SUCCESSFULLY CAPITALIZING FOR GROWTH

How will your company finance its growth?

Your company has an opportunity to grow, but you need access to capital with the right terms to finance that growth. How do you determine what type and mix of debt and equity financing is appropriate? How do you work with investors and lenders to develop the optimal capitalization structure so you can take advantage of that opportunity?

In this edition of *Executive Issues & Insights*, we address the spectrum of alternatives with key insights drawn from the extensive C-suite and Board experiences of the NextLevel team on how to successfully capitalize for growth. Future editions will address specific types of growth capital in greater depth.

NextLevel Case Study

Tech company finances significant growth through convertible debt

A public company in the online marketing services and technology business was growing at a very strong rate. Its net revenue had grown an average of 177 percent per year over the prior three years. It was also very profitable, with operating income growing an average of 195 percent per year over the same period.

The company needed additional capital of about $75 million to help finance a significant acquisition it wanted to make. In reviewing the financing alternatives, the company's CFO, now a NextLevel team member, along with top managers decided to pursue a convertible debt offering. A shortage of high-quality convertible debt offerings in the financial markets at that time gave the company an opportunity to access this market on favorable terms.

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NextLevel Insights

Have a clear picture of your end goal

Thoroughly examine your reasons for wanting to raise capital. Ensure that the assets or initiatives you want to invest in are in line with your growth strategy. Beware of getting locked in to a preconceived idea of what you need. Sometimes adjusting the way you do business can free up cash for those investments without your taking on more debt or dilutive equity.

Understand what types of financing you're eligible for

Early stage companies still funding losses may only be able to access angel or venture equity financing or a form of "non-bank" debt structured to address a high risk profile. As your company matures and becomes cash flow positive, more traditional debt becomes an option. Evaluate the various forms, costs and risks of debt financing and debt/equity hybrids to ensure alignment with your near and long-term objectives and risk appetite. Depending on the stage of your business and other factors, public debt or equity offerings might also play into your mix of options. For many profitable middle market and larger companies, private equity provides another means to fuel growth while creating liquidity for owners. Factors such as your growth strategy and risk, stage of company, competitive positioning, stability of your cash flow, cyclical nature of your business, market conditions, and your current capital structure will all affect your options to finance your growth.

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The CFO worked with the company's investment bank to create an attractive private convertible debt offering. The company's strong financial position, along with conditions in the financial markets, allowed it to raise the capital it needed at a low coupon interest rate of 2.25 percent and a high conversion premium of about 45 percent.

By combining this financing with existing cash, the company was able to complete the acquisition. This was seminal to the company's long-term success, as it provided the basis for the company's continued strong growth in both revenue and profit and over time drove its stock price significantly higher.

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Prepare a three-year forecast of your capital needs

A critical factor in determining your optimal mix of debt vs. equity financing is the reliability and predictability of your cash flow. Put together a cash flow forecast to determine the amount of capital you will need over the next three years. Look at the whole pool of capital the company will need for ongoing operations as well as for organic and acquisition growth. Keep this forecast up to date, reviewing it at least quarterly. This will also ensure you are anticipating capital requirements with enough time to access the most appropriate form of financing, as this can take several months to complete depending on circumstances.

Look for the appropriate mix of financing

The equity/debt trade-off revolves around risk and cost. Factors influencing your mix of equity and debt financing are your stage of business, your growth forecast and type of investments needed to fuel that growth, the expected return and return timeframe, the risks, and your comfort with either adding more debt to the company or the dilutive effect of an equity infusion. Given the much higher cost of equity, start by determining the amount and structure of debt most appropriate, and available, in your circumstance.

Match the maturity of the financing with the timing of strategic need

Use your strategic plan and related forecast to help guide financing decisions. For instance, avoid funding long-term capital needs with short-term financing. It may be tempting to fund long-term structural capital needs with less expensive short-term financing, with the assumption it can be rolled over at each point of maturity. However, when the debt matures, markets or situations may have changed. Refinancing may be considerably more expensive or not available. By keeping your strategic plan and capital requirements forecast current you will be better prepared to make the optimal financing decisions for your company.

KEYS TO SUCCESSFULLY CAPITALIZING FOR GROWTH

- **Your end goal:** Is it in line with your growth strategy?
- **Your financing eligibility:** Do you understand what types of funding your company can get?
- **Your capital needs for growth:** Do you have a current and comprehensive three-year forecast?
- **Your financing mix:** Is it the appropriate blend of debt and equity?
- **Your debt maturity:** Does it match the timing of strategic need?

"CAPITALIZATION PLANNING NEEDS TO ALIGN WITH THE COMPANY'S GROWTH STRATEGY AND OUTLOOK FOR SUCCESS."

Before deciding on a new capitalization structure, be sure you have considered your true strategic need and fully evaluated your options.

More Information

To learn more about how NextLevel can help you successfully capitalize for growth, call us at (800) 833-NEXT or email info@nlbev.com.

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BUILDING ENTERPRISE VALUE