

Raising equity

Q. I work in the hotel industry and am in the process of purchasing a 19-bed hotel and restaurant in the South west of England for £1.2m. I have arranged private finance and equity from my house sale to cover most of the cost but I am looking for an investor or investors (silent) to help fund the purchase (anything from £25k upwards). I am not having much luck finding people or institutions that are looking to invest in private hotel projects though. What can I do?"

The simple answer is probably 'ask the family' but it might be the wrong question that is being asked.

Equity is more expensive than debt – the cost of servicing debt (interest) is tax deductible whilst the cost of servicing equity (dividends) is not. So the entrepreneur should first make sure that he/she has the right amount of debt. As described, the hotel is being bought with an equity release loan on a private house. It depends on the corporate structuring but it is possible that such interest on this debt is not tax deductible – the entrepreneur should ensure that he/she has secured debt on the hotel building or business itself.

Assuming this source of (cheap) finance has been maximized, other sources of capital exist with customers and suppliers. A typical hotel operates with negative working capital (i.e. creditors exceed debtors and stock) and the three or four weeks worth of operating expenses may be a significant source of capital. The cost is hidden in the unit prices charged by suppliers, but is obviously tax deductible. The hotelier can also leverage other aspects of the business to raise capital – granting a restaurateur a lease on the restaurant in return for a lease premium provides a source of finance; selling space on the hotel bedroom walls to the local art gallery raises capital; selling space in the garden for advertising to promote local business raises funds.

Customers are a source of finance through advance deposits – wedding parties that pay a healthy deposit several months up-front can be a long-term source of finance. Customers that use the hotel's meeting rooms regularly might provide funds if a meeting room were named after their founder or a local hero. There are schemes called fractional ownership in which customers become co-investors but these are probably only applicable when all other sources of funding have been exhausted.

And, since there is no such thing as a 'silent' third party equity player, family should not be ignored.

End

Registered office	Phone: +44 1752 873198	Main office
84 Fetter Lane	Fax: +44 1752 872399	Old Cottage at Nymet
London	www.hotelsolutionspartnership.com	Noss Mayo
EC1 4BE	Company registered Cardiff no: 4891951	Devon
	VAT no: GB 819 2713 22	PL8 1ED