

# Business finance options

## What is financing?

Most businesses at one time or another are faced with the need to seek finance for either the purchase or start of a business or continued operation or expansion.

Naturally a small business will grow if it is successful and extra funds may be required for expanding its turnover and purchasing equipment etc. Most people in business know about the availability of funds by way of bank overdraft facilities but many are unaware of the alternative sources of finance for business purposes.

## Be clear on your financing

The borrower should be clear on and understand the functions of the different type of finance if he or she is to obtain the best benefit from the facilities available on the market. Obtaining finance is essentially a matter of convincing a lender that you have a commercially viable proposition for which you seek the lender's willing investment.

Even after finance has been obtained, there will be a need to monitor and control the business to ensure that the business continues to remain viable and to prosper. Sound business planning is an essential part of this process and lenders will be quick to point out that there is a very high rate of failure for most businesses that do not adequately plan.

## Why seek finance?

There are many reasons why small businesses seek finance. The two main categories of business that seek finance are:

1. Existing businesses that have a trading history and simply require additional finance for expansion and growth.
2. New businesses that are being formed for a variety of purposes - these are either purchased or started up from "scratch".

## Typical methods of finance

To summarise, there are typically eight methods in which a business can be financed, whether for purchase or for growth.

1. Business owner and family and friends.
2. The seller of the business will generally leave in some vendor finance.
3. Banks and other lending institutions.
4. Suppliers to the business.
5. Customers of the business.
6. Venture capital companies and individuals.
7. Government agencies and other organisations that invest in profitable businesses.
8. Going public in the way of inviting investment through shares.



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## Summary of funding groups

Funding can be split into four distinct groups:

1. By borrowing money and therefore increasing its liabilities.
2. By pouring profits back into the business rather than using them.
3. By the sale of assets or reduction of investment in other assets, such as stock and debtors.
4. By the contribution of additional funds in the way of capital.

Or, to summarise again into three classifications:

1. Self-funded - the money is raised by the buyer totally.
2. Debt funded - the money is borrowed.
3. Equity funded - finance is raised by other parties coming in to the business and bringing capital for the purchase of a part share.

## Lending criteria

Most small businesses strike problems when trying to obtain loan finance. This is because they are usually under capitalised, their owners have limited assets for security or they do not possess the experience to present a good case for loan money. The business owner, when seeking loan finance, must be familiar with what the lender will be looking for. The lender will want to be satisfied on these points:

- The purpose of the loan is within their lending criteria.
- The owner has the necessary ability and experience to operate the business in a profitable manner.
- Proposals for the use of the funds are realistic and can be achieved.
- Adequate security for the loan is available to ensure that should financial difficulties arise the money can be recovered.
- The borrower is able to meet the full loan repayments as well as interest and other charges.

## Further information

The following fact sheet provides further information on these issues:

- Business planning