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Wealth and Cash Flow Lessons from Shark Tank by Keith Wheelan

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Will Your Investment Decisions Help You Sink or Swim?Â

At the end of a busy week I look forward to winding down by watchingâ€¦five human sharks attack unsuspecting start-up entrepreneurs.Â Alright, thatâ€™s a bit overstated.Â For those of you who havenâ€ yet seen it, â€œShark Tankâ€• is a reality show where early stage entrepreneurs seek funding from five successful and very wealthy business owners.

The business ideas are varied (everything from Talbott Teas to â€œRent-a-Grandmaâ€•) and the pitches are often entertaining. But if you watch closely youâ€™ll notice a common thread in how the sharks assess the feasibility â€“ and value â€“ of a business. Â It involves the relationship between wealth and cash flow, and that same relationship applies to your personal investment decisions.

Each pitch starts with the entrepreneurâ€™s proposal to the sharks, usually a request for an amount of money (say, $100,000) in exchange for an ownership stake in the business (20%, for example).Â This in turn leads to the â€œinformation gatheringâ€• phase of the process, a 5-on-1 grilling by the sharks.

When evaluating an investment, think like a shark!Â

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but also ask the â€œsalesâ€• question (Will it generate cash flow?)

Â Whatâ€™s the first question they typically ask?Â Itâ€™s â€œHow much have you done in sales?â€•Â reason for this.Â As experienced serial entrepreneurs, the sharks know that sales volume is an indicator of whether the business concept is viable (are enough people buying the product?)Â But it also determines how quickly they can recoup their investment. Â Higher annual sales means faster payback â€“ followed by steady positive cash flow.Â So the cash flow question comes first because itâ€™s the sharkâ€™s most important consideration.

Separate but related to the first question is: What is the value of the business?Â The answer to this is also important, but for a different reason.Â A pitch from a recent episode illustrates the point.

Â Sink under the weight of the asset or swim in the income stream?

The owner of a clothing business requested $500,000 Â from the sharks in exchange for a 15% ownership stake. What was unique about the clothing was its â€œtechnology enabledâ€• pockets for cell phones, iPods and other electronic devices.Â The garment design was protected by a patent.

Annual sales?Â $5 million this year and an anticipated $12 million next year.Â Â That got the sharksâ€™ full and undivided attention.Â That is, until the owner clarified that his offer was only for the asset value associated with the patent and not for the retail sales of the clothing.

After recovering from the blow, the sharks countered with offers that included part-ownership of what they called â€œthe real businessâ€• â€“ the retail sales.Â They wanted a piece of the cash flow, not the asset.Â But the owner wouldnâ€™t budge. So he walked away empty handed.Â Game over.

The lesson? Â When evaluating an investment, think like a shark!Â Yes, ask the â€œwealthâ€• question (the asset grow in value?) but also ask the â€œsalesâ€• question (Will it generate cash flow?)

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