Capital markets – financing alternative when banks are cautious 1/36/22

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As company balance sheets become increasingly saturated with liabilities and future cash flows less certain, the scope for obtaining bank finance on balanced terms is limited. Yet companies need fresh capital to continue investing and to make their business more resilient to energy shocks and lack of raw materials, and to cope with rising costs, which often cannot be offset by an increased price of the end product.

If you plan smartly and do the necessary homework, capital markets can help you resolve a shortfall of funds and achieve a diversified portfolio of finance sources for your company in the long-term.

Macroeconomic trends don't let entrepreneurs slack off

Since early 2020, the global economy has been posing challenges to entrepreneurs. The wave of Covid-19 in early 2020 caused many companies to drastically reduce their production capacity in order to survive in the face of the reduced demand. They took on additional liabilities and used their free cash to ensure their future operations.

When the summer came, the global demand recovered rapidly, leading to a coordinated restart of any previously stalled capacity (and human resources) and to additional investment and debt being tied up in new capacities to meet the strong demand.

Russia's invasion of Ukraine in February 2022 made CEOs repeatedly revise their supply chains and optimum capacities to maintain an acceptable level of return to shareholders.

In other words, since 2020 companies have been faced with the "perfect storm", which has led to weakened balance sheets, lower margins and greater uncertainty about the future, including about future opportunities to continue funding their operations in a traditional way.

Benefits from capital markets

Capital markets provide alternative financing on the best possible terms (not only rate or valuation) and overall can ensure access to finance when traditional options are exhausted:

1. Maturity adjustment. When issuing a bond on capital markets, the company can aim at longer repayment periods than in the case of bank financing. It is theoretically possible to issue bonds maturing in 15, 20 or even 30 years, yet in practice the golden standard is 5–10 years.
2. An advantageous repayment schedule. There are many ways to structure the bond repayment schedule, yet a bullet bond is practically the best in Baltic experience. This means that the company issuing bonds pays only interest and repays the principal at maturity. This allows the company to refinance the bond at maturity by issuing a new one where the capital raised is used to repay the old instrument.

3. Easier terms. When issuing bonds on the stock exchange, the company can expect easier terms and fewer restrictions on the capital structure, as well as new capital placement programmes.

How to use the potential of capital markets

To successfully raise funds through the stock exchange and issue bonds on the best terms, a few important pieces of homework need to be done. Everything is based on a good and transparent corporate governance, with a skilled financial management and a clear plan for explaining to the investors why finance is being sought. Three technical steps should be taken to use the potential of capital markets successfully:

1. Hiring a certified stock exchange consultant, who will help issue bonds on the alternative stock exchange (Nasdaq First North) and will then monitor compliance with the stock exchange rules.
2. Preparing a detailed business plan to convince the funders about the amount of finance required, the term and the rate, and to prove that credit risk is limited.
3. Building excellent accounting and investor relationship processes in order to duly disclose financial information to the stock exchange.