

Raising Finance

The financial or capital structure of your business is one of the key areas that will influence the outcome of your efforts. That is, whether or not you will be as profitable as you can be.

The three primary sources of capital available to businesses are:

- Shareholders' Equity - that is, your money and that of other investors
- Borrowed Funds
- Reserves - that is, profits put back into the business

Here we discuss raising capital via borrowings.

Once you have decided to raise capital by borrowing money you need to consider what term of finance will suit your needs. It is important that you match the term of the loan to the purpose for which the finance is being used.

Types of Finance

Business finance can be categorised as short-term, medium-term and long-term.

Short-Term Finance

This form of finance is commonly called "working capital" and is the capital (money) required to fund the day-to-day running of the business. Working capital should not be used for long-term projects as it is generally more expensive (in terms of interest rate charges) than money paid back over a longer period.

Short-term finance, or working capital, typically comes in the following forms:

Bank Overdraft - can be used to cover financing shortfalls from day-to-day according to your cash flow. The interest will be calculated on your daily outstanding balance and is usually charged on a quarterly basis. Depending on your financier, an overdraft facility may also incur other sundry fees.

Commercial Bill - is an arrangement where money is made available for a short period. At the end of the period an unconditional order is made on you to repay the borrowed amount. Commercial Bills can be drawn for terms ranging from 30 days up to a maximum of 180

days. They are commonly used to meet the seasonal funding needs of a business.

Debtor Finance (commonly known as Factoring) - is an arrangement where a finance company provides a cash advance to the business against sales made (invoices). The "loan" is repaid when the debtor pays the invoice.

Medium-Term Finance

This is finance usually required for a three to 10 year period and is principally used by businesses to finance equipment, business expansion and development of new products.

Medium-term finance may come in the following forms:

Term Loans - is a loan paid back over an agreed period (term) where principal and interest rate are paid off in monthly repayments. This type of facility is commonly used by businesses wishing to structure their loan repayments to correspond with the income produced from equipment purchased or sales of new products. It may be for a five or 10 year period.

Personal Loans - Where it is not possible to arrange a loan in your business' name you could consider as an alternative arranging a personal loan. This can then be contributed as equity or a loan to the business.

Leasing - With this type of facility the financier would purchase the equipment you require and then lease it to you in return for regular rental payments (usually monthly) for the duration of the lease period. At the completion of the lease term you are then offered the option of purchasing the equipment at an agreed residual value.

Long-Term Finance

This type of finance is used to fund the purchase of assets such as the business itself, land, buildings, plant or machinery which will directly or indirectly contribute to profit over a

period of years. Term Loans would be the most common way to structure long-term borrowings.

Applying for a Loan

You will need to supply information on:

The Business - If you are buying an existing business, or you are already in business, a short description of your business - its history, past achievements, products and services - should be provided. Also include the number of staff involved, the location and a description of the premises, machinery, equipment, vehicles and other key assets.

If you are starting up a new business, describe the products and services you intend to provide, how you intend to bring in business by marketing and what evidence you have of demand for your products/services.

Your History - You should provide details of your own educational and business qualifications, business experience (whether it relates to your present business or not) and past achievements.

Amount and Purpose - The amount and details of the purpose for which the loan would be utilised should be stated clearly in your proposal.

Repayment - It will be important from the lender's point of view to be able to clearly establish how the loan repayments will be made.

Financial Statements - Projections of sales, cash flow, profits, etc over the term of the loan

should be provided and, for an existing business seeking funds, the last three years' annual accounts. You should also include a monthly cash flow budget for the 12 months ahead with the loan repayments included.

Owners/managers of existing businesses may also benefit from using the [Interactive Financial Analysis Tool](#). The tool will assist in calculating a number of key economic ratios from information extracted from your financial accounts.

Security

It is likely the lender will seek some form of security from you to protect the loan. Security requirements will vary between lenders and the type of loan sought. Some generally acceptable forms of security are:

- real estate;
- shares in public companies;
- surrender value of an insurance policy;
- personal guarantee;
- bill of sale or debenture over assets other than real estate.

Useful Contacts

Please visit our links section on our website for a list of useful contacts.

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