Pitch PERFECT

science

One of the country's leading figures in life sciences, **Dr Andy Richards**, recently spoke to the Numatis FD Club in Cambridge about how to make potential investors want you even more than you want them. Anna Ryland reports

Psychology of financing: The players

"ENTREPRENEURS often compare working with VC investors to swimming with sharks. However, despite their often predatory behaviour, I would say most investors are more akin to sheep. VCs, angels, public market and crowdfunding investors all exhibit sheep-like behaviour. They are comfortable when they are in the pack and often uncomfortable when alone. This herd-like behaviour is a major driver for cycles in the public markets and the fashion aspects of investment.

"The venture investment process should be easy. You prepare a good business plan, you contact the universe of investors, you present to them, they do due diligence, you get multiple term sheets and you close. It shouldn't take much time."

Yet one of Andy's current ventures has been financing continuously for 18 months. "Can the process be made more predictable?" he asked. "Perhaps it can and the key may be in understanding the dynamics of the process – the psychology of financing."

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Dr Andy Richards

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Planning and preparation

“A good FD should always be thinking and planning for the future financing of the business and be a sophisticated conductor of this process. They should be looking for answers to the question: why would we need to be financing and when? It’s about mapping and qualifying investors and the best time to find suitable investors is when you are not financing.

“FDs and CEOs should be talking together to potential investors in order to qualify them. They should also have an intelligence network to help them assess how different investors behave, what their processes are and who the best contacts are. FDs should develop a database of information about who is financing whom, what was the syndicate, what were the dynamics, what they liked and what they did not.

“During financing, they should think about roles within the company’s executive team. Who is going to do the selling, who will manage the process and who will collect the feedback (preferably not the person who does the selling)?

“Who is going to keep the business on the road during the whole process? Who is going to be the sheepdog and who is going to blow the whistle? Don’t forget about your non-executive directors, who often have multiple hats and, as a result, have diverse contacts and perspectives on the business and on investors.”

The business plan and the pitch

“A business plan is an internal process which should help a company be completely honest about its strengths and weaknesses.

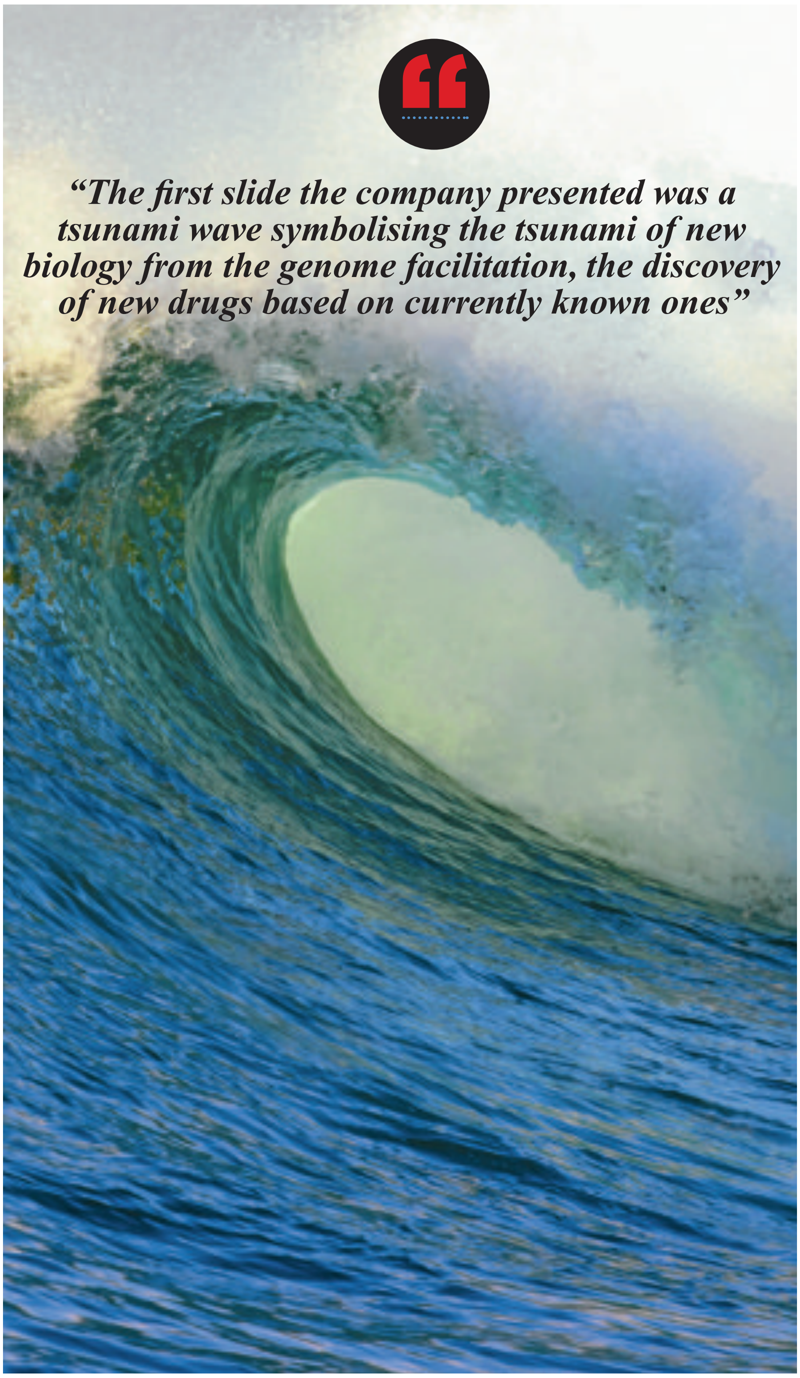
“However, so often, a business plan is put together as an external document that reflects different peoples views of what the company should be about. Such differences of opinion mustn’t come out during the presentation to investors. If cracks in the team became visible at that stage, the investors will drop the pitch but won’t communicate the real reasons to the team.

“The team and the FD need to decide before the pitch how this information fits with the positioning of the company in the market and, more importantly, in relation to the current fashions.

“Don’t forget, investors are sheep and they follow trends, often slavishly. You need to understand where your company fits on the fashion barometer, such as ‘The Gartner Hype Cycle’ and decide how you are going to position the business in relation to that curve.”

Andy illustrated that point with one of his “war stories”. “At the beginning of 2000, the market was in the throes of the genomics revolution, with the human genome having just been sequenced.

“Arakis, of whom I was CEO, was a product-based company, developing products based on re-profiling known drugs, which wasn’t a high science. However, the first slide the company presented was a tsunami wave symbolising the tsunami of new biology from the genome facilitation, the discovery of new drugs based on currently known ones.



“We unashamedly positioned ourselves as a part of the zeitgeist, doing something that everyone wanted to be a part of and this certainly contributed to convincing investors.”

The financial model

“The financial model is a crucial tool during the financing process. It should help the management board have their eyes wide open to all potential options and be flexible throughout the process, as most plans evolve during financing. Independently and in addition, you should have your own valuation model.”

Targeting investors

“Start from answering the question: who not to see? There are many examples of people wasting their time seeing people who will never invest in them.

“For instance, your business may not fit with their criteria. They have no history of investing in companies like yours. Importantly, don’t waste time on companies that don’t have money and are not investing at the present time. These investors still fill their days seeing companies and pitches so use them as cannon fodder for pitch practise by all means, but do that knowingly.

“Also be aware that many funds when they contact a company out of the blue are conducting competitor analysis, not looking to invest. They will only waste your time. You should also be aware of investors that dislike each other because they will publicly drop you when they find out that you’re dealing with their adversaries.”

Qualifying references

“Who should you see? When should you see them and in what order? Keep a focused list of potential investors and don’t send your business plan to all and sundry. Never email your plan to anyone to whom you haven’t already had a verbal introduction. Work out who has bandwidth as it is also a waste of time to send your plan and chase investors who are totally occupied doing a different deal.

“You need to identify leaders and followers among your potential investors and see several second division people first. Most likely your first few pitches will not be very polished. Therefore, test your pitching skills on them.

“Next, work out the theatre of the pitch. Who is doing what and how should it feel? Most selling is done in the first few seconds, so make an effort to assess what effect your first words have on your audience. An FD may well be well positioned to judge this.

“Then maintain momentum, which is often easier said than done. It’s about understanding their processes and their politics. Be aware there are often rivalries and scores to settle inside VC partnerships and investment committees.”

Due diligence

“Due diligence is not just about reviewing all the data and ticking the boxes, more often it is about a process of discovering whether the team of the business in which they are about to invest is able to respond to challenges. You can also use it to your advantage. You can keep them busy. Many funds have a rule that they can only have three opportunities on the go. You have to make sure that your project is at the top of their list. If you keep them working on your deal during the due diligence process, they are not working on others. The more time and energy they invest, the greater their sense of loss or waste if the deal does not happen.

“However, if you get a feeling that an investor is not going to invest in you, then tell them that, terminate the relationship first, reject them before they reject you. They may be hugely relieved, as they hate to say ‘no’, especially to people they like; that is only human nature.”

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Responding to feedback

"During the course of the financing process, you'll get a lot of feedback and listening to it is key. You need to identify a person in your company who is good at listening. That person should listen, analyse the feedback and take heed. The feedback is often about economics and valuation, yet the most important part of it is about the team, and often this is a specific role for NEDs."

Term sheets

"At this stage, the ultimate decision is made, and this is definitively the wrong time to expose divisions within your team, at best you get 'divide and rule' at worst the investors will head for the hills. The golden rule applies, namely 'He with the Gold sets the Rules!'"

Triggers

"Finally, you will be thinking: how do I move things forward? How do I get someone doing due diligence to put a term sheet on the table and close the deal? That often involves setting up 'triggers' both real and psychological and this again is easier said then done.

"Don't take the whole process personally. Even when planned exquisitely, so much of it is about timing and luck."

Andy illustrated his final point, with a "war story'" about a pitch which he managed while working at Arakis.

"Apax, who at the time was a major venture house, desperately wanted to invest in Arakis. We played the psychology perfectly, applying real timing pressure so they told us that they would do the whole due diligence process in one day.

"Hence we lined up nine hours of presentations to their expert team. We started at 8am and ran through the whole day, with each presentation flowing seamlessly from the previous one. At 5pm, someone walked through the door and said that an aircraft had just crashed into the World Trade Centre in New York. The presentations stopped and we heard nothing from them for a month . . . the world had changed."

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Numitas is a professional services organisation providing the expertise of its finance directors on an interim and part-time basis, as well as finance executive search services. A unique asset of the company is its FD Clubs that bring together senior finance executives who work in different industry sectors in the East of England. The quarterly FD Club events are informal gatherings of finance professionals who network with peers and debate key issues with high-profile business speakers.