Mastering the Field: A Critical Analysis of 'Entrepreneurial Finance' by Leach and Melicher

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Abstract

About the Book

Book Name: Entrepreneurial Finance, 7th Edition, 2020
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About the Book Authors:

J. Chris Leach is a distinguished academic and Professor at the Leeds School of Business, University of Colorado at Boulder. He is known for his exceptional teaching abilities, entrepreneurial background, and research in finance. Leach has received awards for his teaching and has played an active role in startups since the 1970s. He is also a faculty advisor and mentor for the Deming Center Venture Fund.

Ronald W. Melicher is a distinguished Professor of Finance at the same university. He is celebrated for his teaching abilities and has held key positions in the Finance Division. Ronald's expertise spans various finance topics, and he has taught at prestigious institutions globally. He is also recognized as an expert in financial management and firm valuation, offering consultancy services and conducting research in critical areas of finance.

INTRODUCTION

Entrepreneurial finance applies principles of finance and economics to ventures led by entrepreneurs, emphasizing value creation, risk management, financial modeling, and venture valuation. It prioritizes the perspective of the entrepreneur over traditional shareholder views, aiming to equip entrepreneurs, venture capitalists, and investors with the necessary tools to navigate the financial landscape of new ventures effectively (Brealey and Myers, 2003). The life of an entrepreneur is characterized by excitement and dynamism, involving the challenge of conceiving new products or services, inspiring others with entrepreneurial spirit, and bringing innovations to market. As described by Leach and Melicher (2020), entrepreneurial finance delves into the financial management aspect of these ventures, particularly those in their early stages with limited operating history. These ventures are focused on rapid value creation, adopting a life cycle approach to financial strategies. The emergence of entrepreneurial ventures is crucial for a country's development goals. Many successful large companies began as early-stage ventures, highlighting the significance of nurturing such enterprises.

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This book offers a comprehensive guide to understanding the theories, principles, and practical tools of corporate finance essential for initiating, developing, and ultimately monetizing a successful entrepreneurial venture in alignment with its life cycle stages. The supplementary materials accompanying the book comprise an Instructor's Manual with a Test Bank, PowerPoint Lecture Slides, Excel Solutions, and access to the Text Website. The Instructor's Manual, authored by the book's creators, offers concise answers to end-of-chapter questions and solutions to end-of-chapter problems. The Test Bank features true/false and multiple-choice questions, as well as brief test problems, exclusively available on the text website for instructors.

Additionally, PowerPoint Lecture Slides provide a comprehensive lecture outline with visuals, equations, and key points, designed by the authors and accessible solely on the text website for instructors. Instructors also receive Excel solutions for end-of-chapter problems requiring Excel usage, accessible on the text website. Furthermore, the Text Website, located at https://www.cengage.uk, grants instructors access to all supplementary materials. The book comes highly recommended as essential reading material for undergraduate and master's students studying Entrepreneurial Finance. It is also highly
beneficial for entrepreneurs and managers of early-stage businesses. Moreover, corporate leaders can use the book as a reference to gain insight into the nature of the early-stage venture journey within their life cycle.

This book is structured into 7 parts, aligning with the life cycle stages of successful entrepreneurial ventures: development, startup, survival, rapid growth, early maturity, exit, and turnaround. The first two parts focus on foundational knowledge, covering idea generation, business plan development, and cash management strategies crucial for the early stages of a venture. Part 3 delves into the types and sources of financial capital, as well as investment processes, essential for entrepreneurs to understand as they seek funding for their ventures. As ventures progress beyond survival, they shift focus toward value creation and calibration. Part 4 addresses valuation tools and techniques vital for ventures emerging from the survival stage. Additionally, Part 5 highlights the legal environment governing financial relationships between ventures, investors, and financial institutions, including venture capital funds and investment banks. Part 6 examines venture harvest strategies, including successful exits and turnaround approaches for troubled ventures. This section also introduces important aspects of financial distress and alternative restructuring methods.

To reinforce learning, leading capstone cases are presented in Part 7, providing readers with practical applications of the knowledge covered throughout the book. These cases offer valuable insights into real-world entrepreneurial challenges and solutions, enhancing the reader's understanding of entrepreneurial finance across different life cycle stages.

ABOUT THE AUTHORS

J. Chris Leach is a distinguished academic who holds the positions of Professor and Chair of the Finance Division, as well as the Robert H. and Beverly A. Deming Professor in Entrepreneurship at the Leeds School of Business, University of Colorado at Boulder. He earned his Ph.D. in finance from Cornell University and has taught at prestigious institutions such as the Wharton School. Leach is renowned for his exceptional teaching abilities and has received awards such as Graduate Professor of the Year. His research, published in prestigious journals, covers various finance topics. Additionally, Leach has a strong entrepreneurial background, actively participating in startups since the 1970s and providing consultancy services in business planning, valuation, and deal structuring. He demonstrates a commitment to fostering entrepreneurship through his role as a faculty advisor for the Deming Center Venture Fund, guiding MBA teams to international success in competitions. Overall, Leach's multifaceted expertise and dedication have earned him respect in both academia and the business world.

Ronald W. Melicher is a distinguished Professor of Finance at the Leeds School of Business, University of Colorado at Boulder. He is celebrated for his exceptional teaching abilities and academic accomplishments. Ronald holds degrees from Washington University in St. Louis, Missouri, and has received numerous prestigious teaching awards, including the esteemed title of university-wide President’s Teaching Scholar. Throughout his illustrious tenure at the University of Colorado, Ronald has held key positions such as Chair of the Finance Division, William H. Baugh Distinguished Scholar, and Faculty Director of various MBA programs. Ronald's teaching prowess spans a broad spectrum of finance topics, catering to both MBA and undergraduate students.

He has also taught at renowned institutions globally, including the INSEAD Graduate School of Business in France and the University of Zurich in Switzerland. In addition to teaching, Ronald has delivered executive education courses and provided tailored finance education for leading corporations such as IBM. Beyond teaching, Ronald is recognized as an expert in financial management and firm valuation. He offers consultancy services and expert witness testimony in regulatory proceedings and various financial domains. His research interests include critical areas such as mergers and acquisitions, corporate restructurings, and the financing and valuation of early-stage firms, making substantial contributions to the field of finance. Overall, Ronald's diverse expertise and unwavering dedication to education and research have solidified his status as a prominent figure in both academia and the business world.

REVIEW

Entrepreneurial Environment

Part 1 of this book provides an extensive overview of entrepreneurial finance and underscores the necessity of crafting a comprehensive business plan. The authors effectively delineate the distinctions between entrepreneurial finance and corporate finance. They portray entrepreneurial finance as the process of fostering value for early-stage ventures through the development of opportunities, acquisition of resources, and effective management and operations. Consequently, readers come to realize that the primary objective of entrepreneurial finance aligns with that of corporate finance: value creation. Chapter 2 emphasizes the critical importance of a well-prepared business plan for entrepreneurial ventures, given their limited historical data. The authors argue that early-stage investors, such as business angels, heavily rely on the business plan when making investment decisions. Thus, the initial chapters of Part 1 furnish readers with the essential knowledge necessary for comprehending the subsequent chapters of the book.

Organizing and Operating the Venture

As early-stage ventures progress from the development stage to the startup phase, entrepreneurs must adopt appropriate business models for their endeavors. Chapter 03 in Part 2 of the book delves into this crucial aspect, highlighting that while the specifics may vary from one country to another, the fundamental principles remain essential knowledge for entrepreneurs. As ventures transition from the startup stage to the survival stage, the preparation of financial statements becomes imperative, especially considering the increased need for external financing at higher stages of the life cycle. Chapters 4 and 5 present...
these concepts in an engaging manner, making them accessible even to individuals without prior financial knowledge. The inclusion of real-world examples further enhances understanding, facilitating the absorption of the material at a deeper level.

Planning for the Future
Managing cash flow is vital for the future growth of entrepreneurial ventures (Azarenkova et al., 2022). In Part 3, Chapter 6 of the book, readers gain insight into cash budgeting, short-term projected statements, and the utilization of conversion ratios to identify short-term cash drivers. Estimating the cost of financial capital for entrepreneurial ventures differs from the calculation used in corporate finance (Menachem et al., 2016). Chapter 7 covers this essential knowledge, incorporating factors such as advisory premium, hubris projection premium, and liquidity when estimating the cost of equity for early-stage ventures. The book's strength lies in its presentation of content aligned with the venture lifecycle, allowing readers to comprehend complex concepts methodically.

Creating and Recognizing Venture Value
Part 4 of the book holds significant importance as it addresses a crucial aspect of entrepreneurial ventures: value creation. Entrepreneurs embark on these ventures with the primary goal of generating value for themselves. Entrepreneurs must possess the knowledge and skills required to assess the level of value their ventures are creating or potentially destroying. Chapters 10 and 11 are particularly noteworthy as they offer insights into various tools that entrepreneurs can utilize to evaluate the value of their ventures. This understanding is essential in entrepreneurial finance and forms a cornerstone of knowledge in this field. While this content is commonly found in textbooks within the entrepreneurial finance domain, its inclusion underscores its critical importance. Furthermore, the book delves into different techniques for venture valuation, which are pivotal for entrepreneurs in determining the worth of their ventures (Damodaran, 2009). The authors focus on methodologies such as discounted cash flow methods, just-in-time equity valuation, and venture capital valuation methods. These techniques provide entrepreneurs with valuable insights into how to assess and understand the financial worth of their ventures, enabling informed decision-making and strategic planning for future growth and development.

Financing for Growing Ventures
As the venture progresses into its rapid growth stage, additional financing becomes crucial to meet the demands of sales growth (Egle et al., 2019). Therefore, the authors have dedicated a separate section to discussing professional venture capital investments and other financing alternatives. The development of the professional venture capital industry may vary from one country to another, but the fundamental knowledge provided in this regard remains universally applicable to readers worldwide. In Chapter 13, the authors explore alternative financing sources such as business incubators, crowdfunding, seed accelerators, and various microcredit programs, particularly from the perspective of the US context. It's worth noting that this knowledge is dynamic and subject to evolution. New and innovative financing mechanisms may emerge over time, shaping the landscape of entrepreneurial finance. Therefore, while the book provides a comprehensive overview of existing financing alternatives, readers should remain open to emerging trends and advancements in the field.

Harvesting or Turnaround
In Part 6 of the book, the focus shifts to a common yet critical area in entrepreneurial finance: the exit stage. As a successful venture reaches this stage, investors realize their returns and exit from the venture. At this juncture, entrepreneurs have the opportunity to consider various strategies, including converting the venture into a different business model or sustaining it as an established business entity. The authors delve into different harvest strategies in Chapter 16, which encompass private sales, asset transfers, buyouts, and initial public offerings (IPOs). Additionally, they explore the possibility of ventures undergoing a natural dissolution or systematic liquidation, highlighting the importance of understanding these aspects for entrepreneurs to make informed decisions at the harvesting stage. However, not all entrepreneurial ventures follow a smooth trajectory. Some may encounter financial distress before reaching a successful conclusion. Chapter 16 further addresses this scenario by presenting different turnaround strategies, accompanied by practical examples. This equips entrepreneurs with the knowledge and tools needed to navigate challenging situations and steer their ventures toward success.

Following each chapter, the authors provide a comprehensive array of resources designed to facilitate self-learning and self-study. These resources encompass discussion questions, internet activities, advanced exercises, and mini-cases. Additionally, an instructor manual is included to support independent learning, offering answers to all chapter-end questions. This holistic approach establishes the book as a complete educational tool for gaining expertise in entrepreneurial finance. Furthermore, the authors consistently update and refine the book to incorporate the latest knowledge and insights in the field. This continuous improvement process ensures that the content remains current and reflective of ongoing developments.

Each new edition introduces pedagogical enhancements based on feedback from previous editions, ensuring that readers are kept informed about any changes or improvements made. This iterative approach enhances the book's effectiveness as a valuable resource for learning about entrepreneurial finance. However, there is room for improvement in the emphasis on economic theories, concepts, and insights related to the entrepreneurial venture cycle. As seen in many other entrepreneurial finance books, the application of finance and economics principles to ventures led by entrepreneurs, with a focus on value creation, is essential (Alhabeeb, 2015).
CONCLUSION

Based on the aforementioned points, "Entrepreneurial Finance" by Leach and Melicher undoubtedly emerges as the preeminent text in the realm of entrepreneurial finance. Its comprehensive coverage enables readers to gain mastery over the entire life cycle of an entrepreneurial venture. Notably, the book stands out as a leader in its field, with few discernible weaknesses detracting from its authority. Highly recommended for a wide spectrum of readers, from novice entrepreneurs to seasoned financial managers in established firms, "Entrepreneurial Finance" serves as an invaluable resource for acquiring knowledge in this dynamic field.

Its relevance extends to undergraduate and master's students seeking to deepen their understanding of entrepreneurial finance, offering self-guided learning opportunities to grasp complex concepts and their practical applications. One of the book's strengths lies in its supplementary materials, including a meticulously crafted instructor manual and comprehensive answers to questions, facilitating effective self-learning among students. This aspect elevates the book's utility, allowing it to function as a virtual teacher in the journey toward mastering entrepreneurial finance.

REFERENCES