



# CAPITAL RAISING WITH A FINANCIAL GUARANTEE

## *Introduction*

Access to finance is fundamental to the development of any business. Capital underwrites innovation, the take up of new technology, the exploration of new ideas and is the basis for business growth and expansion. Without capital a business withers.

SME's are usually sales-driven and growth-oriented, and their entrepreneurial nature often results in earnings and enterprise value volatility that can preclude traditional financing options. Since most business owners are loath to relinquish equity, with as senior debt being the primary form of financing.

More recently, new innovative products have been developed to assist SME's raise much needed capital including mezzanine finance, venture capital, second liens, bridging finance, and pseudo-equity. The greatest challenge that SME's face is the level of perceived risk attached to their business by prospective equity investors.

## *Financial Guarantees*

An Equilinx Financial Guarantee is an innovative financing product specifically developed to assist projects and existing businesses raise much needed capital. This Financial Guarantee is created using an insolvency risk instrument that provides the investor/financier with an irrevocable, non-cancellable security.

For the investor/financier to be able to fully rely on the Financial Guarantee in the event of a claim, the Financial Guarantee is only arranged with insurers with a credit rating of A or higher.

The risk instrument provides the investor/financier with a 100% Financial Guarantee. Should the investee become insolvent the investor/financier will make a claim against the bond for the total amount insured under the Financial Guarantee.

## *How do Financial Guarantees Work?*

Equilinx together with the investee company develops a financing strategy that satisfies both the investor and investee. Equilinx identifies an insurance underwriter who is prepared to underwrite the Financial Guarantee giving the investor/financier a money back guarantee should the investee become insolvent.

Using a Financial Guarantee ensures that in the worst case scenario an investor/financier will get their money back should the investee be in default.

As the objectives of both the investee and investor/financier vary and therefore alignment of both interests are necessary, each transaction is bespoke.



## *The Guarantee (Bond)*

The Financial Guarantee provided to investors is a non-cancellable, irrevocable Financial Guarantee from an A rated insurance underwriter.

The underwriter provides a Financial Guarantee with the investor(s) being the beneficiaries. The risk instrument creates a risk free investment for the investor(s).

## *Benefits to the Investor(s)*

The key benefits of a Financial Guarantee utilising an Equilinx structured risk instrument are:

- ❖ Investors receive a 100% capital guarantee for their initial investment.
- ❖ The above provide investors with a total guarantee on their investment should the investee default or become insolvent.
- ❖ The risk instrument can be structured to meet both the investor and investee objectives.
- ❖ Should the investor(s) make a claim, the underwriter is responsible for salvage/recovery not the investor.

## *Benefits to the Investee*

The key benefits to an investee are:

- ❖ The ability to offer substantial security to investors that would not otherwise exist.
- ❖ The Financial Guarantee can be used by the investee in its marketing campaign to attract potential investors.
- ❖ The transaction could be structured so that existing investors do not give up additional equity.
- ❖ The Financial Guarantee can be structured in such a way that it provides the investee greater flexibility for capital raising.



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## EXAMPLE OF A RECENT TRANSACTION

### The Problem

The firm had a Debt/Equity ratio of 100% and therefore a financial risk rated as being "High Risk" (T/O \$4m; EBITDA: Break-even; Net Worth: -\$3.5m). The business needed to consolidate debt and raise additional equity. The business had significant business opportunities which it could not take advantage of due to the lack of capital and the reliance on 100% debt finance.

### The Objective

The objective was to consolidate debt (\$7m) into one financial instrument (Preference share: cumulative, redeemable, convertible, Coupon 10% pa) with an additional \$1m for payment of Bond premium at Settlement, backed by a Financial Guarantee. The Financial Guarantee was essential due to the prevailing financial risk of the company. The majority shareholder and CEO wanted a solution that minimised his equity dilution.

### Solution

Equilinx undertook financial due diligence and a complete risk assessment of the management and business operations. An Information Memorandum was prepared by Equilinx and forwarded onto an A rated insurer to obtain a Financial Guarantee for \$8m.

### Summary of Financial Guarantee:

Amount:	\$8m AUD
Premium:	5% pa (\$1.2m)
Term:	3 years
Bond Structure:	Max of 8 beneficiaries IE \$1m x 8
Conditions:	Non-cancellable
Insurer:	A rated
Securities:	Provided by Borrower (FFCC, Personal Guarantee of Owner & Major Shareholder, Property Portfolio - \$5.5m)

### Result:

Equilinx identified an off-shore investor who was willing to invest \$8m on the basis of the securities provided and the additional security of the Financial Guarantee therefore there was no need for multiple finders/investors. The Borrower sourced an additional \$20m in equity to implement its M&A strategy, restoring Balance Sheet debt/equity ratios and Net Worth.

## What is the Role of Equilinx?

Equilinx is an accredited risk assessor for the insurance underwriters and evaluates each project on a case by case basis.

Typically, Equilinx's role includes:

- ❖ Undertaking due diligence on the investee.
- ❖ Assessing the level of risk of an investee.
- ❖ Assisting the investee in designing the best financing structure that satisfies all the transaction party's objectives.
- ❖ Liaise with insurance underwriter's Australian representative.
- ❖ Ensure timely execution of documents.
- ❖ Assist the investee in the capital raising process should this be requested.

## What are the Costs?

The insurance premium on the Financial Guarantee (bond) is paid by the investee. Premiums range between 2.5% to 5.0% pa of the amount being insured depending on assessed risk.

Project risk assessment, due diligence and other tasks and activities undertaken by Equilinx are negotiated and agreed with the investee prior to an Equilinx engagement.

*Contact Equilinx and find out how your business can benefit from using an Equilinx Financial Guarantee to enhance your chances of raising the capital required.*