

# Exit War Stories and Life Strategies

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# Exit Strategy and Life Strategy

- Deciding to sell your company is one of the biggest decisions we make as business owners
- It will change your life in ways that are almost impossible to imagine
- And it will often change the lives of your shareholders, employees and their families
- And as important as this decision is,
- The truth is - we are not very good at exits

# Exits are an Underutilized Strategy

- Partly because of a lack of data, and
- Partly because entrepreneurs are incurable optimists
- We dramatically underutilize exits as part of our business strategies and our life strategies
- The result is we have less money
- And are less happy
- My goal today is to improve that

# Why We Aren't Good at Exits

- To succeed, entrepreneurs and CEOs have to learn to be good at many aspects of business
- For many of us, the challenge of that life long learning is one of the reasons we do what we do
- Much of what we learn as entrepreneurs is empirical – we learn by doing, by trial and error
- That doesn't work very well with exits
- Simply because exits don't happen very often

# Exits Don't Happen Very Often

- We don't have much data, but we do know that only about 10% of the companies that receive angel financing have an exit
- Other types have lower exit rates
- And to learn from just one company might require 5 to 10 years of observation from startup to exit
- And the market for exits is changing so quickly that much of what we thought we knew ten years ago is dangerously out of date today

# Most Exits are Under NDAs

- My personal mission is to develop and share best practices on what works with exits today
- In part, to do that I run a boutique M&A advisory firm
- My hope is that each transaction we undertake will contribute to the knowledge that I can share
- Unfortunately I can't even mention some of our most interesting case studies
- Because most exits are covered by an NDA 😞

# The Data We Have is Anecdotal

- We are still decades away from having hard data on exit strategies that will be useful to CEOs
- The knowledge we do have is largely anecdotal
- Based on observation and case studies
- One of things that I've learned is that only 25% of saleable companies have successful exits
- Yes, we end up blowing the most important decision about 75% of the time

# Entrepreneurs are Optimists

- To be a successful entrepreneur we have to be indefatigable optimists
- Our DNA makes us very good at seeing the opportunities, the possibilities, the blue sky
- But those same genes make most of us particularly poor at assessing risk
- And like a law of physics, everything in business is a risk – reward tradeoff
- That's another reason we often blow the exit

# Exit War Stories

- That difficulty most of us have in assessing risk
- Is one of the reasons that War Stories are so valuable in our educations
- They provide the opportunity to learn from the experiences of other business decision makers
- To hopefully benefit from their experience
- So we won't have to learn by making every mistake ourselves

# Exit Case Studies

- Exit case studies with valuations are quite rare
- My team and I have been selling companies for many years
- In just a few cases, we've been able to obtain permission to share the exit stories of companies that we've helped to sell
- I hope you find these stories valuable
- Full case studies on: [www.Exits.com](http://www.Exits.com)

# Every Exit is a Learning Experience

- Every exit is a learning experience
- I love the work I do in part because it's exciting
- But more importantly, because I know I have significantly changed the lives of many people
- One of the fascinating things for me
- Is to learn how it all works out in the end
- Most of the time it's not quite how we imagined it

# Parasun Case Study

- This Canadian company provided high speed internet over cable TV to about 140 communities, mostly in the US
- I invested \$500,000 in April 2004 at a \$3.4 million valuation = \$0.40 per share
- Revenues were about \$3.8 million with a \$500k profit
- My angel fund also invested at \$0.55 per share in June 2005

# Parasun Exit Strategy

- I became Chair and signed on to execute the exit
- The board set a target exit price at the 2005 strategic planning retreat
- The plan was to sell the company in 2.5 to 3 years (late 2006 or early 2007)
- Most of the work was on growing the business

# Parasun Exit Valuation

- Started the exit process in the fall of '05
- Revenues \$8.2 million, profit \$781k with 30% growth rate, 10 million shares
- Approached 100 buyers and short listed 10
- Had several bidders through the final stages
- In Jan 2007 sold the company for 48% more than the target price

# What was Parasun's Selling Price?

- Gross selling price (before transaction fees)
- 
- \$14.8 million - all cash

# What Happened Next?

- ParaSun's exit strategy and execution were perfect
- But the ParaSun shareholders had no idea how lucky they were
- Within two months of the exit, the companies fortunes turned down dramatically
- Six months after the exit it wasn't even profitable
- So what happened?

# The Risk They Missed

- Everyone on the ParaSun board, including me
- And the company that acquired ParaSun
- Failed to adequately assess the currency risk
- ParaSun was a Canadian company, with Canadian expenses but with US\$ revenue
- Within two months, the currency exchange rate started a historically large move
- If they had started the exit 2 months later, I don't think it would have happened at all

# Brightside Case Study

- Spin out from the University of British Columbia Physics Applied Optics Lab
- Technology to make LCD displays brighter and higher contrast
- \$15 billion /yr market
- Biggest opportunity was large screen devices for home TV applications

# My Investments in Brightside

- I first invested when it was just two people and a few patents
- My fund invested three times:
  - \$100,000 at \$3.2 million valuation = \$2.33 /sh
  - \$125,000 at \$4.2 million valuation = \$2.90 /sh
  - \$100,000 at \$12 million valuation = \$5.00 /sh
- In June 2004, Oct 2004 and Aug 2005
- Each investment was based a further demonstration of progress with the technology

# Brightside Financing History

- About \$7 million was raised from angels
- Including one brokered round that used an Offering Memorandum to place with angels in Europe
- But despite being engaged with a dozen VC firms up and down the west coast, no VCs ever invested in the company
- The VCs wouldn't invest in common shares

# The Brightside Exit

- Without the capital to put the product into production, the only other strategy possible was to sell the company
- Still in R&D, zero revenues, 8 patents and 3.1 million shares
- The strategy was to sell to a large Asian consumer electronics manufacturer
- Dolby Labs acquired in Feb 2007 (2.75 yrs)

# How Much did Brightside Sell For?

- Gross selling price (before transaction fees)
- 
- \$28 million – all cash

# What Happened Next?

- Just a couple weeks after the sale to Dolby
- I was in Best Buy trying to convince myself I needed an even bigger TV
- Each of the three investments I made into Brightside were predicated on them showing me a better prototype of their product
- I'd seen dozens of their demos and was getting pretty good at recognizing the technology
- And there it was – right on the shelf!

# I Called the Company

- Right there on the showroom floor, I called the company
- And before I finished my question, they were telling me what I was looking at
- A very big Asian display manufacturer had taken their technology and put it into production!
- Because of who it was, the company knew exactly what had happened

# The Risk They Missed

- The Brightside team had visited this company a few quarters earlier to discuss a licensing deal
- Before they visited they invested in the very best NDA they could get from a very big law firm
- They disclosed the technology to this company
- As near as they could determine, because this was now only a few quarters later
- And because of the typical production cycles
- They must have put it into production that week!

# Imagine What Would Have Happened

- If Brightside had delayed their exit even a couple of weeks, I don't think it would have happened
- The story I heard was that Dolby put 40 lawyers and others on a plane to 'visit' the company
- Dolby can do that – but entrepreneurs can't
- Unfortunately this story happens all the time
- And we entrepreneurs just aren't good at assessing this type of risk
- That's one of the scariest saves I've been part of

# The Pacinian Case Study

- Company in Coeur d'Alene, Idaho
- The CEO and Chairman both attended my Exit Strategies Workshop
- In November 2010
- Before they came to the workshop, they were not sure if they were going to:
  - finance the company to production
  - license their technology, or
  - work toward an early exit

# The Original Idea for a Company

- Two founders - who had worked most of their career on keyboards
- They kept thinking there must be a better way than the conventional keyboard

## Traditional Keyboards

- Thick
- Fragile
- Complex
- Inefficient to Backlight
- Little Innovation in 20 years



Rubber Dome / Scissor Mechanism

# Pacinian's Mission

- To improve the human interface
- Specifically to provide tactile feedback
- On an ultra-thin keyboard or touch screen

## A New Keyboard Technology

By Pacinian



Thin Never Felt So Good

# Pacinian's Funding History

- All angel investment
- About \$4 million raised before there was an exit strategy
- Needed another round to fund to the exit
- In total about \$6 million was invested

# The Third Pivot

- Pacinian did three pivots (in other words...)
- The product was expected to be ready for production by the end of 2012

## Benefit Summary

- Thinner Laptops
- Simple Design / Easy to Manufacture
- More Efficient Backlighting
- Increased Reliability
- Brand Image / Innovation



# But It Was Acquired Before

- Even though the company had not yet built a production prototype
- Pacinian was acquired in August 2012
- And to give you a hint,
- The final price was 50% above the first offer

# What was Pacinian's Selling Price?

- Gross selling price (before transaction fees)
- 
- \$30 million – all cash

# What Happened Next?

- Pacinian executed their exit strategy brilliantly
- They finished the production version of the product
- The team is happy at their new company
- The board distributed the cash to the shareholders
- Founders, employees and investors are all very pleased with the outcome

# The Risks for Pacinian

- I think Pacinian is the most interesting of these three case studies
- Even though the company still hadn't been able to produce a production prototype
- They has several strategic options
- The Chairman and I spent about a year debating the company's strategic options with the board
- Working to assess the future risks and rewards

# Pacinian's Strategic Options

The Pacinian board had several options:

1. Accept the offers of Venture Capital and build a factory to produce their keyboards,
2. Proceed with one or more of the licensing offers and let other companies manufacture
3. Design and execute a pre-revenue early exit

# Pacinian's War Story

- The valuable learning from Pacinian was what happened before the exit
- The process the board went through to weigh their strategic options and make the decision
- At times it felt like a war
- The board were all smart experienced people
- But at the start of the process nobody agreed
- Some very colorful language was used

# Only One Person Voted to Exit

- At the beginning of the Pacinian exit, only one investor believed in the idea of an early exit
- That was the famous angel investor Bill Payne
- Bill convinced the Chairman and CEO to attend one of my workshops – just like the one we had here yesterday
- That got them thinking
- But rest of the board still thought a pre-revenue exit was impossible

# That's What's So Challenging

- The Pacinian board were good, experienced people
- But none of them had even seen, or even heard about, a pre-revenue exit before
- Which is not surprising considering how uncommon they were just a decade ago

# What Might Have Happened

- For me, I often wonder what would have happened to Pacinian if they had chosen one of the other strategic options
- We'll never know for certain
- But I have no doubt that they made the best decision
- The early exit was certainly the lowest risk strategy
- Even though most thought it was impossible

# Your Life and Exit Strategy

- I hope these case studies stimulate you to think more about your company's exit strategy
- And how that intersects with your life strategy
- And how it will affect the lives of your stakeholders and employees
- I believe both entrepreneurs and investors would have more money
- And more fun
- If we more often incorporated a good exit strategy