FINANCE

The Real Costs of Raising Capital

By Stephen Watkins
For NewsUSA

(NU) - **Q:** I am the CEO of a small, privately held company. What advice do you have for calculating the real costs of raising capital?

- Stan Ross, Orange Park, Fla.

Guest Commentary

A: This is an interesting question, because the outcome depends on the method you choose for raising capital. You'll need to consider the amount you are trying to raise and assess your comfort level with spending the time and energy it takes to cultivate personal relationships with potential investors.

Let me start by saying that typically it's the chief executive officer who has the most passion and enthusiasm for a business, and it is often this quality that ultimately attracts investors. Assuming you have an effective business plan, you'll want to make your way efficiently through the process of: 1) introducing your company to potential investors; 2) outlining a deal that piques their interest; and 3) closing the deal.

Without a doubt, mining your Rolodex for sources of capital can be a full-time job that takes your attention away from operations. But on the plus side, in going through this process you'll receive valuable feedback — both quantitative and qualitative — from finance professionals who make a living determining company valuations.

Another approach is to use a "finder" who typically requires a retainer of $10,000 per month. The finder also receives a percentage of the cash plus a percentage of the equity dilution in the transaction, normally ranging from 5 percent to 10 percent. Finders shop your plan among their extensive contacts and can generally get a deal more quickly than a CEO who is acting alone. The Securities and Exchange Commission currently does not regulate finders, but they are commonly used and are extremely effective.

Your other choice is to utilize a broker-dealer or an investment banker. They, too, will typically receive a retainer as well as a success-based fee. They bring the ultimate level of professionalism to the transaction, and depending on the amount of capital you're seeking, this can be an effective use of time, dollars and equity. Most companies use brokers and bankers when they expect a short-term secondary offering or a merger or acquisition.

I think it is key to remember that the more exposure, credibility and liquidity you bring to the table, the higher your company's valuation will be. And that, in turn, lowers your overall costs of raising capital.

Stephen Watkins is the chief executive officer of Entrex. He can be contacted at swatkins@entrex.net.