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Don't Be Afraid to Raise Equity During Tough Times

It's never easy to raise money in the restaurant industry. Yes, there's been a window for a number of years where we've seen private equity, both funds and individuals, investing in promising deals. This is particularly true in new concepts that have shown strong initial growth with the potential to be franchised. The same for fast-growing corporate stores that would eventually be sold to a strategic buyer.

This is a new world and the old window for an easy raise of capital is closing. Let's look at the new thought process, exploring five different ways in which to raise money during these tough times:

Private Equity Firms

Some of the major private equity firms that were participating in the restaurant industry pre-Covid may pull back somewhat because of valuation issues and uncertainty of their previous investments, but don't be totally dissuaded. There are still a number of private equity groups looking for opportunities. I will call them "opportunistic funds."

Many of these opportunistic funds are closely held, and I am aware of at least four firms looking for smaller investments, generally in the $3 million to $10 million investment range. They are looking for emerging concepts. They won't get hung up on valuation because they are probably going to take a preferred class of investment and stage their investment dollars into the company.

Also, one private group I am aware of is looking at loaning money to worthy owner-operators versus their normal equity investment stakes. Obviously the interest rate they will charge is high, but this takes away a little bit of the risk from the current uncertainty. OK, it's easy to talk about these groups, but how do you find them?

A good way is to look for capital is by reading up on previous deals in industry publications, such as the Monitor. The Monitor's Finance & Real Estate Directory is also a great source for capital. Talk to accountants and lawyers who work in the restaurant and franchise finance world. Feel free to contact me, or members of our firm. In summary, private equity is not dead, it is just more opportunistic.

Landlords

I've come to believe that you should partner with your landlords. Landlords need their tenants to succeed, so things such as working capital, Covid-related capital improvements, or converting back rent to equity are all items to be explored. Large national landlords are probably not going to provide equity, although they may look at repayable, or earn-out loans. Local landlords are the best candidates for making investments. Also, it is good to have the landlord investment in a separate entity that only owns that particular store.

Try as much as possible to structure landlord investments as equity, and make sure they are paid back out of profits, sometimes using a waterfall approach where the landlord gets a preferred return first and then to the common shares. All of this can be negotiated.

Private Individuals

The private placement market is still alive. In fact, while potential investors may be somewhat cautious, they also may have a soft spot in their hearts for small business. The nice thing for many investors is that the stock market has come back to life, so they don't feel their net worth has dipped and they also may be thinking that private investments are at historic low values and thus worth considering. So a carefully drafted private placement document can be very effective. If you own a concept that has either bottomed out, or shown some resilience during this period, it may be a good time to raise money with a private placement. Private placement equity can be used to either shore up your working capital position, or to fund future growth.

Crowd Funding

In our online world, what fits better than crowd funding? There are two types of crowd funding: reward-based and equity-based. A pure equity approach may be tough because of the uncertainty in the Covid world, but the reward-based crowd funding tactics are right on point. People who have stayed home and now are looking to go back out again want to get a deal or feel a part of something and are likely to crave gift cards, discounts, clubs, special offers and memberships. All of these crowd-funding techniques and money they raise can help to restore working capital. Try and be creative. Groups like Kickstarter or GoFundMe are a good starting points.

Local, State and National Programs

The last idea for raising investment in this type of market is to look at some of the grants that state and local governments are providing. There also may be some money for minority-owned businesses. You need to scour local, state and national programs (that are more than just PPP) and find other resources that may be available. I can think of a number of states that do have these grant programs available to small business owners.

These are just a few ideas for you to consider. The key is to be resourceful. Check with your professional advisors and don't be afraid of asking others, including your existing investors. They may want to protect their investment and might consider providing some bridge money to get you through these tough times. Just remember this: There is still money out there.

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