HOW TO DO IT

FINANCE YOUR HIGH-GROWTH BUSINESS

HIGH-GROWTH
START-UPS

- Identify what kind of finance you need
- Get your business investment ready
- Prepare a convincing business plan
- Target suitable investors
- Be realistic about what your business is worth

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HOW TO DO IT **FINANCE YOUR HIGH-GROWTH BUSINESS**

Having the right finance in place is essential if your business is to develop. Developing new products or approaching new markets can require significant investment before sales income starts to flow. Even then, as turnover increases, so does the amount of finance tied up in working capital. Without adequate financing, your growth potential will be constrained. At worst, the survival of your business could even be threatened.

In the early days or when you start a new project, the business may suffer a prolonged period of negative cashflow. You may also be making losses while you invest for the future. While banks can offer financing options, a business operating like this may not be able to offer the security a bank requires. Instead, you may need to bring in outside investors to finance your development or explore alternative financing options such as government grants or investment finance. In order to secure investment, you may have to give up equity in your business, however, with the right approach you may end up with a smaller share — but of a much larger business.

1 ASSESS YOUR NEEDS

1.1	**Establish your key objectives.**	■ For example, you might want to increase sales or gain access to a new market. In order to finance these objectives you may need to develop a new product or purchase equipment.
1.2	**Calculate how much financing you need.**	■ You may want to consider a range of options. For example, the minimum needed to take your business forward and how much more would allow you to put all your plans into effect. ■ Include best- and worst-case scenarios. This allows investors to get a feel for the level of risk involved and shows you have a good understanding of the market.
1.3	**Consider what contribution you can make from your own resources.**	■ When starting up, you will probably need to make a significant personal investment. Other sources of funding are unlikely to be willing to provide finance unless you have shown commitment in this way. ■ One option may be to take out a mortgage on your personal property, then lend the money to your business. However, your home will be at risk if the business has financial difficulties and you cannot keep up repayments. ■ Ask family and friends if they would be prepared to invest. Ensure that they only invest money they can afford to lose and draw up legally binding agreements. ■ Once you begin trading you build up retained profits within the business that you can use to finance growth.

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1.4	**Identify which types of financing will suit you.**	■ You may qualify for a grant to cover part of your funding requirements (see section 2). ■ You may be able to use bank finance or similar alternatives if you have reliable cashflow and can offer security (see section 3). ■ If your business needs high-level funding you should consider investment finance, but you will have to offer investors a high return and an exit plan. In return, be prepared to give up equity in your company (see section 4). ■ The balance between borrowing and investment finance depends on your circumstances. High-growth businesses are likely to need a high proportion of investment finance to fund their expansion.
1.5	**Plan ahead.**	■ Arranging finance may take months. ■ Plan your total finance requirements for the next few years, even if you will not need all the money in the short term.

2 INVESTIGATE POTENTIAL GRANTS

2.1	**Find out whether any grants are available.**	■ Grants typically support innovation, research and development, or investment in relatively deprived areas. ■ Grants almost always support specific projects rather than general business growth. ↘ *For more information on government grants visit www.j4bgrants.co.uk*
2.2	**Consider whether it is worth applying for grants.**	■ Obtaining a grant may involve a complex application process and a delay of several months. If you start the project before the grant is awarded you may no longer be eligible for grant funding. ■ You may be required to provide match funding – where you are required to fund at least half the cost of the project – or you may have to change your plans to meet other requirements of the particular grant scheme.

3 CONSIDER BANK FINANCE

3.1	**Find out what financing options the bank can offer.**	■ As a start-up, banks are likely to provide at least some of the finance for your business. Most banks offer a range of options for start-ups looking to grow, including equity and structured finance for investment purposes, as well as options for working capital such as overdrafts or invoice financing. ■ Use bank loans for fixed-term financing — to cover development costs or purchase fixed assets such as plant and equipment, for example. A fixed-term loan is a more reliable form of long-term borrowing than an overdraft, which in principle is repayable on demand. ■ If you are borrowing to acquire an asset such as equipment or leased premises, the term of the loan should be shorter than the working life of the asset. ■ Use an overdraft to finance cashflow fluctuations and for short-term borrowing.
3.2	**Assess how much a bank is likely to be prepared to lend you.**	■ As well as a credible business plan (see section 6) and showing that you will be able to afford interest and capital repayments, a bank will usually require security over assets such as property or equipment. →

3.2	(continued)	■ If your business cannot provide sufficient security, you may be asked to provide a personal guarantee. This means commiting yourself to repaying your business' borrowings – if necessary through the sale of your personal assets. By providing a guarantee, you will be personally liable if the business fails to make payments on time. ■ Alternatively, you may qualify for the Small Firms Loan Guarantee: the Government guarantees 75 per cent of the loan, in return for which you pay a small premium. ↘ *For more information on the Small Firms Loan Guarantee visit the Department of Trade and Industry website at www.dti.gov.uk/sflg*
3.3	**Consider whether alternative forms of borrowing would be more appropriate.**	■ For example, you might lease equipment or use factoring to raise finance against unpaid invoices and improve cashflow. ■ Financing costs for these types of borrowing may be higher, but any comparison has to take into account the upfront costs, interest rates and tax implications. Your business adviser or accountant can help you. ↘ *For more information on factoring and invoice discounting visit the Factors and Discounters Association website at www.factors.org.uk*

4 CONSIDER INVESTMENT FINANCE

4.1	**Consider what kind of investor(s) you might attract.**	■ Business angels – wealthy entrepreneurial individuals – may be prepared to invest between £10,000 and £250,000 (sometimes more). Many then expect to take an active management role in the business. ■ Venture capital investors usually make investments of £1 million or more. ■ There are also specialist venture capital funds. For example, Regional Venture Capital Funds make smaller investments (typically up to £250,000). Community development funds invest only in deprived areas.
4.2	**Consider whether corporate venturing would be a viable alternative.**	■ This is when a large company partners with your business, providing the resources that you need. For example, you might be able to market your product through their distribution network. ■ You need to offer your partner something they want. For example, if your innovative product improves the range of products they offer. ■ The partnership reduces your need for investment finance (for example, if you no longer need to develop your own distribution network). In some cases the company may also want to make an investment in your business.

5 GET YOUR BUSINESS INVESTMENT READY

5.1	**Build a management team.**	■ To secure investment, do not rely solely on your own expertise. Financiers will want to see a skilled team with a strong record of success. ■ Consider whether you need to bring in any new individuals, particularly if your growth plans include new activities. For example, if you plan to export, you may need someone with experience of international trade. ↘ *See How To Do It: Recruit and motivate key team members and Build your company's board* →

5.2	**Ensure that clear contractual arrangements are in place.**	■ If major assets (such as premises or intellectual property) are owned by you personally, you may want to transfer them to the business. ■ Aim to negotiate long-term contracts with customers, suppliers and key employees so that financiers have confidence in these relationships.
5.3	**Make your business as attractive as possible.**	■ Set up effective management-information systems that demonstrate that your business is well managed. ■ Put extra effort into credit control to reduce your level of working capital so that lenders and investors can see that you run a tight operation. ■ Ensure that premises and equipment are well-maintained.
5.4	**Plan how you will address any weaknesses.**	■ Showing that you are aware of any weaknesses in your business and know how to deal with them will give financiers confidence. For example, you might earmark part of the money you are raising to recruit an individual with skills your management team currently lacks.
5.5	**Keep managing the business.**	■ Do not allow your efforts to raise additional finance to distract you from the ongoing management of the business.

6 PREPARE YOUR BUSINESS PLAN

6.1	**Review your business plan.**	■ Keep forecasts and other financial information up to date. Include data illustrating your financial performance when you have it. ■ Base your plan on the assumption that you will receive the financing you are looking for and will carry out your growth plans. Include the costs of finance in your forecasts. ↘ *See How To Do It: Plan and budget for growth.*
6.2	**Explain the key features of your business.**	■ These will include: your products or services; the market, customers and competitors; management and any key employees; operational details; and financial forecasts. ■ Concentrate on proving the business case, rather than getting carried away with details of your product or technology. ■ Provide evidence for your claims. Include detailed supporting evidence (such as market research data and management CVs) as an appendix to the plan.
6.3	**Tailor your business plan to the audience you are addressing.**	■ For example, a bank lender will be particularly keen to see that you can offer adequate security and have good cashflow. A business angel would be more interested in seeing the potential of the business for growth. ■ The larger the funding you are looking for, the more detailed your plan needs to be.
6.4	**Consider what you are prepared to offer investors.**	■ Your assessment of what your business is worth may be far more optimistic than the value an investor will put on it. To justify the risk they are taking investors want the prospect of a significant return. ■ At this stage, you only need to outline what you are offering. Investors are likely to want an equity share of your business, along with a clearly defined exit point. ■ Most investors will want you to retain management control, even if they are putting up most of the money.
6.5	**Ensure that there is a clear exit plan for investors.**	■ Investors typically look to recoup their investment (and profits) over a three-to-seven-year period. →

6.5 (continued)	■ Common exit routes include a trade sale of the whole business to another company or a stock exchange flotation.
6.6 Prepare an executive summary.	■ The summary highlights the main points financiers need to know. Aim to get them excited about your business's potential. ■ Usually the summary should be no longer than two or three pages.
6.7 Take advice on your plan.	■ A good business adviser can help you refine your plan to make it as attractive as possible, as well as talking through any underlying issues you need to address. ■ You may want your accountant to work through the financial forecasts with you.

7 AGREE THE FINANCING

7.1 Approach potential financiers.	■ Locally-based business angels can be found through the Yorkshire Association of Business Angels (01423 810149 or www.yaba.org.uk). ■ The British Venture Capital Association (020 7025 2950 or www.bvca.co.uk) can help you identify venture capital firms interested in making investments. ■ Your accountant may be able to help you identify and approach investors. Alternatively, your Business Link may have an investment-readiness adviser. ■ Consider approaching several lenders for any borrowing requirements. Shopping around can put you in a stronger negotiating position, even if you decide to borrow from your existing bank.
7.2 Sell your business to them.	■ Present your business with enthusiasm and commitment.
7.3 Agree a suitable financial package.	■ Lenders and investors will generally want to structure the deal so that they get repaid before you if the business runs into difficulties. For example, your personal investment might take the form of ordinary shares, while a venture capitalist invests in preference shares (which have a better chance of being repaid if the business becomes insolvent).
7.4 Negotiate the deal.	■ It may well be worthwhile using a suitable adviser to do this on your behalf, particularly if you are negotiating investment finance. ■ Investors may want to place some restrictions on you – by limiting the salary you can pay yourself, for example. These restrictions usually aim to protect investors' interests, and may be non-negotiable.

SIGNPOST

- ↘ For more information on government grants visit www.j4bgrants.co.uk
- ↘ To find your local Business Link call 0845 600 9 006 or visit www.businesslink.gov.uk
- ↘ To find out more about the Small Firms Loan Guarantee, ask your bank or visit www.dti.gov.uk/sflg
- ↘ For more information on venture capital, contact the British Venture Capital Association on 020 7025 2950 or visit www.bvca.co.uk
- ↘ To find out more about corporate venturing, visit www.corporateventuringuk.org
- ↘ For more information on factoring and invoice discounting visit the Factors and Discounters Association website at www.factors.org.uk

Expert contributor

Paul Gardner, c2 Ventures.
Contact 07050 263500;
www.c2ventures.com