

Want Investors to Take a Swing? Practice Your Pitch!

By Kevin Wiley

So, you've got a goose that lays golden eggs, eh? If only you had a couple bucks for chickenfeed, this bird would make us all rich, you say? As an entrepreneur approaching private investors, you'd better come equipped with more than just a fairy tale. Today's angels have short attentions, sharp pencils and rarely give a second chance. A key to being successful in raising early-stage financing for your start-up lies in knowing your market. Not just your product market or your service market, but the market of investors who might give you a chance to pitch your company to them.

By definition, private equity investors are an elusive bunch. Without public due diligence or easily accessible information, private markets exist largely behind closed doors, making it difficult for the average entrepreneur to profile the players and cater their approach to seeking funds.

What, then, do potential backers want to see in a deal? It's more than a 5-page business plan and a spreadsheet full of digits. Right out of the gates, they've got to relate to your business. If it takes you 20 minutes to lay out the landscape in which you're competing, you're already toast. Like a good story, the audience has see where you're going in short order, otherwise you don't have a grounded concept or are talking to the wrong investor.

They've got to value your competitive advantage, which commonly is proprietary in nature. In other words, you often need some intellectually protectable innovation in process or technology that adds to your company's competitive edge by creating a barrier to entry for other like-minded entrepreneurs (or established firms). If it's been done a hundred times or could be done a hundred more, you're going to have a tough sell convincing an angel to risk their capital with you.

What's more, a local or regional market often won't do, as it limits the global potential that defines the greatest angel investments in American history. Thus, lurking in the minds of many investors willing to put hard-earned cash on the line is the chance to hit it big. Without honest forecasts expanding beyond nearby economies goes the prospect of hitting a true home run investment.

Then comes a lucrative path of exit within a definable channel of risk. Companies must make sure all the investor exits are clearly marked, and that they meet the type of returns expected. So, what is an ideal ROI for someone putting risk capital into your start-up? The first thing to understand in asking this question is the historical likelihood that the investor will see a return at all. As noted above, this is an elusive market and getting solid data in and of itself is difficult, much less extrapolating averages. But most anecdotal research suggests that a private equity investor will need to make 10 to 15 investments in order to have one of those succeed, paying for the cost of the others and

generating a positive return to boot. 10 to 15 investments! Of those, it can be expected that several investments will go belly up, several will whimper along (never paying out), and some will return a modest sum that likely doesn't justify the risk taken in the first place. So, that leaves the one great investment that makes it all worth it. While every entrepreneur believes that one investment is their company, you've got to show it in the numbers.

Taken another way, if an investor makes ten \$10k investments, nine of them likely won't pay out. That leaves one \$10k investment that needs to have a 10-fold return in order to make up the difference. So start there – an investor needs to see at least a 10x return possibility given the historical chances for company success. And essentially, that's just to break even from the rest. So 20x to 30x is really much more in the range an angel will look for in terms of payback, most commonly realized 4-7 years down the road through a merger or acquisition of the company.

Note: as conservative as the entrepreneur may claim to be, an investor with a critical eye will often cut the forecasted revenues in half and double the anticipated expenses, then see if the number still can crunch out the necessary returns. So, it's easy to see why fast growth, global potential companies tend to be the type of investments angels like to bet on.

Above all else, investors have got to believe in your ability to execute. And not just believe in it, but be shown a track record of success by either the founder or other key management involved in the company. No matter what the numbers say, no matter what the technology or opportunity your start-up has in its wing, if the angel doesn't think you can pull it all together and sustain long enough to generate returns, they won't invest.

And after all this - after you've made it past the pitch and presented your business plan - begins the real due diligence. Market assessment, competitive analysis, technological testing, background checks, and if you're lucky, negotiations. So if you're out to garner quick sums of cash to turn an idea to an opportunity, think again. You've got to have your cards stacked tight and your game plan razor sharp.

Now, given the fact that I help run an organization committed to fostering the private equity markets of Alaska, doesn't the above seem a bit harsh? Am I trying to scare the pants off potential angels or ruffle the feathers of entrepreneurs looking for capital? Absolutely not. The above doesn't take into consideration civic or community-based motivations for private investing, which are critically important for many angels and the economies in which they take place; nor does it address the entrepreneur who just needs a leg up to get their small business off the ground. However, my job is to help elevate the understanding and sophistication of folks involved in this arena. By outlining in this article the expectations of many seasoned angels, I hope to give Alaska's best entrepreneurs an even greater chance of making a pitch that can lay a golden egg.