Erasmus+

O-CITY

Creativity + Innovation & Technology

**LESSON CONTENT TEMPLATE**

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## 1. Template

Topic 3: Financing a Business
Lesson 2

**Sources of Debt Financing and Equity Financing**

**Introduction**

Funding is needed to start a business. There are several sources to consider when seeking initial funding. The financial needs of a company are depending on the type and size of the company. Once the topic is completed and approved, learners will be able to…make a difference between Debt Financing and Equity Financing.

In this lesson, we will talk more about Debt and Equity Financing, which are the two main sources of financing.


Resource: Pixabay

**Sources of Debt Financing**

**Property-backed loans** are secured by real assets and include mortgages, equipment loans, and inventory loans.

**Unsecured business loans**, such as term loans, do not require any real assets as collateral and are often used to finance working capital, business expansion, and acquisition.



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**Lines of credit** are temporary, short-term unsecured loans that are common it is used for seasonal cash needs or for emergency funds.

**Factoring**, technically (legally) is not a loan. Companies specializing in factoring receivables, purchase orders factoring and a cash advance in a company or merchant provide cash to business owners in exchange for future revenue or customer payments.

**Banks**, from large commercial banks to local savings and loans, have traditionally been the primary source of financing for small businesses. (*Book Entrepreneurial Finance Concepts and Cases*, 2020).

**Peer-to-peer** (P2P) lending is a relatively new source of debt financing for individuals and businesses. (*Book Entrepreneurial Finance Concepts and Cases*, 2020).The business model of most P2P lending companies is the direct connection between small businesses and individual borrowers with investors.

**Accounts Receivable Financing**, also known as account financing or accounts receivables factoring, is another source of funds for small businesses.
There are two types of receivables financing:

1. Non-recourse factoring (Financing company takes responsibility for collecting payments from the business' customers)
2. Recourse factoring (Financing company purchases account receivables from the business, but in the event of non-payment by customers, the business has to buy back these bad accounts receivables)

**Merchant Cash Advance** - Variety of small business financing options characterized by short payment deadlines and small regular payments.



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Resource: [Pixabay]

**Sources of Equity Financing**

**Angel Investors** - Highly regarded person who provides financial support to small startups or entrepreneurs, usually in exchange for capital in the company.

**SBA – Small Business Investment Company (SBIC)** - Small business investment companies supply small businesses with financing in both equity and debt. (*Book Entrepreneurial Finance Concepts and Cases*, 2020).

**Venture capital** - The type of financing that investors provide to startups and small businesses that they believe have long-term growth potential. (*Venture Capital*, 2020).

**Crowdfunding** - The practice of financing a project or venture by raising money from a large number of people who contribute a relatively small amount, usually through the Internet.(*Crowdfunding*).

**Conclusions**

An entrepreneur's dream or idea cannot be realized without some kind of cash flow into the business. For a start-up, it usually starts with a certain stakeholder investment, and can also include money from friends or family members. As the



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business grows, the property will have to turn to a third party for additional funding. Each option has its advantages and disadvantages that must be taken into account when assessing the financial needs of the company for both its short-term and long-term goals.



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