

Financial Statements & Startup Valuation

1. Introduction to Financial Statements

What They Are

Systematically organized records that summarize a company's:

- Financial health
- Performance
- Position over a specific period

Why They Matter

- Help investors, lenders, and founders understand the business
- Used to analyze profitability, liquidity, and long-term sustainability
- Build credibility and guide decision-making

2. Accounting Principles Foundation

1. Accrual Principle

Record income and expenses when the activity occurs—not when cash is received or paid.

2. Matching Principle

Pair revenues with the exact expenses that helped generate them.

3. Going Concern Concept

Prepare financials assuming the business will continue operating in the future.

4. Consistency Principle

Use the same accounting methods each period to maintain comparability.

5. Prudence Principle

Recognize potential losses early; recognize gains only when certain.

6. Materiality Principle

Focus on information that significantly affects business decisions.

3. The Three Core Financial Statements

A. Income Statement – The Profit Pulse

Tracks:

- Revenue
- Expenses
- Profit or loss

Answers: “Are we making money?”

Types

- Single-step
- Multi-step

Common Expenses

- Advertising & promotion
- Legal, insurance, accounting
- Office supplies
- Selling, general & administrative expenses
- Gains & losses (sales, investments, FX, instruments)

B. Balance Sheet – The Financial X-Ray

Shows:

- **Assets** (what the company owns)
- **Liabilities** (what it owes)
- **Equity** (net worth)

A **snapshot** of financial position at a specific date.

Accounting Equation: Assets = Liabilities + Equity (Must be balanced)

Nature of Components

- **Assets:** Future economic benefits
- **Liabilities:** Obligations and claims
- **Equity:** Residual value after liabilities

C. Cash Flow Statement – Cash Control Central

Tracks actual cash movement:

- Cash inflow
- Cash outflow

Answers: **“Do we have enough cash to survive and grow?”**

Shows impact of:

- Operations
- Investing
- Financing activities

4. How Financial Statements Connect

Step 1: Start with Earnings (Income Statement)

Revenue and profit lay the foundation.

Step 2: Profits Power Equity (Balance Sheet)

Net income increases equity.

Step 3: Assets & Liabilities in Motion

Every purchase, payment, or investment updates the Balance Sheet.

Step 4: Money Moves (Cash Flow Statement)

Shows real cash impact—profits \neq cash.

Step 5: Cash Updates Balance Sheet

Ending cash from the Cash Flow Statement updates Balance Sheet cash.

Step 6: One Unified Engine

All three statements operate together to:

- Drive decisions
- Support growth
- Attract investors

5. The Importance of Financial Statements

They help analyze:

- Profitability
- Liquidity
- Operational efficiency
- Long-term sustainability

They provide clarity for:

- Investment decisions
- Business strategy
- Market confidence

6. Financial Analysis: Why & How

Why We Analyze Statements

- Assess financial health
- Understand liquidity
- Measure profitability
- Make investing or lending decisions
- Understand strategy

How We Analyze: Key Ratios

- **Profitability:** Net Profit Margin, ROE
- **Liquidity:** Current Ratio
- **Investor Ratios:** P/E ratio, EPS

7. Reading Beyond the Numbers

A. MD&A (Management Discussion & Analysis)

Includes:

- Explanation of performance
- Future strategy
- Risks
- Management judgement

B. Notes to Financial Statements

Contain:

- Accounting policies
- Commitments
- Contingencies
- Clarification behind reported numbers

8. Annual Report – Key Components

1. Audit Report
2. Letters to Shareholders
3. Business Description

4. MD&A
5. Financial Statements
6. Notes to the Financial Statements

9. Case Study: Flipkart – Building Billion-Dollar Value

Step 1: Ignite the Vision

Ambition: Make online shopping simple and trustworthy.

Seed funding: \$800,000 from Accel.

Step 2: Spot Emerging Opportunities

Innovations such as:

- Cash-on-delivery
- Partnership with India Post

Step 3: Leveraging Financial Statements

Income Statement:

- Revenue grew 93% (₹42,942 cr → ₹82,787 cr)
- Losses used strategically for market dominance

Balance Sheet:

- Assets grew 59%
- Massive equity support enabled Walmart's \$16B acquisition

Cash Flow:

- Raised ₹47,004 cr (FY23)
- Cash improved from ₹39M → ₹6,599M

Result:

Zero profits for 17 years but valued at **\$36B**.

Step 4: Getting Investor Buy-In

Focus on:

- Market share
- User experience
- Potential for future value

Navigating Challenges

- Competition
- Logistics
- Pricing pressures

Outcome

Valued above **\$36B** by 2024–25.

10. Understanding the Balance Sheet in Decision-Making

Example Scenario

Company A: High revenue, fast growth, heavy debt

Company B: Lower revenue, stable growth, strong equity

Insight: Balance Sheet strength predicts recession survival.

Key Truth

- Profits can be manipulated
- Cash flow can be timed
- **But the Balance Sheet cannot be faked**

11. Startup Valuation Basics

What It Is

Estimating how much a startup is worth.

Why It Matters

- Determines equity dilution
- Influences negotiations
- Builds investor trust
- Sets future valuation benchmarks

12. Valuation Methods

1. **Discounted Cash Flow (DCF)**
2. **Comparable Method**
3. **Scorecard Method**
4. **Venture Capital (VC) Method**

13. Key Factors Affecting Valuation

- Traction (active users, growth)

- Revenue model
- Market size (TAM–SAM–SOM)
- Team strength
- Competitive advantage
- Risk level (market, financial, product)

14. Case Study: EduLift – Skill Learning App

Startup Snapshot

- 40,000 MAU
- ₹8 lakh monthly revenue
- 15% monthly growth
- ₹5,000 cr EdTech market
- Low CAC

VC Method Valuation

- Expected Exit Value: ₹200 Cr
- Target ROI: 10x

Valuation = 200 / 10 = ₹20 Cr (Pre-money)

Investor Example

- Investment: ₹2 Cr
- Equity: 10%
→ Matches ₹20 Cr valuation