PRIVATE EQUITY: AS ELEGANT AND SOPHISTICATED AS OUR CLASSIC WATCHES

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Author credit: Justin Reis, Co-CEO Watchbox.com

When the elegant style of a gorgeous Rolex or Patek Philippe luxury watch stops you in your tracks, you probably don't stop and consider the sheer size of the Swiss watch-making industry behind those beautiful pieces. And you might not think of their desirability and craftsmanship as a business opportunity.

But in the world of private equity, a luxury watch suggest dozens, maybe even hundreds of business opportunities. I should know. For 20 years, I helped run an Asian-focused private equity firm in Singapore which I co-founded. We invested over a billion dollars in capital across multiple industry verticals and now I am co-CEO of a company relying on private equity to make our entry in the world of luxury watches a success.

The story of our company, WatchBox, is an excellent introduction to understanding private equity, a term many people find a little intimidating, though it needn't be.

Without getting too technical, private equity is private investment capital organized in equity companies. Private equity companies you may have heard of include The Blackstone Group and Bain Capital. These private equity firms invest in businesses. The goal of the investment is to maximize return for the PE firm's investors, often with a time horizon of several years.

PE firms receive money from private investors, usually institutions or high net-worth individuals who are certifiably sophisticated enough to make sound judgments about investing in the PE firm's funds. Institutional investors include endowments, pension funds and commercial banks.

In the capital marketplace, PE firms are major investors, with infusions often in the billions of dollars. Businesses that receive PE investment use the money as growth capital to expand, make acquisitions, or pay for other specified activities that align with the growth business plan the PE firm has reviewed and found suitable to back.

There are all kinds of PE firms and all kinds of negotiated arrangements the firms make with the companies they fund. For example, some firms will generally rely on company management to make most business decisions and provide the PE firm with an adequate rate of return, so-called "passive investors."

Some PE firms are more aggressive and active, adding value to a company by providing expertise in the form of a CEO or CFO, strategic advisors, or revamping a company's financial management or organizational structure to maximize efficiency.

A PE firm may invest in a company with the goal of eventually buying it and reselling it. This can occur when a firm's investment is substantial enough that they own a majority of the company's shares, and so control the company's business decisions.

Another private equity approach is to provide venture capital, investing in a company the fund managers think has excellent prospects and a lot of potential, but not much of a track record yet. These could be firms that are already operating but cannot expand due to lack of capital, or promising young businesses in less mature industries, such as internet startups in the 1990's. PE firms sometimes take a substantial equity position in such companies in the hopes of triggering and helping to guide a growth phase that benefits both entities.

When most people think of financing a business, they think of a bank loan, which is far different from private equity. Small business bank loans are usually term loans with fixed rates of interest, and a bank will require not only a business plan but often your personal credit information and collateral, such as your home or other significant personal assets.

PE firms do not loan money, and there is no repayment schedule. Their investment is a shared-risk approach with the other company shareholders, though the firm may charge fees for monitoring and for other operational services they may provide. They also charge their investors an investment management fee, and if a PE firm controls the company and sells it or takes it public, the firm and its investors realize a substantial capital gain.

During my time co-leading a large private equity firm in Singapore, I often heard from sponsors that had a good business plan. Most new companies fail, so our judgment involved not only whether to invest at all, but how much equity would justify the risk. In other words, would we have enough control and influence over the company to feel we could direct its operations in the direction of growth, thereby reducing our risk to an acceptable level?

If you are a small or medium-sized company, this is part of the equation when you seek PE funding: you usually have to accept – sometimes to a considerable extent – the involvement of the PE firm in your operations. A careful business owner with ambitious expansion plans will plan for private equity infusion from the very beginning, laying the groundwork that attracts investment and enables the business to make a strong case for the preferred ownership/management role of the PE firm.

So, now that your head is spinning, let's take a real-world example of private equity in action in the form of pre-owned luxury watch company WatchBox, which I co founded and serve as co-CEO.

Swiss manufacturers produce luxury watches each year that have a total retail value of more than $50 billion, and have no trouble selling them. Seasoned aficionados and an emerging new generation of luxury watch enthusiasts across the world snap them up, driving the total value of the global luxury pre owned watch inventory to a conservatively-estimated $400 billion.

Classic, vintage pre-owned Swiss timepieces are proving irresistible to affluent buyers and collectors. With more than $5 billion changing hands annually in the luxury pre-owned watch market, there are new opportunities for those ready to part with their treasured Blancpain or Breitling.

Enter WatchBox, the first global online platform specializing in buying, selling and trading pre-owned Swiss luxury watches. Our business started when I came together with two long-time friends, Danny Govberg and Liam Wee Tay, to develop this fresh, new idea. Danny represents the third generation of Philadelphia's historic Govberg Jewelers, which had already established a profitable pre-owned luxury watch business in the US. Liam is the former owner of Sincere Watch, the leading Asian luxury watch institution, which he took public in Hong Kong and Singapore before selling in 2012.

Our business plan incorporated a host of critical variables. Here are just a few that helped guide our thinking:

- We noted the worldwide demand for luxury watches, especially pre-owned.
- We noted the immense size of the multi-billion dollar global pre-owned luxury watch inventory.
- We considered the illiquid state of this market; owners who are ready to sell lacked a convenient way to do so through a credible, trusted partner.
- We acknowledged that an even more significant number of owners could be prepared to sell if such a trusted conduit existed.
- We knew that Liam and Danny's deep connections and exceptional reputations in the world's two largest luxury watch markets –Asia and North America – gave us an organic advantage in building a ~~to~~ global platform within the watch industry vertical.

We also recognized that in the long run, tapping into this colossal market in a significant manner hinged on adequate capitalization to build inventory, perfect a unique, proprietary purchase and sales process, integrate physical locations into the mix, and staff the business with trusted, Swiss-trained watchmakers and repair experts who could credibly evaluate and price pre-owned watches, then recondition them for sale.

From a customer confidence perspective, we agreed that we must serve as a principal in each transaction - we were not interested in just creating a marketplace where random sellers and buyers came together to bicker and trade. We wanted a long-term relationship with customers and to build that, we had to credibly evaluate and purchase pre-owned watches from our sellers and also serve as the trusted principal in sales transactions, standing behind each watch, putting our reputation on the line every time.

What does all this have to do with private equity? We recognized that we would need a substantial PE investment to bring the vast potential of this market to fruition. While we knew our names and reputations in the watch, jewelry and private equity fields would open doors, we wanted to prepare our approach strategically. We decided each partner would make a deep personal investment, launch WatchBox ourselves, prove the concept, and generate irrefutable data for PE firms when the time came.

The result of that decision was very gratifying.

Our online platform struck the perfect balance of technology, data systems and 24-7 connectedness. By guaranteeing authenticity and giving customers access to personal consultation with top experts, we immediately established ourselves as credible partners and the pre owned trading platform quickly came together.

Our trading platform saw year-on-year growth of 40% in our first three years of operation. We quickly notched several critical accomplishments, registering over 130,000 users on our platform, bringing on more than 120 professional staff at our Philadelphia offices, becoming a certified service center and authorized dealer for more than 50 top brands, opening a new office and a refurbishing/reconditioning center in Hong Kong, and conducting several thousand transactions a month with an average value of $10,000.

That's proof of concept.

It was now time to seize this momentum and launch our major expansion, which meant engaging with private equity investors. We worked with an investment bank that introduced us to several high net worth and institutional investors. The capital raise was relatively smooth, as investors understood the market opportunity and with Liam Wee Tay's superb reputation for personal integrity and success in the luxury watch vertical, it was not difficult for investors to take the opportunity seriously. With Danny aboard to promote our US presence and the resources of Govberg Jewelers, we knew we were in an excellent strategic position entirely by design and execution, not by accident. We were confident our thoughtful and strategic approach, which from the beginning included an eventual private equity ask when our performance warranted it, was precisely what potential PE investors expected of us and would find satisfactory.

Singapore-headquartered CMIA Capital Partners and Managing Partner Lee Chong Min responded to our planning, execution and record of initial success with energy and enthusiasm. By November of 2017, CMIA led a significant first round investment in WatchBox, earmarking over $100 million of additional capital to be deployed in the future to build out our multi-platform strategy.

In doing so, Mr. Lee explicitly stated that our strategy of launching the business and proving our concept in preparing to seek PE funding had been right on target. When we made the investment announcement together, he said: "In WatchBox, we are backing a proven leadership team of industry veterans who offer a fresh perspective on the global luxury watch industry. WatchBox's fast-growing annualized revenue run-rate is set in the near term to exceed US$200 million."

"We believe WatchBox will transform the multi-billion-dollar luxury watch industry. CMIA Capital Partners stands ready to back WatchBox in subsequent funding rounds to further capitalize on certain M&A and business opportunities."

Our analysis of and initial success in the global pre-owned luxury watch market had another critical dividend. In seeking PE funding, we three partners maintained majority ownership of the company's shares and today we continue to control the direction of the firm.

Due to the confidence that our performance and experience have instilled in our private equity investors, they are comfortable that our ability to continue to execute our plans provides the best chance of WatchBox's continued success. Mr. Lee of CMIA and other private investors are represented on our board, providing us valuable guidance and strategic support as our plan goes forward. We are profoundly grateful for their confidence, strategic advice and financial support, and we are moving forward with alacrity, poised, I believe, to have revenues of $500 million annually in the next two to three years.

In sum, the world of private equity is a complex but not opaque one. With proper planning and execution, a business can earn the confidence of major private investors. I hope this basic primer gives you a dose of confidence so that next time you hear the term, you will have a deeper understanding and a more complete appreciation for private equity's role in the dynamic global economy.

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