The Five Common Myths and Mistakes of Raising Equity Capital

Raising capital for your business is fraught with potential pitfalls that can sabotage your success. If you know what the most common of these mistakes are before you begin any capital raising exercise, you can avoid making them and greatly increase your chances of raising the capital you need at the right price and on the right terms.

Behind every mistake we ever make is a mistaken belief or myth that causes us to behave in ways that result in these tangible errors. This article will explore what the top 5 myths of raising equity capital are and what mistakes these false beliefs inevitably lead their believers to make.

Myth 1: "My business is different."

While you may justify this belief with the special qualities of your product/service, your business is like every other business in the eyes of investors, who are looking for a superior return on their investment given the risk they are taking. The large majority of investors don't particularly care what product you make or what service you offer – what they care about is what return on investment you'll generate for them and what the risk of losing their money is. So you are competing in a global market for capital where every business is subject to this risk/return trade-off and evaluation by potential investors.

Believing your business is somehow different from other businesses will cause you to be sloppy in preparing to approach potential investors, so you won't take the time to develop a sound mission, vision and company values that support these, or a sound business strategy. These are the foundation on which you must build your proposal to investors, and we all know what happens when the foundation of a building is weak: sooner or later it collapses. Need I say more about the damaging effects of believing in this myth?

Myth 2: "I'll be alright if I wing it."

No you won't. Any reasonably sophisticated investor will be able to burst your bubble of over-confidence with one or two good questions. Try answering these one's right now to get a taste of the embarrassment, if not total humiliation, that's in store for you if you believe this myth:

"What makes your business different from its competitors?"

"Why should I invest in your business rather than another?"

"How much do you want me to invest, what exactly are you going to use it for and how much equity are you offering me in return?"

"What's the IRR and over what period?"

"What are the risks that could cause me to lose my money or get an inferior return on investment?"

"When and how can I exit?"

If you couldn't answer each of these questions in under a minute without hesitating or stumbling over your words (or didn't even understand some of them!), you are not ready to face a sophisticated investor yet. If you fail to prepare properly, prepare to fail.

Myth 3: "My existing business plan will be good enough to convince someone to invest."

Again, no it won't. Your business plan is almost certainly written from your perspective as owner and/or manager of the business to help you articulate your business strategy and plan for the future, rather than as a document intended for an investor. An easy way to test this is to see if it answers the questions asked above in a one-page executive summary. If it doesn't, you need to edit the document to turn it into an Information Memorandum that answers all the questions a reasonably sophisticated investor will have clearly and succinctly.

You should convert your executive summary into a one-page proposal that you can send to any potential investor to see if they are interested in finding out more because they won't read a 50-page document before they know they're really interested in your opportunity, but they will read one page.

It's also a good idea to develop a short visual presentation summarising all the key points related to the investment opportunity so you have something to support you when you present the opportunity to potential investors before you send them your longer Information Memorandum.

You want to give them enough information at each stage of the courting process to make them interested in finding out more without overloading them. I use the word 'courting' here intentionally because it's useful in this context to think about how you would behave if you were dating someone. Giving him or her your whole life story on the first date is likely to overwhelm them and drive them away, but if you slowly reveal more and more about yourself over the course of several dates, they are more likely to remain interested and want to deepen their relationship with you. The same principle applies to your relationship with a potential investor, so go slow and steady and finish the race with them by your side – remember, raising capital is a marathon, not a sprint!

Myth 4: "I'm sure my potential investors are nice people and I trust them."

Unfortunately, you can't just trust what a potential investor says – you need to do your due diligence on them as much as they need to do theirs on you. Don't be desperate for their money and take them on as a significant shareholder in your business without checking on their track record, credentials and reputation.

Everyone leaves a trail in their business dealings and these days, it's not that difficult to find and follow that with the help of the Internet, and also don't be shy to ask them for references to businesses in which they have invested or been involved in a management capacity. I once did a Google search on a potential investor, a young man that talked a very BIG game, but whom this quick search revealed to be somewhat less than honest and reliable, which was confirmed by a couple of people, whose names and contact details were also given freely by Google, I spoke to who had been involved with this young man in a previous business he had managed.

I wondered why I hadn't done the search sooner, as it would have saved me several hours of time, but at least I did do it – I've heard a number of sad stories from entrepreneurs who have partnered with investors they didn't do any checking on who promised them the earth and ended up taking over control of the company from the entrepreneurs who started it against their wishes and without fair compensation to them.

So be very careful of whom you allow to become a significant shareholder in your business and make sure they sign a good shareholder's agreement that protects your interests and ensures they can't take control of the company or make your life so difficult that you hand it over to them. Also don't give away too much of your business, otherwise you won't have enough equity left to sell without losing control in the next round/s of fundraising.

My final piece of advice on dealing with this myth is to trust your gut feeling – it's never wrong! I've been scammed once in my life and I had a really bad feeling about the man who instigated it after meeting him at a coffee shop and he failed to offer to pay for his coffee. If I'd listened to my intuition, I would have walked away and not lost any money, but my desire to make a deal happen and earn potentially big money from it got the better of me. However, it was one of the best business lessons of my life, as I vowed never to let greed or fear of losing out drown out the voice of my intuition again. Make the same commitment now and it will serve you well in your business career and life.

Myth 5: "I don't need to talk to my investors – our results speak for themselves."

No they don't and yes, you do. If someone has given you a substantial chunk of money to grow your business, they want to be regularly informed about how the business and their investment in it are performing. Wouldn't you? When you are communicating with them, you are also connecting with them and expressing your appreciation and gratitude for their investment and ongoing involvement in your

business. Everyone likes to recognised and appreciated and this should be how you treat everyone you interact with because it's good business sense.

But even if this argument doesn't persuade you, you must see that treating your investors like gold makes complete sense because they are far more likely to invest in your business again if you do. On the other hand, if you fail to treat them well, you'll be killing the proverbial goose that laid the golden egg as they almost certainly won't invest again and you'll need to find new investors for the next round of capital raising, which will take far more time and cost a lot more money than it does to send a quarterly update to a mailing list of all your investors and give the most significant ones a call every few months.

This is the minimum you should be doing to keep your investors engaged and happy, but why be average? Why not send them a hand-written note and a good bottle of wine or other suitable little gift to thank them a few days after they have transferred the money into your account? This will very effectively counter any fears they may be having due to 'buyer's remorse' and help you to build a warm, personal relationship with them.

Remember that giving and receiving are two sides of the same coin, and that if you want to receive abundantly, you must almost give freely and generously. Most people want to receive a lot and give as little as they can away, but although this strategy may seem to work in the short term, it never does in the long run because life has a way of balancing the scales of the giving/receiving equation and you cannot overcome such a fundamental universal law. Again, being committed to living and working in a way that respects this law will serve you well in your business career and life.

So there you have it: five common myths and the all-too-common mistakes often highly intelligent people make when they believe them. Don't be one of the many who buy into these and see their businesses suffer as a result; rather, be one of the few who are wise about the way they approach raising capital and you'll be maximising your chances of finding the money you need to grow your business from the right investor/s at the right price and on the right terms.

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