

# The Nuts & Bolts of Investment Banking

*(Why Investment Banks are a Better Source of Financing)*



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By now we all are painfully aware of the worldwide credit crisis that affects us all. If you have a business or a project that needs capital, keep reading. Because the traditional retail banks of the world have virtually frozen their lending practices it is imperative to locate financing that is liquid and secure! While most of the capital that is missing from the market is being held by the banks, a great portion of the liquidity has moved from the public markets to the private. Where do you go to find this liquid capital? The answer is **investment banking**.

What do you think of when you think of an investment bank? Do you see an investment banker as one that invests your hard earned money into the stock market or other common investment structures? Perhaps you believe an investment banker to be one that caters only to the super wealthy. The answer is both, and much more. Investment banks also bring investors together to invest in high return projects that need financing, hence the super wealthy. Most of these investors, however, are funds, corporations, or other financial institutions. So, how is this done, and how can your project get financing via an investment bank?

Let's look at how the bank brings investors together with projects that need funding. The process is very similar to an IPO (*initial public offering*), which is how a private company offers to sell its shares of stock to the public to raise capital. Thus the private company becomes a publicly traded company via an international stock exchange. However, the process we will be speaking of is called a PPM (*private placement memorandum*). A PPM is simply a vehicle that an investment bank uses to sell shares of a private (*non-public*) company to private investors to raise capital for the client's project. The investors can act as joint venture investors, or they can simply hold a debt against the project. In a PPM the bank goes to private investors for the capital (*many investment banks do both IPO's and PPM's*). A PPM is created to be presented to the bank's investors that are seeking a high yield investment for their capital. This process is much more efficient for the investment bank as they have a relationship with their investors. The bank knows exactly what their investor will and will not invest in. So, the bank will only bring projects to their investors that the bank knows the investor will buy. Now, how is this accomplished? The process is as follows:

**Where do you go to find liquid capital? The answer is investment banking!**

1. The bank receives a high quality business plan regarding the project. This plan is then turned over to the investment bank's team that will spend many days reshaping, rebuilding, verifying accurate numbers, and doing the banks due diligence on the information provided. The bank hires the highest quality attorneys, PhDs of economics for financial modeling and forecasting, CPAs, and other top flight research team members to determine if the submitted business plan has merit. If it does not have merit the team goes to work to determine how the plan can be restructured to gain in value to be sold to the investors. Remember, the bank knows what their investors are looking to invest in. This process can take as long as 20 to 45 days. Once the team of attorneys, CPAs, market managers, etc. has completed the rebuilding and verification of the numbers in the plan, the bank proceeds to the next step.
2. At this point the business plan is ready to be submitted to the investment bank's marketing/management team to create the prospectus for the PPM. This is created for presentation to the bank's investors seeking a high yield return on their money. In this phase of creating the prospectus the client and the investor negotiate their respective positions on how the transaction will be structured. Now, much of this process is already completed in the previous phase, but it is here that any issues are worked out to the mutually beneficial outcome of the project. No one makes money unless the

issues are worked out. The PPM protects the client seeking funds for their project by creating the correct PPM for the correct investor. Remember, the bank has a long term relationship with their investors so all the work up to this point has been geared to make sure the project will deliver the high yield the investor is looking for. So, now the PPM will spell out to the investor what they are getting in return for their risking their money for the project at hand. Therefore it also protects the investor. This process can be very short to as much as 3 months to complete. Once all this is completed the PPM is let out to the investors.

3. Now, the investor has a clear road map of what they are investing in. It is at this point the investor(s) provides the percentage of capital to the project they are seeking, which is known as a subscription agreement. If the financing is structured as a joint venture, the investors will take as much as a 50% equity position. If the financing is structured as debt, the repayment typically has a grace period before commencing. The project may only require one investor, or it can take several investors to cover the entire PPM. In some cases the capital raised can cover 100% of the cost of the project. The projects can be almost anything, from high end technology to an acquisition/development/ construction funding for a hotel. Once the required capital is raised the funds will be placed into a SPV (*special purpose vehicle*) bank account for the purpose of funding the project. Furthermore, in case of a joint venture the clients company will be hired by the SPV to run and manage the project. The investors are typical silent partners that receive monthly financial statements for their review.

Now, a few very important items to remember before you seek out an investment bank:

- a. The bank makes nothing until the investment for the project is raised. Any fees you pay to the bank are used in the due diligence process.
- b. There will always be a cost to you as the client. The client will be required to pay out of pocket for all the due diligence, the creation of the PPM, and the marketing of the PPM. The bank will not risk its capital to determine whether or not you have put together a good business plan. This cost will run anywhere from \$500K to over \$1M depending on the size and magnitude of your project. The bank may allow the client to pay this fee is several payments. The minimum financing amount for the PPM for many investment banks is \$25M.
- c. There are no guarantees from the investment bank. Your best guarantee is how confident you are in your business plan. Remember though, the bank is dealing with investors they have good relationships with. They know what they want to invest in so the risk to you as a client is minimal, if your business plan is of high enough quality. Because the bank is regulated, they are required to give their best efforts to fund your project. Legally they cannot give a guarantee; however, because of their relationships with their investors they know what the investors will buy, so the bank will not accept a project they cannot get funded. No one in this transaction makes any money until the project is funded. Any and all fees that are paid up to this point are paid out to cover all expenses.

Today is a good day to secure financing for your project via an investment bank. Concord Capital works closely with multiple investment banks around the world.

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