

## Business Financial Management

### Session 2

Budgets, Loan Programs and how the Banker looks at things

Audio: 1-866-740-1260

Access #: 3087602

## Other likely requests by lenders or loan boards

- Estimated market value of assets
- Personal Financial Statement
- Business Plan
- Schedules
- Contracts

## Session Content

- The process of budgeting
- Selecting from potential loan programs
- The viewpoint of your lender

## SBDC process in building financials

- Start with existing balance sheet
- Adjust existing balance sheet per the project
  - Add assets being purchased
  - Remove debts/liabilities being refinanced
  - Adjust capital structure with new loans or owner's injection
- Review historical revenues and expenses
- Budget anticipated revenues
- Budget anticipated expenses
  - Adjust for areas impacted by the project
- Adjust Cash Flow due to A/R and A/P
- Review Cash Flow and Ratios for likelihood of financing

## The Process of Budgeting

- Information that is needed for an existing business
  - Last 2 to 3 years tax returns
  - Year to date Profit & Loss
    - Comparative to prior year, same period is best
  - Interest Rate and Monthly Payment on each existing loan
  - Schedule of A/R and A/P
  - Proposed Uses of Funds and Sources of Funds

## Obtaining Financing

- Select the loan program that is most advantageous to the business
  - Impact on cash flow?
  - Lowest cost of interest?
  - Provides safest return for the lender?
- Flexibility in Structure
- Tie life of the loan to life of the asset

## Financing Sources

- Federal
  - SBA
  - USDA
- State
  - REDI
  - APEX
  - Microloan
- Regional
- Conventional
  - Equity
    - Self
    - Angels
    - Venture Capital
  - Grants

## USDA Business & Industry Program

| Use of Funds     | Buildings, Land, Equipment, Improvements, Renovations, Supplies, Inventory and Working Capital                       |
|------------------|--|
| Project Size     | N/A  |
| Loan Size        | Up to \$10MM. Up to \$25MM with special approval   |
| Downpayment      | Flexible, but based on lender. 10% tangible equity on B/S for existing business; 20% for startup                     |
| Interest Rate    | Negotiated with lender   |
| Interest Type    | Negotiated with lender; Variable not more often than Quarterly   |
| Repayment Length | Life of asset. 30 years max bldg; 15 yrs Equip; 7 yrs WC   |
| Advantages       | Similar to SBA 7(a) but higher dollar limits. Not as readily used by lenders in South Dakota. Must be under 50k pop. |

## SBA 7(a) Loan Guaranty Program

| Use of Funds     | Any legal, business related needs including real estate, equipment, inventory, working capital  |
|------------------|---|
| Project Size     | Unlimited   |
| Loan Size        | Loan of up to \$2.0MM   |
| Downpayment      | Typically 10% to 30% for startups. Existing businesses negotiable   |
| Interest Rate    | Based on \$ amount, length of payment and underlying base rate (typical WSJ Prime). Currently around  |
| Interest Type    | Fixed or Variable as negotiated between borrower and lender.  |
| Repayment Length | Life of asset. Generally 15 to 20 years for real estate, 5 to 10 years for equipment and 3 to 7 years for short term assets                                       |
| Advantages       | Very flexible. Banker receives up to 85% insurance on loan, which may increase time given to repay. Sometimes can be set up to function more as a line of credit. |

## State Loan: REDI Loan

| Use of Funds     | Buildings, Land, Improvements, Equipment  |
|------------------|---|
| Project Size     | Varies. Business should be creating "primary" jobs                              |
| Loan Size        | Up to 45% of eligible project costs   |
| Downpayment      | Minimum of 10%. Possibly higher based on project risk and lender's requirements |
| Interest Rate    | 3.00%   |
| Interest Type    | Fixed   |
| Repayment Length | Amortized 20 years on Buildings and 10 years on Equipment. 5 year balloon.      |
| Advantages       | Long term, low interest money.  |

## SBA 504 Program

| Use of Funds     | Long Term Fixed Assets such as Buildings, Land, Real Estate improvements, equipment and small amounts of refinancing if part of a larger expansion                |
|------------------|---|
| Project Size     | As determined by business type and downpayment  |
| Loan Size        | 30% to 40% of the Eligible Project Costs, as determined based on the required downpayment. Max of \$1.5MM unless meets public policy goal...\$2MM to \$4MM if mfg |
| Downpayment      | All projects start at 10%. Add 5% if business newer than 2 years. Add 5% if specialty facility (hotel, bowling alley, etc)  |
| Interest Rate    | Tied to Treasury Rates. Changes monthly for the 20 year and every other month on the 10 year. Currently 5.21% on 20 year bonds and 4.17% on 10 year bonds.        |
| Interest Type    | Fixed for the life of the loan.   |
| Repayment Length | 10 years if equipment only. 20 years if a building is involved  |
| Advantages       | Long Term, Fixed Interest. Bank finances 50% but has 1 <sup>st</sup> mortgage. Minimal downpayment.   |

## State Loan: APEX Loan

| Use of Funds     | Buildings, Land, Improvements, Equipment  |
|------------------|---|
| Project Size     | Varies. Targets Ag processing, Export (outside SD) and rural businesses (less than 25,000 population) |
| Loan Size        | 75% of project size, not to exceed \$187,500  |
| Downpayment      | Minimum of 10%. Possibly higher based on project risk and lender's requirements                       |
| Interest Rate    | 5.00% to 7.00%, though most often 5.00%   |
| Interest Type    | Fixed   |
| Repayment Length | Useful life of the asset  |
| Advantages       | Low interest funds. High percentage of project. Less emphasis on job creation                         |

### State Loan: MicroLoan

| Use of Funds     | Buildings, Land, Improvements, Equipment, Inventory and Working Capital                 |
|------------------|---|
| Project Size     | \$200,000 or less that diversifies local economy  |
| Loan Size        | Up to 50% of project size, not to exceed \$50,000                                       |
| Downpayment      | Varies. Generally 10% or more if required by bank. Smaller projects may be as low as 0% |
| Interest Rate    | 3.00%   |
| Interest Type    | Fixed   |
| Repayment Length | Up to the useful life of the asset. 5 year balloon.                                     |
| Advantages       | More flexible use of funds than other SD programs. Low interest rate.                   |

### Capital Trends in South Dakota

|          | SBA Loan \$ | Growth |  | SBDC Clients | Growth |
|----------|-------------|--------|--|--------------|--------|
| 2010 YTD | \$58.1MM    | 30.8%  |  | \$45.4MM     | 18.9%  |
| 2009     | \$71.4MM    | 6.6%   |  | \$95.5MM     | 12.4%  |
| 2008     | \$67.0MM    | 27.9%  |  | \$85.0MM     | -16.3% |
| 2007     | \$52.4MM    |        |  | \$101.6MM    | 27.7%  |
| 2006     |             |        |  | \$79.6MM     | 25.0%  |
| 2005     |             |        |  | \$63.7MM     | 17.0%  |
| 2004     |             |        |  | \$54.4MM     | 15.0%  |

SBA annual data is Federal Fiscal Year (Oct - Sep)  
 SBDC annual data is Calendar Year

### Regional Loan Programs

- Planning Districts/Regional
  - ABC (Yankton/PD III)
  - SEDF/SECOG (Sioux Falls Region)
  - NESDEC and NECOG (Aberdeen Region)
  - FDDC (Watertown Region)
  - West River Foundation (Rapid City Region)
- REED (Rural Electric Econ. Development) / East River
- County
- Towns

### Lender's Perspective

Keith Robbennolt  
 Business Banker  
 Home Federal Bank  
 Sioux Falls, SD

### Other Sources

- Commercial Loan
  - Less Structured, but perhaps faster repayment. Less paperwork and loan fees.
- Equity Capital
  - Self and 3F's
  - Angel Investors
    - Earlier Stage than VC Funds. Usually \$50K to a couple hundred thousand. Usually no monthly repayments.
  - Venture Capital
    - Later stage. Still high risk (and therefore high return). Usually looking for 30% to 50% annual Rate of Return. Usually no monthly repayments.
- Grants
  - Very rare. Most often a scam. Legitimate sources is [www.grants.gov](http://www.grants.gov)

### Topics To Be Covered

- The Business Plan
  
- The Borrower
  
- How SBA Programs Work in Today's Economic Climate

## The Business Plan

- Be Thorough and Succinct
- Components of the Business Plan
  - Industry Analysis
    - Current industry trends
    - Key industry risks and your plan to mitigate these risks
      - Show you know what your risks are, and....
      - Show that you have thought through an action plan to ensure the effect on your business is minimal should an identifies risk comes to fruition.
    - You may not know what all your risks are, use all of your resources (i.e. SBA, SBDC, SCORE, Lender)

## The Business Plan (Continued)

**Remember.....You  
Are The Expert!**

## The Business Plan (Continued)

- Competition
  - Who are they, and.....
  - How do/will you set yourself apart?
- Management
  - Who will be the key decision makers of your firm?
  - What is the depth and breath of these individuals?
  - What experience do these individuals have to show that they are qualified to run your business?
  - Include a Resume for all key decision makers
- Marketing Strategy
  - How do plan to create awareness?
  - What are your expectations of your marketing strategy?
  - How will you quantify, or measure the success of your marketing plan?
  - How will you set yourself apart from your competition?

## The Borrower

- The borrower itself can also determine the loan program.
  - A borrower with somewhat limited liquidity, could benefit from an **SBA 504** loan, if looking at purchasing or construction of a new facility.
    - Borrower can take advantage of the lower equity injection requirement, that would be consistent with conventional financing.
    - Borrower benefits from considerably lower interest rates on the debenture portion of the SBA 504 loan.

## The Business Plan (Continued)

- Budget/Projections
  - Sources and Uses
    - Lenders use this to help determine:
      - Loan Amount
      - Loan Structure
      - Loan Program (i.e. conventional financing, SBA (7(a), Rural Lenders, 504, Micro Loan), or other programs)
    - Get many of the costs associated with the project in order prior to meeting with SBDC to prepare projections.
  - Financial Projections
    - Do not be too conservative (lenders use this information to make credit decisions)
    - Be realistic
    - Use your resources (i.e. SBDC, SCORE, RMA, etc.), as they will help you identify ratio values specific to your industry, and how they correlate to the local markets you may operate in.

## The Borrower (Continued)

- A borrower with limited collateral available to secure a business loan, could benefit from an **SBA 7(a)**, or **Rural Lender's Advantage** program.
  - Often times lenders will look to one of these SBA programs to mitigate potential collateral shortfalls.
  - These programs work great for projects where intangibles or working capital is being financed, since these items carry no intrinsic value to secure debt.
  - SBA Will, however, look to shore up collateral deficiencies with personal assets if equity is available.

## The Borrower (Continued)

- A borrower with plans on expansion or relocation could be a good candidate for a State funded loan program like the **REDI (Revolving Economic Development and Initiative) Fund**.
  - Typically best suited for land purchases, new commercial real estate construction, and equipment purchases.
  - These programs will usually carry a job creation requirement to be eligible.
  - Start-up firms are eligible!
  - Borrower can take advantage of a 3% interest rate, and favorable repayment options.

## How These Programs Work in Today's Economic Climate

- Use of stimulus funds to offset fees, has made SBA programs very attractive to financial institutions, but funding may no longer be available.
- These programs are intended to mitigate risks to the banks, and to keep financial institutions lending.
- Some programs allow borrowers to keep cash in their business by requiring less equity injection into projects.

## Sessions

- Thursday, July 15<sup>th</sup>: Session 1 10am
  - Difference between P&L and Cash Flow / Revenue and Expense trends
- Thursday, July 22<sup>nd</sup>: Session 2 10am
  - Building a Budget / Loan Programs / Banker's View
- Thursday, July 29<sup>th</sup>: Session 3 10am
  - Business Financial Ratios / Calculating Break Even Points
- These series and prior series are digitally archived at [www.sba.gov/sd](http://www.sba.gov/sd)
  - Survive & Thrive Series
  - Marketing Matters Series