Show me the money! Finance FAQ's

What type of finance do I need?

The type of finance to choose depends upon your reason for needing the funds.

Cash Flow Finance: If you need funds to manage cash flow fluctuations then a bank overdraft or line of credit is your best bet. A more expensive option is factoring, which allows you to effectively sell your accounts receivable at a discount.

Equipment Finance: Normally equipment is financed by a fixed interest rate bank loan, with all payments known in advance. You may also be able to secure finance directly from the vendor.

New Business Acquisition: A secured bank loan, vendor finance or angel investors can be used to finance a new business acquisition. Vendor finance effectively enables you to pay for the business over time. As the population ages and increasing number of businesses come onto the market this is becoming easier to access.

What's the best finance option for my start up?

Sourcing loan finance can be very difficult for a start up business unless you have major assets outside the business that you are prepared to mortgage.

If you are unable to secure a loan and can't scrape together what you need from family, friends and your credit card, then the best option is to explore angel investors, seed funding and venture capital opportunities. This type of finance has become much easier to access thanks to the internet.   Click here for Pollenizer's excellent list of available options. And note that some seed funding organisations offer mentoring and other advantages as well as funding.

Crowdfunding is also an option for start ups – particularly if you are developing a new and exciting product. It is possible to use crowdfunding to establish pre-orders on your new product so you have the cash in hand to make your first production run.

How do I maximise my chances of getting a loan application approved?

Lenders will look at four key factors in assessing your loan application:

Your business risk profile.
The level and nature of security.
Your ability to make regular loan repayments.
Your ability to ultimately repay the loan.

A detailed and well constructed business plan, financial statements and cash flow projections will go a long way toward alleviating concerns about points 1, 3 and 4 above. So make sure that you have done your home work before even contacting the bank.

Security is the other key issue. Think through what personal or business assets you would be willing to offer as security. You don't have to put these on the table up front. But expect to be asked for security and be prepared.

What happens if I default on my loan?

Your loan agreement will set out the conditions considered to be a default. Legally once default has occurred the bank is able to demand immediate payment.

Normally, the bank will have a discussion or send a letter expressing their concerns before calling a loan. So you will have an opportunity to discuss your situation with the bank and possibly negotiate a change in your borrowing arrangements.

Note that if your business experiences financial difficulties it is best to speak to the bank before you reach a default situation. Banks hate surprises.

If the bank decides not to allow continued default they must provide you with written advice that your banking facility has been withdrawn. If you are unable to make payment, the bank has the right to seize any secured assets.

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Should I be willing to offer my house as security?

The decision to put your house on the line is a very personal one. It is becoming increasingly difficult to get any sort of bank finance without personal security. You may find that you are unable to secure the funds you need from a lender without having a lien against your home.

If you are unprepared to “bet the house” then you can consider raising capital, instead of loan finance. Be aware that this will reduce your ownership in your business and in some instances may reduce your control. For small businesses both angel investors and crowdfunding offer capital raising options.

What happens in a bank annual review?

Most lenders will conduct an annual review, usually when the annual accounts are available or on the anniversary of the loan. The bank is likely to require up to date financials and information summarizing operations over the last 12 months and forward projections for future operations.

The bank administration will review your results and a manager will recommend continuance or withdrawal. It is important that you take an annual review seriously, as the bank has the right to cancel your loan.

What are my options if the bank won't approve my loan application?

There is a growing range of finance options for cash strapped small businesses.

Factoring agencies effectively purchase your accounts receivable, advancing you 70-90% of the total.

A Merchant Cash Advance is a good option for businesses with high credit card sales. This type of finance allows you to take a lump sum up front and then pay a set percentage of your daily credit card sales.

Angel Investors can be a good finance option if your venture is too risky for the banks or you have too little security. Remember that you will be giving up some of your ownership with this type of finance and that potential investors are going to expect a strong growth story.

Crowdfunding is another possible option. Crowdfunding can be used to “pre-sell” a new product, effectively raising the funds before you have to pay for production. (Before proceeding with this type of crowdfunding, check out our article on Budgeting for a Crowdfunding Campaign.) It is also increasingly available as a way of sourcing equity from the general public.