FINANCING TENDENCIES FOR AGRITOURISM ACTIVITIES

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Abstract:
Rural financing is essential to the creation of new alternative work places in the rural areas. Theoretically, in a functional market economy, the rural financial system directs financial resources from those who save towards those who invest over a period of time, in exchange for an interest. The level of the rural income is greatly inferior to the average income per economy, and savings in the rural area are very scarce.

Key words: Financing, rural financing, own capital, leasing, bank credit, financing programs.

In order to create new workplaces in agritourism and thus to diversify rural economy, three aspects are essential:

a) capital investment for business development in the rural space;
b) conversion of agricultural work force and of qualifications in order to correspond to the new employment opportunities;
c) the basic infrastructure necessary to the setting up of other economic activities (transportation and telecommunications, current water, sewage etc.)

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greatly inferior to the average income per economy, and savings in the rural area are very scarce.

It is therefore of relevance to present the main possible financing sources, their advantages and disadvantages to various operators in the agritourism industry.

1. Possible financing sources in view of the development of agritourism activities

In view of the development of agritourism activities, starting from the requisites determined based on the business plan, the following financing sources can be taken into account:
1. Own capital
2. Bank credit
3. Financing obtained from supporting programs
4. Risk capital funds
5. Leasing
6. Credits from providers and clients
7. Credits for commercial papers (factoring and invoice discounting)

1. Own capital
This category includes own resources or those drawn from private partners, not financial institutions, and they constitute, at the time of the establishment of a firm, the best possible thing for a start, be it more modest, but which can be continued through a constant development of the firm’s activity.

2. Bank credit
This category of bank credit providers includes: commercial banks, financial corporations, and, in general, everyone granting credits for business financing. The reticence of these organs in granting credits to newly-established firms is well-known. The bank needs to have the certainty that it will get back the money granted as credit, and the newly-established firms do not provide this guarantee for different reasons (they have no history, no experience, not very many elements to make of these companies stable elements within the economy). Mark TWAIN defined in a very plastic manner these categories of financers as those “who will give you an umbrella on a sunny day and then ask for it back when it starts to rain”. Usually banks award special attention to the debtor’s capacity of paying his debt and according to the degree of coverage of the provided guarantee. A creditor will not show interest in the remote perspectives of a remarkable profitability because, irrespective of the size of the profit obtained, he will only receive the amount advanced as credit and the interest due. The presentation of a

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newly-established firm to a bank must be made in such a way as to make the firm seem the best possible, and in order to do that, of special importance is the knowledge of the aspects holding priority in the researches of banking operators, namely:

- The character of the applicant: the bank’s trust and assurance that the debtor will not suddenly disappear when the business hits a bump. The connections with the community (long-term residence, family ties, ownership of a house) are aspects taken into consideration by banking operators upon receipt of a credit application.

- Financial capacity: the possibility that the business presents in generating profit and thus providing the debtor the chance to pay his dues to the bank in time. From the study of financial projections, the creditors search for a business that is strong enough from a financial point of view to be able to cover the current activity and constitute a risk reserve in addition to the credit reimbursement and collateral interests.

- Provided guarantee: no true creditor will finance a business based on a strong guarantee alone, but every professional creditor will try to obtain the largest possible guarantee for a credit (mortgage rights)

- The contribution of the applicant: banks wish for entrepreneurs to hold a sufficient degree of financial involvement into the business that they wish the obtain credit approval for. From practice, a few other considerations have been deemed important in order to increase the chances of benefitting from a credit at the moment when approaching the potential creditor:
  - The credit application for an already existing business has more chances to obtain financing than the presentation of a business plan and of an application for a new business;
  - The acquisition of the fixed assets (buildings, land, equipment) has more chances to be financed, as these goods are more unlikely to lose value in time;
  - The presence of current assets, of stocks and claims, increases the chances for the granting of the credit;
  - The presence of balance-sheets demonstrating that you have had a profitable activity over the past two years greatly improves the chances for credit granting;
  - The more significant the own contribution, the better the chances to obtain the credit.

- In order to increase the chances of obtaining a credit, the preparation of the action has a particular importance, and it should contain:
  - Information on existing financing lines from financing institutions
  - The choice of the institution and of the credit line based on the financing conditions and on the particularities of the business
• Elaboration of the business plan
• Correct evaluation of available guarantees
• Preparation of documents required by the bank.

One of the frequently encountered causes for rejecting a credit application lies in the lack of the necessary guarantees for the granting of the credit (together with credit oversizing in view of the business needs; credit oversizing as compared to the possibilities of the firm; the lack of the documentation necessary to the granting of the credit etc.) As regulated by the Banking Law no. 58/1998, banks cannot grant reimbursable credits without securing their investments. Therefore, banks require guarantees (preferably real estate) to cover approximately 120% of the value of the credit plus interest. Finding these guarantees, in particular in the case of young firms, which have been on the market for two-three years is quite difficult. Real guarantees are represented by the real estate, equipment, automotives (as ready and as demandable as possible), which the entrepreneur or his firm possess and which they are willing to mortgage in favor of the bank in order to be granted the credit.

In addition to real estate guarantees, there are also other various guarantee formulas (guarantee funds, re-guarantees, letters of guarantee from other banks etc.), from which the best-known are funds with credit guarantee. These funds guarantee, by means of letters of guarantee, the firms that wish to obtain a reimbursable credit.

Guarantee funds existing in Romania: The National Fund for Small and Medium Enterprises Credit Guarantees; The Romanian Fund for Credit Guarantee; The Rural Credit Guarantee Fund.

3. Financing obtained from supporting programs

The banking system in Romania has so far showed no great interest in financing businesses in the rural environment, generally perceived as high risk. Financing applications from the rural environment face supplementary guarantee requests and superior financial costs for loans, and there is even a tendency in the banking sector to reduce the activity in the rural environment due to its low profitability. These issues only worsen the operators’ financial situation, thus making economic development in the rural environment more difficult.

Based on these facts, an extremely valuable financing source at this stage is represented by financing programs, in particular non-reimbursable. In order to accede to these, there is a very clear documentation model that must be elaborated. The documentation thus realized, it enters a competition process with other documentations and the best projects are granted financing.

These types of supporting programs provide both reimbursable financing, and non-reimbursable financing. Reimbursable financing consists of financing by certain banks from public money, the bank refinancing the eligible economic
agents for a lower interest rate than the interest on the market. Non-reimbursable financings represent financial aids granted to economic agents, aid coming mainly from two sources:

- The State Budget;
- The European Union or other international organizations

4. Risk capital (investment) funds

Investment funds are organs for the placement of money availabilities drawn from natural or legal persons, with the purpose of obtaining profit. Through the system of the risk capital funds, the entrepreneur takes the fund as his partner and, as a consequence, receives a significant amount of money as contribution to the society’s share capital. In general, the fund desires to be a minority shareholder in the society and to withdraw its participation after a relatively short period of time, usually after approximately five years. In order for the fund to maintain its position as minority shareholder, the entrepreneur must participate with an amount which is larger than the fund’s and this may be a major inconvenience to small, newly-formed enterprises. For this reason, risk capital funds are destined in particular to large firms that want a capital infusion for a certain period of time, but the possibility for a risk fund to want to partner with a newly-formed firm is not excluded.

Investors are attracted by a business first of all due to the profits that they hope to obtain (out-turn of the invested capital of 25-50% or even greater). They represent that specific category of financers who need to find that that the business will grow and have future substantial profits. If they expected to obtain only 10-15% out-turn of the invested capital, they would direct their flows towards public companies, which present much less risk. But they invest in young growing companies because they expect to obtain considerable profit.

Given that the investors are more willing than creditors to take the risk, they consider financial projections much more important. Whereas banks think “guarantees first and then projections”, investors think in the exact opposite way, paying more attention to perspectives than creditors.

The aspects that the investors are interested in at the time of the analysis of a financing application (within a business plan) are therefore represented by:

The judicious approach of the market: proven by means of the compulsory introduction of the characteristics and requirements of potential customers in the business plan advanced to the investor. The description of the products/services realized by the respective business will not be worth anything if it is not shown HOW and TO WHOM they will be sold.

The proof of acceptability: it must incur that the problem that the business tries to solve is important enough for a large number of people to become clients of the company.
Business protection: the investment risk can be reduced if the entrepreneur holds ownership rights under the form of licenses, certificates, patents, trademarks. These can limit competition, at least for a limited period of time.

Credible provisions. It is very true that risk investors pursue businesses with rapid growth, but as they are presented with hundreds of business proposals annually and as they already hold investments in various fields of activity, they already have a good sense of provisions. Any society suggesting provisions that surpass these limits of the reasonable will raise real question marks.

Liquidity is a very important element for risk investors. Although the investors have a long term vision when financing a business, risk investors have a short term vision of placements. They aim to liquidate the investments into small companies over a period of 3-7 years in order to remunerate the individual owners of the invested funds and in order to have financing sources for new promising businesses. Generally, rapidly developing firms do not have sufficient current money to pay dividends, investors can obtain liquidities by selling shares possessed in their share capital. That is the reason why risk investors attempt to assure their exit by selling shares on the stock market or to an interested company.

In the event that an entrepreneur persuades a risk capital fund to join him in a business, then the respective firm has three great advantages:

It receives a capital infusion for a longer period of time, while it needs not pay any interest;

This capital infusion does not appear in the firm records as debt, but as own financial sources (contribution to the share capital);

Together with the money, the fund brings along its specialists, who will assist the entrepreneur in the firm management.

In conclusion, the most appropriate financing source for a business is decided according to the interpretation of the business’s financial projections; if the forecasted evolution is fulminating, there are chances to attract risk investors.

5. Leasing

Leasing (crédit-bail) is a special form of achieving the operation of crediting on the medium and long term in order to procure various equipment through the mediation of certain leasing societies. The equipment is bought by the leasing society and subsequently rented to the applicant. Oftentimes, the applicant himself is authorized in the name of the leasing society to buy the equipment he needs. The leasing contract will then be concluded between the leasing society and the applicant, and through this contract the applicant receives the equipment to use. This form of leasing is also called commercial leasing, and it represents the main form of leasing. Other leasing forms are lease-back and time-sharing.

1. In the lease-back form, the owner of the equipment is the same as the applicant who urgently needs money. In this case, he sells the equipment to a leasing society, then renting it from it.
2. In the time-sharing form, there are several applicants who wish to use the same equipment, but everyone only uses it for a certain period of time. Irrespective of the form in which leasing is made, at the end of the period, the applicant has the following options:

1. cessation of the contract
2. its continuation for a new period of time;
3. buying the equipment at the pre-established price.

Leasing is performed by the bank or by a society specialized in crediting. The documents to be presented are the crediting application, the last two balance sheets, the last two balances, the pro-form invoice of the leasing object, bank statement. The leasing society will buy in its own name the leasing object by means of a sale-purchase contract, and it will then rent it to the creditor society by means of a rent contract.

6. Credits from providers and clients

Financing by means of this method is one of the least expensive financing options for the short term. A buyer buys a product from the provider, and undertakes to pay it over a period of time. All this time, he uses in the interest of his own firm his own money, which he should have paid the provider. Conversely, a buyer pays a provider a certain amount of money, and the latter delivers the good or performs the service at a later date (the case of anticipated payment for agritourism services). All this time, the provider can use the client’s money in the interest of his own firm.

These credit forms are called real credits and are widely spread in Europe, and due to the mechanisms of market economy, they enjoy expansions into Romania as well. We must however mention that this type of mutual financing is achieved between partners who are trustworthy to each other, and the amounts exchanged are not very large, but sufficient in order to optimize a company’s cash flow for a short period of time.

7. Credits for commercial papers (factoring and invoice discounting)

7.1. Factoring represents a short term crediting form granted to a commercial bank by compensating the providing credit. The credit is guaranteed with an invoice before the deadline. The invoice is a result of a sale-purchase contract between the provider and a buyer.

In fact, from a legal point of view, factoring represents a contract concluded between the bank (the factor) and the client (adherent) by means of which the factor (the bank) undertakes payment at the presentation of documents attesting a commercial debt to a certain amount of money in exchange for a commission.

The amount of money that the bank pays upon presentation of invoices is named immediate financing or available factoring. The amount of money that the
bank pays when collecting the invoice amount is named financing upon collection or unavailable factoring.

In the event that there is an invoice payable at the due date, but the need for money appears before the due date, then the invoice shall be paid for by the bank at a smaller price than the one recorded on the invoice, and the bank will then collect the full price. The difference between the price paid by the bank and the collected amount on the due date will be used by the bank to cover expenses and to form profit. The bank will actually buy the invoice for a smaller price.

7.2. Invoice discounting

Invoice discounting represents a short term form of credit granted by commercial banks by paying certain commercial papers before the due date (installments, promissory notes etc.)

Invoice discounting represents the operation of buying by banks of commercial papers owned by their clients in exchange for a grant of the discount credit and the retaining by the bank of an amount named agio, made up of the value of the discount together with the commissions. As with any crediting operation, discounting presupposes the deposit of a guarantee commonly agreed upon and materialized in a percentage applied to the nominal value of the discounted papers.

A commercial paper represents a commitment that a drawer takes in the name of a drawee in favor of a beneficiary. For instance a payer (drawer) deposits the money in a commercial bank (the drawee) and issues a cheque (the commercial paper) to a provider (the beneficiary), so that the provider (beneficiary) will recover the money from the commercial bank (the drawee) at the due date by presenting the cheque (the commercial paper). In the event that the beneficiary needs the money before the due date, he can discount the respective commercial paper at a commercial bank, and the bank will honor this for an amount smaller than the one recorded on the commercial paper, and on the due date he will recuperate the money from the drawee, or rediscount the commercial paper before the due date with another bank or even with the National Bank.

Discounting, rediscounting, and factoring are resorted to for financial reasons (one leu that we do not have today is worth more in its present value than five lei in two years, even if they are not eroded by the inflation).

CONCLUSIONS

The financing of the rural space for agritourism development has started to be of interest to financiers, as well as to investors in the rural environment. The multitude of financing methods and possibilities offers every investor the opportunity to choose the most convenient financing methods, considering the specific character and the profitability of the investment. With the integration of Romania into the European Union special attention must be paid to investments financed from structural funds placed at the disposal of our country by the
European Union, by means of programs destined to the development of agriculture and the rural space.

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