

Investing in Private Companies: Risk Management Tips for the Minority Investor

By Reuben Buchanan, Director of Integral Capital Group

In today's information highway there is no shortage of advice on how to successfully invest in the stockmarket, but very limited information on how to invest into private companies. This is especially more tricky if you are a minority investor and have no control in the company. The main difference between investing into public ASX listed companies, and private ones, is liquidity. There is no ready market for private companies should you wish to exit your position.

The only way you can really get out of the investment is when there is a liquidity event, such as a trade sale or IPO, initial public offering of a firm's first sale of shares. This may take years, if ever, so there are certain steps you should take prior to investing into your neighbours 'exciting new venture that's sure to go global'.

How can I become a private investor?

Anyone can become a private investor, but in order to be a successful one there are some risk management tips you should heed first:-

- You need to have capital that you can invest and a willingness to accept risk with the investment, ie. only invest money you can afford to lose.
- It's best to have some experience of running your own successful business or businesses. The more experience the better.
- You need to be keen to get involved in start-ups and developing companies in a hands-on way should the need arise.
- Do plenty of due diligence on the promoter through ASIC and other background searches. Get some references from the promoter and check up on them. You basically want to know what kind of a track record they have behind them, and also if they are an honest and trustworthy person.
- Back promoters or entrepreneurs who want your expertise and knowledge, not just your money.
- Get the private company or promoter to clearly justify the valuation to you. Question them on it. Ask yourself, is the business really worth what they are asking?
- Get some good legal representation and make sure your lawyer has previous transaction experience. Get them to review the shareholders agreement and make sure you have a qualified accountant go over the projection assumptions.
- Find out if there are any planned dividends to be paid once the company is profitable.
- Question the promoter on the exit strategy for the business.
- Spread your risk across multiple investments. Don't put all your eggs in one basket. Don't get too excited about the first boat that docks at your shores.
- Join a business angel group. There are many business angel groups and associations across Australia. This will also assist you with finding new deals.
- Be patient. Be prepared to wait 3 to 5 years to get your investment back.

- Keep your money onshore. As soon as it leaves Australia, you have no protection under ASIC corporations law. If you lose your money, you are on your own and you can pretty much kiss it goodbye.

A final word of advice...

Last but very not least, follow your gut instincts. If you don't feel good about a deal, or an individual at the first meeting, or there is something not right about the deal, just let it go. There will be plenty more where they came from. As a real estate agent once said to me, 'the deal of a lifetime comes by almost every week'.

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About Reuben Buchanan

Reuben Buchanan is a corporate advisor for Sydney based advisory firm, Integral Capital Group. His primary role involves raising capital for both public and private companies, of amounts between \$1m and \$10m. These companies use the funds to expand or make acquisitions of other companies. Integral Capital also assist companies with their IPO plans as an advisor, and from time to time do private placements into public companies of around \$1m to \$5m.

Integral Capital Group was founded in 1990 by Len McDowall, who previously was a founding partner of Bird Cameron & Associates, who are now known as RSM Bird Cameron.

Previously Reuben Buchanan started and ran Wealth Creator magazine, launched in 2002 (www.wealthcreator.com.au). He on-sold the business three years later to a private investor group. Wealth Creator magazine remains highly regarded publication in the business sector in Australia.