Twitter Thread by Alex Banks

Alex Banks
@thealexbanks

Investing can be complicated.

Let's make it simple.

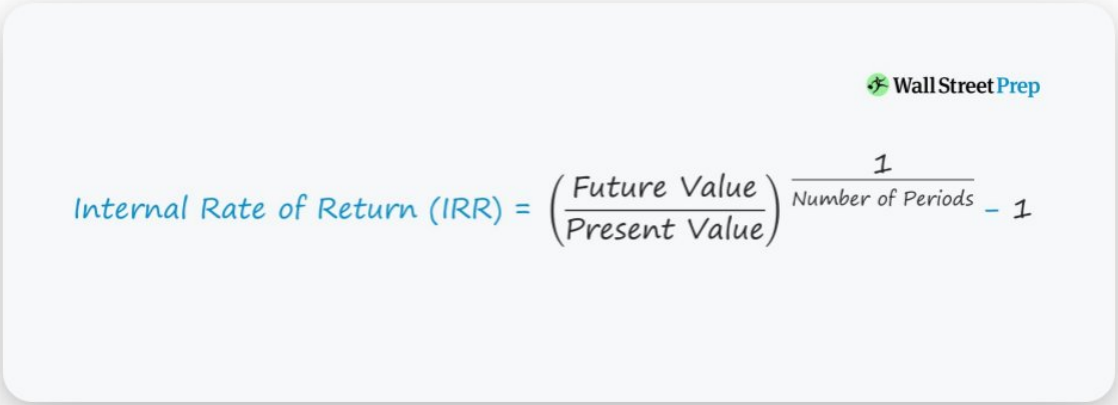
10 terms every entrepreneur and investor should know:

1/ Internal Rate of Return (IRR)

IRR tells you what your average return is when time value of money is factored in.

Let's say you have an option to get 100K today or 100K in 5 years.

You would obviously prefer to get paid today so you can reinvest.



This also prevents future inflation from eating your purchasing power.

An investment that realises returns sooner than later will have a higher IRR.

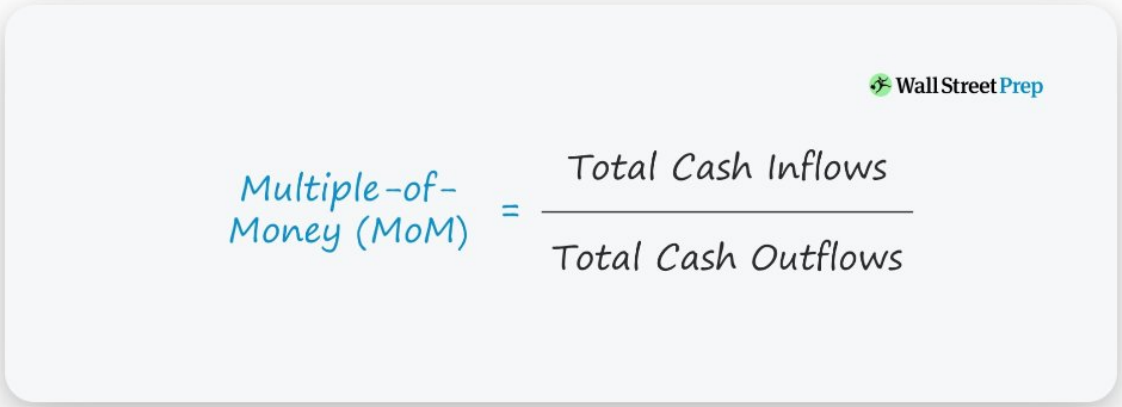
2/ Multiple of Money (MoM)

Also known as cash-on-cash return or multiple of invested capital (MOIC).

Example:

Total cash inflows (proceeds from sale of a company) = $100M
Total cash outflows (initial investment) = $10M

MoM would be 10.0x.



3/ Rule of 72

A “back-of-the-envelope” method to calculate how long it would take your investment to double (2x).

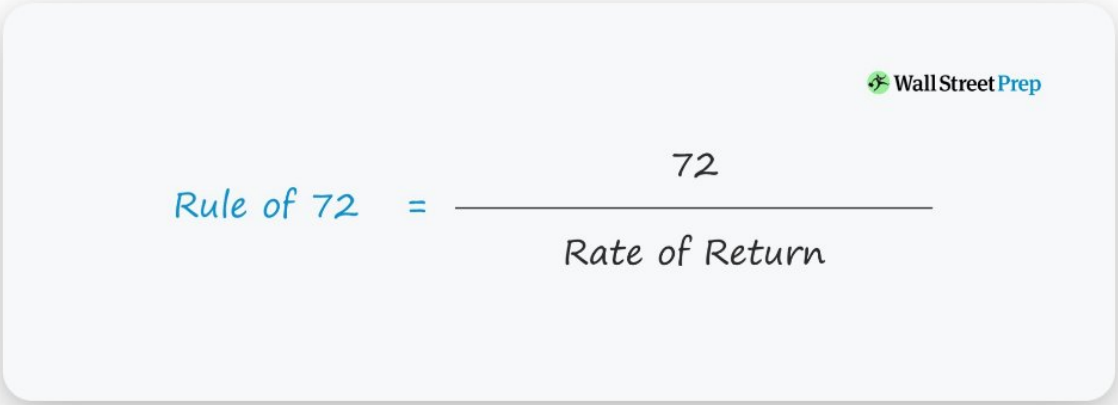
Example:

How long would it take to double my money if I invest in the S&P 500?

S&P 500 average return = 8%

= 72 / 8

= 9 years



4/ Rule of 115

Tells you how many years for your investment to triple (3x).

Lesser known than the rule of 72, still powerful.

Same example:

How long would it take to triple my money if I invest in the S&P 500?

S&P 500 average return = 8%

= 115 / 8

= 14.4 years

The Rule of 115 Formula

- *Number of Years to Triple = 115 / Interest Rate*

5/ Total Value to Paid-In Capital (TVPI)

TVPI answers, “How does the total realised and unrealised profits compare to the initial paid-in capital”

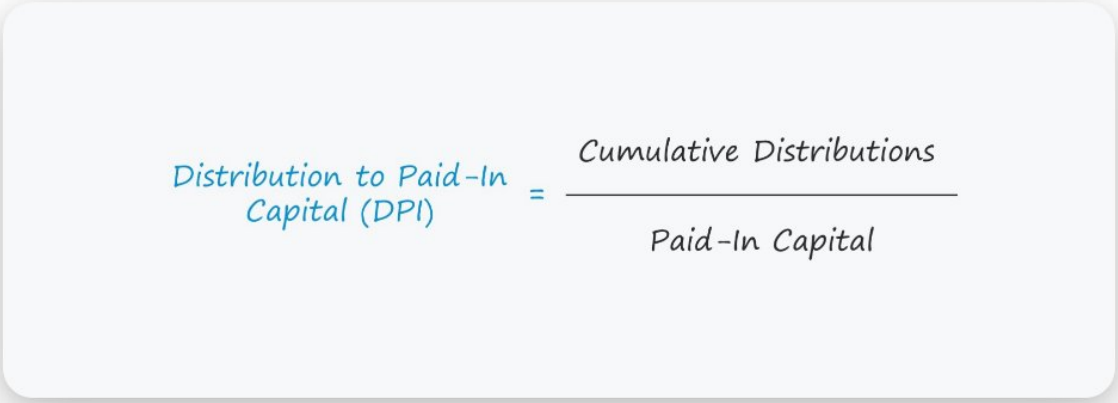
Cumulative distributions = Realised profits
Residual value = Unrealised potential profits
Paid-in capital = Investor's commitment

$$\text{Total Value to Paid-In Capital (TVPI)} = \frac{\text{Cumulative Distributions} + \text{Residual Value}}{\text{Paid-In Capital}}$$

6/ Distribution to Paid-In Capital (DPI)

DPI measures the amount of money returned by a fund to its investors relative to their paid-in capital.

Cumulative distributions = Realised profits
Paid-in capital = Investor's committed capital



7/ Dry Powder

Dry powder is capital committed to private investment firms that still remains unallocated.

It's money that's sitting on the side, yet to be invested.

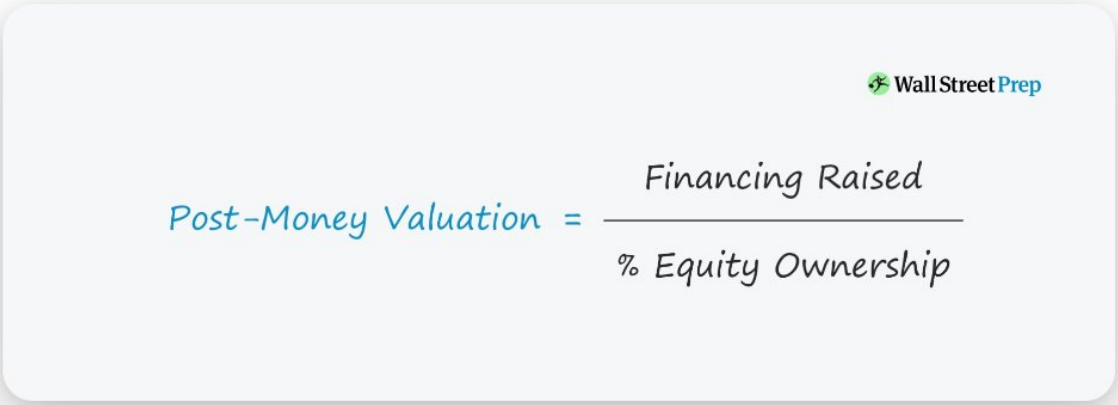


8/ Post-Money Valuation

Post-Money Valuation = The value of a company’s equity once the round of financing has occurred.

This includes the latest capital injection.

Post-money valuation = pre-money valuation + financing raised



9/ Pre-Money Valuation

Pre-Money Valuation = The value of a company’s equity before raising a round of financing.

This is the value of a company excluding the latest round of funding.

Pre-money valuation = post-money - financing raised

10/ Up Round vs Down Round

An "up round" means the valuation of the company raising capital has increased in comparison to the prior valuation received.

A "down round" means the company’s valuation has decreased post-financing in comparison to the preceding round of financing.

TL;DR:

1/ Internal Rate of Return (IRR)
2/ Multiple of Money (MoM)
3/ Rule of 72

4/ Rule of 115
5/ Total Value to Paid-In Capital (TVPI)
6/ Distribution to Paid-In Capital (DPI)
7/ Dry Powder
8/ Post-Money Valuation
9/ Pre-Money Valuation
10/ Up Round vs Down Round

Follow me @thealexbanks for more threads on startups and investing.

If you liked this thread, you'll love the newsletter.

Subscribe here:
https://t.co/rX04WMkBwf

Source: https://t.co/jJNukpld7H

I write threads each week, here's another I think you'll enjoy:
https://t.co/uh8YW1cvgc

> The most important trait of an entrepreneur is someone who can tell a story.
>
> 10 storytelling principles to get their attention, raise money and win deals:
>
> — Alex Banks (@thealexbanks) August 1, 2022

Help others learn and quote tweet this thread:
https://t.co/glkbGd2Dxu

> Investing can be complicated.
>
> Let's make it simple.
>
> 10 terms every entrepreneur and investor should know:
>
> — Alex Banks (@thealexbanks) August 3, 2022