Funding for SME’s - the issues and options

Business owners reading the daily newspapers these days are fed a constant diet of how difficult it remains to secure vital funding for both day-to-day survival and/or growth.

Despite the doom and gloom surrounding our traditional lenders, and the seemingly limp progress of Government initiatives such as Funding for Lending, there are still a number of options open and an increasing band of financial institutions willing to help. You just have to know what to look for, where to look for it and of course what to look out for. In this respect, there follows a few ideas that could be worth considering

In times gone by the overdraft ruled

The bank overdraft was once the ˈgo toˈ product for SME’s looking for working capital. Debenture lending, whereby a bank would nail down just about every asset a company owned in return for lending often less than half the value of them was hardly rivalled. Overdrafts are of course, in theory, still available, but over time, as asset values decreased and questions started to be raised about whether book debts could actually be captured under a fixed charge, the goalposts started to move; and that brings us nicely on to the first option.

Invoice Finance

Once seen as the ˈlender of last resortˈ this product has enjoyed a huge shift in reputation over the years and now accounts for some £16bn of advances to UK and Irish SME’s. In addition to a large number of independent providers all of the high street banks have invoice finance subsidiaries and it is to these that a lot of their overdraft business has been transferred. The fact that under a factoring or invoice discounting agreement the funder purchases the book debts rather than relying on a charge to secure them overcomes that little conundrum alluded to earlier.

Although some critics might suggest that this can be an expensive way of borrowing money it has a lot of good points if you find the right deal. With the sales ledger as the basis of the agreement, high levels of funding (often 85% or more) can be achieved. And as other business assets are often left out of the equation these can be used to secure separate finance deals should the need arise.

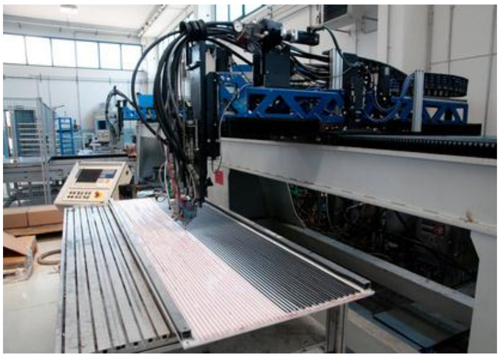
As long as you sell your goods or services to other businesses on credit you will be of interest to an invoice finance provider. Many of them also offer useful add-ons such as credit control and bad debt protection

Tel: 0118 973 7776
Email: mike@mlgassociates.com

which when put together can provide a cost effective way of getting the rump of your sales ledger function outsourced.

Asset Finance

Be it hire purchase (HP) or leasing it makes financial sense to spread the cost of capital equipment. Plant & machinery as well as vehicles and IT equipment can be acquired through either type of facility depending on your specific needs.



At the end of a HP agreement you will own the asset. You will also have all the responsibility of owning that asset which is no bad thing if it has kept its value. If on the other hand you simply want to use it without the hassle of owning it then a leasing deal is probably more of a way forward, especially if it covers costly maintenance and insurance obligations.

Either way, depending on the type of deal you have, you could also benefit from capital allowances, VAT reclaims, and the ability to offset interest payments against profit.

A leasing deal can also be put in place for any assets you already have if a valuation supports it. If you have a machine sitting on your factory floor with life left in it and no outstanding finance against it you could free up some much needed cash in return for fixed monthly repayments.

Business Angels

The television versions are known as dragons and for a good reason; they breathe fire into companies looking to go vertical from start-up or expand very quickly. If you're happy with the way things are but just need a cashflow boost then this isn't for you as you'll not only get cash in the bank but some additional company on your board in return for relinquishing some control.

If on the other hand you feel your potential flyer needs some more weight in addition to the cash, then finding a business angel interested in your sector could be heaven sent. You will have to wave more than a finger in the air when it comes to the nitty-gritty, and show a good return on investment, but if you succeed, your new shareholder will bring a whole host of goodies to the party and not just his or her cheque book. With a wealth of experience and a long list of useful contacts, the sound of doors opening could be a regular occurrence.

Business Pawnbrokers

This industry is not entirely happy with the pawnbroker tag but exchanging short term cash for valuables is what they do. It's a far cry from the three golden balls and popping your wedding ring for a week however with loans these days secured against fine art, fine wines, prestige cars and the odd yacht.

Tel: 0118 973 7776
Email: mike@mlgassociates.com

There are of course different levels of funding with the average SME loan ranging from £3,000 up to £150,000. Recent entries into the market will even go as far as £1 million against prestige assets like those mentioned above. Rates are typically 2.4 – 4% a month depending on the size of the loan so compare favourably with the other products that may not immediately spring to mind to the SME owner looking at funding options. And with loans to SME's growing at 10% per year in recent times there is clearly a market.

The downside to this type of borrowing is fairly obvious; if you fail to repay at the end of the term then you won't get your valuables back.

Business Payday Loans

The success of the personal version of payday loans has prompted the obvious move into the SME market for some providers. The same basic model applies to business lending whereby the use of technology speeds up both the credit checking of a potential borrower and the time taken for approval or decline.

The online nature of these loans makes them simple to apply for and, on the face of it, simple to understand. Customers enter the amount required and preferred term, within the lenders parameters, and can immediately see the weekly repayment obligation along with the total cost of the loan. Typical loan sizes are £3,000 - £15,000, with the potential to gain a higher credit limit based on a good track record. Repayments are usually made weekly via the businesses debit card.

The personal version has come in for some fierce criticism in respect of high APR amongst other things, and whilst the business version has yet to hit those dizzy heights it is worth understanding exactly what the total price includes. What may sound like a good deal expressed as a weekly interest rate might not compare so well with other methods when looked at on an annual basis. There will also be an application fee involved so be ready to add 3% or so to the price.

Directors/owners will also be expected to sign a personal guarantee and at the same time provide personal debit card details. If the business defaults then repayment will be swiftly switched to those cards. The key here is certainty that the repayments can be met. If not the facility could rack up a whole host of additional charges that will also need repaying.

Crowd Funding

This relatively new addition to the business finance arena is gaining market share and a favourable reputation with borrowers and investors alike. Thanks to the internet, those businesses needing finance can very quickly be put in front of a wide selection of investors with cash to lend.

The mechanics are simple; businesses complete an online application form with the necessary credit vetting carried out by the crowd funding company. This company will already have a portfolio of investor members

who have deposited money and who will have usually specified industry preferences and acceptable risk levels. If the application passes the vetting stage it is then put out to auction and interested investors can specify how much of the loan they are willing to fund and at what rate. As the bids come in, those with the highest rates are knocked out, eventually giving the borrower a fully funded loan at the lowest rate available.

Regardless of how many investors may be funding a loan (and it could be lots) borrowers only make one monthly payment to the crowd funder for onward distribution.

Grants

Grants should in no way be considered suitable for day to day financing requirements and any business owner thinking of making enquiries in this respect will be wasting his/her time.

By their very nature, grants for businesses are generally intended for new enterprises or projects and the application process can be very stringent. In addition, if the application lacks any community or environmental benefit it is unlikely to get a favourable reception. Any business intent on going down this path to fund growth will need to convince the provider that the benefits are far wider than just improving its own revenue stream. In most instances the business will also have to match the funds requested.

Despite what the papers say there is cash out there

It is clear then that there are funding avenues open for SME's who find the traditional routes closed off to them. The crucial point to always bear in mind is what best suits the business when it comes to cost, terms and other obligations.

Some of the products listed are clearly based on a short-term need whilst at least one can revolve indefinitely. Either way, the ability to repay any of them should always be based on sound planning rather than hope, and advice and guidance is of course always available.

For reliable, positive and impartial advice about your business challenges, contact Mike Grieshaber.

Tel: 0118 973 7776
Email: mike@mlgassociates.com