Sources of Finance

b.Com vi sem

prof.Vivek chavan

Dr.M.W.P.W.S. ARTS AND COMMERCE COLLEGE

Why do we need to study finance?

Almost half of ventures fail because of poor financial management

What is Finance?

- Who needs money?
  - Every one? you?
  - Can you or a business survive without cash? Why?
- So what is Finance?
  - First, how to have money
  - …

Personal finance

- Where does money for individuals (personal finance) come from:
  - Our own money in pocket
  - Borrows: from friends or credit cards
  - Received from Government if entitled to some benefits
  - Earned by doing something or sales of products and services

Business finance

- Business finance: a business has the same source of money for individuals
  - Its own money
  - Borrows: from friends, colleagues, banks and lending institutions
  - Received from Government grants. Eg. new in deprived sectors
  - Earned by sales of products and services
  - From venture capitalists (seeking profit for spare funds)
  - From private individuals (Business Angels – often seen in entertainment sector)
  - Private companies
  - Microloans

To obtain funding for a business project

- Determine how much money is needed to start your company
- Prove to your investor that your company requires the predetermined amount of money
- Offer incentives, interest, or collateral for the investor’s contribution
- Make arrangements to pay back the loan

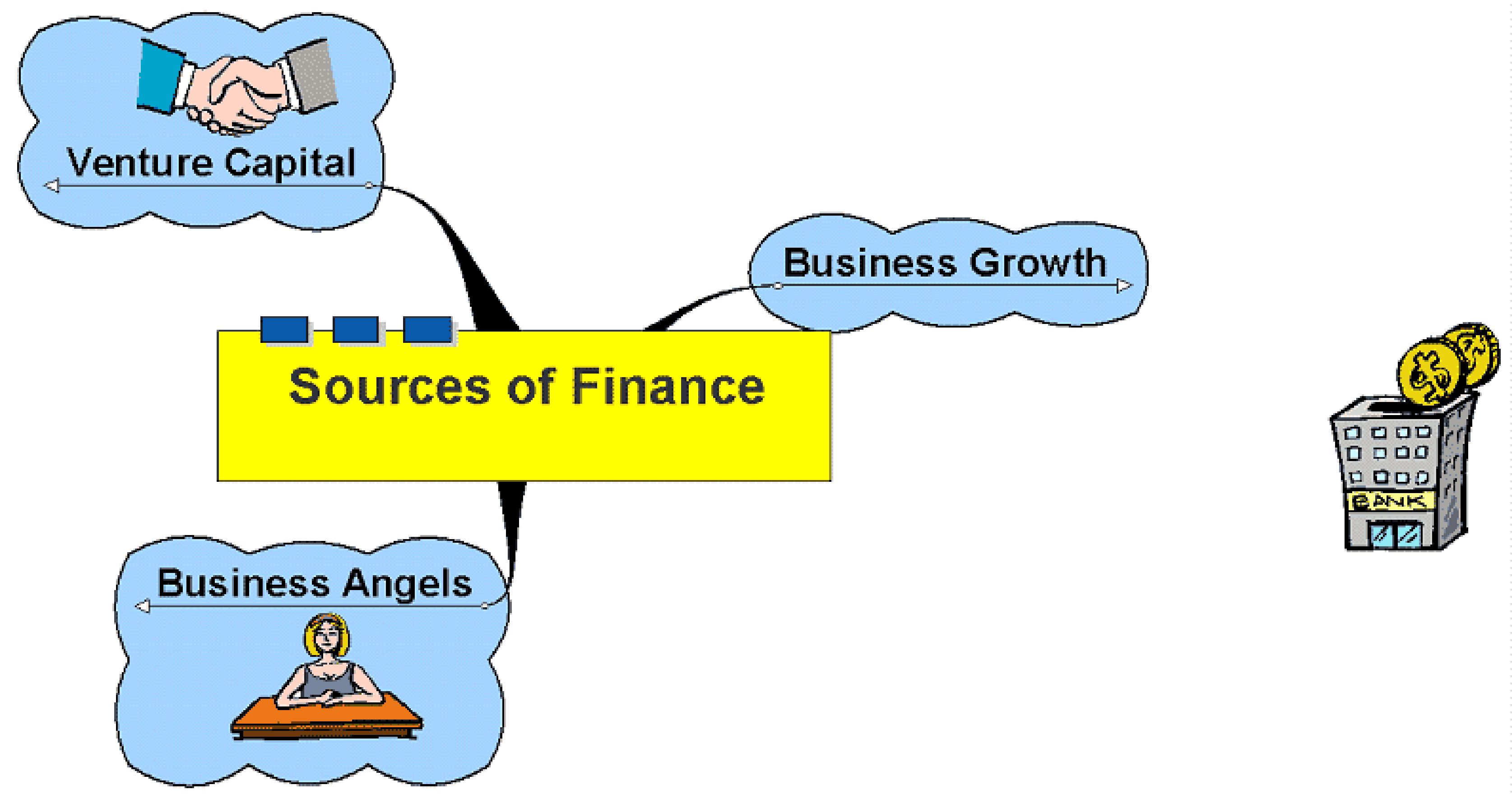
Classifying businesses

- Each type of business can have different ways to finance itself, so we need to look at types of business ownerships
  - Sole trader – owned by one person
  - Partnership – owned by two or more and based on agreement among them
  - Limited company: owned by two or more but separate in law from people who own and control

Business Forms

- Sole Proprietorships
- Partnerships
- Corporations
- Hybrids

Sources of Finance



Business Growth
External

- Long Term
- Short Term
- 'Inorganic Growth`

Business Growth External

- Long Term
  - Shares
    - Ordinary Shares
    - Preference Shares
    - New share issues
    - Rights Issue
    - Bonus or Scrip Issue
  - Loans
    - Debentures
    - Bank loans (mortgage)
    - Merchant or Investment Banks
    - Government/EU
      - Grants

Business Growth External

- Short Term
  - Bank loans
  - Overdraft facilities
  - Trade credit
  - Factoring
  - Invoice discounting
  - Leasing

Business Growth
External

- 'Inorganic Growth'
  - Acquisitions
    - Merger
    - Takeover

External Sources of Finance

- Long Term – may be paid back after many years or not at all!
- Short Term – used to cover fluctuations in cash flow
- ‘Inorganic Growth’ – growth generated by acquisition

Long term (Means?)

- Loans (Represent creditors to the company – not owners)
  - **Bank loans and mortgages** – suitable for small to medium sized firms where property or some other asset acts as security for the loan
    - A *mortgage loan* is a loan secured by real property
  - **Merchant or Investment Banks** – act on behalf of clients to organise and underwrite raising finance
  - **Government/EU** – may offer loans in certain circumstances
    - Grants

- Shares (Shareholders are part owners of a company only in PLC's)
  - **New Share Issues** – arranged by investment banks.

Short Term

- **Bank loans** – necessity of paying interest on the payment, repayment periods from 1 year upwards but generally no longer than 5 or 10 years at most
- **Overdraft facilities** – the right to be able to withdraw funds you do not currently have
  - Provides flexibility for a firm
  - Interest only paid on the amount overdrawn
  - Overdraft limit – the maximum amount allowed to be drawn - the firm does not have to use all of this limit
- **Trade credit** – Careful management of trade credit can help ease cash flow – usually between 28 and 90 days to pay
- **Factoring** – the sale of debt to a specialist firm who secures payment and charges a commission for the service.
- **Leasing** – provides the opportunity to secure the use of capital without ownership – effectively a hire agreement

thanks