



Boots to Business Module 6

Financing Your Venture



ASSOCIATION OF
WOMEN'S BUSINESS CENTERS



MISSISSIPPI STATE
UNIVERSITY

The Boots to Business entrepreneurship training program is provided through the coordinated efforts of the SBA and its valued partner network. All SBA services are extended to the public on a nondiscriminatory basis. Reasonable arrangements for persons with disabilities will be made if requested at least two weeks in advance.

Objectives

- Understand what types of financing are available for your business
- Understand the difference between debt & equity financing
- Explore what lenders and investors look for when deciding whether to finance your small business

The Money Game

Where Do Entrepreneurs Get Their Money?



Featuring Paul Kedrosky
Senior Fellow, Kauffman Foundation

Why Startups Need Funding

CASH FLOW CHALLENGES

Inventory must be purchased, employees must be trained and paid, and advertising must be paid for before cash is generated from sales

CAPITAL INVESTMENTS

The cost of buying real estate, building facilities and purchasing equipment typically exceeds a firm's ability to provide funds for these needs on its own

LENGTHY PRODUCT DEVELOPMENT CYCLES

Some products are under development for years before they generate earnings. The up-front costs often exceed a firm's ability to fund these activities on its own

Preparing to Raise Debt or Equity Capital

STEP 1

Determine precisely how much money is needed and write a viable business plan to support it



STEP 2

Determine the type of financing or funding that is the most appropriate



STEP 3

Develop a strategy for engaging potential investors or bankers

Questions to Ask Yourself

- **How much money do I need?**
 - Based on projections / not just an estimate
- **What will I use the money for?**
 - Equipment, inventory, working capital, marketing, real estate, etc.
- **What type of funding do I need?**
 - Debt and/or Equity Investment

More Questions to Ask Yourself

- **What funds do I have to invest in the business?**
 - **How will I pay back the loan?**
 - Requires Financial Projections/Cash Flow Analysis
 - **What's my credit score? ***
 - **How do I find a lender?**
 - Does your existing bank offer small business financing
 - Local SBA team can assist in locating potential lenders
- * US Federal Trade Commission (FTC) offers FREE annual credit reports
at <https://www.AnnualCreditReport.com>**

Sources of Financing

- Personal Funds
- Commercial Loans
- SBA Guaranteed Loans
- Microloans
- USDA Guaranteed Loans
- Crowd Sourcing
- Peer-to-Peer Lending
- Angel Investors
- Venture Capital (VC)

Personal Funds

You need “skin in the game” before you seek external funding!

Sources of personal funding

- Cash/Savings
- Credit cards
- Valuables, collections
- Home equity loan / line of credit
- Equities and stock portfolio
- Retirement accounts
- Friends and family – get it in writing

Bootstrapping

Finding ways to avoid the need for external financing or funding through creativity, ingenuity, thriftiness, cost-cutting or any means necessary.

Making do with
what you have

Buying used instead of
new equipment

Sharing office space
with other businesses

Leasing equipment
instead of buying

Obtaining payments in
advance from customers

Vendor financing

Coordinating purchases
with other businesses

Crowd funding

The most common source of start-up funding.

Debt/Loan

vs.

Equity

- Loan from a bank, credit union or other lender
- Allows you to maintain ownership and control
- Requires repayment with interest
- Liability ends when the loan is repaid
- Generally considered the cheapest way to grow

- Involves investors
- Money is exchanged for partial ownership
- Is not paid back
- Means you have shareholders
- Can have huge benefits beyond the money

Debt Financing

Provides liquidity, not investment

- Banks are risk averse

Requires “The Five Cs”

- Your **Credit** and/or the Company’s current and past performance
- Your **Collateral** and/or the Company’s assets
- The **Cash Flow** from operations, projected and/or actual
- Your **Commitment**
- Your **Character**

What Lenders Typically Look For

- Business plan with detailed personal & business info
Including financial projections (1 – 3 years)
- Borrower's collateral and/or company assets
- Cash injection (20 – 25% is typical)
- Good credit score
- Borrower's personal tax returns

Main Reasons Why Business Loans Are Not Approved

- Poor credit history for borrower(s)
- Not enough collateral
- Too much previous debt
- Cash flow from operations not strong enough
- Not enough time in business
- Industry perceived as “risky”
- Incomplete application / paperwork

SBA Loan Programs



Lending partner



Loan



Small business
(You)

- **The SBA does not lend money directly to small business owners**
- SBA works with lenders to provide loans to small businesses
- SBA lenders still consider the Five Cs of Credit
- The SBA reduces risk for lenders and makes it easier for them to access capital
 - This makes it easier for small businesses to get loans

SBA Loan Programs

From \$500 - \$5 million to fund your small business

- SBA-guaranteed loans can be used for most business purposes
- SBA-participating lenders work with the SBA to match you with the right loan for your business needs



Working Capital - Like seasonal financing, revolving credit or refinanced business debt



Fixed Assets - Like furniture, real estate, machinery, construction and remodeling

SBA Loan Programs

7(a) Loan Program

- SBA's primary business loan program

SBA 504 Loan

- Long-term fixed-rate financing for real estate, machinery and equipment

SBA Express Programs

- Streamlined, expedited loan process through experienced lenders
- Up to \$500,000 / collateral may be waived on smaller loans
- Maximum interest rate 9.75% APR

Fee Relief for Veteran Borrowers

Zero Up-front Guaranty Fees on SBA Express Loans for military community members, including:

- Soon-to-be discharged active-duty service members, eligible for military Transition Assistance Program (TAP)
- Reservists, National Guard members
- Veterans
- Current spouse of any of the above
- Widowed spouse of service member or veteran who died during service or from service-related disability

SBA Loan Programs for Underserved Markets

Targeted to veterans, women, minorities, rural and other under-served populations

SBA Community Advantage

- Loan amounts of up to \$250,000

SBA Microloans

- Loan amounts of up to \$50,000
- Administered by CDFIs/Non-Profit Lenders
 - Credit requirements not as stringent
 - Management/Technical Assistance provided

SBA Loan Eligibility Requirements

- SBA loan eligibility is generally based on what a business does to receive its income, the character of its ownership, and where the business operates
- Normally, businesses must meet [size standards](#), be able to repay, and have a sound business purpose
- The lender will provide you a full list of eligibility requirements for your loan



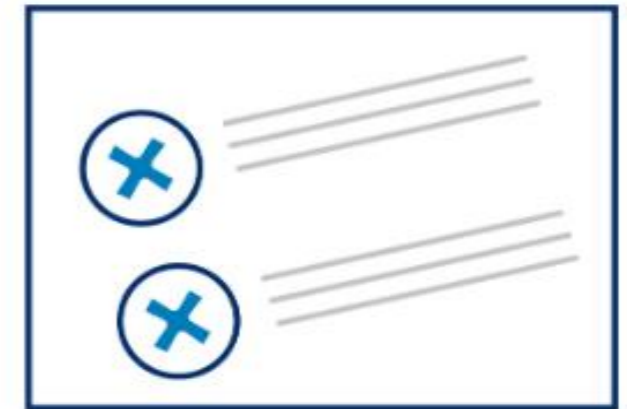
Be a for-profit business
The business is officially registered and operates legally.



Do business in the U.S.
The business is physically located and operates in the U.S. or its territories.



Have invested equity
The business owner has invested their own time or money into the business.



Exhaust financing options
The business cannot get funds from any other financial lender.

Not Eligible for SBA Financing

- Real estate investment/ other speculative activities
- Lending activities
- Multi-level marketing firms
- Gambling or speculation
- Businesses primarily providing sexual material
- Marijuana industry
- Illegal activities
- Religious organizations
- Non-profit organizations
- Charitable organizations
- Borrowers who have defaulted on federal loans or financing, such as VA home loans or education loans

Your Local SBA Team

Can connect you with SBA, its Resource Partners and business advisors

- Assist with cash flow analysis and financial projections

Can help you find the right lender

- Can connect you with lenders with loan programs appropriate to your stage of business, industry, financing needs, demographic, risk level, etc.



United States Department of Agriculture



HANDOUT

USDA Loans & Loan Guarantees

Agriculture (farming and livestock) and non-agriculture businesses in rural areas can use these loans for:

- New business start-up expenses
- Acquiring an existing business
- Purchasing land, buildings or facilities
- Modernization & other business improvements
- See if your location is or will qualify, go to:

bit.ly/usdabusinessmap



Non-Banking & Equity Financing

- Involves financing from non-banking sources
- OR involves investors, usually in exchange for partial ownership of your company
- Is not paid back
- Can have benefits beyond the money invested



Sources of Non-Banking & Equity Financing

NON-BANKING SOURCES

- Crowd Funding
- Peer-to- Peer Lending

EQUITY INVESTORS

- Angel Investors
- Venture Capital

Crowd Funding

Rewards-based online platforms allow early stage entrepreneurs to “pre-sell” their products or projects to gain upfront or growth funding.

PROS: Entrepreneurs make their offers and set their own funding goals. Host sites charge a percentage of the funds.

CONS: No guarantee that you will gain traction. Some channels do not pay out until the goal is reached.

KICKSTARTER

INDIEGOGO.

gofundme™

Peer-to-Peer Lending

Online financial platforms that solicit funds from the public/investors to lend to small businesses.

PROS: May be a viable source of capital with less restrictions for secured and unsecured loans. Can be a faster process.

CONS: Higher interest rates and automatic repayment terms for borrowers.

Potentially higher risks for investors.

No government protection from default.



Angel Investors

- Individuals who invest their personal capital directly in start-ups
- Angel investors are valuable because of their willingness to make relatively small investments, and for their industry knowledge and market connections

Venture Capitalists

- VC firms are limited partnerships of money managers who raise money in “funds” to invest in start-ups and growing firms
- Invest in high growth potential ventures, but not generally at the start-up stage
- Looking for extraordinary returns
- Fund fewer deals than Angels

Financial Statement You Will Use *

- **Balance Sheet**

A snapshot of assets and claims against those assets, i.e., liabilities. Shows what the company owns, owes and how it is financed.

- **Income or Profit & Loss Statement**

Shows revenue and expenses and provides a ‘bottom line’ of profitability over a specified period.

- **Cash Flow Statement**

Shows the uses and sources of cash as it moves in and out of the company through its operations over a specified period of time

* Examples shown are annual statements for a C Corporation

Annual Balance Sheet

ASSETS		LIABILITIES		
CURRENT ASSETS			CURRENT LIABILITIES	
Cash	\$123,000		Accounts Payable	\$100,000
+ Marketable Securities	200,000		+ Notes Payable	150,000
+ Accounts Receivable	345,000			
+ Inventory	100,000			
= TOTAL CURRENT ASSETS	\$768,000		= TOTAL CURRENT LIABILITIES	\$250,000
LONG TERM ASSETS			LONG TERM LIABILITIES	
Building (Gross)	\$350,000		Long Term Note to Bank	\$300,000
-Accumulated Depreciation	<u>-50,000</u>		= TOTAL LONG TERM LIABILITIES	\$550,000
= Net Building	\$300,000			
+ Land	\$325,000			
= LONG TERM ASSETS	\$625,000		OWNER EQUITY (Total Assets minus Total Liabilities)	\$843,000
TOTAL ASSETS	\$1,393,000		TOTAL LIABILITIES	\$1,393,000

Income or Profit & Loss Statement

OPERATING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:

Gross Sales	\$1,200,000
minus Cost of Goods Sold (COGS)	- 850,000
= Gross Profit	\$350,000
minus Selling, General, and Administrative Expenses	- 311,000
= Income from Operations	\$39,000
minus Interest Expense	- 9,000
= Income Before Taxes	\$30,000
minus Income Taxes *	- 12,000
= Net Income	\$18,000

* Income taxes on a business ONLY apply to a C-Corporation

Cash Flow Statement

Operating Activities = how cash comes into and goes out (\$) of the business from “sales” activities

OPERATING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:	
Net Profit	\$18,000
Depreciation/Amortization	\$50,000
Changes in Accounts Receivable	(\$345,000)
Changes in Accounts Payable	\$100,000
Changes in Inventory	(\$100,000)
TOTAL CASH FLOW FROM OPERATING ACTIVITIES	(\$277,000)

Investing Activities = from asset purchases (\$ out) or sales (\$ in)

INVESTING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:	
Payment for Acquisition of Plant, Property & Equipment (PPE)	(\$350,000)
Sale of PPE	\$0
TOTAL CASH FLOW FROM INVESTING ACTIVITIES	(\$350,000)

Financing Activities = from loans or stock sales (\$ in) vs dividends paid (\$ out)

FINANCING ACTIVITIES, CASH FLOW PROVIDED BY OR (USED) IN:	
Issuance of Stock	\$600,000
Dividends <i>* Only applies to a C Corporation</i>	\$0
Net Borrowings	\$150,000
TOTAL CASH FLOWS FROM FINANCING ACTIVITIES	\$750,000
Net Increase/Decrease in Cash: (\$750,000-\$277,000-\$350,000)	\$123,000
Cash at Beginning of Period	\$0
CASH AT END OF PERIOD	\$123,000

Key Takeaways

- Plan for future growth
- Know the difference between debt and equity financing
- Understand how much money you need & what lenders are looking for
- SBA and USDA loan programs can provide financial assistance for a variety of business needs

Questions & Discussion