Why the bank may not be supporting your business

Balance your business debt and equity to secure funding for business growth

Have you ever heard yourself saying… "I have a successful and profitable business that can afford additional loan repayments and I've just been rejected for a new loan. Why won't the banks support me?"

Seeking a new loan or new finance arrangements may be the best option in your mind to increase the growth of your business, however we see many business owners become frustrated when their lender (without our assistance) declines their new funding request.

Part of the answer may be found in the decision made by many business owners to legitimately take advantage of higher tax deductions (usually on the recommendation of their accountant) to reduce the profit shown in their accounts and the resulting amount of tax to be paid.

While this may provide a preferred taxation position, it will ultimately also reduce the borrowing capacity of your business.

While most lenders will place some level of reliance on the individual capability of you as the business owner and underlying performance of the business, the amount of the loan made available will be driven by the profit and cash flow shown in the accounts.

When looking at funding growth strategies for your business, you have two principal options:

1. accessing credit (taking out a loan or line of credit), or

2. raising equity (selling company stock to investors)

Both come with pros, cons and costs. Both are generally determined by the risk and opportunity profile of the business.

Credit or equity?

Accessing credit is generally a more cost-effective source of funding than raising equity, particularly in a low interest rate environment.

Raising equity typically has higher establishment and funding costs, given the dilution in ownership, and can bring complications to your business later on.

Asset assessment

The asset base, cash flow and profitability of your business will ultimately dictate its borrowing capacity, however lenders still typically require loans to be 'secured' by assets. If the business does not have sufficient assets to support a loan, the lender may look to secure the loan using the business owner's personal assets.

Most business owners would prefer to avoid using personal guarantees or mortgaging their own home (requiring them to put 'everything on the line'), so they will seek out alternatives. It is worth noting that director/personal guarantees are required on nearly all asset finance loans.

Good gearing

Lenders may also look at the gearing of the business (the ratio of debt to equity, as represented by the net assets). Typically, the level of gearing will be no more than 50% (although banks will look at 75% or higher depending on the size of the loan and the asset being acquired).

The cash flow of the business is used by a lender to determine the 'interest coverage' and its capacity to repay the loan. This is usually assessed on the ratio of debt to cash flow (or profit) that the lender is willing to accept. This can sometimes equate to three times its annual profit.

Planning for profit

Financial institutions use the company's accounts to determine the borrowing capacity of a business.

The lender's ability to assist a business is dependent upon both a qualitative and quantitative assessment of the business and its owners.

The lender will want to know if the business and the business owners are a worthwhile risk.

Good planning and implementation of strategies regarding a business's overall financial needs is best to maximise both your tax and borrowing capacity positions.

These strategies need to be regularly assessed having regard to the business's medium to long term objectives and funding requirements to ensure they remain appropriate and relevant.

Yes, you can secure a business loan

How to obtain business finance without using your home equity

AUSTRALIAN business owners understand all too well the time-honoured adage of 'It takes money to make money'.

There is a variety of reasons a business may require funding - from cash flow, to research and development and to growth opportunities.

Most businesses don't have a war chest of cash set aside to fund these endeavours, so a loan is required. While securing a loan using the equity in a home may seem the most obvious and easiest option, it is not always a preference for business owners.

That's where unsecured business loans come in.

In Australia, lenders have over $40 billion worth of business loans and advances on the books, but for many, obtaining approval for a business loan can seem like a daunting task. However, with consideration and preparation, you can secure funding for your business goals.

Quality application

In some ways, taking out a business loan is a competition where you are up against other businesses looking for funding. A well-considered application will improve your chances of approval by showing your business has value and potential.

Core requirements

Most business loans have a strict eligibility criteria. It is important to check that you meet all the requirements before applying to avoid wasting time and resources on a loan that will not be approved - and more importantly to avoid multiple enquiries on your business credit report.

Have a plan

Your application needs to show the lender that the money they loan you will help your company become more profitable. In applying for your loan, you will need to include a detailed business plan with cash flow projections and spending intentions. Before submitting your business plan, have it checked by us, your finance specialist, to ensure it is viable and viewed as sustainable by the lender.

Know how much you need

The amount you borrow will determine the risk to the lender and your capacity to repay the loan. Larger loans carry greater risks and are therefore more difficult to have approved. Ensure the amount you wish to borrow is manageable for your business.

Detailed documents

Ensure all the financial information the lender requires is well documented. In addition to this, ensure all your company's records are accurate, up-to-date and well kept. Not only will this help you meet the application requirements, it will show the lender good business practices, thereby increasing their confidence in your ability as a responsible business owner.

Maintain good company credit

Good credit is essential for obtaining finance, especially in business. Defaulting on loans, having outstanding debt and lacking consistent income and payments will work against you when applying for a business loan. Applying for a loan with any of these issues will seriously impact your chances, so it is best to address them before applying.

Tax arrangement tolls

While entering into an arrangement with the Australian Tax Office (ATO) may seem like a good short-term solution to your business's tax debt, many businesses are unaware that such payment arrangements with the ATO or other government agencies can affect their current and future financing arrangements. Simply put, a lender may not lend to a business currently in a payment arrangement. Before entering into any payment arrangement with the ATO, you should discuss it with us first.

Seek help

A business loan can be make-or-break for your business. Gaining approval and avoiding multiple applications is important for the future of your business, so do not try to 'wing it' by applying for finance yourself. Seek our quality, professional services before applying for any business loan