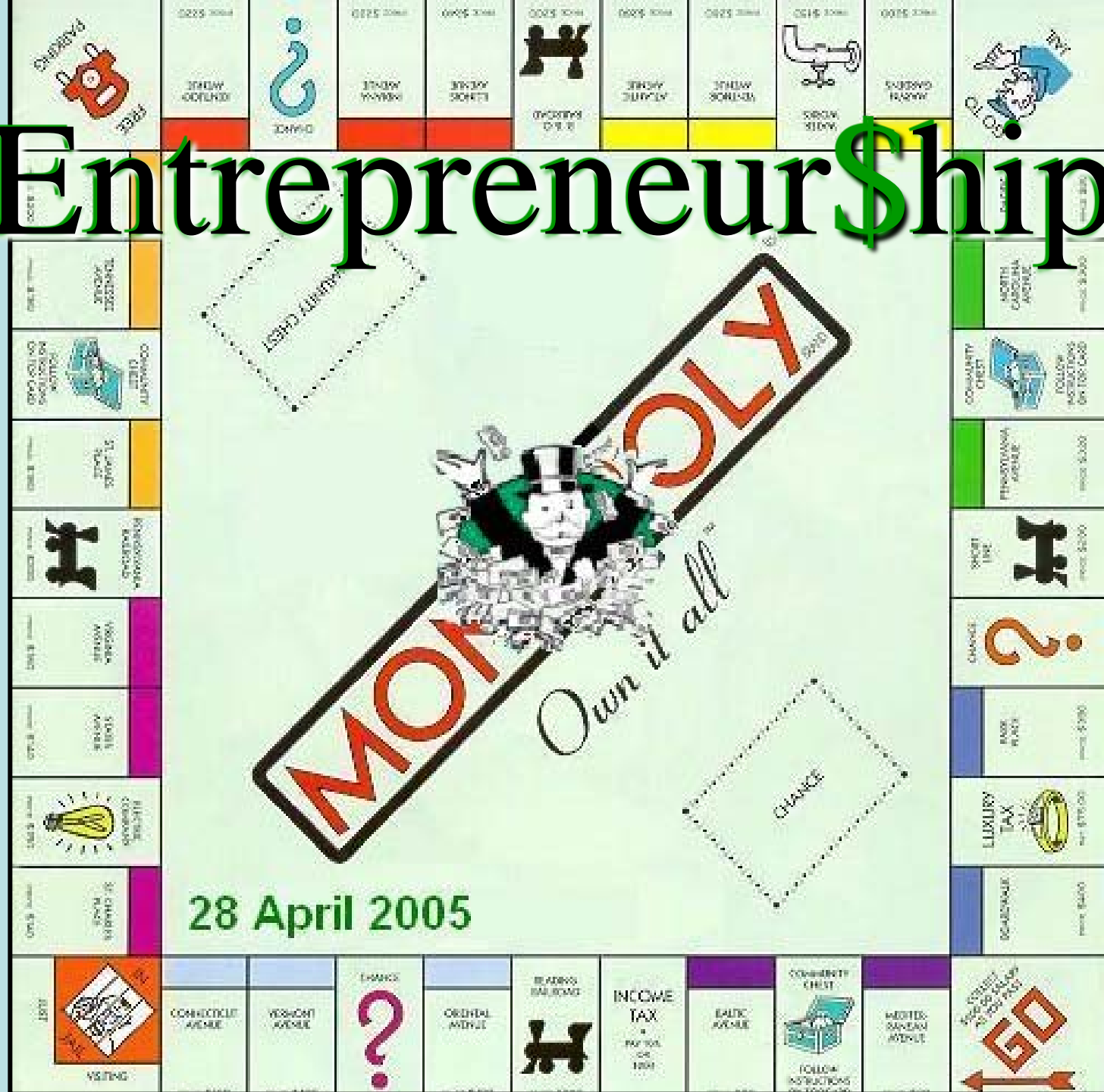


# Entrepreneur\$hip



# Recent Business Cases

- **Bay Collection**
  - Boutique Retail
- **Codonix**
  - Medical Software
- **Signal International**
  - Heavy Marine Manufacturing

# ENTREPRENEURSHIP

*...so you want to own or run a business!*

- Are you a risk taker?
- Are you prepared for hard work and long hours?
- Do you have a high threshold for rejection?
- Do you have fundamental management / leadership skills?
- Do you have a sales orientation?
- Do you possess a vision/passion for
  - starting a new business?
  - buying and growing an existing business?

# Small-to-Middle Market Business

- 2000 U.S. census tallied >25 million businesses
  - 80% closely held companies
  - \$3 trillion in revenue
  - 90% of companies are privately owned
    - Sole proprietorships
    - Partnerships
    - LLCs
  - Family firms 90%-95%
  - 63% lack a written strategic / business plan
  - 40% of all family-owners are exiting in next 5 years
  - \$4.9 trillion transfers of net worth

## Sources:

2000 Census (Washington, D.C.:U.S. Census Bureau)

Russ Alan Prince and Karen Maru File, "Marketing to Family Business Owners"

"American Family Business Survey," Mass Mutual Financial Group

Robert W. Walter, *Financing Your Small Business*, 2004

J. Fred Weston and Samuel C. Weaver, *Mergers & Acquisitions* (New York:McGraw-Hill, 2001)

John Leslie Livingston and Theodore Grossman, *The Portable MBA in Finance and Accounting*, 3<sup>rd</sup> Edition (New York:John Wiley & Sons, 2002)

*OPPORTUNIT*  
*Y!*

# The Value Path

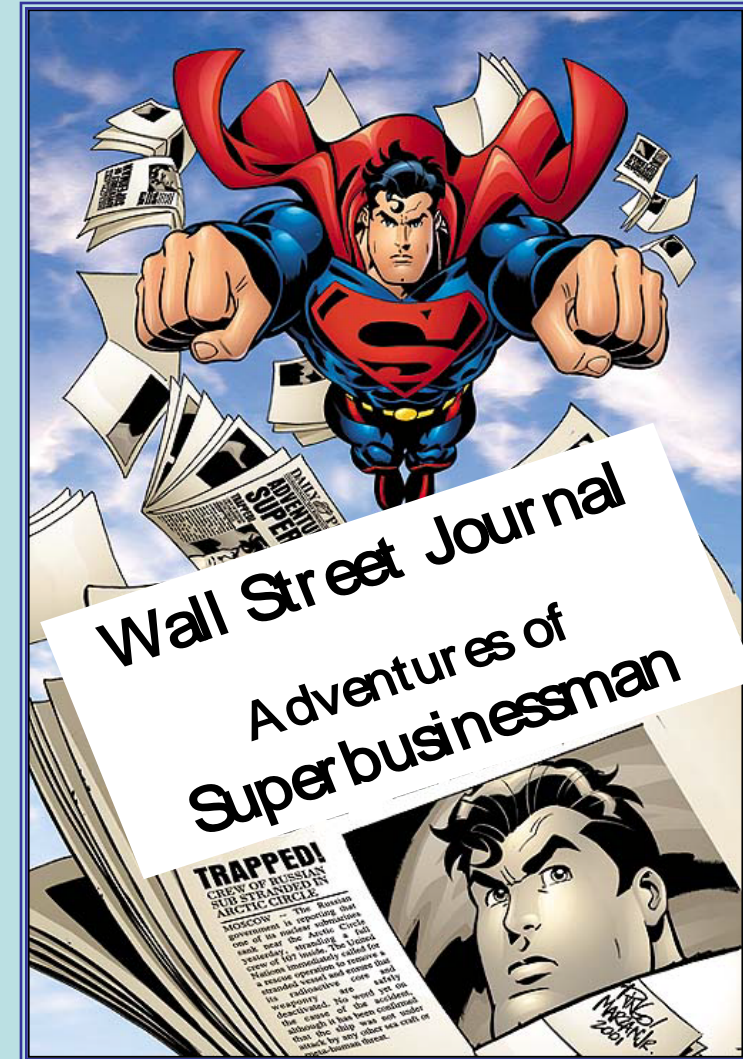
...Typical Events and Needs



# ***Raising Capital***

*... the Greatest Challenge*

- Business Plan
- Management Team “skill and skin in the game”
- Risk Drives Type Lender



# Debt versus Equity

## **Advantages of Debt over Equity:**

- No dilution of founder's stock.
- Loan repayment, plus interest.
- No claim on future earnings.
- Interest is tax-deductible.
- Principal and interest payments are predictable.

## **Disadvantages of Debt:**

- Limits to what a business can carry.
- The larger the debt-to-equity ratio, the riskier.
- Drain on cash flow for payments.
- Debt is not permanent capital; must be repaid.
- Interest expense and restrictive covenants limit flexibility.



# Raising Capital throughout the Value Path Stages

## Objectives

## Source of Equity

## Debt Financing Sources

### *Early Stage*

- Raise capital for R & D
- Create infrastructure
- Limit dilution of founders

- Founders, friends, family
- Angel investor
- Venture capital firms
- Private equity groups

- Promissory notes
- SBA loans
- Equipment leases

### *Growth Stage*

- Fund strategic plans for expansion
- Increase infrastructure

- All early-stage sources plus:
  - Private placements
  - Institutional investors
  - Initial public offering

- Banks
- Institutional investors
- Private equity groups
- Equipment vendors & leasing firms

### *Late Stage*

- Exit options including:
  - M&A opportunities
  - Public offerings
  - Sale of business
  - Stock redemptions
  - Leveraged recaps

- Public offerings
- Private equity groups
- Strategic partners

- Banks
- Institutional investors
- Equipment vendors and leasing firms

# Sources of Equity or Debt

- Founders, Friends, Family
- Banks
  - Collateral
  - Collateral
  - Collateral
- Angel Investors
  - High-net-worth individuals
  - Want high returns
  - Typically \$100-\$400k plus stock options
  - Knows/experience in business space
  - Some management participation

# Sources of Equity or Debt

- Venture Capital
  - Large cash investors
  - Alternative to banks
  - \$\$\$ from pension funds / insurance companies / wealthy individuals
  - Generally favor specific industries
  - Investment range \$250k-\$50M
  - 20% - 40% annual returns
  - Equity position
  - Board seats / control
  - 5 to 7 years exit

# Sources of Equity or Debt

- Private Equity Groups
  - Pools of capital like VCs
  - Rarely fund early stage
  - Favor growth – and late – stage businesses for “mezzanine” financing
  - **Strong cash flow orientation**
  - Management led buyouts and “recaps”
  - 20%+ annual returns
  - 3 to 5 years exit

# Private Placements-Debt and Equity

Questions to consider include:

- Cash flow
- Is the company enjoying strong growth?
- Does the company wish to raise capital to support such growth?
- Does the company need to finance an acquisition?
- Is capitalization a possibility? Does the owner seek liquidity, but not a total sale of business?
- Does the size of the offering make the public markets unsuitable?



# Exit Planning

## **...A Process, Not A One Time Event**

- Determine goals / priorities
  - Continue to grow.
  - Get out.
  - Is the business ready to be sold or transferred?
  - Are steps necessary to cure weaknesses or enhance values?



**“Owners or Investors  
Should Be Prepared To  
Sell, Acquire, or Merge  
At Any Time”**





# Sale, Acquisition or Merger

## ...Recognizing Opportunities

Questions to consider include:

- Is the founder considering retirement?
- Is family/management succession questionable?
- Is the owner concerned about concentration of personal wealth tied up in business; does he desire diversification of his assets?
- Is the owner concerned by the need to reinvest capital to stay competitive?
- Do shareholders desire liquidity?
- Does the company have a division that does not fit its long-term strategies?
- Has the company been approached by a potential buyer?
- Will the company seek to accelerate growth through acquisition?

# Business Valuation

... What Is It Worth?

- **Market Approach**
  - Recent Sale
- **Income Method**
  - EBITDA Multiples
- **Discounted Cash Flow Analysis**
- **Professional Appraisal**

# Why Sell A Business?

- **Capital Gap**
  - Too big to be small.
  - Too small to be big.
  - Risky growth considerations.
  - Unable to obtain capital.
- **Value Maximized (for now)**
- **Time to Retire and “Enjoy Life”**
- **Boredom or Burnout**

# Management Buyout (MBO)

## ...Senior Management Participates

Questions to consider include:

- Does an internal or external management team want to buy a company or a division of a company?
- Does an internal management team want to acquire or substantially increase an equity position?
- Does a minority shareholder(s) desire to buy out a majority (older, retiring) shareholder?

# Initial Public Offering (IPO)

## ...Going from Private to Public

- Public stock sale
- Must be middle-to-large private business
- Financing tool for growth rather than exit
- Owner(s) can take some “chips of the table”
- Real payoff downstream
- Stock options can attract/reward top talent

# IPO Decision

Questions to consider include:

- Is the company enjoying rapid growth? What is the outlook?
- Do the owners require immediate liquidity?
- Does the company have compelling products or services with proven markets?
- Does the company have a strong management team that understands stockholder obligations?
- Does the company have recognized backers (e.g., well-known venture capital investors)?
- Would being public enhance the company's position with customers and employees?

# Company Growth

## **...Through Acquisition(s)**

- Market expansion
- New capabilities and managerial skills
- Competitive advantages
- Development of new customer relationships
- Greater technology and R&D capabilities
- Industry rollups, i.e. consolidating fragmented industries
- Prevention of competitor from acquiring target company
- Globalization

# Other Transaction Paths

- Employee stock ownership plan (ESOP)
- Joint Ventures
- Strategic Alliances
- Restructuring



# Summary

- Opportunities abound
- Know what you know
- Be tenacious...take risks
- Grow, acquire, build...the same skill set / process
- Do not be intimidated by financial engineering - learn and use as tools

Carpe  
Diem!

