Finding funds for the SMEs

Every small business needs new funding at some point. But where do you look, how do you select your "angel"? Here Nathan Boublil of EP Capital answers some key questions

III ***What should an entrepreneur be ready to give away in exchange for capital, network and experience provided by a private equity platform?***

Equity investors will by definition invest in exchange for an equity shareholding percentage in the company. In case of bankruptcy, equity investors will typically lose everything, but will participate financially in the success of the company if it is later sold, listed on the public markets (IPO) or if it distributes dividends to shareholders. Therefore, it is important that entrepreneurs have an informed view on the valuation of their company when they approach business angels/ institutional investors.

For early-stage businesses, traditional corporate finance valuation techniques (such as the well known DCF) cannot apply for two reasons: i) the company is generally not profitable/cash flow positive and ii) financial forecasts are hard to make. Therefore, the most valid technique is to see what valuation level other companies, in a similar sector, region, stage of development and potential are raising at (often called "transaction comps"). As a business angel syndicate, we personally invest in companies which have a valuation comprised between £1m and £10m, for an equity stake between five percent and 40 percent.

In exchange for an equity percent, entrepreneurs will receive cash funding and often other "intangible" services such as network and advice (in an informal or a formal way through a board seat for instance). Some investors will prefer to stay passive but many business angels are ready to offer some form of help and coaching to the entrepreneurs they finance. The beauty of equity financing is that the entrepreneurs' and financiers' interests are perfectly aligned.

It is worth reminding that the UK has put in place an excellent environment for entrepreneurs and investors, with the EIS (Enterprise Investment Scheme), which was further strengthened in March 2011. In November 2011, the UK has also introduced the SEIS scheme (Seed EIS), an even more powerful scheme, targeted at very early-stage SMEs. Therefore, the UK government is determined to make it as easy as possible for UK entrepreneurs to look for equity financing - this is in fact a key feature of its "pro-enterprise strategy to recovery".

How could you help services-based companies? Do you exclusively focus on companies that have an added-value in terms of technologies and innovation?

Not at all, the services industry is one of our sectors of focus, just like many business angels and institutional investors. The UK prides itself on its services industry so it would be hard to ignore it! That being said, from an investor's perspective, there is a distinction that needs to be made between the so-called "lifestyle businesses" and other businesses. The most important parameter for equity investors is not really the industry but the perceived ability to "scale" (which is why investors' bubble has emerged around online businesses).

Should you hire a professional advisor to assist you during such a process?

It very much depends on how comfortable founders are with capital raising processes and what their level of contacts in the investor community is. Some founders are already well-connected with business angels and institutional investors and therefore manage to execute their capital raising without any outside help (except legal) and with minimum disruption to their day-to-day business. Others can really benefit from a financial advisor or a fundraiser, even for the first rounds of funding. For more mature businesses, with multi-million revenue, the vast majority of entrepreneurs hire advisors/fundraisers as they have "too much on their plate" running the actual business.

When hiring advisors, it is important to take the time to select them well and to ensure that they are well incentivised, with a low percentage "retainer fee" and high percentage "success fee" component. It is also important that entrepreneurs do not delegate everything to advisors/fundraisers.

The UK also has many business angel networks which can greatly assist in talking to a lot of business angels in a time efficient manner. ■