MULLEN & COMPANY, INC. • 1582 ASYLUM AVENUE • WEST HARTFORD CT 06117 • T 860-232-7417 F 860-236-2576

MULLEN

jemull@msn.com

The Perfect Executive Summary

How do you measure perfection? That's easy, in the realm of raising capital: it is when capital is raised in a timely manner, on attractive terms and at a high valuation. Like most things in life, perfection is rarely achieved, and most young but successful companies once experienced their own rocky beginning and had to deal with the challenge of raising capital. To make this process just a bit easier, we recommend that a firm prepare an Executive Summary for use with prospective investors *prior* to providing them with a complete business plan.

This is our recommendation, based on many years of advising companies seeking to raise capital, or more recently, as managers of the Brook Venture Fund, which invests in early stage companies. The investor we refer to in this memo is the institutional investor, typically the venture capital firm, sophisticated 'Angel' investor or 'Angel' Investment Group.

Before you can prepare an Executive Summary you need a business plan from which the Executive Summary will be extracted. The Executive Summary should only take a few hours to prepare provided that your business plan is in order. So here are our suggestions for preparing what we believe is the *Perfect Executive Summary*:

1. **The Eye catching Intro**: The first paragraph of an Executive Summary should be <u>compelling</u> and capture the reader's attention. Take your best shot. Play your strongest card by stressing that single feature of your business that is its most eye-catching and distinctive characteristic. Don't rely solely on what *you* think is your strongest feature; ask others to tell you what they think. Here are some examples:

"The replacement of textbooks with a whole new learning paradigm begins this Fall at more than 30 colleges and universities with the first time, class-room use of EduSmith's internet-based electronic textbooks. The cost of electronic vs. printed text is low, the enhanced learning features are high, many of which are much more difficult to obtain, and the target market is well defined. "

"LitmusWorks was profitable in its first year, earning $65,000 on sales of $650,000 last year, and will generate profits on sales projected at $4 million this year and $9 million next year. For a high tech software services company, the Company's ability to be profitable while growing at a high rate, is enviable."

"When our missionary salespeople call on restaurants that are using one of the 2-3 national brands, they try ours, and 6 out of 10 restaurants switch and begin ordering our product through their distributor. The reason? Taste and appearance, never price. We now have 30% of the New England market and are expanding down the East coast. Does the consumer like our product? We have more than 10,000 testimonial letters on file received from consumers over the 5 year life of the company."

2. **Business Definition**: Your second paragraph should define your business, stating clearly what your product or service is, and for whom it is targeted.

   > "Jamesco manufacturers 1/2" to 2" stainless steel check valves for the petrochemical industry. You should then expand on the products or services and the variations so that the reader has a full appreciation of the company's breadth of product line.

   This should be a <u>short</u> . Any paragraph containing excess words, most plans and executive summaries are guilty of, dilutes instead of enhances the impact you are seeking. You should also talk about products you plan to develop.

3. **The Offering:** Right up front indicate how much capital you are seeking, and to what use the proceeds will be put to. This quickly allows the reader to assess the financial parameters of the deal and frames what follows.

   Also indicate a "range of value" you place on the company, so the reader is aware of what equity interest they may receive for the proposed investment. Most early stage firms are reluctant to do this as they are afraid of putting too low a value on the Company, or conversely, too high a value, thus discouraging potential investors. That is why we recommend a range, albeit a rather wide range, with some discussion of the basis for such a valuation.

   One startup firm we met with placed a valuation of $200 million on his firm. The industry was municipal waste treatment systems, and nothing short of a miraculous system would warrant such a valuation. A conservative valuation might not be harmful at this stage. First, it will show that you are reasonable, and an investor wants to invest in a company run by reasonable people. They know that your initial estimate of your firm's valuation is not a firm figure, and that they will probably have to compete with others that may be reviewing your offering, which could bid it up.

   If you've ever received a catalog that precedes an auction of fine art or antiques, there is usually an estimate given for the expected bid or range of bids. They are often lower than what the final bid comes in at . . . which stimulates the bidder's interest in either attending the auction or submitting a bid. The key is to get the firm interested in *participating*, and not discouraging interest too early.

   Some firms prepare an 'offering' which states the price, terms, etc. of an offering. More often than not, this turns off an institutional investor, because it almost certainly says that the offering has been prepared from the Company's perspective, not the institutional investor's. It also says that the offering is intended for individual not institutional investors.

Not only must the investor study the business and decide whether they are interested or not, they know that they must be prepared to negotiate against a somewhat entrenched thought process that went into preparing such an offering document. Most will simply 'pass'.

4. **Management**: Probably management is the single most important part of an Executive Summary in the eyes of most investors. You should look for an imaginative way of describing your management. For example:

> "The four key managers of the firm, while only having worked together for 2 years at Xylo Corp., have worked together in prior firms. They have built close working relationships that have previously been tested under the strain of managing and growing an early stage business or product line within a large company. One of the board members previously was the President's reporting executive at a prior company, so that relationship is also well developed.

Your management should have balance: a visionary who is the driving force, an experienced operations person, a technologist where appropriate, and a sales/marketing executive with a track record. Also absolutely essential is someone who has administrative and financial management experience. A CFO is probably overkill within an early stage company, but where millions are to be placed in the hands of an entrepreneurial group, the question will arise as to who can manage the funds, the books, and be accountable for the use of proceeds. Sometimes a part time CFO can be engaged, but within the team there must be a responsible manager type.

If you have a void, fill it before you seek financing. If you cannot afford to fill the void prior to funding, at least identify the person who has agreed to accept the position upon funding, and who is willing to meet with capital sources.

5. **Financial Performance**: Too many executive summaries place this at the end, whereas most investors want to know what the expectations are for the company in terms of how large will the firm become, and how soon will it be profitable. We recommend using a summary table that shows one or two years of historical performance, and five years of projected performance, and only 2-3 key numbers. For example:

Figure 1: Actual and Projected Revenue & EBIT (FY1997-2003)

	1997	1998		1999e	2000e	2001e	2002e	2003e
Revenue								
Gross Profit								
EBIT								

A brief explanation should accompany the table, including what events might be the cause of a projected spike in revenue or change in profitability.

Here, as anywhere in the Executive Summary, you should take advantage of the opportunity to relate an anecdote that breaks up the monotony of most business plans:

> "Early in 1997 the Company wanted to raise equity but its board vetoed the idea until the Company proved that it could operate profitably, something unheard of in the internet industry. During the 3rd and 4th quarters, the Company managed to be profitable in 4 of the 6 months, satisfying its board's mandate. Thus the Company is confident with its ability to attain the profit projection."

How soon should your Company show a profit? That depends on your type of company. If yours is an exceptional venture, i.e. within the top 1 or 2 % of companies that venture capitalists look at, then you might show losses for more than 1 or 2 years. Biotech companies typically show losses for many years. But we rarely will consider a company that cannot become profitable by the 12th month from funding.

6. **Market**: By now you should have the reader's attention, and he/she is steeled to the task of reading the rest of the Executive Summary or requesting a copy of the full business plan. Now you should briefly describe the market, referencing the source of each statistic or number you present for credibility. You should focus on the market size and growth rates *for the segment in which you will be competing.* You should also indicate who the competitors are within your market segment as well as those firms that might logically enter the market in the future. A large firm entering the market in the future might concern you, hence you may be reluctant to mention them. The investor sees it quite differently . . . such a firm might possibly be a strategic partner or acquirer for the company, which is very important to the investor's concern for an exit opportunity. Also a large competitor would add credibility to what you are introducing, and might accelerate acceptance of your product or service.

   You should briefly describe your firm's competitive advantage, if any. This might be on a regional basis, or within a market segment which you might enjoy acceptance. Finally, you should describe how you plan to address or expand your sales activity within your market, and what resources will be required (personnel and capital, etc.), and how you propose to obtain them, particularly if resources such as highly trained technical personnel are required.

7. **Technology**: For companies in which technology is a key component, describe it and how you plan to remain current or ahead of the rest of the industry. If this is a key aspect of the business, say what you can about it, but be sensitive to the fact that a confidentiality agreement may not have been executed with the reader of your Executive Summary. If technology is a critical part of your company's appeal, you might wish to place your description of the technology nearer the beginning of the Executive Summary.

8. **Closing Paragraph**: Why should an Executive Summary end on a flat note? None of your sales letters do, nor does an appeal to anyone that you are seeking a favorable decision from. Therefore this should be a short paragraph that invites action from the reader, suggesting a

meeting, a conference call meeting (in which others might participate that couldn't attend a meeting because of cost, distance, etc.).

Other Tips:

Appearance

The Executive Summary should be attractively presented, with the occasional and consistent application of bolding and italicized type, indenting, etc. If you are unskilled at this, the tendency is to overdo it; therefore when you do this, do so in an attractive but understated manner. Have others look at it solely from an appearance point of view and give you their opinion.

Target your Recipients

Don't "broadcast" your Executive Summary, by sending it to a large number of venture capital investors. That will lead to overexposure. Rather, do your research on firms and select those you believe might have an interest based on their stated criteria, past investments, etc. Try to obtain an introduction, although that is by no means required. Try to enter at a fairly senior level, i.e. a partner, and try to be put in contact with a partner that focuses on your industry or technology. Speak with them by telephone first, and *if* there is interest, offer to fax them an Executive Summary, but not the full business plan. In your fax, suggest a few dates (not too many) that you are available for a meeting. Appeal to their sense of wanting to 'discover' you and *not* suggesting that you will be in town on such-and-such day as you have other meetings (implying with other venture investors). No one likes to be part of an 'auction' process and some may decline when they sense that such a process is underway.

There are a number of categories of capital, defined by the stage of funding and the amount sought. The following is only a guide that we use, although others may apply quite different rules.

	Sales	**Funding Sought**	**Sources**	**Examples**
Seed (pre-revenue)	$0	$50,000-250,000	Management, families, friends, former co-workers, "angels", and a few small funds or family offices	**Architect Fund** Numerous, Deltech, Fayerweather; groups like Breakfast Club
Early Stage	$200,000-500,000	$250,000-1 million	Angels, Investor groups, very few funds	**Architect Fund** Northbridge, Walnut, Incus Group,

Early Expansion Stage or First Stage	$500,000-$2.5 Million	$500,000-2 million		**Architect Fund**, Commonwealth, Corning, Kestral, Pioneer, One Liberty, Zero Stage, Vimac,
Second Stage	$2.5-$5 million	$2 -5 million	Venture capital funds, SBIC's	Many
Third Stage	$5 million +	$3-10+ million	Venture capital funds	Advent, TA, Summit
Industry specific	$500,000-10 million	$500,000-3 million	Venture capital funds	Ampersand, Atlas

Note: Architect Fund is currently in its fund raising stage.

We have seen early stage companies receive $7 million from institutional investors, however these were exceptional ventures.

In addition, corporate investors are another source of funds, ranging from a few hundred thousand dollars on up into the millions. However corporations are not usually well equipped to consider venture investing and can consume inordinate amounts of time . . . yet they are often the most appealing investor. They can leverage your business into markets it would otherwise take years to penetrate, share technology with you, and might be more willing to invest at a higher valuation than venture investors. But CFO's of such companies usually dislike having to book an equity investment on their balance sheet and can be counted on to vote "no" when it comes up. But the greatest deterrent should be that they will meet with you, pump you dry as they seek to understand your business and your technology (so be sure you have executed non-disclosure agreements), and call repeatedly for meetings . . . and nearly always decide not to invest. Beware!

> One startup firm we've spoken with which is at the pre-revenue stage, is in discussions with Intel. Intel is very interested in their process, and has said that they might do a substantial part of the round of financing provided that a local (New England venture firm) will be the 'lead' investor. A strong strategic investor will greatly add to the appeal of the investment in the eyes of others.

Style

The writing style of your Executive Summary as well as your business plan is very important. Avoid the excessive use of adjectives or superlatives, something most executives preparing business plans are guilty of. The reader becomes numb and soon begins to subconsciously discount what is being said. Build credibility through frankness and a simple choice of words, presented in a direct, somewhat factual style.

There is plenty of time to ‘sell’ in your cover letter, over the phone, and in person. Use the active more often than the passive tense.

The Goal: Set up a Meeting

However you contact the investor or venture capital firm, you should be working towards the goal of meeting with them face to face. That is very difficult to accomplish and you may have to resort to all kinds of methods to entice them. Also, start promptly, and be persistent. Don’t wait 10 days after you’ve sent the plan and heard nothing. Call a few days later, and continue to call, as each time you do, the executive summary or business plan rises to the top of the pile. Some deals get more attention simply because of the persistence of the company seeking funding.

You should offer to meet at their offices, not yours, unless they offer to come visit you. The average investor or venture capitalist is terribly busy, and can more efficiently work when companies schedule their first meeting at their office, not the company’s office. You might prefer to have them come see your product, your plant, your working model, etc., but the benefit of that is outweighed by the greater likelihood of scheduling a meeting much sooner, and the possibility that the person you are speaking with will invite one or more of his/her colleagues to join the meeting, thus increasing the likelihood that interest will develop. Often the person you initially speak with may not have sufficient interest in pursuing the financing, but one of his partners might. That has happened within our firm on more than one occasion.

Getting that meeting will require your marketing charm. Sometimes the comment that might work is something like, “I plan to be in town for a meeting on Thursday from 1:00-2:00, and would like to come by either before or after that meeting to spend 20 minutes with you, to ‘put a face together with the plan you are reviewing’” You might attach your lawyer’s name to the 1:00-2:00 meeting, or whichever person might have referred you to the particular funding source . . . which might create some sense of obligation on that person to meet with you.”

Look for a ‘Sponsor’ and Push for an Answer

Within the investment firm or group you are speaking with, find the person who is willing to be a ‘sponsor’ of your deal. That person will campaign on your behalf. If the first person you contact doesn’t seem to connect with you, either through a demonstrated apathy or a personality difference, it’s not easy to switch, and it may be out of your hands, but you might try. If you haven’t connected with someone on a personal level, it is unlikely that their firm will fund you.

> A few months ago we met with a firm which had come to me through a referral source. I and one of my partners visited them and I was left uninspired. My partner was quite taken by it and I

> shifted the responsibility for reviewing the firm to him. We are currently in the process of funding the deal.

Persistence is Essential

Institutional investors are criticized for how difficult it is to get them to with an answer. A very few firms are timely in their response, but many are so overloaded with funding requests that they are forced to use form letter responses, or simply don't respond at all. Some simply do not want to say 'no'.

Finally, and here is the real secret of getting funded. We mentioned it above, but it bears repeating: be persistent while not being annoying. Always end the conversation with some action item such as a meeting, not simply, "Well, I look forward to hearing from you . . . " because the investor is *really* looking forward to getting off the phone and back to what he/she was reading or talking about with others prior to your call. So, you should try to lever their desire to get off the phone into scheduling a brief meeting with you, when you'll have their undivided attention.

> Some people have good interpersonal skills, and their persistence is cloaked in a style that is pleasant and intriguing. Others, perhaps with more worthy ventures, don't communicate as well, and need to develop their 'telephone pitch'. Practice on a colleague or an advisor such as your attorney or accountant, who you have a close enough relationship so that they will give you good feedback.

Frankly, how aggressive you are in how you go about raising capital is a reasonable proxy for how aggressive you are likely to be in driving your business forward! Your goal should be to keep your venture at or near the top of the investor's pile, and move it out of the pile and into a termsheet. Your persistence will win you either their respect or their coolness, depending on how you do it, and how receptive they are to your calls and their interest in your venture. Our advice: risk it and be persistent.