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IN BOX

Choosing between bank loans and equity financing

February 22, 2010 | By Karen K. Klein

Dear Karen: When financing my business, how do I decide when to get bank loans and other debt financing and when to seek equity from outside investors?

Answer: Equity financing involves obtaining funds from outside investors in exchange for an ownership interest in your firm.

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It is typically used to fund operations during start-up and to attract and retain key employees, said Bob Gellman, director of the CBIZ MHM accounting and consulting firm in San Diego.

While equity usually provides money for long-term expenditures, "debt is usually incurred to cover shorter-term operating needs, such as a line of credit to smooth out cash flows or a term note to cover asset acquisitions," Gellman said. Unlike equity, debt financing allows an owner to retain total ownership and control of the company.

In today's economic climate, it is difficult for many small firms to get debt financing, so equity funding may be your only choice. In general, however, "the use of debt or equity requires a thorough evaluation of your company's strategic opportunities and cash flow requirements," Gellman said.

In addition, there are many personal factors to consider, he said. "A business owner's personal feelings about autonomy, control, ownership, management, succession, debt and exit timing should also be thoroughly evaluated."

Is globalization just for big firms?

Dear Karen: I always hear about globalization, but isn't the impact mostly on big companies?

Answer: For decades, large corporations have been buying supplies and moving manufacturing overseas to cut costs.

In recent years, new technology has allowed smaller firms to do the same thing "The tools are now in place to allow businesses of all sizes to have a global supply chain," said Damon Schechter, chief executive of Shipwire, an order fulfillment firm. "If a company has a fast-selling product they can sell in another country, the only thing that stops them from entering that market is the degree of their desire."

Buying supplies and selling products overseas no longer require a vast product line or budget, Schechter said. Online tools for managing advertising, shipping and other aspects of a business have created a "border-less" marketplace that is wide open to smaller, e-commerce firms.

Questions? E-mail Karen at inbox.business@latimes.com

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