



A long hard look

Investment-ready companies will be the winners from the current recession. How well do you measure up?

One of the effects of the recession is that the natural process of elimination, Darwin's survival of the fittest, is accelerated. Those that adapt and grow will survive. The rest will die quickly or, worse still, suffer slowly and painfully.

The business landscape is going to rapidly divide between the fit, the floundering and the dead. As the recession develops it's clear there will be winners and losers. Too many businesses struggle to grow and wonder why they struggle to attain critical mass or simply die.

Savvy investors always benefit in times of recession. Most of them have already weathered downturns. What is it that they look for in businesses and how do you become one of their investment rock stars? In this article we look at how to use the thought processes of investors to re-access your business. There are simple measures investors use to assess long term winners.

As business owners, you are also investors in your own business: Never has there been a better time to revisit your business model and assess whether you have an investable (read viable) business or not. It may well be time to adapt and modify your business plan, and perhaps even gain additional investment in your business to take it from strength to strength.

Great businesses are still receiving investment even in the current economic climate. At the very least, work out whether your venture is worth your continued investment of time, money and passion. Use the investor thought process to re-access your business.

My recommendation is that, if you cannot present a valid investment case for a stranger to invest in your business, then you need to rethink your business strategy or perhaps even abandon ship.

Do you measure up?

If a business has sustainable growth and can make money, then it's investable. But don't be fooled by your own BS, get someone not involved in the daily operation of your business to help assess your fitness to succeed. Your "investment pitch" is simply the answers to six questions:

- Do you add quantifiable value to your customers?
- Is there is an identifiable large market?
- Do you have a competitive advantage?
- Do you make money?
- Do you have a team that can deliver?
- Is there an acceptable return for shareholder investment?

Real, quantifiable value

Nothing guarantees long term success like an ability to make a measurable difference to your clients.

Give your customers a good reason to try a new solution or service; never before have they been more open to new solutions that will add bottom line value to their business. Companies that can quantify and use client examples of value add stand out from the pack and have lower cost of sales. The key here is proven measurable differences to your customers as a result of purchasing your product or service.

Maximum points if a client will quantify and endorse the value you add to their business.

Action list

Ask your best customers why they buy from you and what impact you have on their business. Look for large percentage change in some business metric.

Get your advisory group to challenge your business pitch.

Make your next hire someone who will increase the efficiency of the company.

Review your financial forecasts and analyse what is the best use of your company resources both from a short term and long term point of view.

Explore new finance options for growth.

Market or opportunity?

Often businesses get sidetracked on one-off opportunities that provide good short-term results but are not repeatable or scalable. Can your business profits grow to be 10, 100 or 1000 times bigger than what they are now? Can you describe and quantify your market and your potential market share? What have you done to validate your market? Do you have a realistic way to reach that market? Look for partners who may already have access to your customers and can use your product to complement theirs. A bottom up analysis of target customers and sales is more powerful than a bland percentage of a known market.

Maximum points again if you have a proven track record of revenue and profit growth.

Competitive advantage?

Too often entrepreneurs convince themselves they have no competition. This is usually a sign of no market or need, alternative solutions or complete denial. At very least the clients have the choice of doing nothing, which in many cases *is* the competition.

Likewise, there needs to be a barrier stopping your competitors – current or future – from taking your market from you. This does not necessarily have to be protected through intellectual property (patents etc). It could be rapid product innovation, community ownership (for example web companies) or even brand.

Top score if you know who your competitors are and how you differentiate yourselves against them. Check your competitors' websites – if they use it in their sales pitch it's not a differentiator for you.

Making money

Do you talk about your business in terms of financial metrics or product features?

Investors are just as interested in

how the business makes money as they are about your product or service. Make sure you are as well.

Profit is the lifeblood of all businesses. Without it, you may have a hobby. Understanding where and how you make money is crucial to the sustainable success of the business. It is amazing how many business owners focus on cost cutting versus revenue growth or profitability to overcome the tough times. Every successful business has effective means for measuring and controlling the flow of money in an organisation.

Do you know what the most profitable parts of your business are and more importantly how you will leverage this in the future?

Do you have procedures and processes in place to protect all elements of your balance sheet? High on the investable scale are businesses that can present a clear description of their business based on financial results and performance as well as product-based story.

If you do not have enough cash and committed orders to last the next six months you are a floundering business rather than a fit and agile one. Floundering businesses don't get invested in!

People to deliver

Sustainable businesses need effective teams to govern, lead and operate them. Adaptability only comes from effective people, not business plans or process. One of the best practices and least used is to make every new hire one that will increase the average intelligence of the company. Human capital is one of the most talked about and least invested in assets of companies. Dead wood, negative or obstructive people will kill an organisation.

From an investment perspective, risk is removed from a company that has great people who work together as a team and have been there before. Do not forget your advisory board. If

the people around you are not the best you can afford then change them.

Shareholder returns

There are endless investment choices. As many have recently found, high risk investments do not always pay off. As Investors need to ensure they have high enough returns to warrant the risk. Most smart early stage investors will invest in a portfolio of companies to balance this risk. Typically one in ten investments produce the return to cover the failure or mediocre performance of the others. For seed and early stage companies seasoned investors expect five to ten times return over five years to balance the risk out. For some investors the hurdle rate is 30 times. What does your projected return look like over the next five years?

As an investor in a growth company you need two key elements to make it an investment: potential for growth in shareholder value and a way to get your money out (an exit). In simple terms, shareholder value is directly driven by the potential for future profits and an exit means identifiable buyers of the business. What is your exit strategy and back up plan?

Test your business pitch

Whether you are seeking investment or not, you should always be able to present your business as one that meets the basic "Fit or Floundering" tests. It's a business pitch about the business, not just the product.

Businesses that struggle to answer these questions will struggle, tough times or not. They are not difficult, but out of the hundreds of companies we assess each year seeking investment, many fail to answer them in a succinct manner. Don't be still claiming to be a start-up five years down the road. Make it or adapt, before it's too late.

And don't let your ego or delusional behaviour get in the way. The test only works if you can convince an outsider. What would you do if you had \$1 million invested in your company today? How would it change your answers?

Remember, if a stranger would not invest in your business, why should you!

Mark Robotham is General Manager of the Escalator Service an NZTE funded initiative to help companies raise Angel Investment.

Contact: mark@escalator.co.nz