

# PRIVATE EQUITY'S SURPRISING BENEFITS

by Jacoline Loewen

It has been said so often that most entrepreneurs probably believe it: Bank loans are your common source of funds. Who but a bank (assuming you meet its covenants) will lend you money at just one or two points above prime?

However, as we learn in most realms of life, the low-priced products are not always best for you. And with a greater number of private investors creating a growing company's market for financing, many Canadian business owners are discovering there are alternative sources of capital. Probably, the most exciting news is that private equity deals are being done for

as little as \$500,000—a sign that private equity is shifting from Bay Street onto Main Street.

Private equity is the alternative source of capital to the big banks but don't

get confused by the title. This private source of money ranges from lending (you retain full control) to pure equity (investor comes on board as a partner). Some private investors take a more interested role in the businesses they choose. Many fund managers are former entrepreneurs who know the difficulty of building a business. For example, the founders of Harvey's Hamburgers now help finance companies with the philosophy of coaching management through the highs and lows, taking a longer-term approach than the banks.

One entrepreneur described how his equity finance investor helped set a growth strategy, even researching and visiting companies to buy. The investor was an old hand in the industry and was greatly able to speed up the company's organic growth. As the CEO said, "You couldn't find a coach with that experience. We really pushed up the growth more than I dreamt possible."



The important thing is the capital gain you make. If you want to continue with the same size of pie, go to the bank. If you want to grow the size of the pie significantly, think private equity partners.

This is not a put-down of the banks. They have a job to do, and they do it well. Depositors trust the banks with their savings and long-term investors buy their stock because they know the banks to be nice, risk-averse lenders—and they wouldn't have it any other way.

Private equity is different. This is risk capital raised from companies, pension funds, and other private investors who accept more risk in return for greater reward.

Because private equity investors do so many deals, they all have active Rolodexes that let them tap specific sources of expertise—from software marketing to exporting to Latin America. Their familiarity with an industry, the latest production and distribution methods, and potential buyers can offer a leap forward that no amount of bank capital can buy.

If your company needs additional management to grow, equity investors can help you find the talent and experience you need. And since their timeframe is to stick around for five to seven years, they won't bail out if your industry goes through a rough spot. As one fund manager put it, "We know that hockey stick revenues do not happen every year."

Private equity can also help you cope with unexpected problems. One fund manager, for instance, was unfazed when the CEO of an investee company suffered serious health problems—without a succession program in place. With his experience, he arranged a quick merger of the company, parachuting management into the main company before it could run into trouble. The deal also gave the founder peace of mind, knowing that both his personal finances and the people he had worked with would be taken care of.

Not all business owners are ready to work with partners like these. Fund managers are the smartest people in the financial business, and they can be just as ego-driven as the entrepreneurs they invest in. They identify weaknesses—such as inadequate management or outdated products—and tell the CEOs things they may not be ready to hear. Nevertheless, they are experienced business owners or analysts who know their stuff. And that's what makes them invaluable partners. Many owners say they are lucky to have their private equity investors, and credit their success as a result of partnering with them.

And if your business runs into trouble, you may be surprised how willingly your investors back you up. They have seen more crack-ups than the average entrepreneur, so they may be calmer about it than you. Rather than demand their money back as conventional lenders might do, fund managers will generally work with the entrepreneur to resolve the problem—even if it means renegotiating the repayment schedule. They may invest more, depending on the firm's prospects. While some entrepreneurs look at that as giving up more equity, others see it as another chance at bat.

One fund manager recalled, "One of our entrepreneurs called with the news that a top employee left and took key accounts. We told him something similar happened to our company back in 1992 and it seemed the end of the world at the time. I told the guy to get a good night's sleep—let's get a plan together in the morning."

You may have to do some sleuthing to find potential investors. You can identify some of the larger funds through the list of members of Canada's Venture Capital and Private Equity Association, at [www.cvca.ca](http://www.cvca.ca). Or, you can ask your accountant or lawyer for contacts. The investment community is a very small world though, so be warned to make sure your request for financing is presented in the best possible light, and that you have introductions from a reputable contact. Be aware that only 5% of companies actually get this holy grail of capital.

Compatible investors are not found on every corner—but once you find them, they'll be in your corner for good. **E**