

Don't Blow The Biggest Deal of Your Life

The Vancouver Chapter of EO
(Entrepreneurs Organization)

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Basil Peters

The First Time I've Told This

- This is the first time I've told this story.
- After almost 20 years in YPO and hundreds of presentations, I know that the most valuable lessons are the ones about real experiences.
- The war stories. The really painful ones.
- Lots of great speakers helped me make millions.
- My goal tonight is to pay some of that back.
- This is my story about the first time I lost several million dollars.

We Started With a Student Project

- The UBC Engineers have always built cars.
- Started as a way to avoid a summer job.
- Ended up as UBC's largest student project (then).
- Three of these students became millionaires from that project.

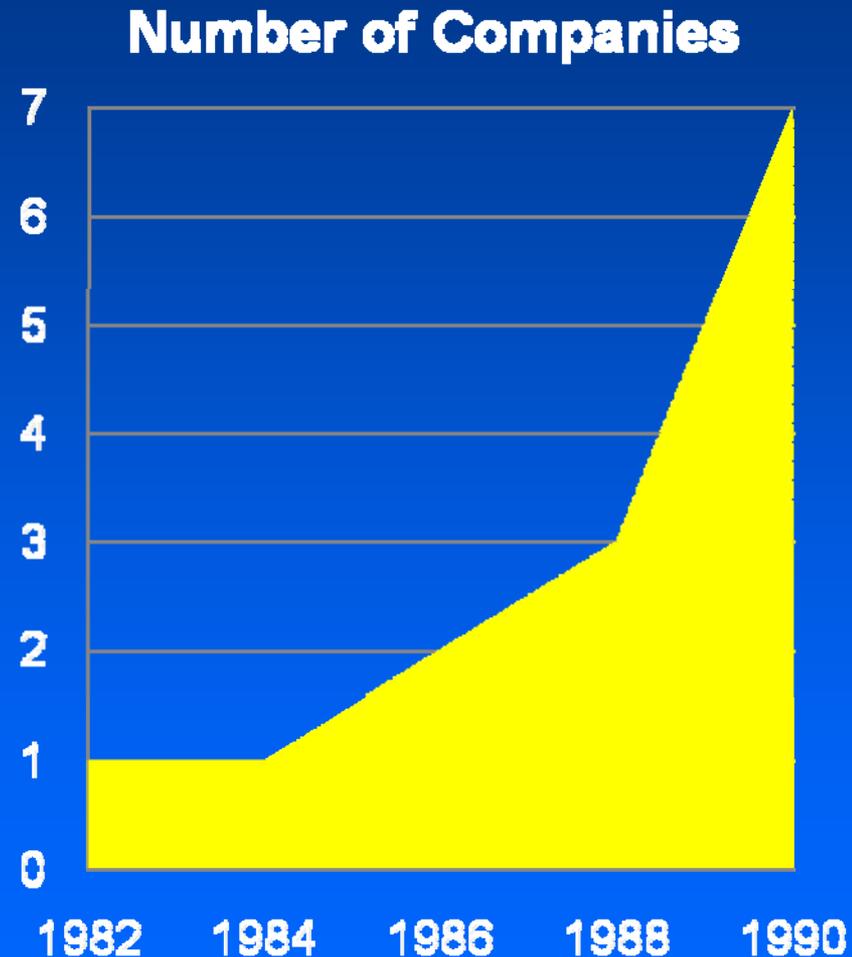


The Original Nexus Engineering

- We started Nexus in our lab at UBC.
- We couldn't borrow another dollar.
- Our strategy was to prevent starvation (or worse, running out of beer).
- Got lucky and found two angel investors who were also excellent mentors.
- Started by manufacturing the central electronics for cable television systems.

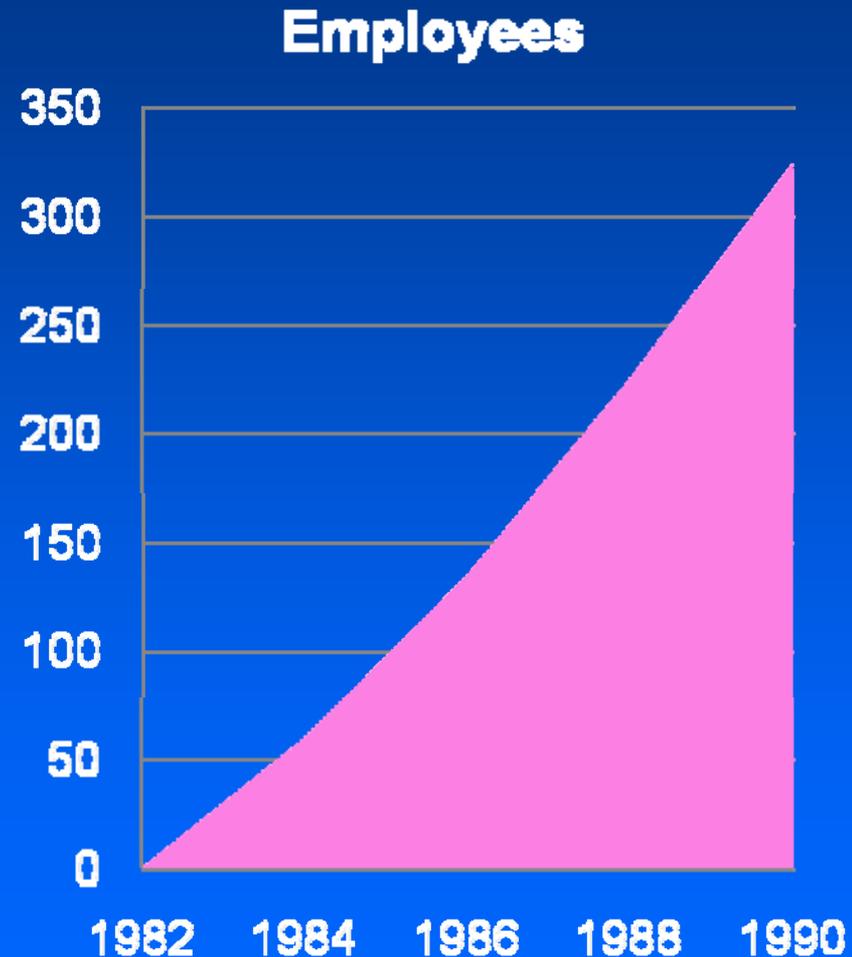
Entrepreneurial Overdrive

- One company wasn't enough fun.
- We had institutional shareholders who wanted us to take more money.
- So we bought three companies.
- And spun out five more.



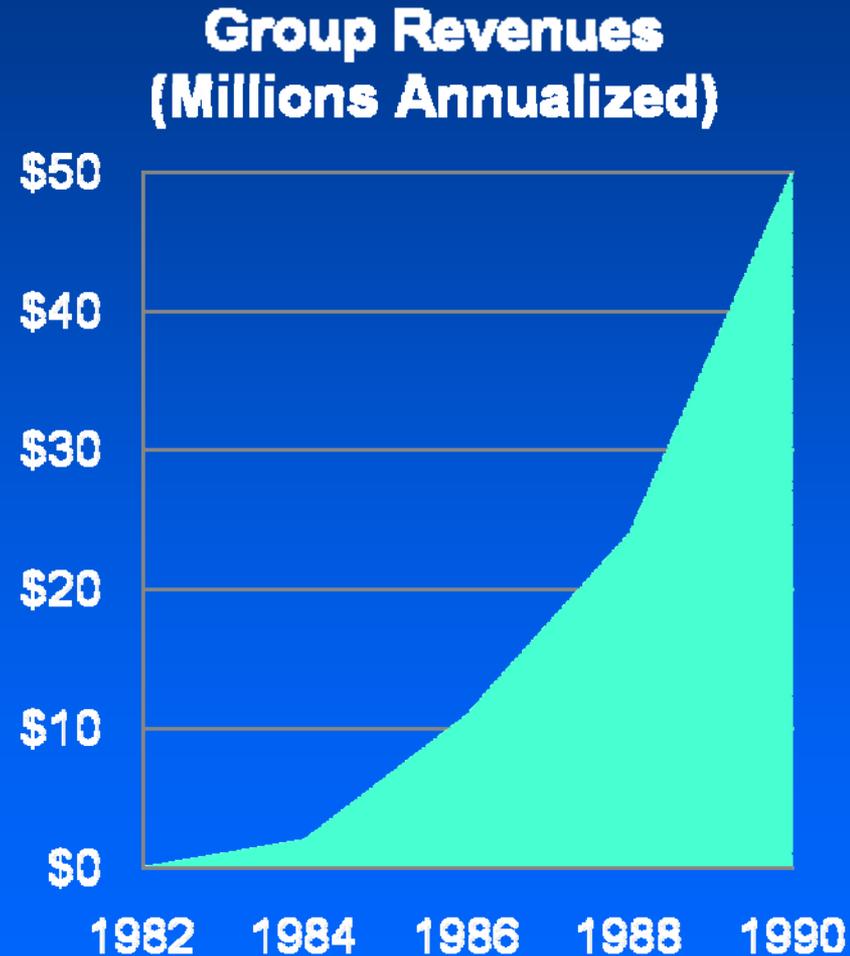
The Team Grew Quickly

- We converted the old Nabob jam factory in Burnaby.
- To a 100,000 square foot tech facility.
- With no walls except for meeting rooms.
- Beer deliveries required two pallets.



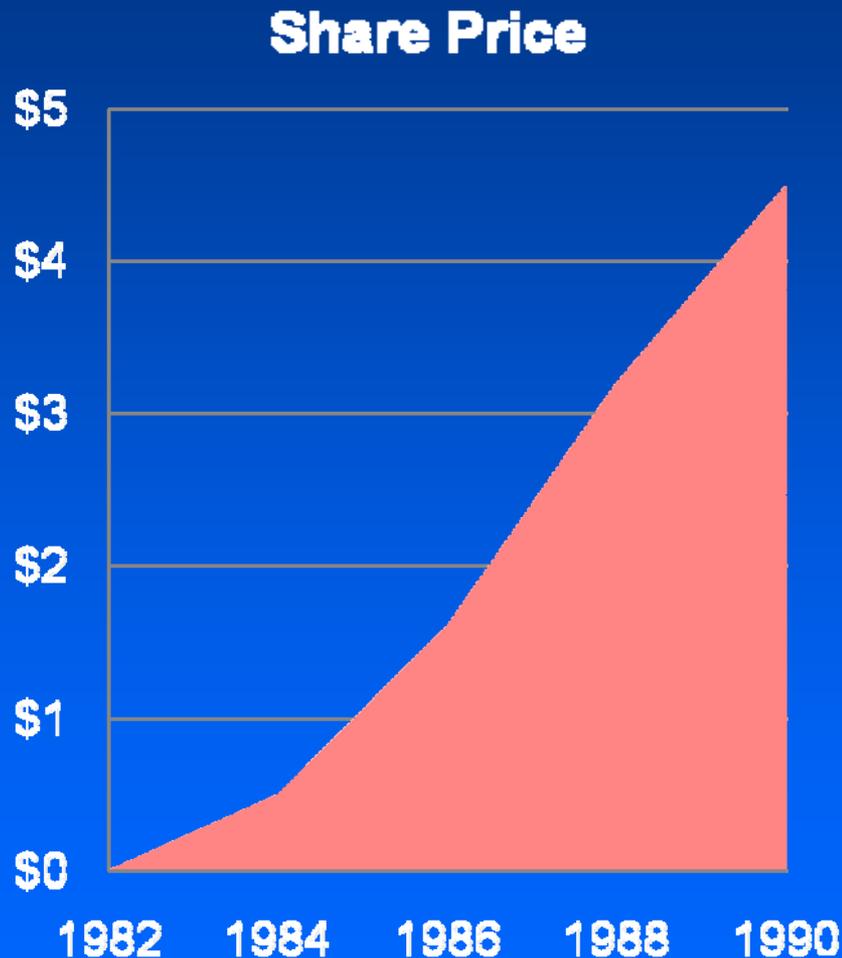
Revenues Grew 200% per Year

- We grew the first company to be the second biggest manufacturer of cable TV headends in the world.
- The smaller companies grew even faster.
- Profitable every year.



The Share Price Tracked Nicely

- We needed external financing to grow that quickly.
- Started with angel investors, then traditional venture capital and finally three institutional investors.

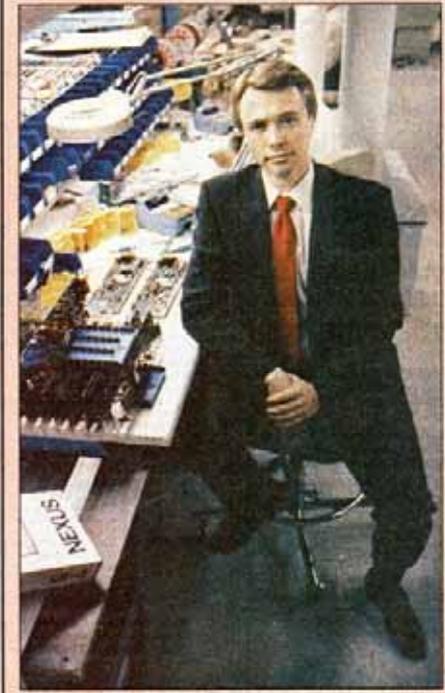


Won Lots of Awards

- Won nine major awards for entrepreneurship:
- Entrepreneur of the Year
- Silver in Entrepreneurship from Canada Awards for Business Excellence
- Business Leader of the Year
- UBC and BCIT Alumni Awards

Business

THE VANCOUVER SUN, SATURDAY, NOV. 8, 1986 ★★★★★



Nexus named top company

Nexus Engineering Corp. has been named B.C. business of the year by the B.C. Chamber of Commerce.

The Burnaby-based satellite, broadcast and cable television equipment maker received the award Friday at a Vancouver dinner.

It is the first year the chamber has made the awards, according to chamber chief executive Bill Guerin.

The awards for the best business achievements are a major thrust by the B.C. Chamber of Commerce to raise and enhance the image of the B.C. business community," said Guerin. "It highlights a select group of private companies which have shown outstanding achievements during the current year."

Nexus Engineering was the idea of a couple of University of B.C. electrical engineering graduates: Basil Peters, who is chairman and chief executive, and Peter van der Gracht, president.

In an interview Friday, Peters said Nexus Engineering will have sales revenues of between \$11 million and \$12 million this year. About two-thirds of the sales will be generated in export markets.

"We are absolutely thrilled about the award," said Peters. "It means a lot to us. We see Nexus as an example to other companies here."

Nexus Engineering got its start in 1982 when Peters, van der Gracht, Tom Holzgale and Marc Phillips founded the company. Two years later, additional capital came from Discovery Enterprise Fund and Ventures West.

The company currently employs 125, according to Peters.

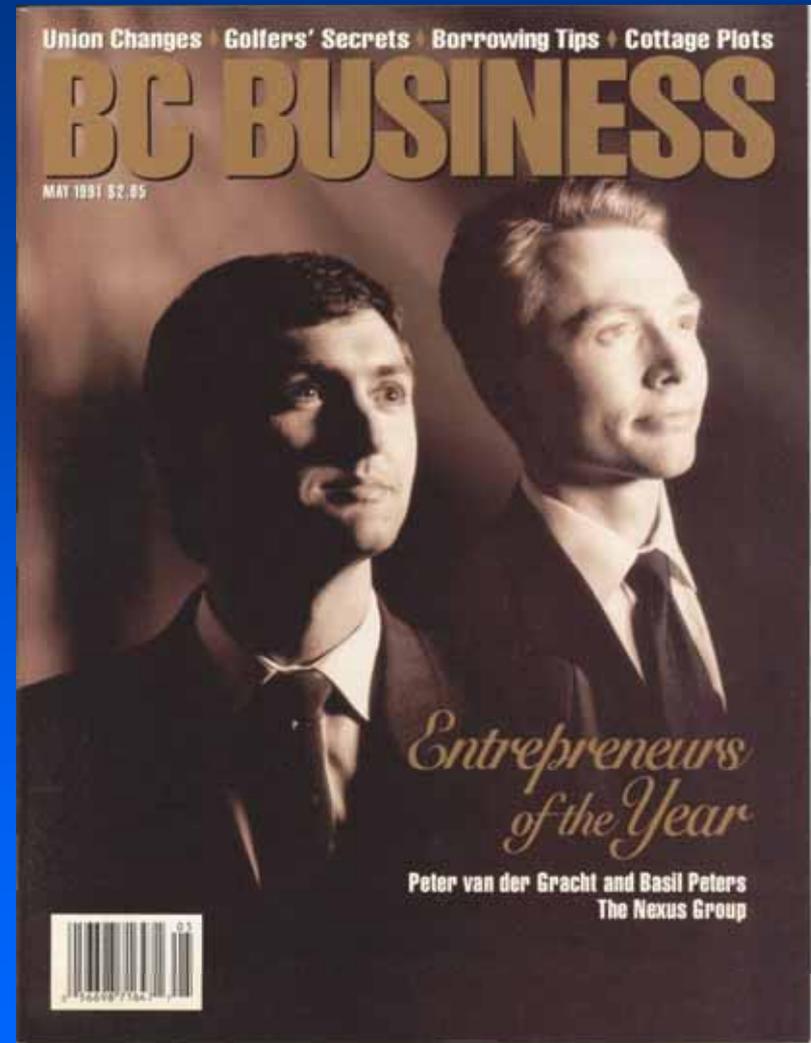
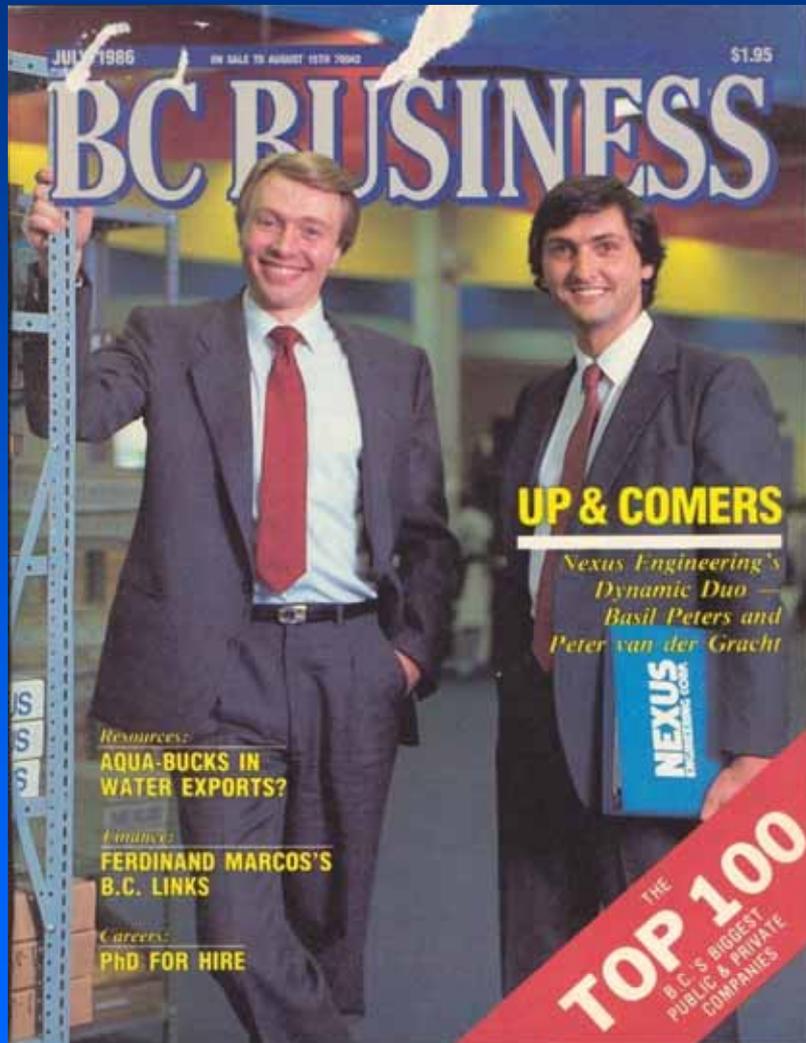
Other winners Friday were:

- Lamford Forest Products Ltd., New Westminster, in the category of business expansion and job creation.
- Wiggins International Communications Ltd. (WINI), New Westminster — community involvement.
- AAA Foods Ltd., Vancouver — agribusiness.
- Flag Shop, Vancouver — services.
- Landco Lumber Ltd., Surrey — manufacturing.
- Solar Systems Industries Ltd., Richmond — exports.
- Lamford Forest Products Ltd., New Westminster — primary production.
- Agri Forest Technologies Ltd., Haldimand — new B.C. product.
- MacMillan Bloedel Ltd., Powell River division — quality of life and physical environment.
- Choi-Na-Ta Growing Products Ltd., Surrey and Lytton — new venture.

JEROLD DREER

AN EXAMPLE for other companies is Nexus chairman Peters' hope for the company and the Chamber of Commerce award. Two-thirds of the company's revenues will be generated abroad.

Generated lots of media attention



Everything seemed to be going well

- Several YPOers warned me that cover stories were the kiss of death.
- After the second cover photo in BC Business several looked downright sorry for me.
- But of course I ignored them.....
- We had 7 companies and were selling in 100 countries – I thought we were diversified.
- But I did worry that things were going too well...

Wham! Our world changed.

- We started Nexus during the 1981- 82 recession.
- People kept asking us how we could grow so fast in a miserable economy.
- We didn't even feel it because we were so small.
- Then, in June 1990, our world fell apart.
- Some guy, yes just one guy, called Michael Milken had invented something called 'junk bonds'.
- That created a real estate crisis in the S&Ls.

What the #@!* is an S&L?

- One day I got a call from my friend, and biggest customer, Ted Rogers. He told me not to worry.
- He said I would hear things in the media about the S&L crisis but that his lawyers assured him the banks couldn't cut off his construction loans.
- The next day I got similar calls from CEOs in the US and the following day from Europe.
- I had to look up what an S&L was.
- It was a "Savings and Loans" but I didn't know what that was either.

Today is almost an instant replay

- The 2000 market crash was an equity bubble – that was different.
- What is happening today is eerily similar to 1990.
- The junk bond and S&L crisis was a debt bubble - just like what's happening now.
- Today it's not junk bonds, it's sub-prime mortgages – just another form of debt.
- Yesterday, Alan Greenspan said he was “mystified” by sub-prime.

I tell others not to worry

- So I told my board that Ted Rogers and the other CEOs said we shouldn't worry.
- Then I went downtown and told my bankers that they shouldn't worry.
- About six months later, I learned what the bank's Special Loans Department was.
- A year later, Ted still hadn't paid me.
- Then I started to worry – a lot.

We worked our asses off

- We were young and naive.
- We thought we could just power through like we did in '81-82.
- We did our best to keep it up.
- But every day things ground down a little further.
- About a year in, I figured out that every day I came to work I lost \$10,000 - personally.
- The other shareholders start to feel the same.

My shareholders want liquidity

- About a year and a half after the S&L crisis,
- One by one, just about all of my shareholders came to me to ask for ‘a little liquidity’.
- We were a private company!
- I had no idea how to provide ‘a little liquidity’ in a private company... during a recession.
- I didn’t even learn what a ‘secondary sale’ was until many years later.

Should have done a secondary

- I realize now, that I should have organized a secondary sale when things were going well.
- It would have provided the founders and the angel investors some liquidity at high share prices.
- Diversifying us and reducing the pressure I was getting at the worst possible time.

Secondary sales, where new investors buy founders' shares in a private company, were rare then, but are much more common today.

Our Only Option – To Sell Fast

- I only had one choice – to find a buyer for one, or more, of the companies.
- We were growth junkies.
- We had never even discussed selling – it literally had never occurred to us.
- So we were starting cold – at the worst possible time – and we didn't have much time.

We didn't have an exit strategy!

We Learn About Exit Strategies

- In one of the worst mistakes of my career,
- We start to learn about exit strategies,
- At the worst time in the economy and at the worst time ever for our companies.
- We had late night meetings to figure out what an exit strategy was and then to design one.
- Our exit strategy was to sell to a big US defense company who wanted a 'peace' business.

Then I Learn About Selling

- My partner agreed to take on all of the day to day operations of the businesses,
- So I could focus 100% of my time on selling one of the companies.
- I worked really hard, often 16 hours a day.
- To be honest, I wasn't very good at it then.
- And the businesses suffered a lot.

The CEO should never lead the exit.

We Build A Sales Funnel

- The strategy was sound.
- Even though I was a rookie, I managed to get three buyers interested – a little.
- For a moment, I thought things were going well.
- That was mistake #3 ...or is it #4?
- One by one the buyers started to drop off the list.
- Until there was just one interested buyer left.
- My plan was to keep pushing to a close.

Mentor to the Rescue - Again

- Once again our mentors rescued us.
- One of our angels had sold several companies.
- He realized we were in big trouble and dropped everything to help us out.
- He suggested we take a big gamble,
- And pay someone (a lot) to leak to our major competitor that we were 'in play'.

It works – thank goodness

- I could not believe that our board approved paying someone a lot of money just to make a phone call. (We didn't have much money left.)
- The strategy worked (this was pre-Internet.)
- Our major competitor came roaring in to make us an offer.
- Just before the last defense contractor went quiet.

Every exit needs multiple bidders!

I foolishly start to feel confident

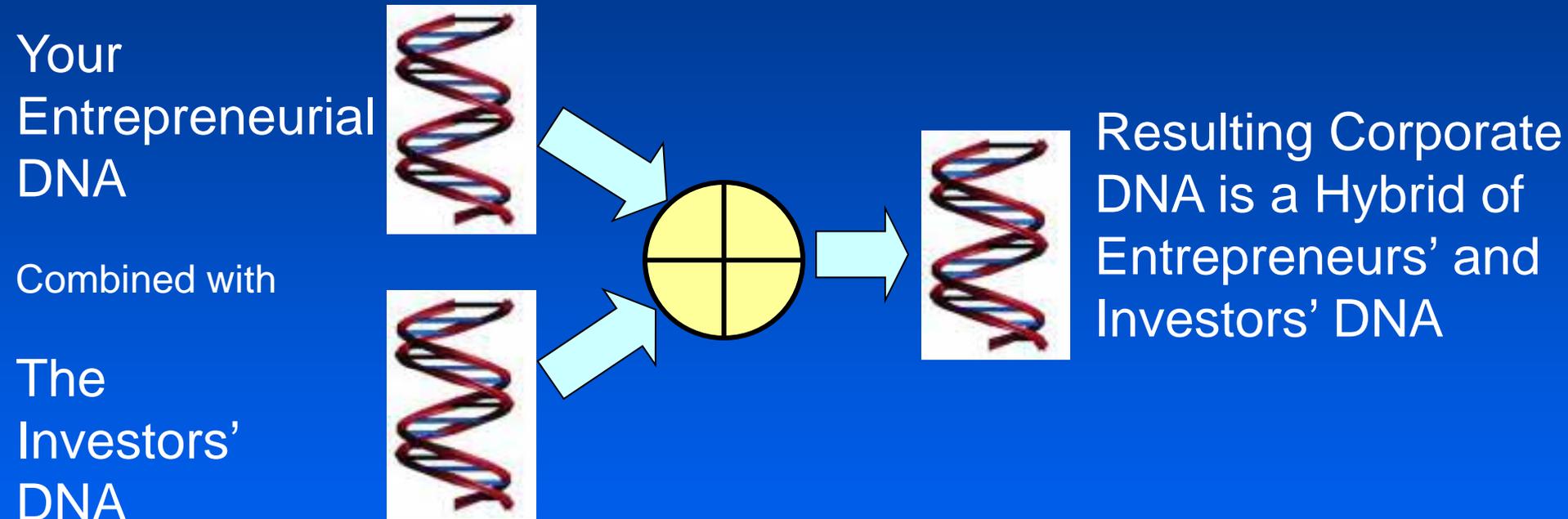
- As the negotiations heated up, I actually started to feel just a little optimistic about our future.
- I was so naïve.
- And about to learn another painful lesson.
- As I was almost killing myself to make the sale happen,
- At the same time, a VC on our board was working on a hostile takeover - from the inside.

We didn't check the DNA

- We'd failed in another critical way.
- We didn't really understand how the math in venture capital funds worked.
- They had invested at around \$3.20 per share.
- And were not going to vote for any sale where they didn't make a 10 x return.

Understand DNA compatibility.

Adding Financial DNA



Check the compatibility first.

And we didn't check alignment

- If we had an exit strategy we would have discovered the serious lack of alignment.
- We would have realized that one of our board members was completely misaligned with the goal I was working so hard to achieve.
- The VC knew we'd all missed this point and was covertly working to kill the deal.

Check alignment at least annually.

Our VCs Hostile Takeover Plan

- We learned later that our VC had a well developed plan to kill the sale to our competitor,
- And then do a wash-out financing to dilute out all of the other shareholders.
- Our angels and the founders would have lost everything we'd spent a decade working on.
- And our VC wasn't 'playing fair.'

A Legendary Board Battle

- The first step in our VC's plan was the board.
- He started to wine and dine other directors and their wives – even ones he didn't like at all.
- Then he scared a couple directors off our board by telling them they were about to lose their houses if we crashed. (That was never true.)
- He asked our CFO for every one of my expense reports. (I'd had the controller fill them out 😊)
- He even tried physical intimidation once.

The VC Tried an End Run

- We had taken on several million dollars of subordinated debt from a big eastern institution.
- One day, I got a call to let me know someone was trying to secretly buy our debt.
- We were offside on some covenants, so if the debt holder wanted to, they could have owned us.
- I managed to convince the decision makers at this institution that our VC was not acting ethically.
- They were good guys and one of them winked.

It came down to a board vote

- I had foiled the VC's debt gambit.
- The boardroom battle raged on for several months.
- They were better – we always played defense.
- I heard through the grapevine that our VC had been saying around town that “he had me”.
- It was all building toward a board meeting where we were going to vote on the offer from our big competitor.

And I ask my wife for one thing...

- As it usually happens in life, it never rains, it pours.
- Around this time we were expecting our second child.
- I sheltered my wife from most of what was going on, but I asked her for just one thing.
- Just one thing – don't go into labor just before the big board meeting.
- I literally went from the hospital to the board meeting.

The Board Vote

- Any of you who are parents know what its like to have a child born.
- I'd been in the delivery room from 2 PM to 7 AM.
- It was an 8:00 AM board meeting.
- I'm pretty tough, but I looked like dog doo.
- Half the board wanted to postpone the meeting at least until later in the day. But I lost that one.
- But I won the big vote - by a single vote.

And I start to feel confident again

- With the board vote in favor of accepting the offer,
- I (foolishly) started to feel a little confident again.
- Our lawyers were working away on the mountain of documents.
- I even took a weekend off to be with my new daughter.
- Then our lawyer said 'Extraordinary Shareholders Meeting'..... What?

The Extraordinary Meeting

- It was a share sale, so it required a super majority of the shareholders to approve the transaction.
(Who knew?)
- No problem I thought. I ordered our regular two pallets of beer and prepared for an un-official, early celebration and shareholders meeting.
- But everyone from the venture capital fund showed up, with one of their lawyers.
- ... and they were all smiling.

What the heck are the Articles?

- I had never read the Articles of our company.
- The VC and a couple of dissident shareholders thought they had enough votes to block the sale!
- They based this on an old set of our Articles they had from their due diligence.
- Luckily our lawyer had updated the articles, and we had approved them. Our lawyer remembered but it took us over an hour to find a copy.

Repair structural defects early!

We rode it over the top

- In the end, we did get the transaction finished.
- I went from being a starving entrepreneur with every cent I could borrow in the company I was running,
- To actually having some investable capital.
- But perhaps my greatest regret was that we 'rode it over the top'.
- We managed to sell for about \$2 per share.
- Two years early we could have sold for \$5 or \$10.

The expensive lessons for me

- It took me ten years to really understand all the things that went wrong on that first exit.
- And even longer to know what we should have done instead at each step along the way.
- The truth is that we were lucky - very lucky.
- I did OK on my first exit. But I could have easily lost it all at least three or four times.
- And we all could have gotten out several times as much money if we had a good exit strategy.

Parasun – an Exit Done Right

- Nexus was my first exit.
- At that point, I didn't even know what I didn't know.
- Luck was a huge factor in completing the sale.
- In the following decade, I helped execute over a dozen exits, usually in companies I invested in.
- When we sold Parasun, we got everything right.

Parasun Background

- New Westminster company in high speed internet.
- I invested \$500k into Parasun in April 2004.
- Became Chairman.
- Signed a contract to execute the exit with a partner and fellow director.
- Organized an offsite strategic planning retreat to:
 1. Build alignment
 2. Develop an exit strategy

Alignment wasn't easy

- Even though I was the only shareholder with cash in the company,
- It was surprisingly difficult to achieve full alignment on the exit.
- Alignment and the exit strategy are usually developed iteratively.
- It's far better to build the alignment and exit strategy in at founding – much harder later.
- Offsite strategic planning retreats are essential.

Parasun's Exit Strategy

- We achieved full alignment at the first offsite.
- Parasun's actual exit strategy from that retreat:
- “Our Core Purpose is to sell the company for more than \$10 million by late 2006 or early 2007.”
- The sale closed in May 2007 (but was agreed early in 2007) - right on schedule.
- But we sold it for **\$14.8 million**.
- The exit strategy drove that success.

Two Secondary Sales

- Parasun had almost done a disastrous exit twice before I invested.
- The founder and some of the early shareholders were very eager to sell some shares. (Just like in the Nexus case.)
- This selling pressure would have almost certainly caused problems during the exit.
- So my partner and I organized two secondary sales, one at \$0.40 and one at \$0.55/share.
- Those investors received about \$1.30 per share.

The secondaries worked because

- Many people think it's impossible to sell founders or angel investor shares in a private company.
- But it can be done, if:
 - The price is reasonable, and
 - There is a clear exit strategy, and a
 - Good team in place to execute the exit.
- In this case the buyers were angels and other accredited investors (about a dozen.)

What we did right

- With full alignment on a realistic exit strategy:
- Cleaned up the structure
- Did two secondary sales
- We improved the financial results
- Prepared all the due diligence well in advance
- Had professionals leading the exit
- The CEO consistently delivered monthly financials that were better than the projections.

The Sales Process

- We developed an online presentation and password protected website.
- Contacted about 100 companies all over the world.
- Got interest from 15 to 18.
- Entered early due diligence with 6 or 7.
- Maintained a short list of 3.
- Had an active bidding process for almost three months driving up the price by several millions.

Comparison of These Two Exits

	Nexus (1993)	Parasun (2007)
Exit Strategy	Didn't even know	Clear and realistic
Alignment, DNA and Structure	Didn't even check	Complete by the first retreat
Secondary Sale	Missed opportunity	Completed two
CEO Should Never Lead the Exit	Another expensive mistake	Experienced Professionals
Multiple Bidders	Only had one bidder – two times	Very successful auction process
Overall Result	Rode it over the top – got under half \$	Sold for 50% more than expected

Good Luck With Your Exits!

(But remember, skill is far better than luck.)