Sources Of Capital

- Debt or Equity financing

  Debt financing :- Obtaining borrowed funds for the company.

  - Asset-based financing ; requires some to be used as a collateral
  - Borrowed funds plus interest need to be paid back.

- Equity Financing :- Obtaining funds for the company in exchange for ownership.
  - Does not require collateral.
  - Offers Investors some form of ownership position.

- Factors affecting type of financing :-
  - Availability of funds.
  - Assets of the Venture.
  - Prevailing interest rates.
  - All financing requires some level of equity amount will vary by nature and size of venture.

- ## Internal or External Funds :-

  - Internally generated funds are most frequently employed ; sources include :
    - Profits .
    - Sale of assets and little-used assets .
    - Working capital reduction .
    - Accounts receivable .
  - Short-term internal source of funds :
    - Reducing short-term assets - inventory, cash, and other working-capital items.
    - Extended payment terms from suppliers
  - Criteria for evaluating external sources of funds :
    - Length of time the funds are available.
    - Costs involved .
    - Amount of company control lost .

- ## Personal Funds

  - Least expensive funds in terms of cost and control .
  - Essential in attracting outside funding .
  - Typical sources of personal funds :
    - Savings
    - Life insurance
    - Mortage on House or Car .

<u>Exit Strategy</u> :- Exit strategy includes -

(1) Initial public offering (IPO).

(2) Private sale of stock.

(3) Liquidation

(4) Merger with another company.

(5) Succession by family member or a non-family member.

<u>Succession of Business</u> :-

(1) Transfer to Family Members -

(i) Role of owner - full time / part time / retire.

(ii) Family Dynamics.

(iii) Transition business environment.

(iv) Treatment of loyal employee.

(v) Tax consequences

(2) Transfer to Non-Family Members -

(i) Train a key employee and retain some equity.

(ii) Retain control and hire a manager.

(iii) Sell the business outright.

<u>options</u> for <u>selling</u> the <u>Business</u> :-

<u>Direct Sale</u>.

Strategies to be considered - ① Focus on narrow, well-defined segment.

② control costs and focus on higher margins and profits

③ Get all financial statements in order.

④ Prepare a management documentation.

⑤ Assess the condition of capital equipment.

⑥ Get Tax Advice.

⑦ Get non-disclosures from key employees.

⑧ Try to maintain a good management team.

⑨ Prepare and plan in advance.

⑩ An important considerations is the type of payment the buyer will use.

⑪ Business brokers maybe helpful.

⑫ The best way to communicate the business to potential buyers is through the business plan.

⑬ The role of an entrepreneur may vary depending on the sale agreement or contract with the new owners(s).

Employee stock option Plan – ① Establish a new legal entity, an employee stock ownership trust.

② obligates the firm to repay the loan plus interest out of business cash flows.

③ Results in significant stock value for employees.

Management Buyout – ① Usually involves a direct sale of the venture for some predetermine price.

② To establish a price, entrepreneur should:
- Have an appraisal of all assets.

- Determine the good will value established from past revenue.

③ Sales of venture can be - (I) for cash
(II) financial through banks.
(III) Through sales of voting or or non-voting stock

Advantages -

① Motivates employee to put in extra time or effort.
② Provides a mechanisms to pay back loyal employees.
③ Allows transfer of business under a planned written agreement.
④ Permits the company to reap the advantages of deducting contributions on ESOP or any dividends paids.

Bankruptcy - Too much time and effort is spent on diversifying in markets where entrepreneur lack knowledge.
Bankruptcy protects entrepreneurs from creditors, not from competitors.
It is difficult to separate enterpreneur from the business. Entrepreneurs should file for bankruptcy early.

Bankruptcy needs to be shared with employees and everybody else is involved.

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