# Ambitious Entrepreneurs - Exploding the Myths of Private Equity Financing

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Plenty of myths surround private equity investors. For example, some business owners fear that, if they partner with a private equity group, it might make off with the value of their company by buying low and cutting them out of the rewards when it later sells the company at a premium.

This kind of concern generally is unfounded. Private equity can be an excellent way to obtain the funds and expertise you need to grow your company. Before taking the leap, however, you should know the facts about these types of investors.

**Private Equity Basics**

Private equity investors buy shares in a private company intending to help grow and, eventually, sell the business. Limited partners provide the funds, and general managers select and manage the investments. Private equity groups usually take a controlling or significant interest in companies in one of three ways:

- Venture capital. Here, investors focus on early-stage companies expected to produce strong revenue in a few years, or later-stage companies that are likely to generate increased profit in a year or two.
- Buyout and acquisition financing. Private equity investors use a new business plan and, sometimes, new management to improve a company's financial performance.
- Expansion or merchant banking capital. With this approach, investors focus on established companies expanding their operations or entering new markets.

**Shared Control**

A partnering company can use the private equity group's cash infusion to launch new products, make acquisitions or pursue other growth opportunities. Selling to a private equity investor doesn't mean losing control of your company. Owners generally retain a substantial interest in the business and, thus, also benefit as the company grows and is eventually sold.

In fact, selling less than half of your company allows you to retain full control. Even if you keep only a minority interest, you may be able to work out an agreement with the investor that keeps operating and strategic decisions in your hands.

**Early Exits**

Another misconception among some business owners is that private equity investors are only interested in their exit strategy. It's true that these groups realize a profit when they sell - so they can't be expected to hold on to an investment forever. However, they typically expect to work with your company over a period of five to seven years.

When it's time to sell, you may even have alternative exit options. You might be able to use bank debt to repurchase shares and recapitalize your company, find a new private equity investor to guide you to the next level of growth, or raise capital from a strategic partner.

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**Importance of Expertise**

Getting a fair price for shares in your company is vital to a successful private equity partnership. Before you seek financing, work with a professional business valuator to determine your company's current market value.

But price shouldn't be your only criterion for a private equity partner. You don't want to give up a chunk of your business to a high bidder that doesn't understand your company and industry, and that may have unrealistically high expectations for growth. This type of relationship is likely to sour when expectations can't be met. Instead, partner with an investor that shares your goals and understands the challenges you face.

Many private equity groups specialize in particular industries - so look for one with multiple business investments in your sector. Expertise investing in similar companies means your partner may be able to recognize patterns that aren't obvious to your management team. The private equity group also can introduce best practices from other businesses and give you access to a network of professionals to help - from recruiting talent to business partners.

**Know Your Goals**

Private equity investors can help your business grow in ways that you would never be able to on your own. A thorough review of your strategic plan, the market environment and your other financing options will enable you to decide if private equity is a viable option.

**How to Interview Potential Private Equity Partners**

The success of your private equity partnership likely will come down to such basic issues as shared goals and mutual trust. When interviewing potential partners, make sure you're comfortable with their answers to the following:

- How "hands-on" will you be in running my company?
- Which individuals at your firm will I work with?
- How many seats will you take on our board?
- What happens if the company doesn't meet growth targets?
- How will you support our business - in bad as well as good times?
- What industry introductions can you provide?
- In what other companies in our industry have you invested?
- How much capital is available to invest in my company?
- How long do you traditionally hold your investments?