Raising business capital and funding innovation

Raising capital is one of the most important aspects of starting and building a successful business. While there are a variety of sources that may supply your business with the essential funds to develop and grow, it is critical to understand the expectations and requirements of investors.

Before approaching anyone for funding for your business, you should determine how much money is needed to support a range of business functions, from ongoing operations to growth objectives. This requires a comprehensive understanding of the capital requirements of the business, such as purchasing new equipment, hiring new employees and expanding office space, and how capital will help the business follow its business plan and achieve short and long-term goals.

There are a number of different sources of business capital, such as private investors, financial institutions, venture capitalists, accelerators and government grants. Which source you choose may depend on where your business is in the business life cycle. Some are more popular for businesses that are in the start-up phase or progressing into the growth phase.

Private sources

Business owners often approach individuals for money – from friends, relatives, a spouse or partner, business contacts, employees and private or "angel" investors. When approaching any of these private sources, there are certain considerations that one should keep in mind.

Individuals who are willing to invest in your business are rarely "silent" and may offer management or policy assistance, to provide contacts or to help with special assignments. Private investors tend to value equity – the right to participate in the future of your business. It is worth noting that the financial gain may be balanced by a certain loss of ownership. Individual investments often come with a highly personal relationship with the investor. If you are setting up a partnership, consider supplementing areas of weakness in the business with individual investors that have strong and complementary experiences.

A written shareholder or partnership agreement is essential when raising capital from financial backers or partners. This agreement will stipulate the rights and obligations of the shareholders or partners of the private business and will also include "buy-sell" provisions. It is important to review all agreements with your legal counsel.

Financial institutions

Although Canadian chartered banks are primarily concerned with short and long-term lending, they also often provide other financing options such as term loans, leasing, mortgages, factoring and support services such as payroll, letters of credit, credit references, and more.

To secure funding from financial institutions, a financial proposal and business plan are most often required. The bank will review facts and figures from statements, records and projections. They need to be sure of the stability of your company and the commitment of the owners.

They will look at your past and present performance, future potential, the amount you have invested, the amount you have left (equity and retained earnings) and the way you run the company. The bank will want proof of your ability to service the debt – that is, to pay the interest and retire the loan on time. They may require security or collateral that can involve the pledging of accounts receivable or inventory, and a personal guarantee of principal. Term loans often require fixed or tangible assets as security.

It is important to keep lines of communication open. Tell your business banking professional in advance if there's bad news coming – the bank's confidence in you will remain strong if you're straightforward. Prepare and share a cash flow budget, and keep your banking professional in the loop each month, even when you're not borrowing. To establish a credit record, borrow from your bank early in your business cycle.

Your banking professional can be a valuable contact and key partner to your business's success. They could offer support to your business beyond financing, such as cash management solutions that improve or create cash flow as an alternative to an operating line.

Your banking professional may also be aware of local economic conditions and suggest potential opportunities in other areas. They can introduce you to prospective customers and suppliers and help you with credit checks. Your banking professional can be your best business friend. Discuss future financing needs with them and take the time to nurture a good business relationship.

Venture capital

Venture capitalists will invest directly in a business if they believe that a business will be profitable and has potential for substantial growth. Almost all deals are based on equity or some form of subordinated debt with conversion or option rights. (This means that in case of bankruptcy, their loans rank behind all other secured creditors but ahead of other shareholder loans.)

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Venture capital companies expect high returns and usually want substantial minority positions – 20% to 40% of shares, or even full control of start-ups. They expect management shareholders to be fully committed financially, providing an efficient, balanced management team.

Venture capital companies can help in several ways, including planning and policy, finance and control, and arranging mergers and acquisitions or an IPO (initial public offering). They will likely require a seat on the board, to attend regular board meetings, monthly statements, life insurance for the owner, involvement in the budgeting process, and a "buy-sell" agreement covering your shares and their shares. Most venture investments usually require more funds to be invested later as the business progresses. Ensure the venture capital company has a good reputation and is well financed.

Venture capital companies may be found in listings on the federal government's website. Check with your provincial department for industry or commerce to see what's available locally. Most provinces or regions have some form of venture capital program providing relatively small amounts of money to start-ups.

Accelerators

Accelerators are programs that are offered to start-up companies in particular. These programs offer business capital and the opportunity to work alongside other start-up companies with the potential for accelerated growth, all in exchange for equity. Connecting with an accelerator is a very competitive market, but successful participation can be very advantageous. Accelerators are usually composed of successful entrepreneurs who will offer advice, office space and access to advisors and operators of other successful start-ups.

Governments

Federal and provincial governments have loan, guarantee or grant programs for creating jobs, increasing capacity, and creating or upgrading technology.

When seeking government financing, you may need to show you can't get the funds elsewhere. Try to tailor your needs to the program and ask for help from the program officers.

Improving and growing your business with innovation

Many business owners raise capital to foster innovation in their company. Innovation may help to gain market share, introduce new products and to become more profitable. To drive your business forward profitably, additional capital may be required to implement innovation.

Business owners can fund innovation from a variety of sources:

- Ongoing cash flow
- Business loans from commercial or private sources
- Government grants
- The business owner's own resources, or financial support from family and friends

There is a network of accelerators, incubators and hubs that allows entrepreneurs to work with experienced mentors in supportive environments and can also assist in attracting funding. For example, the Canada Business Network, a collaboration between the federal government, provincial governments and not-for-profits, supports a wide variety of businesses from start-up to the growth phase. Organizations that support coaching, mentoring and training across the country can be found on the Canada Business Network website.

Seek out and take advantage of all that is out there **to help you build your business**

Conclusion

Seek out and take advantage of all that is out there to help you build your business. Not only sources of funding, but also the invaluable knowledge and learning from experienced business owners that have been there before. Speak with your BMO financial professional to learn more about your options for raising capital and how it can work for you and your business.

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