Finance and governance: Building blocks to startup success

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You’ve scoped the market, determined what you’d excel at, and are ready to take the leap into creating your business and your starting point is the regulatory set-up in your country and business sector.

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First, decide how big or how complex you want this business to be. There are various options for company legal structures but the most common is a sole proprietor, if you intend being a one-person business selling their time or labour or a (Pty) Limited that may have multiple shareholders and offer different legal protections. This also hinges on whether this business will “die” with you, or whether you intend to create something that you can sell and create wealth for yourself and other shareholders.

Assuming you are ready to get sign-up clients, you’ll need to have your bank account set up to receive funds and to manage the expenses of your business. Always keep detailed financial reports, which will be required to prove to an investor, funder or even revenue/tax services the income and expenses you are generating.

Phase one: Income generation

In my experience, the first phase is to work towards generating an income. Once you achieve this, the base is formed and then you can start refining and growing the business.

Importantly, don't focus on putting the frills in place – e.g. the best laptop, stylish office furniture, a top-of-the-range delivery vehicle. First, prove that your business can actually make money before you waste valuable cash.

Rent equipment until you have strong reliable cashflows to buy them. Avoid wasting valuable cash on acquiring assets that you can rent or outsource initially. Keep your cash as working capital for the actual deal you receive from your client. Match your costs with your income where possible.

Don't stress about maximising profit initially – it's more important to get the business started and clients in. Then, start maximising profit as you grow.

Why is getting revenue more important than maximising profit initially?

You will need to prove to funders or investors there is a viable need for your business and that it can generate revenue. The more revenue you can prove, or the more deals that you can show that you have done successfully, the easier raising money from investors will be.

Raising funding based on a business plan if you haven't made any sales yet is really difficult, but showing proof of what you have achieved, even in a small way, gives any investor or financier a bit more assurance that your business plan isn't just a document, but it has some credibility to it.

How does one access finance for start-ups?

It is really difficult to raise money for start-ups. Why? Because this is the riskiest time in any business life cycle. Nobody really knows if the business that you present on paper will actually work, no matter how great the business plan looks. It is a well-documented fact that most start-ups around the world fail. Only a small percentage go on to become sustainable businesses. Some figures place the failure rate at almost 90%.

You can understand then why most funders don't want to take the risk - their rate of return for the risk they take is too high, and most would rather stay away. Investors may be an easier source of funding at this stage, but you will usually have to part with a large part of your shareholding.

Investors know the higher risks of start-ups as well, but may be willing to take the chance because of the higher rate of return they could get from owning part of the business.

However, certain companies, like ProfitShare Partners, have a unique methodology mixing the approach of an investor and a bank. They are almost a stepping stone for businesses. They are also willing to take the higher risk for a higher rate of return, but don't require any shareholding in your business.

This type of funding can assist businesses in the early stages by allowing them to keep their shares while accessing capital to grow their business. As you grow and create a robust track record, you can start to access cheaper capital from the banks.

Transformation in the Financial Sector Codes of Conduct

Codes of conduct and corporate governance within the financial sector demand that business owners "act in good faith, responsibly, with due care, competence, and diligence, without misrepresenting material facts or allowing my independent judgment to be subordinated. I respect the confidentiality of information acquired in the course of my work except when authorised or otherwise legally obligated to disclose". Part of adhering to these codes will obviously include staffing issues and the need for transformation that includes diversity and fairness that affords any employee opportunities to succeed, regardless of religion, race, age, gender and physical impairments.

This must be proven to investors who will be looking to spend their money with companies that show similar ethics to their own. Companies around the globe have been transforming in culture and ethics to ensure they offer investors, staff and clients the best opportunities for growth.

Digital: Another key area of transformation

Digital transformation isn't a buzz word, but a necessity for every business. Why? The traditional way clients access your business and services has changed. Even a little bakery or restaurant now serves up meals to clients it has never met, via food delivery apps such as Uber Eats.

Some restaurants don't even exist in the traditional sense, and are called "dark kitchens". Many online retailers don't have their own stock or warehouses. These are ordered directly from the supplier, who could be anywhere in the world, and shipped directly to the client without the retailer even touching or seeing the merchandise.

This means the barrier to entry becomes even lower and anyone can compete if they have a decent product and great online marketing.
All this is achieved via digital marketing, digital commerce, digital logistics and digital payment tools. If your business cannot integrate with any of these, you risk becoming irrelevant to an increasing digitally savvy client base.

Long-standing existing clients may find it difficult to work with a company that cannot integrate digitally into their world, making their lives and reporting more difficult.

In the major global economies, most businesses are not just digitally transformed but are now using Artificial Intelligence (AI) as the next level to further enhance the digital transformation experience.

While there is much more to starting a business and maintaining proper corporate conduct, it is beyond the scope of this article to include every detail. However, the information noted here will give you a head start on your business plan, and I would suggest adding to this by engaging with successful owners of start-ups and those in the tech industry who can assist with keeping you ahead of the digital transformation and AI curve.

At ProfitShare Partners, we have always encouraged taking advice from those in the know – their value can keep you on track and steer you to greater success.

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