The Realities of Financing Rural Development Projects

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Entrepreneurial Report Card

Indicators to look at:

– # of venture capital investments
– # of manufacturing investments
– Short-term employment growth
– Long-term employment growth
– New business creation
Iowa as an example

In 2005, Iowa was:

- 41st in venture capital investments
- 43rd in manufacturing investments
- 49th in short-term employment growth
- 50th in long-term employment growth
- 50th in new business creation
Business Models

• Food Processing
• Cold Storage
• Agri-Tourism
• Light MFG
• Bio-fuels
• High Tech Application
How Have Deals Changed?
It’s a People Business

• Networking: The Iowa VAASST model
• Cooperation and communication
  – Extension
  – USDA-RD
  – Iowa Farm Bureau
  – Iowa Department of Ag
  – Institute for Cooperatives
  – Iowa Area Development Group (REC’s)
  – Iowa Power Fund
Funding Source

- Angel
- Institutional
- VC
- Private Equity
- Bank
- Public incentive funds, grants, guarantees
The Investment Stages of a company
Right Place at the Right Time w/ the Right Request

Idea
Prototype & Business Plan
- P.O.C.
- Validation
- Market size
- Comp. Analysis

Seed Stage
- Validation
- Market size
- Comp. Analysis

Develop. Stage
- State Funding
- Accelerator
- Angel Funds
- Community Funds

Growth Stage
- State Funding
- SBA / USDA
- Angel Funds
- Rural Devel. Fund
- Other

Mezzanine
- Same as Devel.
- Stage plus larger Regional Investors & Invest. Bankers

Lending Source for the Company
- Friends & Family and/or Local Angel
- Accelerator
- SBA
- IBGC
- USDA
- Tech. Assist.

- State Funding
- Accelerator
- Angel Funds
- Community Funds

- State Funding
- SBA / USDA
- Angel Funds
- Rural Devel. Fund
- Other

- Strategic Part. M & A
- Regional Banker
- IPO
The Vision / Goals

- Increase the number of successful target business start-ups.
- Improve the expansion rate of existing target businesses.
- Increase wealth creation for ongoing community reinvestment.
- Increase the employment talent pool.

www.iavaap.org
The “Classic” Model

• Provide networking and educational opportunities:
  – Events for entrepreneurs to meet vendors, mentors, and investors
  – Opportunities for “road-show” presentations
  – Educational seminars to improve skills.

• Provide guided professional and business direction / hands-on consulting:
  – Diagnose needs.
  – Assemble necessary talent.
  – Provide ongoing support / mentoring.

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What to look for?

Companies that have:

- A compelling idea that meets a need in a targeted marketplace.
- Need a detailed business plan and executive summary.
- Need Financial Proformas with realistic assumptions.
- Need to knock on a lot of doors.
  - Patience & Persistence.
V.C. – How do you get it?

• From the Iowa Farm Bureau Federation perspective we have six fundamental criterion that must be addressed in a business plan for any investment consideration.

• Probably a good template for other VC’s as well.
V.C. – How do you get it?

1. Understanding the Business Concept
   – Is it Sustainable over time?

2. What is the product or service’s “Unique Selling Proposition”
   – Defined as the “differentiator”
     • Preferably, not a commodity but if a commodity, why you?
V.C. – How do you get it?

3. Is there outside validation?
   – Customers.
   – Testimonials.
   – Strategic partners.
     • OEM strategy vs. self branded image.
   – Outside professional assessment.
     • Relating to patents, manufacturing, financial viability.
V.C. – How do you get it?

4. Management team?
   – Depth and experience.
   – Space knowledge.
   – Incentivized.

5. Predictable business model?
   – Grow to:
     • Cashflow (+) and,
     • Enable follow on financing at stepped up valuation.
     • Additional investors.
   – Create enterprise value.
V.C. – How do you get it?

6. Exit strategy
   • Sale?, IPO?
   • M and A financing
     • You acquire
     • You are acquired
   • Mezzanine financing
     • Additional equity
     • Exit for original investors
     • Why mezzanine
       • Relationships that can grow the business
       • Industry expertise
       • Strategic planning
V.C.- Do you really want it?

- Is not a right fit for every company.
  - Valuation of company is always an issue.
  - Liquidation Preference:
    - Preferred stock versus founder common stock
    - Anti-dilution ratchets.
    - Exercise rights to control board of directors.
  - Need an exit strategy with a minimum IRR of 25% to 35% minimum in 5 to 7 years.
## An Example – Any Company USA

<table>
<thead>
<tr>
<th>Amount requested</th>
<th>$300,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type of Investment</td>
<td>17% Common Stock (post deal)</td>
</tr>
<tr>
<td>Stage of Company</td>
<td>Early - $100,000 Revenue</td>
</tr>
<tr>
<td>5th year proforma assumptions:</td>
<td></td>
</tr>
<tr>
<td>Revenue</td>
<td>$8,000,000</td>
</tr>
<tr>
<td>NIBT (8% of revenue)</td>
<td>$640,000</td>
</tr>
<tr>
<td>Enterprise Value (Ave. 1x Rev and 10xPE)</td>
<td>$7,200,000</td>
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<tr>
<td>Company Debt</td>
<td>$3,500,000</td>
</tr>
<tr>
<td>Adjusted Enterprise Value</td>
<td>$3,700,000</td>
</tr>
<tr>
<td>VC Redemption IRR %</td>
<td>30%</td>
</tr>
<tr>
<td>VC Redemption Payment</td>
<td>$1,100,000</td>
</tr>
<tr>
<td>Valuation needed to not dilute owners equity</td>
<td>$10,100,000 ($1,100,000/.17 + debt)</td>
</tr>
</tbody>
</table>
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