

CAPITAL SOLUTIONS NEWSLETTER...

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With equity capital scarce, we highlight several financing alternatives gaining prominence. Plus, a new model for increasingly agile startups: begin as a temporary organization with the sole purpose of discovering a profitable business model. In addition, BusinessWeek's list of the best cities for startup companies contains some stunning omissions, Venture Capitalists trash-talk their peers; and a pair of not-to-be-missed articles on the financial meltdown. Lastly, a tongue-in-cheek private equity glossary (where "S" is for sarcasm).

Equity Financing Alternatives

Given the limited access to equity capital -- and lower valuations if you can find investors -- a variety of other possibilities are emerging as options for smaller and early-stage companies. Among these are mezzanine loans, royalty financing, and a new breed of Community Development Financial Institutions (CDFIs).

Mezzanine financing becomes increasingly popular when valuations are low, and equity is expensive. These investments are generally unsecured loans that, like equity capital, can be used for growth or recapitalization - often with a small equity position attached. A [recent article](#) does a pretty decent job in laying out the fundamentals of mezzanine capital for entrepreneurs - with one catch: ignore the minimum EBITDA of \$5M, for there are mezzanine funds out there loaning to companies with far lower EBITDA levels -- one just has to know where to look.

But for many early-stage companies who have yet to reach profitability, any EBITDA requirement is a killer. Among the other alternatives for entrepreneurs is [royalty-based financing](#), which allows a company to borrow against a future revenue stream. Similar to purchase order financing -- but usually not constrained to a specific customer or order -- royalty financing provides another alternative to growing companies, and can help weather the current equity markets.

Lastly, a number of small institutions -- community banks, credit unions, and some nonprofit groups -- are applying for CDFI status as an 859 lender (which provides access to federal money). To do so, they must agree to direct a majority of their loans to low-income communities and individuals, which can be helpful for startups in either urban or rural locations. A [WSJ article](#) notes that CDFIs "have been increasingly active in lending to startups" since the credit crunch, and their numbers are growing.

Winsome, feisty startup ISO customers, profits, cities...

A fundamental change for many early-stage companies is their increased capital efficiency: it simply takes less money (and time) to bring a product to market, and even to start to achieve scale. An [article](#) in the New York Times highlights this trend towards lean-startups, with a fascinating quotation that details the transformation: "*A start-up*" says one practitioner, "*is a temporary organization designed to discover a profitable, scalable business model.*"

While this view of entrepreneurship sounds a little like a starter marriage, where one is constantly looking to trade-up business models, it's highly customer-focused. Instead of "*Build It and They Will Come*" it's sort of "*Find Them First and Build What They Want.*" Lean startup advocates:

...advise quick development of a "minimum viable product," designed with the smallest set of features that will please some group of customers. Then, the start-up should continually experiment by tweaking its offering, seeing how the market responds and changing the product accordingly.

The ideal place to explore a lean startup might include BusinessWeek's recently published [slide panorama](#) on the top 10 cities for startups. Locals will be pleased to see that Boulder, CO rated the [top slot](#). But beware, the methodology for these rankings produced some odd results. Cities that ranked above the usual leaders San Francisco and Cambridge included Boca Raton, FL (#2), Bend, OR (#4), and Irvine, CA (#5). Bonus points if you can name the state in which city #8 Franklin resides. And despite the [recent binge](#) from New York City, neither it nor Austin, TX even make the list. So don't call the moving company quite yet.

VCs trashing VCs

Among the odd juxtapositions in the venture world, I would add Ben Horowitz, half of VC firm du jour [AndressenHorowitz](#) quoting rap artist [Dr. Dre](#), in [this post](#) trashing many of his fellow VCs for their bad behavior towards entrepreneurs.

Now VCs trashing other VCs is a time-honored practice with many VC's attempting to establish some entrepreneurial [street cred](#) -- as venture professionals trying, albeit desperately, to hold onto their startup roots (or pretend they had them). Many VCs regularly chide their colleagues for (among other things) [arrogance](#), [limited slots](#), and [claiming ownership](#) -- and this is from the VCs who I think are really good. Many VCs take pain to emphasize their non-venture roots in their blogs ([Both Sides of the Table](#), and [Seeing Both Sides](#)) while distancing themselves from many of their peers. And an entire [web site](#) got into the business purely to democratize venture criticism.

But this smackdown seemed a little gratuitous, particularly when you have been a VC for, oh, less than a year with no track record (sort of like the young MC). But unlike hip-hop, trashing your colleagues is rarely a good way to build deal flow and establish syndicates. Mark Solon at Highway 12 even responded with a [posting](#) in defense (and note a few VCs popping up in the comments). But who knows, maybe we'll see Horowitz as a board member of one of Dre's [business ventures](#) - the trash-talk might tone down under a little influence of [the chronic](#).

Reading List: Tim Geithner and the Financial Crises

At a reader's suggestion, I am going to try to highlight longer articles or books that I think are worth some extended attention (tough in a Twitter world, but worth a shot). Recently there were two compelling articles on Treasury Secretary Tim Geithner, one in [The New Yorker](#), the other in [The Atlantic](#).

For, whatever one's politics, the financial meltdown and its subsequent rebound are fascinating financial and personality topics. Geithner worked across both Republican and Democratic administrations, and the plan he has championed both at the NY Fed and as Treasury Secretary has worked far better, while costing considerably less, than both critics on the right and left believed it could. Yet it (and he) remain highly unpopular, and the reverberations still threaten to undermine current economic policy and will be a considerable factor in the upcoming midterm elections. Both articles are fairly long, and well worth the time.

And B is for Bonehead...

From the good-humored folks at Better Capital in the UK comes [Private Equity A-Z](#), an amusing glossary of terms. My personal favorite is probably:

D: DCF analysis (aka Deceit by Computer Fraud); A highly scientific and extremely unreliable method of valuing companies...

And if you have not seen it before, it's worth revisiting Bessemer's [Anti-Portfolio](#), with wonderfully self-deprecating descriptions of how the firm passed on an early-stage investments in Apple, eBay, FedEx, and Google. And does not quote Dr. Dre. .

Alexander Ooms | Managing Partner

alex@clearcreekpartners.com

303.731.2960

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