Trendsetter Barometer

Private companies have plenty of capital
Many plan to spend it on growth

pwc

Highlights

- Most Trendsetter private companies had sufficient capital in the past two years and expect similar access to capital over the next two years.
- Private companies are looking to invest their capital in growth again, shifting their focus from core concerns (operations, personnel) to more ambitious goals (market expansion, mergers and acquisitions).
- While the majority plan to tap existing lines of credit over the next couple of years, some also plan to leverage their relationship network—indirectly sourcing funds through strategic alliances, joint ventures, and suppliers.

Capital has been in good supply over the past two years, according to most of the 245 chief executive and financial officers interviewed from August to November 2010 for PwC's *Private Company Trendsetter Barometer* survey. Two-thirds say their companies' access to capital has been excellent or good, and most expect that over the next two years their ability to obtain capital will improve or remain the same.

Spending agenda: Shift from core needs to growth

Over the past two years, companies have been less intent on seeking capital for R&D initiatives, international expansion, or M&A opportunities and more focused on meeting basic operating needs and maintaining their workforce.

"Private companies have been paying down debt and spending their cash conservatively," says Ken Esch, a partner in PwC's Private Company Services practice. "That's been the norm the past couple of years. We're beginning to see that change, however, as more companies eye growth opportunities again."

Looking ahead at the next two years, Trendsetter private companies say they'll need more capital to further develop or expand into new markets, seize M&A opportunities, and upgrade their sales and marketing operations. "Just how far companies pursue their growth objectives will depend on the degree of certainty they feel about market conditions," notes Esch.

Access to capital: Good but varied

Most Trendsetter private companies had adequate access to capital over the past two years—though some had better access than others:

	Good/ Excellent Access	Average Access
All private companies	66%	23%
Large private companies*	79%	17%
Small private companies*	58%	27%
International	73%	21%
Domestic-only	61%	25%
Product sector	70%	22%
Service sector	62%	24%

Large private businesses have $100M or more in revenue. Small private businesses have under $100 million in revenue.

Capital shortfall: Demographic snapshot

Trendsetter private companies that lacked capital for certain key initiatives over the past two years were smaller and slower-growing than their survey peers but more interested in international expansion:

	Shortfall Group	Survey Peers
Five-year growth rate	71%	101%
Average enterprise revenue	$125M	$319M
Have an international presence	39%	48%
Seek broader international presence	19%	12%

Recent *Trendsetter* data[1] shows that private companies' optimism about US economic growth has gradually declined over the past two quarters. But as Esch observes, "Despite feeling less optimistic about the US economy, companies are increasingly viewing growth as an imperative, upgrading it from a want to a need. Instead of regarding expansion as optional, they've begun to see it as a competitive advantage that will ensure their survival."

Companies seek capital to revive tabled growth plans

While most private companies have had enough capital to meet their basic operating needs, 37% of Trendsetter executives say their companies have lacked adequate capital to fund certain key initiatives over the past two years.

Some of those companies may be looking to revive such initiatives. Twenty-nine percent of surveyed executives said that access to capital would be more important over the next two years than it had been over the past two years; 61% said the importance would remain the same (9% said it would be less important). Those who said the importance of access would increase plan to spend the capital in the following top areas:

- Development of or expansion into new markets, 61% (21% of all firms)
- Upgrading of sales and marketing operations, 48% (17% of all firms)
- M&A opportunities, 40% (14% of all firms)

These same areas were among the top three where Trendsetter private companies had insufficient funds to move key initiatives forward over the past two years.

For a fair number of companies, however, investment in these three areas wasn't even on the agenda during the last couple of years: The percentage of companies with insufficient funds for upgrading sales and marketing operations was equal to the percentage of companies for which such investment hadn't been under consideration (combined, these two groups comprised roughly one-third of the companies surveyed). Likewise, the percentage of companies with inadequate capital to further develop or expand into new markets over the past two years was nearly equal to the percentage that hadn't looked to invest in such activities (combined, these two groups also comprised one-third of surveyed companies). As for mergers and acquisitions, over half of Trendsetter companies were not focused on pursuing such opportunities.

"What we've seen is that over the past two years, many Trendsetter CEOs have focused primarily on meeting their companies' basic needs," says Esch, "and so they've tabled discretionary spending. As a result, a good number of private companies have built up cash reserves, which they can now spend on their business wants. Such businesses are moving beyond survival mode and repositioning themselves for sustained growth."

1 3Q10 *Trendsetter Barometer Business Outlook*.

Two-year outlook: Access to capital

Trendsetter private companies anticipate similar or better access to capital than they had in the past two years.

	Same Access	Easier Access
All private companies	56%	30%
Large private companies*	52%	36%
Small private companies*	60%	26%

*Large private businesses have 100M or more in revenue. Small private businesses have under $100 million in revenue.

Capital horizon: Where companies say they'll look

Most Trendsetter private companies intend to seek capital through traditional lenders over the next two years, though some plan to tap other sources as well:

	Yes	No
Existing credit lines from banks/financial institutions	73%	20%
New bank loans	27%	66%
New credit lines from banks/financial institutions	37%	56%
Strategic alliances	38%	51%
Joint ventures	34%	58%
New credit lines from suppliers	25%	69%
New equity partners	17%	74%

Where companies plan to obtain new capital

Seventy-three percent of Trendsetter CEOs plan to access existing lines of credit from banks or financial institutions over the next two years (51% to a major extent and 22% to a minor extent). "Many private companies have been fiscally conservative these past two years," says Esch, "and so they haven't drawn down their current lines of credit. For some of them, paying for key initiatives may be more about tapping available funds than seeking new sources of capital." However, nearly the same percentage of CEOs (70%) plan to access other sources of capital (42% to a major extent and 28% to a minor extent).

These other sources of capital include new lines of credit (37%) or new bank loans (27%)—with a net 45% of Trendsetter companies planning to seek funds through such avenues. A net 29% of the surveyed companies plan to access a variety of other sources, including new equity partners (17%), venture or equity capital (11%), and "Angel" investors (9%). "For companies looking to grow again, existing lines of credit might not be sufficient to fund ambitious plans," says Esch. "As a result, we're starting to see private companies become more creative in their strategies for accessing capital."

Indirect sourcing is one example of that creativity, with Trendsetter private companies planning to explore ways to share costs through strategic alliances (38%) and joint ventures (34%) over the next two years. One-quarter also said they intend to seek new credit lines from suppliers.

Large private businesses and product-sector companies were more interested than their smaller and service-sector peers when it came to obtaining new lines of credit from suppliers (34% vs. 18%, and 31% vs. 18%, respectively). More service-sector private businesses, on the other hand, said they were likely to seek capital through new equity partners, as compared with their product-sector peers (23% vs. 13%).

"This mirrors what we've seen with many of our clients," says Esch. "Service-sector companies routinely look for new partners. By effectively using their relationship network, they're able to cut costs and extend payments—an approach that's provided a buffer during the downturn. We expect that private companies in general will increasingly turn to this and other funding alternatives as they become more alert to the full range of capital sources available to them."

Knowing what funding options are out there

While a good number of companies are looking beyond traditional lending sources, 59% of Trendsetter CEOs say their most important sources of capital over the next two years are likely to be existing lines of credit from banks or financial institutions. The majority do not plan to seek capital through cost-sharing arrangements with joint ventures (58%) or strategic alliances (51%), nor do most of them intend to tap suppliers for new credit lines (69%). Three-quarters say they have no plans to seek new equity partners.

A primary reason for this may be that most private companies (74%) turn to their current lender first and stop there. "Too often, credit-worthy companies fail to shop around for the source of capital that best suits their growth objectives," says Esch. "It requires some research, but studying a range of borrowing options can be well worth the time and effort for growth-oriented businesses."

PwC's Trendsetter Barometer tracks the business issues and best practices of privately held US growth businesses. The 3Q2010 results incorporate the views of 245 chief executive officers (CEOs/CFOs) interviewed between August 6, 2010 and November 1, 2010:

Profile of management panel demographics:

Average # of employees	737
Average revenue	$168.7 M
Average enterprise revenue	$247.2 M
Average five-year growth	90%

PwC's Trendsetter Barometer is developed and compiled with assistance from the opinion and economic research firm BSI Global Research, Inc.

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1 2009 Forbes America's Largest Private Companies List

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