Emerging & Growth Markets

Driving Growth

Ideas and Insights for High-Growth Companies

- WINNING THE IPO WAITING GAME
- SARBANES-OXLEY AND THE IPO EQUATION
- OPTIMIZING VALUE IN THE M&A MARKETS
- MEET THE ERNST & YOUNG WORLD ENTREPRENEUR OF THE YEAR® AWARD WINNER
- BIOTECH INVESTOR INSIGHTS AND OUTLOOK

Ernst & Young

Quality In Everything We Do

Driving Growth

Ernst & Young's Emerging & Growth Markets Group

Perhaps your company is a first-mover with a dynamic leadership team, global vision, and innovative ideas. How're you going to grow in today's challenging markets? You're going to see the current environment not as an impediment, but rather an opportunity to gear up for growth – to get one step ahead of your competitors... before the market springs back to life.

Introducing: The Growth Drivers Framework

Ernst & Young's Emerging & Growth Markets Group takes an issues-based approach to serving our emerging and rapidly growing clients. We help you address business issues that arise around the following six growth drivers:

- Strategy
- Finance
- Transactions
- Operations
- Reporting
- Risk Management

An Issues-Based Approach

We use the growth drivers as a framework for understanding our clients' business imperatives at their current stage of growth. The growth drivers provide a tool that helps us – and our clients – take an issues-based approach to providing them with practical services. How? By focusing on real problems and drawing on our 30 years of experience serving entrepreneurial companies using the growth drivers approach.

On Top of the Issues

In that spirit, we offer perspectives and insights around the challenges faced by entrepreneurs today under the theme of "Driving Growth." Whether you want to... understand how the most successful companies prepared for their IPOs and how the Sarbanes-Oxley Act of 2002 fits into the equation... learn more about what you can do to position your company for an optimal M&A transaction... find out the success secrets of one of today's top technology entrepreneurs... or tap into the latest biotechnology investor insights and outlook... keep on reading!

To find out how the growth drivers apply to your business, or follow up on any of the issues discussed in the articles, visit us at www.ey.com/us/drivinggrowth.

Sincerely,

Daniel J. Love

Daniel J. Love
Americas Director
Emerging & Growth Markets
Ernst & Young

READY, SET, SLOW:

Winning the

BY **JOSEPH MUSCAT**
Partner, IPO Transformation ~ CEO Retreat Chairman

"Time is on my side, yes it is."

IN a business world that places a premium on speed, these words may seem out of place. Ironically, however, in today's slow IPO markets, the Rolling Stones' lyrics ring true. Today, while companies envisioning an IPO to accelerate their growth face unreceptive capital markets and an increasingly complex regulatory environment, they at least have that rare luxury: time. But for what?

Time to cement their business strategy. More importantly, perhaps, time to act like a public company before actually becoming one. Many of the companies behind the failed public offerings of the 1990s "bubble" viewed speed as paramount and rushed from start-up to IPO. Which is why, now that the IPO market "window" is closed, today's a good time to prepare your organization for going public — before the IPO window re-opens and the pressure to go out becomes too hard to resist. Indeed, fortunately, IPO-bound companies now have the luxury of *lead time* — which, along with preparation and *competitive position* — is common for highly successful public companies, according to Ernst & Young's *Measures That Matter*℠ research.

Not surprisingly, leading the transformation of a private company into a public enterprise has never been more complex. Sarbanes-Oxley and investment banking reform have dramatically changed the regulatory environment over the past year. IPO-bound companies face changed expectations among institutional investors and the investing public. By instituting the right strategies now, a CEO and management team can take an offensive rather than a defensive stance.

Wanted: Solid IPO Candidates

While bear markets come and go, the value of solid, well-managed companies remains constant. That was the message delivered to CEO-led teams from more than 50 high-growth private companies at the seventh-annual Ernst & Young IPO Transformation ~ CEO Retreat held in May at the Ritz-Carlton Laguna Niguel in Dana Point, California. The conference's attendees — CEOs from tech-

IPO Waiting Game

nology, financial services, telecommunications, life sciences, health care, retail, and consumer product companies accompanied by their key team members — heard a clear message. Leaders of recent IPO success stories, investment bankers and portfolio managers strongly believe that companies that focus on business fundamentals, deliver superior financial performance organized with a good corporate governance structure and an effective communications program, will always attract long-term investors.

There was a consensus among conference participants that companies have to "live" longer before they can tap into public funds. They're going back to an investment environment last seen in the late 1980s. Maturity is creeping back into the market.

According to Shaker Khayatt, vice president of Goldman Sachs, "Stories that have the best chance of selling are about companies that have proven business models, have profits or a clear, short path to profits, are well positioned, have a broad and deep management team in place, and have the infrastructure of a public company."

A Process, Not an Endgame

The IPO has too often been seen only in terms of an intense transaction that begins with the selection of investment bankers in a "bake-off" and the drafting of the prospectus, continues with the road show, and ends with the first day of trading. But it doesn't stop there. After the IPO, the organization must meet the operational requirements of a public company while delivering the value it has promised to shareholders.

But it doesn't start there either. Ernst & Young's *Measures That Matter* research shows that the CEOs of the most successful companies (in terms of post-IPO performance) began transforming their company — strategically, operationally and financially — in a process that sometimes began years before they went public. Improvement initiatives in the areas of strategic planning processes, accounting and reporting systems, investor relations and employee incentive compensation, were identified as contributing the most to post-offering performance.

Ernst & Young calls this transformational process the IPO Value Journey™, which includes planning, execution, and realization phases, each of which is designed to position companies for maximum value at the IPO and beyond. The Value Journey is comprised of the following steps:

- **Define Stakeholder Success.** Make sure that stakeholder interests (corporate and personal, financial and non-financial) are aligned.
- **Chart Your Business Strategy.** Prepare a thorough business plan that can serve as your own road map and can communicate your vision to potential investors and other stakeholders.
- **Accelerate Your Plan.** Find ways to realize your business plan faster or more cost effectively.
- **Chart Your Transaction Strategy.** Consider accelerating your company's growth through one or more strategic transactions: acquisitions, alliances, divestitures, recapitalizations, or private financings, etc.
- **Create the Winning Team.** Assemble strong internal and external teams with the right combination of skills to lead the company through the IPO and many years beyond.
- **Complete Your IPO Platform.** Complete the strategic, operational, and financial improvements necessary to operate as a public company.
- **Be the Public Company.** Act like a public company before the IPO. Close the books on time, forecast financial results accurately, manage investor expectations, and benchmark against your public company comparables.
- **The IPO Event.** Write and file your prospectus; then go on the road show.
- **Deliver the Value.** Meet the expectations of investors, analysts, employees, customers and the board, quarter after quarter.
- **Renew and Recreate.** Maintain your momentum, update your vision, create a new set of milestones, and remain innovative and fast growing. (In other words, start the Value Journey all over again!)

Why Go Public?

The first step in the IPO process is to articulate a compelling need for the capital of public investors. Executives surveyed at the IPO retreat were motivated by old fashioned, basic business goals including executing acquisitions, expanding internationally, and developing new content and platforms. In short, emphasized Robert Thomas, president and CEO of NetScreen Technologies, at the IPO retreat, “Public companies have more credibility than private companies.”

Ernst & Young’s *Measures That Matter* research, based on a survey of executives who completed IPOs between 1996-2000, validates the conference attendees’ perspectives. Completed with the Economist.com, this research shows that IPOs that experienced long-term success were motivated primarily by business needs such as funding product growth, market expansions or acquisitions. Unsuccessful IPOs, on the other hand, were associated with motivations like corporate visibility, funding marketing, attracting talent and personal ambition.

Leveraging Your Transaction Strategy

This research also illustrates that many highly successful IPO companies completed acquisitions to obtain critical mass, broaden their product lines, and beef up their alliances and joint ventures to fill gaps in their business strategies in anticipation of the offering. A full 50 percent of the companies surveyed said they wished, in hindsight, that they had completed an alliance or joint venture to fill gaps in their business strategy.

> “If you’re going public in the next six months or a year, then you have to start acting like a public company now.”
> – **John Kunze**, *President and CEO, Plumtree Software*

Beyond Financials

As part of the same research, Ernst & Young surveyed portfolio managers to gain insight into the key financial and non-financial metrics they use when making a buy or sell decision, updating a survey completed in 1996. Not surprisingly, the research shows that superior financial performance measured against comparable companies is paramount. More surprisingly, though, the research showed that non-financial measures accounted for nearly 40 percent of a portfolio manager’s decision-making. The key metrics included quality of management, innovativeness, the ability to attract talented people, management credibility and brand image.

These findings underscore that value is often found off the balance sheet. Which is why company executives who want to realize the greatest value at the IPO and in the public markets must understand, manage and communicate the non-financial metrics for their industry.

The Shock of the New

The recently adopted Sarbanes-Oxley Act brings new challenges for the executive leading a company through the IPO transformation process. It significantly raises the bar for operating as a public company. Panelists at the retreat agreed that the new regulatory requirements under Sarbanes-Oxley are going to make it more expensive to go public. The risks of insufficient preparation are higher than ever. But the silver lining here is that, according to Katharine Martin, partner, Wilson Sonsini Goodrich & Rosati, “Good governance is typically equated with lower risk.”

We talk about some of these challenges in the accompanying article, *Comply Now, IPO Later: Factoring Sarbanes-Oxley Into Your Capital Markets Equation*. To be prepared to operate as a public company under Sarbanes-Oxley, companies must have a board of directors with greater independence, financial expertise, and committee structure. They need the financial systems in place to allow management to certify internal controls and financial results to the Securities and Exchange Commission.

Sarbanes-Oxley also changes how companies work with their auditors. As a private company, executives may have depended on their auditors to provide a wide range of advisory services. Now, the auditor who attests to a public company’s financial statements is prohibited from providing a number of services. But Sarbanes-Oxley is not alone in calling for change in the business landscape. The Securities and Exchange Commission, National Association of Securities Dealers, and New York Stock Exchange have all issued regulations that companies in line for the “first wave” of post-Sarbanes-Oxley IPOs should begin addressing now.

Win the IPO Waiting Game: Get Ready Now

Time is on your side. But you need to use it wisely, so when the IPO market returns, you’ll be ready. As John Kunze, president and CEO of Plumtree Software, said at the CEO retreat, “If you’re going public in the next six months or a year, then you have to start acting like a public company now.” Consider doing the following:

- **Start Your IPO Preparations Early.** If you envision an IPO within the next two years, now is the time to begin putting the pieces in place.
- **Think of the IPO as a “Value Journey.”** See the IPO as a transformational process, not a mere transaction. Begin implementing the strategic, operational and financial improvement needed to perform as a public company and drive value after the IPO.
- **Get a Jump on Compliance.** Learn how Sarbanes-Oxley and other regulatory changes will impact your future transactions and find advisors who can work with you to integrate compliance into your business processes.
- **Leverage Transactions Strategically.** Begin working with your advisors on a transaction strategy and implementation plan early on.

Are you ready?

Further Reading from Ernst & Young

- *IPO Insights 2003: E&Y IPO Transformation ~ CEO Retreat*

To contact an Ernst & Young professional about initial public offerings, as well as to obtain this and other firm publications, go to www.ey.com/us/drivinggrowth. ■

VALUE ON THE HORIZON:

Biotech Investor Insights and Outlook

THE 2003 market rally by biotech companies is evidence of their strength, flexibility and resilience in responding to a dramatic slide in stock values the past three years that challenged the economic viability of the industry. Privately held biotech companies this autumn may see the first open window for initial public offerings since 2000.

How can biotech executives bridge investor impatience and market volatility as they work through tightly regulated, lengthy and expensive product development cycles?

Ernst & Young asked experts from the investment community for their perspectives. Americas biotech leaders Michael S. Hildreth, Scott Morrison and Chris Nolet conducted the interviews. The following Q&A is an abridged version of a roundtable discussion that appears in *Resilience, Ernst & Young's 2003 Americas Biotechnology Report.*

Participants are **Pierre Cantin**, a partner with *CDP Capital-Technology Ventures* in Montreal; **Samuel Colella**, cofounder of *Versant Ventures* in Menlo Park, Calif.; **Jonathan Leff**, a partner with *Warburg Pincus* in New York; **David Molowa**, a managing director at *J.P. Morgan* in New York; and **Eric Schmidt**, a managing director at *SG Cowen* in New York. The discussion was held in March 2003.

E&Y: *How do emerging companies build value?*

Schmidt: The question is extremely hard to answer, and even harder to evaluate as a potential investor or analyst. Until a company has Phase II data around a particular compound candidate, it is extremely hard to evaluate. Investors try to back good science, people, business plans and business models that likely will work. But emerging companies are difficult to evaluate.

Cantin: They have to be creative, but also need to focus on the true key element drivers. They have to get to proof of concept in humans. Some companies are doing a lot of programs at the preclinical level, sort of a big pharma approach. But what investors and big pharma want to see is, does this work in man? Do not bet the whole thing on one product, but selectively progress forward so you can have some kind of proof of concept that this compound would work in humans.

Leff: It comes back to what kind of tangible value-creation can be shown in terms of moving product candidates toward the clinic, into the clinic and through the clinic. Of course, that does not just mean any product candidate. It means quality product candidates that have an attractive opportunity for success and attractive commercial value. It is not about the technology platform itself. It is what that platform can do to create a pipeline of products with tangible progress towards the market.

"Good businesses really do matter...We have to go back to business school 101...The business of drugs is a good business model." – **Eric Schmidt**, *Managing Director, SG Cowen*

E&Y: *Is there a need for the industry to consolidate?*

Molowa: There has been a need to consolidate almost from the beginning of this industry. There has been a tremendous amount of redundancy built over time and a lack of critical mass across the board. But typically, for social reasons, nothing really has happened. Not until companies get their backs to the wall will you see something happen. We are dreaming if we think big pharma is going to come in and save the day by buying out all these broken companies.

Colella: We have no choice but to merge companies to get more critical mass. The statistics are showing there is more M&A activity, and it is more biotech-to-biotech. Some of it is pure survival. There is no question that there will be a lot more M&As in 2003, 2004 and the foreseeable future. There also will be more pharma acquisition of biotech, but it will not be rampant. It is not the nature of pharmaceutical companies to buy small biotech companies. It is more their strategy to consolidate larger entities than it is to pick up a small entity.

(Continued on back cover)

COMPLY NOW, IPO LATER:

Factoring Sarbanes-Oxley Into

BY **DAN MONTGOMERY** *Partner, Ernst & Young National Professional Practice, and* **GIL FORER,** *Venture Capital Advisory Gro*

THESE days it's nearly impossible to pick up a business publication without reading something about the Sarbanes-Oxley Act (SOA). But while much has been said about how SOA affects public companies, less discussion has focused on how it impacts privately held companies that want to become, or be acquired by, a public company. In short, SOA has far-reaching implications for private enterprises bound for public status. To facilitate a smoother, higher-value IPO or trade sale, a company's management must understand what SOA means for them now, and what changes they will have to make to meet its requirements down the road.

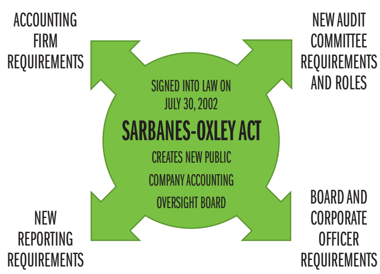
More Compliance Sooner

The time and cost of preparing to operate as a public company — and the risks of failure — are greater than ever before. Prior to SOA, companies sometimes made limited investments in back-office operations in the pre-IPO period. Why? Quite simply, other areas often were viewed as more critical, and a more productive use of capital. These companies made infrastructure investments in complex financial systems and processes, governance and finance personnel usually at the time of, or beyond, the IPO event. They often used the proceeds from their IPO to fund these investments.

Now, SOA greatly increases compliance requirements for public companies, resulting in one-time and recurring costs for the following:

- Internal and external legal counsel
- Changes in corporate governance
- Expansions in the finance and accounting reporting function
- Accelerated enhancements to processes and systems
- Changes in the independent audit scope

Sarbanes-Oxley Act

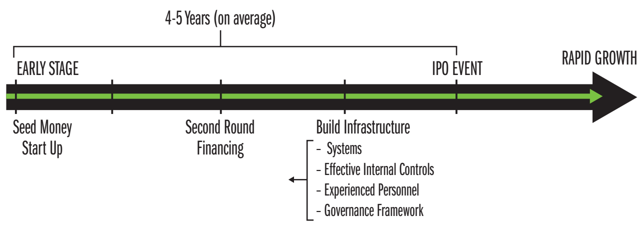


What this means is simple in theory but complex in practice. Compliance will take more time and money than before, and will come sooner in a company's life cycle. Moreover, it will take additional time and resources to meet the requirements of Section 404 and the other SOA provisions (and there can be severe penalties for non-compliance). For this reason, there will likely be a shift in the required timeframe for infrastructure investments to a period of between 18 months and three years before an IPO.

The Bottom Line: A Higher Bar

Post-SOA, executives who want to enter the IPO process face a higher bar than ever before in preparing to meet the requirements of operating as a public company — in terms of systems, processes, internal controls and cost.

Phases of Growth — Post Sarbanes-Oxley



IPO Alternatives

The expected increase in cost and risk associated with going public could dissuade some companies and investors from seeking an IPO. Instead, they may opt for strategic sales or mergers because they're less risky and expensive. Even with M&A, if the acquiring company is public, demonstrating SOA compliance would likely improve its attractiveness to potential acquirers. SOA adds a new layer of due diligence: buyers now want greater assurance that the financial reporting, controls and corporate governance of target companies will not impair their ability to comply with the provisions of the Act and other public company regulations.

Keeping Options Open

When a company backs away from one liquidity strategy to another (i.e., from going public to selling the company), or defers an IPO or other liquidity event due to the regulatory environment, management sends a signal to potential buyers: the company has limited liquidity options. This often translates into a lower valuation. Which is why, clearly, the optimal position is to keep all liquidity options open and focusing attention now on Sarbanes-Oxley compliance will only support this goal.

Your Capital Markets Equation

up Global Leader

What to Do Now: Compliance

Planning and early preparation for SOA are imperatives for companies with IPOs on the horizon. The preferred approach is to develop an SOA-compliance plan, complete with a timeline and appropriate milestones, and integrate it into your business plan. SOA compliance is not a "bolt-on" that can be bought later; and the longer one waits to implement SOA compliance measures, the more expensive they become. What's the bottom line? Executives should consider taking the following steps.

The preferred approach is to develop an SOA-compliance plan… and integrate it into your business plan.

Section 404

The management of a private venture-backed company should become Section 404-compliant at least six months before filing their IPO registration statement. This provision requires management to evaluate and report annually regarding the effectiveness of internal controls and procedures for financial reporting. The company's independent auditors must then attest to and report on management's assertion. Section 404 reporting is required at the time of filing of the first annual report with the SEC, so early compliance demonstrates to venture capitalists, underwriters and others that management recognizes the importance of internal control and the effort required to meet the Section 404 reporting requirements. In addition, early compliance gives management time to take remedial action before the planned filing date, if necessary. Management also should follow up on internal control recommendations from the internal and external auditors, and discuss the results at audit committee meetings.

Section 302

Strong internal control systems and processes will support compliance with Section 302, which requires the management of public companies to certify the accuracy and completeness of financial statements and acknowledge its responsibility for maintaining effective internal control over financial reporting as well as controls over other financial and non-financial information included in the company's periodic SEC filings. Early compliance is again beneficial because the first quarterly or annual financial statement following the IPO must include the Section 302 certification.

Board of Directors and Audit Committee

If you haven't already done so, establishing an audit committee and charter. Establishing an audit committee is an important step in making a company IPO-ready, but meeting the requirements for composition of the board of directors and the audit committee is an issue that requires time, planning, and effort. Recruiting individuals for these posts has become considerably more difficult since the enactment of SOA. The payoff is that proactive SOA compliance may make companies more attractive to potential board members worried about the risk involved with their duties.

On a different note, public companies' audit committee members must be independent and the company must disclose whether at least one member is a "financial expert." Generally, this means the person has "an understanding of and experience with accounting principles and financial statements, internal controls and procedures, and audit committee functions." Nevertheless, it's important to consult legal counsel to determine that you are meeting SOA requirements, including the provisions of Section 402 relating to the prohibition on loans to executive officers or directors.

Ready, Set, (Waiting for) Go

Today's capital markets are experiencing an adjustment period. Sarbanes-Oxley challenges private companies, increasing the infrastructure investments required for regulatory compliance and shifting the timeframe of those investments to before the IPO. But unlike companies born in the technology bubble of the late 1990s, today's IPO-bound companies have valuable time to prepare. Those that use this time to get ready by putting the appropriate corporate governance measures in place can confidently wait for the "green" light from the market.

Further Reading from Ernst & Young

- *Preparing for Internal Control Reporting — A Guide for Management's Assessment under Section 404 of the Sarbanes-Oxley Act.*
- *Managing Financial Risk: A Checklist for Board Members*

To contact an Ernst & Young professional about corporate governance, or to obtain this or other firm publications, go to www.ey.com/us/drivinggrowth. ■

SALE ON THE BRAIN:

Maximizing Value in an

BY **JIM CARTER, SCOTT GEORGE** & **MICHAEL SHEFF**, *Managing Directors, Ernst & Young Corporate Finance*

Sign says "go"?

WHEN it comes to the M&A market, the tide is going in the right direction. Following a broad rise in the stock market over the past six to twelve months, transaction activity has risen since the beginning of 2003. Private equity sponsors, currently controlling over $120 billion in equity capital, are under intense pressure to invest it or extinguish their commitments from their limited partners. As a result, they've become significantly more active and aggressive in seeking out and bidding on attractive acquisition candidates. But before stepping up to the selling block, many issues should be considered to maximize the financial and non-financial value of your transaction down the road.

Know Thyself

The first step in selling your company is to define your financial and business objectives. Are you motivated by financial return and seeking maximum value and liquidity for investors and owners? Is your goal to preserve the culture and legacy of the business you've worked hard to build? Or is it to minimize risk and position the company to thrive despite competitive or financial threats? Understanding your motivations will allow you to design a transaction strategy that will most likely help you accomplish your goals.

Timing is Everything

Determining when to sell is not as simple as timing when valuation multiples are highest. The timing of a transaction should be based on three key factors: (1) overall economic conditions; (2) the prevailing M&A environment; and (3) your unique business, operational, financial, strategic, and competitive dynamics. What are the economic and market risks you face? What investments do you need to make to maintain and improve your competitive positioning? Is your industry growing or can you only achieve growth through "market cannibalization"? Your answers to questions like these will determine when, how, and whether or not you should sell.

Choosing A Buyer: Strategic vs. Financial

It's not enough to know when you want to sell; you should also know what kind of buyer you want to attract. Buyers generally fall into one of two categories: strategic or financial. Each comes with its own pros and cons. Strategic buyers typically seek acquisitions to fill strategic voids in their business models or enhance their capabilities or technologies. Given their track records, strategic buyers are easier to evaluate in terms of their desirability as an acquirer. They'll likely understand your business model and will often bring beneficial customer relationships and distribution networks. Strategic buyers also often provide a more robust infrastructure, including financial systems, business processes, and a marketing department that you can leverage in order to expand. Negatives, however, include the possible loss of control (after the sale you'll probably be reporting to the buyer's senior management); a potential change in strategic direction that could leave your unit an orphan in the new organization; and possible redundancies among your employees as your company is integrated into the new parent.

Financial buyers (e.g., private equity sponsors), on the other hand, are most often private equity funds that make acquisitions with well-defined, time-limited goals for return on investment. Financial buyers, while playing an active and valuable advisory role, generally will retain the current management team and usually will give them an ownership stake in the company. Private equity sponsors also typically promote aggressive expansion and provide the capital to do it. These buyers, however, may not understand your business completely and may invest for the short term, typically seeking an exit from their investment, with substantial returns, within three to seven years.

What A Buyer Wants: Value

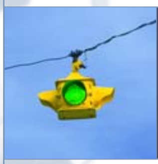
Buyers, whether strategic or financial, seek value appreciation, which usually is reflected in positive cash flow today (EBITDA) as well as strong cash flow in the future. Other key financial and non-financial value drivers for buyers include:

- Solid operational and financial management
- Substantial growth potential
- Critical mass
- Strong customer and vendor relationships

M&A Transaction

- Broad customer base (avoiding customer concentration)
- Operational efficiency
- Significant barriers to entry

That said, much of the recent market activity has come from distressed situations where the cash flow and operating income of the acquired company (or its selling owner) is weak or negative. In these cases, buyers are acquiring proprietary products or processes, customer access, geographic diversification and/or a belief that the firm can largely be "turned around" through prudent operating strategies and balance sheet management.



A successful sale transaction begins with defining what success means to you.

Positioning For Maximum Shareholder Value

Simply stated, ***shareholder value = cash flow x multiple – debt.*** Therefore, there are three primary variables to manage. First, maximizing "cash flow" is essential to maximizing value. You'll need to keep track of non-recurring and unusual charges to earnings as they can be added back to earnings and cash flow. Second, you'll want to enhance the "multiple" by improving your company's growth prospects and mitigating business and financial risks (e.g., customer concentration, succession, litigation, etc.). Third, since the true measure of shareholder value is what you keep after satisfying claims against your equity, you need to work to minimize those claims. One important longer-term initiative you can undertake is to manage your balance sheet to limit the impact of deductions from the eventual purchase price. Take the following examples:

- Optimizing working capital management relating to inventory, accounts receivable, and accounts payable
- Optimizing long-term capital management by deferring discretionary capital expenditures and purely growth-oriented capital expenditures unless it's clear that such investments will yield a higher purchase price
- Selling non-productive or excess assets
- More fully capitalizing on future business opportunities

Before you "pull the trigger" on a sale, make sure you:

- Engage an experienced professional advisor to enhance your preparedness for the sale, run a more efficient disposal process, reach qualified buyers, maintain control of the process and manage your "execution" risk.
- Position the company to support and enhance its future outlook by highlighting key value drivers, synergies, and growth potential (i.e., tell your company's "story").
- Conduct internal "self due diligence" to identify and address potential vulnerabilities and other issues that could erode value during the sale process.
- Work closely with your financial and legal advisors to design a transaction structure that optimizes the form of consideration, and limits purchase price adjustments and indemnity obligations.
- Recognize the importance of proper tax planning.
- Actively manage the timetable to completion (speed of execution often plays a crucial role).
- Maintain confidentiality so that your management team remains focused, competitors do not destabilize your customer base, and buyers do not receive the "wrong message" from an unanticipated source.
- Remember that the option not to sell provides the best leverage (i.e., don't wait until you have to sell).

Transactions in a Nutshell

A successful sale transaction begins with defining what success means to you. You can achieve a good outcome by creating and pursuing a well thought out transaction process and identifying a suitable buyer. With this in mind, you can begin to position your company according to both financial and non-financial measures to realize the best possible sale price. Nevertheless, whether you're planning a sale soon, or anticipate one later in your company's life cycle, take advantage of the time you have now to understand and implement what drives value in a sale.

— First use date September 20, 2003.

To contact our team, go to www.ey.com/us/drivinggrowth. ■

GLOBAL GROWTH SECRETS:

A Q&A with Ernst & Young's World Entrepreneur Of The Year® Award Winner

ERNST & YOUNG recently spoke with Narayana Murthy, founder and chief executive of Bangalore, India-based Infosys Technologies Ltd., who was selected as E&Y's *World Entrepreneur Of The Year (WEOY)* earlier this year.

The WEOY award program builds on Ernst & Young's 17 years of success in running the Entrepreneur Of The Year (EOY) programs, which recognize the most successful and innovative entrepreneurs around the world. Ernst & Young is conducting national EOY programs in 35 countries in the year 2003. Each Entrepreneur Of The Year program honors successful entrepreneurs every year, and in so doing, brings to the public's attention role models for the aspiring entrepreneurs of tomorrow.

Infosys provides end-to-end technology and consulting solutions to small and large corporations and employs more than 10,000 worldwide. It has zero debt, regularly posts growth of 30 percent per year, and is listed on the Nasdaq with a market capitalization in the billions.

E&Y: *What's your greatest asset as an entrepreneur?*

Murthy: I think my greatest achievement is sustaining a value system in Infosys over the last 20 years. This can be summed up as: The softest pillow is a clear conscience. My most prized possession is my conscience. I have always believed that any organization should be built on the foundation of trust. Thus, being trustworthy in all dealings is one of my core values.

E&Y: *What do you see as the most important steps an entrepreneur should take to instill lasting values in his or her organization?*

Murthy: A value system is the protocol for behavior in a company that enhances the trust, confidence, commitment, energy and enthusiasm of every stakeholder in the company — customers, employees, investors, vendor-partners, government of the land, and society. It's like the rudder of a ship that helps the company handle moments of dilemma, doubt, moral confusion and conflict. Subscribing to a value system builds up the character of the company and ensures its longevity.

Values: Walking the Talk

Compliance to a value system requires people who have high aspirations, self-esteem, confidence in the future and enthusiasm to take up difficult tasks. Hence, it's most important for leaders to walk the talk. This will go a long way in institutionalizing the values we espouse. For instance, even when we were a private company held only by the founders, we didn't use company resources for any personal benefits. Similarly, I come to the office earlier than my junior colleagues.

We also have a formal process of introducing new employees to Infosys' value system — the Infosys Leadership Institute is a detailed interactive session on our value system. In fact, Infosys was the first Indian company to institute a formalized leadership institute.

E&Y: *Ninety-eight percent of your company's revenues are generated outside India. Please describe your global vision and "blueprint" for this success.*

Murthy: Infosys' vision is to be a globally respected corporation that provides best-of-breed business solutions that leverage technology and are delivered by best-in-class people. This has to be achieved in an environment of fairness, honesty and transparency towards our customers, employees, investors, vendor-partners and the society-at-large. I want this company to be a place where people of different nationalities, races, and religious beliefs compete in an environment of intense competition, but with utmost dignity and courtesy in order to add more and more value to our customers day after day.

End-to-End Solutions

To achieve the next level of growth, Infosys has to move up the value chain and develop the capability to offer end-to-end solutions, from consulting to implementation. Towards this objective,

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Ernst &Young's *World Entrepreneur Of The Year,* **Narayana Murthy,** founder and chief executive of India-based *Infosys Technologies Ltd.*

we've introduced new services such as IT consulting, package implementation, systems integration, and business process outsourcing. We have teams working to extend the power of the global delivery model, which will move a substantial part of the project effort to cost-effective offshore locations like India to enhance our margins. We've also established the Domain Competency Group to enhance our expertise in functional areas like banking, finance and retailing.

Expanded Target Markets

Infosys has expanded its focus in the global marketplace and has identified Europe, Asia-Pacific, and Latin America as areas for further growth. In fact, we want to enhance our revenue contribution from Europe to 30 percent from the current 20 percent. The company has opened Proximity Development Centers in the United States and the UK and Global Development Centers in Canada and Australia. We have a representative office in China and are in the process of starting a new development center there.

E&Y: *Infosys went from a start-up to a billion-dollar company in 20 years. What were the keys to this phenomenal growth?*

Murthy: Progress requires an environment where aspirations are high and people are willing to make short-term sacrifice for long-term benefits. Creating such an environment requires leadership. To me, leadership is best summed up by what George Bernard Shaw once said: "Most people see things as they are and wonder why. I dream of things that never were and say why not?" In fact, one of the most important attributes of Infosys leaders is the courage to dream big, to make sacrifices, and to stand behind one's convictions.

Attracting the Best

Successful growth depends on the ability to attract the best and the brightest people from around the world. We have focused on globalizing our workforce since we believe multicultural teams are very important for our success. We operate in an environment where the only constant is change, so, we select our employees based on their learnability. And we ensure meritocracy is held sacred in the company and that high performers are recognized.

Processes, Technology and Measurement

Our business depends on people, processes and technology. I've already talked about our people focus. Regarding our focus on processes, we've adopted an integrated model implementing the Capability Maturity Model for software development; the Six-Sigma Model for support functions; and Malcolm Baldrige Framework for aligning the top-level organizational objectives with ground level processes. The company is also a leader in adopting new technologies for improving our productivity and spends a significant percentage of revenue on technology R&D every year.

There are five context- and time-invariant attributes of a successful corporation: speed, imagination, excellence in execution, an environment of openness to learn new things from others and, finally, a system that encourages meritocracy, fairness, and justice. Every Infoscion (Infosys employee) understands the power of these attributes and practices constantly to improve in these attributes through measurement. If you cannot measure, you cannot improve.

Incentive to Innovate

Every day we ask ourselves: "Are we doing things faster and more creatively and executing ideas with a higher level of excellence today than yesterday?" We want more and more innovations, so we create incentives for behaviors that produce them. We encourage our people to proactively render their own innovations obsolete by disseminating their innovations to the outside world. For instance, we have willingly shared the company's innovative practices in business processes and other financial, legal, corporate governance, and infrastructure areas with our counterparts in the software industry and beyond.

Corporate Governance and Risk Mitigation

Corporate Governance (CG) is an extremely important principle because we want to enhance the enthusiasm, confidence and energy levels of our people. I define CG as the task of maximizing shareholder value on a sustainable basis while ensuring fairness to every stakeholder — customers, employees, investors, vendor-partners, government of the land and the society. Also along these lines, we focus on risk identification and mitigation in every function. Risk parameters are monitored, a Risk Metrics Report is prepared, and the risk mitigation plans are formulated by the risk council, which is headed by the CEO.

Further Reading from Ernst & Young

- *The Ernst & Young Entrepreneur Of The Year Award: Insights From the Winner's Circle.*

To contact an Ernst & Young professional about the Entrepreneur Of The Year program, and to obtain this and other firm publications, go to www.ey.com/us/drivinggrowth.

Biotech Investor Insights and Outlook *(Continued from page 5)*

Schmidt: You can characterize M&A in one of two camps. There is good M&A, done from a position of strength. We have seen examples like that at a steady pace over the last five or 10 years, a bigger company buys a smaller company for top line growth. That will continue. There are plenty of big names looking to acquire a fast-growing top-line product company. On the other hand, in this market, the bad M&As, out of a position of weakness, are likely to accelerate slightly. There may be some critical mass to be gained by putting together two smaller, yet unsuccessful biotech companies. But it is not the type of M&A that interests investors.

***E&Y:** What lessons have we learned from the latest down cycle in the capital markets?*

Molowa: It is all about products in biotechnology. Technology platforms and information can quickly become obsolete. Or you can have intellectual property issues that make it hard to determine the value of the technology. This is the area where we have the greatest hyper-valuation. At the end of the day, this is really a product business. We know the business model there. We know what the gross margins are. We know who the customers are. We know how people get reimbursed. We know who the potential partners are for these products.

Cantin: Conduct expectation evaluations and reality checks because operational plans and clinical plans most often have delays. It is back to basics. The genomics bubble is gone so people want to see more proof of concept at different stages before they are going to pay a specific price for these companies, at the investor level and pharma level.

Schmidt: Good businesses really do matter. There was a fundamental flaw in some of the business models proposed to investors over the last two or three years. No one ever built a business in life sciences on a sale of information, and most likely, no one ever will. We have to go back to business school 101. Get back to fundamentals in terms of what makes a good business and what does not. The business of drugs is a good business model.

Colella: Sometimes we over-complicate things. We learn what we always knew: Cash is king. We learn we have to control burn rates. We have to be more conservative in our clinical developments. We know management is critical.

Further Reading from Ernst & Young

- *Resilience: America's Biotechnology Report 2003*

To contact an Ernst & Young professional about life sciences or VC investing, and to obtain this and other firm publications, go to www.ey.com/us/drivinggrowth. ■

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