GUIDE

LOANS FOR GROWTH

ACCESS TO CAPITAL: SBA, CDFI & BANKS

UPDATED AUGUST 2023

FUNDED BY: KAISER PERMANENTE, WELLS FARGO

CONTENTS

TO THE NEXT LEVEL

FAQs

START HERE: BANKS & CREDIT LOANS

CDFIs

TO THE NEXT LEVEL

INTRODUCTION

Drive, creativity, and back breaking work got you here. You have survived. Finally you are thriving [or maybe you're so close you can taste it].

Perhaps you're asking yourself: "Self, is it time to take a calculated risk?"

Do the math. What kind of profit could you make in a year with a surge of cash now? Do you stand to gain more than the interest you'd pay? Maybe a lot more?

Can you visualize having the capacity to make reasonable monthly payments in exchange for a real boost now? Does it pencil out?

You've been betting on you. Maybe it's time to let someone else bet on you.

FAQs

WHAT IS DEBT FINANCING?

Lenders offer two main types of debt financing — *term loans* and *revolving credit.*

TERM LOAN

A *term loan* is a lump sum of cash that you get immediately, which you have to pay back over a set amount of time (the term). Along with paying back the lump sum (or 'principle') you make interest payments, which is the price you pay for immediate access to the cash.

- **Personal finance equivalent: home and car loans**

For businesses who are looking to make a big acquisition — like a building, a key piece of equipment, or even another business — a term loan is a great option.

REVOLVING CREDIT

Revolving credit is when you have access to a certain amount of cash during a certain amount of time — for example, $5000 every month. If you pay back all of the cash you used during the month, you get access to $5000 again the next month. If you can only pay some of it back, you only get access to the balance the next month, and you'll have to pay interest on the unpaid amount.

- **Personal finance equivalent: credit card**

For businesses who want to smooth out their cash flows and have more breathing room at the end of each month (when rent, utilities, payroll, etc... are all due), revolving credit might be the ideal solution. You can also think of revolving credit as a kind of insurance policy — you pay a small fee to originate a line of credit or credit card, and it gives you access to cash you can tap into if an unexpected expense arises.

REVOLVING CREDIT FOR YOUR BUSINESS

LINE OF CREDIT

If your business has been around for a few years, apply for a line of credit (whether you need it or not!). According to a 2023 SFMade survey, about a third of San Francisco manufacturers use this option.

Interest rates on lines of credit tend to be around 8%

BUSINESS CREDIT CARD

Next, get a business credit card. After you've broken it in and kept a zero balance for a while, call in and ask for a credit limit increase. Repeat annually.

Business credit card interest rates tend to be around 24%

GETTING STARTED

The very first step is to ask yourself — if I had more cash now, how would I turn it into profits?

Spend some time looking at your numbers, sort out your strategy, and when you get to a place where you feel like you can't fail, you're ready to borrow.

The second step is to talk to someone at your bank.

IF YOUR BUSINESS IS:

Pre-revenue:
Set up a checking account and start building a relationship with your point of contact at your bank. Ask them what you need to do to get a line of credit and a business credit card.

Pre-profit:
Check in with your banker about revolving credit options. If they tell you it's too early, but you still need cash, that's ok. A term loan from a Community Developed Financial Institution (CDFI) might be just the leg up you need to break through.

Growing quickly:
Your banker should jump at the opportunity to offer you a line of credit and business credit card, and if you can come up with a plan to turn a term loan into more profits, they will want to help you make it happen.

In a down cycle:
If you've already done all you can with revolving credit and your bank can't find a way to make a term loan work, put together a plan for getting back into the black and talk to a CDFI.

WHO IS IT FOR? WHO IS IT NOT FOR?

There are lenders for all types of businesses and all types of financing needs. There are lenders in the Bay Area whose clients are 91% people of color and women. You have options.

The key to using credit to your advantage is planning ahead. If you can project your cost of goods and sales, you can build the cost of financing into your profit margin. However, if you are still figuring out your sales channels, or your supply chain, you might want to wait before taking out any loans, depending on the strength of your conviction in your business plan.

WHAT'S THE DIFFERENCE BETWEEN A BANK AND A CDFI?

Business lenders fall into 2 main buckets: traditional banks (which includes Credit Unions for our purposes) and Community Development Financial Institutions (CDFIs).

Traditional banks take deposits and use those funds to make loans. They have to be risk averse when they make loans because they need the repayments to be able to honor deposits. There are also strict regulations in place to make sure they do this. Banks have to operate within a predetermined set of criteria for lending, and legally cannot consider factors outside of those. Their overhead costs mean that making smaller loans (anything less than ~$750K) isn't profitable.

Community Development Financial Institutions (CDFIs) are lenders who exist to serve businesses that banks cannot.

CDFIs start with a pot of funds and make loans to businesses in their communities that they think can make a positive impact. They are able to take on more risk in their lending, so long as they see the potential to generate that positive impact they set out to foster.

Because CDFIs consider non-financial factors when making lending decisions, and make riskier loans, they do charge somewhat higher rates.

One way to distinguish between how traditional banks and CDFIs operate: banks have to look at the past when making lending decisions, while CDFIs have more freedom to focus on the future.

OVERSIMPLIFIED

Banks look at the past: **Historicals**

CDFIs look at the future: **Projections**

You should always maintain a good working relationship with your bank — that's where you keep your cash after all. If you're looking for extra capital, start with a conversation with your banker. If they tell you that you're "too early" or "not ready", they just mean, at that bank. That's when you can seek out a CDFI.

HOW DO CDFI INTEREST RATES COMPARE TO BANK LOANS?

The range for CDFIs in the Bay Area at the moment is between 7-14%. If a CDFI thinks you can qualify at a bank, and get a better rate there, they will refer you. Banks offer lower rates than CDFIs, and can even adjust rates based on the strength of your relationship.

WHAT KIND OF CREDIT SCORE DO I NEED TO GET APPROVED?

Banks look for a minimum ~680, while CDFIs don't have minimums. However, in either case, more important than your score will be the story your report tells. The person evaluating your report will consider the context, and ultimately is trying to determine whether you have made a good faith effort to make payments when you could.

WHAT IF MY BUSINESS DOESN'T SHOW A PROFIT ON PAPER?

It's not uncommon. Every lender has different standards, but many are willing to look past your last year's Profit and Loss statement (also referred to as "P&L" or "Income" statement). Banks and CDFIs will respond differently if you're in the red.

AT YOUR BANK:

- The idea is to use credit to stop the bleeding
- The first step is likely to get you a credit card (high interest rate) that you can use for the next 6-9 months to get back into balance
- From there, you'd move onto a seasonal line of credit (low interest rate), to continue the cash flow management practices you've just established

AT A CDFI:

- The idea is more like shock therapy
- If you can come up with a solid business plan that turns an injection of capital into profits, they'll take a long look at that plan, and most of all *your capacity to execute that plan*
- Make sure when you prepare your business plan you demonstrate your ability to break even on your debt service right away, and become profitable within 2 years

WHAT CAN I USE THE MONEY FOR?

Once the cash is in your account, it is yours to spend. However, there are few constraints on how you put borrowed cash to use.

In general, CDFIs can't make loans for real estate purchases or tenant improvements (if that's what you want to do, they might refer you for an SBA 504 loan — more on that below) but they are usually eager to support working capital — the money you use to cover rent, utilities, raw materials, payroll and all of the other day to day expenses of running a business.

Banks tend to support working capital needs with revolving credit, and reserve term loans for specific projects, like real estate or equipment purchases.

WHAT IS THE TURNAROUND TIME?

The limiting factor on turn around time will be your level of preparation and responsiveness. For some loans, the application process is streamlined and can be completed on your phone. More complicated applications, like those for real estate transactions, will require appraisals, insurance and escrow.

A microloan from a CDFI can close in as little as 1 week, while a term loan for a building might take up to 6.

I'VE HEARD OF SBA LOANS, IS THAT FOR ME?

The Small Business Administration (SBA) insures a couple kinds of loans, they go by the names of 7(a) (or Community Advantage) and 504. These loans come from a bank and/or CDFI and are guaranteed by the SBA.

The 7(a) loan is a term loan of up to $350K. It can be used for working capital.

The 504 loan is reserved for major assets like real estate or equipment. It's a 10, 20 or 25 year fixed rate loan, with a 10% contribution requirement (down payment). The loan is fully amortized, which means there is no early maturity or balloon payment. The rate is determined by monthly bond sales, and not adjusted to your circumstances. It is basically the best rate you can get on any loan anywhere.

Your lender will be able to identify if you are a good candidate for these programs and will guide you towards them if that's the case.

WHAT DOCS WILL I NEED TO GATHER?

Every lender has their own criteria, but we recommend getting all of the documents below together as part of your process of determining how much you should ask for.

DOCUMENT CHECKLIST

- ☐ Last 3 years tax returns
- ☐ Last 3 years income statement, balance statement, and cash flow statements
- ☐ Year to date balance sheet and income statement
- ☐ Projections for the next 12 months of revenue, cost of goods sold and operating expenses

Taking a long hard look at your business through these documents will help you better understand how you're going to turn your new capital into profits.

Other requirements could include a summary of accounts receivable and accounts payable, a business debt schedule if you've already taken out other loans, and an inventory report.

HOW MUCH CAN I GET AND WHAT WOULD IT COST ME?

TYPE OF LOAN/CREDIT	RANGE	INTEREST
Term loan from a CDFI	$10K-$350K	8-15%
Term loan from a bank	$750-$30M	7-9%
Line of credit from a bank	$50K-$10M	8%
SBA 504 loan	No Min/Max	6%

A three year, $10,000 loan with 9% interest will cost you $724. Your payments would be an easy to swallow $318 per month. Doable for most small businesses.

A $200,000 loan over 3 years at 11% interest would end up costing you $35,718 in interest. Your monthly payments would be $6,547. Ouch. That's daunting, right?

But imagine if you use that $200K to buy raw materials that you used to create $400K in revenue. That's $200K in profit for your bottom line (if you subtract the $35.7K from your $200K in profit, you could think of it as $164.3K in profit you couldn't have made without the loan).

IS A PERSONAL GUARANTEE REQUIRED?

Almost all loans do require a personal guarantee from anyone who owns more than 20% of the business.

There are some exceptions of course — a loan that's used to purchase a building can take the building as collateral instead, for example.

One model that lenders use to evaluate a potential loan is the *4 legs of the table:* ***cash flow, collateral, character, credit*** — you don't necessarily have to have all 4, but if one is missing, you still have to be able to stand.

It's worth noting again that when you work with a lender, it will become a personal relationship. A CDFI with a mission to support economic empowerment in your neighborhood isn't looking to hurt anyone. They'll do what they can to make sure you succeed. Your bank makes a lot more money when you grow than if you were to fail.

WHAT OTHER OPTIONS EXIST?

SMBX

If you're really turned off by the idea of a personal guarantee, there is a debt financing product out there that doesn't require one — and it actually comes with some other unique benefits.

SMBX is a marketplace for crowdfunded bonds. You set a goal and an interest rate — for example $100k at 10% interest. Anyone — ranging from your friends, family, and customers to the general public — can buy your bonds through SMBX. You get the cash as soon as your campaign closes, and you start making monthly payments to your investors immediately.

The Pros are that there's no personal guarantee, you can use the crowdfunding campaign to market your brand, your customers who invest are more likely to remain loyal, and investors who find you through the campaign are likely to try your product at least once.

The Cons are that crowdfunding campaigns take a lot of work — you'll probably be dedicated to promoting yourself full time for a while — and to stand out in the marketplace, you might need to offer a higher interest rate to attract investors.

ICA FUND

Maybe you don't like the idea of debt at all, and you'd rather raise money by selling shares of your business. Be warned that most equity investors are a lot harder to convince than banks (they don't have monthly repayments to look forward to) and this kind of fundraising can quickly turn into a full time job. However, there are equity investors that focus on supporting small businesses and entrepreneurs from diverse backgrounds, like ICA Fund.

ICA runs two programs, The Lab and Accelerator. The Lab is for companies who have been in business for 1-2 years, and have at least $50K in annual revenue. There's a lengthy application process, but if you are accepted, you get 20 hours of intensive coaching, and the opportunity to apply for $50K in seed funding.

Accelerator is for companies who are more established ($500K+ in revenue) and want to take it to the next level. You apply and if you are accepted, you get to participate in a 14 week intensive strategic development program. At the end of that, you can apply for $300K — $1M of funding, which will most likely cost you ~5% of your company.

START HERE: BANKS & CREDIT LOANS

If you haven't already, build a relationship with your bank. Wherever your business checking account is should be the first place you look for credit as well. Find someone you can talk to, on the phone or in person — bankers will tell you their business is all about relationships. The more they know about you and your business goals, the better equipped they are to identify the right solution if you run into a cash crunch, or have a brilliant (but expensive) dream in the middle of the night.

DIRECTORY

TOP RATED BY SFMADE MANUFACTURERS

Mechanics Bank ↗
Richmond, CA

SF Fire Credit Union ↗
San Francisco, CA

Silicon Valley Bank ↗
San Francisco, CA

Wells Fargo ↗
San Francisco, CA

OTHER INSTITUTIONS THAT THE SFMADE COMMUNITY RECOMMENDS

Ally ↗
Sandy, Utah

Bank of America ↗
Charlotte, North Carolina

Bank Of The West ↗
San Francisco, CA

Chase ↗
New York, NY

Community Bank of the Bay ↗
Oakland, CA *(SFMade's bank!)*

Heritage Bank of Commerce ↗
San Jose, CA

Umpqua ↗
Tacoma, WA

US Bank ↗
Minneapolis, Minnesota

SFMade would be happy to make a warm intro to our contacts at any of the banks listed above.

CDFIs

If your bank isn't able to give you a loan "at this time" don't give up. CDFI loans often cost a little more — but they are easier to get.

DIRECTORY

Accion Opportunity Fund ↗
San Jose, CA
Min: $5,000 Max: $150,000

Main Street Launch ↗
San Francisco, CA
Min: $10,000 Max: $350,000

Pacific Community Ventures ↗
Oakland, CA
Min: $10,000 Max: $250,000

TMC Financing ↗
Oakland, CA
SBA 504 specialists,
Min: $50,000 Max: $250,000

Working Solutions ↗
San Francisco, CA
Min: $5,000 Max: $100,000