



Business
LINK

Choose the right finance when starting up

Every new business needs money when starting up. The majority of businesses will need to buy equipment, establish the workplace and meet marketing costs - all before the first sale is made. Then once you're trading, you'll need cash to pay the bills and keep the business going.

There are a range of financing options when starting up and choosing the right ones for your needs is essential. You can use your own money, borrow from banks, family and friends or attract outside investors. Grants and government support may also be available.

Most businesses use a combination of these alternatives, according to their specific needs and circumstances.

This guide looks at how to work out how much money you need, the best financing options for your business and their advantages and disadvantages.

Work out your financial requirements

When starting your business, you need to prepare a business plan. This plan sets out how you intend to operate your business and includes essential financial forecasts. These forecasts will help you determine how much funding the business is likely to require, what it is needed for and when you will need the money. See our guide on how to prepare a business plan.

Good planning will also make it easier to raise the money you need. Use your business plan to explain your business to your bank and other potential sources of finance. A good plan helps convince investors that you know what you are doing and that it is worth risking their money backing you. See our guide on how to use your business plan to get funding.

How much will you need - and when?

It's essential to have an accurate idea of your financial needs. Once you have calculated the amount you'll need to cover your initial start-up costs, you'll also need to factor in your running expenses. Customers may not pay you immediately - but you will still need to pay all your bills to keep trading. It's sensible to have sufficient capital to cover projected expenses for at least six months.

Consider your own needs

At the same time, you need to make sure that you have taken into account how much money you need to live on. In the early stages, a new business is unlikely to produce spare cash that you can spend on yourself. See our guide: how do I survive until my business is off the ground?

Choose the best financial option

The type of finance you choose will depend on what kind of business you are starting, how much money you need and what you will use it for.

- Many people use their own **savings** or personal borrowings to fund the business. This may be the only choice if you can't convince anyone else to lend you money or invest in the business - see the page in this guide on how to use your own money to set up your business.
- **Family or friends** might back you. However you should carefully consider the risk that they could lose their money if your business fails - see the page in this guide on how to use finance from friends and family.
- If you have a credible business plan, you may be able to **borrow from a bank**. Many businesses use overdrafts for day-to-day borrowing and to manage cashflow, and loans to finance large purchases such as equipment. If your business is likely to have peaks and troughs in its cashflow, it's essential to be able to clearly illustrate these to your bank so you can plan an overdraft - see the page in this guide on how to use bank finance to start your business.
- A larger business with good prospects might attract **outside investors**. For example, 'business angels' typically invest £10,000 or more in exchange for a share in the business - see the page in this guide on how to get outside investors to help finance your business.
- You might qualify for a **grant** - for example, if you are setting up a business in a deprived area. See the page in this guide on grants and government support.
- If your business is setting up in a deprived area, or in a sector that is not normally catered for by mainstream lenders, you might be able to attract finance from a **community development finance institution**. Alternatively you might be able to attract support from other businesses in your peer group. See the page in this guide on other sources of finance.

Most businesses use a mixture of finance sources. For example, you might invest your own money in market research, bring in outside investors to share the risk and borrow from the bank to purchase equipment and machinery.

You can use our interactive tool to identify the right finance options for your business.

Use your own money to set up your business

If you're starting a new business, it's likely that you'll have to put up at least some of the money yourself. In fact, it's usually difficult to borrow from a bank or attract other investors unless you're also investing some of your own money.

The easiest way to provide your own financing is if you have savings you can use. If not, you'll have to think about other possibilities, such as:

- getting a mortgage, or second mortgage
- borrowing privately - see the page in this guide on how to use finance from friends and family
- getting an unsecured loan, or borrowing on credit cards
- selling possessions or assets

You should think carefully before borrowing to finance your business and should match the financing to your needs. For example, using credit cards for long-term expenditure can be crippling expensive, while some loans can be inflexible -

you could end up paying interest over many years.

Don't over-extend yourself. If you borrow too much, you may not have enough money left to cover your living costs while the business gets going. You should also try to leave a contingency fund, in case you need extra money to see you through a difficult period.

Advantages

Self-financing your business gives you far more control than other finance options. Outside investors or lenders could decide to withdraw their support at any time and most will expect a good return on their investment in the form of interest, shares or dividends.

Disadvantages

You must be aware of the risks. If your business fails you could lose your home and other personal possessions. And just knowing how much you have borrowed can put a lot of pressure on you and your family.

It's a good idea to take professional advice. Find your local Business Link using our Contacts Directory.

Use finance from friends and family

If you can't raise enough money to start your new business yourself, friends and family may be willing to help. They might lend money to you or to your new business or they might invest in your business, eg by buying shares. See the page in this guide on how to get outside investors to help finance your business.

You should provide potential investors with an up-to-date business plan. It will help demonstrate how their money will be used and explains the long-term plans for the business. You should also make sure that you have a written agreement in place that sets out terms and conditions, including any interest and repayment terms. This should help avoid misunderstandings.

There may also be tax implications for you and your family, especially on interest-bearing loans - see our guide on financing from friends and family.

Advantages

- Friends or family may be more willing to lend you money than a bank, particularly if you cannot provide security for a loan.
- Friends and family may offer easy terms - eg an interest-free loan.
- If you can raise some finance from your own resources or friends and family, it should make it easier to get additional finance from the bank.

Disadvantages

You need to be careful. You may feel under personal pressure, particularly if your business starts to struggle and there's a risk that friends or family will lose their money. Remember that they too may worry about their money and this may put a significant strain on your relationship.

You should never ask them to lend you more than they can afford to lose. You should also seriously reconsider whether your business is a viable prospect if

traditional lenders such as banks are unwilling to lend you money to start up.

It is wise for both sides to take professional advice before proceeding with any agreement. You should consult your financial adviser or solicitor. Find a solicitor that participates in the Lawyers for Your Business scheme on the Law Society website - [Opens in a new window.](#)

Use bank finance to start your business

Overdrafts and bank loans are the most common sources of additional finance.

Before lending, a bank will want to know that you are a good risk. Typically, the bank will want you to:

- present a credible business plan
- provide evidence that you have a successful track record in business
- offer security for any money it lends you - either business assets or a personal guarantee
- invest some money in the business yourself

If you don't meet all the bank's normal requirements, you may qualify for a loan under the Enterprise Finance Guarantee scheme. For more information, see our guide on bank finance.

Whatever type of borrowing you use, you may have to pay arrangement fees as well as interest.

Many small businesses use an overdraft to cover their borrowing needs. If you need longer term financing, it's a good idea to consider taking out a loan.

Advantages and disadvantages of overdrafts and loans

Borrowing method	Advantages	Disadvantages
Overdraft	<ul style="list-style-type: none"> • a flexible way of funding your day-to-day financial requirements • interest is only payable on the amount you are overdrawn 	<ul style="list-style-type: none"> • higher interest rates than loans • leaves you with no contingency funds if you are regularly overdrawn • bank can ask for repayment at any time
Loan	<ul style="list-style-type: none"> • you can match the term of a loan to your requirements • easier to budget for repayments 	<ul style="list-style-type: none"> • no flexibility - you could be paying interest on funds you are not using • the need for regular payments could cause cashflow problems • you may have to offer some form of security - either a business asset or a personal guarantee

For more information, see our guide to bank finance.

Always take advice from your accountant or business adviser to ensure the loan meets your requirements and you understand the terms before signing any agreement.

If you are refused finance - Business Link financial intermediary service

There is no guarantee that your application for finance will be successful. If you have had difficulty accessing bank finance, Business Link offers a financial intermediary service.

The service helps businesses review possible reasons why funding was not granted, especially if lender feedback has been limited or where the decision appears arbitrary or inconsistent.

If you are eligible for this service, Business Link advisers can help you to build a stronger relationship with your business' bank, guide you on what to do when seeking finance and offer support with other access to finance issues.

Find your local Business Link through our Contacts Directory.

Get outside investors to help finance your business

You might want to bring in outside investors. If the business does well, they share in the profits - but if the business fails, they lose their money.

Typically, your company issues ordinary shares (standard shares with no special rights or restrictions) to investors in return for their capital. See our guide to shares and shareholders.

Outside investment can suit promising businesses that do not expect to produce a lot of spare cash in the short term but offer the potential of greater returns over the longer term.

Advantages

- Attractive for businesses looking to bring in additional expertise as well as funding.
- Unlike loans and overdrafts, you do not normally have to make payments to investors until the business can afford them.
- Increasing the capital invested in the business makes it easier to borrow from the bank.

Disadvantages

- Your share of the business, and of its profits, will be lower.
- Investors may want control over how you manage the business.
- Investors may want the business structured in a way that makes it easier to sell their shares in the future.

Sources of investment

There are several different sources of investment:

- **individuals**, such as friends and business contacts
- **business angels**
- investment funds and **venture capitalists** for larger investments

Business angels are wealthy individuals who typically invest £10,000 upwards and who may also offer business expertise. Venture capitalists usually invest more than £2 million in businesses where they believe they will receive a high

return on their investment by exiting (selling their investment) at a certain time.

Before approaching potential investors you need a good business plan, including evidence of your management ability. Your plan should include detailed financial forecasts and demonstrate what you will do with funds invested in the business. You will also need to prepare a pitch, which will sell your business to potential investors. See our guide to equity finance.

Grants and government support

Your business may qualify for a grant or government support to help you get started.

The main advantage of grants is cheap financing. For example, you might get a subsidised or zero-interest loan, or even an outright cash grant. In addition, support schemes can provide expert advice, information or subsidised consultancy.

However there are drawbacks:

- there is strong competition for grant schemes - you may spend a lot of time on an application which is not successful
- you must meet the scheme's criteria - such as business location and size, and how you plan to use the money
- the application procedure can be complex and drawn out
- you normally have to use the grant for a specific project, rather than general business costs
- grants usually only cover a percentage of the costs - you also have to provide matching funds

The government provides several Solutions for Business financial products that might help you get your business started.

Understanding Finance for Business provides entrepreneurs and businesses with advice and support to ensure they understand their options for getting the money they need to start, sustain and grow. You will also be introduced to potential sources of finance.

The **Enterprise Finance Guarantee** helps viable businesses that would not normally qualify to get a loan due to lack of security or track record. See our guide on bank finance.

Small Loans for Business offers loans of up to £50,000 to small and medium-sized businesses that have viable business plans but have been refused bank finance.

Finance for Business offers flexible finance solutions such as loans and equity finance for businesses with viable business plans that are unable to get support from commercial banks and investors.

These products are subject to specific availability and may not be available in all regions. To find out if you can benefit from these Solutions for Business products and for more options Search our business support finder for grants, loans, expertise and advice for which your business may be eligible or contact your local Business Link Helpline on Tel 0845 600 9 006.

Solutions for Business is only available in England. Government support for business is different in Scotland, Wales and Northern Ireland.

For more information, read our guide government support for businesses.

Regional Employer National Insurance contributions (NICs) holiday for new businesses

New businesses may also be able to benefit from the government's Regional Employer NICs holiday scheme. This may entitle you to a reduction in your national insurance contributions. For more information, see our guide on regional employer NICs holiday for new businesses.

Other sources of finance

Many start-up businesses do not require a great deal of money to get up and running. These small amounts of finance - known as micro finance or micro credit - are often not available through traditional lending sources.

If your business is setting up in a disadvantaged area or a sector that is typically underserved by mainstream lenders, you may be able to secure finance or support from one of the alternative sources of micro finance. These include community development finance institutions (CDFIs). Alternatively, support might come through other companies in your peer group.

CDFIs are sustainable, independent organisations established to develop and create wealth in disadvantaged communities or markets. They provide capital and support to individuals, micro enterprises and small businesses.

A loan from a CDFI can be used to purchase equipment or property, to finance working or start-up capital or to fund marketing campaigns. Loans can be for as little as £50 or up to £1 million depending on the project. Find out about CDFIs on the Community Development Finance Association website - [Opens in a new window](#).

Some businesses find that they can access finance, support and advice from other businesses in their peer group - known as peer-group lenders. There are many organisations that have been set up to support specific groups of individuals and businesses. These include:

- Prowess - the UK association of businesses and individuals that specifically support women in business. See our guide on starting a business - advice for women. Find out about the support available to women in business on the Prowess website - [Opens in a new window](#).
- The Asian Business Development Network (ABDN) Ethnic Minority Enterprise Network - assists Asian and minority businesses by creating access to opportunities and sharing best practice. Read about the Ethnic Minority Enterprise Network on the ABDN website - [Opens in a new window](#).
- The Black Business Initiative (BBI) - aims to support the black and minority business community. Find information on the services provided by the BBI on the BBI website - [Opens in a new window](#).

See our guide on starting a business as a minority ethnic person.

For more information about raising finance for your business, see our videos about understanding business finance on the Business Link YouTube channel - [Opens in a new window](#).

Here's how I found the right sort of finance for my new business

Tabitha Potts

Mimimyne - Opens in a new window

Tabitha's top tips:

- "Do as much research as possible. You can never have too much information."
 - "See what's available locally. A lot of things are dependent on your postcode."
 - "When giving a presentation, dress comfortably and relax."
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Mimimyne, a London-based online retailer of eco-friendly children's products, started trading in September 2008. The company's managing director, Tabitha Potts, wanted her business to have a high-quality website to reflect the design and workmanship of the products she planned to sell. Here Tabitha explains how she found the finance she needed to set up her business.

What I did

Considered all options

"I researched every option and looked into a range of different sources of finance. I've worked as a researcher, so I'm good at finding information and sifting through it quickly. I did it all on the internet.

"I didn't want to approach family and friends because I was looking for about £10,000, which I thought was an awful lot to ask for. I also didn't want to mix my personal and business affairs."

Searched for grants

"I used the Business and IP Centre at the British Library, which has a grant and funding database, as well as Grantnet, J4B Grants and Business Link to find grants, but I couldn't find anything suitable for me.

"A couple of them offered small sums, while others were either for small charities and social enterprises, or for large companies trying to go green. But I wasn't eligible."

Pitched for loans

"I then approached banks. I only wanted to go to an ethical bank, but Triodos and the Co-operative Bank both wanted match funding, which I wasn't able to provide.

"Next I went to Fair Finance, which offers community loans in my area. They were helpful but I had to offer my house as security and I didn't feel comfortable with that. I even went to an ethical business angel but I was too small to be considered.

"Then I met with the East London Small Business Centre (ELSBC). I presented to about ten people, but I treated the pitch like a conversation and I knew my financial projections and the figures in my marketing plan.

"I now have a £10,000 loan from the ELSBC through Deutsche Bank. It has to be repaid over three years. They have been very helpful and given me a couple of months' payment holiday while I set things up."

What I'd do differently

I'd ask for a bigger loan

"I underestimated costs. For example, there were some things I just hadn't anticipated, such as the cost of going to trade shows where I had to pay for everything, from an awning to price tags."

Business Link Helpline

0845 600 9 006

Related guides on businesslink.gov.uk

Use our interactive tool to identify the right finance options for your business

Manage your personal list of starting-up tasks with our Business start-up organiser

Search our business support finder for grants, loans, expertise and advice for which your business may be eligible

Download our sample cashflow projection spreadsheet (XLS, 83K)

Starting a business when economic conditions are tough

Prepare a business plan

Use your business plan to get funding

An innovation start-up

How do I survive until my business is off the ground?

Financing from friends and family

Bank finance

Grants: the basics

Shares and shareholders

Equity finance

Choose and work with an accountant

Debit and credit cards for your business

Commercial mortgages and lenders

Choose and work with a solicitor

Use our interactive tool to assess your eligibility for government guaranteed lending schemes

Government support for businesses

Innovation, research and development grants

Regional employer NICs holiday for new businesses

Starting a business - advice for women

Starting a business as a minority ethnic person

Related web sites you might find useful

Business plan templates on the Microsoft Office website

<http://office.microsoft.com/en-gb/templates/CT010253062.aspx>

Sample business plans on the Bplans website

http://www.bplans.co.uk/sample_business_plans.cfm

Download an equity finance overview from the British Private Equity and Venture Capital Association website (PDF, 407K)

http://admin.bvca.co.uk/library/documents/Guide_to_private_equity.pdf

Business angel guidance on the British Business Angels Association website

<http://www.bbaa.org.uk/index.php?id=1>

Women in business support on the Prowess website

<http://www.prowess.org.uk/support/support.asp>

Ethnic minority support on the ABDN website

<http://www.abdn.org.uk/>

Support services for ethnic minority businesses on the BBI website

<http://www.bbinitiative.com/>

Find a course on working to a budget on the learndirect business website

<http://www1.learndirect-business.com/business-courses/working-to-a-budget/>

Business finance videos on the Business Link YouTube channel

<http://www.youtube.com/BusinessLinkGov>

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