

— *Afema*

VC financing –
some aspects on VC investments

Tartu, Estonia
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Get the pictures at www.afema.se

Eric Martin

- In the business of VC and entrepreneurs since 1982
 - Svetab, largest Swedish VC in early 80's
 - Företagskapital, first VC in Sweden, founded 1973
 - TUAB, specialized in university start ups
 - Aldano, VC with Industrifonden and 30 proven entrepreneurs as owners
- Own consultancy organization since 1984
 - Afema, business development of entrepreneurial companies
- Secret talent:
Former water ski coach for Swedish national team
- Present assignments
 - AirNet Holding
 - Azpect Photonics
 - Sourcecom
 - COB Foundation
 - Thonab
 - VIAB
- Former chairman of Connect Eastern Sweden and Swedish Venture Capital Association as well as consultant in some 100 entrepreneurial companies
- BSc in Business Administration with a technical background

What to come

- Part 1 – In theory
 - Definitions
 - Deal flow
 - The American model
- Part 2 – In practice
 - The Entrepreneur vs The VC
 - The curve of Akbar
 - What to expect along the way
 - How do you choose your VC

When to choose VC

- ❑ You want to grow fast
- ❑ You are prepared to take influences from the outside on running your business
- ❑ You are willing to make an exit in 2-7 years

How do VCs act

- ❑ Minority share holder (mostly)
- ❑ Active owner
- ❑ Always a board position
- ❑ 59% have at least one contact a week
- ❑ Basically no fees
- ❑ Active strategy towards exit

VCs bring in 3C

□ Capital

- As equity

□ Contacts

- Often for the most part in finance and law

□ Competence

- Specialists on rapid growth

The essence of

Love

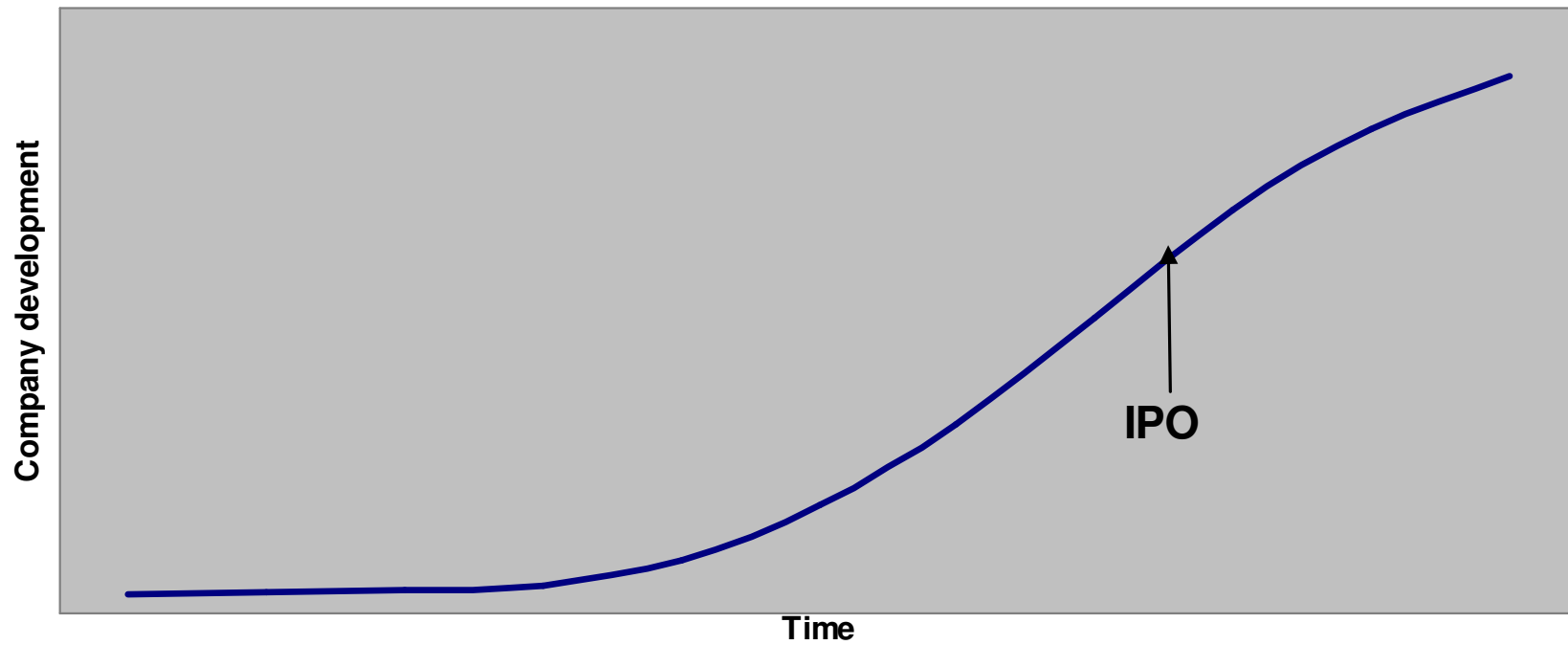
- ♥ **In love**
- ♥ **Engagement**
- ♥ **Wedding**
- ♥ **Marriage settlement**
- ♥ **Matrimony**
- ♥ **Happy divorce**

Venture Capital

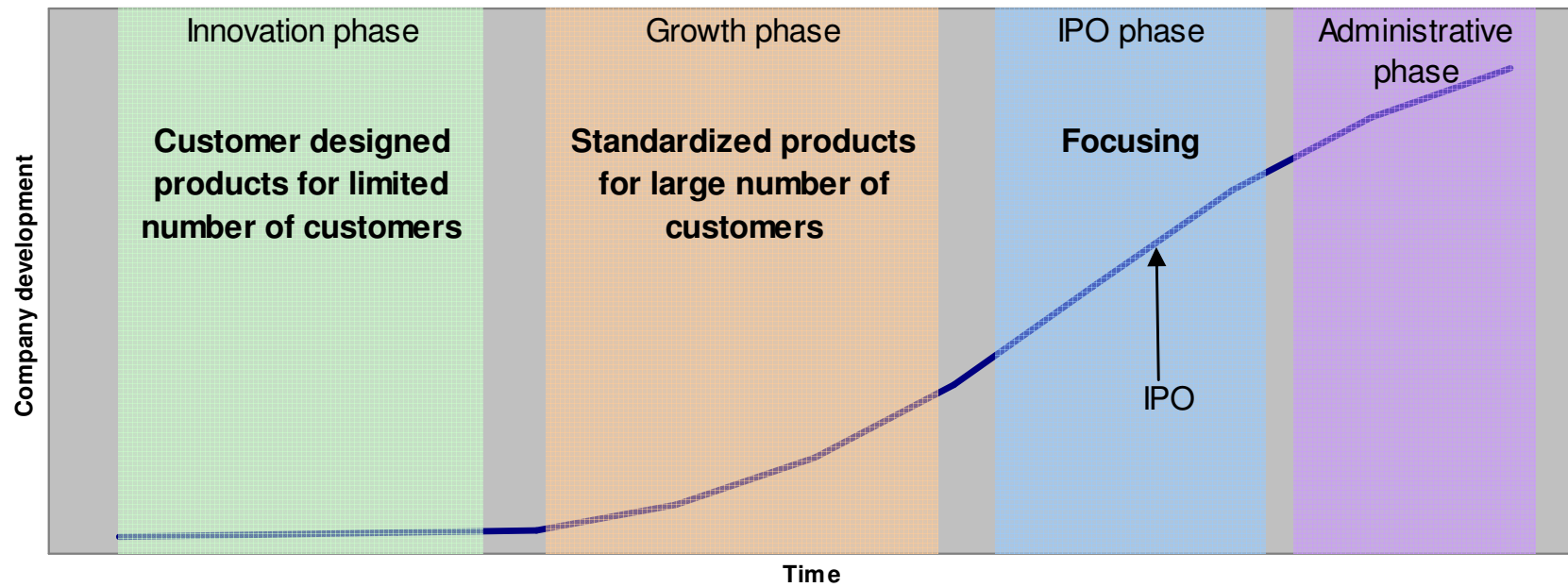
- \$ **Deal flow**
- \$ **Due diligence**
- \$ **Investment**
- \$ **Shareholder agreement**
- \$ **Monitoring
(Business development)**
- \$ **Exit**



The development curve of a company

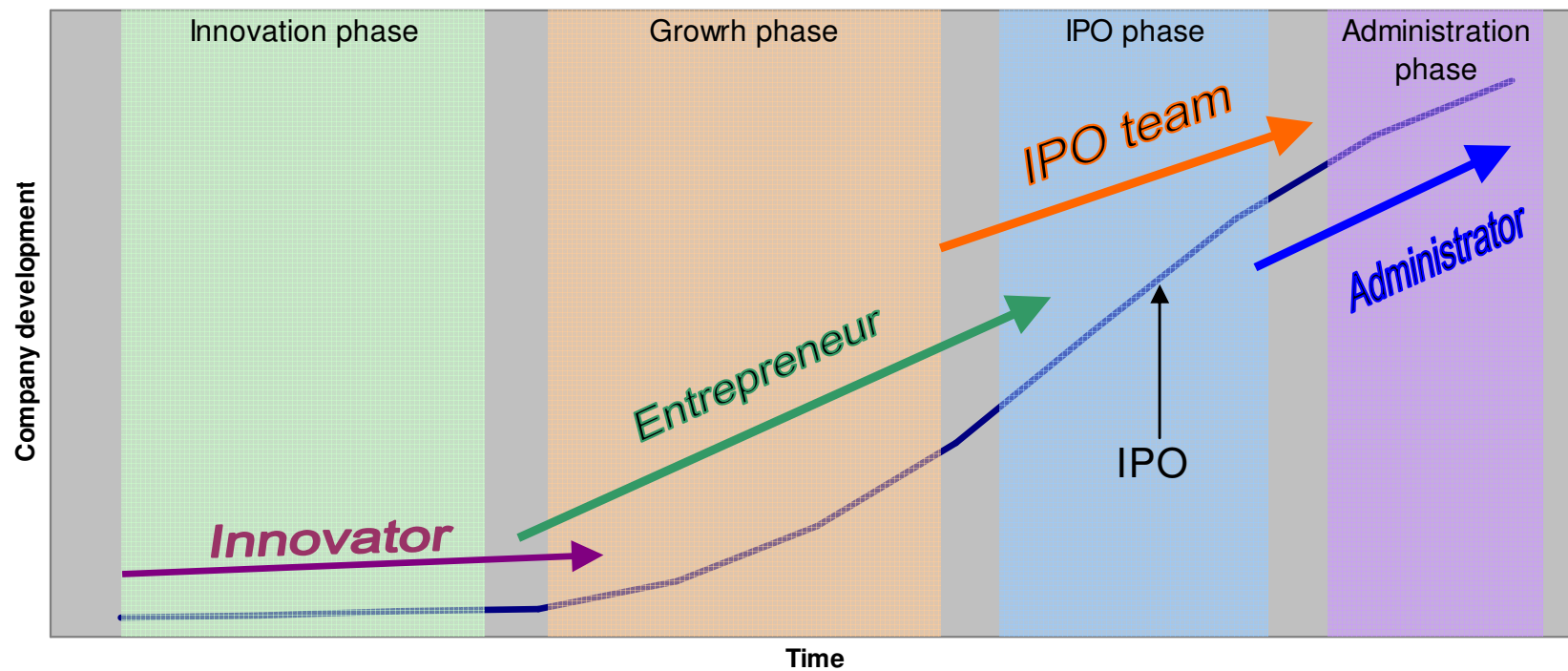


Development phases and company strategies





The American management model



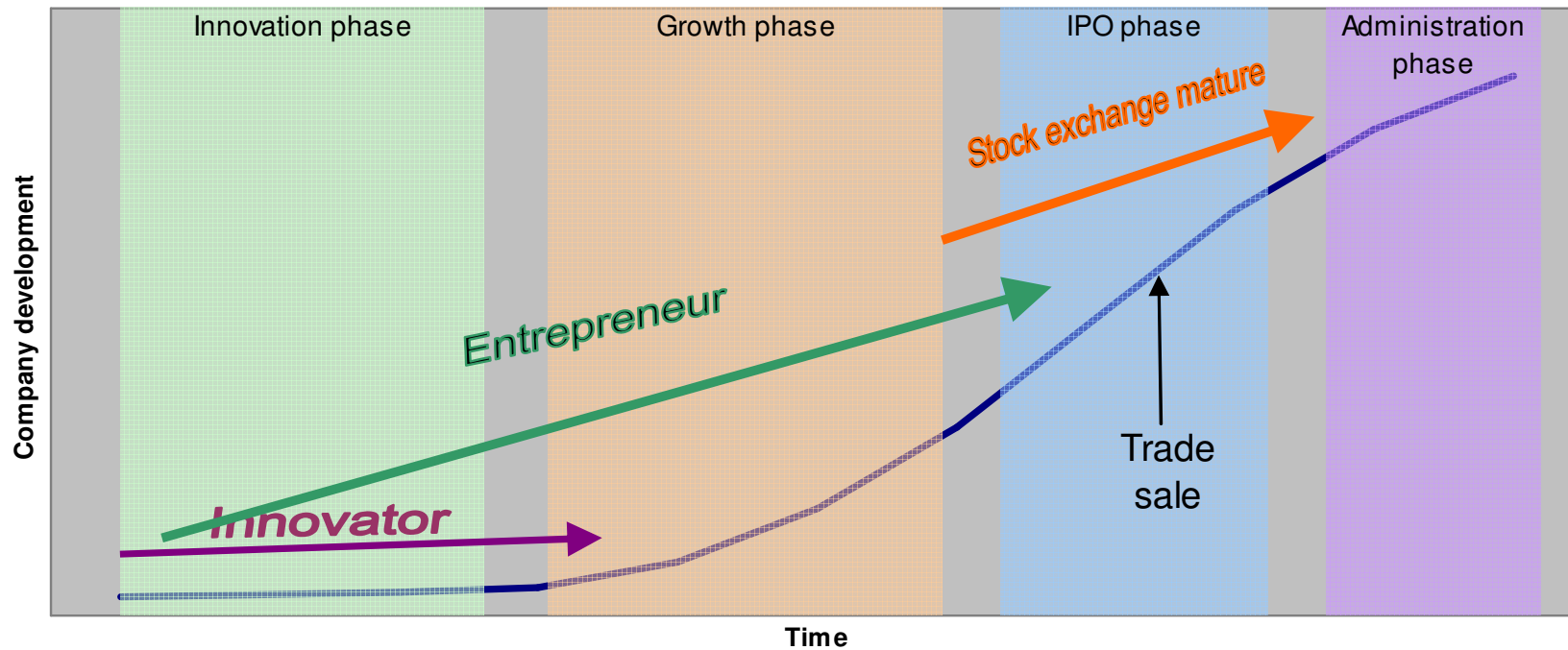


Characteristics for Sweden

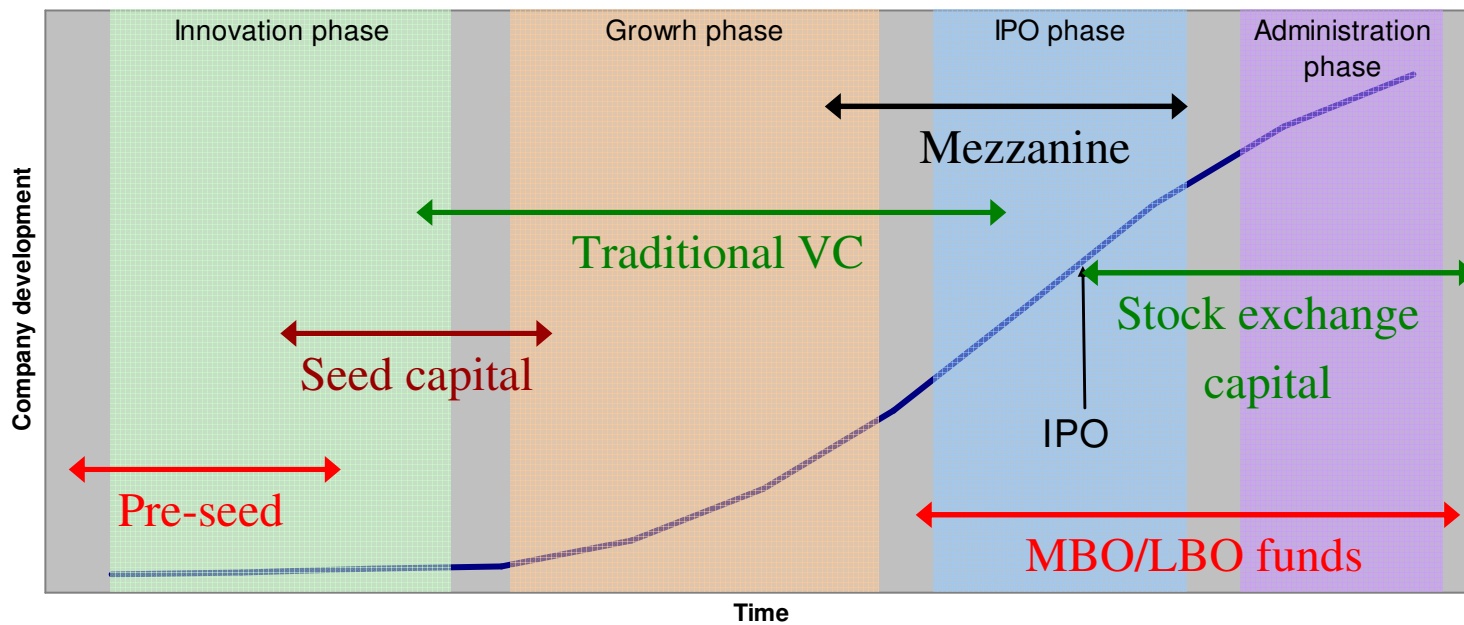
- ❑ Salesmanship does not come natural
- ❑ Small home market
- ❑ Few business angels and early phase VCs – limited financing in early phases
- ❑ Only a few companies reach IPO characteristics



Adaptation to Sweden



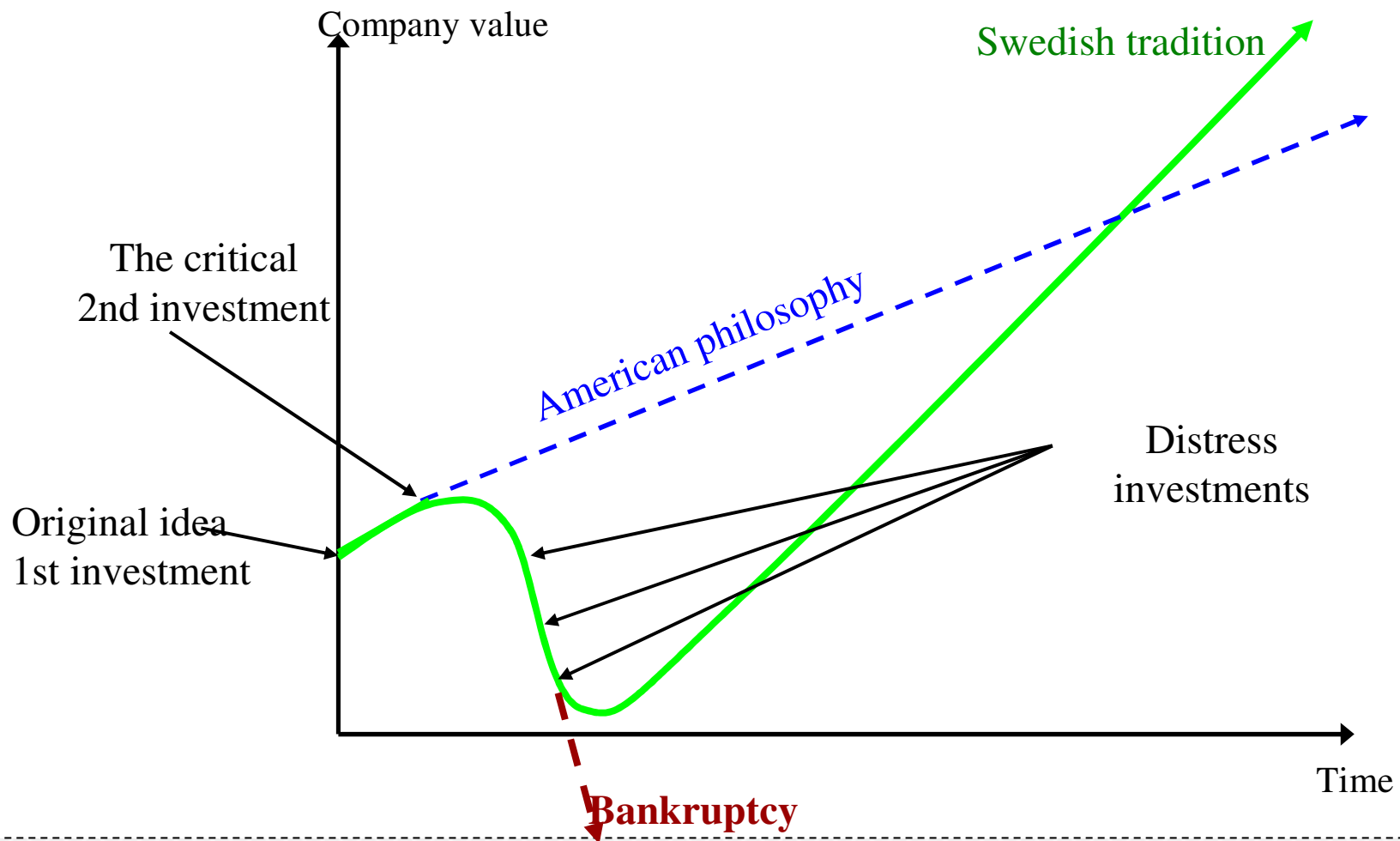
The equity possibilities



First contact

- The presentation
 - The pitch (6 sec)
 - The short version
- The business plan
 - A good executive summary
 - Customer satisfaction well described
 - The sales process well described
 - The key persons well described
 - Team characteristics
 - SWOT analysis
 - Ownership – goals and strategies
 - Exit possibilities
- The funnel
 - 100 proposals
 - 10 prospects
 - 1 investment
- Red flags
 - Basics – Out of scoop
 - Characteristics of the entrepreneur
 - Lack in sales
 - Lack in customer satisfaction
 - Limited growth potential
 - Weak exit possibilities
 - Multiple risks
 - Different agenda

The curve of Akbar



Evaluation and Negotiation

□ Traditional methods

- Substance
- P/e
- P/s
- Cash flow
- Comparisons

- Consider the p/e-arbitrage
 - Liquidity in the share
 - Minority holding

□ In practice

- Horse trading
- Depending on future outcome
- Magical shares
 - 10%, 20%, 30%, 49%, 51%, 68%, 90%
- What is the cost of the marginal share
- Depending on performance

Rate of return on investment

- ❑ 10 investments >>
 - 3 total losses
 - 3 +/- zero
 - 3 limited
 - 1 splendid

- ❑ Time of investment 2 – 10 years

- ❑ Desirable rate of return 18-28% p.a.

- ❑ A priori expected rate of return minimum 50% (30%) p.a.

Shareholder agreement

- ❑ The investment
 - How many share for how much equity
 - Guarantees
- ❑ Business development
 - Board of directors
 - Minority protection
- ❑ Exit
 - Shareholder goals
 - Time frame
- ❑ Quibbling
 - Disputes etc

Ownership strategies – two tracks

Operative reality

- ❑ Turn over and profit
- ❑ Outside relations
 - Customers
 - Colleagues – competitors
 - Enviroment issues
- ❑ Organization

Ownership issues

- ❑ Number of partners
 - Single
 - Equal partners
 - Institutional partner
 - Large number of partners
 - Listed company
- ❑ Financing
 - Equity
 - Customers
 - Bank
 - Loans from owners
- ❑ Ownership goals
 - Livelihood company
 - Trade sale
 - IPO

Business development

□ Management style in growth companies

- The goals sets the direction, not the cross bar
- Sales is the engine of growth
 - Invests in sales
 - Everyone is a sales man
- Organization
 - Task force, puts out fires, monday meetings
- Prepare for working capital
- Give priority to time tables before cost savings

□ Focus

- Outsource
- Growth through buying functions
- Prevent narrow sectors

Exit

- ❑ The stock market is an emergency exit
 - Lock up effects
 - Quotation influences
 - Insider issues
 - "Small stock lists" are one time deals
 - No liquidity for trade and new issues of shares

- ❑ Trade sale
 - Stock market mature
 - Industrial
 - Financial

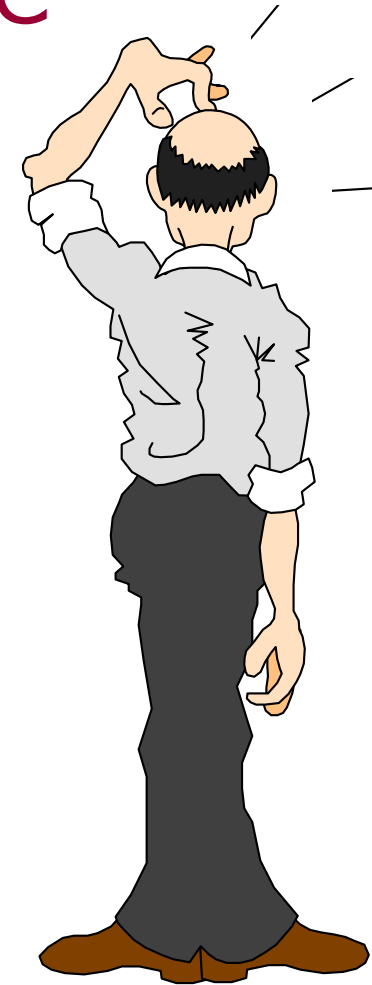
The time aspect

- ❑ Rome was not built in one day
 - and neither was IKEA
- ❑ To build organization and company culture is time consuming
- ❑ To build a customer base is time consuming
- ❑ To build a trade mark is **very** energy and time consuming

- ❑ Immediately start selling and create cash flow
- ❑ No excess financing – live on the hump

How do you choose your VC

- ❑ Motives
- ❑ Muscles
- ❑ Personal chemistry
- ❑ Track record - references
- ❑ Network
- ❑ Competence



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