# FUNDING MODALITIES A COMPANIES AT NATIONAL AND EUROPEAN LEVEL

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**Abstract:** *Whether we are discussing ways of financing at national or European level, doing business at the level of a company generates important financing needs related to the exploitation cycle, as well as development, restructuring or modernization activities. For their funding, internal and external resources can be used. As a rule, investment activity is the most important "consuming" of external resources. As the company has more possibilities to finance its business, it is a question of choosing the ones that best fit its needs. This selection is made taking into account certain conditions limiting the scope of resource procurement. Long-term resource needs can be met by appealing to the banking system, the capital market, specialized firms or the state. Since these resources are part of the permanent capital, being found in the company's financial mechanism for a long period of time, a proper substantiation of the financing decision is required. In this respect, the ratio between leverage finance and equity must provide the lowest funding cost, with funding decisions based on optimizing the proportion of the funding source, allocation and use of funds, and obtaining future financial surpluses that will allow reimbursement lending and business development. Establishing a financial structure is an important decision that is included in the company's financial policy. Thus, it is necessary to decide how to allocate funding between short-term debt and the use of permanent capital. Moreover, we are currently witnessing a great deal of challenges in how to finance a company, funding using digital technologies is one of the most current ways.*

**Keywords:** *financing, sustainability and business development*
**JEL Classification:** *F17, G23 and O31*

## Introduction

The analysis needs to be deepened on the structure of permanent capital, making it necessary to choose the proportion of equity to borrowed in the medium and long term. the financing decision must be based on leverage, the level of financial profitability, the type of financing needs, the cash-flow forecast for the upcoming period. However, the fact that the financing decision is also subject to the influence of the evolution of some indicators macroeconomic: inflation, interest rate, exchange rate, GDP but also fiscal and legislative components.

## Research methodology

In order to underpin research methodology, we used classical observation and examination instruments, research methods based on the basic principles of scientific research. Procedures based on factual analysis, intensive documentation at the level of internal and international literature have been used, using the existing databases and scientific material in endowing the libraries of specific institutes in Romania and internationally (Manta 2018a).

The methodology of the research paper has as a direct instrument the collection of data and information from the literature and from the existing practice in public and private institutions, but especially scientific articles published on specialized research networks (ResearchGate, Academia.edu, etc.), published articles in various journals, relevant books in the field of reference, legislation, analyzes and studies, official documents of various tax bodies, fiscal documents and interactive database of the National Bank of Romania, other relevant sources identified in the libraries: CCFM, Romanian Academy , INCE, IEN, BNR, National Library, INS, etc. Moreover, in the methodology we analyzed the documents using the comparative, analytical, descriptive method, the nonparticipative and participatory observation, the use of a set of information sources, the collection of financial data in the established databases. Also, the paper was based on annual reports, publications, consolidated statistical data provided by the European Commission, the National Bank of Romania, the European Central Bank (ECB), the International Settlement Bank (BRI), the European Commission, OECD, published annually. have been processed in order to be able to offer an overall and analytical picture of the most important changes taking place in the European Union as a whole but also globally -

considered to be representative of the understanding of the phenomena studied, and especially in Romania (Manta 2018b).

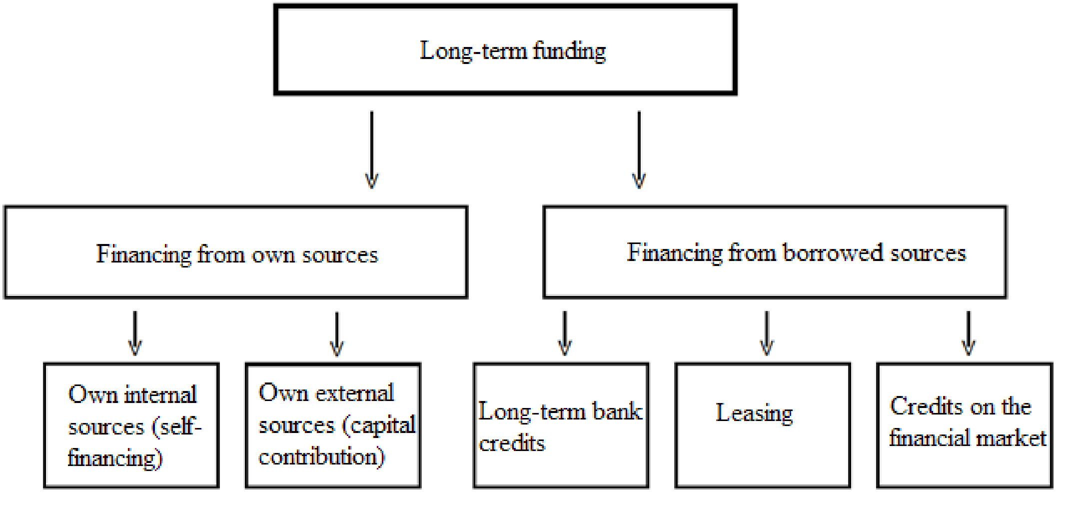
## Research results

Improving the methods and tools for selecting funding means appropriate to the needs of the entity put together four types of financial resources (Vasile 2006):

- Self-financing;
- External financing through participation in the company's equity;
- External financing through loans or credits granted to the company;
- Lending between businesses / commercial credit.

In general, long-term funding can be described schematically in the following figure.

**Figure 1. Long-term financing of the firm**




*Source: own processing*

Firm financing from internal sources depends on the amount of depreciation and provisioning, calculated and not yet consumed, by the amount of unpaid profits, and by the size of disinvestment revenue. Since depreciation is a tax deductible expense, it results that the tax savings thus achieved significantly reduce the cost of self-financing.

Self-financing is the basis for any company development (Vasile, 2006). It is the most widely known form of financing for economic agents and requires the entity to provide its own development, using as a source part of the profit obtained in the previous year and the amortization fund. It aims to cover the need to replace fixed assets, but also to increase operating assets.

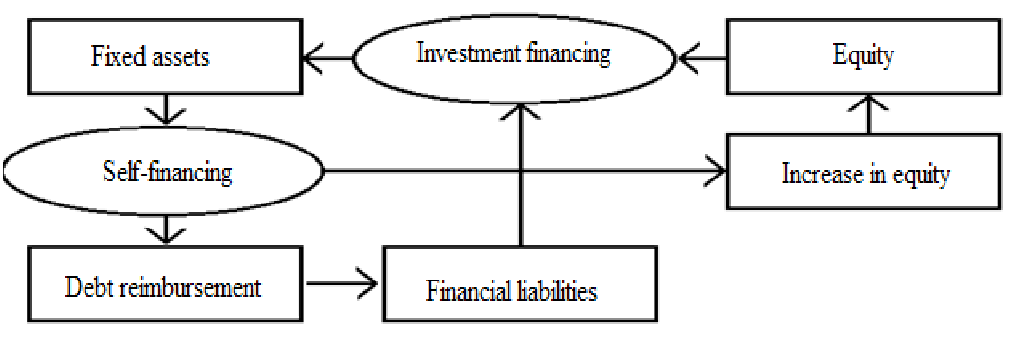
*In a market economy the main advantages of self-financing are* (Sandu 2000):

- is a safe means of financing, given that in some situations the firms face difficulties in collecting capital on the financial and monetary market.

- defends the company's freedom of action in the sense that the financial autonomy gained through self-financing allows it the independence of management from financial and credit institutions, bodies that exercise rigorous control to ensure the guarantee of the recovery of the loan capital. However, self-financing has a number of limitations, due to the fact that any other financing category of the firm outside self-financing is in fact based on the expectations of creating a future self-financing capacity. These limits are expressed by the fact that some firms may have a high self-financing capacity but do not need large financing, while other firms face the reverse phenomenon (Sundararajan 2007). For this reason, self-financing does not ensure a real meeting between funding capacity and funding needs, which, in the national economy, can cause some imbalances. In addition, self-financing capacity may be highly fluctuating over time, often for reasons not attributable to the firm in question, but to the economic environment in which it operates.

From a dynamic point of view, the accumulation cycle of the firm's money resources from which self-financing will be fed can be described in the following figure.

**Figure 2. Cycle of accumulation of firm's money resources**




*Source: own processing*

Self-financing (AF) has two components:
a) self-financing of maintenance (AFm);
b) Growth self-financing (AFcr):

$$AF = AF_m + AF_{cr} \text{ , where: } AF_m = Am + Pr \text{ , where:}$$

***Am*** represents the depreciation (gradual extinction of long-term credits, successive payments or redemption of claims); creation of the funds needed to replace the physical and moral wear and tear of fixed assets owned by a firm in kind (through repairs and capital construction) they transmit their value on the value of each product unit.);

***Pr*** are the provisions (percentage remuneration due to the one who commits a commercial business, draw, commission)

$$AF_{cr} = B_{nd}$$

where with $\mathbf{B_{nd}}$ the value of the undistributed profit in the form of dividends was noted (Dobrota & Chirculescu, 2009).

*Share-capital increase through equity* is a form of self-financing as well as self-financing. The difference lies in the fact that while self-financing is an internal financing achieved through the company's own effort, capitalization of a part of the profit - the capital increase through the issuance of new shares represents financing from external sources, funds from outside the company by actual or potential shareholders. From this point of view, capital increases through equity issuance resemble debt financing (Dobrota & Chirculescu 2009). The issue of shares leads to the increase of the company's money, to the increase of its solvency, to the strengthening of the working capital and thus to the strengthening of the financial equilibrium as the increase of the capital permanently determined by the increase of the share capital is not immediately accompanied by an increase of the immobilized assets of the working capital is transient (characterized by the change over time) because afterwards these funds will mostly be invested in immobilized assets).

Subscription to shares has a contradictory, dilutive effect on the firm's valuation by investors: on the one hand, it has a negative effect on the profitability of the company's shares because the overall net profit realized will be distributed over a larger number of shares, so the profitability of an action decreases and, on the other hand, has a positive effect, as the creditworthiness and guarantee of the firm grows due to the increase in equity, which may require additional credits. The capital increase can be done by issuing new shares by distributing free shares by increasing the nominal value of the old shares (the third alternative is less frequently used). The issue of new shares can be done in two ways: - at the nominal value of the old shares; - at a higher value, depending on the market value of the old shares.

Although the increase in share capital may not only result in the subscription of new contributions but also in the incorporation of reserves or debts converted into contributions to the share capital, only the creation of new contributions to the share capital contributes to the financing of the net investments, the other sources being only conversions a (state) loan issued earlier, in the sense of changing the amount of the interest, the extension of the payment term, the merging of several previous loans, etc.

The capital increase through the issuance of new shares can only be achieved when the old subscribed capital has been fully paid. In order for the issue to be practically achievable and attractive, the issuance price of the new shares issued should be lower or at most equal to the market value of the old shares.

*Financing by bank credit* (Dobrota & Chirculescu, 2009). Bank credits are contracted for periods of time established by the contract between the banking institution and the applicant for well-defined purposes. They are generating costs in the form of interest and bank charges that can be paid monthly, annually, at the end of the period or at the time of contracting (commissions and fees (expenses incurred by someone for a journey, for certain services, for putting into practice of an initiative, etc.). The loan terms, ie the interest rate, the repayment term, the possible grace period, the penalties for non-observance of the contractual clauses, etc., are negotiated between banks and debtors. The level of interest on bank loans is higher than that used by specialized financial bodies. The size of the bank loan cost, ie the interest rate, is determined by three factors: credit volume, interest rate, and lending time.

*Reimbursement of loans* is made in accordance with the annual and half-yearly, quarterly or monthly interest rate staggering, by constant or variable annuities or once, at the final maturity, with or without a grace period. Based on this, the company's financial compartment determines the financial flows generated by the credit decision that can be included in the income and expense budget. The cost of a medium to long-term bank credit to be reimbursed in annuities can be measured by the updated cost. This is why the discount rate allows for the equal amount of the contracted debt and the annuities (repayment rate plus interest) to be updated with respective rates (King, 2016). Annuity can be broken down with or without taking into account the incidence of tax and the reimbursement method.

As stated, *bank loans* can also be reimbursed in other ways, with the cost of financing being determined by them. Regardless of the way of reimbursement, it can be concluded that these are generating costs that can significantly influence the company's treasury (especially if various management, insurance, reimbursement fees, etc.) are perceived, and impose the burden of equity on the guarantees required by the bank (sometimes, the guarantees required by banks can not be provided by soliciting firms, which requires orientation towards other financing methods, which may be more expensive).

*The obligatory loan* is a way of setting up financial resources at the company level for a period of more than one year and is realized through the issuance of bonds or securities that give the holder the right to a fixed annual interest regardless of the results of the company (Dobrota & Chirculescu 2009).

*The borrowed loan* typically has a lower cost than capital underwriting. Also, unlike share issue, the use of bank credit does not affect the profitability of shareholders, their ownership, nor does it change the influence of shareholders on the firm. In the case of a classic debenture loan without various commissions, issue or reimbursement premiums, the actuarial cost (total expenditure incurred for the purpose of producing or constructing a fixed asset intended to replace another totally used fixed asset with the same characteristics taking into account prices from the moment of replacement.) is equal to the nominal interest. However, in order to dimension the cost of the obligatory loan, it is also necessary to identify other categories of expenses, besides interest, including: issuance, advertising, bank fees, emission premiums, reimbursement premiums, etc. These are determined by initially in percentage, to be deducted from the total amount of the loan.

*Bonding involves both advantages and disadvantages* (Dobrota & Chirculescu 2009). Thus, the advantages of using this way include:

- determines the mobilization of important funding resources;
- allows banks and bank expenses to be avoided in obtaining the necessary resources;
- higher reinvested earnings are achieved than share-based financing;
- provides the possibility of early repayment in line with interest rate developments;

- does not change the ownership structure;
- does not entitle the company's claimants to take decisions.

At the same time, bond issues also have disadvantages, as follows:

- involves financial expenses, regardless of the company's results;
- causes the issuer's liquidity to diminish as a result of the repayment of the loan;
- there is a risk that the underwriting operation will not succeed.

*Leasing* is a financing method that can essentially assimilate to the loan, being used by companies that can not obtain loans from banks or do not want to impose their assets on movable or immovable property by installing pledges or mortgages. The user company of the acquired investment objectives is not the owner but the usufructuary tenant in this contract. So, from an accounting point of view, the borrower does not have the property of owner, the good necessarily in his balance sheet asset. However, leases are mandatory in off-balance sheet debt.

*Payments by the borrower* cover both the amortization of the loan and its cost, ie the normal remuneration of the leased asset (interest, commission and risk premium).

The cost of financing increases as the payout period expands and the advance paid by the soliciting firm is lower.

*Leasing financing* involves some advantages:

- the user company can channel its own resources for other purposes, avoiding their immobilization in long-term assets and accessing the new technologies in the field, as at the end of the period established by the lease, it can return the asset to the leasing company and can conclude a new lease for a good with superior technical-functional parameters;

- the good obtained is also a guarantee for the respective operation, the company's own capital remaining legally not engaged;

- the lessee can pay the customs duties at the end of the contract in the case of the imported goods at the residual value;

- tax incentives are recorded (in the case of the financial leasing contract, the goods that are the object of the lease are recorded as fixed assets in the user's account, deducing the expense of its depreciation, and the interest rate on the lease, in the case of the operating lease, shall be recorded as a fixed asset in the accounting of the leasing company and the lease rate shall be totally deductible for the user);

- the procedure for obtaining financing in a leasing system and the performance of such a contract are much easier than in the case of bank lending;
- the leasing company may provide certain services related to installation, commissioning, etc.

This means of financing also leads to disadvantages linked primarily to the high financing cost (which requires obtaining at least a return) and to the fact that it affects future self-financing due to the periodic payment obligations, and failure to pay a rate entails the loss the good and the obligation to pay all outstanding installments (in the current period, many companies are unable to pay their rates on the goods purchased under the leasing system).

Also, unlike bank credit, in the case of leasing, the transfer of ownership is done after the last installment has been settled. However, the latest legislative measures adopted in the tax area also affect this financing option for car purchases. Thus, VAT deduction for the purchase of new cars by legal entities and leasing companies is no longer granted, which will cause many economic agents to reorient themselves to other forms of financing.

The option for one or another mode of financing must also be based on the size of the marginal cost of the capital used. In other words, it is not sufficient to compare the specific cost of each funding source, but also to analyze the cost of each additional capital allocation, so that a comparison can be made between the effects of the funding process in different ways (Economides and Katsamakas, 2008).

The marginal cost has to be compared with the marginal rate of return and the cost of the capital must be determined in relation to the financial return required by the shareholders. Either an economic agent who has not regularly paid equity to shareholders may face difficulties in persuading shareholders or foreign investors to allocate or invest additional capital.

## Conclusions

Improving the business climate is a fundamental requirement for achieving effective market economies, but also for building a democratic system.

It is to be appreciated that, in the last period, the opportunities for financing all the economic and social activity were a basic concern of the economic policy.

Analyzing the financing mechanisms of the companies according to the reality of the national level, we observe that the companies in our country are poorly capitalized, indicating a poor prospect of increasing their profitability and what makes the privatization process in the country quite difficult, is the lack of capital necessary for development and reorganization.

The economic agents in our country have mainly focused on financing by bank leverage and leasing and less on the issuance of shares or bonds. However, due to the emergence of a variety of financing instruments and risk mitigation on the market, there has been a tendency towards a varied financial structure that allows for an optimal ratio between the profitability determined by the resources used and the risk generated by their use.

*The financial structure and option for a particular structure* is an important decision of the funding policy, as the company's financial balance and management independence are conditional on them. The option for the equity / borrowed capital ratio should not be determined solely by the desire to obtain a high return but also by the risk that the manager agrees to assume.

In order to substantiate the financing decision, it is necessary to optimize the interests of the shareholders, the creditors, the state as well as the analysis of the influence exercised by the financial factors and the macroeconomic indicators.

Thus, we can conclude that the decision to opt for leasing or to buy a good by resorting to bank credit must be based on comparing the funding costs of the two alternatives and choosing that funding source at the lowest cost. Recording more difficult conditions in the use of share issues and accessing bank credits has increased the interest of bond investors as they generate secure incomes, unaffected by the economy's trend and the financial situation of the issuing company. It also requires an analysis of the leverage effect, respectively, of the impact of borrowing on financial profitability so that the ultimate result is maximizing the firm's value.

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