Be creative in your approach to funding

Conventional wisdom holds that you should never do business with family and friends, but when it comes to raising funds for your business, the bank of mum and dad (or sister and good friend) is an invaluable and often-overlooked source.

Adam Molai, an African industrialist and founder of TRT Investments

So says Adam Molai, an African industrialist and founder of TRT Investments which manages a diversified sector portfolio and operations in Nigeria, South Africa, Zimbabwe, Zambia, Mozambique and Botswana, and whose latest interests have seen a foray into the US and European markets.

With lack of access to funding cited by South African entrepreneurs as a perennial obstacle to setting up or expanding their businesses, Molai – who has started scores of successful businesses in the country – says it is critical that entrepreneurs are creative in their approach to funding.

“Many entrepreneurs blame lack of funding for the failure to get their business off the ground or for the reason that their businesses fail, but they are not being creative about accessing money. While the more formal access routes to capital – such as loans from banks or lenders – should obviously be pursued where available, crafty entrepreneurs look for other ways to access capital, ways that are not necessarily monetary but are as valuable,” he says.

Borrowing money from family or friends is one source of funding that is often overlooked

“It is true that you shouldn’t do business with friends and family, but you should not discount crowd funding from friends and family when you’re trying to raise money to get your business off the ground. Raising small amounts from friends and family in return for equity in your business or in return for interest is another way to raise capital as it is a cheaper way to borrow money than the more formal routes,” says Molai.

Molai says that to avoid burning bridges, the entrepreneur should have formal agreements in place with a clear plan for repayment of the loan or loans, or for giving equity in the business in return for the loan.

Another source of credit which entrepreneurs often overlook is their home loan

“If a house or car is not generating income for you, it’s a liability. Entrepreneurs need to look at how they can convert their liabilities into assets. In the case of entrepreneurs who own a home, most have access to an access bond which they can be used to fund their business. It’s cash that’s readily available to them that they are not accessing,” says Molai.

Then there are stokvels

Stokvels are worth billions, and they are increasingly turning to investing in small businesses and stocks to generate better returns for members.

Molai says entrepreneurs should also look at taking advantage of Enterprise Development (ED) and Supplier Enterprise Development (SED) programmes that lots of companies have established.

“Almost all big and not so big corporates in South Africa have set up ED and SED programmes as part of their policy to improve their Broad-based Black Economic Empowerment ratings. Entrepreneurs should look at the companies working in their fields and see what ED and SED programmes they have in place and investigate how they can become part of those programmes. This may not only potentially provide a source of seed funding or access to cheaper loans or a regular monthly stipend, but also provides a guaranteed pipeline for their services and products which all businesses require,” he says.

Pay attention to value

Molai cautions however that entrepreneurs need to pay particular attention to value for equity when looking to access capital.

He says entrepreneurs who want to raise funds by selling a stake in their enterprise need to have a thorough understanding of the value of their business so that they can “approach funders in terms of a value discussion not just price”.

“In terms of raising capital, most entrepreneurs and funders look at price and value as the same. But they are not. Price is arbitrary and value is fundamental. If entrepreneurs are able to demonstrate value rather than just talk about price, they have a better chance of accessing funding or resources,” he says.

Continues Molai: “My partner and I set up Pacific cigarette company by selling 10% of the equity in the business, at concept stage, to raise capital. However, the valuation was rich because we valued it using the net present value of future cash flows method which – because our projections were strong and attainable and supported by a robust plan – allowed us to fund the company from the sale of the 10% equity.

“But with these kind of transactions, there has to be performance as you are selling equity on the basis of your credibility. Should the projections underlying the valuation fail to materialise, this will raise potential equity upliftment issues in the future where the investor will now request more equity for their funds invested, based on your actual performance.”