MODULE 2 · SESSION 3

Size the Funding Requirement

How to translate a cash forecast and a working-capital gap into a timed, defensible estimate of external funding.

Theory session

Intermediate

Running case: FreshRoute Kitchens

ORIENTATION

Where this session sits

2.2 produced the cases; 2.3 turns the downside into a number and a date

MODULE 1
Build Reliable
Financial Foundations

MODULE 2
Manage Cash
and Uncertainty

MODULE 3
Choose and
Manage Funding

SESSIONS IN THIS MODULE

2.1 Trace Cash Through Operations
Finding the cash trapped between purchase and collection

2.2 Model Forecasts Under Uncertainty
Driver-based base, downside and upside cases

2.3 **Size the Funding Requirement**
Turning a cash forecast into a defensible ask

YOU ARE HERE

SESSION OUTCOMES

What this session explains

Converting a forecast into an ask that survives scrutiny

01 **The requirement has three parts**

The operating deficit, the working-capital gap, and the buffer — each sized separately.

02 **Timing matters as much as amount**

Money that arrives after the breach is not funding; it is a rescue.

03 **Match the instrument to the use**

A permanent need and a seasonal one call for different structures.

04 **Defensibility comes from evidence**

The number is only as good as the operating facts behind the drivers.

DEFINITION

What the funding requirement is

Not the amount you would like — the amount the plan consumes

WORKING DEFINITION

The external funding requirement is the maximum cumulative cash shortfall the plan produces, plus a buffer for being wrong, expressed with the date it first bites and the period over which it is repaid.

1

Maximum, not closing

You must fund the deepest point of the trough, not the balance at the end of the period.

2

Cumulative, not monthly

Monthly deficits add up. It is the running total that determines the facility size.

3

Dated

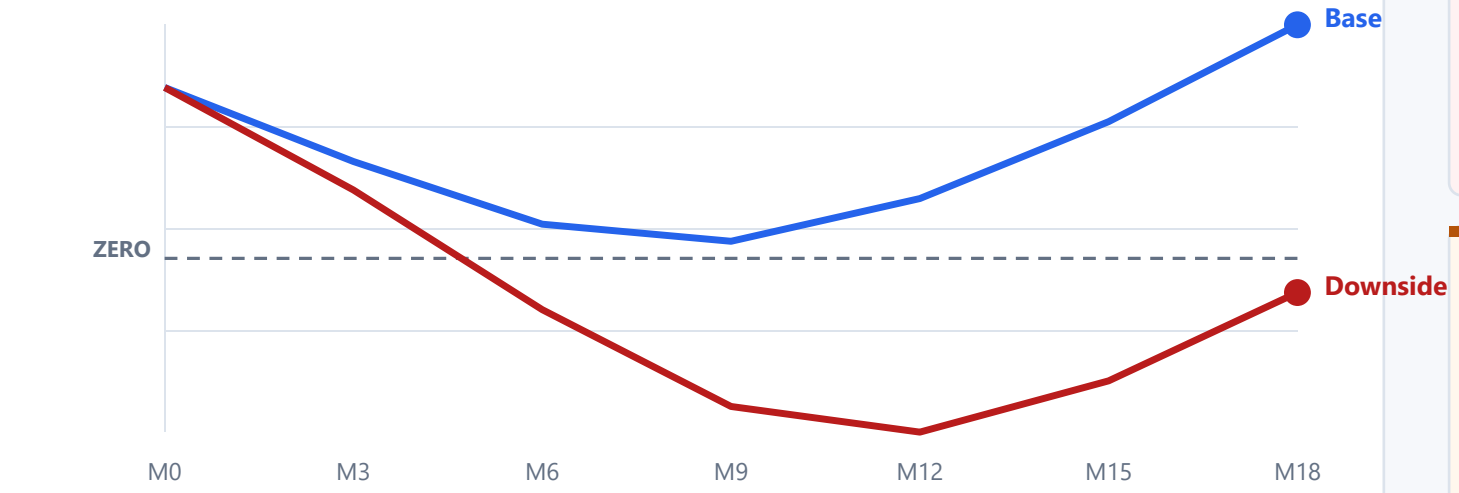
"£1.4m" is not an ask. "£1.4m, first drawn in March, peaking in August" is.

Sizing from the cumulative cash curve is standard commercial-lending practice; see Brealey, Myers & Allen (2020), ch. 30.

CONCEPT 1 · SIZING

Read the requirement off the trough

The deepest point of the downside case, not the base case



The downside trough is £610k at month 12. That figure, plus a buffer, is the facility size.

WHICH CASE TO SIZE ON

The downside

Sizing on the base case means asking again, from weakness, at exactly the wrong moment.

THE BUFFER

Add for being wrong

Typically three to six months of operating outflow, justified by your sensitivity analysis.

THE DATE

When it first bites

Month 6 here. Raising takes three to six months, so the process starts now.

CONCEPT 2 · COMPONENTS

Three uses, three different repayment profiles

The Idaho line funded all three, which is why the timing question mattered

Use	What draws the cash	How it repays
Start-up operating deficit	Costs incurred before the operation reaches planned performance.	Only from future trading profit. This is the riskiest component and the least self-liquidating.
Inventory	Cash committed to material before product is sold.	Self-liquidating — it converts to receivables, then cash, on the Session 2.1 cycle.
Receivables	Cash committed once the sale is made but not yet collected.	Self-liquidating on collection, and it grows with revenue.
Capital expenditure	Plant, equipment and fit-out, paid before any output.	Over the asset's life — which is why it should not sit on a short-term line.

MATCHING USE TO INSTRUMENT

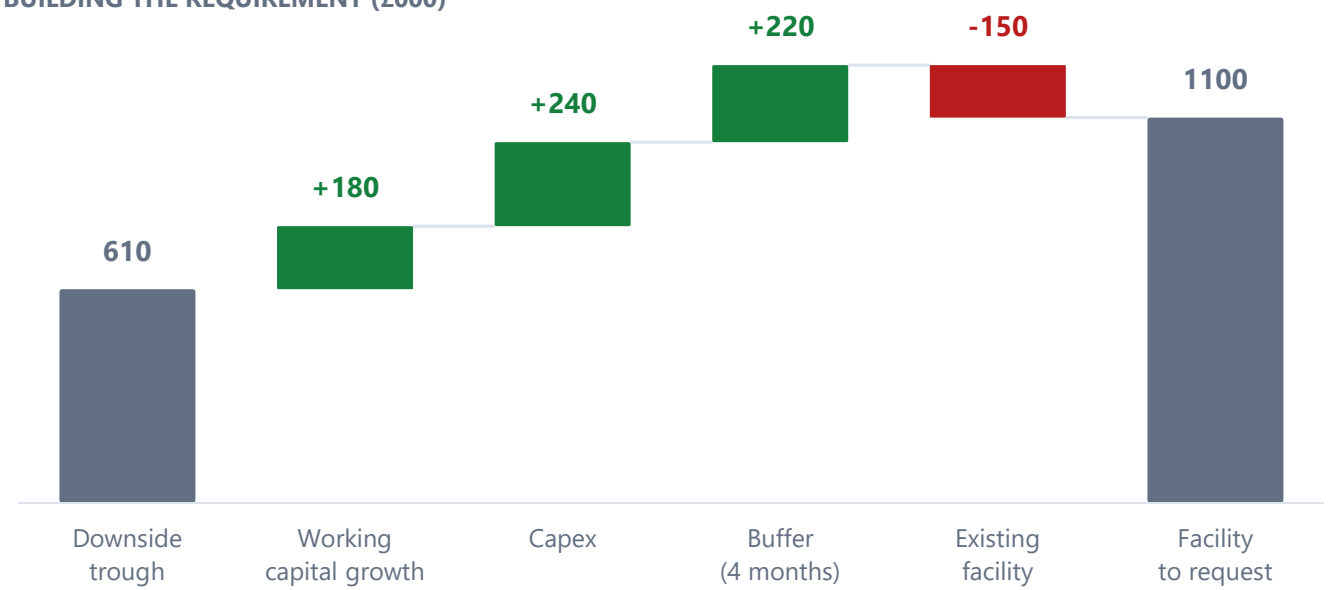
Self-liquidating uses suit a revolving facility. A start-up deficit does not — it needs equity or a term instrument with a repayment holiday.

CONCEPT 3 · THE BUILD

Assembling the number

Four components, each traceable to the forecast

BUILDING THE REQUIREMENT (£000)



Every component traces to a line in the model. None of it is a round number chosen for comfort.

THE DISCIPLINE

No round numbers

"About two million" signals the work was not done. £1.10m with four components signals it was.

NET OF WHAT YOU HAVE

Subtract existing headroom

Undrawn facilities and committed receipts reduce the ask and improve credibility.

JUSTIFY THE BUFFER

From the sensitivity

"Four months, because a 10% adverse move in our two dominant drivers costs £550k."

CONCEPT 4 · CREDIBILITY

What a lender or investor actually tests

The Idaho review is the template

THE MODEL

Is the arithmetic sound?

WHAT IS CHECKED

That the statements tie, the drivers are explicit, and the downside is genuine.

HOW IT IS CHECKED

Reading the model, changing an input, and watching whether it behaves sensibly.

WHAT IT CANNOT ESTABLISH

Whether the drivers themselves are realistic.

THE OPERATION

Is the plan achievable?

WHAT IS CHECKED

How the projections were developed, the business strategy, and the people responsible.

HOW IT IS CHECKED

Site visits — the plant and the dairies — and interviews with management and the guarantor.

WHY IT DECIDES THE OUTCOME

A sound model built on unachievable assumptions is a well-formatted wrong answer.

PREPARING FOR DILIGENCE

Expect the second column. Prepare the operational evidence for your two dominant drivers before you present the number.

CONCEPT 5 · TIMING

When to start raising

The process takes months; the breach does not wait

TOO EARLY

Raising before the plan is evidenced. Terms are poor because the case rests on intention.

THE WINDOW

Six to nine months before the trough. Evidence exists, and you can still decline bad terms.

TOO LATE

Inside three months of the breach. Every term is worse, and diligence delay becomes an existential risk.

WHY THE WINDOW IS THAT WIDE

Stage	Typical elapsed time
Preparing the model, evidence and pack	3–6 weeks.
Approaching and meeting funders	4–8 weeks.
Diligence, credit approval and documentation	6–12 weeks, and longer if site visits are required.

CONCEPT 6 · FAILURE MODES

Three asks that get declined or repriced

Each fails on construction rather than on the business

The round number

Looks like "We're raising two million."

Why it fails It signals the requirement was not built from the plan.

Fix Present the four components and their dates.

Sizing on the base case

Looks like A facility that works if nothing goes wrong.

Why it fails You return for more from a weak position.

Fix Size on the downside trough plus a justified buffer.

Mismatched instrument

Looks like Capex funded on a revolving line.

Why it fails Repayment is demanded before the asset has produced anything.

Fix Match the instrument's term to the use — Session 3.1.

CASE STUDY

An Idaho milk producer

A $200m facility proposal, and a lender who tested the operating reality behind the forecast.

CASE STUDY · AN IDAHO MILK PRODUCER

Testing the model and the operation

Field diligence is what converted a forecast into approved credit

THE REQUEST

An operating line of credit

THE PROPOSAL

A facility producing highly refined powdered milk for large US food producers, with projected annual revenue of $200 million.

WHAT THE LINE WOULD FUND

Start-up operating deficits, inventory and receivables — three uses with different timing.

WHY THAT MATTERS

Each use draws cash at a different point and repays on a different schedule.

THE TEST

Model and operating reality

BEYOND THE PROJECTIONS

Cordes & Company reviewed how the projections were developed and considered the business strategy.

FIELD DILIGENCE

Visits to the plant and the dairies; interviews with management and the guarantor.

THE OUTCOME

The viability report enabled the lender to approve credit, and the facility was built.

READING THE CASE

A financing need is strongest when the lender can test both the model and the operation behind it. An attractive end-state forecast is not a funding case.

Drawn from the session case pack.

APPLICATION

Bringing the theory to FreshRoute Kitchens

From the Session 2.2 downside to a defensible ask

Step	What you produce	FreshRoute example
Find the trough	Deepest cumulative shortfall in the downside case.	£610k at month 12; first negative at month 6.
Add committed uses	Working-capital growth and capex already decided.	£180k cycle growth; £240k second production line.
Size the buffer	Justified by sensitivity, not by habit.	£220k — four months of operating outflow, covering a 10% adverse move in covers and food cost.
Net off headroom	Undrawn facilities and committed receipts.	£150k undrawn overdraft already in place.
State the ask	Amount, first draw, peak, repayment.	£1.10m: first draw month 5, peak month 12, repaid from month 15.
Prepare the evidence	Operational support for the dominant drivers.	Twelve months of covers data and signed supplier pricing for food cost.

WHAT COMES NEXT

Module 3 chooses the instrument and negotiates the terms on which this is raised.

SUMMARY

What to carry out of this session

1. **Size on the downside trough, not the closing balance.**
   The deepest cumulative point is what the facility has to cover.

2. **A funding requirement carries a date.**
   Amount, first draw, peak and repayment — an amount alone is not an ask.

3. **Match the instrument to the use.**
   Self-liquidating working capital suits a revolver; a start-up deficit does not.

4. **Justify the buffer from your sensitivity analysis.**
   It converts a round number into a defended one.

5. **Expect diligence on the operation, not just the model.**
   The Idaho lender visited the plant and the dairies before approving.

FURTHER READING

Sources for this session

Primary references behind each concept

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