

Raising Venture Capital



NEWPORT CAPITAL

Newport Capital Group Pty. Limited

Venture Capital basically is money raised from financial investors who make money available to assist unlisted companies grow and develop. It is provided usually on a medium term, unsecured basis as risk sharing equity capital by Venture Capital companies for the purpose of increasing a company's value to its owners, without the venture capital company necessarily taking control of the business.

Lenders to business such as Banks, have a legal right to interest on a loan and to the repayment of a loan, irrespective of the success or failure of the borrower. However in the case of a Venture Capital investment, the investor's returns are entirely dependent on the growth and profitability of the business.

In seeking a Venture Capital investment, owners and shareholders of the company will need to sell some of their shares in the company to the venture investor, who will probably also seek a non-executive Board position and attend monthly Board meetings.

A good venture capital investor does not only provide equity capital. They should also be able to provide experience, advice and contacts. In this way, Venture Capital investors seek to set themselves apart from other providers of capital.

Raising Venture Capital

Raising Venture Capital is one of the most traumatic experiences that most entrepreneurs will ever undergo. It involves much preparatory work and exposing the company to a frustrating and exhaustive process during which the company itself will need to be exposed to strangers. Before contemplating raising Venture Capital, NCG recommends that you consider the following questions;

- Do you have high growth ambitions for your company ?
- Are you willing to sell some of your company's shares to a Venture Capital investor in order to be able to increase the value of your own equity over a period of years ?

If the answer is basically yes, then it is definitely worth considering Venture Capital. Firms which provide this type of capital only target companies with real growth prospects, and even then only those companies that are driven by a skilled, ambi-

tious management team, so it is important to feel personally comfortable with this.

How to Prepare Yourself

Venture Capital investors have a wide range of investment preferences, which include the actual amount of capital required, your company's investment stage, the industry sector, the location of your company etc. All of these factors must be taken into account when selecting the right potential investors to approach. Investment stages include seed capital, start-up, expansion and other stages such as management buy-in, management buy-out and rescue/turnaround situations.

Raising any capital needs proper research and strategic targeting. Before approaching any source of venture capital, you will need to have:

- a good business plan, based on a sound business model and carefully reasoned assumptions
- made certain that you are mentally sure that raising venture capital is the right thing to do
- know how much money you require and what it will be used for
- selected those Venture Capital sources that match your needs and requirements.

NCG can assist you with all the necessary preparation and with the actual negotiations. We can assist with;

- strategic business reviews to identify all relevant issues
- management reviews
- preparation of a Business Plan
- financial needs analysis
- preparation of a suitable Information Memorandum

Most submissions for Venture financing are rejected and therefore to be successful, your presentation has to stand out from the crowd. Through careful analysis of your business and its' financial needs, NCG can help you maximize your chances of success.

NCG also maintains contact with a number of major Venture Capital firms and can introduce you to those most likely to match your company's needs.

The Business Plan

NCG believes that the key to the successful raising of Venture Capital is the preparation of a structured business plan, based on a realistic review of the company and its needs. We recommend that the following format be used.

1. The Executive Summary

This section should be a mini plan or one page summary of the essential facts and should be capable of being used as a stand-alone document. Some potential investors will read this page first and not proceed with the rest of the document this section is not convincing.

2. Background to the Plan

This section should be 1 - 5 pages only, giving an overview of the origins of the product, identification of the business opportunity, reasons why there is a market need for the product.

3. Product Description

What it is? What it does? Why is it useful? Where does it "fit"? Why is it better than its competitors? Are there any proprietary features? Are there any "family of product" implications? What are the benefits to customers? Why is the company successful?

This is the section where the glamour needs to be. Illustrations and/or diagrams are very useful here.

4. The Market

In this section the market should be defined and documented evidence provided as to market size, growth, trends, pricing, need for the product etc. This section should also identify names of customers, prospects etc. All assumptions used should be clearly stated. This section should also clearly show that you understand the competitive environment in which you operate.

Present as much information as possible graphically. Where possible, include





corroborating opinions of industry leaders, prestigious consulting firms such as Gartner, IDC etc. as well as trade associations, government agencies etc. Include back up statistics and a market segmentation analysis. Show that you understand who is the market leader and what share of the available potential market you are aiming to capture.

5. Marketing Strategy

Describe the distribution strategy, sales cycle, sales channels available, sales costs, unique promotional, delivery or other features of the strategy. If possible, demonstrate some grasp of the costs of marketing.

6. Operations Plan

How is the product "produced"? Describe what training courses, materials etc. exist and what support facilities are offered to customers. Describe key business partner relationships and how these relationships are/will be managed.

This section can be fairly light as most investors will tend to assume that you can at least produce what you say you can.

7. Research and Development Plan

State the objectives, costs and time schedules for R & D. Stress the "D" part - investors generally hate paying for the "R" part.

8. Ownership

Describe the ownership of the technology and the company as it is before financing. Describe any commitments or factors which might affect the value of the product or the business.

9. The Executive Team

Identify all members of the executive team and describe their qualifications. Identify why the team will function as a team. Include an organization chart and identify the Directors.

Make it convincing as some potential investors will turn here first.

10. Staffing Plan

Briefly outline what additional resources are needed in the short to medium term, identifying skills needed together with availability and cost. Be brief. Investors are usually willing to

assume that the right people can be hired.

11. Financial Strategy

This is the core of the Business Plan. It is necessary to show what cash is needed and when. Also, for what purposes? Short term and long term needs should be identified with a rationale for each. A twelve month cash flow forecast should be prepared and presented graphically as well as numerically.

It is important to demonstrate an understanding of cash flow. Pro forma financial statements showing the best and worst case scenarios should be prepared. It is important to be intellectually honest here.

In preparation of these documents, the pro forma Profit and Loss Statement based on "best case" sales projections is the starting point. Developing this into a cash flow projection will reveal the amount of cash theoretically needed at each stage of the company's future growth. You will however note that a little "what if" analysis of your model will demonstrate how treacherous such predictions can be as the future cash balance projection is unbelievably sensitive to minor variations in factors such as assumed growth rate, product cost, overheads, collections and billing cycles. If you attempt to develop meaningful best/worst cases from this sort of analysis, the results are often mind blowing. Also if you try and vary every factor at the same time, your projected cash requirements can suddenly assume the proportions of the national debt!

The most sensible way of tackling this task is to have an "expected", a "worst case" and a "best case" sales forecast and work out the cash consequences of each, *assuming other assumptions are constant.*

As an aside, you should realize just how rubbery these cash projections are and don't start believing them too much yourself!

12. Contingency Plan

Outline a general plan for dealing with the three most likely crises that might arise. Do not show much detail, just demonstrate that you have thought it through.

13. Concluding Summary

Identify what are the benefits to the investor, identify the major risk factors. Should be limited to one page and show how the

risks will be minimized. Show why this is a desirable investment relative to other opportunities that the investor has available.

Concluding Notes

- Documentary overkill causes as many problems as under kill.
- Remember that those who will read the plan are people, not information processing machines.
- The purpose of the Plan is to arouse interest, not to fully inform readers on every aspect of the business.
- Keep the Plan readable. Don't make it so inter-locking that every preceding page must have been read before the present page makes sense.
- Make the Plan visually attractive. Set it out in a pleasing print font and if possible, use color printing for diagrams and charts etc.

Above all, always keep in mind a picture of a very busy person with 8 other business plans on his desk and phones constantly ringing. He doesn't need minute detail. He needs a fast overview of what your business is about, and sufficient corroborating evidence to suggest that you know what you are talking about. Have the plan properly bound using spiral binding so that it will stay open on his desk. *Don't forget to say how much money is needed but don't spell out the deal. That will come later!*