How To Secure Financing as a Start-up Using a Feasibility Study

WHITEPAPER

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RK Fischer & Associates Overview

RK Fischer & Associates is a business consulting and coaching firm that helps business owners increase value in their business by improving their operational and bottom-line financial performance which enables them to achieve profitable growth. All of the services we provide are focused on meeting those goals for every stage of a business.

We offer and deliver our services in multiple formats to meet the needs of our clients and how they choose to learn through a combination of facilitation, coaching, consulting, coaching with consulting, and training. Our services assist you, so you can focus on working more "on your business." Though we are located within Southwestern Ontario, we can provide many of our services to businesses remotely across Canada.

As business advisors, our primary focus is on owner-operated businesses who are under 150 employees. Our two partners have significant managerial and executive experience in complex businesses, such as manufacturing, hi-technology (Fintech, SaaS), business services, as well as financial services. We have worked with clients in a variety of industries from retail, construction, transportation, manufacturing, professional services, healthcare, recreation, and food & beverage, to name a few. We work directly with the business owner to understand their specific business goals and challenges, so we can implement the right solutions ensuring you have continued long-term success.

We have associations and affiliations with other professionals such as lawyers, financial accountants, business brokers, business valuators, lenders, and other service providers who help us in providing you with one-stop-shopping for your business requirements.

Our goal is to bring clarity and focus to your business.

Visit us at www.rkfischer.com, to find out more about all of our offerings and how we may help you with your business, or contact us at info@rkfischer.com.

Our Partners

RUDY FISCHER

Rudy Fischer is a management accountant with a CPA, CMA designation who works closely with our clients to help them improve the financial health of their business. Management accountants focus on your financials going forward and create value for your business by combining strategic planning, performance management (financial & non-financial), and expertise in providing owners with the intelligence they need to grow their business. He will work closely with your financial accountant in understanding the financial history of your business, which is their focus.

Rudy has over 25 years' experience in the hi-technology sector in finance, manufacturing, engineering, product management and marketing disciplines. He has held executive management positions with Everlink Payment Services, Rogers Communications, Sprint Canada, Nortel Networks, Newbridge Networks and Mitel, where he was responsible for various business units.

Rudy has expertise in planning, managing, and marketing products through all stages of the product life-cycle, including setting strategic direction along with the building and directing of the teams who will accomplish the necessary goals. Rudy has launched and been responsible for taking many new products to market including small business voice systems, wireless solutions, data centres, enhanced voice services, fixed-mobile convergence, card payment solutions, and financial transaction acquiring solutions.

Rudy was a Board Member, Member of Audit Committee, and past Chair of the Audit Committee for the Education Credit Union in Kitchener, Ontario from 2013 to 2017. He currently is a Board Member of Southwest Regional Credit Union. He holds a designation of an Accredited Canadian Credit Union Director (ACCUD).

He volunteered before moving from the GTA for the BACD in Durham Region where he acted as a mentor for their clients and provided training as needed. He is a mentor for Futurepreneur.

KAREN FISCHER

Karen started RK Fischer & Associates in January of 2010 after 25 years of success in marketing, sales, channel development and general management with the hi-tech, business services and manufacturing sectors. She held management or executive management roles for companies such as Cognos, Entrust, Mitel, Siemens, and Pitney Bowes. In the last six years of her career before starting RK Fischer & Associates with her business partner, she held start-up Executive roles that included help with plans for financing and acquisition. Based on this experience, Karen felt the small & medium business market was underserved by the consulting industry. She found most firms focus on larger businesses and if they do acquire a smaller client they try to implement large business methodologies in the small business, which is not a fit for most businesses under $25M in revenues.

Karen is passionate about having the chance to help business owners whether that is through growth, increased profitability, or obtaining financing. She is happy to share her expertise and experience that she gained from her prior career with business owners to help them and their businesses flourish. Since the time she started RK Fischer & Associates, she has built strong partnerships in the GTA with other professionals that offer complementary services.

Karen is a past Member of the Board of Directors for the Business Advisory Centre of Durham Region where she held the position of Secretary/Treasurer. This is the small business centre that serves the region of Durham.

She served on the Membership, Marketing and Event Committees for the Ajax-Pickering Board of Trade and was responsible for the development of their Professional Development Series. She filled in for a semester at Durham College for a professor on leave and developed and delivered a Digital Marketing course to the Entrepreneurship Program. She also volunteered as a mentor for BACD and provides training as required.

Upon moving to Southwestern Ontario, Karen has become a Board Member for the Sarnia Lambton Chamber of Commerce and she volunteers for the Chamber on the Business After 5 Committee.

What Is a Feasibility Study

A feasibility study provides analysis of a project or a business. A study should normally be done prior to starting a project or a business to determine the actual viability. At times a feasibility study might benefit a project or business which is been underway for a short period time and is having issues to help get things back on track. A feasibility study ultimately look at the strengths, weaknesses, opportunities, and threats related to the project or business and determines the probability of success as well as delivers recommendations of what can be done to increase the chance of success. It is important that a feasibility study be performed by someone who has the background and experience in business and finance as well as having an objective and unbiased view. Anyone involved with or having some tie to the business or project should not be performing a feasibility study. If a financial institution or investor has asked to have feasibility study performed, this is one of the major factors they will insist upon.

When you, as a business owner, put together a business plan and financials for a lending institution, the numbers are still very speculative. Though the numbers may make sense for that industry, what a bank or investor is looking for is whether the plan can be executed to reach those financial goals. In many cases, business owners underestimate a lot of their start-up costs and do not include the possibility of over runs. Even if an accountant put the numbers together, most accountants are not going to delve into your business and question if they make sense, they are going to ensure whether they are accurate and make sense from an accounting standard, not necessarily from a business or industry standard.

A feasibility study will look at your business to understand the following:

- Does your business make sense from an operational, financial, human resource, marketing, and sales perspective?
- Based on your business plan / model, do the financials make sense if the plan is followed and executed?
- Are your financials achievable based on your revenue forecast and expenses?

- Are you able to support your loan or investor's repayments from a debt & equity perspective?
- Are there holes in your plan and changes that will need to be made to make your project or business viable?

Securing Financing for a Start-up

There are many variables that a lending institution or investor looks for in trying to reduce their risk in providing lending or investment in a business. This is true whether you are a start-up or a mature business. This is why a feasibility study is helpful to a lender or investor, as it validates whether the financials make sense. They are using the financials provided to calculate the variables they use to determine whether the business is worth taking a risk in lending.

The lenders or investors will tend to look at the following:

- If this is for a new business, they are going to look at your personal credit rating because your business does not have a credit history.
- Normally a lender will look at your revenue, but if there is not any, they will look at how much you are investing in the business which will show as equity.
- A lender will want your debt to equity ratio to be around 2:1, so it is important that your expenses and forecasted numbers make sense as this is what they will be using to determine if you will be able to pay them back.
    - Debt to Equity = Total Liabilities / Total Equity
- Lenders will also look at your projected current ratio which projects how liquid your business will be.
    - Current Ratio = Total Assets / Total Liabilities
- Since this is a start-up, unless your equity amount shows that you are able to pay the investor or lender, there will need to be assets as security against the loan/investment such as equipment, building, or even personal assets.
- If this is not your first business, then they will look at your history and success in those other businesses as well.
- The lender will want to review the cash flow projections and future prospects. This will be a very important part of the decision since

1. if it is a new business, they want to know when and where the money is being spent, or

2. if this is an existing business, they want to see if recent decisions will provide expected results

Feasibility Study Success – Case Study

The client was a new start-up business that is in the Family Entertainment Centre industry. The business owners had developed a business plan and had worked with their accountant to put together some projected numbers and develop a financial model for the bank. They had approached two lending institutions to help secure approximately $800K for their new business.

Though the business on paper looked very good and the owners had done an excellent job with market research, the two institutions required the client to obtain a feasibility study through an outside firm to help confirm the viability. They were asked to fund this study themselves. This client believed in and was committed to the business. They wanted the funding, so they contacted RK Fischer & Associates to develop a feasibility study which included a plan and 5 year go forward financial model.

Client Hesitation

The client was a bit hesitant of the process when we were first approached, as they were not sure what might happen. If the business model did not make sense and it was felt the revenue could not be achieved, this could also hinder them in receiving the funding they required. They told us their accountant had prepared the numbers, so they did not understand what the bank wanted. This was true, but their accountant had prepared the numbers based on their input.

Accountants generally compile financial statements based upon the information that is provided by the client. There is no requirement to validate that the business is well and is trouble free; they report the numbers based upon historical inputs.

Where a more detailed assurance is required, Licenced Public Accountants will validate that transactions are recorded correctly and have supporting documents to validate the revenues and expenditures. Asset and liability valuations are conducted to generally accepted accounting principles. Unless adverse financial results are encountered there is no assurance that the company is executing to best practices or that past performance will be an indication of future achievements.

When asked to compile forward looking statements, accountants will again (based upon the procedures used before) rely on the numbers you give them, put them in the appropriate format for the lender or investor and will tell you if something does not look right or make sense. Although the structure of the analysis will be provided in a format that most bankers and lenders understand, they are not going to verify the numbers are reasonable based on your particular business as compared to similar business in your ~~or~~ industry. They will not verify the following:

- The revenue forecast is achievable.
- Your sales and marketing strategy makes sense.
- You have allocated enough money for staffing or hired enough people.
- You have not missed any of your expenses.
- You have all of the areas of your business covered and you have the cash flow to support paying back the loan/investment.
- Determine where there are holes and what will happen if you do not hit the revenue you have projected.

The Process

Questionnaire / Preparation

Since this client had a business plan, a questionnaire was put together based on areas where RK Fischer & Associates saw potential holes or where items were missed and were not covered in each area of the business. Normally, the questionnaire is more detailed as there usually would not have as much information on the business provided before meeting with the client. The questionnaire is given in advance to the client, so that they have time to review the questions and get an idea of the working session.

Working Session

There is a working session with the owners. In the case of this client, we met with one of the business partners and went through the questions and developed an open discussion on each of the areas and questions.

This is an interactive session which the client can ask questions and understand why that information is important. This lasts between 3-6 hours depending on the size and complexity of the business.

Report and Financial Model Developed

A report is developed based on the working sessions. Recommendations are provided on areas that may have been overlooked or where there might be a matter that could cause an issue in the business not reaching their revenue targets or have an effect in the overall viability of the business.

At the same time a financial model will be developed with inputs from the client in relationship to all of the sources of revenue, expenses, assets, and other liabilities. From the information that the client enters, a 5 year projected financial model will be created. This is a tool that will help down the road as well as things change in the business to understand how those changes will impact the financials as it is built with sensitivity analysis employed.

The report and financial model will be reviewed with the client.

Client Process

In the case of the Family Entertainment Centre client the process was followed as described above.

Areas of Concern

The following areas of concern were uncovered in the business model and financials:

- There were not any expenses for the following allocated during the building process prior to opening of the business:
  - Start of loan repayment
  - Building expenses which included utilities, condo fees, and payment of contractor
  - Marketing expenses and costs associated with grand opening of business and building awareness prior to opening

- The client had extensive information on their target market and made very reasonable assumptions about what percentage of the target market that was obtainable. The client had not calculated all of their areas of potential revenue, so the revenue was lower than it should have been based on the programs they planned to roll out.

- The client had not allocated enough money toward marketing in order to meet the revenue numbers. They had not developed a marketing plan yet, so were unaware of the costs of the type of marketing mediums that they were going to have to purchase for their industry. There had not been any money allocated to marketing for the grand opening and programs that were to be in place for the opening.

- The client had not calculated based on customer traffic, the number of actual staff that would be required throughout the day. The expense line for this area was too low.

Remedies

Once the areas of concern were uncovered, RK Fischer worked with the client to address potential holes in the current model.

- Client was able to move some money that was allocated to a long term project to marketing, so there was money being spent on the grand opening and earlier in the first year to achieve the revenue target.

- During development of the financial model, RK Fischer worked with the client in outlining all the potential areas for revenue. The previous revenue potential had been understated.

- RK Fischer worked with the client to define all of the staff types required and work out a reasonable schedule based on traffic patterns based on time of day and time of year. This helped determine a more accurate expense line for staff.

- Client was able to get one of their vendors to move their last payment out a couple months in order to help with the cash flow.

Once all of these remedies were put back into the financial model, the financial model not only was more accurate, but the model provided the client with his cash flow and how changes can be made to remain positive if the revenue target was missed at some point in a month. They were also able to see how if the revenue was higher, how this could positively affect the business.

The Outcome

The new financial model and plan were provided to both of the lending institutions. Because the new financials contained more realistic numbers, not only did the client receive the funding for the loans for which they were asking, they were able to get an additional $25K to purchase capital assets, which previously was going to have to be taken from their personal line of credit.

This is a true feasibility study success story for the following reasons:

- The client themselves had made a very large equity investment into their own business.

- Since the loans were for capital assets and equipment, the loans were fairly secure. It was still important since the loans were for such a large sum that the banks felt secure in the ability for the client to make the loan payments.

- The client had a very good understanding of their industry and target market and the overall business.

- The areas of concerns for success once uncovered were able to be remedied and their financial model ended up stronger than before and they were able to get a jump on the areas of concern and address them so they did not end up being a worry for the business owners.

The feasibility study allowed them to see how viable their business really could be if they execute their plan. As a creator of anything, it is sometimes easy to get tunnel vision and not look and verify all of the areas of your business. If someone has not ever run a business before this is especially true. A fresh set of eyes where someone can walk through your business and ask you the tough questions to make sure you have thought everything through can be very important in whether you have failure or success.

What this client understood after the fact was that even though it was the bank that wanted the feasibility study, the feasibility study helped them get a better handle on their business. This was not about just getting a loan from the bank. This client invested over $250K of their hard earned money. It would have been a shame to see this business not be successful by missing business issues that were easily remedied before the business started. If not remedied, these issues could have affected the business as their expenses were underestimated which could have caused them to default on a loan. Even worse, they could have lost the large investment they made themselves in their business. As it turns out they underestimated their revenue as well, which provided upside for them. The new financial model was more complete and went through sensitivity analysis – so the model was tested. The only thing left to do is for the owners to execute on their plan.