

# NEW PLAYBOOK FOR COMMERCIAL FINANCING

Lending options while banking rules shake out.

BY MARC PORTER

The playbook for banks has disappeared. Why? The Federal Reserve Bank, under the directive of the new presidential administration, infused mind-boggling capital at the speed of light to shore up a crumbling economy. With that came an ambiguous borrower's agreement between the institution and the Feds. With more questions than answers, the rules continue to change daily. In less than five months, no one, especially the federal government, could have possibly performed the due diligence necessary. The rules of the game are in flux. Lack of clear direction whether to loan or to invest, have created confusion. Is it any wonder there is volatility and angst in the marketplace?

It will likely take another 12 to 24 months for new rules to be developed and implemented to stabilize the economy and restore consumer confidence. So what do we do now? The first order of business IS business.

The way we carry on business has changed; temporarily or perhaps for the long haul. Banks will be vigilant. Clients will be required to meet higher standards and adhere to stricter guidelines for commercial financing. Due diligence will require that clients have substantial collateral, and proof that they are credit worthy with a low degree of risk as a prerequisite for a loan. In many cases the money the bank is working with is no longer just their own. It is government infused capital, and with that comes another layer of scrutiny—yet to be fully determined. Nonetheless, the unknown makes the banking industry even more skittish when it comes to lending. Big brother is watching. But watching what? They can only guess. In the interim, banks are trying to create a safety net of sorts. Banks are implementing their own security measures. They are limiting their lending, and focusing attention on core customers that add value

to the bank. This creates stability, lowers risk, and builds the capital that banks must have to get out from under the need for federal funds and scrutiny.

Gone are the days when banks would lend on a per project basis, a single retail development, an apartment complex, or a commercial construction deal. Today, they are looking for a banking relationship with their commercial customers. This is much more than a nice quarterly chat about how business is going. They want a client's complete portfolio of money management: checking, savings, deposits, and treasury management. Not only does it provide fee income for the bank, it allows banks to keep tabs on how a business is progressing. They can see deposits, cash flow, growth, and stability. In other words, their due diligence happens daily, not just when a loan request comes in.

Bridge loans and other higher risk lending options will likely evaporate from a bank's portfolio of available financing products. These fee-based products were a source of income for banks, and will need to be replenished through other means; enter the "banking relationship" era. Clients don't like it, banks aren't happy. But, it's a new day, and like it or not change has occurred. Now what?

Most businesses have never had to look outside a bank for commercial loans. Many businesses, and banks, refer to other independent commercial lending institutions when their needs or requirements don't meet the restrictions set by a traditional lender. Independent commercial lenders are funded by private investors for the purpose of lending to small and mid-size businesses. If not governed by federal restrictions, they can offer a variety of lending instruments to ensure a finance option meets the particular needs of the business and do it quickly. Quite often, accounts receivable or bridge

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loan financing can provide the best solution. This is not permanent financing, but alternative financing for a temporary situation that cannot wait.

Accounts receivable financing or a Bridge loan is short-term, 12 to 36-month financing used as start-up funds, to stimulate fast growth, handle a crisis situation, a tax issue, or a production/deliverables situation. Assets are used as collateral in exchange for immediate funding. This type of loan has a place and distinct purpose regardless of economic conditions. Here's a recent example of what is being talked about: An electrical company applied for a bridge loan to grow their business nearly ten years ago. Now, with the green movement surging, the company saw another opportunity. With more of its customers looking for ways to save money and save energy, the time was ripe to launch a new company. The electrical company went back to its lender for start-up funds to launch this new business. It allowed the company to be cash positive in the first month of operation. The working capital gave it leverage to negotiate big discounts by paying suppliers in advance, and subcontractors early. It freed up a line of credit, and quick pay gave the electrical company a good reputation and instant credibility as a new business. The company also knew it was very unlikely for a bank to finance a start-up given the current market conditions. Although the company may have paid a somewhat higher rate for this type of financing, it was able to make up that difference or even come out ahead because of the big cash advantage that was yielded.

Some businesses are using bridge loans to take advantage of great deals on land, buildings and equipment purchases. Others need a low risk solution to stabilize their business through a temporary situation. Yes, the interest rate will likely be higher than what you may have paid elsewhere in a stable economy. It may not be the ideal price or the ideal solution. But, that was then... this is now. Banks have had to cut their losses, shore up reserves, and tighten their lending practices. Yet, ample funds are readily available from reputable independent lenders. Businesses and consumers alike would do well to embrace change, weigh the alternatives and find new rules for a new playbook. Then we can get on with the business of living.

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