chapter 12
A Firm’s Sources of Financing

PART 3
Developing the New Venture
Business Plan
The Nature of a Firm and Its Financing Sources

Factors That Determine Financing

- Firm’s Economic Potential
  - Growth Prospects & Profitability
- Company Size and Maturity
  - Life-cycle of Business
- Types of Assets
  - Tangible (physical) OR Intangible (IP, brand)
- Owner Preferences
  - Debt vs Equity
  - Tradeoffs
Debt vs. Equity - There is never a right or wrong answer
Exhibit 12.3 **Sources of Financing Funds**

- Personal Savings
- Friends and Family
- Other Individual Investors
- Commercial Banks
- Business Suppliers
- Asset-Based Lenders
- Government-Sponsored Programs
- Venture Capital Firms
- Community-Based Financial Institutions
- Large Corporations
- Public Sale of Stock
Large Corporations

This way in
Large corporations are eager to tap into the expertise of innovative entrepreneurs. To do so, many have established incubators or funds aimed at start-ups. Here’s a quick look at a few of those opportunities.

<table>
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<th>Nike</th>
<th>Microsoft</th>
<th>Pepsi</th>
<th>Johnson &amp; Johnson</th>
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<td>Nike teamed up with TechStars for a three-month program that mentors 10 start-ups that are building technologies for Nike’s activity-tracking devices, like its FuelBand. <strong>WHAT IT OFFERS:</strong> Each start-up gets a $20,000 investment from TechStars and the chance to pitch investors and Nike at the session’s end.</td>
<td>Microsoft also joined with TechStars to create a three-month incubator in Seattle for companies that are designing products for Microsoft Kinect and Windows Azure. <strong>WHAT IT OFFERS:</strong> Start-ups get mentorship, technical training and support, and the chance to pitch to angel investors and venture capitalists at the end of the program.</td>
<td>Pepsi’s PepsiCo10 is a digital incubator program that selects 10 tech start-ups in entertainment, mobile, retail, and sustainability. <strong>WHAT IT OFFERS:</strong> In addition to receiving funding, companies are matched with PepsiCo brands, such as Gatorade or Frito-Lay, for mentoring and pilot campaigns.</td>
<td>J&amp;J is creating four innovation centers—in Boston, London, Shanghai, and San Francisco—to fund early-stage life-science companies. It also created a biotech incubator in San Diego that houses 18 start-ups. <strong>WHAT IT OFFERS:</strong> Companies that rent at the San Diego incubator have access to office space, lab equipment, and mentoring.</td>
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[http://siliconbeachla.com/](http://siliconbeachla.com/) Go to Events for “Startups Socials”
Startup Financing for Inc. 500 Companies in 2003

- Personal Assets: 70%
- Family/Friends: 10%
- Bank Loans: 8%
- Business Angels: 4%
- Suppliers, Customers: 4%
- Government Loans: 2%
- Venture Capital: 2%

Bank Financing

Types of Loans

- Line of Credit
  - Revolving Credit Agreement
- Term Loans
- Mortgages
  - Chattel
  - Real Estate
Bankers’ Concerns

- How much the bank will earn on the loan?
- What is the likelihood that the debtor will be able to repay the loan?

The Five C’s of Credit

- **Character** of the borrower
- **Capacity** of the borrower to repay the loan
- **Capital** invested in the venture by the borrower
- **Conditions** of the industry and economy
- **Collateral** available to secure the loan
Loan recipients most likely to succeed

How Much does Credit Matter for Entrepreneurial Success in the United States? (December 18, 2012)

Cesare Fracassi University of Texas at Austin - Shimon Kogan University of Texas at Austin - Mark J. Garmaise University of California, Los Angeles (UCLA) - Anderson School of Management - Gabriel Natividad New York University (NYU) - Leonard N. Stern School of Business

Study Findings:

Entrepreneurs with

- High education,
- No prior senior management experience, and
- Plan to invest in something other than working capital

Make for the most attractive recipients of funds, from the point of view of either an early stage investor or a policy maker.
Crowdfunding

Many sites available that may help:

http://goo.gl/mk3UY

http://www.crowdfunding-website-reviews.com/
Your Credit Report

Understanding your Credit Report **FILM** (4 min)
Get your Credit Reports for FREE at:
https://www.annualcreditreport.com/cra/index.jsp

**FILM** Credit Report fraud alerts (3 min)
Get your FICO score
Free: Discover credit card (on statements)
For low price (not free):

**[LINK](https://www.myfico.com/Store/BureauSelection.aspx)**

**[FILM](#) FICO Score (3 min)**
Meeting with your banker (7 min)

1. What are the tips offered?
2. Which one tip is most meaningful to you? Why?
Financial Information Required for a Bank Loan

**Three years** of the firm’s historical statements
- Balance sheets, income statements, and statements of cash flow

**Pro forma financial statements**
- The timing and amounts of the debt repayment included as part of the forecasts

**Personal financial statements**
- The borrower’s personal net worth (assets – debts) and estimated annual income
Business Suppliers and Asset-Based Lenders

Accounts Payable (Trade Credit)

- Supplier-provided financing of inventory to a company, which sets up an account payable for the amount.
  - Short-duration financing (30 days)
  - Amount of credit available depends on type of firm and supplier’s willingness to extend credit
Small Business Administration (SBA) loans

- The 7 (a) Guaranty Loan Program
  - Video (2 min)
  - SBA guarantees repayment of loan to lender

- The Certified Development Company (CDC) 504 Loan Program

- The 7(m) Microloan Program

- Small Business Investment Companies (SBICs)

- Small Business Innovative Research (SBIR)