COMPASS NORTH INC.

- *providing management & advisory services*

How to Prepare a Company to Successfully Raise Equity Capital

by

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- We Help Businesses make More Money in Less Time -
by helping them execute focused market-oriented strategies, access more resources
and adopt improved business practices

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Start-up and early-stage companies typically face significant challenges getting established, commencing operations, growing, and ultimately reaching a meaningful state of stability. Unfortunately many, the majority in fact, struggle, fail or get folded into other companies some where not too far down the line. Even established companies face challenge, change, set-backs and turmoil along the way. But what all of them need to get started and survive is equity capital.

Rarely, however, do sufficient cushions of equity capital get created solely by the profits thrown off from success (i.e. from the organic growth of the business). Rather, almost all companies - from those in start-up and at the early early-stage to even those more established corporations – experience times when they feel compelled to seek third party capital which often comes in the form of equity funding in order to hurdle a growth hump they've run up against or get through some rough patch that they've found themselves falling into now or then.

Clearly, not every company succeeds when they go seeking new capital from investors. But often, like that old Boy Scout motto suggests, preparation is the key to funding success.

One take-away lesson I have to offer based on my extensive major transaction experience is this: any company hoping to successfully close a funding transaction needs to be well well-organized, highly-focused, capably-led, well-prepared and offering a satisfying risk-adjusted payoff within a reasonable time.

Furthermore, the company needs to be seen to be promoting and delivering, or at least promising soon to do so, one to three key offerings, rarely more. For these offerings to be viewed as 'wealth creation engines', they must relieve significant material/real-world 'pain', or deliver significant meaningful/measurable 'benefits' to money-paying customers or their hangers on such as advertisers.

Importantly, these critical solutions being offered to customers must be directly tied to recognized needs they have in respect of important addressable problems or action compelling aspirations or benefits that they have today or would have if they had enough knowledge.

Doing this and being seen to do this, or at least being seen as setting up to do this, is what generates appealing upside potential for all enterprise stakeholders such as shareholders, staff, suppliers and current and prospective new debt and equity capital providers alike. And in keeping with what defines all good business investment opportunities, investors and other capital providers will expect what the laws of economics demand, namely that the company's revenue is or will soon (hopefully always) exceed the company's operating and opportunity costs as a result of the product or service being sold commanding such a material (hopefully significant) margin that the company's net cashflow and profit generated is so positive that after all is said-and-done it has made everyone very happy indeed.

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Unfortunately, many companies need to attract third-party equity capital before they reach the point where they are driving positive cashflows or profitable results, sometimes even before operations have begun. This means that before there is some positive reality to substantiate all that is being said, company principals need to be out telling prospective capital providers a believable, credible, supportable and verifiable story of the bright and promising future their company has before it. And they will also need to be prepared to put their credibility (and likely their job as well) on the line by giving prospective capital providers their next-thing-to-an-absolute-guarantee that their 'suggested golden future' will in fact get delivered on time within acceptable parameters. An additional expected message to this is that the interests and economic welfare of all outside capital will be the company's absolute first and foremost concern. And all of the above must be communicated in a sincere, honest, truthful and compelling way if the company principals can hope to succeed in attracting the outside support they believe they require.

For most early-stage businesses, third party financial support usually comes in the form of private equity because such companies typically have too few assets and too little track record or positive results on which to justify getting a loan on anything other than a personal loan or credit card advance. Even if one is available, often a loan is not considered an acceptable option for the entrepreneur because they resist either signing the personal guarantee required or putting most or all of their personal / family assets at risk to access the cash they want.

Consequently, setting up to tell a compelling story of business opportunity - one that captures and captivates prospective capital providers - is no small feat or quick 'hocus-pocus' communication effort.

In significant contrast to how family, friends, and fools invest without much expectation, thought, due diligence or required terms & conditions, 'serious-money' private equity investors like angel investors / venture capitalists / private equity firms / and the like all typically demand a lot. At the top of the list of demands for almost all such new equity investors is the need that any investment opportunity they are going to put money into must virtually guarantee them a satisfactory return. The type of return they seek is one that typically comes by way of a cash-out capital gain of between 5 to 10 times their all-in invested amount. Another way of saying this is that they are looking for 30 to 100+% per annum gain on all money they put in over their investment holding period, which typically ranges from one to seven years. Where exactly in the demanded return range a particular investment opportunity slots in depends on general market conditions, the opportunity's risk profile, its opportunity substantiation, and what competing alternative money-placement opportunities investors have.

If your investment play offers material, quantifiable, and verifiable cashflow, marketable unpledged asset values that offer an alternative source of repayment and a satisfactory degree of piece of mind, you maybe able to do business with other capital providing groups such as mezzanine lenders, tier 2 or tier 1 financial institutions, or even the general public if your deal qualifies as a public market securities offering. Then, as the assured value that you put on the table goes up, the price you have to give up to get your deal comes down. But no matter what, however, your cost of getting capital (other peoples' money) almost always will seem to you way beyond your comfort zone. So you best be prepared early on to answer this question: *what price are you willing to pay, or what can you justify, if your company is to get its shot at that successful future you say you can deliver?*

Additionally, before we go too far, it is important to take note that serious public markets oriented equity investors typically refuse to put their money into any business that does not have the potential to generate between $20 to $100+ in annual revenue now or within some reasonable period of time, which currently is best being shorter than later but the typical range is no more than 1 to 5, or sometimes 1 to 7 years.

Furthermore, the vast majority of 'serious money' investors frustrate many entrepreneurs by taking a careful, studied, profession approach to investing when the amounts involved represent more than a small sum. This basically means they will demand the deal be free of worry (theirs not yours), which you can take to mean that they want to sleep well at night through out all the period of your mutual association. In start-up and early-stage company situations, or when the amount being put in is a large sum, what this generally equates to is that the investor will want to either control of the company from the moment they give over their money, possibly offering back an option to the entrepreneur to regain control based on some success driven formula, or at the very least, they will demand a material, even veto, say over all significant decisions that the company could and will make as the venture goes forward.

To raise equity capital, entrepreneurs and executives all absolutely need to insure they give prospective investors good / solid information about their company and its prospects in order that the investor can fairly and properly evaluate the investment proposal being made to them. And if you expect to convince investors to 'rent' you their money for awhile in order that you can grow your venture, the information you give them better be honest, full, plain and true disclosure, for it's a deal killer to get caught or even suspected of misleading or making false representations.

When evaluating your investment proposal, you should keep in mind how many private equity investors make their decisions, which typically they do by basing on their assessment on an evaluation of the following investment-opportunity dimensions:

- Market Potential
- Sustainable Competitive Advantage
- Management Team
- Operating Strategy & Scalability
- Proposed Financial & Investment Terms
- Performance Already Demonstrated & Investment Raised To-date

Therefore, in whatever you do, say or write, you need to provide positive information along these dimensions about your company and its business opportunities so that your prospective investors do not have to ask for key information that should have been presented to them as a matter of course, or worse yet, dismiss the opportunity because they found it lacking on essential grounds.

In light of the above, it should be now reasonably obvious that to succeed in attracting investment capital, entrepreneurs and executives must serve up opportunities that meet equity investors' attractiveness criteria. A good way to start conveying that is to develop your own high-quality, compelling answers to the following rather vague questions:

1. How pressing is the need for the proposed investee's product or service?
2. How feasible is the venture in the eyes of target customers and knowledgeable people?
3. How much can an investor make, when, and how likely is that outcome to be?
4. How much might the investor lose, how, and how likely might that happen?
5. How many ways or means exist for the investor to get their money back?
6. Who else credible besides you says your deal is any good?
7. Who else has agreed to participate in the deal and for how much?
8. Why should the investor believe what they are being told?

The answers companies have to these questions represent the foundation upon which sits both the structure of their business and the basis for financing it.

To succeed in raising capital, no matter if it is equity or debt, companies also will need prepare the right set of communication 'tools' and other documents for the job, ones that fit the "answers" they have for their particular situation.

The Principals at Compass North Inc. recommend that companies seeking significant capital investments put together their own customized **Deal Tool Kit** made up of the following items:

- Proposed/Requested Financing Deal Outline of amount, type, terms, etc.
- PreDeal Business Valuation (pre-new money being received)
- Summary Business Description (the 60 sec elevator pitch)
- Investor Presentation
  (10 to 20 minute overview of key elements - see attached 12 slide outline)
- Projected Business Milestones
- Referenced Market Information like surveys etc substantiating sales potential
- Management Team and Board Organization Charts and Key Person Bios
- Exit Plan Options for Investors
- Security / Guarantees if any offered on deal (description, valuation, etc)
- Financing-oriented Business Plan that states the Company's growth strategy, its competitive position in the market, the value-add driving its competitive advantage, and mission and vision statements, etc (see attached outline)
- Financial Statements, Cashflow and Funding Usage Reports – historical, budgeted and projected with supporting details
- Valuation Estimates for Company as-of the target investment exit dates with projection of anticipated ROI for investors
- Table Detailing Investments already made by whom in the Business to-date
- Due Diligence Documents - incorporation papers, financial statements, annual and quarterly reports, contracts, etc
- Other Documents as required by investors, advisors, agents and the like

Finally, it is important to have a good commercial / securities lawyer involved in your deal from the early developmental stages, at least to some reasonable extent, so as to make sure your deal, its preparation, negotiations, due diligence review and closing, all have a much better chance of staying on track. Beyond good preparation, this is one of the best ways we know to help make sure you've maximized your odds for deal success. Chose carefully in this regard, however, for there is much variety among those lawyers who will tell you they can do this job for you. After the fact is not the time to check:

- how much deal experience your 'chosen legal advisor' has, or
- how much time they have for you, or
- what their legal and other services will cost, or
- if their style is to take over negotiations with counterparties on your behalf because their goal is to protect your interests at all costs even if this means doing your thinking for you, or
- whether they will act simply as your legal advisor, sounding board and on-call/at-your elbow support.

So there you have the facts about doing start-up and early-stage capital deals from our perspective. While we have laid out the dimensions of deal making, be advised that there is much art involved, for the devil is in the detail and good listening skills, timeliness, deft reactions and ultimate execution are often critical - even vital - to success.

If you need to raise new capital, be it debt or equity, we are here to help you make the most of your opportunity. Compass North Principals have extensive experience as in-company deal-making executives and as external advisory support. Based on the records of success we have raising funds for companies, we know how in practical reality you only have one-shot ay catching an investor's interest. Also from experience, we know how investor memories for bad pitches and disappointing people are often very long indeed. Because of these things, we strongly advise companies to carefully think out how they are going to best insure they're taking their best one-shot at getting a funding deal done before they go out to pitch any prospective investment counterparties.

Having negotiated and closed over $2.5 billion in public & private debt, equity, alliances, hedging and M&A deals, we at Compass North Inc. know what to do and how to do it when it comes to major transactions.

Give us a call to discuss how we can help you and your company significantly increase your odds for deal success.

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Attachment

Investor Presentation Outline
- 10 to 12 slides max in large font (20 to 30 pt.) given in 20 minutes or less followed by Q&A

- **Slide 1** - **Presentation Title:** (First Impression) name of company; presenter; contact info; product or company image
- **Slide 2** - **At-a-Glance / Executive Summary**
  Business model: i.e. - *Provide imaging solutions to diagnose and analyze skin surface core strength*
  Core strength: i.e. - *Patented XXXX platform*
  Goal: i.e. -
    - *Sell to the US medical field – 2H, Year*
    - *Expand to the international market – 1H, Year 2*
    - *License technology to the consumer arena – Year 3*
  Revenue projections (early 3 yrs) i.e. -
    - *Year 1 – $3.4M*
    - *Year 2 – $10.5M*
    - *Breakeven in Year 3*
  Presentation Goal such as projected need for financing (early 3 yrs) i.e. -
    - *Year 1 – series A funding of $3.5M*
    - *Year 2 – series B funding of $3.2M*
    - *Year 3 – series C funding of $2.0M*
- **Slide 3** - **Market & Problem being Addressed -** Describe why prospective customers are in need of a solution & size of market - from the point of view of the customer; not the point of view of what your product does
- **Slide 4** - **Solution Offered & Value Proposition -** Describe how your offering solves customer needs and how compelling are the advantages offered by product or service
- **Slide 5** - **Business Model** - Detailed but brief technical overview of what is involved in the business transacted and how company expects to make money from customers
- **Slide 6** - **Company Compelling Underlying Magic & Competitive Position -** Description what makes your offering special relative to the (expected) competition and how you can and will beat them with description of the compelling (whole solution) value proposition offered end-users
- **Slide 7** - **Go-to-Market Strategy & Sales and Marketing Issues** – Present clear and actionable blueprint of market entry and growth strategies as applicable (how, where, with whom and why your company is going to get and grow sales)
- **Slide 8** - **Management Team –** Describe what smarts, pedigree, commitment, track records these people have that support their ability to be winners and make big gains for investors
- **Slide 9** - **Key Metric and Milestones** – List the significant business metric and accomplishments in number terms expected to be achieved with target completion dates which your company will experience along its road to success
- **Slide 10** - **Financial Results, Projections, Funding Requirements, & Use of Proceeds** – Describe where the funds will be used and what has been and is expect to be accomplished in financial number terms
- **Slide 11** - **Exit Plan** – Tell prospective investors how you expect they will get their money back and when (allude to the prospective investment ROI but avoid making promises that you can't ~100% keep or make happen; remember, better to under promise and over perform than getting caught having it go the other way round)
- **Slide 12** - **Final Slide** (Last impression) Summary slide repeating request (i.e. restating presentation goal) and giving the high-points that you believe should convince your audience why they should invest in, or otherwise support, your company and its opportunity

Simple Business Plan Outline:

1. **Executive Summary**: Write this last. It's just a page or two of highlights but this is THE critical attention grabber.
2. **Company Description**: Legal establishment, history, start-up plans, etc.
3. **Product or Service**: Describe what you're selling, why it is unique and its business model. Focus on customer benefits and how the company will create, deliver and get paid for the value offered.
4. **Market Analysis**: You need to know your market, customer needs, where they are, how to reach them, what you competition is, etc.
5. **Strategy and Implementation**: Be specific. Include what challenges the business needs to face and set out management responsibilities with dates and budgets. Make sure you can track results.
6. **Marketing & Sales / Web Plan Summary**: Discussion of sales and marketing strategies and website, development costs and operations if applicable.
7. **Management Team**: Describe the organization and the key management team members.
8. **Operations / Human Resources Plan**: Describe what the company needs to create and deliver its value.
9. **Key Metric and Milestones:** List the significant business metric and accomplishments in number terms expected to be achieved with target completion dates which your company will experience along its road to success
10. **Financial Results/Analysis**: Make sure to include at the very least your projected Profit and Loss and Cash Flow tables.

Expanded Business Plan Outline:

1. **Executive Summary**
    - 1.1. Introduction
    - 1.2. Situational Need
    - 1.3. Company Solution
    - 1.4. Objectives
    - 1.5. Key Milestones to Success
2. **Company**
    - 2.1. Company Ownership
    - 2.2. Mission
    - 2.3. Vision
    - 2.4. Description of pressing market need being addressed
    - 2.5. Description of unique differentiated value-add offered
    - 2.6. Company History (for ongoing companies) or Start-up Plan (for new companies)
    - 2.7. Company Locations and Facilities
3. **Products and Services**
    - 3.1. Product and Service Description
    - 3.2. Competitive Comparison
    - 3.3. Sales Literature
    - 3.4. Sourcing and Fulfillment
    - 3.5. Technology
    - 3.6. Future Products and Services
4. **Market Analysis**
    - 4.1. Market Segmentation
    - 4.2. Target Market Segment Strategy
        - 4.2.1. Market Needs
        - 4.2.2. Market Trends

Important Notes –

1) **In order to succeed, planning is indispensible but …**
2) **Without a time-specific goal, purpose and audience, making a detailed and specific plan is usually a waste of time:** plans are only point-in-time models of what might be that are useful in communicating with others in order to coordinate resources and actions;
3) **Savvy practical people typically conceptualize first, get interest second and do planning in detail third and act fourth:** actual results almost always differ from what was anticipated, which is why what you do and achieve is more important than what you

plan, although planning can help you learn what the right thing is that you need to do when the unexpected occurs

4) **Tailor every plan you prepare to the objective it is meant to support:** for instance, financing oriented plans are distinctly different in focus, rational and content to a material extent from strategic business plans written for a company board of directors or joint venture partner
5) **Size your business plan to fit your business** Remember that your business plan should be only as big as what you need to run your business. While everybody should do some market, operational and financial planning to help them get the most out of their business opportunity, not everyone needs to develop a complete formal business plan suitable for submitting to a potential investor, bank, or venture contest. So don't include the above outlined points / topics just because they are some big list of must haves somewhere unless you're developing a standard business plan to show to somebody expecting to get a standard business plan.