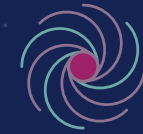


THE HITCH-HIKER'S GUIDE TO

FUNDING READINESS

FOR SMMEs



**Western Cape
Government**

Economic Development
and Tourism

THE HITCH-HIKER'S GUIDE TO

FUNDING READINESS FOR SMMES



1. Understand the funding eco*system.



2. Understand the funder mandates.



3. Identify the correct form of funding.



4. Document your problem/opportunity.



5. Plot and link your needs to the funder's mandate and form of funding.



6. Prepare for application.



7. Build a data-room.



9. What to expect in a due diligence.



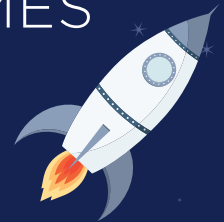
11. Credit Committee/ Approval Stage.



12. Disbursement.



10. Success factors of a due diligence: Deal Makers and Breakers.



8. Submit application.

1.



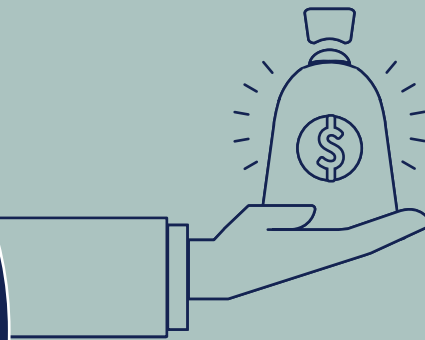
Understand the funding eco-system.



The diagram on the next page illustrates the various sources of **funding** which takes into account businesses at all levels.



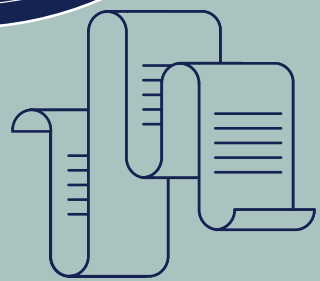
THE FUNDING SOLAR SYSTEM



The use of a solar system as an illustration depicts funders as planetary objects.



The idea here is that as with planets the **further they are from the earth the more complicated it is to reach** them.



The various funders are similar, here it is illustrated that the **further away from the earth** (you - the entrepreneur) the **level of sophistication increases in terms of the information they require** from you and their application process. The sources are by funding source & phase of Business:





YOUR FUNDRAISING SOLAR SYSTEM

VENTURE CAPITALIST

GOVERNMENT
PROGRAMS

DFIs

CORPORATE
PROGRAMS

BUSINESS
START-UP
COMPETITION

BUSINESS
INCUBATORS

CROWD
FUNDING

FFFs





Understand the funding eco-system.



	FRIENDS FAMILY AND FOOLS	CROWD FUNDING	START-UP AND BUSINESS COMPETITIONS	BUSINESS INCUBATORS	CORPORATE ENTERPRISE DEVELOPMENT PROGRAMS	GOVERNMENT PROGRAMS	VENTURE CAPITALIST	DEVELOPMENT FINANCE INSTITUTIONS & BANKS
CONCEPT/ IDEA PHASE	X	X	X			X		
START-UP (PRE REVENUE)	X	X	X	X		X		X
START-UP (POST REVENUE)	X	X	X	X	X	X	X	X
GROWTH PHASE		X	X		X	X	X	X
MATURE PHASE			X		X	X	X	X



2.



Understand the funder mandates.

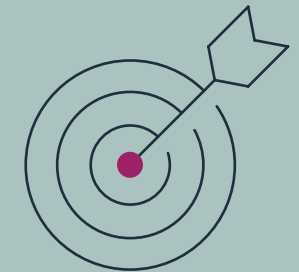
Raising funds takes time, effort and resources. It is not advised to approach a funder without having **researched them properly.**



Find out what each investor's mandate is, and make sure your project, industry or the reason for your investment requirements **suits what they are looking for.**



Their mandates are **published on their websites** and there is a specific reason for them focusing on certain areas.



THE IMPORTANCE OF UNDERSTANDING FUNDER MANDATES



THE TIP:
To be noticed, target the right funder at the right stage.

If you ignore those mandates you could tarnish your credibility before you are out of the starting blocks. **Funders file every business plan they receive.** If you keep sending the wrong information to them, they will remember you. By the time you finally send something that does suit their investment profile, you may not be taken seriously.

3.



Identify the correct form of funding.

Understanding the type of funding you require is one of the most important aspects you need to make a decision on in your attempt to source funding, the type of funding you need is linked to the opportunity or requirements you have for instance. Below is a matrix which can assist you to understand the types of funding and its uses.

Debt repayable with terms and over a set period at an interest rate.	<ul style="list-style-type: none"> • Assets • Property 	<ul style="list-style-type: none"> • Working Capital (Opex) • Fixed Assets 	Mezzanine financing is a hybrid of debt and equity financing that gives the lender the right to convert to an equity interest in the company in case of default. This can also assist to make the deal more financially viable.
<ul style="list-style-type: none"> • infrastructure Improvements 	LOAN FUNDING	MEZZANINE FINANCE	<ul style="list-style-type: none"> • Moveable Assets • Property
Venture capital is a type of private equity, a form of financing that is provided by firms or funds to small, early-stage, emerging firms that are deemed to have high growth potential, or which have demonstrated high growth.	VENTURE CAPITAL/ EQUITY FINANCE	CASH FLOW LENDERS	Debt Factoring is a financial arrangement in which a factoring company takes responsibility for collecting money relating to a business's invoices, and immediately pays that business part of the total amount owed on the invoices.
<ul style="list-style-type: none"> • R & D • Sales & Marketing • Hiring Specialist • Asset Investments 	<ul style="list-style-type: none"> • Working Capital • Consultants 	Stock Trade Finance is a mechanism which releases working capital for stock such as finished goods or raw materials, which works by lenders purchasing stock from a seller on behalf of the buyer.	Invoice Discounting is the practice of using a company's unpaid accounts receivable as collateral for a loan, which is issued by a finance company. all invoices less than 90 days old.

IDENTIFY THE
CORRECT
FORM OF FUNDING

4.



DOCUMENT THE PROBLEM OR MARKET OPPORTUNITY



“ It is important for you to develop a **UNIQUE STATEMENT** which clearly defines the hurdle you have to grow in your business or the opportunity you can commercialize on in the market.



This will give you an **INDICATION OF THE TYPE OF FINANCE** you may need and what the investment may need to be spent on.”

Here is a guide on
how to define this



Document the problem
or market opportunity.

WRITE AN OPPORTUNITY STATEMENT BY ANSWERING THE 5 W'S

What is the opportunity? _____

Where did it originate from, or where is it located? _____

When will you have to be in a position to commercialize the opportunity? _____

Why do you think you will be able to commercialize the opportunity? _____

Who are the clients/ customer? _____

Now plot the resources you will require to operationalize your team/business to commercialize the opportunity.

1. _____ 2. _____

3. _____ 4. _____

5. _____ 6. _____

7. _____

5.



PLOT AND LINK YOUR NEEDS TO FUNDER MANDATE AND THE FORM FUNDING

	FUNDER 1:	FUNDER 2:	FUNDER 3:	FUNDER 4:
FUNDS MY CORE BUSINESS ACTIVITY OR SECTOR				
FUNDS MY RESOURCE REQUIREMENTS				
PROVIDES THE TYPE OF FUNDING I'M LOOKING FOR				

6.



PREPARING FOR APPLICATION

Below is a list of documents and important information you will be required to compile before submitting an application:

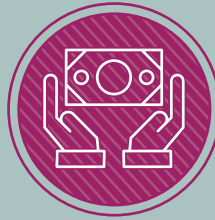


- Business Plan
- A Critical Market Analysis
- Operational Plan
- Marketing Plan
- Product(s) Based
- Service(s) Based
- Cash Flow Projections
- Verified Historical Financials (if available)
- Compliance Documents
- CIPC Registration Documents
- Tax Clearance Certificate or Certificate of Good Standing
- Business Licenses
- Your Relevant Industry Approvals/Licenses or Certifications
- Cvs and Skills Profile of The Management Team
- IP Related Registration Documents
- A List of Contracts and Agreements
- Asset Lists and Values (Movable and Immovable)
- Minutes of Management Meetings
- A List of Staff Members and CVs

6.1



Interpreting financial performance & key financial metrics to know.



NPAT Margin

Shows % of profit the company has made from its trading activities. Affects companies retained earnings/cash reserves and shareholders equity.



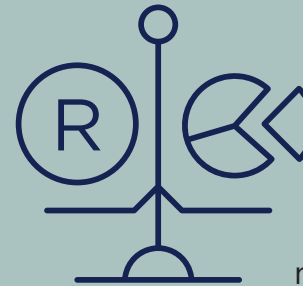
GP Margin

Shows % cash available after cost of sales goods/services are paid.

Paints the picture of how much operating capital the business has.

KEY FINANCIAL METRICS

INTERPRETING FINANCIAL PERFORMANCE AND



Quick and Current ratio

Shows amount of cash available to cover medium term debt.

Expressed as a ratio,

e.g: 1 : 2 – for every R 1 of debt owed over the next 12 months, the company has R2 to cover it.



To calculate this, the diagram on the next page gives you a guide where this key financial information is located on your company's balance sheet (for existing businesses).



“You need not know how to **calculate** this, you need to know what this means to you”

NB: note that start-ups, due to very little trading history may not need/have this information.



Interpreting financial performance & key financial metrics to know.

STATEMENT OF FINANCIAL POSITION AS AT 28 FEBRUARY 2017

	Note	2017 R	2016 R
Assets			
Non Current Assets			
Property Plant and Equipment	2	117,086	516,502
Current Assets			
Trade and Other Receivables	4	35,850	-
Cash and Cash Equivalents	5	282,353	96,718
Total Assets		435,289	613,220
Equity and Liabilities			
Equity			
Share Capital	6	1,000	1,000
Retained Earnings / (Loss)	7	(2,004,963)	(2,191,686)
Non Current Liabilities			
Loans from Member's Shareholders	3	2,366,530	2,803,906
Current Liabilities			
Trade and Other Payables	9	26,782	-
Provisions	8	45,941	-
Total Equity and Liabilities		435,289	613,220

Curr Asst / Current Liab=
R318,203 / R72,722=
R4,37
RATIO = 4:1



Interpreting financial performance & key financial metrics to know.

EBIT:
Earnings Before
Interest & Tax.



EBITDA:
Earnings Before
Interest, Tax,
Dividends &
Amortisation.



INTERNAL RATE OF RETURN (IRR):

- The IRR measures how well a project, capital expenditure or investment performs over time.
- The internal rate of return has many uses. It helps companies compare one investment to another or determine whether or not a particular project is viable.



CAGR

- Describes the rate at which an investment would have grown.
- Expressed as a percentage.
- Shows investors how well the investment will do over time.



Tip: Investigate investors' minimum acceptable IRR

GEARING

- Compares some form of owner's equity (or capital) to borrowed funds.
- Gearing is a measure of financial leverage, demonstrating the degree to which a firm's activities are funded by owner's funds versus creditor's funds.



LEVERAGE

Look at how much capital comes in the form of debt (loans), or assesses the ability of a company to meet financial obligations.



Does your business plan explain how your business model works?

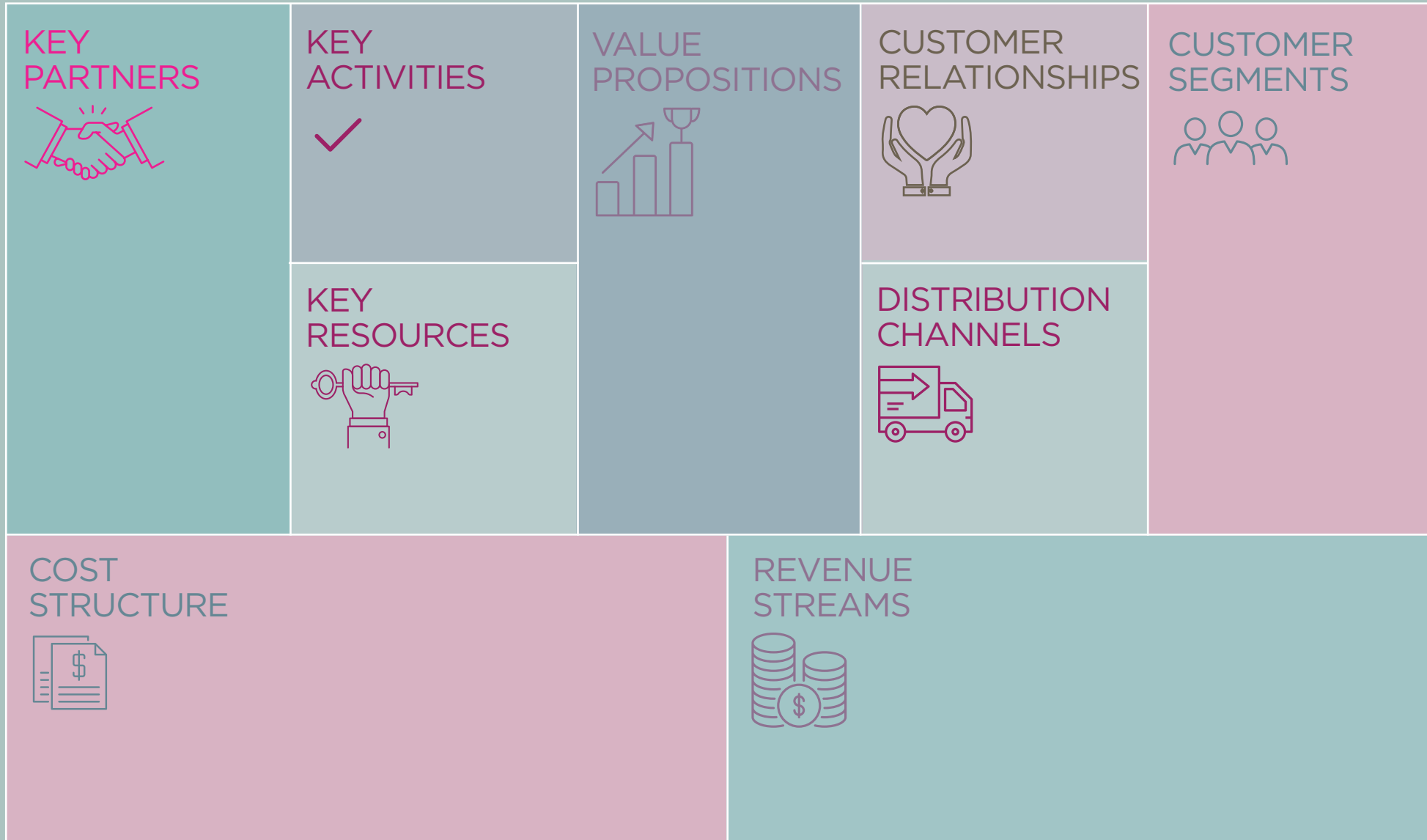


The diagram on the next page gives you a clear indication on what funders are looking for in your business plan - turn over to see...



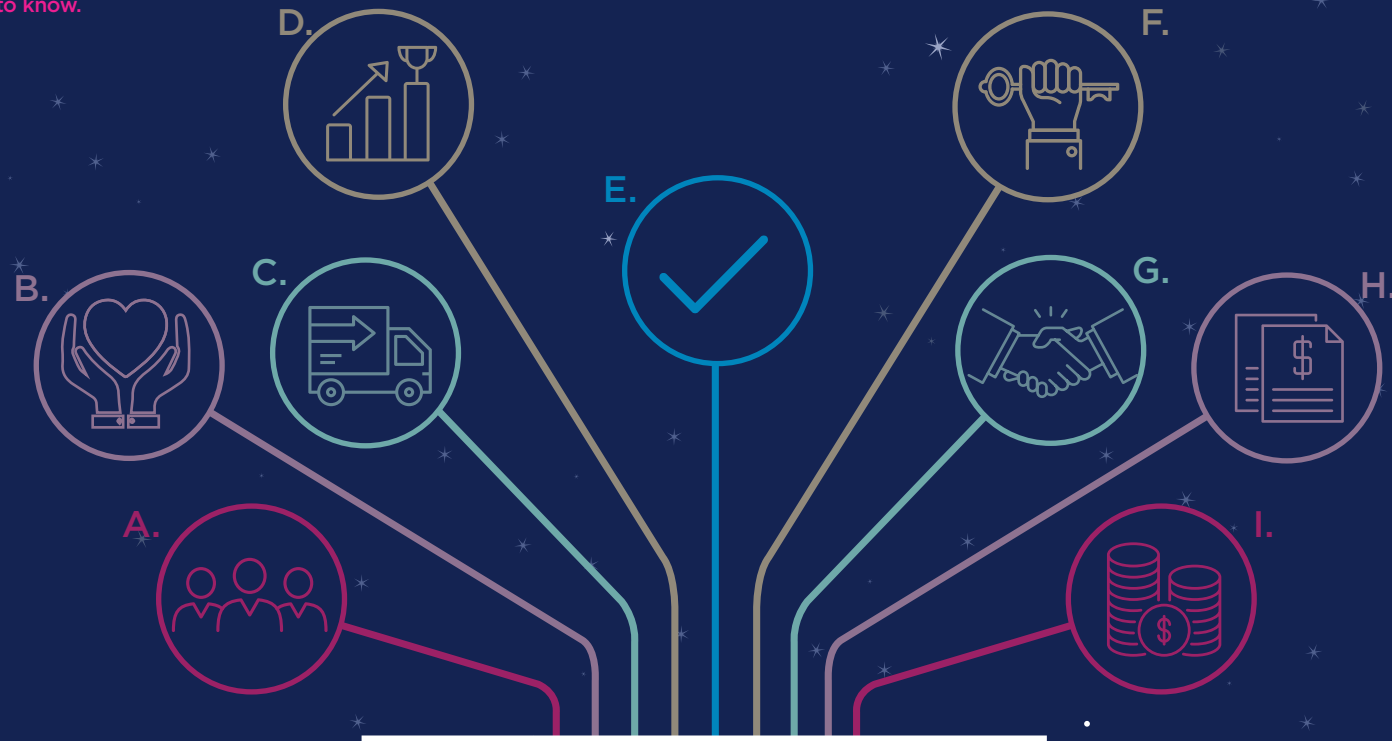


Interpreting financial performance & key financial metrics to know.





Interpreting financial performance & key financial metrics to know.



9 BUILDING BLOCKS OF BUSINESS

There are 9 (referenced A to I) critical areas of any business which enables businesses to operate, function and compete in the open market. The following gives the 9 areas and what should be covered in each area:



Interpreting financial performance & key financial metrics to know.

A.



CUSTOMER SEGMENTS

- Who are your customers or what type of customers are you currently or intend on serving?
- What distinct needs do each of these have?
 - List the problems or demands you are satisfying
- What distinct **BUYING** behaviours does each of these have?
 - Where, how, why do they spend money?
- What distinct attributes does each of these have?
 - What they are like?

Market Data required

- Number of potential customers (Open Market)
- Geographic coverage (Open Market)
- Demand quantities (Contract Clients + Open Market)
- Realistic ability to supply demand (Scale of Operations)
- Average pricing (norms and standards)
- Comparative pricing (differentiators)
- Number of customers/clients targeted for Y1 & Y2 or Phase 1/ 2

B.



CUSTOMER RELATIONSHIPS: “BUILDING A CUSTOMER BASE”

- How do customers interact with and access your services and products?
- How do your customers prefer to know about your products and services?
- How do your customers prefer to access products and services?
- What are you doing or going to do to:
 - Identify customers
 - Reach out to them
 - Entice them to choose you
 - How are you going to hold on to them?

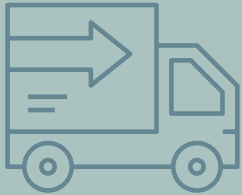


Interpreting financial performance & key financial metrics to know.

C.

DISTRIBUTION CHANNELS: ROUTES TO MARKET

- How customers interact with and access your services and products?
- How do your customers prefer to obtain your products and services?
- What do they best respond to?



Here are a few methods your business may use to reach clients:

- A direct sales team
- A website
- Independently owned stores
- Chain store retailers
- Wholesalers
- Hosted e-commerce
- Licensed resellers/Agents
- Independent retailers

D.

YOUR VALUE PROPOSITION: PRODUCTS AND BUNDLES

- What are the products and service you sell?
- How do you present them?
- Why do customers want these?
- **Which of these elements do you offer the market in comparison to competitors and how do you ensure this?**
 - Better pricing points
 - Newness/Novelty
 - Product performance
 - Customization/Personalising
 - Functionality
 - Design
 - Brand/Status
 - Accessibility/Convenience
 - Risk reduction
 - Cost reduction



“What is your underlying magic?”





Interpreting financial performance & key financial metrics to know.

E.



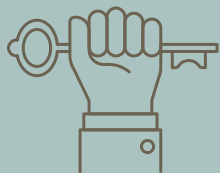
KEY ACTIVITIES

Key Activities describes the most important things a company must do to make its business model work. For Microsoft Key Activities include software development. For PC manufacturer Dell, Key Activities include supply chain management (sourcing and securing quality components).

You need to look at:

- Production
- Problem solving
- Platform/networks you require to put your service out there
- Procurement
- Sales & marketing
- Administration and customer support, etc.

F.



KEY RESOURCES

Resources are required to support your business operations, enable functions or build/ make a product. You need to explain how this enables your business and why the funding is required in this component. Ultimately the funding will be used to acquire assets or services which enables your business.

Here are a few categories to consider:

- Physical
- Intellectual/Specialists
- Human
- Financial
- IT
- Raw material



Interpreting financial performance & key financial metrics to know.

G.



KEY PARTNERSHIPS

Because a business does not possess, perform or create all the resources it requires, partnerships can deliver these. This describes the network of suppliers and partners that make the business model work.

Why and which partnerships are you looking to acquire?

Which of these are possible reasons?

- To optimize your business model,
- reduce risk, or
- acquire specific resources.

H.



COST STRUCTURE

Approaches:

- **Cost-driven:** this takes an expense saving approach to deliver competitive pricing, if pricing points are part of the your competitive advantage.
- **Value-driven:** this takes into account the end product competes on the underlying value it delivers to customers and pricing is not part of the primary competing factors. Features and benefits are the competitive advantage. All necessary costs will be incurred to deliver on the features and benefits to customers.

Costs are characterized by:

- Fixed costs
- Variable costs
- Economies of scale
- Economies of scope



Interpreting financial performance & key financial metrics to know.



REVENUE STREAMS- “HOW DOES YOUR BUSINESS MAKE MONEY”

A business model can involve two different types of Revenue Streams:

- Transaction revenues resulting from one-time customer payments.
- Recurring revenues resulting from ongoing payments.

Examples of how these are captured are:

- Asset sale - once off purchases
- Usage fees/Pay Per Use
- Subscription fees
- Lending/Renting/Leasing
- Licensing
- Brokerage/Commission fees
- Advertising

“The Revenue Streams represents the **cash a company generates** from each Customer Segment.”

7.



Build a Data Room.

BUILD A DATA ROOM

A Due Diligence Data Room is the place where your company places copies of the financial, legal and business documents that define the history and future of the company for prospective investors to review prior to submitting a formal offer.

A due diligence data room is **accessed by potential buyers or investors** after being approved by the seller and after having signed an Non Disclosure Agreement (NDA). The investment banker representing the seller is responsible for identifying viable buyers/investor, securing signed NDA's and scheduling access to the due diligence data room information.

There are two types of Due Diligence Data Rooms: Traditional Due Diligence Data Rooms and Virtual Due Diligence Data Rooms.

Traditional Due Diligence Data Room: copies of information are kept and prepared in hard copy.

Virtual Due Diligence Data Room: copies of information are kept and prepared in soft copy.



THE MAIN OBJECTIVE OF THE DUE DILIGENCE DATA ROOM FOR THE SELLER IS TO:

Remove any concern the potential buyer or investor has in the viability and profitability of the company.

Disclose all data required or requested by the buyer/investor to close the sale quickly.

Present business records with emphasis on growth and future value to maximize the offer amount.

Expose any "skeletons" up front in the most positive way possible before final valuation offers to minimize any potential downward trend in the offers.

A Seller uses the due diligence data room to draw attention to the best attributes of the business to try to **INCREASE the buyer's/investor's valuation of the business.** A well-constructed due diligence data room can increase the final valuation offer by several percentage points.





Build a
Data Room.

THE BUYER'S/INVESTOR'S KEY OBJECTIVE OF THE DUE DILIGENCE DATA ROOM

The main objective of the due diligence data room for the potential buyer/investor is to:

- Use financial data to arrive at the Valuation Model.
- Determine any operational costs that can be reduced or eliminated.
- Identify business data or trends that could be used to justify a lowering of the valuation offer.
- Identify any “skeletons” that will risk achieving future revenue or earnings | projections.



KEY INFORMATION REQUIRED FOR YOUR DATA ROOM MAY INCLUDE THE FOLLOWING AREAS:

Corporate books and records
Financial information
Employee records
Contingent liabilities
Contracts, Agreements, and other Arrangements
Proprietary rights
Plant, Property, and Equipment
Insurance
Sales/Marketing
Miscellaneous

A Buyer/
Investor uses
the data in the
due diligence
data room to
validate their
valuation model
and to identify
anything that
could risk
future earnings
thus providing
a reason to
LOWER his
valuation
offer.



8.



SUBMITTING AN APPLICATION

YOU MUST ENSURE THAT THESE DOCUMENTS ARE COLLATED AND SUBMITTED IN HARD AND SOFT COPY



- A Business Plan
- A critical market analysis
- Operational Plan
- Marketing Plan
- Product(s) based
- Service(s) based
- Cash Flow Projections
- Verified historical financials (if available)
- Compliance documents
- CIPC Registration documents
- Tax clearance certificate or certificate of good standing
- Business licenses
- Your relevant industry approvals/ licenses or certifications
- CVs and skills profile of the management team
- IP related registration documents
- A list of contracts and agreements
- Asset lists and values (movable and immovable)
- Minutes of management meetings
- A list of staff members and CV

9.



WHAT TO EXPECT IN THE INVESTMENT PROCESS



10. SUCCESS FACTORS OF A DUE DILIGENCE

- Misalignment between the business plan and the conversation
- Spelling mistakes
- Credit rating - people invest in people!
- Over gearing - over indebtedness
- Lack of market insights - vision is blurred
- Inability to justify market assumptions - affects projections
- Slow revenue growth and poor profit margins
- Over estimating sales, with no growth strategy or evidence of revenue streams and customer pipeline
- Cannot show how supply and demand issues will be managed

Lack of uniqueness - why do customers want/need you?

- Insufficient experience of key management and entrepreneur
- No strategic insights or plan
- Lack of scalability elements (growth)
- Non-compliance issues - (HR/Legal/Tax/statutory issues)
- Failure to deliver key outstanding documents
 - customer contracts/distribution license agreements/agent contracts
- Inaccurate financial requirements - how much funding you will need to induce growth
- Over investing - Buying vs Leasing (cost benefit analysis)

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