HOW ENTREPRENUERS CREATE ENDURING VALUE

As part of my series on the possibilities of investing in local sustainable small business stock and new methods for capital formation outside of the traditional publicly traded venue, today's article will be devoted to the successful small business owners in Northern New Mexico who are may be looking to expand their companies and for the education of the many individual investors who one day may wish to put some of their personal capital in such ventures.

It is often difficult for busy people who have created something from nothing to stop and think about the future. It is essential to do so, both for their health and sanity, and also for the long-term security of their families.

The first goal of most small business owners is to make a good living. Hard work, resourcefulness, tenacity, and rootedness in the community are common components of most successful, local small businesses. As ample cash comes in over time, and a positive track record is established, it is important for the owner to step back and think how the company will look to the next generation of owners. Central to most business people's plan is a strategy for retirement. Unless there is an immediate family member available and capable of taking over, entrepreneurs traditionally have only a few options: selling their business to employees, to competitors, and, in some cases, to large regional and national firms.

I believe that the key to sustainable economic development is the ability of successful, small firms to attract local investment capital. This is a recurring theme as institutional investors, such as the State of New Mexico, non-profit foundations, and some private individuals have a high degree of interest in seeing their funds invested in the local community. To be viewed as a candidate for this kind of capital, it is important for entrepreneurs to assess the possible impact of outside investors on their business.

In order for entrepreneurs to envision retirement, they must plan for their own succession. To get a business operating on its own, means having a plan to grow from a mom-and-pop size operation to one where there is a group of key employees who can act as a team. This helps attract investment capital.

Outside investors generally operate under a three- to seven-year time horizon. The main goal is to liquidate their initial investment at the term's end for a profit. For growth to happen and to be financially successful, the founding business entrepreneurs and the employees of the company *have* to share in the fruits of the expansion, so it is a win-win situation.

Another key issue to outside investors is how the founding entrepreneur is planning for his or her succession. Is there a team in place that can take on the business responsibilities if something were to happen or at the eventual retirement of the founder? Most investors will not put money into a firm if it is clearly a one-person show.

Traditionally, private equity investors seek returns of 15 percent or higher. This puts a huge burden on a company to grow at a fast rate, one that entails acquiring other small companies and obtaining large amounts of credit from banks or other loan sources. This often comes along with a boat load full of stress.

Local investors may have interest in a local business that can grow at sustainable rates and in ways that don't drive the owners and employees crazy. While most non-community minded investors look only at profits and cash flow, entrepreneurs, employees, and concerned local investors look at how the company and the community can both thrive on an on-going basis. This doesn't mean that entrepreneurs don't need to grow their businesses in order to maximize value. It merely points out that growth needs to be achieved in a way that makes sense for all stakeholders, not just the investors.

In thinking about a strategy for growth that is sustainable and will also attract outside capital at the right time, business owners need to think about the impact of future technological changes on their company. For example, there are many ways that the Internet has changed the business environment, and many local firms have gone out of business due to competition from large chains while manufacturing jobs have gone abroad.

The true value of a small business in most localities lies in the personal relationships that the entrepreneurs have created with their customers. Small business owners add further value by doing something qualitatively different than their large competitors. Small business owners, especially those in

New Mexico, need to be able to react quickly to changes and steer clear of the morass of government and environmental regulations that ensnare many businesses.

One common trap that small businesses fall into is relying on a formula that may be working now but is headed on a downward slope. It is only by stepping back from a business and asking what really is the unique service or special product mix that could be provided that makes businesses prepare well for future growth. Strategic planning consultants can help people think through these issues. Many universities and non-profit organizations, with proven strengths, have found that they can parlay their specialized expertise into money making ventures. New Mexican small businesses need to successfully reinvent themselves, probably every eighteen months or so, to stay on top of the changing business scene.

In looking at the management team in place at a small business, investors will often perceive that one or more business skills are lacking and that this will inhibit the firm's growth beyond its current stage. Small business owners looking for outside investors should be prepared for the introduction of a new management team member, one put in place to help the small business grow as well as to protect the investor's interests.

Strategic assets that can be owned by small businesses include intellectual property, real estate, a brand name, and established networked relationships with the local community. A successful entrepreneur who wants to create his or her own retirement will recognize that these assets will benefit when time and effort has been dedicated to solidifying and articulating these assets to the employees. When an outside investor comes in, employees will then feel comfortable with changes as they know that they are an integral part of maintaining those successful relationships.

Management teams are also held together by employment and non-competition agreements. Outside investors look to these in order to ensure that the intangible assets such as people, reputation, and service levels do not dissipate once there are new owners.

To attract outside investment capital as well as run a business requires reliable financial statements. This does not mean that small businesses have to hire expensive national accounting firms. Having clear, concise, and reliable financial statements that correspond to the reality of the business is crucial to keep outside investors informed.

The preparation of forecasts is important for businesses to show how growth in the future will impact investors' returns. Without projections, the business plans for the future may lie locked inside the mind of the entrepreneur/founder. This does no one any good.

It is often good for small businesses to have outside people come in and review their books and procedures, even if it seems like an unnecessary expense. Outside investors generally impose additional reporting requirements on the small business. This usually taxes the small business owner's patience and often more time is spent on reporting than on conducting business unless workable business structures are in place.

Founders who take time away from their business to think about and write down their plans for the future, with detailed steps about how they expect to stimulate growth, will enhance the business's value. Creating a council of advisors allows people in the community who are friends to the business and who like interacting with the founder and management team to come together on a regular basis. The council can review, critique, and offer suggestions to the founder and management team about ways to grow, operate more efficiently, or just have more fun.

When a small business decides to get bigger or the founding member nears retirement age, everyone gets nervous. Change, while difficult for most people, is a constant in the business world. It is better to prepare for change, to involve everyone in consideration of all the options, than to keep information bottled up inside one person and wait for things to happen. In order to get value from an enterprise that took much effort to create, entrepreneurs would do well to investigate ways they can attract outside investment capital, even if the route eventually taken differs vastly after further contemplation.

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