How to Get Capital for a Startup

(Part #1 of 6)

In the past few years, it seemed that anyone with a bright idea could snap their fingers and easily find the funding they needed to make it a reality.

The private markets were flush with cash, and those in the know could quickly secure multimillion-dollar investments.

But times are changing. The global economy is still reeling from the effects of Covid, slow economic growth, and high inflation. As a result, many investors are now much more cautious about where they put their money.

Venture capitalists are starting to tighten their purse strings, and it will be harder for startups to find the investments they need to grow.

It's becoming increasingly difficult for startups to get the money they need to get off the ground, but not impossible.

It's more important than ever to have a clear plan and a strong team before seeking funding. In addition, with increasing competition, investors will want to see that you have solid cash management and financial modeling to ensure their money is in the best hands.

There are a few different avenues you can explore when it comes to funding your startup.

Let's take a look at the most common.

Crowdfunding for Startup

Crowdfunding can be an excellent way to raise money for your startup.

It relies on small contributions from many people and can be a great way to generate buzz and get people talking about your product or service.

To be successful, you'll need to have a great pitch and a compelling video. You'll also need to set a realistic funding goal and offer rewards to those who contribute.

The beauty of crowdfunding is that when it's successful, it not only provides you with the funds you need to get started and gives you a built-in customer base.

They could be raving about your product, rooting for your success, and supporting your marketing efforts organically.

Crowdfunding campaigns that build a sense of community, engage their backers, and provide great rewards tend to be the most successful.

And backers are more likely to contribute and share their excitement around the project if they feel like they're part of something larger and you make them feel invested in the mission behind the project.

There are a few different crowdfunding platforms available to help you get started, such as Kickstarter and Indiegogo, but it's essential to do your research before choosing one. Each forum has its own rules and regulations, and you'll want to make sure you pick one that's the best fit for your project.

Personal investment

If you're not interested in crowdfunding or don't think it would work for your particular project, another option is to invest your own money. This is often the route taken by startup founders who are passionate about their product and confident in its potential.

If you go this route, you'll need to be prepared to risk losing everything you put in. You'll also still need to make sure you have a solid business plan to convince potential investors to take a chance on you if you choose to go for external financing further down the road.

Personal investment can be a great way to start, but it's not always an option for everyone.

When considering this route, carefully weigh the pros and cons and only invest what you can afford to lose.

And if you don't have the personal financial resources to invest in your own business, you'll need to look for other sources of funding.

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How to Get Capital for a Startup Part #2

Friends and family

Another common source of startup funding is friends and family. **Again, this can be a great option because you'll likely have a built-in support system from people who believe in you and your product.**

The downside of this route is that it can strain personal relationships if things don't go as planned or if there's a miscommunication about expectations.

It's essential, to be honest about the risks involved and ensure everyone is on the same page before moving forward.

There are different ways that your friends and family can help you fund your startup. They can give you loans, invest in your business or simply make donations.

- **Loans** will need to be repaid with interest, so be sure you have a solid plan for how you'll do that.
- If they're interested in **becoming investors**, you'll need to give them equity in your company which means they'll own a portion of your business.
- And if they're just making **donations or gifts**, there's no expectation of anything in return, but be sure to show your appreciation.

If you decide to go this route, it's essential to treat it like any other business transaction. After all, even though these people are close to you, they invest their hard-earned money in your business. That means creating a formal agreement that outlines the terms of the loan or investment, including repayment terms and interest rates.

Be professional, have everything in writing and make sure you deliver on your promises. This will help to avoid any misunderstandings down the road and protect you, your loved ones, and your business.

Business incubators

Another option to consider if you're just starting is business incubators. **These programs help new businesses get off the ground by providing resources like office space, mentorship, and funding.**

The eligibility requirements and selection process vary from program to program, but they're often quite competitive. And while not all incubators offer to fund, many do, and it can be a great way to get your business up and running.

The mentorship they offer is also invaluable, as you'll have access to experienced entrepreneurs who can help you navigate the early stages of starting a business. If it's your first venture into entrepreneurship and you have a mind equally brimming with ideas and questions, business incubators can be a great way to get your feet wet and learn the ropes.

You'll also come away with a network of other entrepreneurs in similar phases of starting their businesses as you. As you're all going down a similar route together, you can help hold each other accountable and offer support, collaboration, and advice.

By sharing a workspace and the ups and downs of entrepreneurship, you might also create some long-term business relationships that last well beyond the life of the incubator program.

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How to Get Capital for a Startup Part #3

The Small Business Administration

Another source of funding for small businesses is the Small Business Administration (SBA). **The SBA is the only government agency dedicated to helping small businesses.**

The organization does this by offering loans, guaranteeing loans, and providing counseling and training. They also have a variety of programs specifically for women, minorities, veterans, and the disabled.

Some of the SBAs funding programs include:

- **Small Business Investment Companies (SBIC)**. The SBIC Program provides funding to small businesses through private capital, but with the SBA partially matching the investment and guaranteeing the loans. SBICs then invest in small businesses and help them grow through equity or debt financing.
- The 7(a) program is the SBA's most popular loan program. It helps small businesses access funding by guaranteeing loans from banks and other lenders. These loans can be used for various purposes, including working capital, equipment, inventory, or real estate.
- **Microloan Program**. The Microloan program provides loans of up to $50,000 to small businesses and some non-profit organizations that might be unable to get funding from traditional sources.
- **504 loan program**. The 504 loan program provides long-term, fixed-rate financing for major asset purchases like real estate or equipment. In addition, the SBA guarantees a portion of the loan, making it easier for small businesses to access the funding they need.

The SBA also offers grants for community organizations or small businesses researching and developing.

Your business must meet specific criteria to be eligible for an SBA loan, like being a US for-profit business, operating in one of their approved industries, and being small by their standards.

As well as funding, the SBA has a wide range of resources available for small businesses, so it's worth checking out.

Government grants and subsidies

Another source of funding for small businesses is government grants and subsidies.

State or local governments usually give these out, but sometimes the federal government will also give out grants.

Government grants are typically given to businesses doing research and development or companies that are seen as beneficial to the community.

For example, businesses developing new green technologies might be eligible for government grants. This is a way to incentivize companies to work on economic activities considered necessary for the country's development.

Small businesses can also get subsidies from the government. They typically go towards companies that provide some essential service but might struggle to survive without some form of government support.

For example, businesses that offer child care or public transportation might be eligible for government subsidies. This is because these businesses provide services that are considered essential but might not be profitable.

Farmers or manufacturers might get subsidies to keep food prices low or to protect production and established jobs. They're also given out to businesses creating new jobs in disadvantaged areas.

To determine if your business is eligible for government grants or subsidies, you can start by searching through the government's grant database. You can also contact your state or local government to see if they have any programs for that you might be eligible.

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How to Get Capital for a Startup Part #4

Lines of Credit

Whereas for a standard loan, you agree with the lender on the amount of money being borrowed, a line of credit is an open-ended loan. This means that you can borrow up to a certain amount of money, but you don't have to use all of it right away or at all if you don't need it.

You can only pay interest on the portion of the loan that you use. Note, that you will have to pay back the principal amount at some point to stop paying interest.

This can be helpful for businesses with irregular cash flow or needing funding for short-term expenses.

One thing to be aware of with lines of credit is that they typically have variable interest rates. The interest rate can go up or down depending on economic conditions. This can make it challenging to budget your loan payments, so it's essential to be aware of this before you take out a line of credit.

A line of credit can be secured or unsecured. A secured line of credit is backed by collateral, like a piece of equipment or a real estate property. If you can't make payments, the lender can take the collateral and sell it to recoup their losses.

An unsecured line of credit doesn't have any collateral backing it up. This makes it riskier for the lender, so they typically charge a higher interest rate.

It's important to note that a line of credit is not intended to fund long-term projects or asset purchases because of its variable nature and higher interest rates. Instead, it's best used for fluctuations in cash flow or short-term expenses.

Bank loans

Traditional bank loans are another option for small businesses looking for funding.

A loan is a generic term that overlaps with some of the funding options we've already looked at. For example, a line of credit is a specific type of bank loan, or an SBA loan is a loan that the Small Business Administration backs.

Banks also offer the options to take out a personal loan, a working capital loan to cover day-to-day expenses or invoice factoring. In addition, businesses can sell their invoices to a bank at a discount to get the money they're owed more quickly.

But here, let's look more specifically at a term loan.

A term loan has a fixed interest rate and a set repayment schedule.

The repayment schedule is set in advance, so you know exactly how much you need to pay each month and when you will finish paying the loan off. This makes it easier to budget for your loan payments.

Term loans can be used for various purposes, like funding the purchase of equipment or real estate or covering expansion costs.

One thing to note is that bank loans tend to have stricter eligibility requirements than some of the other funding options we've covered. So, for example, you might need to have been in business for a certain number of years or have a minimum amount of revenue.

And because banks are for-profit institutions, they're more likely to be interested in lending to businesses they think will be able to repay the loan with interest. This means that if your business is in a risky industry or if you have bad personal credit, you might have a more challenging time getting approved for a bank loan.

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How to Get Capital for a Startup Part #5

Angel investors

Angel investors are individuals who invest in small businesses. They typically provide funding in exchange for a percentage of ownership in the company. Think Shark Tank, but without the television cameras and the drama.

The benefit of working with angel investors is that they're usually more flexible than traditional lenders. For example, they might be willing to take on additional risk or give you more time to repay your loan.

The downside is that because they're putting their own money into your business, they generally want a say in its run. This means they might want a seat on the board of directors or want to be involved in decision-making. If you're uncomfortable with this level of involvement, it might not be the right funding option.

The upside is that by securing funding from an angel investor, you can benefit from their experience and expertise. In addition, they might be able to provide valuable advice and connections that can help you take your business to the next level.

Angel investors can be a great source of funding for businesses just starting out or in the early stages of growth.

Venture capital

Venture capital firms are companies that invest in small businesses. They typically provide funding in exchange for a percentage of ownership in the company.

These firms tend to be interested in businesses that have high growth potential. This means they're typically only willing to invest in companies in industries with much room for growth, such as technology or cutting-edge research.

As well as growth, they'll look for high-profit potential, expecting a high return on their investment. This means that they're mainly interested in companies that have the potential to be sold for large amounts of money or to go public.

To make sure that their investment pays off, they'll usually want a seat on the board of directors or to be involved in decision-making. And they're more likely to be interested in businesses with a proven track record or some indication of future success.

The downside of venture capital is that it can be challenging to secure funding from these firms, as they receive many applications and only invest in a small number of companies.

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How to Get Capital for a Startup Part #6

Online/Alternative Lenders

Online or alternative lenders are companies that provide loans to small businesses.

They typically have a quick and easy application process and can provide funding in as little as 24 hours. They also tend to be more flexible than traditional lenders, which can benefit you if you have bad credit or your business is in a risky industry.

These lenders typically charge higher interest rates than traditional banks, but they can be a good option for businesses that need funding fast. For example, if you need to take advantage of a time-sensitive opportunity or to take care of an unforeseen expense.

One thing to remember with online or alternative lenders is that they typically have shorter loan terms than traditional banks, so you might have to pay back the loan more quickly. So if you're not sure you'll be able to repay the loan on time, it might not be the right funding option.

Funding selection criteria

When deciding what funding source to go for, it's essential to consider your business's needs and priorities.

This is when solid business planning becomes critical, as it will give you a clear understanding of what your business needs to grow.

And alongside business planning, cash flow forecasting is crucial when looking at your business venture's different growth stages.

This will give you more clarity on the best time to seek external funding and what type of funding would be best suited. It will also help you anticipate any bumps in the road to plan accordingly.

Many small businesses go bankrupt not because they're not profitable but because of poor cash flow management.

So, understanding your business's cash flow is essential to making sure that you don't run into any problems down the line. And any potential investors will want to see evidence of this before they invest in you.

Once you have a good understanding of your business's needs, you can start to look at different funding options and compare them based on the following criteria:

- How much money do you need, and at what stages of your growth?
- What do you need the money for?
- How quickly do you need the funding?
- What are the repayment terms and conditions?
- When will you be able to repay the loan?
- How involved will the funding source be in your business?
- As well as funding, do you want or need mentoring, expertise, or some other form of support?
- Do you have any collateral or assets that you can use to secure the loan?
- Finally, what are the risks involved with this type of funding?

Ultimately, there's no one correct answer when choosing a funding source, depending on your individual business needs and preferences.

The most important thing is to do your research and make sure you choose the right option.

And with competition for funding becoming increasingly fierce, it's more important than ever to make sure your business is well-prepared before you start applying for loans.

Before approaching potential investors, ensure you have a solid business plan and cash flow forecast. This will give you the best chance of success in securing the funding you need to grow your business.

And if cash management and financial modeling isn't your thing, working with a finance professional will help ensure that you've covered all the angles and have a solid plan before reaching out to potential funding sources. They will also be able to advise you on what sources of funding would be best suited for your business and when.

In the end, many entrepreneurs start with only a great idea and a burning desire to make it happen.

But only by having a solid understanding of the finances involved and responsible cash flow management will you be able to secure the funding you need in today's competitive market and ensure the long-term success of your business.

If you feel you could benefit from a **practical and experienced fractional CFO**, please connect on LinkedIn and message me to set up a time to discuss what you would like to accomplish within your business and a plan to get you there.

So, if you appreciated this six-part series on" How to Get Capital for a Startup," Please like and share it.