

the way forward?

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Here be dragons – a brief guide to 'Private Equity'

We have been involved in a number of projects where clients have benefited from private equity funding. The potential benefits to the investee company are the flexibility of the funding package on offer and the additional skills brought to the business by the investor.

Also, an increasing number of early stage businesses are seen as 'equity propositions' by the banks and therefore we see private equity as forming part of the initial finance package.

This fact sheet aims to explain what is meant by 'private equity' and to outline the mindset that must be adopted for an equity investment to 'work' for an Owner/ Manager.

So, what is 'Private Equity'?

According to the British Venture Capital Association, private equity is: "medium- to long-term finance provided in return for an equity stake in potentially high-growth unquoted companies".

For instance, let's consider a company which is 100% owned by Owner / Manager. He or she has begun to build a strong business based on a well thought out business plan but is lacking the necessary finance to develop.

Perhaps there are no assets on which to secure traditional debt or possibly early-stage cash flow will not support loan repayments; instead, a private equity provider is approached to invest in the business (i.e. to buy shares).

This should be familiar to those who watch "Dragon's Den" - as should the concept that equity providers not only contribute money to the business but also bring with them business expertise.

business expertise

"equity providers not only contribute money to the business but also bring with them business expertise."

Is Private Equity for you?

The prospect of "losing" some control over your business is against most people's instincts. So when might private equity be the way forward?

The following table shows some examples of situations where we have seen a need for equity finance, along with a summary of the key requirements for successful equity fundraising:

	Issues with debt finance	Requirements
Start-up	Absence of security and cash-flow issues	1. A clear, considered strategy. 2. A strong management team. 3. Contacts within the field of equity finance. 4. A viable "exit-route", i.e. a way out for funders in 3-7 years. 5. A robust, detailed business case.
Expansion	Need to reinvest profits into growth as opposed to servicing debt	
Turnaround	Security and cash-flow issues	

streamline the process

"We're here to try and ensure that the process is as painless as possible and our working with other professionals to streamline the process and reduce costs."

Mindset. And the cake analogy...

Before considering equity investment seriously, the current Owner/ Manager should have reconciled:

- the need for equity i.e., that equity is the 'right' finance for the business's development plans;
- the fact that in exchange for the finance invested they will be selling part of their company to a third party; and,
- that someone investing in its future prospects of the company will want to look over the business and will also be keen to build in some 'say' in the operation of company going forward.

Whilst the above can combine into some highly emotive discussions, the analogy which should underpin the decision making process of the current owner/ manager if equity is required for the company to deliver its potential is:

- is it better to have 100% of a small cake OR a lesser percentage of a much bigger cake?

Sources of Private Equity in Cornwall

In recent years, the most active sources of private equity funding in Cornwall and Devon have been:

- Business Angels (high-wealth "sophisticated investors"), including networks operated by SWAIN; and,
- regional Private Equity firms - including Finance Cornwall, South West Ventures and Finance South West.

Whilst, Finance Cornwall and Finance South West are currently closed for new investments, we have seen an increase in interest in the region from fund managers of national over the recent years. The national funds tend to be sector specific.

How can we help?

Successfully obtaining private equity funding can be a time-consuming procedure compared with, say, arranging a loan. We're here to try and ensure that the process is as painless as possible and we are working with other professionals to streamline the process and reduce costs.

We can support you in preparing your business plan, including the construction of detailed financial models and preparing an indicative value for your business. We can also help with initial identification of possible equity providers, subsequent negotiations and, together with your corporate solicitor, getting your business investment ready including:

- tax planning / business structuring; and,
- preparation for due diligence.

And, to identify potential 'deal breakers'.

What next?

Private equity isn't for everyone, but if you've read this fact sheet and thought that it may be relevant to you then where do you go from here? If you believe you have:

- a high-growth business with a viable exit route for an equity provider within 3-7 years; and,
- business objectives that will align well with those of the funder,

then contact us or your corporate solicitor to discuss the matter further.

If you would like to discuss any issues raised in this guidance note, please contact:

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