Business Basics: Finding the right finance for your business

The simple and easy way to apply to multiple lenders

fsb | Funding Platform

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Finding the right finance for your business

Your business is your passion, which is why it can be easy to lose focus on finances and other administrative chores, or not feel confident to discuss finance. Funding is important to every business' growth.

From knowing when you're ready to take out finance and preparing your business, all the way through to looking at funding options and applying, we've simplified the process.

In this guide, our finance experts from FSB Funding Platform will walk you through five key steps in the funding journey, so that you can be confident, prepared and get back to doing what you enjoy the most – running your business.

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Step 1: When is the right time to take on finance for a business?

Being your own boss and running a successful business is a huge achievement - but how do you keep growing without damaging your hard work? How can you expand without taking on too much debt and leaving yourself exposed if everything doesn't go to plan?

When it comes to business funding, there is a lot of misinformation trying to encourage borrowing when you might not be ready to grow your business. Stability needs to come first.

Here are some of the key things you need to consider before taking on finance.

1. What's the opportunity?

Be realistic about the opportunities you're chasing and whether they would be a good fit for your business. Make sure your business goals are underpinned by solid projections and a reliable sales pipeline. You should never take growth finance and just hope for the best.

Typical use cases where external funding can be put to good use are:

- Start-up funding
- Launching a new product or service
- Investing in revenue growth
- Expanding into new markets/internationally
- Investing in new equipment
- Reducing cost of existing borrowing
- Acquiring another business

2. How realistic is your growth plan?

A plan is key. Avoid taking growth funds, absorbing them into the business and then not following a defined growth plan. Work up a schedule that shows when and where the funds will be invested and the impact on your business' cash flow. Keep updating your plans in light of new opportunities, how viable they are, and what business challenges you come up against.

3. What's the worst-case scenario?

Run the numbers and make sure you understand what happens if your anticipated growth doesn't materialise. Be clear about the ups and downs of your target market and how this would impact different scenarios. Prepare a detailed forecast and track your KPIs so that you can spot challenges before they happen.

Idea stage

- Your business doesn't have a product or a service, and has no customers
- Debt finance: Start-up programs, accelerators, etc
- Equity finance: Limited options

Pre-profit

- Your business has a product or a service, but not enough customers or revenue to cover all the costs of running the business
- Debt finance: Start-up programs, accelerators, etc
- Equity finance: Some options

Profitable

- Your business has a product or a service, and enough customers and revenue to cover all the costs of running the business. Depending on seasonality, the business may have trouble being profitable all year round
- Debt finance: Various options
- Equity finance: Various options

Established

- Your business has a product or a service, and enough customers and revenue to easily cover all the costs of running the business at any time of year, irrespective of seasonal trading patterns
- Debt finance: Most options
- Equity finance: Most options

Growing

- Your business has a product or a service and wants to grow its customer base/ revenue through additional investment. This may mean that the business needs to incur more costs than it can normally afford, meaning that short-term the profitability may not be possible but this is offset through future growth
- Debt finance: Various options
- Equity finance: Various options

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Step 2: Is my business eligible for funding?

Let's take a look at how you can best prepare your business for new investments and funding.

1. Cash is king

Before looking for external capital, you should make sure you're managing cash effectively. Being able to demonstrate good cash management sends out the right signals to potential investors or lenders.

A weekly cash-flow forecast is often essential, particularly in a growing business. Make sure you understand the amount of cash and working capital required to operate the business.

- [ ] Review stock and work-in-progress levels
- [ ] Issues sales invoices in a timely manner
- [ ] Review contractual agreements with suppliers
- [ ] Assess capital expenditure
- [ ] Use automated payment method

2. Business planning

Preparing a solid business plan is the key to securing funding. A robust business plan helps potential lenders or investors understand your vision and goals for your business. It also helps you to understand the risks of your strategy and the impact of any deviations from the plan.

Every business plan is different, but here are some key elements to think about:

- [ ] Executive summary
- [ ] Who are the key personnel? What are they responsible for?
- [ ] Market analysis
- [ ] Current and intended client base

- [ ] Marketing plan
- [ ] Historical financial information and accounts
- [ ] Cash flow data and financial forecasts
- [ ] How creditors, capital expenditure, debtors and stock will be managed
- [ ] Additional 'flexed' forecasts showing the impact of key downside scenarios, such as sales targets not being met or cost savings taking longer to come on stream
- [ ] How equity investors can exit or refinance the business, and realise their investment

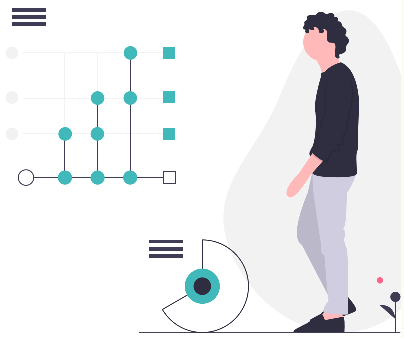
3. Does my business need investment?

Running your own business isn't easy. How do you know when you need to start making investment for growth?

☐ Missed sales targets

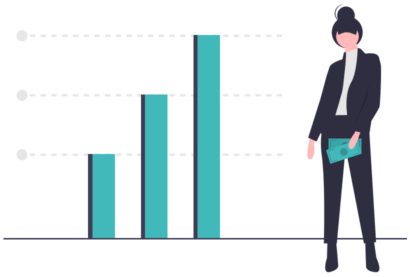
Are you so busy with admin tasks and day-to-day duties that you can't find time for the most important job of all: chasing down sales?

A little bit of this is normal, but it will mean you've got fluctuating sales income and a hard-to-predict future. Hire some staff or bring in new sales processes so things don't get out of hand.



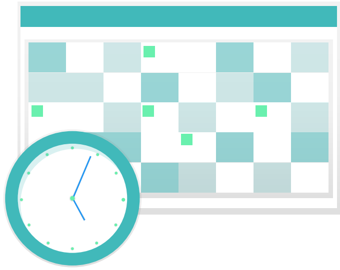
☐ Low return on investment marketing

If your marketing spend doesn't seem to be translating to sales, it may be time to make a change. This is especially true if you're trying to do everything yourself. That time could be used better if you invested in proper digital marketing support.



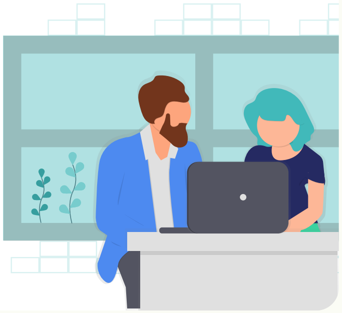
☐ ### You're delaying things

You can't do it all. It's time to recognise what you're really good at and start building a team around you to deal with the other stuff. Trying to take on too much responsibility generally leads to things not being done.



☐ ### Running out of space

Work environment starting to feel cramped? This can have a negative influence on everything that happens there – including the quality of work, team morale and practical concerns such as storage. Knowing when it's time to size-up is important.

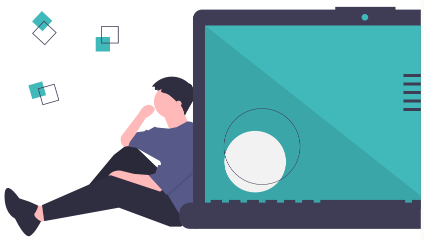


☐ ### Not enough employees

If you need to start turning down work or are not meeting your normal levels of service, think about expanding the team with more staff. Just make sure you have enough work coming in to justify their contracts.

☐ ### Falling behind

Outdated tech? Unreliable tools? Time-consuming manual processes? You might find that you need to invest in new systems to keep up with the competition.



Spotting the need for investment will help alleviate short term pressures and can be the catalyst for driving your business on to better things.

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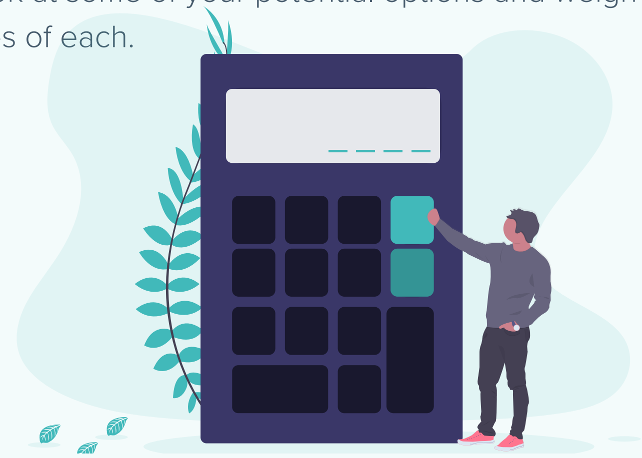
3 Step 3: What is the right type of finance for my business?

Once you know the time is right and you've done all your preparation, it's time to start looking at your finance options, and matching them to your needs.

Getting a business loan can sound simple – but making sense of finance options can be overwhelming, especially if you don't know what would be the best fit for your business.

By now you should have a good idea of how you'll use the finance within your business. Let's look at some of your potential options and weigh up the advantages and disadvantages of each.



I want to enter new markets and expand my operations

Also referred to as growth finance, this is a type of funding that works well if you're looking to expand your business and enter new markets. Whether you're developing new products, buying new equipment or embarking on new sales initiatives, growth finance can help you generate more revenue and profit.

There are a wide variety of funding products available for businesses from challenger banks, alternative finance providers and high street banks. Credit can be obtained on a secured basis against business assets, or on an unsecured basis, where your credit score and ability to offer a personal guarantee will be more important.

Advantages

- Gives your business the flexibility to take advantage of new opportunities.
- Invest in new products or services.
- Meet short term funding gaps, for example customers with long payment terms.

What should I watch out for?

- For a standard term loan, you agree a repayment period with the lender upfront. This helps you forecast accurately, but if you want to settle early you may need to pay an early repayment fee.
- Speaking of forecasting, watch out for variable interest rates – especially if you're intending to borrow over a longer term.
- What is the security arrangement on the loan? Providing a personal guarantee against assets such as your home is very common, but can be limited to avoid problems down the line. One option is to take out PG insurance.

I want to invest in new or used equipment

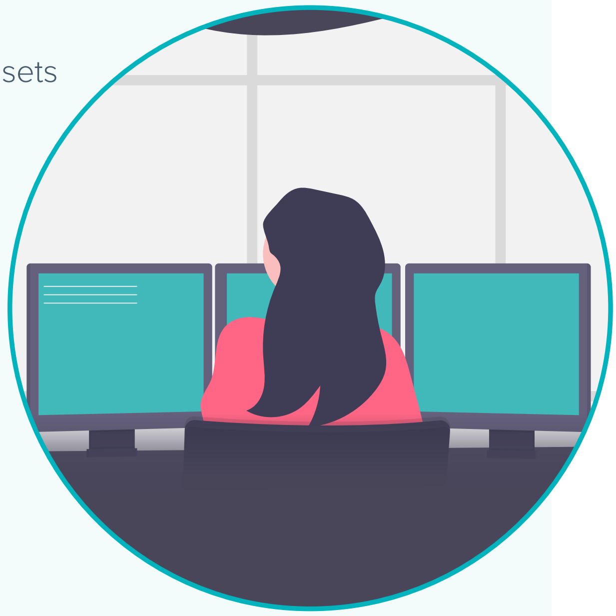
Asset finance helps your business to access the assets you need, like machinery, computers, office equipment or vehicles, with an agreed monthly repayment over a period of time, typically one to three years. Once you've paid off the loan, you then own the asset.

Advantages

- Great option for businesses that might find it had to arrange unsecured finance, such as a traditional bank loan or overdraft.
- Secure assets that may otherwise be out of your budget, by spreading the costs as part of a hire purchase agreement.
- The lender carries the risk, so you have less to worry about (though you should always check the small print or ask our experts if you're unsure).
- Often quicker compared to other finance options as there are fewer checks and balances.

Disadvantages

- You can't claim capital allowances on leased assets if the lease period is less than five years.
- With longer terms, it could be more expensive than buying the asset outright, so it's worth running the numbers to see if you might have the cash to purchase upfront.



I want to buy a business premises or make residential/ commercial investments

It's rare for businesses to be able to buy a property outright, as this requires a large upfront investment. **Property finance**, such as a commercial mortgage, can help you to buy your own premises.

Advantages

- Extra income if you let or sublet the property, to support mortgage repayments.
- More control over costs compared to a rental agreement.
- Tax deductible – interest payments on a commercial mortgage are offset against corporation tax.
- Security – the landlord won't sell the property or move you out at the end of your lease.
- Freedom to carry out renovations and improvements without needing a landlord's permission.

Disadvantages

- Upfront costs – deposit, legal and survey fees require lots of capital.
- Lost capital – could have been used elsewhere in the business.
- Risk of repossession if you don't keep up with repayments.
- Responsible for maintenance costs and health and safety compliance.
- Harder to relocate if you need to move the business.

Fees to watch out for:

Arrangement fees – as well as the headline rate, ask about arrangement fees. These normally come in at 0.75% to 2.5% of the overall value. This could also include a commitment fee on acceptance of the mortgage offer.

Valuation fee – some lenders may charge this so they can conduct their own assessment of the property before making an offer, so be sure to ask if this applies.

Legal fees – commercial mortgages are often more complex than residential, so the legal fees tend to be higher. In addition to your own fees, there may be some costs you need to cover for the lender. Find out how this works upfront to get a clear picture of total costs.

What other options are there?

A short-term loan: Bridging or development finance is a short-term option if you expect to clear the loan within 12 months. It also gives you more flexibility as a result.

Funding for an auction property: Auction finance can be used to secure quick funding for a property being auctioned.

Less capital investment: Mezzanine finance is a hybrid of debt and equity finance often used to top-up another loan. It's a good option if you want to keep control but lower your own capital investment.

Opening another branch: If you already own one property and are looking to expand your business, portfolio finance could be an alternative property finance, where borrowing is secured against more than one property.

I want to improve cash flow and smooth out seasonal trading

Invoice finance is a way of borrowing money against unpaid invoices for a fee. You typically receive up to 85% of the value of an invoice immediately, which can help to ease cash flow worries. The funder will collect the money owed from your invoices, and pay you the balance, less any fees.

Flexibility: Selective invoice finance (SIF)

This finance option lets you pick and choose which invoice you want to fund. There's typically no contract tie-in, making it a flexible option if your business has a one-off requirement, or if you don't want or need to fund your full sales ledger. It's also a cost-effective option as fees are only applied to the invoices you choose to fund.

Confidentiality: Invoice discounting

The funder is advancing cash for your unpaid invoices, but the debt collection is conducted by your business. Generally, the lender advances between 70 – 85% of the invoice value, and will release the remaining amount minus a small fee upon payment from your client. Recourse – required to pay back any amount advanced on invoices if the client defaults on the payment. With invoice discounting, you keep your credit control in house.

More working capital: Invoice factoring

Package of services including credit control that requires you to sell the whole of your debtor book for a pre-defined time period. Unlike invoice discounting, lenders might advance as much as 95% of the invoice value, but this does result in being tied into a contract.

Less risk: Non-recourse invoice discounting or factoring

Passes the risk of your clients to default on payment to the lender.

Advantages

- Boost your cash flow without waiting for invoices to be paid.
- Greater flexibility with working capital, allowing you to reinvest and grow your business.
- Faster turnaround for setting up the facility, compared to other finding options.
- Some facilities offer credit insurance or bad debt protection.

Disadvantages

- Potentially tied into a 12-24-month contract.
- Invoice factoring is not confidential as the lender will do the debtor chasing on your behalf.
- With invoice factoring, you may be required to refund the cash advance if they are unable to collect money from your client.
- The Annual Percentage Rate (APR) can be as high as 48%, meaning it should be considered as a short-term option.
- Invoice finance is great for cash flow because you get a high percentage of the invoice value as soon as you raise the invoice. But most providers take a percentage of the invoice as a service charge. Make sure that cut won’t damage your margins.

I import and export goods, and want to increase my working capital

Trade finance is an important external source of working capital finance. It’s a form of short-term credit typically used by companies that export or import goods. It’s relatively easy to secure short term finance if you have a string trading record, secured against good or backed by an insurance policy.

It removes the payment risk and supply risk – exporter gets good sooner, and the importer benefits from extended credit.

Advantages

- Easy way to arrange short term finance.
- Your business can focus on growth activities.
- Finance is typically secured against the goods, or backed by an insurance policy.

Disadvantages

- Based on having a good track record in terms of operations and repayments, so is less accessible for new companies.
- If payments are not made on time, it can become very expensive.

I want to grow my business with more freedom and security

Pension finance is a type of alternative finance. It sounds complicated, but it works like a business loan - money is borrowed from your personal pension(s) and paid back with interest by the business. You can raise funds based on the pensions accrued by one or more owners or directors.

Advantages

- Interest paid back increases the pension pot, meaning you can grow your business and your retirement fund at the same time.
- HMRC compliant scheme.
- Personal guarantees and charges over property may not be required.

Disadvantages

- Pensions are a long-term savings scheme to provide for retirement, so this type of financing comes with risk, as your pension pot isn't guaranteed to grow.
- The amount you can borrow is limited by your pension size.
- Set up time can be several weeks.

I am seeking investors that can help me build my business

Equity funding isn't right for every business, it means selling parts of your business through shares. One way this is talked about, is as selling an 'equity stake'. Unlike other forms of finance, finding a suitable investor is not trivial. And since you are giving up a degree of control, you are not just sourcing funding, but essentially to go into business with your investor. Therefore, you need to consider several issues before selling a stake in your business in exchange for capital.

Advantages

- Fund your business growth, potentially without making loan repayments.
- Access business expertise from your investor(s).
- Access additional resources such as legal, tax and human resources.
- Utilise your investor's network of connections.
- When crowdfunding, you may gain investors as well as customers.

Disadvantages

- If an investor or group of investors has a large stake in your business, this will lead to you having less control of your business, as investors will want to have an influence on important company decisions.
- May result in minority ownership status of your business, depending on the size of your investor's stake in the business.
- Investors increasingly want to see a return on their cash during the life of their investment, giving rise to venture loans or other fees.
- A significant amount of time is required to prepare for the fundraising, networking, negotiation and ultimately, securing funding.
- Selling shares in your business requires legal agreements, creating additional costs for you, thus reducing the amount you have available to put to work in your business.

What is the difference between debt and equity?

There are two main ways of funding your business – **debt** (through a loan) or **equity** (where investment is made in exchange for a stake in your business).

Debt	Equity
Start-up loan	Seed finance
Overdraft	Angel finance
Bank loan/bond	Equity crowdfunding
Peer-to-peer lending	Venture capital
Asset-based finance	Corporate venture capital
Leasing or hire purchase	Private equity
Export or trade finance	IPO/public offering
Growth finance	

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4 Step 4: Loan agreements and monitoring

Getting a business loan sounds simple to start with – but as you explore your finance options in detail, you may feel it becomes overwhelming. But don't despair, if you don't know what would be the best fit for your business, there is help available.

Whether you're looking to grow your business, make investments or support your cash flow, our finance experts at FSB Funding Platform are here to help you get started.

Like other business decisions it's all in the prep. Have a clear picture of where your business is at now, and put your estimate together, as to what impact you expect the external funding to have. With this knowledge in hand, getting a business to a position where it can take on additional capital need not be too daunting a task.

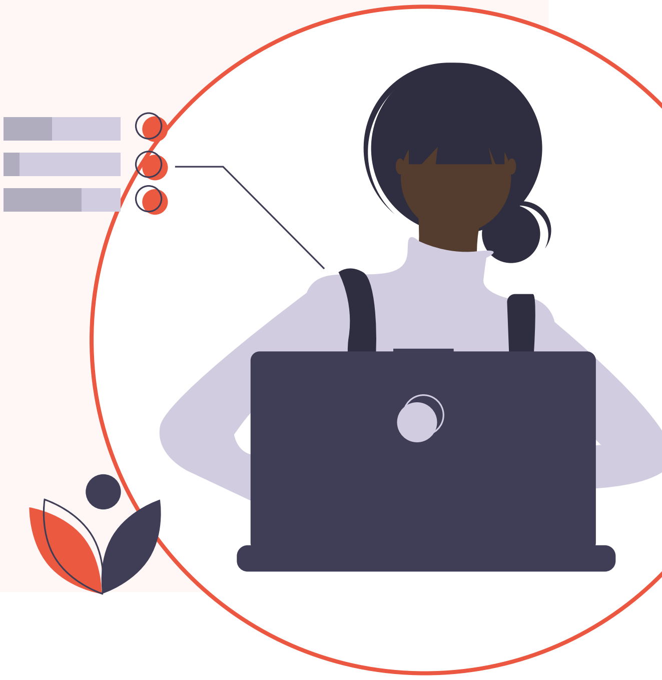
Equally, your current finance arrangements may feel like they are not working as well as they should. Hence it is important to keep on monitoring your arrangements, and the progress you are making against your business objectives.

In either scenario, start by looking at the business afresh, with a questioning mind, so that you have relevant documents and have prepared answers to the typical questions a lender will raise.

What should I do?

Don't rush into taking out a loan. Some providers might try to encourage you to take that step before you're ready. There's a lot of choice and a lot of competition out there, so make sure you're being advised fairly and honestly – especially when it comes to fees.

FSB members can call one of our finance experts 24/7 for impartial advice and guidance on 0330 097 2359



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Step 5: How do I apply for finance?

Whether you're looking to grow your business, make investments or support your cash flow, our finance experts at FSB Funding Platform are here to help you get started.

Funding platforms have already started setting the foundations for effective matchmaking systems, linking those seeking to invest with those wanting to borrow.

Find the right finance with one easy application

Finding the right finance to suit your business can be complex and time consuming as a small business owner – FSB Funding Platform is here to make it easier.

As an FSB member, you can save time and effort with one easy application, and let our experts handle the rest. We take the hassle out of searching through hundreds of finance options, and our finance experts are just a phone call away with honest and impartial advice.

Get in touch

Visit FSB Funding Platform to apply for finance today,
or call us 24/7 on **0330 097 2359**.

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