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Business Mentoring

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How To Get A Small Business Bank Loan

Capacity, capital, collateral, credit, and character are the "Five Cs" that loan offers learn in Lending 101. But to most small-business loan applicants in need of money, it is an esoteric exercise that makes them garner reams of paperwork without a clear path to funding.

Financing a business "is based on a simple principle," Charles Green says.

He founded a community bank in Atlanta, Georgia, received a financial services award from the U.S. Small Business Administration for making lots of small business loans and recently published his third edition of *The SBA Loan Book*.

The simple principle, he says, is "lenders always require the borrower to agree that the loan will be repaid." If it were that simple, of course, all applicants would walk out of banks with wads of cash.

Bankers want a comprehensive business plan supporting "your

ability to repay the loan," Green says. "The lender will expect you to provide realistic projections about how the proceeds of the loan will be invested to generate revenues for your business."

Furthermore, the revenues generated, less the business operating expenses, must be sufficient to make the loan payments. Additionally, lenders require a cash-flow cushion should revenues decline or operating expenses increase. The projections and an extensive narrative about how you arrived at your numbers is the crux of your business plan. Yet many loan applicants are stumped when it comes to projecting income and operating expenses.

To help, most SCORE chapters are offering a course called, "Financial Projections." It is part of their QuickSTART workshop series and explains how to project believable numbers.

Believable means that your

projections and financial ratios must pass muster with the bank's underwriters. Moreover, the underwriters have to accept your narrative describing how you arrived at the projections.

"The integrity and reasonableness of these projections are often the most important factors in granting loans approval," Green says. Paradoxically, "The lender is not an expert in your field and may not recognize exaggerated revenue projections or inadequate expense estimates."

Even more perplexing for underwriters, small businesses within the same industry can be very different. That is why projecting your numbers and getting the lender to buy into them is as much an art as it is a science.

The science is learning the lender's acceptable range for key financial ratios in your industry. The art is doing impeccable market research and citing it as the rationale for getting your projections to fit. In

other words, you have to know the benchmarks that your lender uses. Then, extensive research and the resulting narrative will support your projections.

Many lenders use the Risk Management Association's "RMA Annual Statement Studies Users Guide" to glean average financial ratios by industry. Thus they will match your projections against others in similar businesses. Any variances from RMA need to be explained. Furthermore, your proficiency in explaining the variances can mean the difference between approval and rejection.

The trade associations in your industry will likely have average and mean financial ratios in your industry. They may also segment businesses within the industry more definitively than RMA. You can find a list of trade associations in the Encyclopedia of Associations. Many libraries have it in their reference section or you can purchase a copy online.

Green, the former banker, says, "The company may not compare well with RMA results because of extraordinary local reasons." So get data from local chambers of commerce, business owners and franchise operators merchandising similar products and services. Interpret the data to explain how your company differs from RMA's averages.

I will write about the other Cs of lending in future columns.

Jerry Chautin is a business columnist and SBA's 2006 national "Journalist of the Year" award winner. He is a former entrepreneur, commercial mortgage banker, commercial real estate dealmaker and business lender.

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