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White Paper

UNDERSTANDING THE TRUE COST OF CAPITAL: WHY APR ISN'T THE WHOLE STORY

LOOKING BEYOND APR

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EXECUTIVE SUMMARY

AOL Sourcing

AOL Sourcing turns North American retail and consumer product companies' toughest supply chain and cash flow challenges into competitive advantages through strategic global sourcing and innovative financial solutions. With 30 years of China sourcing expertise and diversified global networks, we deliver supply chain excellence while preserving working capital—offering integrated manufacturing, logistics, and import solutions with FTZ and bonded warehouse access for unmatched efficiency and flexibility.

Strategic Dual-Source Manufacturing

AOL Sourcing's integrated global manufacturing partners and Made in USA facilities transforms market volatility into competitive advantage, delivering strategic flexibility to optimize costs, mitigate risks, and capture opportunities across any trade environment. AOL has exclusive cooperation agreements with the leading global factory groups offering "best of breed" payment terms, improved pricing and tariff relief for manufacturing and sourcing hard and softlines in over eight countries.

More than sourcing—we're financial strategists with deep manufacturing expertise.

We revolutionize how businesses approach global manufacturing—transforming supply chain complexities and financial constraints into strategic competitive advantages through three decades of manufacturing intelligence, innovative off-balance sheet capital solutions, and an integrated global network that preserves your working capital while delivering supply chain excellence across any trade environment.

- **90-Day Payment Terms** – Improve cash flow with extended terms.
- **No Deposit Required** – Preserve capital with deposit-free production.
- **Tariff Expertise** – Avoid margin loss through strategic trade navigation.
- **Diversified Manufacturing** – Reduce risk with non-China supply options.
- **End-to-End Sourcing** – Full support from design to delivery.
- **Financial Tools** – L/Cs and payment guarantees to ease manufacturer requirements.
- **Direct Import Oversight** – On-ground teams ensure quality and real-time management.
- **Exclusive Deals** – Access closeouts and overruns not available elsewhere.



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UNDERSTANDING THE TRUE COST OF CAPITAL

Why APR Isn't the Whole Story

As a borrower, it's tempting to focus solely on the Annual Percentage Rate (APR) when evaluating financing options. A lower APR appears to promise lower interest costs, making it an intuitive metric. However, APR is a narrow and often misleading measure that doesn't fully reflect the real cost of capital for your business. This document explores why relying only on APR can lead to suboptimal decisions and introduces a broader perspective—the true cost of capital—to help you assess financing options in alignment with your business's growth goals. It also integrates insights on Revenue-Based Financing (RBF) and factor rates, highlighting why comparing these to APR is flawed and how to strategically deploy alternative financing for maximum value. Additionally, an interactive calculator is embedded to help you compare the true cost of capital between financing options.

The APR Trap: What It Misses

APR was designed for consumer loans, assuming a full year of borrowing under consistent conditions. For business financing—especially short-term loans, revenue-based financing (RBF), or invoice factoring—this assumption doesn't hold. Here's why APR falls short:

- **Misleads on Short-Term Costs:** APR annualizes interest, exaggerating the cost of loans repaid quickly. For example, a \$10,000 six-month loan at 23% APR costs \$646 in interest and fees, while a two-year loan at 10% APR costs \$1,029. The shorter term saves money despite the higher APR.
- **Ignores Opportunity Cost:** Waiting for a low-APR loan can mean missing revenue opportunities. A \$500,000 project earning \$20,000 monthly profit delayed by a 90-day bank loan at 7% APR loses \$60,000, while a faster loan at 30% APR funded in 5 days captures that value.
- **Overlooks Flexibility and Risk:** Low-APR loans often demand collateral or fixed payments, increasing risk. Alternative options like RBF offer flexibility that APR doesn't account for.

The Small Business Finance Association notes APR is "more a marketing tool than a useful way to evaluate short-term loans."

Partner Spotlight

- **Glencoe Advisors:** Helps businesses understand the limitations of APR and evaluate alternative financing options with holistic financial and transaction advisory.
- **Gateway Trade Funding:** Specializes in flexible financing options, including RBF, helping clients access capital that aligns with their revenue cycles.

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Revenue-Based Financing (RBF) and Factor Rates: A Different Approach

Revenue-Based Financing (RBF) is an alternative financing method where repayments are a percentage of your business's revenue. Unlike traditional loans measured by APR, RBF uses a factor rate—a fixed multiplier of the borrowed amount. For example, a factor rate of 1.35 means you repay \$1.35 for every \$1 borrowed, totaling \$135,000 on a \$100,000 advance.

Why Comparing RBF to APR is Flawed

- **Different Calculation Bases:** APR is an annualized interest rate, while factor rates are static multipliers. This fundamental difference makes direct comparisons invalid—like comparing apples to oranges.
- **Time Horizon:** APR assumes a year-long term, but RBF repayments often conclude faster, tied to revenue. Annualizing a factor rate inflates its perceived cost unfairly.
- **Repayment Structure:** RBF payments flex with revenue, aligning with cash flow and reducing strain during slow periods. APR-based loans have fixed payments, ignoring this adaptability.

For example, a \$100,000 RBF with a 1.35 factor rate costs \$35,000 total. If repaid in six months due to strong revenue, its effective cost may outshine a traditional loan with a lower APR but rigid terms over a longer period.



Partner Spotlight

- **D.B. Group:** Provides global logistics and customs solutions that optimize cash flow, reducing the need for expensive short-term financing. Minimizes operational risk through advanced logistics and compliance solutions.
- **Fallingst Technologies™ LLC:** Connects IP-rich and innovation-driven companies with strategic capital, helping them leverage RBF and other alternatives for growth.

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The True Cost of Capital: A Smarter Lens

The true cost of capital goes beyond APR, factoring in:

- **Speed-to-Capital:** Fast funding captures opportunities. A \$200,000 inventory order with a 5% discount (\$10,000 savings) funded in days with a \$6,000 fee nets \$4,000, versus losing it waiting 60 days for a bank loan.
- **Opportunity Cost:** Delays cost revenue. A \$500,000 RBF funded in 5 days secures a \$150,000 profit order, while a 90-day wait for a low-APR loan loses it all.
- **Flexibility:** RBF's revenue-tied payments ease cash flow strain, unlike fixed APR loan schedules.
- **Working Capital Cycle:** Match financing to your cash cycle. A 30-day cycle retailer uses \$100,000 RBF (1.35 factor rate, \$135,000 total cost) to sell inventory for \$180,000 in 15 days, netting \$45,000.
- **Time Value of Money:** Money now is worth more. A \$500,000 RBF repaid in 15 months totals \$675,000, often cheaper in present value than a 10-year SBA loan at 7% APR totaling \$809,135.

Strategic Deployment of Alternative Financing: High-Return Opportunities Only

Alternative financing, like RBF with a 1.35 factor rate, is “rocket fuel” for growth—but only when deployed for high-velocity, high-return opportunities. The cost (e.g., \$1.35 per \$1 borrowed) is justified only if returns significantly exceed it.

The Golden Rule

Use alternative financing for asset creation—inventory expansion, equipment purchases, or proven marketing—not debt restructuring or low-return activities. Misuse leads to value destruction.

Partner Spotlight

- **Los Angeles Apparel:** Demonstrates how flexible financing can support ethical, domestic manufacturing and rapid inventory turns.
- **Rolla Coster:** Uses flexible, rapid-turn manufacturing models that benefit from RBF's adaptable repayment structures.
- **Exit 21 Apparel Solutions:** Guides emerging brands in choosing the best-fit financing structures for launching and scaling product lines.

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When It Makes Sense

- **High-Margin Inventory:** A retailer invests \$500,000 (total cost \$675,000 with 1.35 factor rate) in inventory sold for \$900,000, netting \$225,000 (33% ROI).
- **Large Purchase Orders:** A manufacturer funds \$600,000 in materials (total cost \$810,000) for a \$1.2M order, yielding \$390,000 profit (48% ROI on financed amount).
- **Equipment with Impact:** A \$150,000 equipment purchase (total cost \$202,500) generates \$25,000 monthly revenue, justifying the cost with 48%+ annual ROI.

The Math

- **Break-Even:** Revenue must hit 1.35x the financed amount (\$675,000 on \$500,000).
- **Target:** 2.5x–3x (\$1.25M–\$1.5M) for strong returns.
- **ROI:** Minimum 50%+ on total investment (e.g., \$337,500+ profit on \$675,000).

Danger of Misuse

Using RBF for debt restructuring fails because it generates no new revenue to offset the 1.35 factor rate. A \$75,000 advance (repayment \$101,250) adds \$8,437 monthly burden without income, accelerating collapse.

Partner Spotlight

RSR (Retail Systems Research): Offers benchmarking and analytics to help retailers quantify the real impact of funding speed and flexibility.

Retail Marketing Society: Provides educational resources and thought leadership to help businesses understand the nuances between APR and factor rates. Fosters innovative thinking and industry dialogue to help businesses rethink their approach to capital and growth.

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Practical Framework for Borrowers

Evaluate financing with this checklist:

- **Opportunity Cost:** What's lost waiting? (e.g., \$20,000/month x 3 = \$60,000)
- **Speed:** How fast do you need funds?
- **Flexibility:** Do terms match cash flow?
- **Cycle:** Does it fit your working capital needs?
- **Total Impact:** Compare repayment and growth potential.
- **ROI:** Returns must exceed 50%+ for RBF's 1.35 factor rate.

Interactive True Cost of Capital Calculator

Use the calculator below to compare two financing options (e.g., a fast RBF loan vs. a slower traditional loan) by factoring in speed, opportunity cost, and total repayment. Input your loan details to see the true cost of capital in action.

Compare True Cost of Capital

Loan 1

Fast Funding, e.g., RBF

Loan Amount (\$): 100000

Factor Rate (e.g., 1.35 for RBF): 1.35

Days to Funding: 5

Loan 2

Slow Funding, e.g., Traditional Loan

Loan Amount (\$): 100000

APR (%): 7

Term (Months): 120

Days to Funding: 90

Business Impact

Monthly Profit Opportunity (\$): 20000

Calculate True Cost

Results

Loan 1

Fast Funding, e.g., RBF

Total Repayment: \$135000.00

Financing Cost: \$35000.00

Opportunity Cost: \$0 (Funds available in 5 days)

True Cost of Capital: \$35000.00

Loan 2

Slow Funding, e.g., Traditional Loan

Total Repayment: \$139330.18

Financing Cost: \$39330.18

Opportunity Cost: \$56666.67 (Due to 85 days delay)

True Cost of Capital: \$95996.84

Analysis

Despite Loan 1 having a higher factor rate, its true cost is lower when accounting for the opportunity cost of waiting for Loan 2. Speed and flexibility can outweigh nominal rates.

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Real-World Example

ABC Electronics needed \$500,000 for a \$150,000-profit order. A 90-day SBA loan at 10% APR lost the deal. An RBF at 1.35 factor rate funded in 5 days secured \$75,000 net profit after \$675,000 repayment, proving speed trumps APR.

- **Beyond APR:** Additional Concepts to Consider
- **Risk Exposure:** Low-APR loans often require collateral, increasing downside risk. Unsecured options like RBF protect your assets.
- **Cash Flow Alignment:** RBF's revenue-tied payments match your cash flow patterns, preventing crunches.
- **Return on Investment (ROI):** A loan's value lies in what it enables. A higher-factor-rate loan funding a 50% ROI project beats a low-APR loan missing it.

Your Next Step: Rethink "Cost"

APR is one metric, not the whole picture. For RBF and alternative financing, factor rates reflect total cost, not annualized rates, making APR comparisons flawed. Focus on speed, flexibility, and ROI—use the calculator above to see the true cost in action, and consult a financial advisor to align financing with your highest-return opportunities. The true cost of capital isn't just interest; it's about maximizing your business's potential.

Key Takeaway: "The cheapest loan isn't always best. Slow funding loses opportunities; fast capital with high returns, even at a 1.35 factor rate, drives growth."



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Our Partner Directory

Barrett Distribution Centers: Ensures that capital-smart sourcing is matched by rapid, scalable logistics—so funding decisions translate into operational agility. Ensures that fast capital translates into operational agility and fulfillment success.

D.B. Group: Provides global logistics and customs solutions that optimize cash flow, reducing the need for expensive short-term financing. Minimizes operational risk through advanced logistics and compliance solutions.

Exit 21 Apparel Solutions: Guides emerging brands in choosing the best-fit financing structures for launching and scaling product lines. Offers financial modeling for apparel brands to ensure capital deployment meets break-even and ROI targets.

Fallingst Technologies™ LLC: Connects IP-rich and innovation-driven companies with strategic capital, helping them leverage RBF and other alternatives for growth. Advises on restructuring and warns against misusing high-cost capital for non-growth activities.

Gateway Trade Funding: Specializes in flexible financing options, including RBF, helping clients access capital that aligns with their revenue cycles. Supplies the data and expertise needed to power these comparison tools.

Get Hyped: Helps brands maximize the ROI of growth capital through influencer marketing and high-impact digital campaigns.

Los Angeles Apparel: Demonstrates how flexible financing can support ethical, domestic manufacturing and rapid inventory turns.

Retail Marketing Society: Provides educational resources and thought leadership to help businesses understand the nuances between APR and factor rates. Fosters innovative thinking and industry dialogue to help businesses rethink their approach to capital and growth.

Rolla Coster: Uses flexible, rapid-turn manufacturing models that benefit from RBF's adaptable repayment structures. Supports brands in deploying capital for rapid product launches and market testing, maximizing returns.

RSR (Retail Systems Research): Offers benchmarking and analytics to help retailers quantify the real impact of funding speed and flexibility.

Write Way Digital: Supports businesses in communicating their financial strategies and decisions to stakeholders through effective digital marketing, website content, and brand messaging.

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