FINANCE & ACCOUNTING VIEW

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# CLIENT SUCCESS

## THE BUMPY RIDE OF A SUCCESSFUL HIGH-TECH STARTUP, PART I

Kodeos Communications, Inc. was launched in 2001, just as the telecom bubble was about to burst. Many of the high-tech ventures launched around that time are long gone, relegated to footnote status in the tale of the great high-tech/Internet bubble of the late 1990s.

Kodeos not only survived, it has just been purchased by Finisar, an industry leader in the infrastructure that enables high-speed data communications for networking and storage applications. Finisar paid about $7 million in cash for the equity interests in Kodeos, with possible future payments of up to $3.5 million to the company's equity holders and employees contingent on the achievement of certain milestones.

Recently, John Wyatt, who had joined Kodeos in November 2002 as CEO, sat down with Geller & Company's *Finance & Accounting View* to talk about Kodeos' six-year journey from startup to cash-out. It's a tale best told in his own words.

**F&A:** Was acquisition by a larger company such as Finisar the ultimate goal when Kodeos was started?

**Wyatt:** By way of background, Kodeos was started in 2001, at a time when the telecom bubble was reaching its end. No doubt, the initial expectations for the company included multiple exit possibilities, such as an IPO or merger/acquisition. However, with the market turning down during the 2001-2005 timeframe, small companies such as Kodeos had to scramble just to survive. Many of them failed; hence, there have been many casualties and even fatalities along the Information Highway.

During 2005 and 2006, the optical networking market (the business Kodeos is in) began to stabilize, and systems makers again started looking to technology for next-generation applications. Around midway through last year, Kodeos management and investors felt the timing was right to pursue an exit strategy based on acquisition, given the current environment. We started an active campaign to meet with the industry leaders who were marketing optical modules to the telecom sector.

Further, there had been a shuffling of the industry leaders. Companies such as Finisar, which had moved solidly into the top tier of suppliers, wanted to strengthen their leadership by selective technology acquisitions. Kodeos' extended-reach technologies, both Optical DuoBinary and MLSE electronic dispersion compensation, fit the parameters for which they were looking. Thus, we executed an exit strategy based on acquisition by a larger industry leader in our market space.

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**F&A:** You made some acquisitions over the past few years at Kodeos. What were the biggest differences between being an acquirer and being an acquisition target?

**Wyatt:** First, consider the common thread whether buying or selling, which is technology. You have to consider how strategic and synergistic the combination of the two companies' portfolios is likely to be. This, of course, is part of the initial and ongoing due diligence.

The differences are like most buy/sell roles. If you are acquiring, as we did with Intersymbol in March 2006, then you want to make sure the acquisition target is a good fit with your strategic plans. Kodeos is a small company, so I had to make sure that any acquisition we made would be financially affordable – i.e., I had to consider what it would do to my burn rate and my funding runway.

The Intersymbol acquisition by Kodeos was strategic, since it positioned us as the only company with both technologies for extended-reach solutions (ODB transmit-side processing and MLSE receive-side processing). This strengthened our competitive position but, at the same time, made us more attractive to possible acquirers.

On the other hand, if I am the acquisition target, my considerations will vary according to who is the buyer. For example, I have to consider whether the buyer is a competitor who just wants to take our technology off the market or someone who wants to augment a new market capability with our technology.

The latter situation is much more attractive to me as the CEO, because I know the acquirer will likely want both the technology and the team as part of the deal. Also, I feel the deal will likely be more financially attractive, because the acquiring company will see the acquisition as adding to future revenue possibilities, adding customer base and new market segments.

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*In Part II of this article in the next issue of Geller & Company's* Finance & Accounting View*, Wyatt discusses the things that made Kodeos attractive to Finisar, his reaction to the outcome of the deal, the role financing played in Kodeos' success and resources on which he relied for help during the transaction. He also offers some advice to owners of early-stage high-tech companies with an eye toward ultimately selling their firms and talks about his own plans for the future.*