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# Innovative ways in the search for funding

By Jonathan Moules

Banker bashing may help to relieve the economic gloom for business owners, but many are more focused on the increasingly desperate search for funds to expand their operations.

A growing number of founders and chief executives are finding creative ways to find alternative sources of fundraising.

A report published this week by the Centre for the Study of Financial Innovation identified dozens of alternatives to traditional bank funding, ranging from the online marketplaces that bring together businesses seeking finance and those with the capital, such as Funding Circle and Seedrs, to the retail bond schemes used by hotel chain Mr & Mrs Smith and foreign exchange broker Caxton FX among others to raise money direct from the public.

It also acknowledges the collection of challenger banks, such as Aldermore and Silicon Valley Bank, which are creating new ways of providing finance. However, the list of alternatives is much longer.

Andy Davis, the report's author, admits that many of these funding innovations, particularly the online business models, have yet to gain significant traction in a market dominated by bank lending. However, this could change as the lending environment changes and companies move from hoarding cash to looking to borrow to expand operations.

Tony Curtis is a new entrepreneur. Until last September, he was a behavioural specialist working with schoolchildren in Bristol, but he quit his job to commercialise his idea for heated sports gloves.

As if this was not radical enough, Curtis then decided to make his secure local government pension pot the source of seed capital funding for his company, Alago.

First, he transferred the money into a self-invested personal pension (Sipp) set up with the help of Clifton Asset Management, a local specialist financial services firm. Curtis then effectively invested in himself, using half of his £60,000 pension pot to secure the patent on the heated gloves. Alago pays a regular fee to his pension fund for use of the intellectual property.

The funds were three times the £10,000 overdraft Curtis's bank had given him, and enabled him to pay for his first batch of gloves to be manufactured in south-east Asia. However, this type of borrowing entails risks, not least that you are borrowing from your future nest egg.

Although Curtis claims he has no regrets, he warns others to think very hard before putting a "gold plated" pension such as the one he had into the kind of retirement vehicle he has now.

Others agree with this analysis. Henry Ejdelbaum, managing director of independent funding broker ASC Finance for Business, does not provide this kind of service for his clients, though he says he can see the logic for it.

"It is eminently sensible because you know the borrower better than anyone else," he says. That is not to say there are not restrictions on the scheme, however, not least that you can only borrow half of the total pension pot. Ejdelbaum adds that it is hard to see how effective this is as a method of funding because few people who use this method of funding talk about its success.

Curtis adds that he does not have a bad relationship with his bank, HSBC, which he claims has been very supportive. However, he also believes that you need to look at other options.

He appeared on the BBC's long-running pitching contest *Dragons' Den*, but was sent home with nothing. He also tried "crowd funding", by reaching out online to his network of contacts, but was unsuccessful. "You need to know a lot of people to invest in your business and to signpost them to your website," he says.

Simon Littlewood, head of business growth services at Grant Thornton, says being imaginative about raising finance should not mean dismissing bank finance, but being more creative in the sort of borrowing you organise.

"People are starting to put together packages of finance from their bank," he says. "It might be an £80,000 loan, but topped up with finance with some different risk profile. You are trying to get to the same result [as a single term loan] but with different products and not necessarily from the same lender."

Alternative financing sources

**Peer-to-peer business lending platforms**

The extent of peer-to-peer lending to small and medium-sized enterprises (SMEs) in the UK remains small, though this could rise sharply in coming years. Under its Business Finance Partnership, the government is inviting bids from platforms such as these for part of the £100m it is making available through "non-traditional lending channels". Examples include Funding Circle, Thincats and Relendex.com.

**Online financial matchmakers**

Numerous companies are seeking to broker finance between lenders and small business owners by creating online exchanges where institutional lenders and business borrowers can meet. One example is Fundingstore.com, set up in March 2011, matching businesses that want to raise equity, debt or asset-based finance with potential funders. It charges a fee of two to five per cent of the funds raised. Another example is Finpoint, a matchmaking service launched in Germany in October 2010, which plans to launch a UK operation in the summer.

**Payday loan lender**

Wonga, the online payday loan lender, recently announced that it would offer short-term business loans of up to £10,000. These are aimed at companies that need cash at very short notice for a brief period. The interest charges on these loans are high, although the company points out that repayment is in a matter of days and the cost is far less than that paid for unsecured overdrafts from the high street banks.

**New forms of factoring and invoice discounting**

Following the success of Receivablesexchange.com in the US, several online platforms for invoice discounting by SMEs have sprung up in the UK. A key feature of these websites is their use of auction systems to enable bidding from multiple lenders, which has the effect of bidding down the ultimate cost of working capital to the business borrower. Marketinvoice was the UK's first auction-based invoice discounting platform, completing its first invoice auction in February 2011 and since then about 90 companies have auctioned invoices on the platform.

**Supply chain finance**

This is described as invoice discounting on steroids, providing a short-term advance on an outstanding receivable in return for a percentage fee but with additional features that can reduce the cost of borrowing. The most important of these is that in a supply chain finance transaction the invoice has already been approved for payment by the customer at a fixed future date. There are thought to be a few hundred supply chain finance programmes running in the UK.

*Source: Centre for the Study of Financial Information*

Companies that are growing are unlikely to find that a straightforward overdraft or term loan are likely to meet their needs, he adds.

Rather than getting the bank to back you, it might be worth tapping the personal wealth of bankers themselves. This has been a successful strategy for Shoreditch-based Tom Adeyoola, who used the proximity of his business Metail to London's Square Mile as an opportunity to tap the wealthier members of its workforce for angel funding.

Adeyoola has raised more than £2m for his business, which has developed a clever 3D visualisation system enabling online clothes shoppers to see what they would actually look like in garments before they buy. All of this has come from wealthy individual backers, many of whom are bankers, Adeyoola says.

"I have actively sought out that community because they make quick decisions and they have still got jobs," he explains. "They have certainly got some money."