The Art of the Exit:

Choosing Your Exit Path and Maximizing Value When You Get There

by John Grillos

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CHAPTER 1

Introduction

Ever hear a dying company owner say, "I wish I could have spent more time at the office?"

Paychex founder and chairman Tom Golisano was quoted in Chief Executive Magazine: "At some stage, every CEO must ask himself or herself: Is my long-term goal to sell the business—or will I stay until they wheel me out in a box?"

This book is about preparing for a financial exit for company owners/CEOs (referred to hereafter as owners). I am writing it now for four reasons:

- The Covid pandemic amplified the forces of creative destruction by making us do things more virtually. I believe this jump into the future will not go away after the pandemic as the effect of these forces have, at a slower pace, been in play for some time. Their impact is likely shrinking the timeline between where your business is now and where it needs to be to maximize its value at an exit.
- Even before the carnage caused by the Covid, I believe that company owners needed to prepare for the sale, merger or IPO of their company well in advance, often years ahead of undertaking a transaction. That is the only way to ensure value maximization, or for that matter, survival. "An organization is a living, breathing organism that has a life cycle and responds to the forces of nature" (Tony Robbins). How fast you travel the path of your life cycle is a function of broad economic forces out of your control and some number of forces under your control.

- Several forces not under your control impact your exit planning and opportunity set in ways that are hard to predict. I believe that the frequency of the events triggered by those forces will likely occur at an increasing frequency.
- Change continues to accelerate, much like the expansion of the universe. Change creates opportunities for startups and threats for established companies unwilling to understand the effect of change on their companies or without the resources needed to respond to it.

The primary goal of this book is to help business owners understand the process of preparing their companies for an exit, merger or IPO. On the one hand, that understanding is necessarily based on considerations of the broad economic environment within which they operate and the implications of accelerating change. On the other hand,

that understanding includes treating key management performance variables and expectations about the process involved in sale, merger and IPO exit paths. The book is divided into the topics below:

- Chapter 2: Broad Macro-Economic Forces—The forces over which you have no control but need to keep an eye on as they have a material impact on your plans.
- Chapter 3: A Look Into the Future—Covid created a jump into the future of the forces of innovation that are reshaping pretty much all aspects of human life and work in most countries.
- Chapter 4: Picking Your Exit Path and Managing to Maximize Value When You Get There.
- Chapter 5: The Journey to the Exit—Discusses the mechanics of the exit process.
- Chapter 6: Capital Raising Realities—What to expect from equity and debt sources if raising money is part of your getting ready for an exit.
- Chapter 7: War Stories—Presents examples of how uncontrollable and controllable forces have effected the outcomes for several companies with which I have been involved.
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CHAPTER 2

Broad Macro-Economic Forces

"Economic medicine that was previously meted out by the cupful has recently been dispensed by the barrel. These, once unthinkable, dosages will almost certainly bring on unwelcome after-effects. Their precise nature is anyone's guess, though one likely consequence is an onslaught of inflation." Warren Buffett. I would add that increased taxes are inevitable, which will affect the value of your company and how much of the consideration you get to keep when you sell it.

Covid is not rare in the sense that it has created a recession. The US has been through 26 recessions and stock market meltdowns since 1835. Here is the recent history of such events:

- November 1980 to August 1982—Federal Reserve caused this recession by raising interest rates to 20% to fight inflation.
- August 1987 to December 1987—This stock market crash was caused by concerns about stability in the middle east, the introduction of program trading, and an overvalued stock market.
- 1990–1991—This recession was triggered by Savings and Loan organizations making large amounts of poor real estate loans.
- March 2000 to October 2002—this stock market crash and the attendant recession was caused by the excess valuation of .com companies in the public market.

- October 2007 to March 2009—This market crash and recession were caused by excessive lending on real estate.

I believe that the pandemic and world governments' reaction to it has created a new set of economic ground rules:

- This is not the first virus epidemic, and it will not be the last. The Spanish Flu, Hong Kong Flu, AIDS, SARS, Swine Flu, Ebola, MERS and Covid-19 are but a few of the millions (or billions according to some sources) of viruses in our world waiting for the right environment to attack. Future government lockdowns and the resulting economic damage from them may become some form of "new normal."
- The open question is if the world will react to future virus attacks with the same intensity of economic activity destruction as it did to Covid-19, and where will the support resources come from to finance the economic damage?

For purposes of planning for future outcomes, using past recessions to predict the future will likely be unreliable. Here is why:

- This is the first time the government has put the economy into an induced coma, suspending a large part of its economic activity.
- The FED and the US government are throwing an unprecedented amount of money and debt purchasing at the problem, as are most other economies in the developed world.
- All of this support will give the government more power over the economy. The continuing and growing dysfunction of the US federal government will likely make their involvement more of a problem than a solution. Even dismissing the dysfunction, the government is always slow to make necessary changes as their size and incentives do not align well with effective problem-solving.

- Several studies suggest that tens of millions of Americans have fallen into poverty due to the Covid reaction (admittedly, they were not doing so well before Covid). Government programs and spending must deal with this problem.
- More spending is being prompted by the need for environmental mitigation and infrastructure rebuilding, and a host of non-essential wish list items.
- The major world economies are increasingly becoming intertwined. Because of its size, China is influencing the economy of the US. India and other rapidly developing countries with large populations are on the way to doing the same.
- Covid has pushed forward many socio-technic practices (technology enabled ways we do things) that have been growing more slowly for some time, creating an ever more unpredictable future. Brian Chesky, the CEO of Airbnb, recently commented that "I did not know that I would make ten years' worth of decisions in 10 weeks!"
- Last but not least, there is no returning to the way things were before the Covid, for three reasons. First, this "new normal" was just a jump forward into a future that was on the way anyway. Second, because of the long time we have been doing things differently, the new ways have become engrained into our expectations about how we will do things after we emerge from the pandemic restrictions. Third, some of what we used to do were merely habits, and we have likely concluded that some of those habits no longer serve us.

Appendix B discusses debt and other macro changes likely to impact the US economy for some time. This includes the likely deleveraging that is in our future as governments at all levels in the US deal with the simultaneous problems of needing to spend more while paying the debts they have accumulated. As a business owner considering an exit, you had better keep in mind that the further out that exit occurs, the less of the consideration you get for the company will go in your pocket. There will be higher income and capital gains taxes and, perhaps, a wealth tax. I am reminded of when I sold a company at the end of 2012. I was hit with a $50K tax bill for a retroactively applied California state tax increase, which passed months after the close of the sale.

Appendix C takes a look at the US economy's future, highlighting forces that will likely affect your company in the medium term.

It seems clear that the future holds more taxes, more government control, compressed business lifecycles and more uncertainty. So, let's now turn to some things you can analyze in determining your exit opportunity set and timing.

CHAPTER 3

A Look Into the Future

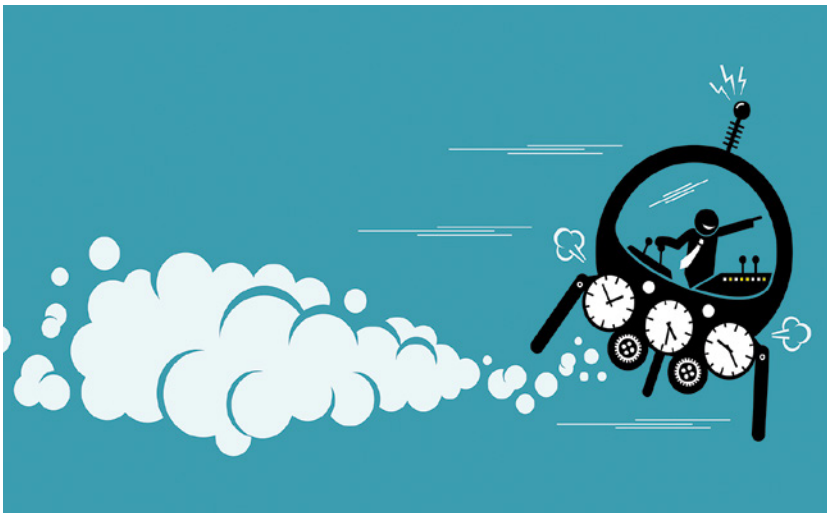
"The greatest danger in times of turbulence is not the turbulence—it is to act with yesterday's logic."

—Peter Drucker

What is going to happen as the pandemic subsides? Will we have a U or V-shaped recovery (or K if you subscribe to a certain political point of view)? My crystal ball is no better than anyone else's, but I think the macro forces that have existed for some time will have an increasing role in shaping the economy going forward. Covid created changes in how we do things are becoming patterned into the fabric of the future. There is no going back to how things were done before the pandemic.

This book is for company owners and CEOs who expect to sell their company, merge it with another company, or take it public. It is not intended for those who expect to transfer ownership or control to a family member. Though at this particular time, you may not know which exit path you will take, it is best to begin the process of thinking through that issue by rolling your mental clock forward to the time of the outcome and working backwards to today. This book helps you figure out the end points needed to maximize exit value. The difficulty/feasibility of the path between where you are and where you need to be dictates which exit paths are available to you.

Areas of Important Innovation



Accelerating innovation in technology has continued to make our lives better. Over the next few decades, its contribution, fueled by innovations in the areas below, will be providing basic needs for everyone in the world at massively lower-cost—energy, food, shelter, health, and safety for beginners. For a current business owner, the list helps to form a picture of opportunities for or threats to your business.

- Energy production is ready for a revolution. Here are my top three favorite reasons why:
    - Next-generation, safe, Nuclear fission reactors should be near, created by such companies as NuScale and TerraPower (which got an investment of $500 million from Bill Gates).
    - Fusion reactors are being developed that do not have the meltdown risks of fission.
    - Hydrogen generated from water using renewable energy sources can fuel transportation and facility power generation.
- Genetic engineering and growing techniques (such as vertical growing facilities) will maximize food production with minimal land use and environmental damage. It will also lead to low-cost and more effective drug development and direct non-drug cures that are virtually free. This is just the beginning of what we can expect in the upcoming decades.
- Biotechnology including such wonders as gene editing's promise to eliminate human ailments.
- Nanotechnology has far more possible uses than can be explained here. For example, it is one of many ways to create nearly costless materials to construct houses and furniture. Nano-materials and concepts are currently in development that show potential for producing energy from movement,

light, variations in temperature, glucose and other sources with high conversion efficiency.

- Low orbit satellite rings are being implemented to make high-speed internet available anywhere on the face of the earth.
- Artificial intelligence (AI), which enables machine learning, is a powerful tool currently being used to do such things as streamlining workflows, enabling more efficient communications, improving customer support, and providing insight into purchasing behavior. Its development, going forward, is exciting and frightening. More on this later.
- Robotics is becoming a well-established approach to doing dangerous or repetitive tasks. In some cases, robots are partners to human workers doing the parts of a job that are dangerous. In some other cases, robots are remote-controlled by humans doing tasks that cannot be preprogrammed into the robot.
- Blockchain is an information system technology that holds promise for supply chain management, enabling transparency into the origin and journey of materials from origin to product. Blockchain technology allows better record management, providing a snapshot of any record from its origination. Blockchain technology could be used to verify orders, purchases, returns, receipt of the product; you name it.
- Cybersecurity has become a critical business function and will be an integral business process as companies leverage emerging trends and move towards cloud computing. It is also playing a central role in protecting our physical and intellectual assets as we continue our cyber wars with China, Russia, North Korea, Iran, and other countries.
- Drones help transform certain verticals, giving an edge over competitors and offering a technologically-powered physical connection between businesses and end-users. The remote

capabilities of drones coupled with AI applications are transforming business in the industrial, public safety, construction, and insurance sectors, just to name a few.

- Internet of Things (IoT) is a conglomeration of devices that interact, providing substantially greater user control over the devices and systems in their lives, and greater insight into how products and services are being used for everyday tasks.
- Quantum computers leverage the principles of superposition and entanglement to process information exponentially faster than current computer architectures.
- Virtual Reality/Augmented Reality/Mixed Reality (referred to as XR) helps provide context to possibility. Consumers and businesses may know that they need a solution but have difficulty visualizing how a product or service will enable a particular outcome. Companies can use XR to enhance their offerings and inform effective decision making. These are just a few examples of the many applications for XR.
- 3D printing allows businesses to customize a product according to personalized specifications and enable businesses to offer nearly limitless possibilities. In recent years, providing this kind of customization required either significant reprogramming or manual intervention. With 3D printing, personalization is now one more task that can be automated. 3D printing also enables the use of various materials that offer cost-saving and environmentally sustainable benefits.
- 5G data networks offer the supporting foundation that businesses can leverage to embrace emerging technologies requiring the speed of wired networks.
- Autonomous Driving (AD) employs a suite of data capture and AI technology to allow vehicles to drive themselves. For most business owners, AD will be a tool to improve the productivity

of their Staff. Seniors can look forward to keeping more of their independence by having self driving vehicles take them where they want to go. There are scores of other applications for AD.

Where Opportunities Abound

"A pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty."

—Winston S. Churchill

The good news about the pandemic is that it has shaken us out of our state of homeostasis, meaning doing things as we have done them in the past as the sole justification for avoiding the disruption caused by innovation. Innovation is now the name of the game, and you likely have the opportunity to rethink every aspect of your business to make it better going forward. Ask yourself questions about sales, marketing, product and service offerings, operations, etc. In each of these areas, there are things you can do to make them better. Change can be exhilarating and a lot more fun than focusing on what is not working. Get outside advice if you need a specialist to help you through the process. Insiders are often too wed to doing things as they have been done in the past.

The technologies discussed above and government involvement are fueling changes in how we do business in those areas discussed below. It is critical to know if that is the case and what you need to do to take advantage of or protect your business from them.

1. Work-from-home—as technology such as Zoom and Google Hangouts make meetings and communications as efficient as being in the same room, and cities make moves to discourage commuters. The debate continues, but I believe that work from home is here to stay. Why? Commuting costs and time-spent commuting are ever-increasing. Commuting is bad for the environment, and regulators are making

it harder to do. Office rent is expensive, as are the in-office perks demanded by employees. The modern open office environment makes concentration a thing of the past. (We had these bullpen layouts in the 1950s and 60s and went away from them for productivity reasons). Here are some current pro and con arguments:

a. Work from home plays well into the growing environmental protection movement.

b. Companies get the benefits of:

    i. Increased productivity as people spend less time traveling to and from work.

    ii. Other company costs for on-site benefits are reduced or eliminated.

c. A recent Wall Street Journal survey found that from an employee perspective, work from home is mixed positive:

    i. Biggest benefits

        1. 32% ability to have a flexible schedule

        2. 21% not having to commute

        3. 26% flexibility to work from anywhere

        4. 11% ability to spend time with family

    ii. Biggest struggles

        1. 20% collaboration and communication

        2. 20% loneliness

        3. 18% not being able to unplug

        4. 12% distractions at home

d. In the book, *Rework* a published study showed that at least 65% of a workforce had to work from home for the remote workers not to feel isolated from the important things going on in the company. I feel that a Corona effect will be moving the number of remote workers toward that threshold.

e. According to an article in a recent Economist, the work from home movement has limitations. The percent of jobs that cannot be from home for nine countries listed in the article is over 50%. Greece is the highest with 68%, and the US is the lowest with 58%. These percentages are highly correlated with the percentage of GDP from retail, transportation and hospitality, with Greece at 23% and the US at 16%. Clearly, this reinforces the arguments that Corona reinforces job inequality as most of the jobs requiring physical presence are in lower-paid occupations. Add to this that these jobs will be ones most impacted by returning to work practices.

f. There will be some pushback on this trend, but I believe the tide is just too strong to bring us back to where things were before the pandemic. The key objections, for the purpose of discussion are:

   i. The digital divide—too many in the US and the world do not have internet access or smart devices to run education applications.

   ii. Monitoring—it is currently too hard to diagnose when someone working remotely is failing.

g. 5G and low orbit communications satellites will fuel this movement.

2. On-shoring—The trade war with China was initiated to try to rebalance trade rule disparities, which had been growing for decades. The advantages of offshoring have been declining as the wages of workers in China, South Korea, and other ASIA Pac countries have risen. In the US, companies are using AI and Robotics to replace jobs that had been shipped offshore. Many companies have begun to rethink their supply chains to trade cost savings with reliable performance and control and not paying for cost savings with their intellectual property. The $2 B bill passed on March 27, 2020 added

impetus to that movement by making government loan guarantees unavailable to companies headquartered outside the US. Even before the virus, the renegotiation of key trade agreements included stronger provisions to provide more parity between US and foreign labor costs, raising foreign manufacturing costs.

3. 5G and a newly allocated part of the 6 GHz mid-band spectrum—will provide enough speed and resolution to support virtual applications and interaction for most applications. For example, a German manufacturer implemented remote parts inspections enabled by the resolution afforded by 5G.
4. VR/AR/MR—usage will spread with 5G and the continued improvement of headsets.
    a. Education and Training
    b. Real-time task support for such things as improved worker productivity
    c. Tighter integration with information from the cloud, internet and other information sources
    d. Virtual Reality for touring (a la the movies Total Recall and Ready Player One)
5. AI—Will continue to advance and invade human activities, not requiring hands-on activities. There are almost no human work activities (even doctors, lawyers and accountants) where AI replacement is not a threat. AI's rapid evolution is being fueled by what is being called Huang's law, which is the observation that the Silicon chips that power artificial intelligence more than double in performance every two years. An example of this is that between November of 2012 and May of 2020 performance of Nvidia's chips, which fuel artificial intelligence increased 317 times for an important class of AI calculations. One current example of job elimination by AI is cashier-less checkout. Cameras throughout a grocery store

capture the information of shoppers as they grab objects off store shelves; the system tallies it all and bills them through their mobile devices as they leave the store.

6. Automation and Machine learning—will help AI invade work task areas where hands-on is not needed.
7. The Environment— Increasingly, the pressure is being put on companies and the government to mitigate climate change.
    a. Clean energy is growing, and creating jobs of the future as jobs in the fossil fuel sectors will continue to decline. Currently, 63% of US energy production comes from fossil fuels, 20% from nuclear and 17% from renewable sources. That mix will change over the next decade for the following reasons:
        i. Fuel for transportation will continue to decline as electric vehicle demand continues to increase. In 2020, the governor of California mandated that no new fossil fuel-powered cars could be sold in the state beginning in 2035.
        ii. The coal industry in the US is on life support, and that is not likely to last much longer as demand in other parts of the world declines in the face of a growing environmental threat.
        iii. New generation fission and fusion reactors can, with a little help from the overzealous regulators, provide for a very low cost all of the world's power generation needs.
        iv. Solar and wind energy production is being used to generate hydrogen for hydrogen fuel cells. This solves the problem of power generation when the wind is not blowing or after sunset.
    b. Public companies in the US are coming under material pressure to "clean up their acts." Investors interested in the environment are increasingly making investments in "sustainable" companies. The Sustainable Accounting Standards Board is a non-profit

that ranks public companies according to 77 measures. The major dimensions of measurement include environmental impact, human capital (employee and workplace issues), social capital (external social and product considerations), and business model/innovation. Blackrock is making a statement on this issue with its $7T in financial firepower equal to 18% of the total capitalization of all US security markets by not investing in companies that do not take active steps to protect the environment or are in the fossil fuel industry. I see a future market where "sustainability" will rank with earnings growth in determining the market value of public companies. Private companies will likely need to adjust their business models to fit into this future.

8. Education and Training—Higher education is too expensive and too irrelevant to be worth the cost for those needing to work. Employers are looking to hire people ready to go to work, not ready to be trained, and much of the standard bachelor level curriculum is not relevant to earning a living. The success of Kahn Academy, Udacity, the Power MBA and many others suggest that the future may be dominated by certifications (nano degrees or whatever) based on the needs of employers, most of whom will be involved in defining curriculum and financing tuition. Online provides the platform for education and training in the future, but its importance has macro-economic consequences.

    a. Training will be very important in preparing the workforce for the jobs that are replacing the ones they once had. Among other things, employers and educational institutions will need to work together more to create job-relevant educational content and credentials.

    b. A key issue is the digital divide. Many rural and poor do not have access to devices or high-speed networks. Low orbit

satellite rings and likely government subsidies should solve this problem in the next couple of years.

9. Human Enhancement—the race is on between enhanced humans and robotics and AI.
   a. Exoskeletons—can give humans the strength and speed of robots and have the advantage of dealing with unforeseen disruptions in work patterns.
   b. Brain implants—can add the resources available to AI to the human brain giving humans an edge created by what humans can do that AI cannot, such as exercising judgment in the face of the lack of data and gut instinct. Take a look at the web site of one of the pioneers working on this. https://neuralink.com.

10. Personalized and predictive medicine is being enabled by our ability to capture data from wearable devices such as smartwatches, which give us the ability to increasingly predict and treat health issues in people even before they experience any symptoms. When it comes to treatment, we will see much more personalized approaches. This is also referred to as precision medicine, which allows doctors to more precisely prescribe medications and apply treatments, thanks to a data-driven understanding of how effective they are likely to be for a specific patient.

11. If your company is in one of these segments or provides products or services to companies in these industry segments, then your future post-Covid should be bright.
    - Health care and medical sciences. e.g. Teledoc.
    - Remote fitness means using such things as Peloton cycles and exercise routines available free on YouTube.
    - Transportation and delivery—are moving rapidly to drones and ride services. On the one hand, these services and the coming (air shuttles) will improve traffic congestion. On

the other hand, the demand for transport services will likely decline as work-from-home spreads.

- Enterprise software, must-have, not nice to have.
- Privacy and internet safety products and services.
- Cybersecurity.
- E-commerce logistics for delivery (e.g. drones).
- E-commerce business applications.
- Industries with good gross and net margins and little need of Capx.
- Clean Power.
- On-line delivered financial services.

Industry Segment Where Virtual Replacements will do Permanent Damage

As mentioned previously, I do not believe we will go back to what was "normal" before Covid. Business owners need to be conscious of how their company products or services relate to industry segments, resulting in permanent decline. If your business is one of the below or a supplier to one of them, careful consideration of how to create your future is warranted.

- Travel, in general, may decline as virtual experiences replace activities at the end of journeys. For example, in the fourth quarter of 2020, Amazon introduced its first set of virtual destination experiences.
- Venues where people congregate in close quarters, where there are alternatives, and where reduction does not have a major impact on quality of life.
    - Air travel—will continue to decline as flyers use conferencing and virtual entertainment to replace travel. Air travel because of crowded terminals or the planes themselves are well known for spreading viruses.
    - Health clubs—are being replaced with home fitness equipment and classes/instruction available on-line.
    - Cruises—like airplanes, large cruise ships have been Petri dishes for colds and flu.
    - Movie theatres— We see what I believe is an emerging trend to sell streaming of first-run movies. Who will miss expensive stale popcorn, people talking, and the lack of workable closed captioning?
    - Concerts—can be done on-line
    - Seminars—can be done on-line

- Bars and restaurants—the biggest problem here may be the number of them that go out business before the end of 2020, as half of them in good times operate at the edge of insolvency. The good news is the survivors may pick up the traffic that used to frequent operations no longer in business.
- Conferences—can be done on-line
- Sporting events—can be watched on media devices.
- Nursing homes—will be replaced by in-home care.
- Hospitals—Too many people admitted to them never come out. I believe home care not requiring special equipment will replace many hospital visits. Portable and less expensive versions of equipment found only in hospitals are in development for use in-home care.

CHAPTER 4

Picking Your Exit Path and Managing to Maximize Value When You Get There

In some ways, business mirrors biology. Darwin may have said it the best when he surmised, those who survive "are not the strongest or the most intelligent, but the most adaptable to change." The Wall Street Journal recently published an article entitled "Adapt, Pivot, or Stay the Course." Obvious stuff for the most part— focus on what sells, stay focused on what you know, it's not too late to go digital, all hands on deck, and get simpler and go small.

Staying focused on what you know when the sands of change are shifting under your feet can put you out of business.

At this point, I think there are three things on which we can agree. The only thing that will not change in the future is change itself. Covid has jumped change forward by at least a few years. Accelerating change shortens the life cycle of companies that do not or cannot adapt to the new business environment caused by rapid change. As the leader of your company, you need to have or to develop the mental discipline and management systems needed to assess the impact of a constantly changing environment on your business and to take needed action to protect the downside or take advantage of change to build the upside. Since I assume you are interested in preparing your company for a high valued exit in the future, I present here a process for evaluating your company and undertaking the needed planning and execution required to maximize its value at the time of an exit, IPO or merger.

The choice facing you as an owner is which exit path will be most suited to your business, its characteristics and your goals. The three primary exit paths open to most businesses are:

- Sale – transfer of ownership from you to another owner.
- Initial Public Offering (IPO) – turning your ownership into securities that trade in a public market, such as a stock exchange.
- Merger – combining the ownership of your business with another, producing a new business and new ownership structure.

There are two key considerations in determining the most advisable exit path for you.

One is the set of business measures (e.g., revenue level or revenue growth rate) you must accomplish to make your company conform to the requirements of any path you wish to pursue at the valuation you want.

The second is figuring out how to apply, grow and make better the Performance Assets under your control (e.g., people and management systems) to get the measure values you are after at the time of an exit.

Here is a summary of the 5-step process you can undertake to evaluate an exit path and choose which one will work for you.

1. Determine where your business is now concerning Measures used to determine its value and where you want it to be at the point of an exit.
2. Determine what adjustments, improvements or additions need to be made to each of your Performance Assets to make your company conform to the Measures' values at the exit you are analyzing.
3. Combine the analysis of each Performance Asset into a single overall evaluation that allows you to determine if you have the capital and time needed for implementation.
4. If your exit value aspirations are not in sync with your capacity to meet them, adjust the analysis or the exit value considerations to bring everything in line.
5. Undertake the detailed planning and management projects needed to get from here to the desired exit state.

Here are the details of the process.

Table 1: Relating Key Business Measurements to Exit Paths

(Importance to an Acquirer, Public Market Investors or Merger Partner)

Measure	Transaction Type		
	Sale	IPO	Merger
Revenue Level/Growth Rate	Critical	Important	Important
EBITDA	Critical	Nice to Have	Nice to Have
ARR or BARR	Important	Nice to Have	Nice to Have
Cash Flow	Critical	Important	Nice to Have
Net Worth	Important	Nice to Have	Important
Bal Sheet Strength (Current Ratio, etc.)	Critical	Nice to Have	Nice to Have
Debt Service Coverage Ratio	Critical	Nice to Have	Important
Market Size (TAM)	Important	Critical	Important
Competitive Position	Important	Critical	Important
Competitive Threat Level	Important	Important	Important
Barriers to Entry	Important	Important	Important
Strategic Fit/Synergy	Important	Not Relevant	Critical
CEO Quality	Important	Critical	Important
Team Quality	Important	Important	Important
Board Quality	Not Relevant	Nice to Have	Not Relevant
Management Systems	Nice to Have	Important	Nice to Have

The process is based on key business measures relevant to the three exit paths, as shown in Table 1. The table provides a framework for your analysis of which paths are available to you.

Any company working toward an exit can use Table 1 and the process described below to decide on which exit path(s) to take and what needs to be done to maximize the value of your company on any chosen path. Here is how:

1. For each path you want to consider, construct a rank-ordered list of measurements, from Critical to Not Relevant.
2. Assess where you are in each measurement and where you want each to be when you begin the exit process. Determining where you want each Measurement to be at the exit can be challenging as knowing what values maximize exit value takes a bit of guesswork

or advice from qualified sources of information. I have helped many entrepreneurs analyze and arrive at values for these measures. Set your goals high as you have little chance of meeting a stretch goal if you have not defined what it is. An approach to the assessment is shown, as an example, in Table 2 below. Not all rows from Table 1 are included. That reflects that some of them may not be relevant enough to require much thought.

3. Do the necessary analysis and determine what improvement is needed for each Measure: the cost of improving the Measure and a schedule for doing it. The goal is to make each Measure meet the intended exit value. Almost anything you want to do to improve your performance in one of the Measures requires making improvements in one or more of the Performance Assets listed in Table 3 below. Table 3 is an example format for documenting your considerations of each Performance Asset. The section below, Managing Your Performance Assets, provides considerations I think are important in understanding their contribution to the process of value maximization.

4. Step 4 is to create an overall picture of Measure improvements needed to get to the exit aspiration. This step is accomplished by combining the individual analyses done in Step 3 into a unified picture of what must be completed, what it will cost, and how long it will take. The unified picture must guide you in deciding if you have the financial resources and time needed to get to the exit aspiration. If you determine that you need outside capital to finance the changes, you need to evaluate your options for getting it. That is covered in Chapter 6. If a disconnect between required and available financial resources is not resolvable, then a partial redo of steps 1-4 needs to be done to bring financial capacity and

needs into alignment. I suggest the following order for adjusting the Measurements to get them to conform to a constraint:

a. High Value and Easy

b. High Value and Hard

c. Low Value and Easy

d. Low Value and Hard

5. Once you have a balanced view of the Measures you want to take the hard work starts. That is preparing and executing specific project plans to get the desired results. The details of how to construct your plan require extensive analysis, but my IntelliVen colleagues and I have helped dozens of entrepreneurs to generate effective exit strategies. The Toolbox page of www.intelliven.com has many forms for structuring your detailed plans.

Table 2: Example Partial Measure Priority Table for a Sale Transaction Type

Measure	Color/Value	Current Value	Value at Exit
Revenue Level/Growth Rate	Critical	$15M/12%	$40M/25%
EBITDA	Critical	$3M	$12M
Cash Flow	Critical	$1M	$9M
Balance Sheet Strength (Current Ratio)	Critical	1.5	4
Debt Service Coverage Ratio	Critical	3	9
Competitive Position	Important	#3	#1
Competitive Threat Level	Important	Medium	Low
.....			

Table 3: Example worksheet for Evaluating Changes Needed in Each Performance Assets
Measure: EBITDA

Performance Asset	Asset Improvement	Issues/Constraints
Product/Service		
People		
Sales & Marketing		
Operations		
Communications		
Experience		

Managing Your Performance Assets

In most small- to medium-sized businesses, there are 30 key functions grouped into nine categories of what I call Performance Assets. These assets are the things a company has the most control over. They are the

variables you manage to create the values in the Measures you need to have a successful exit event. This section sheds light on each asset's importance in determining how valuable your business will be at an exit.

People

Hiring and firing, compensation programs, compensation levels, leadership development, succession planning, management and peer review machinery, employee engagement, and environmental stability are the operational areas.

I believe that people may matter more than any other variable in a business for several reasons.

Productivity differentials are enormous. The Navy in the 1970s studied the productivity of computer programmers and concluded that the most productive programmers could develop 100 times as much debugged code as the least productive programmers. Since then, other studies have confirmed this result. We do not know how to measure productivity for such things as creativity or problem solving, but I believe that as with programmers, there are one or two orders of magnitude difference between the results we can achieve from the best performers over the worst.

The cost of producing any result rises with the cube of the number of people involved in the process. Other studies usually involving the development of software systems, prove this point, and, once again, I believe that there is an analog to any intellectual job function.

The implications of this cost multiplication effect are enormous. Keeping teams small improves results if the team has enough total brainpower to get the job done. The smarter the assignees, the smaller the teams can be.

The ability for organizations to operate effectively goes down in proportion to the size of its decision making body. I claim that large organizations are bad decision makers in large part because of the

number of opinions (many of which are just noise) that need to be taken into account in the decision-making process.

Strategy

Critical success factors, approach to the business, positioning (company, product, service), competition, barriers to entry, knowing how to allocate essential resources such as capital to legacy and future offerings are some of many things that strategy must address.

In a rapidly changing world, you need to conduct a periodic review of strategy and make adjustments essential to long-term success. The arrival of the COVID-19 pandemic has made such strategic review and planning even more critical. Rapid change is now accompanied with great uncertainty about the future, complicating and making more important the review of strategy. As part of the hard work of developing and keeping a strategy current, I like to ask myself these questions:

- What things, if I get them wrong, will kill the company?
- What do I do to protect the downside?
- What elements of the strategy are subject to the highest level of uncertainty?
- What highly uncertain elements of my strategy are the most dangerous to my long-term survival?
- What elements of my strategy produce the greatest opportunity for growth with the least amount of risk?
- In the current environment, do I have enough of the key resources (people, money, etc.) needed to survive and thrive? If not, what am I going to do about it?

Products & Services

Quality, price, competitive advantage, customer fit, and defensive measures needed to ensure survivability in the face of such things as price erosion are some key considerations. Over time, costs and prices decline as most offerings become commoditized. In the face of accelerating change:

- The timescale for price erosion can accelerate.
- Customer needs may shift, requiring changes to your offering/ design.

Capital

Adequate capital to finance the business now and in the future, access to capital, cost of capital, types of capital (equity or debt generally) and approach and timing for raising capital may be important considerations for you. This is covered in detail in Chapter 6.

In times of uncertainty, the environment for capital raising will be different.

Bankers assume loan risks are increased and tighten lending qualification requirements. They look for two sources for repayment, and uncertainty negatively effects their view of both. They lower the value of your tangible assets (one source of repayment) and your stated cash flow (the other most common source of repayment).

Venture capitalists slow their pace of investment and toughen terms. Their behavior is labeled as having "deep pockets and short arms." If you need capital from an existing investor, you can expect that the terms of your next round will likely be less generous than the previous round.

Angels and friends-and-and family rounds become unlikely funding sources as uncertainty is most commonly associated with decreased personal wealth, reducing or eliminating any appetite for making investments.

Timing

Having the right product and service mix for the market at the time, knowing who may be coming up on you with a better or cheaper offering, knowing how and when product and service innovation is critical to ongoing success are key considerations for most businesses. Consideration of these variables can change in uncertain times. In general, in times of uncertainty, competitive threats are softened as established companies slow their developments, and startups cannot get funded.

Experience

Having the people in place that "have been there and done that," but who have what it takes to "be here and do this" in the current market environment is important. Experienced individuals have two important qualifications:

- The more experience they have, the more they know about what works and what does not.
- They tend to be calm as previous disruptions have taught them that fear reduces the ability to think clearly.

Sales and Marketing

Distribution strategy, lead generation, funnel processing, compensation systems, tracking, and the best sales organization you can recruit are critical assets in any company. Having mature and effective processes for demand generation and fulfillment are essential for hitting growth targets in the Measures, especially those related to financial performance. Marketing programs and spend can make a huge positive impact if designed to enhance fundamental goals such as customer acquisition and retention.

Communication

Internal and external communications systems are critical to your organization's success. Your employees need to know what they must do to pull in the same direction and why. Your customers and prospects need to be kept informed about your achievements and changes. The reality is that many teams operate on the assumption that they share a common understanding of their business, strategy, offers to market, target customers and other elements. But in reality, there are often very badly misaligned views among teams. One of our specialties in IntelliVen is helping teams to evaluate and reach alignment.

Operations

Key Performance Indicators, dashboards, reviews, periodic goal reviews, tracking progress over time and similar mechanisms are essential to achieving operational efficiencies that feed into the Measures, especially around profitability and financial performance. You cannot tell the score without a scorecard carefully designed to keep everyone on track.

Ready to Get on the Path to Exit?

The template I have provided here and the outline of the Performance Assets provide a basic guide for choosing a path to exit and building a plan for the journey.

In practice, there can be many nuances to the analysis and planning because every business is unique. You may have access to capital or possess certain strategic assets that will tilt the scale toward one path or another.

Assessing these factors and formulating an achievable exit plan is one way my IntelliVen colleagues and I have helped entrepreneurs in a wide range of industries to reach their goals.

Want to explore your options? Reach out to us at www.Intelliven.com or check out my coaching services at www.johnmgrillos.com.

CHAPTER 5

The Journey to the Exit

Chapter 4 dealt with the selection and analysis of each exit path; sale, merger or IPO. The writing is oriented toward a sale but the core principals and process apply to IPOs and mergers. A key introductory thought is that the journey discussed should begin well in advance of undertaking the process of a transaction. The more time you take in advance, the better the chances of getting the company to conform to the measures that will maximize value.

The purpose of this chapter is to tell you what to expect from the process of the exit. Sections II through IX contain information that a company must assemble to support the due diligence being done by acquirers/merger partners or financial advisors to evaluate your company in advance of a transaction. Appendix A somewhat duplicates this information but adds some granularity. The details are important for

two reasons. First, examining a checklist item may reveal weaknesses in your company you need to address before undertaking the journey. Second, you may find that you do not have some of the data, in which case you need to implement processes to get it and track it. My value add to the topic is Section I, where I explain important considerations, the understanding of which can make a huge difference in the outcome of a liquidity transaction.

I. The Journey

When you get to the point where you want to pursue an exit actively, a key to the process is the selection and management of an advisor (aka M&A firm) or an Investment Bank to help with the transaction. The balance of this section covers what to expect from an adviser and what to expect from the process.

First, a cautionary warning about M&A firms and Investment Banks. They work for you, but they are subject to forces that can reduce the realized value of your company:

- M&A advisors make more in fees if they sell your company for the highest possible consideration, but they can be quick to take a lower price in exchange for getting a deal done quickly so that they can move on to the next assignment. Besides, they have a built-in and necessary conflict of interest. If they have a specialty in representing companies in your industry niche, they will have ongoing relationships with potential acquirers for those companies. Their maintenance of good relations with these acquirers, while at the same time getting maximum value for your company can be a tricky proposition for them, as their loyalty to acquirers helps ensure a stream of fees from future engagements.

- Investment Banks have a conflict similar to that of M&A firms. In this case, the buyers of your stock are clients of the bank that pay commissions to buy the stock of many other companies the bank takes public or sells. For an IPO, this conflict can mean the bank has an incentive to sell your stock below its market-clearing value so that their investment clients can get an uplift in the price immediately following your stock offering, or they can benefit by exercising their right to buy and then resell at a higher price shares from an allocation called the "Green Shoe." You have likely heard of companies "leaving money on the table" as a possible result of this conflict. In their defense, determining a market-clearing price is tricky, but I believe there is an institutional bias to price low.

Advisors work for a combination of retainer fees, expense reimbursement and a success fees payable if a transaction is closed.

1. Retainer fees range from a few thousand dollars a month to much more depending on the expected value of the company and the company's ability to pay. They are negotiable. I am not a fan of these fees because I believe that they work against the advisor working as hard as possible to make a deal happen.
2. Success fees generally work on a sliding scale (commonly referred to a "Lehman"). For example, the advisor may take 10% of the first $10M in purchase consideration, 5% of the next $10M in consideration and 3% of everything over $20M. These fees are negotiable.

An Advisor can be essential in getting a transaction concluded because that is the business they are in, but selecting the right advisor is key to getting a good outcome. Here are the key questions, the answers to which will aid you in selecting the right advisor:

1. Does the advisor have an extensive resume for closing deals in your industry?
2. Does the advisor deal with companies in your revenue size range?
3. Who will be working on your deal? It is important to have the senior personnel that have created the firm's track record work on your deal.
4. Does the advisor focus on sell-side or buy-side transactions? If you are selling, you want a sell-side specialist.
5. Does the advisor have a potential conflict of interest—e.g. they have a sell-side assignment with one of your competitors? Or, do they have a strong buy-side loyalty to a potential acquirer that could result in limiting your market or maximizing your acquisition price?
6. Does the advisor really understand your business, its warts and its potential?
7. Can the advisor show you a list of likely acquirers with solid reasons why they should have an interest?
8. Is the advisor's target list large enough, which trades off with point 10 below?
9. Does the advisor's comparables analysis used to justify a price target have other private companies in your size range in it?
10. What is the advisor's marketing plan? Will they approach a targeted and finite list of potential acquirers, or will they approach anyone on their list of buyers (aka "spray and pray")?
11. Are you comfortable with the advisor?

Be prepared for some disappointment along the path from hiring an advisor to completing a transaction. Here is why.

1. The sale process will likely take six months or longer. There are several steps in the process:
   a. It begins with the advisor's due diligence process, which can take a month or more.
   b. Preparation of marketing materials: (a "book" and supporting detail) can take weeks of drafting and reviews.
   c. Initial acquirer approaches which, with responses, will take a month or more depending on the time of year.
   d. Lots of initial meetings between the company and potential acquirers. If there are several possible suitors, this process can take a month.
   e. Acquirer due diligence, which will take a month or more.
   f. Offer or offers and attendant negotiations.
   g. Acquisition document negotiation. This can take a month or more for larger acquisitions.
   h. Closing.

2. Downward revisions to your expected valuation can occur because:
   a. The advisor was just too optimistic on the front end of the process.
   b. The advisor diligence process reveals warts that impact value.
   c. The market changes in the downward direction.
   d. Interested acquirers are unwilling to pay the target price.
   e. Acquirers' diligence reveals things that reduce the value of your company to them.
   f. Acquirers sensing they are the only ones at the party will likely take advantage of a tiring seller to get a lower price.

3. You or your advisors may overlook important considerations such as:
   a. The need for strategy changes.
   b. The need for management changes often comes up when the need for continuity past the close of a transaction is an issue.
   c. Needed product or service offering changes or additions.
   d. Needed positioning changes.
   e. Existing partnerships that somehow muddy the waters (e.g. using a distribution partner that is a competitor to an acquirer).
   f. The need to raise equity or debt to fund needed changes for a liquidity event or keep the company solvent during the process.

Working such issues well in advance of beginning the sale process can reduce their severity.

The balance of this chapter calls out the information that needs to be assembled to support any liquidity process—sale, merger, or IPO.

II. Financial Information

The information provided is slanted toward companies that sell to enterprise customers through most of it applies to any type of company.

A. Annual and quarterly financial information for the past three years—how do the following results stack up in the sector and against key competitors

1. Income statements, balance sheets, cash flows, and footnotes
2. Management financial and management reports and dashboards
3. Breakdown of sales and gross profits or margin by:

   a. Product or Product Type or Series
   b. Channel
   c. Geography

4. Current backlog by customer, customer type and/or geography
5. Accounts receivable aging schedule—with explanations about old receivables and customer concentration.

B. Financial Projections

1. Quarterly financial projections for the next (usually three) fiscal years
   a. Revenue by product type, customer, and channel
   b. Income statements, balance sheets, cash flow projections
   c. Financial results and timing for future products and services
2. Major growth drivers and prospects
3. Revenue or profitability predictability (recurring revenue, long term contracts, etc.)
4. Risks attendant to foreign operations (e.g., exchange rate fluctuation risk, government instability or negative business rules, etc.)
5. Industry and company pricing policies and comparison with key competitors
6. Economic assumptions underlying projections
7. Projected capital expenditures, depreciation, and working capital requirements and their relationship with financial projections
8. Sources and uses of capital if needed to finance the projected results

C. Capital Structure

1. Current shares outstanding, by class and preferences, associated with each class.
2. List of all stockholders with shareholdings, options, warrants, or notes
3. Schedule of financing history and terms for equity, warrants, and debt (date, investors, dollar investment, percentage ownership, implied valuation and current basis for each round)
4. Schedule of all options, warrants, rights, and any other potentially dilutive securities with exercise prices and vesting provisions.
5. Summary of all debt instruments/bank lines with key terms and conditions
6. Off balance sheet liabilities

D. Other financial information

1. Summary of current federal, state and foreign tax positions, including net operating loss carry-forwards
2. General accounting policies (revenue recognition, etc.)

III. Products and Services

A. Description of each product or service

1. Major customers and applications
2. Historical and projected growth rates
3. Market share and market share position vis a vis key competitors
4. The effect and timing of technological change on the business
5. Timing of new products, product enhancements
6. Cost structure and profitability

7. Schedule of investments needed to keep product or services competitive

IV. Customer Information (Applicable to enterprise suppliers, not retail companies)

A. List of customers comprising at least 50% of sales for the past two fiscal years and current year-to-date by application (name, contact name, address, phone number, product(s) owned, and timing of purchases)

B. List nature and summary financial impact of strategic relationships (name, contact name, phone number, revenue contribution, marketing agreements, etc.)

C. Revenue by customer (name, contact name, phone number for any accounting for 5 percent or more of revenue)

D. Brief description of any significant relationships severed within the last two years. (name, contact name, phone number and explanation)

E. List of top suppliers for the past two fiscal years and current year-to-date with contact information (name, contact name, phone number, purchase amounts, supplier agreements)

V. Competition

A. Description of the competitive landscape within each market segment, including:

1. Market position and related strengths and weaknesses as perceived in the market place
2. Basis of competition (e.g., price, service, technology, distribution, bundling, etc.)

3. List of key competitors with a detailed comparison of product, service or other important information. Competitive position vis a vis each competitor

VI. Marketing, Sales, and Distribution

A. Strategy and implementation

1. Discussion of domestic and international distribution channels
2. The positioning of the Company and its offerings
3. Marketing opportunities/marketing risks
4. Description of marketing programs and examples of recent marketing/product/public relations/media information

B. Major Customers

1. Age, status and trends of relationships
2. Prospects for future growth and development
3. Pipeline analysis
4. Issues

C. Salesforce productivity model

1. Compensation
2. Quota Average
3. Sales Cycle
4. Plan for New Hires

VII. Research and Development

A. Description of R&D organization

1. Strategy

2. Key Personnel
3. Major Activities

B. New Product Pipeline

1. Status and Timing
2. Cost of Development
3. Critical Technology Necessary for Implementation
4. Product or service offering release schedule
5. Risks

VIII. Management and Personnel

A. Organization Chart

B. Historical and projected headcount by function and location

C. Summary biographies of senior management, including employment history, age, service with the Company, years in current position.

D. Compensation arrangements

1. Copies (or summaries) of key employment agreements
2. Benefit plans
3. Incentive compensation plans
4. Equity or debt holdings or options for key employees

E. Significant employee relations problems, past or present, including identification of relatives or family members in key positions.

F. Personnel Turnover

1. Data for the last two years

IX. Legal and Related Matters

A. Pending lawsuits against the Company (detail on the claimant, claimed damages, brief history, status, anticipated outcome, and name of the Company's counsel)

B. Pending lawsuits initiated by Company (detail on the defendant, claimed damages, brief history, status, anticipated outcome, and name of Company's counsel)

C. Description of environmental and employee safety issues and liabilities

1. Safety precautions
2. New regulations and their consequences

D. List of material patents, copyrights, licenses, and trademarks (issued and pending)

E. Summary of insurance coverage/any material exposures

F. Summary of material contacts

G. History of SEC or other regulatory agency problems or licensing or operating permissions in a state or country

CHAPTER 6

Capital Raising Realities—Equity and Debt

Along the sometimes long and difficult path to an exit or IPO you may want or need capital to grow or protect your business. This chapter describes the process involved with the most sources of equity or debt. The environment for raising capital or debt goes through cycles like the overall economy. I have tried in this chapter to highlight behavioral aspects of capital and debt sources with some focus on what I expect from them in the years just following the pandemic.

Raising capital during 2020 and likely into 2021 is different than has been the case in the past. "The greatest danger in times of turbulence is not the turbulence—it is to act with yesterday's logic." —Peter Drucker. Here is why:

- Covid-19 has increased the acceleration of the creative destruction of how we do things that have been underway for some time. This created the possible need for capital needed to keep your company ahead of well-financed competitors earlier in their lives.
- Coming out of the induced coma government put most economies in is a business environment high in unpredictability, which makes the addition of capital a possible necessity for downside protection.
- The government's increased influence over the economy has uncertain implications that can make the addition of capital an important consideration.

The table below summarizes the considerations made by equity and debt investors when evaluating getting involved with a company. At each major stage of development of a company, early stage, growth stage of mature stage, what is important to an investor or lender varies as represented in the table.

Measurement	**Equity Investors (VC, PE, Family Office, Angels, Friends&Family)**			**Debt Investors (Banks, Venture Debt)**		
Company Stage	Early Stage	Growth Stage	Mature Stage	Early Stage	Growth Stage	Mature Stage
Big Idea, Large Addressable Market	X	X	Y	X	X	Y
Great Founder, Team, Board and Advisors	X	X	Y	Y	Y	Y
Product/Service	X	X	Y	Y	Y	Y
Competitive Barriers	X	X	Y	Y	Y	Y
IP Protection	X	X	X	Y	Y	Y
Revenue Growth	Y	X	Y	X	X	Y
EBITDA	Y	X	X	X	X	X
Cash Flow	Y	X	X	X	X	X
Asset Collateral	Y	Y	Y	X	X	X
Personal Guarantees	Y	Y	Y	X	X	X
Legend	X=Critical	Y=Important				

The entries in the table above are relative. For example, a "Y," depending upon specifics, can range from "nice to have" to "pretty important" in the minds of those evaluating involvement. An "X" is generally not variable, meaning that not having it is a non-starter for a lender or equity investor (save friends and family and family offices with an agenda that puts financial performance in the back seat of their investment criteria). Personal note: NEVER SIGN A PERSONAL GUARANTEE! Life is too short to deal with the financial implications of a creditor foreclosing on your assets!

What follows is an explanation of each type of equity and debt source. It is intended to give you some background needed to determine which source best fits your needs.

Venture Capital Firms (VCs)—These are professionally run partnerships that invest the capital they raise in private companies. Here is a useful introduction to the funding class. "There are…on the order of 4000 'fundable' companies a year, that want to raise venture capital… about 200 of those will get funded by what's considered a 'top tier VC'; about 15 of those will someday get to a $100M in revenue…and those 15 from that year, will generate something on the order of 97% of all the returns for the entire category of VC in that year." Marc Andreessen (very well-known and successful VC). What this means is that venture capital is hard to get.

- What they do—they invest money generally in the preferred stock of companies. Preferences include getting their money back with interest before founders, having voting rights in excess of their ownership percentages, and many other protective provisions.
- Where they get their money—mostly from state pension funds, insurance companies, large companies and really rich individuals.
- Forms of investment—equity and/or convertible debt.

- Return expectations—For early-stage companies where the risk of loss is high, VCs need to model paying a valuation that will give them 10x their investment in an expected exit 3 to 5 years in the future. For later-stage companies, return expectations are more like 3x in 3-5 years.
- Lead investors vs followers—VCs that commit capital ahead of other investors, take the lead role in the due diligence process and manage the post-investment management of the investment generally by taking positions on the company's board of directors. Followers are VCs that add to financing round sizes but generally depend on the diligence and post investment work done by the lead investor.
- Their focus—At any given point in time, or for a specific fund, VCs focus on one or more industry segments and stage of company development (early vs late stage generally).
- Dry powder and follow-on capacity — dry powder is the amount of money a fund has to continue to make investments in new and existing companies. Follow-on capacity dictates how much a fund has reserved for making investments in existing portfolio companies.
- Fear vs Greed—when times are booming, they are greedy, meaning they invest liberally at relatively high valuations and expect high valuations on sale or IPO transactions. In recessions, they demand low valuations, slow their investment pace and get tough on current portfolio companies needing additional capital.
- If you are not VC financed and are looking for a first-round you need to understand two things;
    - VCs are always looking for great (not good) deals. Square, Zoom and Air-B&B got their first rounds of VC backing during the 2008 downturn.

- In recessions, VCs develop what is called "deep pockets and short arms," meaning they are reluctant to invest in new deals, even though they have the money to do so.

- If you are VC financed you can expect in recessionary periods pressure from your investors to cut cash consumption (burn rate) and/or to become cash flow positive. If they need to provide additional capital, you can expect the terms of such capital to be punitive, meaning they end up owning more of the company and you own less.
    - Punitive terms for follow-on investments include:
        - Lower valuation
        - Pay to play—punish co-investors that do not participate in the round
        - Cram downs—are ways that investors can increase their ownership at the expense of non-participating co-investors and common shareholders.
        - Wash Outs – are ways for investors to become the major owner of portfolio companies.
    - Convertible notes—existing ones coming due will be extended with lower conversion prices and higher interest rates. New notes will have tougher terms as well.
    - Your current investors may not be able to provide additional capital. They may not have funds available for the next round, or they may be out of dry powder altogether. After the 2008 meltdown, half of the VC funds went out of business. Most of the VC funds in 2000 could not raise additional capital, and half of them eventually went out of business. Having said that, the number of firms rises dramatically when the stock

market is booming and investors like pension funds want to increase their allocation to the VC class.

- Management changes may be part of any new financial arrangements, generally involving the replacement of the CEO.

Family offices—These are VC firms that get their money from the fortunes made by their principals. Their behaviors are pretty much the same as a VC firm, with these notable differences:

- Invest smaller amounts of capital than VCs
- Generally are less well-positioned to attract professional co-investors
- Do fewer follow on rounds in existing portfolio companies

Angel Investors and Angel Networks—These are high net worth individuals or groups that invest their own money in, usually, early-stage companies. They behave similarly to VCs with these notable differences;

- They will usually invest in only one round and cannot be counted on for additional capital if things go wrong.
- They invest relatively small amounts of capital in their deals.
- When the economy gets bad, they move to the sidelines, not making new investments and not supporting the companies in which they have made investments. In other words, high net worth investors generally become low net worth investors.

Other equity-like sources

- Crowdsourcing—Getting this money requires getting the attention and support of the folks running the site. A single round is all you can expect from this source.

- Friends and Family—Like angels, this source may be good for a small amount of capital in a first round. The key problems with this source are that you are risking relationships, in addition to capital. And, generally, they will only invest in one round.
- Direct listing—this is a recent route for raising capital in the public markets. Not much is known about this other than it is hard to do and expensive.
- Shell company acquisition and reverse merger—not done much these days. It requires capital and involves a complicated and expensive process for raising capital after the merger is complete. It is done to take a company public that otherwise could not get that accomplished. Raising capital after the merger is challenging as it involves getting public market investors interested in the company, which is hard to do.
- IPO—This is the route taken by fairly large, fast-growing, profitable (or having a good story about a compelling future) companies looking to raise a lot of capital and create liquidity for their investors and employees.
- Incubators—these entities provide a little capital and a lot of advice to startups that are lucky enough to be in them. They generally do not offer capital after the small seed round, but they have a network of professional investors to whom they will introduce their companies.
- Corporate Investors—many large companies invest in the equity of private companies. Their interest is usually tied somehow to their current business strategy. Corporate investors generally move to the sidelines in times of economic uncertainty.

Debt Sources

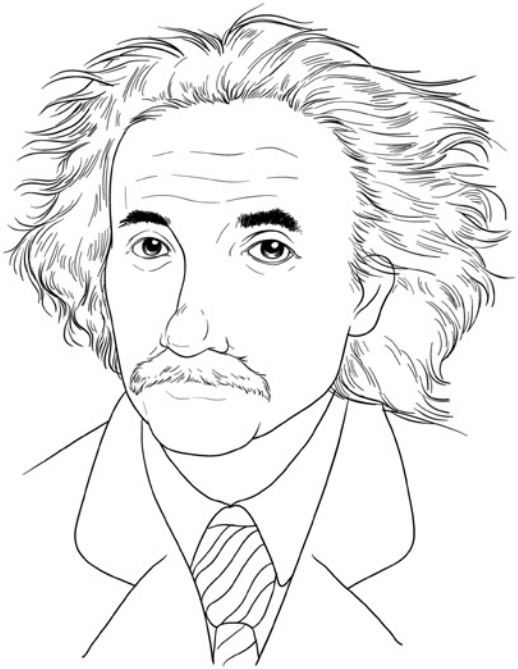
- Venture Debt—these firms invest in private companies that are backed by professional equity investors and are generally cash flow positive.
- Banks—these firms invest in private companies where they can see two ways to get their capital back. The security they attach is based on the type of loan:
    - Credit lines—secured by A/R, the expectation of future cash flow and corporate assets.
    - Accounts Receivable (A/R)—secured by the receivables and, sometimes, other corporate assets.
    - Asset Loans—secured by the assets of the company.
    - Personal Loans—secured by the personal assets of the borrower.
    - SBA Loans— are provided by the Small Business Administration (SBA). It invests in private companies generally through a convertible debt structure, meaning they will get their capital back as the repayment of the loan or they will convert the debt to equity and get the capital back by selling the stock.

CHAPTER 7

War Stories

"The only source of knowledge is experience."

—Albert Einstein



I have gone through the life cycle with nearly 30 companies. I was an investor and/or board of director's member in all of them, and CEO or Executive Chairman in 19 of them. I have mentored dozens of other CEOs. As with most of us, I have learned more from my failures than my successes. In thinking about this, I am reminded of a couple of old saws—"What doesn't kill you will make you stronger," and "Good judgment comes from experience which often comes from bad judgment."

My five over-the-wall home runs (6 counting a fund-to-fund investment in Google) taught me less than six zeros on my track record. If I knew then what I know now, at least half of the failures may not have happened, even in the face of the bad business conditions that existed when most of those failures occured. The thing I am happiest about is that on this long road, I have gotten better as a leader and human being.

Here are some highlights (and low lights) from some of the companies I worked with. In some of these writeups, I have been coy about using the full names of the companies as there may be ex-management, investors or board members that may be unhappy about my revealing certain facts about the companies. Consistent with the overall structure of the book, groups of stories are divided by:

- Economic conditions—outcomes determined primarily by a change in economic conditions over which management had no control.
- Shifts in the market—outcomes caused generally by the accelerating forces of innovation.
- Protecting the downside—outcomes determined largely because of a focus on future outcomes without considering how to survive if the future was delayed or did not materialize as hoped.
- Focus on what key operational details—outcomes determined primarily by the quality of management's focus on what matters.

Being too early to market is not included because I find it too hard to distinguish between it and having a bad idea in the first place.

The writeups below cover companies whose main challenge was a change in the state of the overall economy.

- LWM— was a semiconductor technology company developing a wafer fab technology that would reduce the size of integrated circuits dramatically. It had a great team and deep-pocketed investors. Late in 1999, it had an offer for purchase by a large equipment manufacturer, but the board got greedy and dragged their feet on the negotiations hoping to get a better price. Unfortunately, before a deal could be concluded, the company got caught up in the 2000 downturn, which cratered the deal and, subsequently, the company.
- WorldSage— When the 2008 crisis hit, I was in the middle of rolling up 13 European private universities into a public company I had acquired. The concept was to trade my public shares for the target schools' shares and make a large secondary stock offering on the NYSE. The school owners would benefit from getting a financial exit for the years they spent building their schools. My team would benefit from building a large education holding company with revenues of 250 Million Euros. The crisis killed the company, and I folded it up after distributing the remaining cash to investors.
- MVC Capital— In 2000, we raised $330M in an NYSE listed retail investor-focused IPO to democratize venture capital. A few months after the IPO, the public market for tech stocks crashed, and the fund became vulnerable to hedge funds wanting to raid the fund for its cash.

The writeups below cover companies that were challenged by shifts in their markets.

- ZP intended to disrupt the print reference book publishing business with CD ROMS. It acquired the rights of market-leading encyclopedias and dictionaries, among other reference material and began selling product. The company subsequently went bust as the content became available on the Internet for free.

- VsSW developed a graphical user interface for popular versions of the UNIX operating system. They intended to sell the product to companies distributing versions of UNIX. Their plan was disrupted by a company that developed and sold for a very low price, a vastly inferior but sufficient competitive product. The company consequently went bust.
- PFM was an early venture-backed company developing the first videogame platform for remote players to use on the internet. The market changed when their communications providing partner decided not to involve themselves in the business. The company consequently had to pivot and luckily marketed a screensaver one of its developers had created as a computer toy. That lucky pivot allowed the company to be sold to a large player in the computer gaming business.
- SS— provides a content development software platform to the higher education marketplace. The company's expansion into the US market did not go well, caused by a product/market fit problem that plagued all companies offering similar products. We decided to exit the US market and sell the company. This decision radically reduced the company's cash burn rate and allowed it to survive until a sale was completed. Relatively speaking, the outcome was great as the sale price was higher than that of a competitor that had raised and burned through nearly $100M, before being sold for very little consideration.

Here companies that did not survive because they did not manage their resources to deal with likely delays in getting their products to market—they did not protect the downside.

- SCT had a great idea for a product that increased the range of current cell towers by order of magnitude. However, the product implementation required a superconductor technology that

delayed product implementation beyond its financial runway. Investors lost confidence in the management team's ability to deliver, and the company went bust.

- IWC was formed to provide wireless communications infrastructures in several developing countries. The idea was that developing countries could not afford to build a wired telecom infrastructure, and today we can confirm that their assumption was correct. The deals took too long to finalize, and the company ran out of money before it could prove the business model would work. Investors lost confidence in the management team's ability to deliver, and the company went bust.
- W.c was going to disintermediate the alcohol distribution model by promoting and selling wine online. That model has struggled for a couple of decades as alcohol distributors have significant political clout, and laws governing mail-order alcohol vary widely.

The successful companies listed below were successful because of their focus on what mattered.

- CBT Systems (which later became SmartForce and later merged with Skillsoft) was in the online technical training space. It became the largest company in its market fueled by a creative revenue model, relentless focus on outcomes and a great management team. The company went public and, for several quarters, was one of the "darlings of Wall Street."
- Tsrct was a very small personnel software company financed by a Silicon Valley VC with two key problems. It was not selling enough to be profitable and its product was missing payroll functionality (a critical application). As the CEO I solved the first problem by hiring a world class VP of sales who brought her team with her from a competitor. We solved the payroll

functionality problem by entering into a partnership with three large customers who financed the $5 million needed to build a payroll system.

- SPSS was, at the time I joined it, number 2 in the statistics and graphics software market. Its primary competitor, the SAS Institute, was ten times its size, very well run, and seemingly not interested in having competitors. I joined the company as its CEO under the presumption that improvements in operational management would solve what turned out to be a product strategy problem. The owners of the company were trying to compete head-to-head with SAS and were failing at it. Raising capital to continue with that strategy was not possible for several reasons. What was needed was to pivot to a market space where SPSS could erect protective barriers. Our research and some testing convinced us that porting the product from mainframes to PCs and focusing marketing efforts on data analytics functions in corporate marketing departments could be our solution. The market fit was good, and SAS could not follow as their system could not be ported to the smaller capacity of a PC. This pivot, along with needed operational improvements put the company on the growth path that lead, a few years later, to a successful IPO.
- VTCorp was an early producer of PC based technology for video conferencing. It operated as number three in its space and was losing business to two better-financed competitors. There were two keys to saving the company: positioning and additional capital. We determined that our competitive advantage was our application software, which provided call and participation management, Zoom long before Zoom. Positioning the product line behind the application software engaged a growth ramp and financing needed to grow the company to an IPO. The company went public in 1992 and

later purchased one of its two larger competitors. The current company, taken private in 2002, provides PC based hardware and software to support Zoom conferencing.

- Summit Design provided circuit design software. It had a good product, but with a replacement of the CEO with someone with a relentless focus on what mattered, we got the company public, producing a large return to investors and management.
- NTT Training— Four months after shutting WorldSage down, I acquired NTT Training in Centennial, CO. Its revenues were $10M and it was bleeding cash at $50K/month. I bought its shares for $1. Its owners saw that as a better deal than bankrupting the company or continuing to feed it cash. During the three years I owned it, we increased revenues by 30% without investing any money. We sold it for $10M cash in 2012.

CHAPTER 8

The Short Pitch

I hope this book has helped you determine what you need to do to maximize the exit value of the company. But change is hard. The dreaded day-to-day can divert you from staying on track. Getting your management team and employees to do what they must to implement change compounds the difficulty. Successful implementation requires consistent application of procedures and policies at all levels of the organization to ensure change happens. Using outside resources whose job is to make sure change happens increases the odds of success by a lot! A coach for you and coaching/consulting resources for your employees are the only guaranteed way to ensure successful change happens. Here are a couple of sources for your consideration.

www.johnmgrillos.com for coaching

www.IntelliVen.com for consulting and training

APPENDIX A

Sample Due Diligence Checklist

This is a detailed list generally used by investors in doing their due diligence. It overlaps with the list above but adds some things that company owners may need to know about should they be seeking financing from professional investors.

1. Basic Corporate Documents:
    a. Articles of Incorporation, including all amendments.
    b. By-laws, including all amendments.
    c. Minutes of all meetings of directors, committees of directors and shareholders, including copies of any written notices (if given) or waivers thereof and any written-consent to action without a meeting.
    d. List of all states where property is owned or leased or where employees are located, indicating in which states the Company is qualified to do business.
    e. List of all countries where the Company is doing business, indicating in which countries the Company is qualified to do business.
    f. Samples of common and preferred stock certificates (if any), warrants, options, debentures and any other outstanding securities.
    g. Copies of any voting trust, shareholder or other similar agreement covering any portion of the Company's shares.
    h. Copies of all agreements relating to repurchases, redemptions, exchanges, conversions or similar transactions.

i. Copies of all agreements containing registration rights or assigning such rights.

j. Copies of all agreements containing preemptive rights or assigning such rights.

k. Stock books of the Company.

l. All quarterly and annual reports and any other communications to the Company's shareholders within the past five years.

m. All press releases issued by the Company within the past five years.

n. List of all subsidiaries.

2. Documents for any Subsidiary: Same as those listed under No. 1 above.

3. Securities Issuances:

   a. Equity Financings: copies of any stock purchase agreements.

   b. Debt Financings: copies of convertible debt agreements.

   c. Stock option or purchase plans and forms of option or purchase agreements which have been or may be used thereunder.

   d. Any other agreements relating to securities sales by the Company, including any private placement memoranda or other offering circulars.

   e. Blue Sky permits notices of exemption and consents for issuance or transfer of the Company's securities and evidence of qualification or exemption under other applicable state blue sky laws.

   f. Forms D or any other forms filed to establish an exemption under the Securities Act of 1933.

4. Shareholder Information:
   a. Records setting forth all issuances or grants of stock, options and warrants by the Company, listing the names of the issuees or grantees, the amounts issued or granted, the dates of the issuances or grants, the number of shares presently exercisable (if applicable) and the consideration received (or to be received) by the Company in each case.
   b. Lists of all current shareholders, including addresses and numbers of shares, owned.
   c. Numerical listing of stock certificates showing certificate number and date, name of the shareholder, number of shares, date of Board approval and permit and tracing transfers.
   d. Lists of all options proposed to be granted, if any, including names and addresses of proposed option holders and the number of options to be held by each.

5. Material Contracts:
   a. Bank line of credit agreements, including any amendments, renewal letters, notices, waivers, correspondences, etc.
   b. Other agreements evidencing outstanding loans to or guarantees by the Company, including correspondences.
   c. All outstanding leases for real and personal property.
   d. Material contracts with suppliers or customers. Please indicate which suppliers are the sole source.
   e. Model sales or manufacturing contracts.
   f. Agreements for loans to and any other agreements (including consulting and employment contracts) with officers, directors or employees, whether or not now outstanding.

g. Schedule of all insurance policies in force covering property of the Company and any other insurance policies such as "key person" policies, director indemnification policies or product liability policies.

h. Partnership or joint venture agreements.

i. Bonus plans, retirement plans, pension plans, deferred compensation plans, profit sharing and management incentive agreements.

j. Form of employee confidentiality/invention assignment agreement.

k. Any other material contracts outstanding.

6. Patent and Trademark Matters:

a. List of all foreign and domestic patents and patent licenses held by the Company.

b. List of any trademarks, trade names or service marks.

c. List of any copyrights.

d. Copies of all material agreements for licensing of Company technology to third parties.

e. Copies of all material agreements for licensing of technology from third parties.

f. Describe the importance of existing patents and whether additional patents are necessary.

g. Any correspondence from third parties regarding potential infringement of the intellectual property rights of others.

h. List of proprietary processes controlled by the Company.

i. Please provide the law firm's name that handles patent and trademark matters for the Company and the contact there.

7. Manufacturing:
    a. A breakdown by manufacturing site of the products manufactured, personnel employed, number of shifts and capacity, if any.
    b. List of major suppliers showing total and type of purchases from each supplier during the last and current fiscal years, *and indicate which are sole sources.*
    c. List of contract manufacturers or assemblers, if any, showing total and type of purchases from each contract manufacturer or assembler during the last and current fiscal years.
    d. Material or outside of the ordinary course of business contracts with suppliers, manufacturers, etc., if any.
    e. Description of all toxic chemicals used in production and manner of storage and disposition. Description of any EPA or other investigation or claim.

8. Operations:
    a. List of third party developers showing total and type of project for each developer during the last and current fiscal years, contact names and phone numbers, together with forms of agreements entered into with third-party developers.
    b. List of third party software duplicators and manual publishers showing total and type of services from each duplicator and publisher during the last and current fiscal years.
    c. Form of agreements relating to the sale or lease of material capital equipment.
    d. List of largest material accounts payable with contact names and phone numbers.

9. Sales and Marketing:
    a. Copies of all market research or marketing studies conducted in the last three years.
    b. List of the Company's products and services.
    c. List of the Company's competitors.
    d. List of the Company's customers or representing as a group 50% or more revenues in each of the last two fiscal years, indicating the types of products and the amounts of each purchased, and contact name and phone number for each customer.
    e. All material licensing agreements, franchises, and conditional sales contracts to which the Company is a party.
    f. Agreements with distributors, VAR's, OEM's, dealers and sales representatives.
    g. Copies of long-term sales contracts.
    h. Company-financed customer purchase agreements, if any.
    i. Service and support contracts and marketing agreements, if any.
    j. All material agency and advertising contracts to which the Company is a party.
    k. Forms of warranties and guarantees provided to customers.
    l. Copies of all market research or marketing studies.
    m. Copies of sales literature and forms, including price lists, catalogs, purchase orders, etc.
    n. List of top 20 accounts receivable with contact names and phone numbers.
    o. Backlog at the end of the most recent fiscal year and the most recent fiscal quarter.

10. Tangible Property:
    a. List of real and material personal property owned by the Company.
    b. Documents of title, mortgages, deeds of trust and security agreements pertaining to the properties listed in (a) above.
    c. All outstanding leases for real and personal property to which the Company is either a lessor or lessee.
    d. List of any security interests in personal property, including any UCC filing.
    e. Documentation of significant acquisitions or dispositions of assets.

11. Litigation and Audits:
    a. All letters sent to auditors in connection with year-end and current interim audits, including "litigation letters."
    b. Copies of any auditors' letters to management regarding internal accounting controls.
    c. Descriptions of (and reasons for) any change in accounting methods in the past three years.
    d. Active litigation files, including letters asserting claims, complaints, answers, etc.
    e. Any litigation settlement documents.
    f. Any decrees, orders or judgments of courts or governmental agencies.
    g. Description of any warranty claims which were made against the Company, any subsidiary, or any partnership or joint venture and the resolution of such claim.
    h. Information regarding any material litigation to which the Company is a party or in which it may become involved.

12. Environmental:
    a. Schedule of Hazardous Materials stored, manufactured or located at any facility of the Company either now or in the past, or that the Company ships or transports. (Hazardous Materials means any substance or any material containing a substance that could be considered toxic or hazardous under Federal or state law, including solvents, petroleum, pesticides, paints, asbestos-containing materials, lead-based batteries, radioactive materials and PCB containing transformers.)
    b. Schedule of chemicals, toxic substances or air contaminants regulated by OSHA present in any facility of the Company.
    c. Schedule of any incidents involving the release of a potentially hazardous amount of any carcinogen into or presence of asbestos in the workplace.
    d. Schedule of all instances in the past in which the Company has corrected unsafe working conditions.
    e. Schedule of all the Company's facilities that discharge waste into any body of water, stream or any sanitation systems.
    f. Schedule of all permits or approvals obtained from any governmental body responsible for environmental or health regulation.
    g. Schedule of all occasions in which a liquid or solid waste material or any fuel or other Hazardous Material was accidentally or intentionally spilled or released.
    h. Any notices of violation or requests for information that have been received or threatened at any time for the alleged failure of any facility to comply with applicable air pollution laws or with any air quality permit.

13. Employees:
    a. Description of any significant labor problems or union activities the Company has experienced, including any collective bargaining agreements.
    b. The number of employees broken down by major types of employees and a management organization chart.

14. Management:
    a. Completed copies of Directors' and Officers' Questionnaires.
    b. Detailed resume of directors and top management personnel.
    c. Founders agreements, management employment agreements, indemnification agreements, and ''golden parachute'' agreements, if any.
    d. Schedule of all compensation paid in the most recent fiscal year to officers, directors and key employees showing salary, bonuses and non-cash compensation (e.g., use of cars, property, etc.) separately
    e. Bonus plans, retirement plans, pension plans, deferred compensation plans, profit sharing and management incentive agreements.
    f. Agreements for loans to and any other agreements (including consulting and employment contracts) with officers or directors, whether or not now outstanding.
    g. Description of any transactions between the Company and any insider (i.e., officer, director, or owners of a substantial amount of the Company's securities).

15. Other:
    a. Copy of any internal or outside studies of the Company or the market for its products (*e.g.*, management consultants).
    b. Summary of all OSHA inquiries (if any).
    c. Summary of all EPA, EEO (etc.) inquiries (if any).
    d. Summary of all Department of Labor inquiries.
    e. Status of contracts subject to Renegotiation Act.
    f. Summary of Federal, State, local and foreign income tax status, *i.e.*, Have all returns been filed? All taxes been paid? Any audits by taxing authorities?
    g. Permits for the conducting of business, including licenses, franchises, concessions and distributorship agreements.

APPENDIX B

Government Involvement in the Economy

If you are smart and want to make a million dollars a year in the US, get hired by Google. If you live in China and are smart and want to make a million dollars a year, get hired by the government. I made the case in Chapter 4 that intelligence matters, and I am not optimistic that the government's increased influence on the economy will be managed by the best and brightest. Having smart people in government is key to getting the best we can from the legislative process. The legislative bodies set the overall agenda, but government bureaucrats sort the details and the smarter they are, the better the outcome.

We demonstrated in Chapter 7 that for institutions the cost of making a decision goes up with the cube of the number of people involved in

the decision. This problem is much worse in the US federal government because, besides its size, the agendas of individuals involved in decisions vary widely based upon the interests of voters in each legislator's home district and the enforcement of strict party rules on voting. Large successful private companies have avoided this problem by organizing themselves into smaller working units where effective and efficient decision-making can be accomplished. Unfortunately, the US constitution does not facilitate this kind of solution to the problem. The party line enforcement has created a toxic environment where the acquisition of power trumps serving the country. We can, therefore, expect the government's growing influence in the economy to be fraught with poor and slow decision making.

The reason for increased government control of the economy is pretty simple. As a percent of GDP debt by sector (I believe excluding debt instruments used for investments) as a percent of GDP is:

- Federal government—88.9%
- State and Local Government—14.4%
- Household—75.4%
- Business—74.9%

(Source: Federal Reserve Bureau of Economic Analysis)

Federal government spending to date as a percent of GDP is approaching 35%, according to the St. Louis Fed. That level is the second-highest in the past two centuries, being outdone only by spending during WWII. The US is $20T in debt now. By the time we exit the Covid recession, that number will likely be $23-25T ($2.2T approved in 2020 by the administration and another $1-2T likely addition in early 2021). The likelihood of writing off $1.5 T of the student debt problem the government created, and the over $1T "normal" deficit we have seen annually since Donald Trump took office. Other additions to the deficit will be infrastructure repair and mitigation of the effects of

climate change, both of which will add trillions of dollars to the debt. As Congress muses about the second installment on the current support program, fringe spending ideas have moved into the mainstream, such as a guaranteed minimum income and government control over private sector investment incentives and executive compensation. When we get to a point where the government can no longer make debt payments and its other obligations, a deleveraging will occur involving three activities. Taxes will increase considerably, especially on the wealthy. (After WWII, the top marginal individual tax rate was 95%). Large volumes of money and money substitutes will be created (with its attendant inflationary pressures), and debt restructuring will occur (treasury bondholders will not get all of their principal back). The need for deleveraging will trigger a recession, as has been the case with Greece and other countries who have had to go through it. Warning signs of the coming of the event in the US will be restructurings that will occur in some states, including Illinois and California, which will occur earlier because of their inability to print money. Ray Dalio did a great presentation explaining how the economy and deleveraging work. See it on YouTube. https://www.youtube.com/ watch?v=PHe0bXAIuk0.

APPENDIX C

Brave New World—Forces Affecting All Companies

I believe the forces of innovation will play an increasingly important role in economic activity. AI and Robotics are at the top of my impact list. Is this something you need to plan for as a value enhancer for your business or as a major threat to it? Stephan Hawking and Bill Gates have expressed their fear that AI is a threat to mankind. It is coming fast, as suggested in the below link, an interview conducted by Tony Robbins with Sophia, a three-year-old very sophisticated AI Robot (synthetic life form?).

https://www.youtube.com/watch?v=Sq36J9pNaEo

I believe there is an interesting race developing between machines and human evolution. By evolution, I mean integrating the mind and body with technology. For example, we are likely pretty close to connecting a chip to our brain that provides us with all of the information needed to know anything or solve any problem. (Watching my grandkids with their smartphones leads me to conclude the step to an implanted chip is a mere detail), or to head off a mutiny by the machines.

Conventional wisdom based on recent history says that 25% of today's jobs will be gone in 5 years, replaced with a larger number of jobs, the requirements of which are not known. So far, so good. But even assuming the job creation trend will continue, those new jobs will require a higher skill level than the ones that were lost, requiring the retooling of displaced workers with skills that they may or may not be able to master. The past attempts to retool most of them had failed when the skill differences between the old and new jobs were large. Historically, the economy has written those workers off, and they went on welfare (long-term disability, I believe they call it). Besides the claims made in Chapter 3 about how education will change to support effective retraining, we can expect:

1. Immigration has and will continue to alleviate the problem somewhat to the extent that immigrants have the skills for the jobs of the future. This source of workers is very important because;
    a. In the US, the ratio of people working to retirees is 2.9 to one and is expected to drop to 2 to 1 by 2030. The ratio needs to be 3 to 1 to support the retirees given the current tax structure.
    b. Acceleration of job displacements will put upward pressure on the number of retirees and, possibly, downward pressure on the number of workers.

2. Industry is accelerating the use of AI and robotics in part because of the inability to recruit workers. For example, four years ago US industry could not find 500 thousand skilled trades workers to fill open positions. By the beginning of 2020, that number grew to over a million.
3. Even as AI and Robotics continue to invade most job areas, new industries and jobs will be staffed initially by people. Automation comes later once the detailed nature of the work is known and incorporated into the data sets that program machine learning.

APPENDIX D

Growing a Company's Management in the Covid Disrupted Business Environment

Covid is likely making you rethink important aspects of your business. Critical to surviving and thriving will be the decisions you make about your management team. If you do not have the right people to implement needed changes in your business strategy/model, you need to retrain who you have and/or hire new key contributors. Roles that may need strengthening include management team members, members of the board of directors and advisors.

Hiring senior management starts with figuring out what you need and why you need it. Figuring out what you need can be derived from the

business plan reflecting the current business climate and operating restrictions. Key elements of any plan include:

- The market the company serves—its size and geographic range, and how the current business climate has changed it.
- The problem the company solves—its size, severity, etc.
- The solution the company provides—product and/or service.
- The purchasing process—who has the budget, who is the sponsor, who else is in the decision loop, and how long is the purchasing process from lead qualification to closing and payment.
- How the company works
  - How the company does what it does
  - How the company creates demand for what it does
  - How the company will scale what it does and how it creates demand
- Competition—analysis of competitors, comparisons and competitive advantages.
- Traction.
- Business model— product business, service business, recurring revenue business, etc.
- Financial projections.
- Use of available or acquirable capital.
- Team, advisors and board of directors—including experience, titles and roles.

Here are some key considerations regarding recruiting the right people:

- Credentials—many things can be considered there, but there are a few that are of overriding concern.

  - Demonstrated success in pivoting a company when its business was not working.
  - Experienced in one or more companies that have a deserved reputation for excellent management performance.
  - Some proven experience in companies of a similar size to yours. Too often, persons with all of their career-shaping experience in larger companies bring ways of doing things that do not fit well in smaller companies.
  - Having proven skills in solving the specific issues of interest to your company currently.

- Culture fit—finding people with shared beliefs and behaviors about how a company's employees and management interact and handle outside business transactions and interact with each other.
- Shared vision—it is essential the founders and new executives have a shared vision of where the company is going and how it will get there. The business plan details are a starting point for determining if visions align. Still, founders must be able to convince themselves that the whole team will move together when external events change the business plan. Mike Tyson entered each fight with a plan, which lasted until the first punch landed.
- Broad acceptance—any added executive should have been vetted by the broadest set of current employees as possible, and the opinions of the interviewees should be an important input to the hiring decision. You want a job at Google, easy to do after surviving a couple of dozen interviews. Broad acceptance helps guarantee a broad interest in creating a bond between current and new employees.

- Demonstrated interest in the business—management candidates should be put through a drill that measures their grasp of the company and its history and how their approach to doing their job will enhance its likelihood of success.
- Alignment—involves new contributor's commitment to creating the communications needed to keep everyone moving in the intended direction.
- Trust—it is essential that top management's "gut instincts" support the notion that a new hire can be trusted and testing that trait with a person's previous business associates is an important due diligence item.
- Ability to do the job—this most important consideration should be tested as thoroughly as possible before hiring. One measure is confirmed, if possible, performance in previous jobs. Another is making recruits construct in writing what they will do in their first month or two of employment.

APPENDIX E

Small Business Reorg Act of 2019

If you are a small business struggling to survive, you may have the leverage you can use to control your liabilities and stay in business. The Small Business Reorganization Act of 2019 is a change to Chapter 11 bankruptcy law and generally applies to business debtors with secured and unsecured debts less than $2,725,625. More on this below. The key point of this writing is that you can use the threat of invoking the act to renegotiate your liabilities, avoiding the cost involved in hiring a lawyer to navigate the processes of the act. Here are the key benefits of the act.

1. Only the debtor can propose a plan of reorganization, avoiding the need to get approvals from creditor classes.
2. The act removes the requirement that equity holders provide "new value" to retain their equity interest without paying creditors in full. The act only requires that the plan is fair and equitable and provides that all of the debtor's projected disposable income will be applied to payments under the plan (or the value of property to be distributed under the plan is not less than the projected disposable income of the debtor).
3. If you provided your residence as collateral for business loans, the act protects your home equity from seizure by creditors.
4. The act now stretches the payment of administrative expense claims out over the plan's term instead or requiring payment on the effective date of the plan.

5. The court must grant the debtor a discharge after completing all payments due within the three to five-year plan schedule. The discharge relieves the debtor of personal liability for all debts provided under the plan (with two minor exceptions).

The act is helpful to small businesses but keep in mind that a federal process is a process, taking much time and energy to complete. My experience is that most creditors are sympathetic to your plight and may be having their own financial problems. I can help you work with them to your mutual benefit as I have done with many companies during three other economic downturns. Contact us through our site www. johnmgrillos.com.

Let's get through this together.

The most useful aspect of the act is that it can be an incentive for creditors to play ball with you without you going through the pain of the process.

About the Author

Who is John Grillos?

John is a successful entrepreneur, company financier, exit coach, and IntelliVen Principal Consultant with an impressive four-decade track record in every aspect of starting and growing companies and orchestrating successful exits. Here is how John explains what he has learned and what drives him:

My passion is helping companies become leaders in their markets. I have developed the needed skills to help company owners and CEOs over several decades as a C-suite operator and financier of dozens of companies. I started or bought, built and sold two companies. I managed four venture capital firms, including two I founded, with combined capital under management exceeding $500 million.

I have been a highly influential director of over two dozen for-profit, both private and public, and non-profit organizations. My efforts have helped create billions of dollars in market value and thousands of jobs.

I have gone through the company life cycle with nearly 30 companies. I was an investor or board member in all of them, and CEO or Executive Chairman in 19 of them.

My ventures and professional investment initiatives have been associated with a broad range of industry success stories, that have helped create billions of dollars in market value and thousands of jobs.

Today I help entrepreneurs and owner-operators plan their own paths to exit via my mentoring and coaching services.

The Art of the Exit

- ✓ ***Broad Macro-Economic Forces***
- ✓ ***A Look Into the Future***
- ✓ ***Picking Your Exit Path and Managing to Maximize Value When You Get There***
- ✓ ***The Journey to the Exit***
- ✓ ***Capital Raising Realities—Equity and Debt***
- ✓ ***War Stories***
- ✓ ***The Short Pitch***

John Grillos

Who is John Grillos? John is a successful entrepreneur, company financier, and exit coach with an impressive four-decade track record in every aspect of starting and growing companies and orchestrating successful exits. Here is how John explains what he has learned and what drives him.

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