

3

essential
steps
towards
successfully
financing your
innovative R&D
company

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Three essential steps towards successfully financing your innovative R&D company

- Most innovative life science companies are dependent on external financing for 10+ years before their new technology can generate income and/or is ready for an exit or license deal. Developing and validating new technologies is characterized by high risk and the need for significant capital. In this paper, we provide key pointers to the development of a successful financing strategy that helps you achieve your goals in three essential steps.



Successful fundraising is one of the biggest challenges when developing an innovative life science idea into a market-ready product. There is no 'one size fits all' solution for tackling that challenge. Yet there are essential steps to mitigate the risks involved, and to achieve your ambitions. In the following chapters, we look into the three-step iterative process that exploits the benefits of the different funding tools to meet your financing needs and to attain your short- and long-term goals:

1. **Identify** the funding sources for which you are eligible
2. **Select** the funding sources that match your personal and business needs
3. **Get financed** in accordance with your funding need



Step 1:

Identify your potential funding sources

As a director of an innovative company or project, you have a wide range of potential funding tools that could cover your financing need. The first step is to define the funding sources for which you are potentially eligible.

Once you have established the amount of funding that you need in each product and business development step, the funding source selection can start. The type(s) of funding should fit your end goal(s), the Technology Readiness Level (TRL) of your product, the Business Readiness Level (BRL) of your venture, and the timelines that you ambition. When you want to raise a large amount of money for a short development plan to reach the market, for example, this requires a strong focus on investors. While a long and riskfull development path towards making money will, in most cases, require a strategy which is dedicated more on other types of funding, such as grants, loans, and tax credits.

Basically, all of the different funding tools can be subdivided into:

- **Equity financing** – money from investors that take a shareholder position in the company, i.e. informal investors, family offices venture capitalists, or private equity;
- **Non-dilutive funding** – money provided by parties that do not take a shareholder position in the company, such as governments that provide grants, loans, and tax rebates, health funds that have specific grants, and banks that provide loans.

Considerations for equity funding

Investors are essential for most innovative companies. Equity financing, also known as dilutive funding, provides the basic funding for the business and covers costs (e.g. patents, lawyers, accountants, rent, and salaries of business people) that are usually not financed by non-dilutive financing sources. Furthermore, equity is needed to secure most grants, since governmental funding often requires companies to match the funding with their own co-financing.

Investors are not a homogeneous group, however, there are many flavors and types. These vary from angel or informal investors, professional investors that target early development phases, and venture capital firms and private equity parties that usually target later-stage investment opportunities. It is of critical importance to carefully consider in advance which investors best suit you, your management team, and your goals. Creating the right investment deal for

your venture can be complex and time-consuming, requiring in-depth skills to understand the drivers and processes involved. In reality, it often takes a year or more before a deal with a new investor is finalized and the investment deposited.

Different stages, different investors

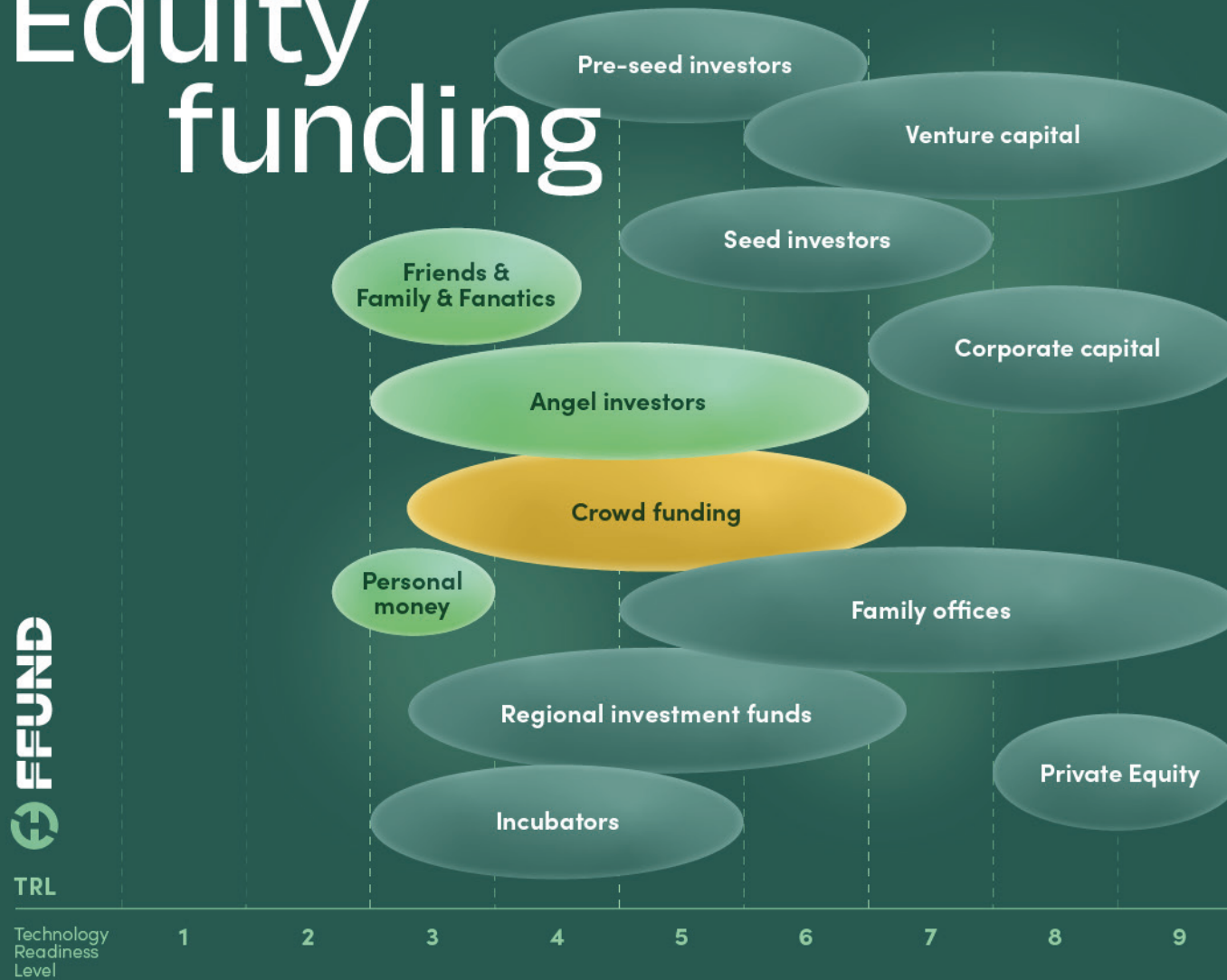
At early development stages, various investor types may be interested in supporting your innovation, including wealthy private individuals and small investment funds, in addition convertible loans also provide an attractive funding source in the early stages. Convertible loans are used when the value of the company cannot be determined yet. You receive money that is only converted into equity at a later stage when a lead investor is attracted and the first company valuation is determined. Convertible loans are provided by various parties, including regional investment funds.

When the project advances, it is important to look into attracting investors who bring more than just money. The onboarding of knowledgeable and experienced life science investors has historically been demonstrated to be a key driver for success and brings the opportunity to accelerate critical

business processes. If you have a valid business idea, investors can provide the money you need together with in-depth knowledge and strategic networks to accelerate critical business processes, albeit in return for company shares.



Equity funding



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TRL

Technology
Readiness
Level



Individual investors



Crowdfunding



Organized investors

Time to get prepared

Entering into a financing round requires thorough preparation to get everything in order and can never be started too early. Investors will ask you for financing strategy and development plan, IP strategy, licenses and contracts, the intended product use, and product-market fit. Furthermore, a well-structured company valuation with sound underlying data and arguments is essential to strengthen your negotiating position. Being prepared and taking enough time helps to ensure that you find investors that bring in the funding, expertise, and momentum you need to steer towards your end-goal(s). And last but not least, taking time to get to a good mutual understanding of the goals of the company and each investor is important as well. Once a shareholder is on board, the chance of parting with them is quite small.

Considerations for non-dilutive funding

Life science innovations are not always appealing to investors in the early stages of a project due to the high risks and uncertainties involved. In those stages particularly, but also later on, different kinds of non-dilutive funding can offer interesting possibilities to obtain financing without giving away shares in the company. This enables the founding partners, management, and existing shareholders to retain company ownership and control, while developing the product and increasing the company's valuation.

Non-dilutive funding sources include government research grants, donations from non-profit organizations, loans, vouchers, prize money, and tax credits, but also compromises revenues that are generated via a service model. However, most non-dilutive funding sources cannot simply be deployed across all TRLs and BRLs. Instead, most funding is specifically available to cater a particular technology and company development stage.

Grants for EU innovations

Different kinds of grants are available to finance (parts of) the product development stages, including feasibility studies, scientific research, and research and development (R&D). Examples of well-known funding bodies in Europe are the European Commission (including but not limited to the Horizon Europe program and EU4Health program), Eureka network, and European Institute of Innovation and Technology (EIT). And most European countries and provinces/regions also have local grants for innovative projects from their area.

From a business development perspective, a company can also use grants to overcome unforeseen issues, relieve financial pressure, extend the horizon of the venture, and reduce the risk of projects. Finally they offer the opportunity to close attractive partnerships under favorable conditions.

Grants and loans are excellent non-dilutive funding tools to raise funding, but the rules and regulations as well as the requirement for application need to be evaluated carefully. Grant applications are often complex, have very specific requirements, and have specific deadlines for submission. The application process may take up a lot of time and effort, while the chances of success are fairly low. And when you are successful, the administrative reporting of awarded grants is often bureaucratic and time-consuming.

Some key parameters to check you eligibility and match with a grant:

- funding amount
- funding percentage / cofinancing
- timeline for the project
- TRL/BRL requirements
- requirements to collaborate with specific parties
- ownership of IP

Loans for innovators

While grants can be used across all TRLs, hard loans are generally more interesting at a later stage when the technological and business risks are lower. Loans are an interesting non-dilutive funding tool to raise considerable sums of money. As loans need to be paid back with interest, however, they do have a significant impact on the future company financial position and cashflow need.

Tax incentives for innovators

Tax incentives form an important non-dilutive funding source for innovative companies. This governmental regulation exists to support R&D in a simpler and more predictable way than grants. Most frequently, the tax incentives provide a payroll tax reduction on the R&D personnel.

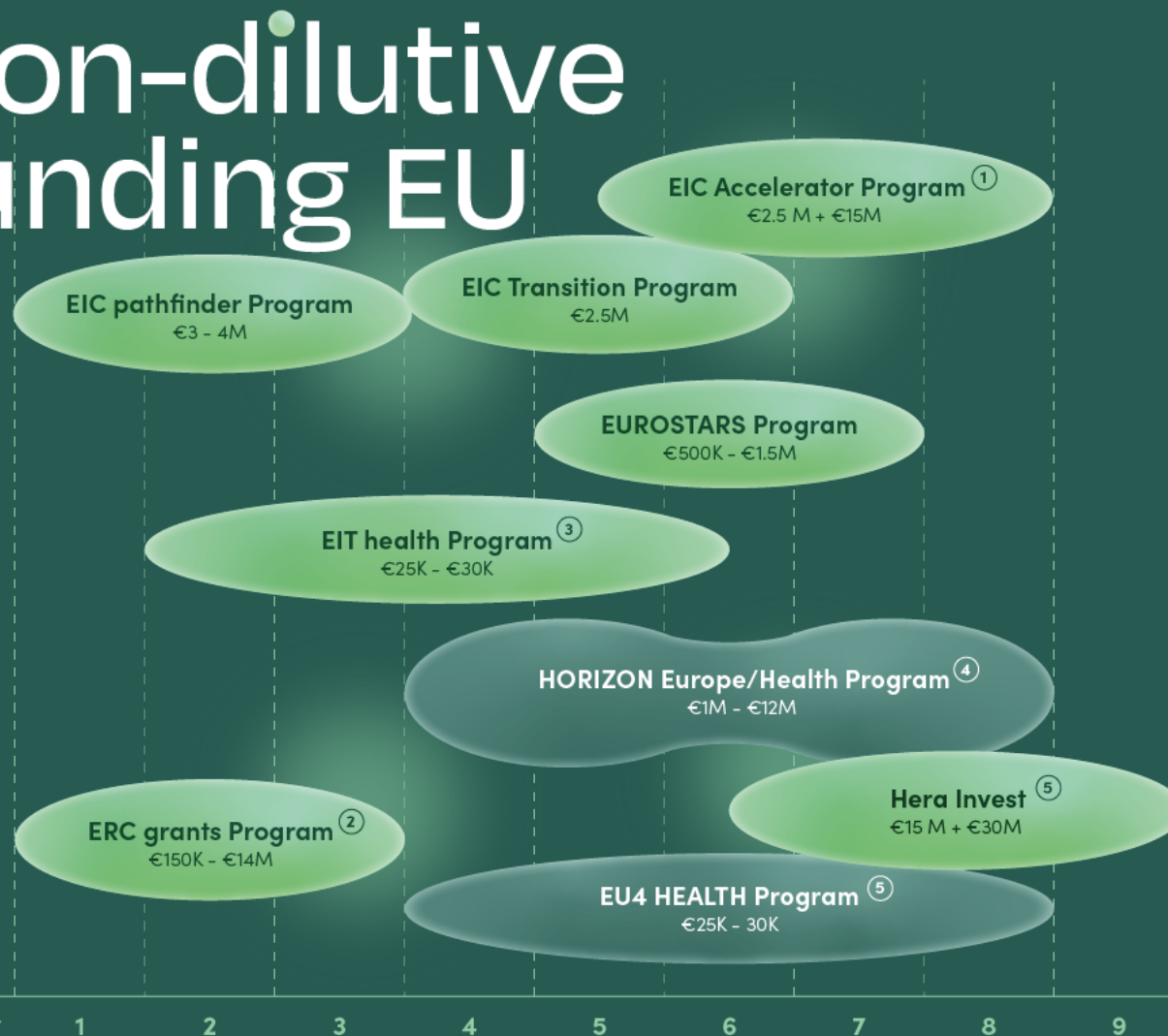
The design and execution of tax incentives falls under the responsibility of each individual country in the EU, therefore as the owner of an innovative company, you should contact your national contact point, to check if and how you can make use of this non-dilutive funding. AS a final note, please be aware that next to relieving the financial burden of the company, the use of tax incentives makes you more attractive to (venture capital) investors as well.

Non-dilutive funding EU

FFUND

TRL

Technology
Readiness
Level



Bottom-up calls for all innovative life science projects



Top-down calls for specific innovations

- ① **EIC Accelerator** is a combination of €2.5 M subsidy and up to €15 M equity investment.
- ② **ERC Grant Program** consists of 5 different calls: ERC Starting (€1.5M - €2.5M), ERC Consolidator (€2M - €3M), ERC Advanced (€2.5 M - €3.5M), ERC Synergy (€10M - €14M) and ERC Proof of Concept (€150K)
- ③ **EIT Health Program** consists of multiple programs with small in cash and in-kind prizes and/or vouchers for training, networking, expert support, and (business) booth camps.
- ④ **Horizon Europe Program** consists of 3 different calls: HORIZON - HEALTH (indicative funding per project €6M - €12M), Innovative Health Initiative (indicative funding per project €8.5M) (2 Calls in future) and HORIZON - EDCTP (indicative funding per project €1M - €5M)
- ⑤ **EU4 Health program** consists of grants/vouchers/prizes (€25K - €30K) and equity funding options. The HERA Venture loan program is also part of EU4 Health, with an indicative funding range of €15M - €30M, but other amounts are also possible.

Step 2:

Align the funding sources with your critical personal and business goals

The better you define the goals for yourself and the company, and the better you are aware of and connected to a variety of funding sources, the higher the chance of success and the shorter the path to make the technology available to the healthcare system.

Thinking about the end game upfront will help to ensure that you make the right funding choices along the way, to enable you to reach the (end) goals for the product, the company, and yourself. Do you primarily want to focus on making your product and company successful within a certain

timeframe. Or is it equally important to you to keep a strategic position, steering power, and ownership of the company? Such choices are of critical importance in selecting the right funding tools.

Identifying the key drivers

— To be successful, you need to know what you, your co-shareholders, and the company define as success. Below, you will find three critical components that need to be defined in setting goals for the company, to enable you selecting the optimal funding sources.

Is your business driven by technology push or demand pull?

Are you developing a technology for which you are flexible to determine the optimal target market (technology push), or are you driven to develop a solution for a specific group of users, i.e. patients (demand pull)? In the latter case, you should be flexible in adjusting your technology, or even completely changing gears and letting go of the original intellectual property to acquire a better/alternative solution for the same target market.

For your financing strategy, it is essential to identify a good product-market fit and avoid misalignment between the business goals and the ambition of the original founders. When the goal is clear, you will be able to identify financing instruments that match your ambitions and, most importantly, will support you in that same line when changes need to be made to the development plan.

What is your timeline to market?

Typically, founders may think they are on the same page, until choices have to be made about how money is invested, and when to make the transition from explorative research to a focused R&D plan that will lead to a validated and ready-to-scale product. As soon as there are multiple shareholders in the company, the timeline to see a return on investment in time, effort, or money will become the driver. Be sure to make it a continuous part of your shareholder conversations to find common ground and understanding on the definition of success regarding the timeline towards return on investment.



Ownership, collaboration, and network?

The final essential aspect is achieving alignment between the shareholders of the company. When designing the ultimate funding strategy, it is crucial to know upfront if and how the various funding options align with your company requirements. Besides money, different funding sources may provide a huge accelerator function (i.e. by opening doors to critical deal partners or

providing expert insight) or a tremendous time or focus lag (i.e. by requiring you to lead a big consortium of partners). In this respect, you should know if you are prohibited or enabled by the attracted funding.

Your goals and your definition of success are the foundation on which to create your product and company development plan, determine

your overall R&D costs, and build your financing strategy. Once this foundation is clear, you can start to select funding tools that match and facilitate the development of the company and product in line with the ambitions. The financing strategy is a guideline that describes the different dilutive and non-dilutive funding tools at your disposal, and how and when they can be strategically used. One type of funding is not necessarily preferable to the other, but they each have specific pros and cons that can be exploited depending on what you want to achieve. Certainly, the potential impact on the personal position of the founding team should not be underestimated when attracting funding from parties with different expectations. When the alignment is right, your funding strategy will enable you to greatly accelerate the path to success.



Step 3:

Gain financing in accordance with your funding needs

In most cases, creating the right mix between equity and non-dilutive funding is crucial to finance the company and product development.

Making strategic use of the benefits of different equity and non-dilutive funding instruments, enables you to bring cash flow into your company, keep the required steering power, and mitigate experimental- and business-related risks. This can be achieved by working according to a financing strategy that is dedicated to achieving the end goal(s), and which is tweaked to recover from setbacks when needed and to accelerate when possible.

The three most common financing strategies are:

- **Full focus on the use of grants and loans** to fund the R&D and to keep full ownership of the innovation.
- **Full focus on attracting and connecting knowledgeable investors** to accelerate the product development and opportunities towards a fast exit through a (license) deal.
- **Full focus on generating revenues through services** as soon as possible to obtain financial resources for R&D and to build a long lasting business.

A financing strategy acts as a guideline to decide which type of funding to use at different TRLs and how they can best support each other. Ultimately, you need to make a list of the preferred options and a list of alternative options that will be explored when the priority list is not (fully) secured. Non-dilutive funding sources generally use expert stakeholders with deep domain knowledge to review a project proposal, which provides important validation of the team and technology. When successfully securing regional, national, and European non-dilutive funding in the earlier R&D phases, this may at later stages provide more success when reaching out to equity investors.

As non-dilutive financing helps to increase the company's valuation whilst retaining company ownership, it provides the founding partners and existing shareholders with a stronger negotiating position with new investors. It demonstrates to the potential investors that you have a professional management team that can attract funding and that you are a reliable investment. Combining multiple funding sources also helps you to deliver to your investors, even when there are unexpected (scientific) circumstances.

In conclusion, make sure to regularly align the progression in the technology and business development steps with the goals of the shareholders, and the new funding sources that are identified. When you make this three-step fundraising strategy approach an operational process in your business that receives continuous attention, you will maximise the chances securing a continuous financial runway, to reach success.

Financing your business is a continuous process

Once you have secured the optimal financing mix that matches your current funding need, you would be well advised to keep reviewing it every annual quarter as the field is continuously evolving. New types of investors may enter the market, or new grants may become available. You do not want to miss any investment opportunities or grant application deadlines that could have been a perfect match for your company. And if your attempts to gain funding do not have the desired outcome, making some adjustments to your personal and business goals might create a better fit.

The three top funding challenges

Of the many aspects to think about when developing a financing strategy for an often-uncertain product development path, the following will help you steer through the most crucial funding challenges:

1. Check Timelines

Smartly align the time windows from certain investors and funding sources with your company development plan and ensure that you are fully prepared to pitch and present your proposition when the window for funding is opening at the funding agency. Be aware that each funding source works with a timeline during which they are able to select projects in which to invest. For investors, this window may take several years, while some grants will only be available once, or at best a couple of times per year; small time windows to submit your project proposal.

2. Read Terms & Conditions

Be aware and choose the right funding sources to align the contractual terms and conditions that accompany the receipt of external funding from (governmental) funding bodies and investors with you and your goals. Be aware that most funding cannot be spent on all company costs, but may only be used for activities that are selected and approved by the party that provides the money. Furthermore, most funding providers and investors will require you to follow their specific rules for i.e. collaboration, reporting and decision making.

3. Prevent dependencies

Avoid full dependency of one funding source on another. Especially when various investors or funding providers want the other party to take the first step, or when different funding streams might be linked to the same company milestone, you need to be ready and prepared with strong communication skills, data, and steering power to unlock the next stage of venture financing and prevent stagnation of the company financing due to unforeseen events that postpone the completion of a milestone.