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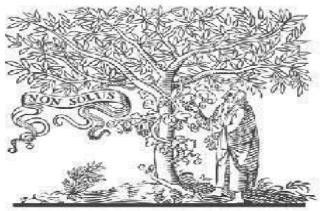

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Paper Authors: **Dr.D.Praveena devi, Dr.S.Geetha**

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Importance of financial structure for startups

Dr.D.Praveena devi, Assistant Professor, Management Studies, Koneru Lakshmaiah Educatio Foundation (Deemed to beUniversity) Guntur, Andhra Pradesh, raveenadevid86@kluniversity.in
Dr.S.Geetha , Assistance Professor, Department of Commerce, Mannar Thirumalai Naicker College, Madurai. geetharaja20@gmail.com

Abstract

In this article financial structure for startups has been examined that helps to understand the characteristics of the assets included in the startup as well provide relevant information related to the startup. The article also discusses the attributes related to the financial structure of the startup. Higher liquidation values of the physical assets support the startup that allows the entrepreneurs to employ external loans in their financial structure. Higher asset specificity and lower collateral value allow the startups to use human capital as intellectual property assets to use as finance. The small, solo, first-time, unincorporated, and home office-based are the various characteristics of the startups which are financed by self, family, or friends. The startup also uses external sources as financial support to control the other attributes of the startup. Start-ups of men as well as women are of the same time and don't differ from the other startups.

Keywords: financial structure, assets, startups, external loans, and bank

Introduction

The financial structure of the startup has been little known as most of the articles provide information regarding the financial structure of the startup. Startups have a major contribution to the economy of the country. It is quite difficult to determine during the financial crisis period whether credit conditions have a benchmark assessment of the financial structure of the startup (Szarek and Piwcuch 2018). Kauffman Firm survey has been done to understand the financial structure of the startups. In the Kaufman]a Firm survey it has been found that less than 25 employees are present in 98 percent of the firms. In the article, the startup has been investigated which is newly started in the year 2021. Details present on these firms are impressive that involve detailed data on the business sector activity, entrepreneur, financial structure as well as location (Almahirah et al., 2021).

The startup that uses physical assets in a large amount is the startup where the owner has other businesses and has external debt in the financial startup. Debt is less likely to be used by businesses with greater human capital embodied in the entrepreneur or more intellectual property assets. The most opaque firms are those that operate out of the entrepreneur's house, where credit card debt dominates their financial structure (Kozubikova et al. 2019). Internal and external equity is more common in team-run firms and those with serial entrepreneurs than in other startups. Due to owner characteristics, older and better-educated entrepreneurs are more likely to employ debt financing, whereas African-American entrepreneurs are more likely to finance their enterprises with their resources. When other aspects of the startup are taken into account, the financial structure of female-owned startups is comparable to male-owned startups (Kumar, 2022).

Startups' financial structure is influenced by regional considerations and local situations.

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Internal debt is more likely to be used to fund businesses in areas where residents are better educated (Durda and Kjucnikov 2019). The likelihood of external ownership in a startup's financial structure is higher in innovative states and states with stronger venture capital (VC) activity. Bank loans are more likely to be included in the financial structure of startups in larger states at the start. There are substantial differences in the financial structures of hi-tech firms and businesses in other industries. Some of the most significant inequalities may be traced back to the relationship between financial structure and race, citizenship, and business knowledge (for example, having related enterprises in the same industry (Sehgal; et al., 2018). The financial structure of a company is critical to its business strategy and has significant ramifications for how the company operates.

Materials and methods

Kauffman Firm Survey has been done to gather the primary data from a year-to-year panel of about 4500 businesses. The unique identification number is provided to every business. More than 1300 questions were asked to each organization including detailed questions on the financial structure, innovation activity, and location characteristics (Bednar et al. 2018). All the firms during the startup period have been investigated in this study to know the financial structure during that period. In this study franchise firms and not purchase startups have been excluded; only true startups have been chosen. In the given table 1 summary statistics for the year, 2021 sample have been shown. From the table, it has been shown that 62 percent of financing inception is internal equity for the average startup. 28 percent of the startup take external plans whereas the rest of the entrepreneurs take loans from family and friends and external equity financing (Kumar, 2022).

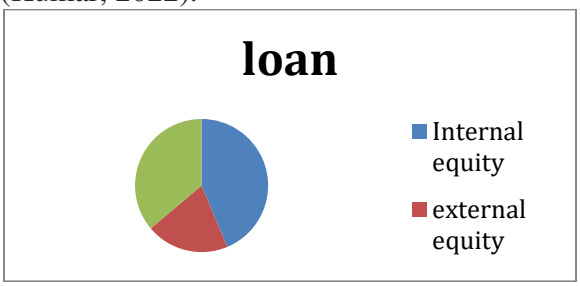

Figure 1: Financial inception (Source: Roland et al., 2021)

A deeper investigation regarding the financial structure has been done through the KFS. The higher the opacity of information in a company, the higher the share of internal finance, followed by external debt such as bank financing, and finally external equity. Three information opacity metrics have been developed: whether the company operates from a home office, if it is managed by a team, and if it was founded by a serial entrepreneur (Giraudo et al. 2019). The higher the asset specificity in a business, the larger the share of internal finance, which is followed by external equity (equity from angels/venture capitalists) and then external debt. Industry experience, business knowledge, tangible assets, R&D personnel, and intellectual property are the various measures to specify the asserts for both tangible, intangible, and human capital. The concentration of startups varies a lot depending on the state and the industry (Kakti et al., 2021).

Result and Discussion

The study employed a multinomial logit model to look at how asset specificity, information opacity, and entrepreneur and startup traits are related to financial structure. The main study of the KFS financial structure took into account a four-way multinomial option of financial source

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In the given below table, the multinomial logic model has been shown to investigate the financial structures which are common

to startups. Internal equity is considered as the base type of finance.

Base: Internal Equity	Internal Debt	Ext
Assets		
Business Knowledge	0.056***	0.0
Industry Experience	-0.006	-1.5
Share of R&D	-0.032	-0.0
Personnel		
Information Opacity		
Serial Entrepreneur	-0.032	-0.0
Team Run Business	-1.000**	-0.3
Dummy	-0.960**	0.0
Home Office Dummy		
Owner Attributes		
Black Primary owner	-0.143	-0.8
Dummy	-0.157	0.025
Age of Primary	-0.031	-0.0
Owner	-0.129	0.2
Education Level	-0.490	0.0
Dummy		

Table 1: Financial strcutre_ for way of startup
(Source: created by author)

Along with our primary variables of interest on assets, information opacity, and owner and venture characteristics, we incorporate controls from the state and industry (2-digit NAICS). The raw coefficients are shown in the tables, and the odds ratios based on the relevant tables are shown in the discussion following (Berggren et al. 2019). When it comes to asset specificity metrics, we find that having more tangible assets increases the likelihood that the firm would have both internal and external debt. This is in line with the fact that these assets have a higher liquidation value, making them better as collateral for external loans or borrowing from friends and family. The likelihood of using both internal and external loans decreases as the entrepreneur's industry experience (as specific human capital) grows.

This reduced likelihood of loan use corresponds to lenders' concerns that the entrepreneur would default on the startup's financing obligations (Sehgal et al., 2022). This reduced likelihood of loan use corresponds to lenders' concerns that the entrepreneur would default on the startup's financing obligations. Startup finance is also influenced by the features of the company. We discovered that new business initiatives with more physical assets and business experience are more likely to receive external financial financing (Schuckes and Gutmann 2021). Startups with more human capital embodied in the entrepreneur are less likely to use loans, which is consistent with its low collateral value.717

Discrete Variables	0.0	Obs.	Ones
Four choices	0.5	4200	1075
Internal equity	-0.6	4200	125
Internal debt		4200	2940
External debt		4201	55
External; equity		4201	1069

Table 2: Summary statistics for dependent variables
(Source: created by author)

Startups run by a team are less likely to need debt financing and, as a result of their higher knowledge, are more likely to have outside equity. Startups based in the entrepreneur's house are less likely to borrow money from friends and family and, as a result of their lack of transparency, are less likely to have external ownership in their financial structure. The KFS demonstrates the diverse range of funding options available to entrepreneurs. Table 2 shows that team company was less likely than other firms to have debt in their financial structure.

Conclusion

Startups are more prone than large established organizations or even tiny ongoing firms to suffer from greater information opacity and asset specificity. The existence of human capital-specific assets, along with low levels of traditional tangible assets, is critical for startups. In the financial structure of startups, we might anticipate greater total reliance on internal sources of money. Because a startup's finances may be limited, the entrepreneur will look for ways to supplement his or her resources.

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