Finance

Businesses need finance for their day-to-day activities and in order to grow and change over time. Businesses must respond to their external environment in which the actions of their competitors, customers, suppliers and other parties influence the decisions they make. Business finance comes from a range of sources:

* Internal finance comes from owners - shareholders in the case of private and public companies.
* External finance is provided by banks, and other institutional lenders, as well as creditors.

Businesses frequently need to grow or to change their structure in response to changes that are taking place in the external environment.
Internal finance therefore can be quite an inflexible way of responding to the changing environment because profits take time to develop, although they can be ploughed into a reserve fund.

External financing

A quicker way of growing therefore is to raise finance from external sources, typically loans. However, the danger of borrowing too much externally is that there are associated interest payments. In ongoing periods the business is saddled with these interest payments which can curtail future profit making potential.

A food processing business like Kraft or Kellogg's is faced by a highly competitive external environment. This requires continual change in the organisation e.g. in the form of investment in new food technologies and plant. Part of this expansion can be financed from internal profits, but these organisations will typically seek some form of external financing including loans and other forms of credit to fund their expansion programmes.

Finance for internal (organic) expansion typically comes from selling new shares or ploughing back profits. Finance for external expansion will often come from borrowing.