**KEYWORDS**

**Debt Finance -** This is money that is borrowed that has to be repaid with interest

**Equity Finance -** This is money that is usually got from selling

shares. It is the owners capital

**Working Capital** - This is the money that a business uses for the

day-to-day running of a business Working capital is calculate by

using the following formula - Current Assets – Current Liabilities

**Liquidity** - This is the business ability to repay debts as they fall

due. It is about cashflow and if the business can pay its day-to-

day expenses.

**Debtors-** These are the customer who owe use money. We have

sold goods to them on credit

**Stock**- This is making sure that the business has the optimum

level of stock. This is not having to little or too much stock.

**Cashflow** - this is like a household budget but for a business. It

shows the expected monthly income and expenditure. It helps to

identify future surplus and deficits

**SELF TEST QUESTIONS**

1. Understand the different financial needs of a business

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2. Explain the different types of short, medium- and long-term sources of finance

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3. Describe the factors a bank considers before giving a loan

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4. Define the term Working Capital

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5. Prepare and analyse a cash flow forecast

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**SHORT TERM SOURCE OF FINANCE**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Cash** | **Bank Overdraft** | **Accrued Expenses** | **Trade Credit** | **Credit Card** | **Invoice Discounting** | **Factoring** |
| Using the cash the company has to pay debt. | This is an agreement with the bank to withdraw money that you don’t have in your current account up to a certain limit.  You pay interest on the overdrawn amount | This is also known as deferred payment. You don’t pay a bill when you get it but leave it to the last minute.  It can affect you credit rating. | This means buying now paying for them at a later date.  If you pay before the date you will receive a discount.  Interest can be charge on overdrawn amounts | This is buying now and paying for them at a later date.  The credit card company will pay for the purchase and you will pay the credit card company back with interest.  It is can be very expensive | This is borrowing money based on payment from an invoice.  The business will collect payment and will use this to repay the loan.  Interest can be charge on overdrawn amounts | This is when a business sells a debt to a factoring company for less value of the amount owed. They used this money to pay bill and the factoring company will get the full value from the debtor |

**WHAT ARE THE FINANICAL NEEDS OF A BUSINESS**

**Short Term needs** -These are needs that must be repaid within 12 months (0-12 Months). Example include Wages, Insurance Rent. They are usually current expenditure. Current expenditure is day to day expenditure.

**Medium Term Needs** -These are needs that must be repaid within 1-5 years. Example include buying vehicles. They are usually capital expenditure. Capital expenditure is once off expenditure.

**Long Term Needs** -These are needs that must be repaid within over 5 years. Example include buying premises. They are usually capital expenditure.

**Matching principal -** The matching principal states that the short, medium- and long-term needs should match the short, medium and long term source finance

Consumer

**LONG TERM SOURCE OF FINANCE**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Share Capital** | **Venture Capital** | **Retained Earnings** | **Grants** | **Debentures** | **Mortgage** | **Crowd Funding** |
| This is money that is  invested into the  business by  its shareholders.  In return for this  they will receive a  dividend. | This is like dragon  They invest in new or  high-risk business.  They will sit on the  board of directors  The investors will  look for a high  return on their  investment. | This is when the  business puts the  profits from the  year back into the  business.  This is a form of equity finance. There are no interest repayment or loss of control | This is money given by the Government to a specific purpose.  There is no interest charged as long as the money is used for the intended purpose. | This is s long term  loan that has to be  paid back a specific  date in the future.  They will have to pay  back interest each  year. There is no loss  of control, but  security will be  required | This is s loan that is used to purchase a premise.  It is usually paid back between 25-30 years  If the business can’t repay the mortgage, they may loss the premises. | This is asking  investors for small  amount of money for  which they will  receive a reward  It can be hard to  raise finance this  way. A share of  the profits may be given to investors |

**LOAN APPLICAION FOR A BUSIENSS**

**The purpose of the loan** – What does the business require the loan for. Will the loan help the business to be in a better position. Can the business repay it

**A Business Plan** – This will set out the vision for the business and help the bank understand the future projection of the business

**Collateral** – A bank may require some form of security. This will be sold if the business fails to repay the loan

**Credit History** – The bank will make a credit check on the business to see if they had got out previous loans and if they were repaid

**Own Investment** – The banks like to see the business put up some of the money themselves. This means the business will share the risk.

**MEDIUM TERM SOURCE OF FINANCE**

|  |  |  |
| --- | --- | --- |
| **Leasing** | **Hire Purchases** | **Term Loan** |
| This is renting an  asset form a firm  It allows the  company to use the  asset as long as they  pay regular  payments.  It is a legally binding  agreement.  is expensive as you never own the asset | This is when a business pays a deposit for an asset, then a finance firm pays the balance. The business pays back the finance company with interest. The business doesn’t own the asset until the last instalment is paid | This is usually a loan from a financial institution. The business swill make fixed repayment to the financial institution until the loan is repaid. This repayment includes the interest plus the loan repayment amount. |

**HOW TO CHOOSE A SOURCE OF FINANCE**

**The purpose of the finance –** What is the finance needs for is it short term, medium term or long term

**The amount of finance required –** How much do you need. It is important not to get too much because you will have to pay back interest, and this is expensive

**Cost of Finance -** This is known as the financial Cost. The company should compare the APR of different financial institution

**Control –** will the company lose control of their business r

**Security –** will the company have to give Collateral in case

|  |  |  |  |
| --- | --- | --- | --- |
|  | May | June | July |
| Income | 1500 | 2000 | 2500 |
| Expenditure | 1600 | 1700 | 1500 |
| Net Cash | (100) | 300 | 500 |
| Opening Cash | 1000 | 900 | 1200 |
| Closing Cash | 900 | 1200 | 1700 |

**SUCCESS CRITERIA**

Step 1 Input relevant income figure into the budget and add up the figure to get the total for each month (A)

Step 2 Input relevant figure for fixed (regular) expenditure into the budget and add up the figure to get the total amount for fixed (regular) expenditure for each month

Step 3 Input relevant figure for irregular expenditure into the budget and add up the figure to get the total amount for irregular expenditure for each month

Step 3 Input relevant figure for discretionary expenditure into the budget and add up the figure to get the total amount for discretionary expenditure for each month

Step 4 Add up the totals for regular, irregular and discretionary expenditure (B)

Step 5 To calculate net cash take the figure from step 4 away from the figure in step 41

Step 6 Enter the opening balance as per the question (if none is given leave it blank)

Step 7 The closing balance is calculated by adding the opening balance to the net balance. This will give the closing balance

Step 8 The closing balance for one month become the opening balance for the next month and repeat step 7

Step 9 the balance for the Total Column must be the same as the balance for the last month in the budget