Equity Capital Raising and Usage – Webinar One

MILLHOUSE

Please study the following 3D-strategy model developed by Dr David Millhouse©

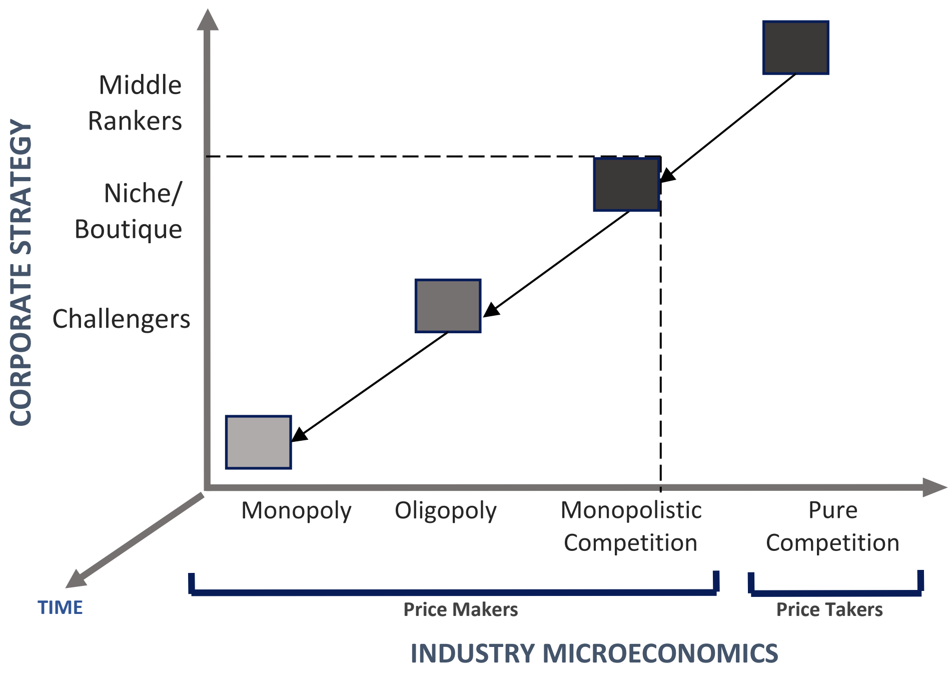

FIGURE 1.12.1: The Dr David Millhouse 3-D Share Pricing Model

This 3D model has time on the Z axis, industry microeconomics on the X axis and corporate strategy on the Y axis.

Strategy development, industry economics, and your company's position in this model will and should change over time.

IMPORTANT TIP: *If you undertake a capitalisation process, you should align yourself with investor's interest by seeking an industry position where share prices can be maximised. This can mean significant changes in how the business is managed and directed.*

The Z-axis

Time is important because product and company life cycles are getting shorter and because of the concept of time value of money. Once you start this process, time becomes ever more critical.

The X-axis

….describes the microeconomic groups of industries. Economics tells you what you can do at all in an industry.

Your opportunities in a monopoly are very different from those in price taking mode. Different again where there is limited industry competition and difference where there are lots of entrants, but with methods of differentiation.

It establishes what the company is capable of doing in its market segment
In each of these categories there are different economic fundamentals which place constraints on strategy possibilities but also provide competitive opportunities for those that understand the model.

Where you are on the X axis starts to define your strategic opportunity and therefore your need for funds.

IMPORTANT TIP: *Some companies are like King Canute holding back the tide. No matter how hard you work, you cannot make an economic profit. Many private companies are in this position.*

The Y-axis

….defines how corporate strategy is implemented. It is the "*how*" of the model and feeds directly into your Application of Funds.

IMPORTANT TIP: *Different corporate, competitive, and marketing strategies are required for each of the categories in the vertical axis.*

Where is Share Pricing Maximised?

Most companies looking for capital are price takers-middle rankers.

This sort of business will continue to be unattractive to equity capital providers until they can be positioned closer to the boxed areas. The only exceptions are where very large volumes can be generated.

Companies in this position can still be accounting profitable, provide pleasant life styles, and sustain secured bank debt.

Where a company starts to become attractive to equity providers is once they have migrated to price making, strategy driven mode.

It is usually a multi-staged process to move from "*A*" towards "*B*", "*C*" and "*D*".

To do so requires a multi-year commitment from management; it requires capital investment, and very importantly it often requires a series of changes in the senior management and leadership.

This process is driven by strategy implementation using the application of funds identified in your Business Plan.

The economics of industries generally will push you the opposite way – and especially in a globalised world.

The real unit price of what you sell normally will decline over time – often quickly in technology companies.

Therefore you need constant investment into product development and product marketing.

Share prices are maximised where the opportunity costs to the investors are eliminated. This is at position "*C*" and "*D*".

Financing of Each Stage

IMPORTANT TIP: *Each stage of the migration into the concept of a corporation attracts financing from different parts of the equity market.*

"A" to "B"

Generally, the capital required here is from family and private angel investors, supplemented by various forms of bank and non-bank debt. It is not normally a venture capital investment.
The business usually stays within the control of the Founders and family members in this stage.

"B" to "C"

Generally, this is where the venture capital investor can contribute since it is the expansion of a proven business model to increase the economies of scope and scale in the business.
Original management may need to be supplemented in this stage.

"C" to "D"

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This stage often involves merger and acquisition activity, larger scale financing as the business drives to market leadership position.

The change in the management skill sets required often results in the original Founders moving aside and treating the business as an investment rather than as a place to go to work.

IMPORTANT TIP: *treat your business as your largest investment. This aligns your interests with those of your shareholders and reduces executive performance pressures as the needs of the business change away from the original skill sets which founded it.*

What you must be able to demonstrate: