BASICS OF FINANCING

BASIC CONCEPTS TO KNOW WHEN CONSIDERING FINANCING.

Did you know that there are several ways of funding your entrepreneurial venture?

There is a tendency to believe that to start your own business it is important to have your own vast and infinite funds.

Fortunately, if you already have a clear idea and a detailed business plan, then it is very likely that you can choose one of the several financing options that exist.

It is in your hands, and in the dimension and stability of your project, to determine which is the financing method that suits you best, for example: equity or debt could work for you, or the combination of both –a usually successful formula.

As an entrepreneur. you must take into account both the investment necessary to start your business and the working capital required for its operation when exploring funding options. Ideally, a start-up venture should have at least 3 to 6 months of working capital already guaranteed through a reserve fund or a line of credit that prevents the business from closing down in the event of not making as much as expected in the first months.

We summarize below some of the potential sources of financing for entrepreneurs.

Self-Financing

Although your first option is to apply for funding from institutions created for this purpose, or from other schemes we later describe, it is essential to have a portion of your own capital to invest in the business.

It can be paid in cash or with assets, such as vehicles, equipment, and others. Usually, it is part of the company's net worth, or the entrepreneur's if such legal entity has not been established.

Friends / Family

: Sometimes it may be preferable to raise money from friends or family instead of borrowing from a financial institution, especially if as an entrepreneur you feel it is difficult to meet the bank's requirements before you have the business experience required in the country where you are located. If that is the case, and you have a friend or family member willing to give you a loan, it is very important that you keep a professional attitude and treat them like any other investor or lender; that is, let them know your business plan and information about cash flows, sign a legal document that supports the transaction, and always make the payments on time.

A relevant aspect to consider is whether it is convenient to agree to receive the funds as a loan or as equity, since the former can give you more freedom to manage the business. If it is agreed to receive funds as equity, it is important to document the transaction and decide on the benefits that the acquired shares will bring to the friend or family member. In any case, transparency is always important to safeguard personal relationships and the venture.

Venture Capital

These are firms or investor associations that are dedicated to fund companies in early stages. This type of financing is delivered in exchange for ownership equity of a new company and generally support young entrepreneurs with a robust and innovative business idea. To obtain funds from a Venture Capital, it is important to research the sector and type of investment that attracts them, as well as presenting a solid strategy to cover any questions about the business.

Business Incubators

These are organizations dedicated to accelerating the success of new businesses and can vary depending on the strategy they have set. For example, in some cases they are only dedicated to offering a location for entrepreneurs (similar to an office) where they can interact with startup “coaches” and do networking with other entrepreneurs and with some “angel investors” interested in financing new businesses. In other cases, the incubators have capital from government agencies or “angel investors” to finance interesting projects for some region of the country or for some sector of the economy. What you should do is to research about these organizations to determine if there is any possibility of financing your business this way.

Funding from government agencies for entrepreneurs

Many countries allocate resources in their budget to support ventures that promote the development of the country’s economy. In some cases, they may have even created specialized institutions to finance new businesses to which they give information about the sector and explain why it benefits the country (tourism, commercial development of a specific area, etc.) in order to obtain financing. There are other cases when a local government wants to promote tourism or commerce in a specific area and allows the use of spaces for restaurants free of rental charge for a certain time, or it provides specific equipment for the entrepreneur’s business.

Microcredit

Most banks offer some financing opportunity for entrepreneurs; particularly, some banks offer microcredit schemes for entrepreneurs. Sometimes, the bank can offer financing for entrepreneurs depending on the use of the funds. In the case of restaurants, the bank can finance the renovation of the premises, the purchase of specialized equipment or the project of the entrepreneur as a whole.

In this sense, it is important to identify the potential sources of financing, evaluating all the possibilities, in order to properly quantify the financial costs and decide on the best combination for financing the project.

Regardless of the origin of the funds, you must have a clear idea that is supported by a business plan and that, in turn, can answer the financial concerns of any independent third party and that allows you to present a solid strategy for the business venture.

About microcredits

Microcredits are a specialized form of financing for small businesses or for people with low income who have an interesting business initiative. Sometimes, this initiative has some social benefit that supports the generalized connotation of microcredit as one of the tools to eradicate poverty. Nowadays, most banks have a portion of their loan portfolio dedicated to microcredit or have created a branch or foundation dedicated to these purposes. Depending on the local regulations of each country on the banking sector, microcredits may have lower interest rates and do not require guarantees on the amount granted, which is usually a moderate amount. Similarly, it is possible that the requirements to obtain a microcredit are less strict than those that apply to a commercial credit.

There are non-profit organizations often dedicated to financing micro-entrepreneurs with their own resources or to mentor them to strengthen their venture. In this sense, it is essential to carry out exhaustive research on these organizations and on the main banks that grant microcredits to evaluate the alternatives that are best for the business. It is advisable to make a comparison chart including the benefits granted by each financial institution, as well as the associated financing costs. Then, such costs must be added to the business plan and the cash flow forecast that will be part of the funding request requirements. This shows that the entrepreneur is committed to meeting financial obligations and will seek the returns that allow them to meet them.

Financing costs not only include the interest paid on the loan received, but may also include commissions, legal and/or registration fees, among others. It is important to inquire about these costs in different banks to include them in the comparison chart and thus get a full picture before making a decision.

Below are some of the most common requirements you would need to meet to request funding at financial institutions. These examples may vary depending on the requests made to the banks by the financial regulatory entity of each country. That is why as an entrepreneur you must inquire what the requirements are in the country in which you are located.

- Articles of incorporation of the company duly registered before the competent authorities of each country, as well as minutes of shareholders or board of directors that demonstrate the individual who submits the applications to the financial entity is an authorized representative.

- Identity document or identity card.

- Business experience; the term required by each financial institution may vary in months or years.

- Business client background information, usually documented through business reference letters that must be easily verifiable.

- Age of majority depending on the country.

- Good credit history, which is usually obtain through entities that determine people's creditworthiness or that consolidate information on people's credit for banks.

- Income tax returns for the last few years (the specific year requirement may vary by country).

- Financial statements for the current year and previous years signed by a certified public accountant in the country; it can be personal or of the incorporated company and include:
    1. Profit and Loss statement.
    2. Balance Sheet.

- The specific years requirement may vary by country and sometimes the financial institution may require financial statements audited by an independent public accountant.

- Proof of address, for example, receipts for payment of services or certification from the mayor's office or city council.

- Last pay stub (if employed) or proof of income, such as a certified financial statement duly signed by a certified public accountant in the country.

- Business plan that includes: investment plan, financing scheme, supply, demand, prices, costs and other relevant financial information about the future of the venture.

- Bank and personal references of both the company and the individual submitting the funding request, easily verifiable.

- Guarantor. A guarantor is someone who agrees to pay the debts of another person, in case the latter cannot do so. It works as a guarantee for the one who grants the loan. Some banks require a guarantor to be appointed before granting the loan and it usually should not be a family member or spouse, but a third party. On occasion, the bank may request information about the chosen guarantor (identification documents, credit worthiness, bank references, personal financial statement, etc.)

Recommendations to succeed in obtaining funding

- A business plan prepared with details that allow an investor/lender to answer financial questions about the business being considered, especially about the entrepreneur's ability to generate income and positive cash flows that allow making dividend/interest payments.

- Clarity in the funding request and the loan purpose: is it for working capital, equipment acquisition, renovations, real estate acquisition?

- Demonstrate with solid ideas and goals the commitment to the success of the business.

- Effective presentation of the information requested by the lender for the financial analysis.

- Own investment funds together with funding from other sources.

References

- StartUpChile:
  http://www.startupchile.org/

- These are the main sources of financing for entrepreneurs:
  https://www.forbes.com.mx/estas-son-las-principales-fuentes-de-financiamiento-para-emprendedores/

- Entrepreneur in spanish
  https://www.entrepreneur.com/

- Getting Started With Business Incubators
  https://www.entrepreneur.com/article/52802

FOOD
BUSINESS
SOLUTIONS

@PANFOODBUSINESS

P.A.N. FOOD BUSINESS SOLUTIONS

@PANFOODBUSINESSSOLUTIONS

P.A.N. FOOD BUSINESS SOLUTIONS

HTTPS://PANFOODBUSINESS.GLOBAL/