

# How to Get a Small Business Loan

Bankers state a major reason they turn down loans is business owners do not put forth complete or attractive "loan packages." Putting together a loan application can seem overwhelming, but it is your opportunity to impress the loan officer by proving the value of your business.

If this is your first time seeking a loan for your business, one of Santa Fe's many assistance programs can help you understand what will be expected of you and get your paperwork ready to apply for a loan. Local resources include SCORE, SBDC, WESST, ACCION, and the city's two Chambers of Commerce. They can provide training, advice on where to go for a loan, and an independent opinion on whether your business is ready for a bank loan.

Make sure you follow the 5 C's of Credit to put together a complete loan package.

## The 5 C's of Credit

**CAPACITY** to repay is the most important thing a bank considers when looking at a loan application. A bank will not lend to a business if they are worried the business will not be able to repay the loan.

- **Personal Credit Score:** Your personal credit score will be used to evaluate how well you manage the finances of your business. Find out your credit score and take steps to repair it if necessary. A good credit score (over 700) will help you secure a loan and better interest rates.
- **Financial Statements:** The financial health of your business is evaluated using financial statements. This means you must prepare a balance sheet, statement of cash flows, and income statement so your banker can better understand your business and your ability to repay.

**CAPITAL** is how much you have personally invested in your business. This is important to the bank because investing your own money makes you more motivated to make sure your business succeeds.

- **Written and Verbal Information Sharing:** Your financial statements should include the amount of your personal investment, but you should also mention this information in conversations with your banker as proof of your dedication to the business's success.

**COLLATERAL** or guarantees are sometimes necessary to secure a loan.

Collateral is anything you or the business owns that could be sold if the business isn't able to repay the loan. Common examples include equipment, buildings, inventory, and accounts receivable. A guarantee is a promise from another person or government agency to repay the loan if you default (cannot repay the loan).

- **Independent Appraisal:** If necessary, have an independent appraiser provide an estimate of the value of your collateral.
- **U.S. Small Business Association Guarantees:** The U.S. SBA has increased its loan guarantees in the face of the current economic crisis.

**CONDITIONS** are the reasons you are asking for a loan. Are you planning to open a new store, invest in some new equipment, or run a marketing campaign to generate more business?

- **Written Explanation of Conditions:** If you are a new business, your reasons for requesting a loan should be included in your business plan. If you are an existing business, you need to prepare documentation stating how you will use the money (what you will buy, how much it will cost, who you will buy it from, etc) and how the money will increase your profitability.

**CHARACTER** is the most subjective factor impacting your loan application. The lender is trying to evaluate how trustworthy you and your business are. You can turn this factor in your favor by highlighting your team's education, experience in your area of business, and any relationships that will contribute to the success of your business (industry connections, respected board members who advise you, etc.)

- **Biographical Summaries:** Prepare brief biographical summaries on the major decision-makers in your company, highlighting education, experience, and relationships. Providing this information is a good way to open communication with your Banker about his or her expectations.

## After the 5 C's

Once you have a good handle on what kind of information you will have to provide, head to Santa Fe Economic Development Financing for options on where to apply for a loan.

**Non-Bank Financing** exists if a conventional banking loan isn't for you:

1. **Local Microlenders:** Santa Fe and New Mexico are home to a number of "alternative" microlenders, including ACCION, WESST, and the NM Loan Fund. These lenders make small business loans, often to businesses that are not yet "bankable" by commercial banks.
2. **Small Business Association:** The U.S. SBA offers loan guarantees to small businesses. SBA is also offering a special ARC Loan, through participant lenders, with up to \$35,000 in short-term relief for eligible businesses facing immediate financial hardship in the economic downturn.
3. **Credit Cards:** Many small business owners use their personal credit cards to finance their growth. While convenient, carrying a balance on your credit card(s) is expensive and can sink a business (and destroy your personal credit) quickly if you aren't careful.
4. **Vendors and Clients:** Business owners can negotiate with vendors to pay them later and with customers to be paid sooner. For example, "2/10 net 30" means the customer must pay within 30 days of the seller sending the goods/service, but the customer receives a 2% discount if they pay within 10 days. Typically there is an interest penalty that starts to accrue for customers who pay after 30 days.
5. **Invoice factoring/discounting:** Your business might be able to sell some of its accounts receivable (invoices) to an invoice factoring company at a discount, in exchange for immediate payment of those accounts receivable. Factoring can act like short-term borrowing by benefitting a small business' working capital and cash flow position.
6. **Peer-to-Peer lending:** Consider seeking a peer-to-peer or social loan. It is a relatively new type of lending that uses the internet to cut the bank out of the lender/borrower relationship. Sites include [www.prosper.com](http://www.prosper.com), [www.kiva.org](http://www.kiva.org), and [www.lendingclub.com](http://www.lendingclub.com).
7. **Family and Friends:** For entrepreneurs considering a loan from a family or friend, there are services that can help formalize a loan agreement in a professional way so all parties are on the same page in terms of expectations.