Financing Growing Businesses

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Business Advisory Services

MEDEI/MRI

About Business Advisory Services

26 Senior business advisors in 11 offices across southern Ontario

Seasoned private sector business executives

Specializing in growth companies with 10 -500+ employees - IT, manufacturing, trading, consulting, biotech, export oriented – we do domestic expansion

Access to finance and operational advice, contacts, general business connections and government programs – we don’t charge anything

We play well with others such as SBEC’s, IRAP, BDC, RICs, CLA’s, EDC, Banks, angel investors, VC’s, factoring companies

Your client has been in business for a year, has generated sales and is gaining traction in the market. It is now time to scale up and pursue greater opportunities.

The issue: How are they going to find the money?

This session will discuss how to assist these companies source the financing required for growth and how to find their way to the right lender or investor. The content will include an outline of the opportunities and resources available to these companies and the requirements and risks they will face in their search for growth capital.

What is "Finance"

The <u>art</u> of getting money from other people to aid in your business or personal goals, aka

OPM (other people's money)

You can’t do finance without context

All this matters greatly

Size – Small companies don’t get the same choices as larger

Markets – Are you in a high or slow growth market?

Scalability – How much can you grow quickly?

Speed – Is management capable of fast growth

You can’t do finance without context

Leverage – will a small amount of money yield great results

Location – the right location for the kind of business

Who you are - contacts, board members, networks, skills, past exp.

Communication – can the owners articulate their story

Capability – does management have the correct skill set

You can’t do finance without context

Is the business generating a profit – if not, fix it – don’t be delusional

Who are the owners/leaders/team - How much have they invested

Are the owners psychologically ready for various types of finance

What is the business model – is it asset light or heavy – fast or slow growth – B2B, B2C, service, manufacturing, internet based, Platform dependent (mobile? - What are they selling, to whom, where, how)

You can’t do finance without context

Do the owners know and deeply understand their business model and business plan – do they have a credible accountant and financial statements

Where is the business located – can it expand/manpower/skills

How much traction has occurred - growth rate expectations/reality – What is the cash flow really like – is it seasonal

What is the money to be used for (Use of Funds) - How much is needed and what kind of money is appropriate for the company

First Sources - Internal (operational)

- Equity investment – self, friends and family
- Profits – nothing succeeds like profitable sales
- Vendor sources – machine manufacturers, raw material suppliers
- Extend payables – Pay wages monthly, take minimum salaries
- Collect fa**s**ter – take credit cards, adjust terms of sale
- Progress payments and down payments – for not-on-shelf items
- SR&ED filings – can be factored
- EDC insurance – protect foreign receivables
- Letters of Credit from overseas buyers – can be discounted

Nature of Debt Providers

Debt providers are not in the business of taking equity risk

Banking – still the same after all these years

Five C's of Credit:

Character – Business owners track record, guarantees
Collateral – Assets to lend/borrow against, guarantees
Conditions – When will borrowing occur and under what circumstances – (D/E, ratios, foreign receivables etc.), guarantees
Capacity/cash flow – can debts be repaid, guarantees
Capital/ your investment – how much skin in the game, guarantees

Working capital and fixed assets

What is to be financed:

Turnover in accounts receivable and inventory

Fixed Assets and Quasi-fixed such as machinery, including installation, royalties, real estate, leasehold improvements,

Who needs this kind of financing:

- Virtually every business - manufacturers, distributors, importers, service companies, IT companies with service contracts and sales

Who does this kind of lending?

All the Canadian banks – operating and term

Some credit unions – collateral mortgages against personal homes

Business Development Bank of Canada (BDC) - term

Export Development Corporation for foreign orders (EDC)

Banks and finance houses whose customers are vendors selling equipment

Some private funders – factors, Asset based lenders

Pre-production Equipment Finance

Financing to build customized machinery with a long construction time, typically with progress payments. Sales order for end products is far greater than normal annual sales. Not normal working capital situation.

EDC – for foreign sales

BDC – for domestic sales

Some Canadian banks

Banks for the customers for whom the product is being built

Factors/discounters

Some private lenders

Crowdsourcing – Indiegogo,

Kickstarter – presales to consumers

Revenue and IT Development lenders

Monetize future cash flow from maintenance fees and software sales

Discounting SR&ED refunds

Sub or mezzanine debt

Some US banks - Silicon Valley Bank

Some Canadian banks with specialist knowledge based lenders (RBC, TD)

Boutique lenders, BDC possibly combined with some angel or institutional “angel” investment, SOFII

Coming soon “Crowd lenders”

Foreign receivable financing

Receivables from foreign buyers

EDC – insurance and lines – guarantees to domestic banks to increase working capital operating lines

The Difference between Debt and Equity

Debt is sold on the basis of risk

The Difference between Debt and Equity

Equity is sold on the basis of greed

Angel Investment

Companies with a rapid growth trajectory – early revenue – need to break out in terms of marketing or other distribution

Likely candidates: IT, Biotech, advanced manufacturing, steady B2B companies with good cash flow that want to buy another company or establish subs in other countries

Promise of good returns over a relatively short period of time, 2-6 years

Conditions could be they stay in after subsequent capital raises – Looking for minimum 25 percent return per year

Often invest in groups for moral and effective board support – Maple Leaf angels, Georgian angels, York angels

Angel Investment

How much of the company do investors receive
What is the expected return on capital and when
What is the money to be used for
Who is going to sit on the board of directors
Who is going to run the company
What is the valuation formula and why
How is the investment to be made – lending, debtquity, equity

Venture Capital

Your company has invented/created/assembled something that is so “value added” that people/businesses all over the world want it – they may not need it – but it can be sold.

What is missing is significant capital to market it, distribute it or grow so you can be a major player and you are a visionary who can really tell a story but in the end, it’s the team that counts.

Various Canadian or international VC funds

Valuation is based on the future not the past

Many fund managers accumulate funds from private investors and aggregate. They make their names by funding some companies in the hope of a grand slam.

Venture Capital

How much of the company does the VC receive – as a starter rule of thumb money is worth 80 percent of the company

Are there follow-on rights

What is the expected return on capital and when – exit strategy

What is the money to be used for

Who is going to sit on the board of directors

Who is going to run the company

What is the valuation formula and why

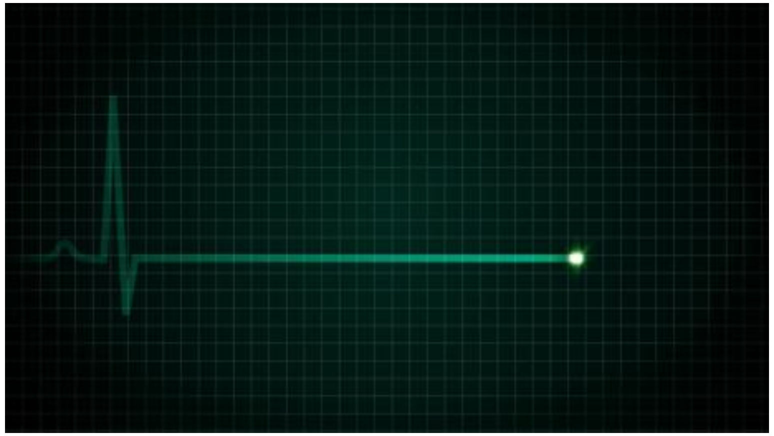
How is the investment to be made – lending, debtquity, equity

Nature of Equity Providers

Equity providers can take greater risks because:

- they look for a return of 20 – 35%
- they can make up a principal loss on the next “5 bagger”

Equity Providers



Equity investors want to buy growing companies not flatliners

Good Practices

- Keep your banker or financier in the loop – take him/her to lunch every 6 months
- Provide your reports A/R, Inventory, Monthly or quarterly financials on a very timely basis – don’t miss deadlines
- Provide a commentary on your financials or security listing
- Financings take place frequently – if you are growing submit projections of your needs well up front and negotiate line increases
- Don’t spend operating loan funds on fixed assets – get a term loan
- Provide a yearly update to your business plan
- Form an Advisory Board and let your financier know who they are

Who can’t get financing

Companies with a history of losses or has ongoing losses – next stop bankruptcy

Companies with withholding payments in arrears, Inc. Tax, EHT

Companies whose management is un-coachable/un-manageable or have previously been bankrupt

Companies which don’t have positive retained earnings and where owners are not willing to invest – keep cash in the business

Owners who don’t know how the company is to make money – often happens where the business plan has been written by a 3rd party.

Untrustworthy individuals

Government - Most Commonly Discussed Programs

Relative Complexity Scale

0 **5** **10**

Employees

Employment Services: new hire program

COJG (Canada Ontario Job Grant): use of external trainer

Notes:
- ✓ **Service Provider channel**
- ✓ **Caution: funds availability <u>within</u> channel**
- ✓ **Some confusion re: program and funds availability**

www.tcu.gov.on.ca/eng

Exporting

EMA (Export Market Access):exporting products and/or services to foreign markets

Notes:
- ✓ Must have a 3rd party reference
- ✓ Primarily manufactured in Ontario
- ✓ 10 – 500 employees, $ 500k+ revenues

OEF (Ontario Exporters Fund): Revenues, FTE, industry. More complex / less approvals

www.occ.ca

Equipment Investment

SMART: Advanced Technology (AT)

Notes:
- ✓ 1) Adv. Manu.project 2) export 3) job creation
- ✓ Incorporated for 2 or more years, 15-1,000 employees

www.cme-smart.ca

Transformative Investments

Jobs & Prosperity Fund (JPF): Min. $ 10 million in eligible costs

Notes:
- ✓ key sectors, including life sciences, advanced manufacturing and ICT

www.ontario.ca/business-and-economy/jobs-and-prosperity-fund

Potential Global Players

FedDev – IBGP (Investing in Business & Productivity): established businesses with innovative and unique opportunities to accelerate growth and support job creation

Notes:
- ✓ 15 – 1,000 employees
- ✓ Process: 1) Statement of Interest 2) Full Application

http://www.feddevontario.gc.ca/eic/site/723.nsf/eng/h_01867.html

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