

Overtrading and running out of cash is one of the biggest problems facing fast-growing firms. Mark Crossfield of M3 Corporate Finance offers crucial advice to cash-strapped businesses seeking funding.

It is often assumed that every new order a business wins is a good thing – but this is not always the case.

Sometimes businesses grow so fast that they run out of cash and can no longer continue trading. This problem of overtrading - growing a firm without adequate funding in place to cope with the working capital requirements - is now one of the most common reasons for business failure.

Business owners will usually have a plan ready in case sales are not as high as expected. But even experienced managers sometimes fail to plan ahead if sales are much higher than expected.

This is surprising given that rapid growth can put a serious strain on cashflow and can prove fatal for fledgling firms. This is because cash is often burnt very quickly supplying goods and services to customers, but bills may not be paid for months – creating a hole in the company finances.

Businesses can avoid this potentially serious situation by planning their cash requirements carefully to ensure sustained and manageable growth. Your chances of successfully securing the finance you need will be greatly increased if you follow a few basic rules:

Compare offers - try a variety of institutions or types of lenders including banks, asset-based lenders, venture capitalists or business angels.

Bank overdrafts can be a quick source of working capital, but are generally a very expensive way of financing. Applying for bank loans may take more effort and time, but may well have a lower interest rate. They will also create a monthly outflow of cash in the form of interest and capital repayments that must be considered when planning future cash requirements.

Factoring is flexible and should support cash for growth, but is expensive. Invoice discounting is cheaper, but is offered to more financially robust businesses with good internal control systems and processes. Debt Factoring involves selling your debtors book to a third party, who will then collect those debts in themselves. Invoice discounting is similar, except you maintain the task of collecting the debt.

Venture capital is a more suitable option for fast-growing firms that are prepared to sell a stake in their business to raise finance. Be aware, however, that most venture capitalists expect to see a high return on their investment and will want to realise their profits within three to seven years. It is not appropriate for businesses needing smaller amounts of equity.

You should consider approaching a business angel if you are prepared to give up shares and some control in your business for a smaller lump sum, typically £50,000 upwards. Both venture capitalists and business angels will want to scrutinise you and your business closely to ensure they are not backing a losing horse.

Whatever avenue you decide to go down, get at least two offers on the table to compare so that you get the most competitive and flexible deal. Also be aware of the conditions that apply and what you need to do to meet them both now and in the future.

Don't leave it to the last minute - give yourself plenty of time because sourcing funding takes much longer than you think. Ensure that you are fully prepared for each stage of your funding application as you will be required to write business plans, provide up-to-date financial information and projections, as well as present your plans to potential funders.

It can take months to put an application together, present your case to funders, have your application approved and receive the cash. To minimise the delay, get your business plans and forecasts in order before making the application. Engaging a corporate finance advisor will speed up this process greatly.

Keep your proposal short and punchy

Make sure that your business plan explains the key business and market opportunities and don't get too bogged down in minute technical detail about your product or service. Your application should also include details of your skills and experience as well as information about the business. Remember, funders are just as interested in the person running the company as the business itself.

Know your audience

Ensure that your business plan is tailored to the funder. Venture capitalists will be more interested in the growth potential of your business, the key individuals and the likely return on their investment, while banks are more interested in the security you can offer and your cashflow. Banks specifically like to see stability and consistent results in your trading and business environment. Try to see your application from the funder's perspective and understand what elements of your application are most important to them.

Get personal

Be prepared to answer questions about your personal finances including personal income and domestic budget, particularly if you are asked to secure debt finance as is often the norm. You should also be prepared to offer some or all of your personal assets – such as your home and shares – as support for personal guarantees. Be aware that these assets are at risk if you are called up on your guarantees, although this is always after the assets of the business have been realised first.

Unlock the hidden assets in your balance sheet – you may find that you have certain assets - such as freehold property, trading assets, plant and stock – that can all be used to leverage finance. It is much easier for funders to lend you money if they have a “charge” on an asset. This allows them to recover some or all of the money they have lent and takes a lot of risk out of the transaction. If the cash generation of the business has been historically strong then there are also ways of gaining loans against future cash receipts.

Recruit an experienced advisor

Make sure that you seek professional advice before approaching funders. Your advisor should have a good understanding of the different finance options available and experience of working in the corporate finance world. Also, try to find an advisor who has established connections with a wide network of lenders and knows which institutions and people to approach for various types of financing

For more information about raising acquisition or growth finance, or buying or selling a business, call **M3** on **0845 2700345**, email info@m3cf.co.uk or visit www.m3cf.co.uk