Overview

I raised a search fund, drawing down the initial capital in September 2009 after originally writing my PPM in April and May 2009, (the months before I graduated HBS). I had been seriously considering raising a fund since September 2008 and in fall 2008 did a field study with a former unsuccessful searcher. The intention of this document is not to replicate anything that is in the excellent Stanford GSB reports but rather to give a personal perspective on the process and my decision making. The rationale for writing it is that I found the search process an emotional one with highs and lows, which as a single searcher is a responsibility that is best described as lonely. I made numerous mistakes, which in hindsight were an integral part of the process but which at the time I would disproportionately agnonize over.

I successfully purchased a business in June 2011, a transaction for which the initial contact began in September 2010. It was a deal which at the time of closing was one that the investment group was extremely excited about. Ultimately the success of my search process will be defined by how well the deal performs, however the business ownership and leadership process is one far more extensively covered and studied in business school. The intent of this document is to focus on the relatively unique "search fund" fundraising and searching process.

The main reason for writing this document is that the search fund 'community' has been extremely generous with their time, encouragement and backing. I learnt a lot from previous searchers who did not find a company to buy, or searchers for whom the process has not been a home run. These people extensively gave of their time and were a much more valuable resource to me than those who had extensive success. I spoke with 82 searchers both before fundraising and into the first year of the search.

As a perspective on me, I am not very academically smart and do not tend towards strategic industry analysis. I trained as an accountant, for some professional discipline, and prior to business school I had done a number of cash flow lending deals whilst working at a bank. However I am much more of a salesman and the most useful lessons for my search were learned during my time as a door to door salesman which I did for 6 months before taking a 'real job'. I am relentlessly determined, which means that the areas in which I lack talent I can somewhat overcome by working very long hours and trying to find people to help me, which suits the search fund model.

I try to split each section into (a) numeric analysis (b) techniques and (c) Thoughts. However it is worth remembering that I am no academic superstar and therefore do not have any great skill in writing (but then neither does Dan Brown and he managed to sell a lot of Da Vinci codes). In addition this document is mainly written for prospective searchers, a point at which I wanted as much information as I could possibly get. It therefore tends towards detail and length. Jim Sharpe, one of my investors, despairs at my wordiness (I am slowly improving), so talk with him if you want mutual exasperation.

My phone number is 617 319 0794 and my email is paul@scotamerican.com , if you feel reticent about reaching out, that is a very strong sign that you shouldn't do a search fund. However my time is over scheduled in running a company and hence please, at a minimum, do the research I mentioned in the fundraising part, prior to reaching out.

Fundraising

<u>Numeric</u>

I contacted 92 people that could possibly have funded a unit in my search. I was unwilling to allow people to take more than one unit and wanted 12 units, so that I would have enough investors that some could drop out in the next round, and some would come to not have faith in me. About 35 did not ever reply. 28 said no (about half of whom met me), I include quite a few in this who 'passed' by simply procrastinating (which was really the same as no). I ended up with 29 possibles, of which 14 were particularly committed and I thought would be good investors. I then added one half unit after closing the fund raising (to a formerly successful searcher who I really liked and was in virtually no other funds). Of the 14 I didn't take, many had a very short term timescale or wanted unrealistic conditions (such as I had to focus my search on industries they chose). In the main though I am counting in this 14 a number who procrastinated and who may have committed had I really needed them too, but weren't really sold on me. I do not know why I did not ask the professor who I had done a field study with to invest (probably fear he would say no) which was my sole point of regret post search.

The fundraising cost me about $20,000. This was a combination of paying my rent and costs in New York with no salary, extensive travel (a lot of people said no!) and general living costs. Whilst no investor would think this worthy of being counted as a financial commitment, nonetheless it should be considered by those thinking of doing this when finishing business school i.e. you need some resources to pay for fundraising (excluding NY rent it was about $12,000 mainly on travel).

<u>Techniques</u>

Prior to fundraising I read every document I could find, watched the videos of all the search fund panels numerous times and met with as many search funders as I could. I viewed these as basic minimum requirements.

Jay Davis and Jason Pananos (Nashton Partners) were local in Boston and very open with me about how their process was going and I focused on them and the searchers from 2006 to 2008 to learn initially about fundraising. These searchers mostly had the same core group of investors; due to the success of funds from 2000 to 2005, and the capital events from successful 1990s searches (particularly Asurion). A group of funders had emerged but were largely now 'full' in their appetite for search funds. Many of the 2006, 2007 and 2008 funds had difficulty in buying businesses due to the financial tumult and the withdrawal of bank lending. 10 groups and singles from HBS set out to raise a fund in 2009 and I was the only fund that closed. My particular style of hustle and relationship building was probably more suited to the environment than the cerebral nature of other potential searchers who were raising. Clearly style of fundraising should adapt to the environment at the time.

I decided I wanted to talk to as many searchers past and present, (and as many experienced funders) as I could. I spoke with 82 searchers, a process which significantly widened the pool of potential investors as they referred me to investors if they liked me (90% of those I spoke to didn't refer me to anyone, and I didn't ask, but my volume of searchers talked to meant I found a few that I got on extremely well with).

3 of my eventual investors came from this process and had not been asked to invest in funds for over 4 years, despite having funded a number of searches historically. Openness to talking to everyone was probably my most defining search strategy and the single biggest defining factor in raising the fund.

I also knew the answers to why what I viewed as the 3 key questions

1. Why I wanted to go the search fund route
2. Why I was different and would therefore find a company
3. Why it was the right time for me to do it

Most searchers who contact me don't really know the answers to these questions and focus much more on whether they can run a company or on why they are slightly more experienced than other potential searchers (everyone is inexperienced, being slightly less experienced is like being the tallest man in a midget line up and not a compelling reason for investors). I felt these were the questions that would allow me to communicate effectively to investors. The PPM process is largely boilerplate and the investors (or at least the first pass) are heavily contacted, hence there is little to differentiate groups. My answers to these 3 questions were:

1. I wanted to raise a fund as I fundamentally believed that blending the experience and knowledge investors with my commitment, personality and flexibility would be a formula for success. I had the opportunity to do venture backed or self funded businesses and was fully committed to entrepreneurialism, but I actively chose the search fund structure.

I also believed that for the right investors they would enjoy building a relationship with me and that I would listen to them and execute. I told them it would be fun to deal with me, which I think wasn't something they often heard. I did not see capital as a commodity, but something that came as a process of building a team. I insisted on meeting all investors in person (other than one who came highly recommended but was sailing around the world on a boat). I also told them I would always be rewarded after them and that as long as I could earn up to 30% of the equity, they could have whatever terms they wanted. This was relatively different from most search funds who tried to raise and yet something I believed was fair.

2. I had been a door to door salesman working over 100 hour weeks relentlessly. I also had traveled to over 100 countries. I had failed in my professional sports career (I was a rugby player for 5 years) and thereafter shown complete willingness to relocate anywhere in the world. Therefore I communicated that I would be on the road all the time (I actually ended up traveling over 252 days in the final 12 months of the search, and almost all of the 8 months before that). I was upfront in my shortcomings that I was not cerebral and industry selection would be a process of trial and error but that cold calling, and building relationships was a lot easier than door to door sales. I had absolutely no faith in a broker process, feeling that they favor the numerous PE funds who had a lot of dry powder. I was going to perform an entirely proprietary search and use a number of techniques along with dogged determination to find a company. The biggest factor was that I had total belief I would find a deal ….in hindsight this was extremely optimistic but perhaps compelling when meeting me at the time

3. I had given up a senior and well paid job to go to business school and then become an entrepreneur. Additionally I was entirely self funded since the age of 16. I was 'all in' and had no back up plan, and was completely committed. Meeting Christian Lawrence (a 2003 searcher) was also extremely useful as they had taken 9 months to fundraise. At that point I also knew I would fundraise until I literally had no more money (I think I may have been deported then!). I had a long term serious girlfriend but my commitment to locational flexibility and constant travel was full (and it turned out the relationship fell apart, the search being a significant factor). I was going to pursue an entrepreneurial venture and this was my preferred option. I was going to keep fundraising until I had no further method of continuing.

In meeting me at the time I would have come across as extremely committed, actively choosing to go this route (rather than due to a lack of options) and

I very quickly got to 5 investors, from 2 personal contacts and then 3 experienced search fund investors. The next 22 people were a lot more work and all said no. Rarely when people said no, were they honest about their reasons. Other searchers I have seen then seem to focus entirely on these answers (which most of the time are not very helpful or correlated with their decision). Rarely will investors just say, "I don't really get a good feel about you" – which has no correlation with whether others will, but is more the answer searchers should 'hear'. I focused on building relations with historic searchers particularly those running companies and these contacts were the ones that led to investors 6 through 10 (actually 9 people as there were 4 half units). Investors 11 and 12 came from a classmate and one of the other investors

<u>Thoughts</u>

The model is proven,so there is no need to go to the same core of investors, and besides those that are overcommitted aren't necessarily the best for you personally. I also believed it' s not about terms, just accept you can earn 30% of the equity if you get it right, and they can fire you at any time if you don't. Their confidence and support is the key, if you make it a success they won't nickel and dime you.

You'll best get a warm link from a middle person – speak to enough people, research people, keep going and you'll work it out. This is much like the search for a company process.

I wanted at least 12 investors (I ended up with 15) and wanted to be efficient and hence was reluctant to have many half units ($25k was unit size as I didn't feel any need to raise more money). I decided $300k was as much as I needed. Also I only drew down half on day one. If they wanted to back out they could. The investors I got could often on the day of draw down, not remember how much they had committed, which is a reflection that they back the person, not the financial number. I also delayed closing to wait for one investor, waiting for him to return from vacation, then going to see him. He never made a decision, which was his way of saying no. Most investors decide relatively quickly, if they are actually in, given my personality and style.

I learned a lot from the fundraising process and whilst it only took 4 months, it wasn't straightforward and there were a lot of self esteem hits. I failed to celebrate or mark the closing of fundraising of the fund, which was a mistake. I would recommend taking 2 weeks off before starting the search.

The search

Numeric

I did not use salesforce or a CRM after the first 4 months of the search as I preferred excel spreadsheets and google documents (for sharing with interns), hence I don't have 'auditable' statistics and it would be too much work to go back and calculate, but I can make close estimates (as I lived and breathed this for 20 months). I had a list of 9000 business intermediaries and whilst I intended to outreach to them monthly I only ever mass mailed this list 3 times. This is probably due to my lack of any belief in business brokers. About 25% of these emails were opened and the process, I believe, had negative effects of my domain being classified as spam (we switched to a different email for outreach thereafter). My proprietary search reflected my own style and my belief in what would find the type of deal I was looking for. I did not get any industry tips or insights from brokers, who I believe would sell their own mother for 2% of the deal value.

In the 3 main industries where I did extensive outreach (electronic medical records, autistic services and insurance managing general agents) I contacted a combined 1,700+ business owners, many multiple times. I also contacted another 100 in all kinds of industries from the Inc 5000 lists. In the core outreach period (months 5 to 14) I would send 50 new letters a week, a process which took over 65 hours a week of work and the use of between 2 and 4 interns working 45 hour weeks (I expand on my techniques below). I attended 23 conferences and did not keep track of how many business owners I talked with at these, but it was often upwards of 25 a day. It would be a fair estimate that this was over 500 more business owners in industries I quite liked.

I looked at more than 40 industries in some degree of depth (more than 2 days analysis), but expanded the analysis in only 9 of these (electronic medical records, medical transcription, content management systems, autistic services, e recycling, at home kidney dialysis, insurance managing general agents, content creation, boxing gyms). I only outreached extensively in 3 (electronic medical records, autistic services, insurance managing general agents).

I felt I was very good at the techniques of outreach and yet I would estimate the response rates at somewhere between 2% and 5%, though the recognition was far higher (an important, but perhaps missed metric). By recognition I mean the business owners remembered the letter distinctly when I met them later, for instance at a conference.

I aimed to travel as much as possible and when I had an owner who had agreed to meet me, I would then try and get any other owners within a 50 mile radius to take a meeting (I would phone and tell them "I'll be in town all week, would you just like to chat?"). This led to a number of meetings.

Techniques

Outreach

I understood marketing techniques well, including the process of search engine optimization (see Rand Fishkin's sites for advice), inbound marketing (the hubspot model), facebook and other social networks and direct mail. I also had a good feel for both traditional marketing routes (mass ‘snail mail’ outreach), cold calling and in person cold calls. I also explored and understood mass email outreach programs (those that send an email a minute, day and night, to lists that you can purchase). I also sourced Chinese and eastern European spam mail options that I never used but had as an option.

I looked at outsourcing deal finding (there are a few retained search companies that charge about $2000 a month and then 2% of the deal value), but decided it was a core competency of the searcher and therefore should not be outsourced.

It is a process and you need to build recognition and constantly refine your techniques (i.e. the wording of your outreach, see appendix 1 for mine – I was never very happy with the wordings though). This is the absolute core of the search. It is critical to set yourself targets for outreach and to hit them. In the process this is about the only thing you can control (as well as the hours you put in). I regularly worked 80+ hours a week, which allied to my average of 2 FTE interns (4 people, roughly averaging 20 hours a week) still meant it was challenging to get 50 new letters out a week. The volume comes not in simply tailoring the letters and printing, addressing and posting, but in finding enough companies, then the right mailing address and email and then researching the company so that you can make one or two little comments that might make a difference. You are probably also doing various other tasks, such as attending conferences, industry analysis, travelling to see companies, writing investor letters, working on deals, recruiting interns, dealing with the accountant etc etc. Often I would be at less than 20 letters on Friday at 3pm and would work long into the night and over the weekend to make sure I had 50 out. These numeric totals are critical to maintaining your sanity and believing that you are making progress.

My process was a letter that arrived and looked like a wedding invitation and included a Scottish toffee bar (not able to be purchased in the US, and the toffee is really good!). I sent a follow up letter a month later. An email a month after that and then would call a month later. .The letters took approximately 50% of the interns time and about 15 hours a week of mine. Every letter was individually tailored (some to a greater degree than others) from an overall templates.

In over 80% of the phone calls they knew who I was and had read the letters. The letters had less than a 5% response rate, but I would estimate an over 80% recognition when I met people at conferences or called them on the phone to say I would be in town close to their offices (and they would over 50% of the time take this meeting in the industries I really liked). I would write the second letter and initial email at the time of the first letter (hence 50 letters a week was actually tailoring 150 outreach items).

I used the team of 4 interns to do this and in fact when I started to visit a lot of conferences the interns maintained the volumes themselves. We sent 50 new letters a week, hence at full outreach there were approximately 150 unique outbound approaches (50 new letters, 45 follow ups, 40 emails , 15 phone calls). I did not call extensively, but when I did it was usually positive. However I felt initial cold calls would not be a good route – I had nothing other than instinct for this. I was not afraid or reluctant to call but my theory was that if they had had 2 letters and an email, by the time I called they knew who I was and had at least thought about it.

The letters with the toffee had to be hand franked at the central NY post office, hence every Saturday at 8am I would be first in line with the 50 letters and 50 follow ups. The mailing cost of the toffee letter was $1.44 and the follow up letter was a stamp. In addition the nice paper and envelopes and the cost of ink to print was about $0.50 a letter. In essence we were spending about $2.50 per company. Over the course of the search this was about $5,000….. which really highlights that the main expense is your time!

Jim Sharpe's document on outreach is better worded than I can write and my thoughts are closely correlated

http://www.people.hbs.edu/jsharpe/Harbus_Lessons/100308%20HARBUS%20-%20Lesson%20-%20Finding%20a%20Business(15)-Cropped.pdf

In addition to the mass mailing, there would be companies that I would get very fond of (often for no sensible reason, e.g. Dub Love's insurance company that owned the domain www.welove.com i.e. "We Love Insurance" (he never replied to my 10 letters, 4 emails and 6 phone calls, he probably now feels lonely without his stalker!). Thos e that I loved I would be creative with. My favorite book is "The Curious Tale of the Dog in the Nighttime" and I would send that sometimes to business owners whose businesses I liked a lot (and also to people I'd met but where backing off in correspondence). I would also send particular research or articles I found interesting to them (again pretty much always by snail mail).

Industry Analysis

Industry Analysis

Industry analysis and outreach are the two most fundamental search fund roles that are the sole responsibility of the searcher. Don't expect the investors to help you because they won't. This isn't due to any lack of desire or effort on their part but rather because the crux of industry analysis is being out there and being completely enveloped in it.

The best industry in 2011 is different from that in 2009. What's available and when it is available at an attractive price is constantly evolving. It is very stressful to not have an industry you are sure you can fully immerse yourself in. 8 months into my search I found myself without any industries I truly believed in. In the end there was only one I believed I had an advantage in and which the timing was right. I committed the last 12 months of my search to only this industry, which was both risky and yet had advantages (I got to know a lot of people in the industry and saw a lot of companies I could learn from when I eventually purchased).

You cannot hide from the truth that this is the sole domain of the searcher and the responsibility and worry lies firmly on your shoulders. It should however be noted that the most successful search fund performed a pivot from car rescue into insurance, which drove their ultimate success, hence getting in the game is also part of the strategy!

I tried numerous techniques starting with using the phone directory and the SIC industry lists. I loked at all the industries previous searches had looked at (and in fact in the Stanford GSB there is a list of historic PPMs and so I looked at things previous searches had talked of). I went to a number of industry conferences which often led to industries closely correlated (e.g. electronic medical records led to transcription and medical tourism). I looked at the portfolios of private equity firms and extensively analyzed the Inc 5000 list from both the current year and back 5 years (as far as I could get lists). I also looked at growth lists from the UK (to see if there were any trends or ideas I could copy). I also looked through all the industries that the HBS business plan teams had tried to launch in over the last 10 years. I extensively went to meetups in industries I liked and taught a class at NYU school of medicine on business in order to get more access to medical companies and trends. I also volunteered at United Cerebral Palsy of New York with a recreation program on the weekend. This was for my own enjoyment, but led to a number of industries that I liked but ultimately had some flaw (like concentration on one payer)

I tried using grids to score the companies, which had some degree of utility (see appendix for a grid) but the scores would typically come out highly at whatever I was most fixated on at the time. I followed closely venture capital investment trends and read blogs.

In the end, I just wasn't innately very good at industry analysis and perseverance rather than intellectual thought was my only trick. I include in another appendix a list of the industries I looked at for over 2 days and those that I had no interest in at all.

I found classmates at private equity funds no help at all in industry analysis as they were largely execution professionals and PE funds tended to rely on generic trends and brokers. Hedge fund classmates were very high level and had defined timescales, hence again it was difficult to correlate to the search. Venture capitalists had very interesting growth trends, but their type of companies were largely too over priced for the search fund model. I found being obsessed with finding a company meant I began to see the world through the eyes only of what may fit the search, and industry ideas would then come in waves.

I spoke extensively and entirely openly with the other current searchers which was great for morale. They were certainly not competition and in fact we usually disagreed on which industries we liked. Andrew Tam and Max Sadler were both single searchers and I would try and pass them deals in industries they were focusing on and vice versa. I would highly recommend this, which as I understand is a significant variance from a lot of searchers historically.

Costs

My budget was $12.5k a month (24 months for $300k, I took an extra half unit which covered up front legal costs). I was exactly on track. About $7.8k a month was salary and taxes (unavoidable as for visa purposes it had to be this high, but I also spent my own money on travel for the search). My office averaged $0.5k a month (in Manhattan!), and accounting fees, outreach costs and phone totaled about

$0.5k a month. Therefore I would spend about $3.5k a month on travel. As I stayed 85% of the time with classmates (including 106 nights out of 150 with one guy whilst getting the deal done), most of the cost was flights and rental cars/ gas/taxis (in NY). I booked all travel with kayak (originally I would spend too much time trying to get every penny off, an exercise of diminishing returns), just picking the cheapest option, though I would also use any points I accumulated to pay for travel. The Jet Blue 'All You can Jet Pass" ($699 in September both years for unlimited travel) allowed me to take 28 flights in 30 days both times.

I aimed to minimize costs wherever I could, whilst not compromising on my ability to appear in front of business owners and therefore my absolute focus was on traveling as much as I possibly could. I would stay in the worst motels and rent the cheapest car. However I would always pay for the business owners lunch and drinks and often take a gift (mostly a book, or some Scottish toffee)

I took an office in Tribeca subletting from an architect for $450 a month including all bills. Later I moved to an office for $650 as my lease was not renewed as someone else bid more than double.

I went to 26 conferences and only paid once. Typically one of the main costs of a search and with conferences fees averaging $1500. I did this by writing articles for the HBS school newspaper after graduating and writing to conference organizers as a journalist for a free pass. It would often allow you to go for free and I would simply amend the badge to say Scottish American when I got there. I did have to go through the rigmarole of some interviews and write some articles on pointless topics, but the money saving was worth it.

I learnt to book cars well in advance of any trip I even remotely considered taking as there was no penalty for that and the rates rocket in the days before.

Staying with friends and classmates was essential for costs, but was also great for morale. I would try and let them allow me to take them for dinner but they mostly refused.

Interns was a critical part of my search and cost virtually nothing (other than lunches, beer and my time).

It is worth noting that investors never asked what the money was spent on or asked for a report (though I updated them in the quarterly reports). This makes sense as as a searcher you get 'paid' last. The idea of using the money for anything other than a focused search is ridiculous and in fact I bolstered funds with my salary whenever possible.

Interns

I began by approaching NYU and Columbia and asking their recruitment department whether either would be interested in providing interns. Both said their students would not be interested. I then approached Fordham university and met the business school dean and others . This took time and their timescales were for months later, so again was a dead end.

I had a couple of Ivy league students through referrals, but these were dreadful experiences as they mostly just wanted to ask questions and felt entitled to be there.

I eventually (after 3 months) simply posted an advert on craigslist. I did not check it for 48 hours, but then realized I had 322 responses (including 2 HBS classmates, though they wouldn't have known it was me). The wording of the posting is included in the appendices. I repeated this 6 times in the search (I only did it once, thereafter interns recruited and managed other interns). Each time over 150 applications would come in. At least 25 each time were what I would consider extremely good applicants.

The hardest factor in determining whether an intern was suitable, can be answered by finding out their motivation for being an intern (one intern was 34 and a Stanford grad but hated his job, one was 26 and ran his own internet design company, one was a freshman at Wharton, one took a year off from Columbia – there were many others equally varied). If their reason is vague, it generally didn't work out. If they saw it as unique and realized they would glean a lot from the process, and they were someone I could see I would like, it usually worked out extremely well. I would have got no more effort, nor a better quality (in fact I would argue I would have got worse) had I remunerated them. However I remain in their debt and would make and have made a lot of calls on their behalf and provided excellent references to help them. In addition I have hired one and am actively trying to hire another to work at my company. The final intern took a year off from Columbia to work for me full time. He was excellent and I was extremely fortunate that this happened.

They mainly worked on outreach (finding companies in industries, finding the addresses and then sending the letters), but I would show them everything I did, explaining models, deal booklets, due diligence, the communications with investors and the economics of the search. In addition I would do industry brainstorming with a group of them. At least 50% of the interns enjoyed it so much they came in all their spare time and we built good camaraderie, though as they are younger and more junior, it is not like working with peers and does not lift any responsibility.

I did not formalize anything about the search process, relying more on instinct (and in fact other interns instinct). We had many nationalities and were entirely open to any background, creed, color, gender or age. Though it should be noted that we had zero transsexual applicants, we actually had an intern of almost other color, persuasion or 'category'. The only 'category' that did not uniformly adapt well to the search was Ivy league Chinese engineering students. They applied in vast numbers and I was unable to find one who ever worked out.

When I thought of the intern program it made little sense that interns would apply in such numbers, but then the head of NYU recruiting is the perfect case in point – 58 of the students she said wouldn't be interested applied in the 24 hours after I posted the advert. Sometimes it is better just to follow the market dynamics of supply and demand (it should be noted that this was at a time of high unemployment!).

A minimum commitment should be 10 hours a week, scheduled at exactly the same time each week (otherwise it becomes a logistical nightmare). I couldn't imagine doing a search without interns

Thoughts

Philosophy

Spend the money in 2 years (extending longer is a false economy). Save wherever possible and then get in front of business owners face to face and spend sensible amounts of money on them. If a business owner agreed to see me, I did not need any financials nor commitment from him before traveling to see him.

Things to know

1. You are all in
2. It's emotional
3. Be humble

Every business in the US gets sold, its just a matter of when. The timing of that is the thing you have to most accurately consider – why would this person sell to me now. It took me a long, long time and a lot of dead ends to realize that the biggest factor is that the seller has to have a reason to make a decision now…. Or they'll delay and delay.

The biggest factor in your search is developing your own 'style' and executing consistently with that. I felt that there were enough private equity funds and industry buyers so I had to come across differently than them.

You should think extensively about your style. Your website, communication, linkedin, method of outreach and everything in your digital footprint and those of the investors will be investigated – make sure you have an entirely coherent story.

Speak to as many historic searchers as you can – many will just repeat what's in the search fund studies but you'll gain unique insights from those who failed to find a company, or those who bought a company and it didn't work. The successes are well documented, there is as much to learn from those who it didn't work out for.

Historically some people tried to represent themselves as a private equity firm. Jim Sharpe had on his card Jim Sharpe and Associates and the first question was "who are the associates". In 2003 if you stuck up a website that said anything you were innovative, it takes much more than this now, so think, be creative and innovate.

The Deal

Numeric

I 'issued' 4 actual LOI's during my search, but these I only sent out when I was sure the seller was serious about selling and where their signing meant they would follow through. This was probably a mistake, but reflected my style. Perhaps sending these out earlier is a better 'process'. I walked away from the autistic services company LOI as I lost faith in the ability to make money in autistic services in New York due to the politics (and reliance on the single government payer). In both the other insurance LOIs the son of the owner was the main competition and in one I lost out to him even though he had no money (after an intense 3 month process, including the father showing me houses to move into) and the other the son and I didn't agree on which areas of insurance were best (and besides I wanted only to combine it with the company I eventually bought).

The Missouri based insurance company I bid on, I bid 7x earnings, (2x debt, 2x equity, 2x seller financing and 1x if we grew more than 10% in the first 3 years). That was the market rate bid by large competitors. In other bids involving private equity competition, I often bid over 6x but would lose out to greater than 6x, all cash bids. I then realized I had to find a seller for whom price was only one consideration. My actual deal is a turnaround, where the company has great contracts and a great reputation, but had been badly mismanaged by the team the owner delegated to before stepping back in. The owner is 79 years old. In the deal I did we did not get external due diligence and the actual investors equity agreement was not signed at the time of purchase (in fact I drew down most of the money before the deal was agreed). By the time of the deal, and due to the nature of the deal, the investors and I had an extremely high level of trust in each other.

Techniques

The two largest factors to getting the deal done were that the owner and I liked each other and that I spent 6 months, almost full time 'camped' on a classmates sofa almost on the sellers doorstep. In the final 2 months I would work each day in a café in Venice Beach, always ready to see the seller (and in fact the owner of another company close by).

On a number of deals I went to senior lenders for debt and this was relatively straightforward, though I did not have to ever go to credit committee stage (I was very comfortable with bank processes due to my background). I cant talk with any authority on this though. There were deals funded by self funded searchers, almost entirely with mezzanine financing which allowed the searcher to maintain a lot of the equity. I did not feel I wanted to go down this route as I liked the group of investors I had put together and was more than happy with the opportunity to earn up to 30%.

I also felt loyal to those who had funded my search and therefore was extremely reluctant to go outside my initial group for any monies that weren't taken up by investors (in fact this was what happened and I understand it is relatively rare).

My process was extremely bespoke and fitted perfectly to the flexibility of the search fund model. My investors very quickly understood the key dynamics of the deal and certainly 4 investors would have done the entire deal themselves. I believe the deal reflected my personality (which on analysis a lot of the search fund deals do vs the actual searchers) in that it is different with very significant upside but relies heavily on sales.

Thoughts

There isn't any deal you "can't" do as a searcher. My deal 'broke' almost every rule I was told about (turnaround, loss making, no due diligence, management team had been removed). However 6 months prior to my deal a retail franchise of frozen yoghurt shops was a deal done with a searcher, and it covered two of the 3 other 'excluded' search fund categories (retail and franchises – only manufacturing still drew a blank!). A good deal, particularly for a search fund, doesn't 'look' like any particular category. The lack of actual trend correlation with the timing of my search and the most successful searches meant I felt empowered to look at almost any type of deal (after all Id ignored having a partner).

Final Thoughts

I wish I could have found a way to genuinely enjoy the search, but I honestly didn't. Every single day I was searching I felt the tension of getting closer to running out of money and whilst it was extremely intellectually interesting, and led to a great many humorous stories and enjoyable experiences, I cannot by any stretch call it enjoyable. I started the process in a committed long term relationship and she even met other searchers partners. Regardless the uncertainty of the search is a lot to deal with, which in addition to my approach of almost constant travel is a terrible combination.

I volunteered at weekends at United Cerebral Palsy, which was great for stopping feeling sorry for myself. I also box competitively and I had a mentor who told me to eat right, sleep and exercise. I managed the first and the last but cant say I slept well at all. I allowed the team from Tough Mudder (which has gone on to be fabulously successful) to share my office and I formed a close bond with their company as they grew. It also provided a great counter offer to the search. I would have earned a lot of money joining them and would have fitted in well, but it served as a reminder how much I wanted to succeed on my own path and how committed I was to my investors.

I did always try and find other jobs that excited me or would be a good other option. This was my method of checking whether I really believed in the industry opportunity and the company I found. The best job I had seen in 10 years for me personally, appeared 2 months before I closed my deal, however I still felt the CEO role and the industry I picked were exactly what I wanted to do, and that my investor group was the right one.

OUTREACH LETTER (Bob's is a made up name)

SCOTTISH AMERICAN

228 East 45th Street, Suite 1801, New York. 10017
Telephone: +1 (617) 319-0794
Email: paul@scotamerican.com
www.scottishamericancapital.com

I hope this letter finds you well. What you have built at Bob's Insurance Group, Inc. by focusing on a variety of insurance products and services really stands out to me in my nationwide study of Managing General Agents and wholesalers. Bob's is an incredible part of the world and it is not surprising that a company like yours is based where employee loyalty, long term relationships and camaraderie are so fundamental. I have been focused on the insurance industry for many years and have raised a fund to invest in a business and grow it to its full potential. I am looking into Bob's Insurance Group, Inc. specifically as your reputation is as strong and the products and services you provide.

I am sure you have given some thought, every once in a while, to selling Bob's Insurance Group, Inc. taking on some capital to grow, or transferring ownership in an orderly way. I'm sure on a near daily basis you receive emails, phone calls, and contacts from brokers, investment bankers, competitors, accountants, and "deal makers."

I am none of these. I am a business operator who has raised capital in order to purchase a business and join the management team on a full time basis. I am looking to buy into one business and then spend more than 10 years growing the right company as we know that growing a great company takes time. I'm someone who will be as proud and conscientious about your business as you are. The capital has been raised from a number of experienced investors, who bring great contacts, relationships, and input to help further grow the business. We are looking to grow that company by the addition of significant capital, by acquisitions, and by broadening the services offered.

My investor group has deep experience and contacts in the insurance market, firstly by being intimately involved with Asurion's growth from $10m to $2.4bn, but also with Southern California Risk Management. I was personally responsible for lending to a Lloyds name broker Price Forbes. I understand MGA relationships and the insurance market well. If you were interested in our offer and wished to stay on post deal that would be fantastic. I would be able to release a considerable amount of capital (which you have earned for growing such a great business) and then partner to grow an even larger company on an exciting journey. Regardless of if you stay on board, the employees will all be taken care of, Bob's Insurance Group, Inc. will keep the same name, and we will ensure that your company's history is expanded and built upon.

I have spent considerable time looking into who would be the right partner and which business has the right culture for expansion and is ready to scale. I think that your well-established business has even greater potential.

Hopefully my website www.scottishamericancapital.com will give you a flavor of the seriousness of our intent and will give you an insight into the capital behind me. I maintain strict confidentiality and any deal would involve no broker or finder fees. Please call or e mail at your convenience if you are interested.

As you 'chew over' the decision, I thought I'd let you have a taste of some Scottish toffee to help you consider the proposal.

Kind regards,

Paul Thomson

OUTREACH LETTER 2 (1 MONTH AFTER 1st LETTER)

SCOTTISH AMERICAN

228 East 45th Street, Suite 1801, New York. 10017
Telephone: +1 (617) 319-0794
Email: paul@scotamerican.com
www.scottishamericancapital.com

I hope you are well. I wrote last month introducing my fund. I am very interested in talking to you about investing in and being part of the future success of Bob's Inc. Your company's focus on surety bonds and fidelity coverage has earned the respect of the industry, but I am confident there is room for more growth. I am sure that you have considered taking on some capital to grow, or transferring ownership in an orderly way, or more particularly, hiring talented people. I am not a remote fund, broker, competitor, investment banker, or some middleman. My fund is backing me directly to join the company to be part of a great growth trajectory. We are looking to invest in only one company.

The capital has been raised from a number of experienced investors, who bring extremely good contacts, relationships, and input to help further grow the business. I knew most of the investors from my time at Harvard Business School. XXX, one of the investors, created XXX, the largest XXXX company, and it grew to a value of over $400m - he is very excited about the prospects of your company. XXX is known as the professor of professional selling and has written McGraw Hill's best-selling books on sales strategy – he thinks there is significant potential with your firm. This is to name just two of the investors we have directly involved in this fund. We have a very long term horizon and known that it takes many years to grow the right company and such growth can only be done from the platform of a great culture.

We hope that we can help you grow by joining you. By providing the right kind of investment base, we can ensure that your focus on innovative solutions is maintained and that Bobs. remains an inspiration for other companies to emulate. I hope that you will consider meeting in either XXX or New York so that I can explain more about what we would offer.

Hopefully my website, www.scottishamericancapital.com, will give you more information and indicate that my intent is serious and that my backers are interested. Please feel free to reach out to anyone who you think may know or have heard of myself or my company as a reference.

I maintain strict confidentiality and any deal would involve no broker or finder fees. Please call or email me at your convenience.

Kind regards,

Paul Thomson

INVESTOR LETTER AFTER 6 MONTHS

Floor 4, 86 Walker Street, New York. 10013
617 319 0794 paul@scotamerican.com
www.scottishamericancapital.com

I hope you are well. Things are progressing reasonably well at Scottish American Capital. We are now 6 months in to the life of the fund, essentially a quarter of the way in to the timescale we raised money to search for. Whilst we have not signed an LOI we had 2 bids accepted on businesses but pulled out of the processes due to factors in the businesses we were not comfortable with and weren't able to see prior to bidding. We are currently most excited about the autistic services industry and are talking to number of business owners in proprietarily sourced deals. Included in this mail out is a document describing the autism industry and our approach which hopefully over the next few months will be something to refer to as deals start to firm up!

I use the term 'we' as in addition to the active investor involvement, the intern program has been very successful and we are now a firm of 3 FTEs. The interns continue to get more useful and the low cost makes this a great model. It is somewhat insightful that all of the good interns came via craigslist and the poor ones through the school noticeboards…. which was an unexpected recruiting trend.

Deal sourcing

We continue to believe that proprietary deals are going to be our source of purchase, so whilst we have a strong deal flow, the good proprietary flow has taken a while to build up, as relationships with river guides, attending and following up from conferences and ramping up our proprietary outreach (and honing our techniques) is slower than simply dealing with brokers. We believe the considerable hours and efforts we have put in to the mechanics are beginning to bear fruit, but as we have only just hit the search fund 'sweet spot' of the time when most searchers begin to get deals closed then we will be a lot surer at the next update whether this groundwork has been effective.

Hopefully you'll enjoy the toffee bar and the letter format via which this report came to you. We are mailing CEOs through this format which is proving successful considering the normal rates of response for outreach. We find cold calling and e mails to have an extremely low response rate (and poor deal quality), but find this letter format, conference attendance and river guides to be far better avenues. The particular format was honed by discussions with Jim

Sharpe, Neil Rackham and Steve Hollis of the investor group who suggested that 'snail mail' and disruptive marketing (the toffee bar) are less likely to be ignored than emails and phone calls. Naturally Jim and Coley at Pacific Lake's advice on the importance of river guides has been followed and is also showing signs of success, particularly in the autistic market.

Conferences are the most significant source of proprietary deals so far. I continue to attend a number (and travel a lot), and my 'teaching role' at NYU school of medicine ensures I pay very low fees, if I have to pay at all. We average $100 per conference vs full fees of $1000+. I attended HIMSS (electronic medical records, in Atlanta), Green Expo (in NYC), and 2 Autism Conferences (at Penn State and in NYC). The conference season is now upon us and so the next few months will mean a far higher number (autism conferences in NY and San Antonio, transcription services in Florida, back office processing in Atlanta and a number of different conferences at the Javits center are on the list so far).

<u>Brokers (we don't ignore this channel)</u>

We now have an up to date list of 8500 brokers. Our last email outreach generated 53 deals. We looked closely at 9 and bid on 2. Both bids were accepted but we became uncomfortable with aspects of the business as we progressed. In the first, a post production services company (technical work on reducing movies to fit smaller devices e.g. airline screens and smart phones, $2.3m EBITDA, price 3.8x). I was uncomfortable that the High Definition switch hadn't driven a recent unsustainable revenue bump and secondly was unsure that the CEO's relationships were transferable. The second deal was in-home Kidney dialysis. Whilst the EBITDA of $2.7m was good (price 4x), its defensibility of margins from insurance companies (94% Gross Margins) vs medicare/aid (6% GMs) worried me over the long term given its 50/50 revenue split from these sources. The increasing number of customers and cost vs in hospital treatment were favorable. In all the deals we have looked at, 25%+ of the price has been available via seller financing in addition to some senior debt, so the economic 'recovery' seems to be helping to allow funding for sensible deals.

<u>Fund expenses</u>

The expenses for the first 6 months of the firm were $78k. This amount is almost exactly one quarter of the funds raised but is skewed by the start up legal costs and the year end accounting fees. Essentially spending is below budget, though given the increasing amount of travel it is fair to say we are now tracking a 'run rate' that has us on target for the 2 years.

<u>My situation</u>

Personally there was a significant change during this last quarter in that my long term relationship ended. Essentially despite the amount of insights achieved prior to raising the fund, my partner was unwilling to continue with the uncertainty of not knowing where we may end up and my frequent travel. The only impact on the fund so far is that the amount of hours worked has gone up and I no longer have any compromises on my time, but I'm sure you can imagine it hasn't been the easiest readjustment. As a single searcher, and reflecting on the questions most investors asked during fundraising, I felt it right to update you on this....though please don't expect future updates on this area! One of the investor group just reminded me that I effectively 'saved' 50% of my upside – which is a nice thought!

Industries of Interest

We put significant work into the electronic medical records market, then carried that over into the medical transcription market. Essentially the market has a great growth potential, though doctors are very hard to sell to and no one has cracked the sales model below the medium sized hospital level (90% of doctors are still entirely paper based). We looked at a number of deals but the market is very heavily skewed (in terms of pricing) by the sheer volume of venture capital dollars and private equity suitors. The LA based company we looked at had revenues of $12m and broke even. It valued the company at over $40m and had little in the sales pipeline. A coding company we looked at had EBITDA of $1m and had signed a contract believed to add $4m more. Yet it was only willing to consider 20% of the equity for $10m. We have pulled out of a number of other transactions at early stages due to the valuation issues, which if the growth rate was backed by a sales pipeline would be sensible, but most of the companies will not exist in the long run and so the pricing seems to preclude a sensible deal.

Transcription is something we continue to look closely at and are in discussions with 4 business owners. The good companies have very strong recurring revenue streams and are clearly differentiated. The move to offshoring 5 years ago has not gone well and a number of contracts are being 'onshored'.

We have looked closely at the Inc 5000 list for the current year and additionally have back to the list from 2004. We have reached out to a number of these companies in various industries and are in early discussions with some. We believe some other niche industries may pop out of this approach. Autistic services (a fuller explanation is in the attached document) is our number one target at present.

Please don't hesitate to get in touch, whilst the morale is good at this end, and I love the job/search (though am very keen to get managing a company), we are a small team and any insights you have are always most welcome

Kind regards,

Paul

	Fragmented Structure	Historically High Margins	Defensibility of business model	Flexibility for Growth	Historic Stable Growth	Basic Operations	Limited Cyclicality	Favorable Labor Market	Low Liability/Regulation	Low Seasonality	Score
Transcription	5	2	2	4	4	4	5	3	4	5	38
Digital Marketing	4	4	2	3	3	2	2	3	4	3	30
Electronic Medical Records	4	4	3	5	4	3	3	3	2	3	34
Solar Installation	4	2	1	3	3	5	2	4	4	2	30
Bank	4	5	4	3	4	1	3	3	1	3	31
Content Creation	3	3	3	3	3	4	3	4	5	3	34
Specialist Safety Equipment											0
Medical Tourism											0
Building Energy Management	4	3	3	4	3	2	3	3	3	4	32
Pollution Control (hazardous waste)	4	3	4	3	3	4	4	4	3	3	35

Industries Analyzed

Those I wouldn't look at

Manufacturing

Retail

Oil and Gas

MRI scanners (I never knew why, just everyone was selling them and that was a bad sign)

Car washes

Distributors

Industries I looked over 2 days at

Erecovery

Embedded software

Content Management Systems

Digital Marketing

Post Production movies

Medical Practice Management

Legal Transcription

Medical Education

Staffing

Data Centers

Ice Machines

Government infrastructure contracts

Medical Schools

Search Engine Optimization (and related business models)

Prison medical services

Online pharmacies

Gun supply

Non prescription drugs

Subscription Management

Insurance Agents (retail, and lead management)

Home healthcare

Ambulances

Green buildings

Green analytics

Plumbing supplies

Mortuaries

Coffin Makers (particularly for larger people)

Medical collections

Medical coding

Accountants

Wine distributors

Event Planning

PEOs (professional employer organization i.e. outsourced HR)

Closed captioning

Company training

In more depth

Kidney dialysis

Autistic services

content management systems

Electronic Medical Records

Medical Tourism/ Travel

medical transcription

content creation,

boxing gyms

Craigslist wording

Small Manhattan based Private Equity firm seeks interns for research/deal analysis.

Run by Harvard Business School alumni and investing in the small/middle market area, a new private equity fund (founded Jun 2009) seeks interns. The internship can be full time (from immediately until school restarts) and/or can continue through the school year.
We seek both undergrad and MBA students. The minimum commitment is 10 hours a week.

Once we purchase a firm there will be opportunities for full time roles within the purchased companies.

You will work directly for Harvard MBAs and be exposed to live deals and transactions.

The work is typically able to be considered for college credit and we will provide letters of recommendation as well as introductions to our vast network of contacts in consulting firms, banks, other private equity firms etc.