Carter Clark
Financial Recovery

Briefing Sheet

Business refinancing

What is the aim of refinancing?

While replacing bank facilities, renewing overdrafts, obtaining bank loans, guarantee scheme loans, factoring or capital expenditure requirements are fine in normal business practice, they need careful consideration when the business is struggling. The aims of refinancing must be established in the context of returning a business under strain to a viable business model.

A stop-gap arrangement in the hope of some improvement is not a sensible plan and will not encourage lenders to offer support. The funding requirement of the business must be assessed and the funding structure optimised to maximise liquidity at least cost. The ultimate effect of the process on the business must be planned and monitored.

Refinancing options

A number of financing products are available, though the degree of availability and the conditions attached to them will change with circumstances. Each must be assessed for suitability in the context of the firm's current position and anticipated performance if the finance is secured.

- Bank Overdraft: a temporary increase in facilities from the bank may be possible. The bank will want to see that the problem will be of short duration: a well-argued case can lead to a rapid decision. If the bank is not persuaded, further effort may be required along with commitment from the owners/directors. This may take the form of personal investment or guarantees.
- Small firms loan guarantee scheme: this government-backed scheme can underwrite up to 75% of a loan between £1,000 and £1m for up to 10 years. There are qualification criteria, there is normally a premium on the loan rate, and banks vary in their approach to the scheme. However, capital and/or interest holidays can usually be agreed.
- Factoring: the business sells the debtor book to a factoring company which advances working capital against that asset. The advance will range from 50-80% of value and the charge from 0.5% to 3% depending on the number of invoices, the quality of the debt and how much work the factor is required to collect. All future invoices pass through the system, improving debtor control and cashflow. Factoring is a flexible form of finance but if margins are very low or your debtors pay slowly it may not be suitable.
- Asset Refinance: assets including property, machinery, stock, land and buildings may have an actual value above their 'book' value as a result of depreciation. This can form collateral for loans, providing quick access in a crisis. However, this form of finance may not be cheap and lenders may have a different perception of asset value.

Executive summary

Refinancing, if successful, can transform a company, not only by providing the funds it needs on terms that will aid, rather than add to the strain, but also by opening a relationship with sources of support, expertise and useful contacts. Timing is crucial and so is staying friendly with existing funders.

However, a sound business plan supported by strong reasons for the refinance and a detailed picture of how this will lead to a viable future are essential. If the numbers fail to add up, finance will not be offered.

Have a question?

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- Business Angels: Various angel networks have been set up in the UK to assist in early stage investment. The angels themselves are often high net worth individuals who invest either on their own or as part of a syndicate. One key advantage is that skills, expertise and contacts are also available to accompany funding. Angels often favour high growth businesses where an exit via Venture Capital or Trade Sale is anticipated in the medium term.
- Directors' loans: if directors or senior staff can raise funds privately these can then be loaned to the firm. There may be tax efficiencies in such a process but insolvency or liquidation may affect the right to have the funds repaid. While this may be a quick and cheap option it poses dangers for the directors making the loans if they cannot be repaid and may be a signal to the bank or other funders to start to reduce their advances to the business.

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