



Different Types Of Funding And Investments Available For Your Business

Description

Getting your business funded is about more than just having a [list of businesses that could potentially fund you](#). There are several different types of funders, and before committing, choose the best one for you. Some important options to consider are;

1. Qualification criteria for each source,
2. The total amount of funding you need,
3. The amount of ownership and control you are willing to cede for funds.

Once you've established these factors, you need to go through each option and pick one that ticks most boxes.

I say most because it's highly unlikely to find a funder who'll meet all your requirements, especially as a small business. Some of the options that will be available for you to choose from include;

[Government Grants](#)

[Angel Investors](#)

[Venture Capitalists](#)

[Traditional Loans](#)

[Traditional Equity Investors](#)

[Crowdfunding](#)

[Self Funding](#)

Business Partners

Government Grants

Many governments will have policies for the development of small businesses, and the South African government is no different. Because small businesses are viewed as a vehicle for economic growth, they get attention from policymakers.

Small businesses are at the centre of economic development and poverty affiliation and governments offer support. Though it's often argued that not enough is done to foster entrepreneurship, there are quite a few grants to consider.

Government grants vary widely in terms of requirements and terms, and some are even specific for particular sectors. The variation is particularly big when it comes to payment terms. Some may not require repayment at all, while some may seek competitive market rates.

Most government grants, however, tend to have more relaxed terms than traditional lenders, as they cater to marginalized individuals. These relaxed terms and accessibility make for a double-edged sword.

They result in a lot of entrepreneurs flocking for grants, which may significantly reduce your ability to get funded. This can extend even to entrepreneurs with strong ideas, strategies and policies.

And because they are designed for mostly marginalised members of the economy, they may disqualify your business even if it offers a great return. The best advantage, however, is that government grants tend to be a well-rounded funding source.

Because they are more concerned with the entrepreneur than the business, they tend to give more than just money. They may include mentorship, incubation, networking opportunities among other benefits a new entrepreneur may not otherwise get on their own.

Angel Investors

Angel investors are groups of wealthy investors who invest in small business in exchange for equity stakes. They sometimes band together to value projects and invest mutually, thereby minimizing their risk.

Angel investors tend to focus on industries they have experience in. Because of this, they can bring invaluable knowledge to the table. Some investors will actually stipulate that the entrepreneur should go through their mentorship before funds are given.

That in itself has given entrepreneurs a good strategy to get angel funding. It includes approaching an industry leader and asking for mentorship if the idea makes sense, it increases the chances of the mentor accepting to fund it.

Entrepreneurs are about growth by nature, and as such would be very willing to lend a hand to a young entrepreneur. Angel investors also increase your chances of meeting the right people, as they are likely to have built large networks.

Angel investors tend to consider a lot more factors than traditional lenders and apply flexible terms. Because of this, your business has a better chance of being funded by angel investors than, say, your bank.

The biggest drawback of this type of funding is the amount of equity you need to give up to get funded. Small businesses carry a lot of risks, and the returns angel investors demand are very high. You may be compelled to give up your equity for a fraction of what it would be worth in a very limited amount of time.

Venture Capitalists

Venture capitalists share similarities with angel investors, except they invest in companies to profit when they are sold. The sale could be an acquisition by another company or a public listing. Either way, there should be a detailed exit strategy that allows the venture capitalist to make a good return on their investment.

Venture capitalists are always looking for early-stage start-ups with very high growth potential. They then invest large sums of money into the business in return for a very high stake. At times, most of the time, they will demand a controlling stake for their capital.

There is very little autonomy in running a business under this scenario. Venture capitalists tend to drive business growth towards maximizing growth above anything else. This is so they can recoup their investment in the shortest amount of time possible.

While aggressively pursuing growth is not inherently a bad thing, it can detract from other equally important goals. It may result in you building a company that sacrifices longevity for short term goals.

Traditional Loans

Though not as accessible for small businesses as it is for their larger counterparts, term loans may be used as business finance. This involves any line of credit from a financial institution. Many financial institutions have small business products in their portfolios to improve accessibility.

While this does help, it doesn't alleviate the problem completely. The issue exists because financial institutions are designed to minimize their risk exposures to the fullest. Small businesses though are very risky investments.

Additionally, they tend to leave entrepreneurs in an unflattering financial position, with additional mortgages and credit card bills. As a result, small businesses tend to not only be unattractive investments, they usually don't meet the requirements. Unlike most other sources of funds, loans carry the advantage of not requiring any ownership to be given up.

Under loan agreements, you retain all ownership and control of your business. However, the strict repayment terms under loan agreements are a big risk factor. They can strain cash flows, and can even lead to premature liquidation during bad periods.

Traditional Equity Investors

You can always sell some shares in your business in return for funding. While it's highly unlikely you can do an [IPO\(Initial Public Offering\)](#) as a small business because of the strict requirements and costs, you should still be able to issue shares to those around you.

These could be family and friends or anyone that you know. While venture capitalists and angel investors are technically equity investors as well, traditional investors have more relaxed requirements. They may be willing to invest for a significantly longer period and not seek astronomical returns.

They may also be willing to not interrupt in the running of the business. Plus, you may be able to get funding for any sort of business if your idea resonates with investors. Angel investors and venture capitalists, on the other hand, tend to be most attracted to high growth tech companies.

Crowdfunding

Crowdfunding has shot up as a capital source in recent years. Crowdfunding relies upon appealing to a group of people who may benefit from your business and asking them to pool funds for it.

In some cases, it may simply entail telling a compelling story behind the business, and you can capture the hearts of funders. Crowdfunding has been responsible for the development of many products,

spawned many businesses and even funded personal needs.

Crowdfunding can be accessed from several online platforms such as [Kickstarter](#), [Indiegogo](#), [GoFundMe](#), and a whole lot more. These sites perform the task of connecting investors with those who need funds. Some may charge a small fee for facilitating your funding, but it's usually a manageable amount.

Furthermore, some may be specialized, catering for, say non-profits or tech companies. Crowdfunding usually doesn't involve paying back the funds, but some businesses may offer a perk in return.

Game developers, for example, give early access or free passes to funders as a reward for their funding. As a result, crowdfunding doesn't carry as much risk as other forms of funding. The biggest advantage to crowdfunding is it overcomes the limitations of traditional funding for small and medium businesses.

Factors such as creditworthiness or experience can be overcome if you are compelling enough to your target market. It also gives validation for the product; if you can convince people to invest in it, there should be a market.

Those early investors could actually also be your initial market. It can, however, be very tough and time-consuming to pitch a winning crowdfunding campaign. Plus, crowdfunders have a tendency to be attracted to shiny things, so more grounded and practical ideas may not stand out.

Moreover, truly visionary and unique ideas are at risk of being stolen. Because you have to share your full idea and strategy in your campaign, you may fall victim to those who already have the funds to bring it to life.

Self Funding

Self-funding is the least risky source of capital. You can self-fund by saving up from your other sources of income and ploughing into the business. Self-funding can also continue after the business has commenced operations.

You can, for example, establish a second source of income to sustain yourself. This would allow you to forego a salary or dividend, so you can reinvest profits into the business for growth. Self-funding can also include amounts you amass from friends and family.

These can, however, possibly have more conditions attached that funds you come up with alone. For entrepreneurs who are already employed and funding their business from their salary, it can be a little tough to determine the best time to retire.

A good rule of thumb is to;

1. Save up enough from your job to sustain you and the business should you have a bad revenue or cash flow month. The fund should ideally last at least 2 months, or any period you think it will take your business to recover.
2. Retire only if your business is making enough to pay you without strain. This could be the amount you are currently earning or an amount that allows you to maintain your current lifestyle.
3. If you are basing the amount on current earnings, don't forget allowances and benefits.

Self-funding allows the most freedom in the running of your business. It also carries the advantage of not having to give up part of your ownership to secure. Best of all though, in the event of the business failing, it has the least consequences.

While it can be devastating to have your savings wiped out from a failed investment, you don't have to worry about creditors knocking on your door. The biggest drawback to self-funding is its limited potential.

Unless you are already a multi-millionaire on to their tenth business, there's only so much you can raise. This can seriously increase your time to getting started and stifle your growth.

Self-funding is therefore ideal for business with limited capital requirements or that can apply the [lean start-up](#) model.

Business Partners

Taking on a business partner to secure more funding may be a lucrative option. It's an extension of self-funding, one that allows you to increase your funding potential significantly. Partners may be able to help with more than just liquid capital but may contribute skill as well.

These skills could be utilised within the business, reducing overheads by way of salaries. This does, however, need you to be willing to cede both ownership and control.

It's very unlikely to find a partner willing to plough time, effort and money into the business without the ability to influence its vision.

This may be a particularly sore spot should your visions significantly diverge, and has led to a few businesses closing down. Even where you want to formalise the agreement, it can be a bit tough to determine the best way to split ownership.

With traditional equity investors, you simply give them a proportion that corresponds to their capital contribution. Because business partners contribute more than just money, the division may not be as straight forward.

However, if you can find a partner you have a common vision and work ethic with, you might just have found more than just financial capital.

Conclusion

Not all funding sources are made equal and it's important to know what best suits your individual needs. Among the factors to consider are;

1. Availability
2. Repayment considerations
3. Ownership seeded
4. Cost of funding
5. Type of business

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