BUSINESS FINANCING GUIDE

A Toolkit for Your Business

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BUSINESS FINANCING OPTIONS

The Right Approach For Your Business

One of the most common questions for business owners, whether they are a start-up, established or growing, is how can they access funding for their business. Entrepreneurs often find it challenging to obtain the funding they need when they need it.

As a business owner, you need to understand the types of funding that are available, how these funding arrangements are structured, and how to be prepared to access these funding opportunities. Obtaining financing can take time and requires preparation. Anticipate what you will need, and when, to help your business grow and succeed.

THIS GUIDE WILL HELP YOU:

Understand the most common types of financing.

Determine which aligns best with your business stage, industry, and unique needs.

Learn where to access financing that is right for your business.

Discover tailored financial sources suitable for your business size, industry, and specific objectives to optimize growth potential.

Review and evaluate your options to determine the best solution for your business.

Explore various financing solutions, weighing their pros and cons to choose the right path for your business.

Prepare effectively for approaching lenders and investors.

Equip yourself with insights and strategies to present a compelling case to potential financiers, enhancing your chances of securing funds.

We wish you success on your financing journey.

Table of Contents

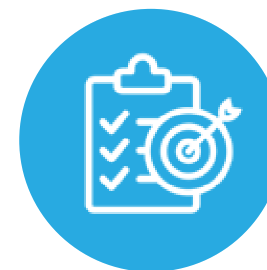
05	Financing Your Business
06	How Start-Ups Are Financed
07	How Growth Is Financed
08	Get Ready For Financing
09	Debt or Equity: Which Is Right For You?
10 - 11	Debt & Equity Financing Options for Each Stage of Business
12	Debt Financing
13	Asset Financing
14 - 15	Prepare a Winning Loan Application
16 - 19	Equity Financing
20 - 21	Prepare a Winning Pitch
22	Crowdfunding
23	Get Advice & Support

FINANCING YOUR BUSINESS

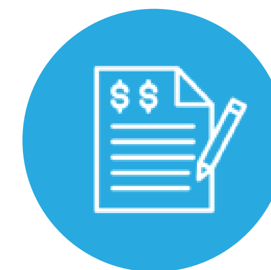
Whether you are starting or growing a business, you'll need money to help you move forward. The right kind of financing at the right time allows you to invest, grow, and create jobs. Obtaining financing can be one of the most challenging aspects of starting or expanding a business.

There are plenty of options for businesses. As a start-up, you may leverage your personal savings or money from friends and family to get your business off the ground. As your business grows, you may utilize more traditional sources of financing such as bank loans or even venture capital to fund aggressive growth strategies. You can also explore alternative sources of financing such as crowdfunding. The right approach depends on the stage of your business, the type of business you are operating, and what your goals are.

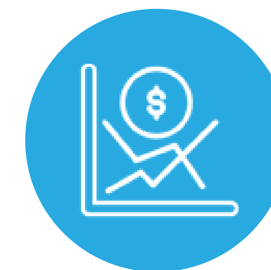
TO ACCESS THE RIGHT CAPITAL FOR YOUR BUSINESS, YOU NEED TO BE PREPARED.



Research the financing options available to you.



Prepare a thorough business plan.



Understand and manage your credit.

Prepare accurate cash flow forecasts.

As with all major business decisions, it's a good idea to get professional advice before choosing which financing option to pursue. There are plenty of resources in your community to help you navigate this important decision.

HOW START-UPS ARE FINANCED

Taking your business from idea to reality needs start-up financing – an infusion of capital that will help you get your business off the ground.

Most businesses are self-financed at the outset. Without a proven track record, it can be difficult to attract traditional lenders or investors.

To finance their new business personally, entrepreneurs dip into their savings, sell off assets, borrow against their homes, use credit cards or personal lines-of-credit, and bootstrap – build their businesses up quickly, and leanly, then pump profits back into the business to fund growth.

COMMON START UP FINANCING APPROACHES	%
Personal Financing	76.4%
Credit from Financial Institutions	34.6%
Financing from Friends or Relatives	13.0%
Trade Credit from Suppliers	6.7%
Capital Leasing	6.1%
Retained Earnings (previous or other business)	6.2%
Credit from Government or Government Grant	3.7%
Other	5.4%
Angel Investor/Venture Capital Funds	0.9%

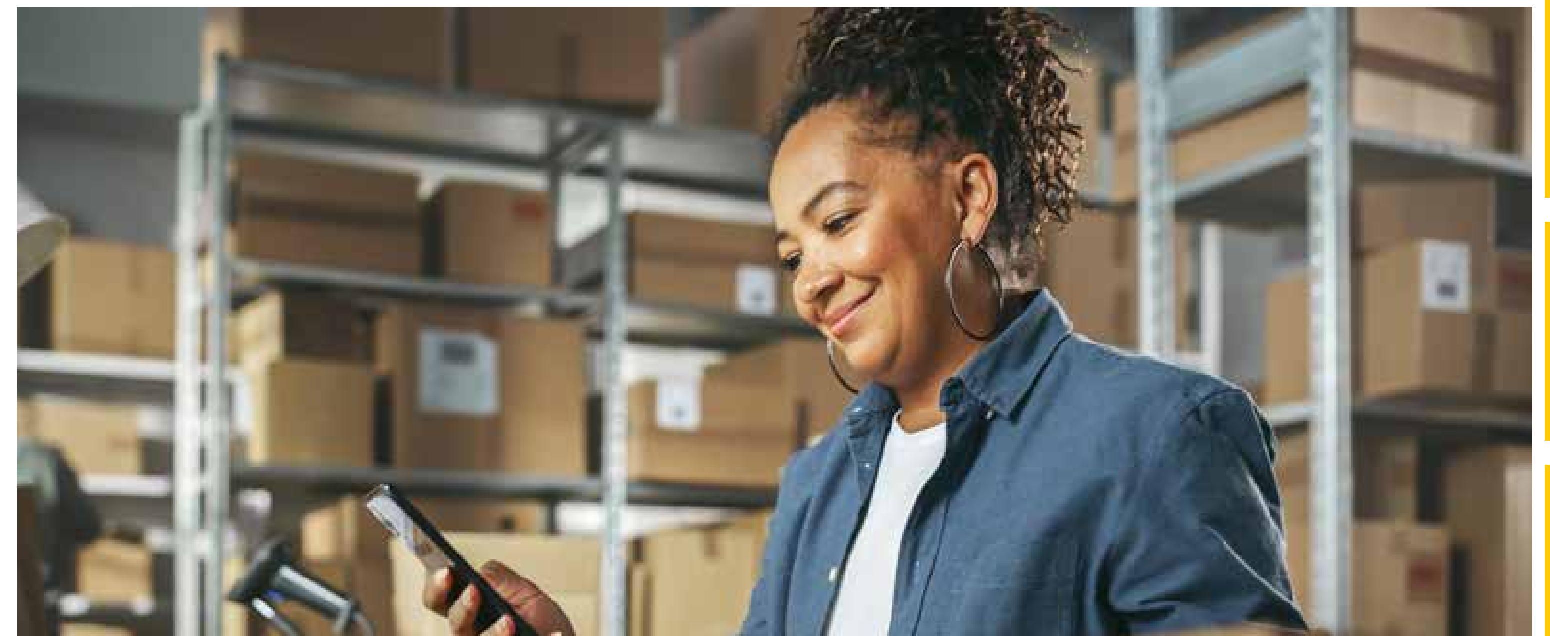
*Statistics Canada, Sources of financing used to start up business by small and medium enterprises, 2022.

Once you get over the initial hump into advanced start-up and early stage, you may be able to access additional funding sources. Most lenders and investors will want to see that you have equity in the business and are sharing the risk, commonly known as "skin in the game".

HOW GROWTH IS FINANCED

As your business grows, you'll likely need to invest in technology, staff, equipment, space, and other resources. These investments can strain your cash flow. For many businesses, financing growth is the only way to move forward. As businesses become more established, they may be eligible for and tend to leverage different kinds of funding to finance growth, such as:

- Debt & external financing
- Trade credit
- Leasing
- Equity
- Government programs



GRANTS AND SUBSIDIES

Small businesses often inquire about grants and subsidies for their business at all stages of operation. However, there are few grant programs available, and most small businesses do not qualify. Less than 4% of start-ups are able to access government grants and subsidies. Be wary of companies that promise access to grants and funding for a fee. These organizations may appear as if they are a government service or department. You can access information about government grants and programs for free through the Canada Business Benefit Finder (Canada.ca - Business Benefits Finder).

GET READY FOR FINANCING

No matter what kind of financing you plan to pursue for your business, the first step is to prepare.

Write or Update Your Business Plan

Even if you have an existing plan, make a fresh assessment of your business, what the opportunities are, how achievable your goals are, and what new challenges you face.

Show that you have thoroughly researched your market and your competitors. Demonstrate a clear grasp of your financials, emphasizing your ability to make payments. Include a detailed analysis of how much capital is needed to finance your plans, and how the money will be spent.

Don't underestimate how much money you will need - coming back for more funding later can be expensive and undermines confidence in your ability to manage your finances. Make sure you build in enough for working capital. Avoid the common mistake of overestimating revenues and underestimating costs.

Check Your Credit Score

Potential lenders or investors will check your credit. Avoid surprises by checking your credit report in advance.

Your credit file is created when you first borrow money or apply for credit. The file is updated regularly by lending institutions, credit card companies, mobile phone companies, and others.

The file includes a credit score (also called a Beacon Score) which is used to predict the likelihood that you will repay future debt. Your credit score reflects the types of credit you use, your credit and payment history, and your debt load. You are generally considered a good credit risk if your score falls between 670 and 739.

You can order your credit report from Equifax or TransUnion Canada.

Get Your Cash Flow under Control

Potential lenders or investors want to know that you are managing cash effectively. Make sure you understand the flow of money into and out of the business. Be sure to:

- **Review inventory and reduce excess where possible.**
- **Issue invoices and collect payments in a timely manner.**
- **Review credit terms with suppliers to generate cash.**
- **Automate payment methods to help increase the speed and certainty of payment.**
- **Address seasonality in your business if it is a factor.**

DEBT OR EQUITY: WHICH IS RIGHT FOR YOU?

Debt financing is by far the most common financing approach for small businesses, but equity financing can be a good option depending on your goals.

DEBT	EQUITY
Borrowing money from an outside source with the promise of paying back, with interest, over a set period of time.	Raising capital by selling shares of your business to an investor.
Pay back through a set payment schedule over the term of the loan.	Pay back through share of profits. Most investors expect a return within 3 to 5 years.
No change in ownership.	Investors become partial owners.
Can be used at any stage (start-up or growth).	Can be used at any stage – more common in growth phase after 1 - 2 years in business.
May be secured against personal or business assets, depending on risk.	Investor shares in risk of the business.

TO DETERMINE WHICH KIND OF FINANCING IS RIGHT FOR YOU, ASK YOURSELF:

How much time do you have?
You can get a loan fairly quickly, especially if you're prepared and approach the right lenders. Finding the right equity partners takes time.

How much capital do you need?
Equity financing rarely comes in small amounts. Debt financing makes more sense if your capital needs are modest.

Do you want more than just money?
The right equity financing can come with knowledge, contacts and expertise that will have a hugely positive impact on your business. Debt financing is more transactional.

How do you feel about sharing?
Equity financing means giving up partial ownership of your business. It's not for everyone. But if you'd welcome the experience and expertise of an investor and their input into your business, then it can be good option.

How big a business are you building?
Equity investors look for businesses with large growth potential and an emphasis on profits and return on investment. If your goal is to stay small and local, equity financing may not be the best option.

DEBT & EQUITY FINANCING OPTIONS FOR EACH STAGE OF BUSINESS

	SEED FINANCING	ANGEL FINANCING	EQUITY CROWDFUNDING	VENTURE CAPITAL	PRIVATE EQUITY	IPO/ PUBLIC OFFERING	OVER-DRAFT	TRADE CREDIT	LOANS	DEBT CROWDFUNDING	ASSET BASED REFINANCING	LEASING
Pre-sales	✓								✓			
Pre-profit	✓	✓	✓	✓			✓		✓			
Growing		✓		✓	✓	✓	✓	✓	✓	✓	✓	✓
Stablw						✓	✓	✓	✓	✓	✓	✓
Making Acquisitions					✓	✓			✓	✓	✓	✓
Refinancing/ Restructuring			✓					✓	✓	✓	✓	✓

EQUITY FINANCING OPTIONS
PAGES 16 - 19

DEBT FINANCING OPTIONS
PAGES 12 - 15, 22

DEBT FINANCING

Most businesses use some form of debt at some point in their growth. The type of debt you choose will depend on the purpose of the financing, the type and stage of business you operate, your credit record and the amount needed.

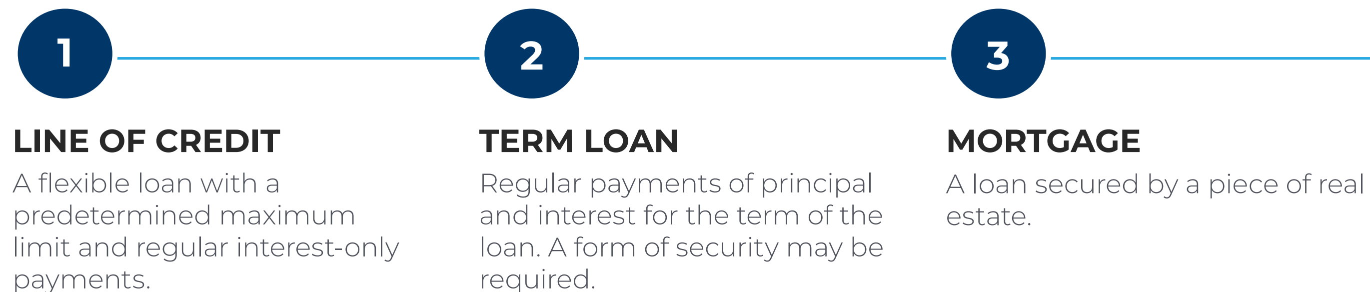
The three most common sources of debt financing are loans from friends and family, loans and overdrafts from lending organizations, and asset financing. A business is likely to need a mix of these over its lifetime.

Friends and family – This can be an important source of capital in the early stages of business development. In some cases, it may make sense to bring these people on as equity investors. In others, however, a simple loan will be more appropriate. In either case, the arrangement should be formalized with a proper legal document that outlines expectations clearly, including payment terms.

Lending organizations – Traditional banks, credit unions, community-based lenders and government lending organizations offer loans, lines of credit, or overdrafts to businesses in the start-up and growth phases.

Different lending organizations have different advantages, from personalized services to specialized products to customized repayment options. Shop around for the best fit.

MOST COMMON TYPES OF DEBT FINANCING FROM LENDING ORGANIZATIONS:



1 LINE OF CREDIT
A flexible loan with a predetermined maximum limit and regular interest-only payments.

2 TERM LOAN
Regular payments of principal and interest for the term of the loan. A form of security may be required.

3 MORTGAGE
A loan secured by a piece of real estate.

Overdrafts can help address day-to-day, short-term requirements in a business that is growing slowly but steadily. Loans are generally suited to larger, longer-term purchases such as investments in facilities, equipment, and inventory.

To qualify for financing, you will have to prove that your business will generate the income needed to pay back the money. Many loan applications fail because the business either hasn't shown how it will repay the loan or has a poor existing track record. Make sure to include loan repayments in your financial projections as part of the application for financing.

Small banks, credit unions and community-based lenders may be more willing to offer financing to small businesses.

ASSET FINANCING

The two main forms of asset financing include:

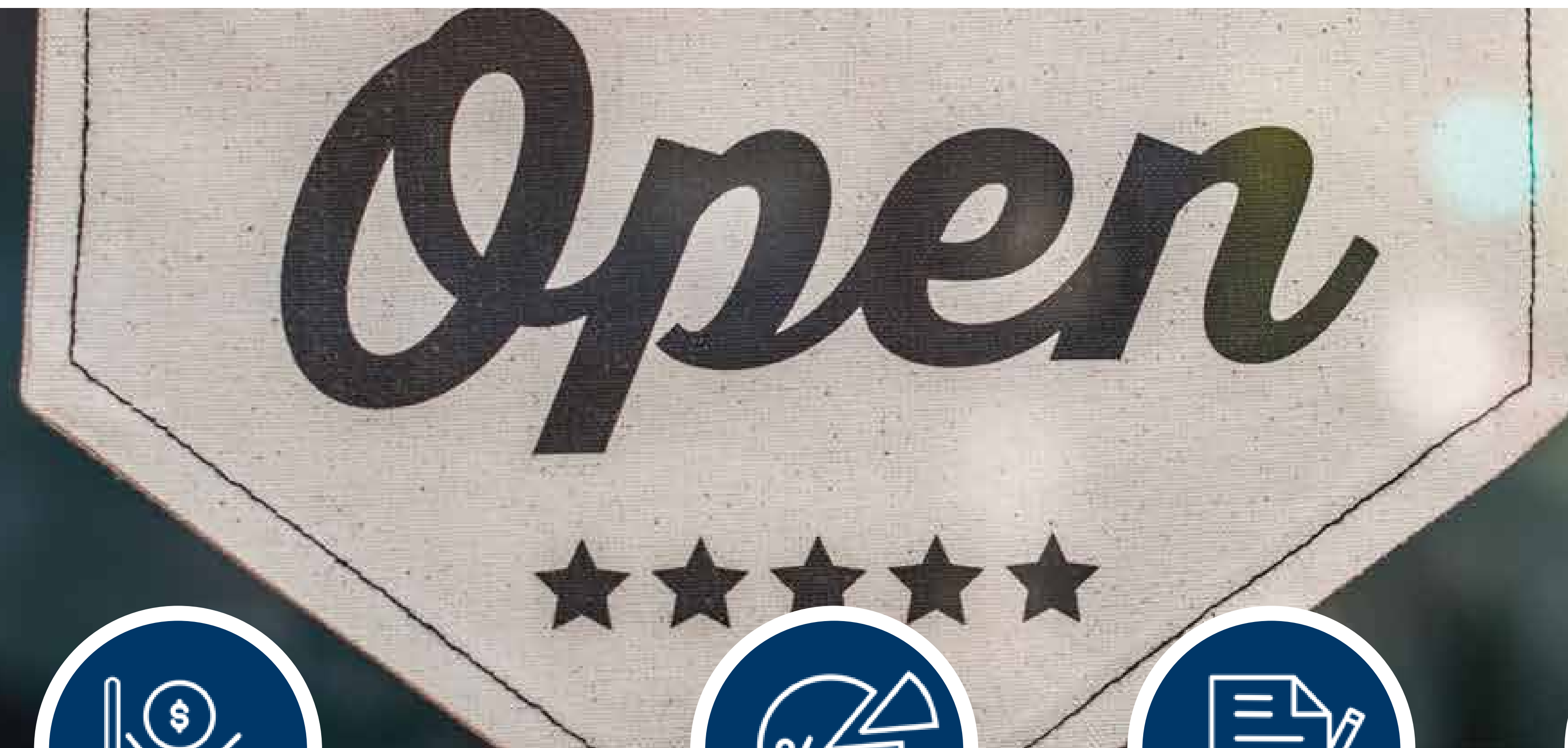
Leasing – Leasing business assets such as equipment, machinery, and vehicles, can reduce the risk of owning and maintaining, and can also offer various tax advantages. Leasing can make new equipment affordable. Since the loans are secured in whole or in part by the asset being financed, you won't need a lot of additional collateral. At the end of the lease period, you can replace or update equipment, which means you won't be stuck with outdated resources. Leases are available directly from specialist providers or indirectly through equipment suppliers or finance brokers.

Asset-Based Loans (ABL) – These are loans or lines-of-credit that are secured against company assets, such as accounts receivable, inventory, work-in-progress, equipment, etc. The money from asset-based loans is most often used to fund short-term needs like employee payroll and the purchase of raw materials. Asset-based lending tends to be more expensive than other means of financing but can be effective for business owners who have collateral or assets and need short-term financing.

THE PROS & CONS OF DEBT FINANCING

PROS	CONS
You are in control of how you spend the loan funds. Some lenders impose certain restrictions, but for the most part you remain free to run your business as you see fit.	If your cash flow is seasonal or irregular, being locked into a rigid repayment schedule can be challenging.
Loans can be short-term or long-term depending on your needs.	The cash comes at a cost - interest. Ideally, however, it will help you earn even more back by increasing your profit margin.
The interest on loans is tax deductible.	Depending on your credit score and financials, it can be tough to qualify for the loan you want.
Repayments are scheduled and predictable, so it's easy to plan for them and manage cash flow.	If you fail to repay the loan, your business assets can be seized.
Some institutions / products can offer flexible repayment terms and interest only payments to accommodate fluctuations in cash flow.	Overdrafts can be reduced or called in if the lender thinks the business may be in difficulty. There are also penalties for exceeding overdraft limits.

TIPS: PREPARE A WINNING LOAN APPLICATION



Prepare a strong business plan

Craft a clear business plan by defining clear objectives and showcasing your understanding of the market. Ensure it resonates with potential investors and stakeholders.

Build a solid financial picture of your business

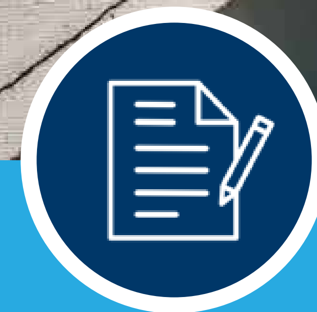
- Be clear on how much money you need and how you will spend it.
- Don't forget working capital.
- State how long you need to have financing in place.
- Include principal and interest payments in your cash flow that demonstrate your ability to pay back the loan.
- Be realistic in your sales projections.

Check your credit report

Check your credit report and correct any errors you find. Know your credit score before you approach lenders. Be wary of becoming a credit-seeker. Too many credit inquiries from multiple lenders can negatively affect your credit score.

Have Skin in the Game

Have equity in your business to show you've got skin in the game and are sharing the risk. Sweat equity does not count.



Provide background information

Supplement your application with profiles of the owner and management team and a list of assets. Include positive client feedback/reviews and success stories if available.

Build strategic relationships

Develop a relationship with your lender and ask for feedback on your application. You may not get approved the first time, but you can use the experience to learn for next time.

EQUITY FINANCING

Equity financing is selling ownership interest in your business for the purpose of raising funds. This type of financing can range in scale and scope, from a small investment from friends and family to an initial public offering (IPO) where a substantial amount of shares are sold. If your business is at an early stage and ready for an investor, a long-term backer can fund it through to revenue and profit. If you're looking to grow, equity financing can support an aggressive growth strategy.

Equity investors can be silent or actively engaged in the business; the degree of involvement will be part of the negotiation. Some investors want more control and can bring valuable expertise and connections to the table in addition to their financial investment.

Since they share in the risk, equity investors generally look for a higher return than debt providers. Like all investors, they'll want to see a comprehensive business plan with realistic financial projections, a detailed marketing plan and the projected return on their investment.

Sources of Equity Financing

Yourself, Friends & Family

The money you put into the business yourself is the first and most common source of equity financing. You may also have friends, family or other contacts that are interested in your business idea or plans for growth and would like to invest.

Depending on their skills, experience and expertise, friends and family may or may not be able to contribute much beyond money to your business. Consider their value carefully and formalize any agreements with a written contract.

Angel Investors & Venture Capitalists

Angels Investors are wealthy individuals who invest directly in small businesses. They often contribute not only experience and a network of contacts but also technical and/or management knowledge. Angels tend to finance the early stages of the business with investments of $10,000 to $150,000. Larger investments can be made through Angel Networks where several individual investors contribute capital to an organization.

Venture capital funds are a pool of funds typically controlled by a venture capital firm. Venture capitalists favour proven track records and rarely invest at the start-up stage. They prefer larger investments, in the order of $1,000,000 or larger. Like angel investors, they can bring a wealth of experience to the business and often help focus the business strategy.

Both angel investors and venture capitalists want to make a return on their investment, so they most often look for high growth and an exit strategy. They'll likely push for growth in the early years, which may mean an initial loss for the business and a bigger future payoff.

Securing larger equity investments from angel investors or venture capital firms can be a complex, costly, and time-consuming process. A detailed business plan or pitch deck is essential. Expect to incur legal fees through the negotiation, even if you don't ultimately get the investment.

The **Canadian Venture Capital & Private Equity Association | CVCA** allows you to search for potential investors by sector category.

Pitchbook is a good resource for exploring the venture capital ecosystem.

The **Canadian Investment Network** (Canadian Investment network – Global network of Entrepreneurs, Angel Investors & VCs), **Canadian International Angel Investors** and **NACO Canada** can help to connect you with angel investors.

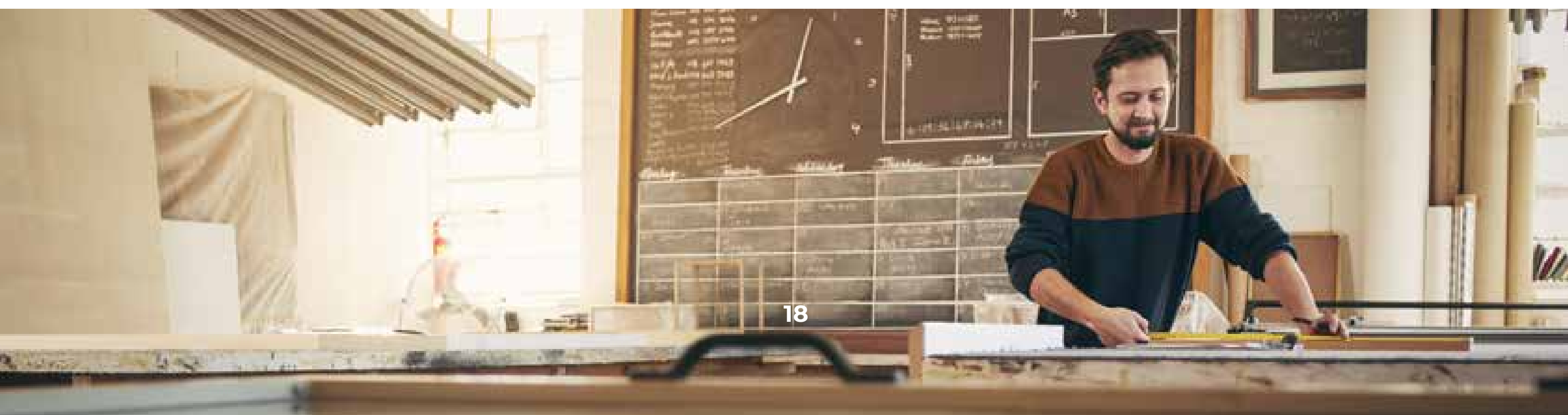
Canadian Angel Investment Foundation is a not-for profit organization that promotes best practices and education in this field. Connect with your local business incubator or accelerator to obtain advice about accessing the right type of investment for your business – they offer great resources and connections.

Other Forms of Equity

Government-Backed Corporations: Various levels of government offer programs and incentives for both investors to contribute capital and for high-growth companies to access investment.

Employees: You can leverage your employees as a source of equity financing by selling them stock and sharing control with them rather than with outside investors. This can offer a number of tax advantages and give employees a greater stake in the company's success.

Private Equity: Private equity makes medium to long-term investments in, or offers growth capital to, companies with high-growth potential. These investors usually make operational and other improvements, grow revenue through investment in product lines or new services, or encourage expansion into new markets. They normally sell their shares after 5 to 7 years.



THE PROS & CONS OF EQUITY FINANCING

It can be very valuable to have investors with aligned interests and expertise on board for your growth journey but it means giving up some control of your business.

PROS	CONS
Investors are committed to the business, even if plans change. The value of their investment grows alongside the business.	You may have a manage personality conflicts or differences of opinion about strategy with new partners. You'll no longer be fully in control of your business and will need to defer your choice to that of your investors.
They share risk – and return – by acquiring shares. If the business fails, you won't be on the hook to repay their investment.	Raising equity financing can trigger more elaborate legal and regulatory requirements. For example, raising capital in public markets comes with more disclosure and governance requirements.
The right angel or venture capital investors and bring valuable skills, experience, and contacts to the business.	Dividend payments are not tax deductible.
Investors are often prepared to provide follow-up funding as the business grows.	Legal costs can be incurred even if the investor does not agree to provide funds.

What to Know Before You Go

- Be prepared to "pitch" or promote your business to potential investors.
- Potential investors will scrutinize your past results and future forecasts, and investigate background information, including the management team.
- As the owner, your share in the business will be diluted. Depending on the nature and scope of the investment, shareholders may have a significant influence on major strategic decisions.
- Investors will expect regular updates and information to help them monitor their investment.

TIPS: PREPARE A WINNING PITCH

Prepare a strong Presentation

Craft a tightly focused presentation. Leave plenty of time for questions.

Start with a bang

Aim to make an impact within the first 2 minutes, or you risk losing the interest of potential investors.

Be prepared

An analysis of start-up pitch decks found that investors spent the longest on two slides: Financials and Team.

Keep it visual

Help data speak for itself with graphs and icons.

Use prototypes

Provide a visual example of your product so investors can see what they're being asked to invest in. If you don't have a working product, show a prototype, demo, or mock-up.

Polish & Practice

Put your best foot forward. A sloppy presentation won't reflect well on you or your business.

CROWDFUNDING

Crowdfunding, or peer-to-peer financing, uses online platforms like Kickstarter, or Indiegogo, among others, to raise money for a project or venture, usually from a large number of people who each contribute a relatively small amount.

Crowdfunding provides access to a wide pool of potential investors. It's also a great way for start-ups to get early market feedback.

TYPES OF CROWDFUNDING AVAILABLE TO BUSINESSES:

1 **REWARDS-BASED CROWDFUNDING**

Rewards-based crowdfunding is a popular and widely used type of crowdfunding. In this model, you seek contributions to develop and launch a new product. In exchange, contributors receive a reward such as a version of the product once it's developed, a T-shirt or trinket, or other reward.

2 **DEBT-BASED CROWDFUNDING**

Also called 'crowd lending' or 'peer-to-peer lending', allows businesses to borrow money from an online platform funded by many different investors.

3 **EQUITY-BASED CROWDFUNDING**

Equity-based crowdfunding is the offering of unregistered securities through a registered funding platform. It is similar to debt-based crowdfunding, only investors receive shares in the company in exchange for their investment. Investors make their money once the company is sold or listed on the stock market.

What to Know Before You Go

- Crowdfunding is usually 'fill or kill' which means that you have to hit your target to get any investment at all.
- Like any form of investment, crowdfunding requires a clear business plan and a compelling presentation.
- Do your research - The **National Crowdfunding & Fintech Association of Canada** is a great resource for businesses interested in crowdfunding.

GET ADVICE & SUPPORT

Community Futures South Georgian Bay can provide assistance in your financing journey. We are happy to help guide you as you move through the financing process, or refer to experts, organizations and other resources that can help. Also seek input from professionals including lawyers, bankers, accountants, and insurance brokers to support your business growth.