implicit "gaps" may have serious implications, though, if hybrid instruments are considered in addition to a share capital increase, such as, for instance, convertible notes.

Regardless whether a share capital increase were done by a startup or any other considerably more mature firm, its eventual value creation or positive share price impact will largely depend upon the efficient use of proceeds raised. Hence, if the transaction´s purpose is merely to amend a firm´s capital structure (with the business plan largely unchanged), then as per the Miller-Modigliani-Theorem the enterprise value will not change, at least not much.

Such will have to be analysed in detail, though: Whilst the relative weighting of the Cost of Equity (CoE) component will increase, simultaneously CoE itself is expected to come down amid a lower beta (driven by a lower volatility of earnings). In case that the issuer had already debt outstanding, then due to the anticipated decrease in default risk, cost of debt may actually also decrease.

However, if the share capital increase will enable a revamp of the firm´s business plan in that its strategy can now be rolled out much more aggressively, then a value impact is almost assured. From an investor´s point of view, though, the increased number of shares outstanding post-transaction, will technically result in a dilution of current shareholders.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