FINANCING SOURCES FOR COMPANIES AND THE IMPLICATIONS ON THEIR IMAGE

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Abstract

In a market economy in which competition is the main selection criterion for companies, decision taking concerning the financing sources is an extremely difficult process. Selecting and combining various financing sources, based on the updated netto value of each of them is the basis of business development, on which the success of the companies' activities itself can depend

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Introduction

The financial stock market is extremely important for the development of modern economy, and it contributes to resource transfer, from the companies with surplus to those who seek financing resources for their activities. At this level of the financial market we find the „collection of temporary capital available in economy, it's reallotment of the insufficiently or inefficiently exploited one at a certain point and even favoring certain sector reorganization"[1].

Financing sources of a companies

During the development of a commercial society, an important role is played by financing, respectively the used financing sources. Enterprises can choose from a wide range of financing sources, more or less diversified, depending on the development level of the financial system.

Roughly, a commercial society can choose between the following categories of resources:

- Self-financing
- Discounting the commercial output and selling debts (factoring)
- Issue of financial titles on the capital market
- Loans on the banking market
- Commercial credits

Self-financing is constituted from the financial excess resulting from the commercial society's activity, which is used for financing subsequent activities.

Self-financing is the main financial resource used by enterprises, many times being the sole source for financing their activity. Depending on the level of necessary financial resources and the commercial society's capacity to cover this requisite by self-financing, external resources may be used. This position of self-financing – as an indicator in choosing financing sources is based on two elements:

- the number of resources assigned to self-financing emphasizes the performances of the commercial society, being a criterion for assessing the degree of remuneration for investors financing the commercial society;

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- self-financing generates the capacity to reimburse the commercial society's debts, and the risk fund providers take can be assessed.

As opposed to the other financing sources of a commercial society, self-financing defines a society's capacity to independently proceed with its activity, generating the reproduction of available capital and ensuring the capacity to reimburse potential loans.

By self-financing, the company can ensure a viable financing policy, being able to increase the capital by reinvesting the resulting capital and at the same time ensuring the long term absorption of active elements, as well as compensation of risks that appear in a society's activity, for which they create supplies.

Thus, obtained through a profitable activity, self-financing represents a guarantee of autonomy and financial stability for the society, being the starting point in launching any long term business plan. The insufficiency of self-financing would determine a decrement of the possibilities for external financing, given that external fund suppliers will be ready to provide their resources only in the case of proper self-financing.

Discounting the commercial output consists in its being ceased to a beneficiary, in exchange for its value in the moment the operation was executed. This is one of most managers' favorite transactions, for it manages to obtain funds that do no generate future expenses, as in case of loans.

The issue of securities on the capital market results into the increment of the own capital through capital attraction from outside the society, brought in by holders of available funds, who wish to participate in the society's capital. These financial resources providers can be both old share holders of the society, and other investors, each of them placing their capital at the society's disposal and receiving in exchange shares, which prove their participation to the society's capital.

The reason for which external resources are called upon is the insufficiency of the self-financing resources. But turning to capital increment and the issue of financial titles on the capital market can have both advantages and disadvantages, given that the owners of the company can loose control over it, when new share holders own an important number of shares.

When movable assets are issued, the issue price is smaller than the stock market course, formed on the market through direst report between remand and offer, and greater than the nominal value of the shares. This price is thus established so it is attractive for the potential investors and to cover the company issue costs.

The shares issued for capital increment can be purchased both by the old share holders, and by new share holders. The privilege of the old share holders is constituted by the subscription rights they have based on the number of old shares they own, thus covering the losses brought upon by the issue of new shares. Theoretically, these subscription rights are materialized, in the sense that they can be separated from shares and are rated separately at the stock market. The old share holders, owning subscription rights, shall purchase the new shares at their issue price, whereas the new share holders shall purchases the shares at their issue price, plus a number of subscription rights purchased from the stock market. The number of subscription rights necessary for purchasing one share varies from one issue to another, depending on the report between the old number and the new number of issued shares. The same as for shares, the stock market rate of the subscription rights can be greater or smaller than its theoretical value, depending on the **offer and demand**.

These stock market rates of shares result into the fact that the company's value on the stock market is greater or smaller than its theoretical value. This situation is possible because the during the patrimony assessment, the market takes into consideration the society's future evolution. Thus, when a company decides a capital majority by the issue of titles on the stock market, it must have a favorable image and a profitable activity, which should allow it to place shares at a high price and ensure sufficient resources.

As a result of that, stock assessment on the market is an extremely important element for a company who wishes to increase its capital.

Also, loans on the capital market can be materialized in **issuing bonds**, which can be purchased by physical and juridical persons, becoming creditors of the society and not co-owners, as when purchasing shares. The value of the bonding loan is established by the SGA (Stock holders' General Assembly), depending on the offer on the capital market when they are being issued. As in the case of shares, most of the times, the issue value of the bonds is lower than their rated value, in order to make them more attractive and to beat the competition determined by the other titles quoted on the market.

Societies who do not quote on the market usually prefer **loans on the banking market**, which represent for them one of the most accessible options in order to attract capital.

In order to be granted bank credits, societies must provide the creditor with the accounting synthesis documents, based on which there shall be performed an assessment of the economical-financial situation, important for taking the decision of crediting.

The information from the last three years' balance shall be analyzed by the credit officers and used in order to determine the real value of the assets and of the entire patrimony, and for the correct establishment of the risk level for the client, comparing to the risk taken by the bank.

The profit and loss account expresses the way the patrimony figures from the balance were obtained, which was the income and expense fluctuation, which has defined the economical agent's economical-financial evolution, from the beginning until the end of the exercise.

Based on the information submitted by the credit solicitor, the bank shall determine the indicators on which the analysis and assessment of the potential debtor's eligibility were based, respectively how shall analyzed the level and structure indicators, liquidity, solvability and performance indicators. To all these indicators, the analysis of the investment projects add up, as well as the analysis of the economical agent's internal factors, determined by the society's management, the applied strategy and performed activity, and the loan shall be granted only if it's before deadline reimbursement is certain.

The **commercial credit** is used between economical agents and is manifested in the form of payment postponements granted by providers. A commercial society can be granted such credits, but it can also grant them, in all, the deadlines for received and made payments exerting the need for a redemption fund for the enterprise.

The advantages of financing companies through the capital market, as opposed to the banking market

The financial market provides societies with a series of financing resources, which either taken singularly or combined, are at a certain point, the best solution for a certain investment.

Self-financing is the main option for developing an activity. But when their own resources are not enough, societies must turn to gathering capital through various types of loans, either from the banking market or the capital market.

Financing commercial societies through rented resources is a very difficult decision which can affect not only their economical-financial performances, but also their survival capabilities. Choosing the financing methods depends on the number of necessary financial resources for the period they are intended to be mobilized, on the price of the borrowed resources and especially on the society's capacity to reimburse the contracted funds. To these factors, the method used for activity administrations also adds up, the company's relations with the providers and customers, the administration of the cash-ins and payments, as well as the company's financing policy, the manner in which it decides to use the profit resulting from it's current activity.

Depending on all these factors, as well as on other factors specific to every society, they must choose one of the following external financing solutions:

- Banking loans (credits), contracted for different periods of time (short, medium or long term);
- The financing obtained through the capital market, by stock and bond issue.

Each of these financing variants has both advantages and disadvantages, which will make them more or less attractive for the subjects searching for financing resources.

On the Romanian market**, bank loans** are still the most popular method for acquiring the financial resources necessary for the development of a commercial society. No matter if we are talking about contracting short term credits, usually used for acquiring goods and services and for financing an exploitation cycle, or about long term credits, for financing investments or acquiring real estate, economical agents prefer bank credits, as opposed to loans on the capital market.

Banking societies have also diversified their offer of credits for juridical persons. There are credits for realizing new objectives or production capacities, for the expansion, modernization and technological improvement of the existing capacities or for purchasing machines, equipment, means of transportation, or other fixed assets. There are also credits destined for large, medium or small societies, capable to correspond with the reimbursement capacity of each potential debtor.

The value of the credit that can be contracted is generally established based on the proportion of the investment project, on the credit size, as well as on the debtor's reimbursement capacity.

But financing through a long term bank credit has the disadvantage of high costs and the increment of the company's indebtment, which can affect the activity for the next period (for example, it can affect the society's eligibility for certain bids).

Financing through the capital market is an alternative to bank loans, but it is unfortunately not used very often by Romanian societies. It is materialized through sales issues, mainly stock and bonds, but other financial titles as well. One of the most important roles on the capital market is actually attracting financing for societies who wish to develop their businesses.

Financing through the capital market is more advantageous than through banks. In case of banking financing, companies are placed at the banks' disposal and their regulations for being granted the funds necessary for their activity, but when they publicly issue movable goods, the issuing company dictates the conditions of the title sale. Also, being listed in the Stock Market brings companies benefits related to the financing cost, respectively attracting financial resources with advantageous cost conditions, as well an image improvement.

If until 2005 few companies were interested in entering the Stock Market ring, or even on the contrary, many of them chose to withdraw from the Stock Market Rate, this year more and more companies want to be rated in the Stock Market. Proof of this we find in BVB statistics regarding the evolution of movable goods transactioned during 1995-2006. (Table no. 1.1).

Evolution of financial titles transactioned at Bucharest Stock Market (BVB) during 1995 - 2007

Table no. 1.1

Year	2nd Category	1st Category	Liabilities	Total
1995	9	0	0	9
1996	17	0	0	17
1997	63	13	0	76
1998	105	21	0	126
1999	101	26	0	127
2000	92	22	0	114
2001	46	19	2	67
2002	46	19	6	71
2003	44	18	10	72
2004	43	17	25	85
2005	44	20	19	83
2006	46	20	17	83
2007	40	19	17	76

Source: Annual statistical report regarding the activity of BVB

The main reasons that can determine a company to start the stock market rating procedures can be represented by the company's expansion and of its market to a level that requires financing.

The first phase of participating in the capital market is the transformation of the commercial stock society from a "closed society" into an "open society" by building a public offer, certified by CNVM. The object of this public offer is drawing money resources on the capital market, by new issued of other movable values (stocks, bonds etc). The open commercial society must draw up a public offer folder, where it should mention that it has set as target for the next phase to be registered within the Stock Market Rate. Being registered with the BVB Rate facilitates any subsequent operation of capital attraction from the market, making it possible for the company to find the resources necessary to the further development of its activity. Compared to the "closed" commercial societies, where the real share value is more difficult to measure, **commercial societies with shares rated in BVB Rate, are easily granted credits**, because it's easier for creditors to use the current stock market share value than the theoretical approximation which they must perform for unrated issuers.

Investors are generally tempted to buy stock from rated issuers or from future rated issuers, rather than from non-rated issuers. This tendency will make it easier for "open" societies rated on BVB Rate to successfully issue new movable goods and thus attract important cash resources from the capital market.

Subscribing a commercial society in the BVB Rate brings more practical financing means, materialized by the existence of a wide range of instruments specific to the capital market. This category includes the issue of convertible bonds or shares, with attached warrants. These instruments grant the right to subsequently buy share of the issuer's, for a previously established price. Investors will easily be convinced to buy such instruments that grant the right to subsequently buy shares rated on BVB, rather than unrated shares, due to this market's transparency and accessibility.

Another advantage of stock market quotation of commercial societies' shares is publicity. All commercial societies that have movable goods rated on BVB Rate benefit from free publicity all over the country and also internationally, through the following methods:

- The name of a certain company appears in the main newspapers and on the national television stations, after each transactioning session;
- The name of rated issuers appears in the Dow Jones telerate international network.

Also, commercial societies rated on BVB Rate benefit from a reputation that can increase the commercial market segment where they act, this being an important element against competition. Reputation improvement can be manifested directly – through commercial crediting and payment facilities which the issuer can get from its providers and clients.

International statistics show that the admission on the stock market of movable goods issued by a society publicly owned increases its reputation and there's a growth of its shares' prices with an average of 20%.

By subscribing movable goods issued in the BVB Rate there's a growth of the respective society's assets, because than the issuer's activity is performed in good conditions, it's shares' value on the market is greater than their accounting value, having a great request on the market and as a result, increasing their price constantly. Stock market rating also leads to the increment of the commercial fund and movable goods liquidity.

The Bucharest Stock Market (BVB) is an institution specific to the capital market, which by the available means imposes on quoting companies to distribute the information related to their activity and financial situation, to the general public. This information reaches the final investor, directly or indirectly, through studies performed by specialized annalists and advisors. The transparency of issuers rated on BVB contributes the easier follow up on transactions and ratings on the stick market and attracts investors by the easy and viable access to this capital market, thus increasing the liquidity of movable goods.

Other advantages granted by stock market quotation of commercial society's stock:

- **getting employees interested by distributing shares –** through market transparency they avoid social tensions that might appear;
- **the existence of an acknowledged market value**– potential creditors of the issued have the possibility to compare the accounting value of shares with their value on the market;
- **increasing the rate of market management – this being influenced by the activity of the rated society, well known on the market;**
- **simplifying registration in the stock holders' registry,** by having the issuers subscribed to BVB Quote draw up a Registry Contract with BVB, which transfers the obligation to keep account of the property right over issued real estate to BVB;

A financing possibility for Romanian companies is quoting at other stock markets. The main advantages brought by these solutions are:

- better protection of small investors;
- increasing transactions and stock liquidity;
- access to financing sources at a level much higher than the one offered by the capital market in Romania.

But quotation with other stock markets is risky, because the interest of invertors in the respective titles can not be estimated. In 2004-2005, foreign investors have manifested an interest for Romanian stock, but the weight of foreign funds in BVB has not raised, one of the reasons being given by the complicated investment procedure, which imposed the use of a local broker and fund transfer. Should the Romanian stock be available on markets which foreign investors usually place their money, the operational difficulties would disappear, and the investors would be granted easier access to the Romanian titles.

Conclusions

Choosing the financing sources for developing the activity of an economical agent is an important and extremely difficult decision, given that the Romanian financial market is not very well developed and it does not provide a very wide range of instruments to attract the necessary financial resources.

Any of the financing methods presented above can be the ideal solution for a company, depending on its activity, on its economical financial results, but also on its being open to the financial market's opportunities and to the new means of accessing financing.

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