

Alternatives to Bank Financing

In today's economy, using banks for financing business start-ups and expansion is not a viable option for many businesses given the banks' current lending requirements. The old adage that banks only lend money to those who do not need it definitely applies today. Here are some alternative sources of financing.

Family loans - These have the advantage that you do not have to go through the credit approval process you would with a bank; you may find that a number of family members are willing to contribute a small share which can add up to a significant amount. The primary disadvantage is that your relationship with family members changes when they become your creditors. If the business does not succeed, it is harder to explain this to family members who you see at Thanksgiving dinner, than to an investor with whom you only have a business relationship.

Micro loans – Small loans, normally under \$50,000, for start-up and/or newly established small businesses.

For more information see: <http://www.sba.gov/content/microloan-program>; www.accionusa.org; www.makemineamillion.org; <http://www.microloan.com>

Home equity - If you have enough equity in your home, you can apply for a home equity loan line of credit or a second mortgage and use this money to finance your business. The major disadvantage here is that this places your home at risk if the business fails.

Retirement plan funds - Under certain circumstances you can use money in your retirement accounts to finance business start-up costs. Check with a qualified accountant and attorney for advice here.

Equity financing - If you have a great business idea backed up with a solid business plan, you may be able to find an investor willing to provide financing in return for a share of the business. Ideally they would simply provide financing while you control the business operations and have the option to eventually buy out the investor.

Venture capital – This is financing provided to high risk, high growth potential early stage companies by investment firms that take a significant equity share combined with management role in the companies they invest in. This is the best known form of equity financing, but not the only one. About 60% of the money invested by traditional venture capital firms goes toward high-tech, software and bio-tech companies, according to the Money Tree Report published by Coopers & Lybrand L.L.P. The competition for venture capital investments is intense, but venture capital has helped finance companies that are now household names such as Amazon, Google and Facebook.

Angel investors - These are individuals who look to invest in businesses, often in their area of interest or expertise. The advantage is that angel investors have more flexibility than banks in deciding which businesses to fund and the terms of their agreements. Downsides are that one angel may not be able to supply all the funds you need and that, depending on your product, finding an angel investor may be difficult.

Resources: [Angel Capital Association](http://www.angelcapitalassociation.com); The Capital Network (www.thecapitalnetwork.com)

Small business investment companies (SBICs) - Much like venture capital firms, SBICs operate using money pooled from private businesses. However, they are licensed by the SBA to fill an important gap in the venture capital industry in that SBICs usually invest in main street businesses rather than high tech industries. See www.nasbic.org for more information.

Social lending groups - These are entities that facilitate person-to-person (P2P) lending and borrowing without using a traditional financial institution as an intermediary. Examples are: [Prosper](#) and [Lending Club](#).

Crowdfunding - This is similar to social lending except that the organizers are usually non-profit entities and the return to "investors" takes the form of gifts, recognition of sponsorship or a simple Thank You for Your Support, similar to a Patron of the Arts. Examples are: [Kickstarter](#), [RocketHub](#), [IndieGoGo](#); [Peerbackers](#) and [Funding4Learning](#).

Credit unions – Regulations for credit unions vary by state, in some states they are permitted to make commercial loans. If you are a member of a credit union, you may be able to get slightly better terms and interest rates than banks offer.

Grants – since grants do not have to be repaid, these are not available to most businesses. They do exist for businesses that meet certain criteria, such as high tech companies in select industries. You will want to check at the state and city levels rather than with Federal government for grants in most cases. Here is one resource: <http://www.businessgrants.org/>.

Susus – these groups are a more grassroots approach to raising capital, popular in the Caribbean and Asian communities. In a susu, a group of family members, friends or associates pools their money, and each person gets a turn at using the entire amount collected. For more information see: www.internationalcacci.com

Following are some alternative sources of cash for businesses that are already operational.

Equipment Sale-Leaseback - For a business that owns expensive equipment or machinery outright, one option is to find a lender who will buy the equipment for a lump sum and then lease it back to the business, in what's called a sale-leaseback.

Factors - They provide interim financing to small and mid-sized businesses by agreeing to purchase the business's outstanding receivables at a discount.

Merchant Cash Advance - A growing number of capital providers are willing to give businesses a lump sum upfront in exchange for a share of their future credit card sales.

Purchase Order Financing - A financing agent will advance money or issue a letter of credit against a signed purchase order for finished goods or value-added products to help fund manufacturing and fulfillment of the order. This is helpful for importers/exporters, for example, who must pay for their supplies immediately when placing orders for raw materials, but whose customers may take 60 days or more to pay. Once the goods are shipped to the customer and invoiced, the transaction is closed out.

Supplier financing - Suppliers have a vested interest in helping you meet your capital needs. Their flexibility with loans and credit lines translates into successful and loyal customers.

Additional Resources:

Venture Capital Directory: www.vcaonline.com; www.infon.com

Factors Chain International A global network of more than 250 leading factoring companies in 66 countries that seeks to facilitate trade through factoring and other financial services.

Commercial Finance Association - Industry association for more than 300 asset-based financial service firms in [North America](#).

North American Merchant Advance Association - Not-for-profit trade association representing organizations in the U.S. and [Canada](#) that provide working capital advance products based on credit, debit or other card and electronic payment-related revenue streams to small and mid-sized businesses.

Greater Newark Business Development Consortium - provides financing to small businesses
<http://online.wsj.com/article/SB123844971755171099.html>

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