

# Business Finance Basics

- Equity Financing
- Debt Financing
- Finances and Firm Stage
- Empirical Data on Use of Debt & Equity
- Examples
- Finance Instruments & Disaster Recovery

# Equity Financing

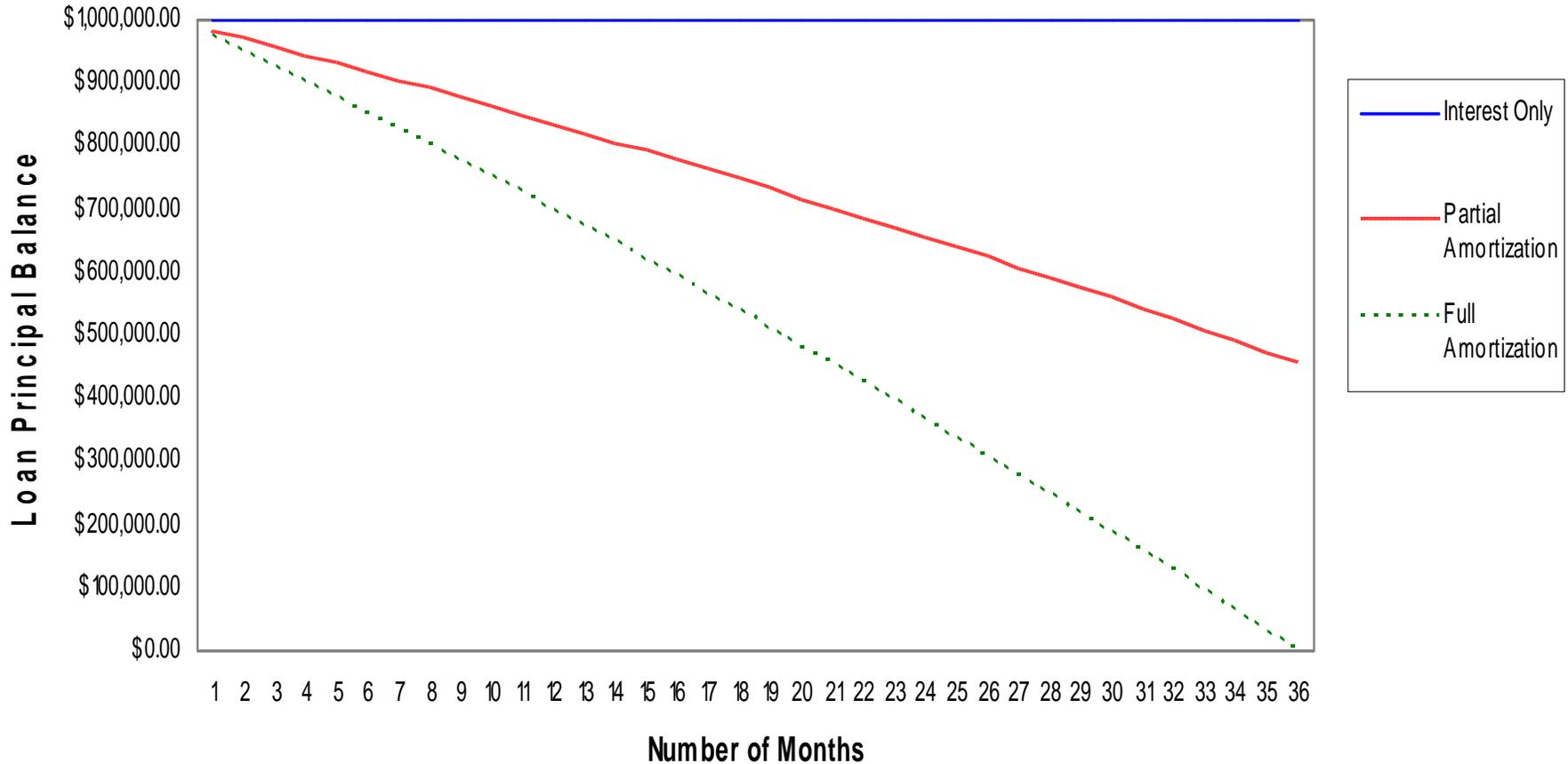
- Definition of equity
- Governance and financial rights
- Forms of equity: preferred stock, common stock, partnership interest, “project equity”
- Key equity terms
  - Company valuation
  - Voting rights & board representation
  - Registration rights
  - Anti-dilution covenants

# Debt Financing

- Definition of debt
- Financial terms:
  - Principal
  - Interest rate
  - Loan term (maturity)
  - Amortization period
- Non-financial terms
  - Collateral and security
  - Financial covenants
- Debt service coverage ratio
- Loan-to-value ratio

# Debt Examples

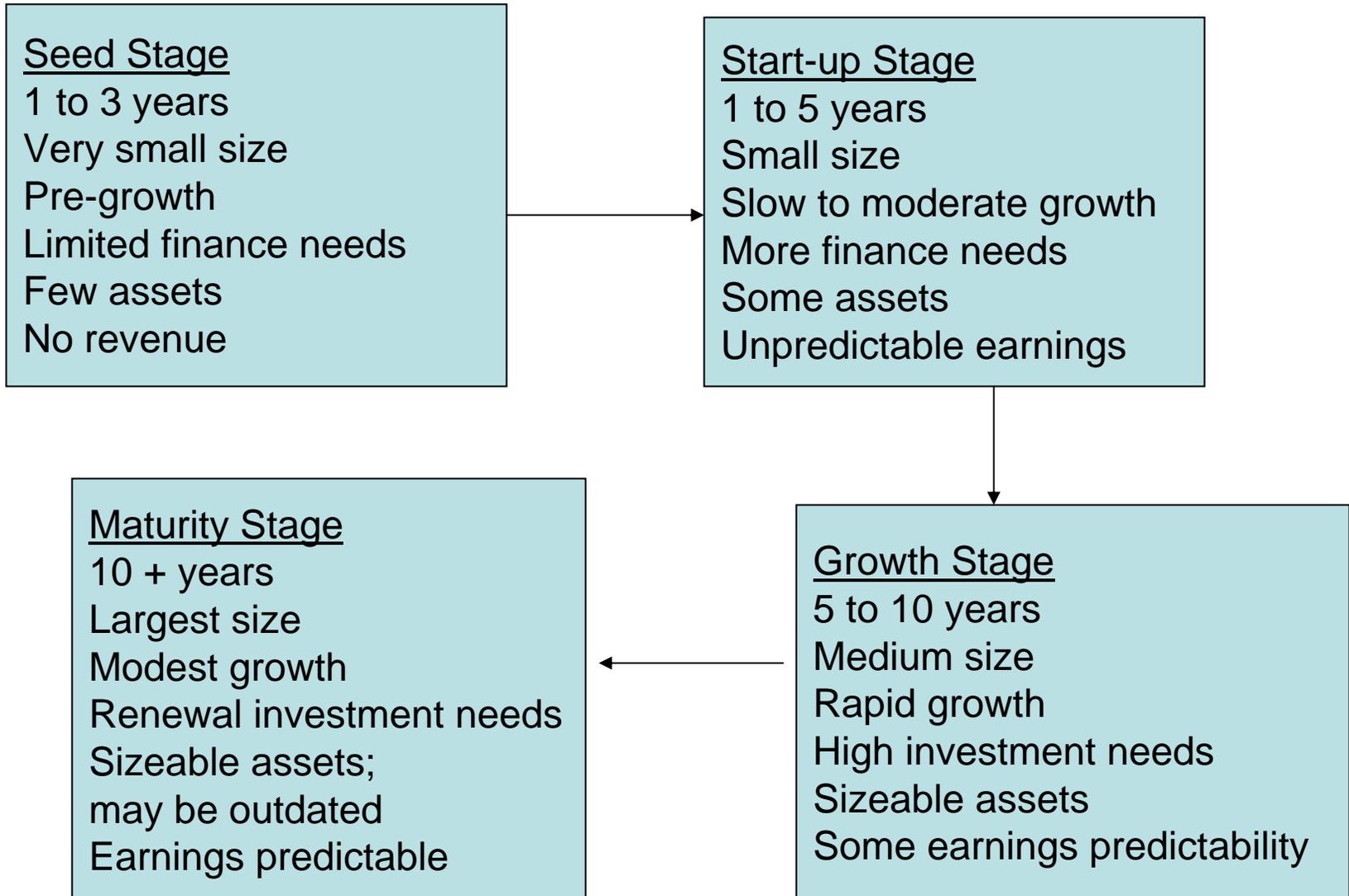
Figure 2-1. Comparison of Principl Balance Over Time for Interest Only and Amortizing Loans



# Small Firm Capital Sources

Capital Source	All Small Businesses	Small Firms < 20 workers, sales < \$1 mm	Small Firms > 20 workers, sales > \$1 mm
Principal Owner Equity	31.33%	44.53%	27.22%
Angel Finance	3.59%	n.a.	n.a.
Venture Capital	1.85%	n.a.	n.a.
Other Equity	12.86%	n.a.	n.a.
Total Equity	49.63%	56.00%	47.67%
Commercial Banks	18.75%	14.88%	19.94%
Finance Companies	4.91%	3.08%	5.47%
Other Fin. Institution	3.00%	3.53%	2.83%
Trade Credit	15.78%	11.81%	17.01%
Principal Owner Debt	4.10%	5.59%	3.63%
Other Sources	3.83%	5.11%	3.45%
Total Debt	50.37%	44.00%	52.33%

# Firm Stages



# Capital Sources by Firm Age

Capital Source	0-2 Years	3-4 Years	5-25 Years	25+ Years
Principal Owner Equity	19.61%	17.37%	31.94%	35.42%
Total Equity	47.90%	39.37%	48.00%	56.50%
Commercial Banks	15.66%	30.84%	17.86%	17.25%
Finance Companies	8.33%	2.51%	5.85%	3.28%
Other Fin. Institution	3.84%	2.36%	2.87%	3.38%
Trade Credit	13.40%	13.42%	17.10%	13.86%
Principal Owner Debt	6.02%	6.19%	3.91%	3.68%
Other Sources	4.85%	5.31%	4.41%	2.05%
Total Debt	52.10%	60.63%	52.00%	33.50%

# Empirical Data and Growth Stage Theory

- High reliance on debt (> 50%) finance at start-up and early stages
- Heavy use of external institutional debt (40%) at start-up
- Growth in principle owner equity and total equity after 4 years
- Owner's personal assets are important to raising external capital