Growing Your Company with Equity

Many small to mid-sized companies reach a plateau where they find it difficult to obtain the capital to grow and expand, implement efficiencies to improve margins, or launch and sustain the marketing and advertising necessary to penetrate new markets. In the world of small business financing, there are lenders and there are investors. These are the two sources of funding that can provide the funds needed to grow your business. Which is attainable and therefore the better option?

Debt Lending

If you can get them, traditional secured loans, like those offered by banks, credit unions, and savings and loans are the typical form of debt financing. Forget the cost of these instruments, the much bigger issue for small businesses today is in obtaining them at all. When you are successful in getting a loan, they eat into profit dollars and usually are repaid in monthly installments and almost always require a personal guaranty on the part of the borrower. Inventory, accounts receivable, equipment, real estate and insurance policies can all be used as additional security on a loan. If the borrower can't pay back the loan, this collateral can be used to satisfy payment.

Factoring, merchant cash advances, and the use of personal or business credit cards are all examples of other alternative debt financing options. Unlike traditional loans, some alternative debts like merchant cash advances are paid back as a weekly or monthly percentage of a merchant's sales, not as a set monthly payment. The risk to the business is alternative lenders charge higher interest rates than traditional banks do, conversely, they are also more likely to fund business owners whose credit scores are less than perfect or those who don't have sufficient collateral to guaranty a loan.

A traditional perceived advantage of using debt financing over equity financing is that lenders, unlike investors, don't have any say in how you run your business. With debt financing, business owners enter a relationship with lenders that ends as soon as the lender has been paid back.

Debt Downside

Loans are by far the most common source of small business funding, but using debt to finance a business does have its drawbacks. For businesses that are strapped for cash they will have to spend a sizable portion of their monthly revenues repaying the money they borrowed from lenders. Thus, the biggest disadvantage of using debt to finance growth is that debt requires repayment. Every month, regardless of revenues or how well the business is doing.

Equity Investment

Usually a more profitable option for business owners is investing your own money and/or attracting investor money into your business in the form of equity financing rather than debt financing. Equity financing is when you sell “shares” of your company to outside investors to finance your business. When you make money, your investors are entitled to a portion of the profits instead of you servicing a loan payment. Unlike debt financing, the capital raised through equity financing isn't paid back in monthly installments with interest. Instead, investors put money into a business and become partial owners of that business. They are then entitled to a share of the business's profits over time.

The most common source of equity for small business owners is friends and family. Friends and family investments are usually made when businesses are just getting started, before entrepreneurs can obtain debt or equity financing from other sources. Unfortunately, for most, this is a very limited resource.

You may next search for Accredited or Angel investors, these are people who either have $1 Million in the bank or make $200,000 annually. These are the “sophisticated investors”, that is people who the government considers smart enough to decide whether to invest in a risky company, like yours. While an excellent resource, mining it can be a tedious process, and it is likely you don’t know many such Accredited Investors.

Accredited (Angel) investors and venture capitalists are often lumped together as one source of funding, actually they are very different and serve two distinctly different functions. Angel investors are individuals who invest their own money (usually between $25,000 and $100,000) into a business, typically during the early development of a company. Venture capitalists, on the other hand, usually fund substantial multi-million-dollar business growth into burgeoning businesses. Unlike angel capital, venture capital is not private, it's typically controlled by a venture capital firm or a fund, not an individual.

The Equity Advantage

Equity financing isn't for everyone, but it does provide a welcome alternative to debt financing for many business owners. In fact, equity financing cannot be charged with the two biggest gripes business owners level against debt financing: the constraint it places on available cash flow and the risk associated with personally guaranteeing a loan. Equity eliminates the disadvantages of debt in that it does not divert capital from the business in order to pay down debt, and it also shares in the business risk along with the owner. Equity investment for many is an accessible and attainable solution for their growing capital requirements.

Perceived Equity Disadvantage

The biggest perceived disadvantage of using equity to fund a business is that equity investors actually own a percentage of the business in which they invest. Most owners understand they will wind up with a smaller piece of a much larger pie. What the business owner fears is a loss of control, that by giving up too much of an equity stake in his or her business, he or she can quickly lose control of the day-to-day operations of the business. They fear an equity partner could be influential in the culture and operations which could have many implications (positive and negative) on a business.

Cardiff Lexington offers equity financing with the promise of not taking control of, or exerting influence on, the companies in which it invests. Quite the opposite, Cardiff seeks great management partners who prefer to maintain control of their business and want a passive financial partner.

Why Companies go Public?

There are two basic reasons. Raise Money. Create Liquidity.

First, technically an Initial Public Offering (IPO) is just another way to raise money, but from a much larger pool of investors. Through an IPO, a company can sell stocks on the stock market and anyone can buy them. Since anyone can buy the stock you theoretically can sell quite a bit of stock in a short period of time rather than the tedious process of going to individual investors one by one and asking/convincing them to invest. For companies looking to grow and expand and in need of capital, equity investment is often preferable and achievable when conventional financing is either not readily available and/or as attractive.

The second reason for an IPO is to create liquidity for all the people who have invested in your company so far, including you, and are holding either il-liquid or restricted shares of your stock. This is stock for which there is no ready market where you can simply go and sell it for cash. The people who have invested so far want a liquidity pathway whereby they are finally able to convert or sell their stock and realize whatever gain they are due. Future investors will have greater interest when there is liquidity and therefore a known dependable exit strategy for their money.

Cardiff Equity Alternative

Cardiff Lexington is a public Holding Company. We raise money. We provide liquidity. We are growth oriented. Equity financing for companies through Cardiff Lexington takes the form where that company becomes a wholly owned subsidiary.

What does that mean? Cardiff Lexington acquires the company through and exchange of cash and common or preferred shares or makes a tax-free exchange with the business owner providing an anti-dilutive Cardiff Lexington preferred share class unique to that business owner in exchange for the current outstanding shares in the business owner's company. After a brief period, usually six months, this preferred stock may begin to be transitioned over time converting, often at an advantageous premium to our marketable common stock. The business owner may through preferred shares retain up to 90% ownership and absolute control of their subsidiary company.

Cardiff Lexington does require the business owner to concurrently enter into a five-year management agreement to operate their subsidiary. They now have access to Cardiff Lexington Investors and can also offer liquidity to any investor.

When a business owner joins the Cardiff Lexington diversified portfolio that immediately mitigates their risk and that of their old and future new investors. The owner continues to manage all the affairs and activities of their company with the authority to take all steps necessary or desirable to make decisions concerning day to day operations of whatever type without limitation. Cardiff Lexington seeks to partner with, and invest in, companies comprised of great management, well positioned within their market and industry who are producing strong margins. Together we achieve to grow exponentially and mutually prosper accordingly.