Bridging the Capital Access Gap

A Curriculum for Lenders, Business Development Organizations, and TA Providers

LISC ICIC

Main Topics

CHAPTER 1

Lending Landscape

(Modules 1 - 4)

CHAPTER 2

Underwriting Basics

(Modules 5 - 8)

CHAPTER 3

The Best Version of the Business

(Modules 9 - 14)

CHAPTER 4

Preparing for the Next Level

(Module 15)

CHAPTER 5

Resources for Professional Development

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CHAPTER 1

Lending Landscape (Modules 1 - 4)

Lending Landscape

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Purpose of this training series

Support business development organizations to:

- Understand the products best suited for the businesses in their communities.
- Prepare small businesses to create loan applications with the best chance of approval.
- Understand what lenders in different financial markets look for when assessing loan applications.
- Most importantly, gain knowledge and skills to increase capital access for clients who are often left out of traditional financing options.

Financing is Hard! Take Time to Plan.

- Ask your team to watch this LISC capital access training series.
- Discuss where your organization should focus based on your mission and resources.
- Take an inventory of existing skills and knowledge.
- Identify gaps and a plan for filling the gaps.
- Determine budget needed.
- Make a plan: undertake professional development, design services, research lenders, conduct outreach.

Lending Landscape: What You'll Learn

- Inequality in accessing capital
- Who are the lenders:
  - Banks
  - Credit Unions
  - CDFIs
  - Online Lenders
  - Crowdfunding
  - Small Business Administration
  - Venture Capital

Learn more:
[Overview of Small Business Finance Report]

This report is part of this training project and provides an excellent overview of small business lending.

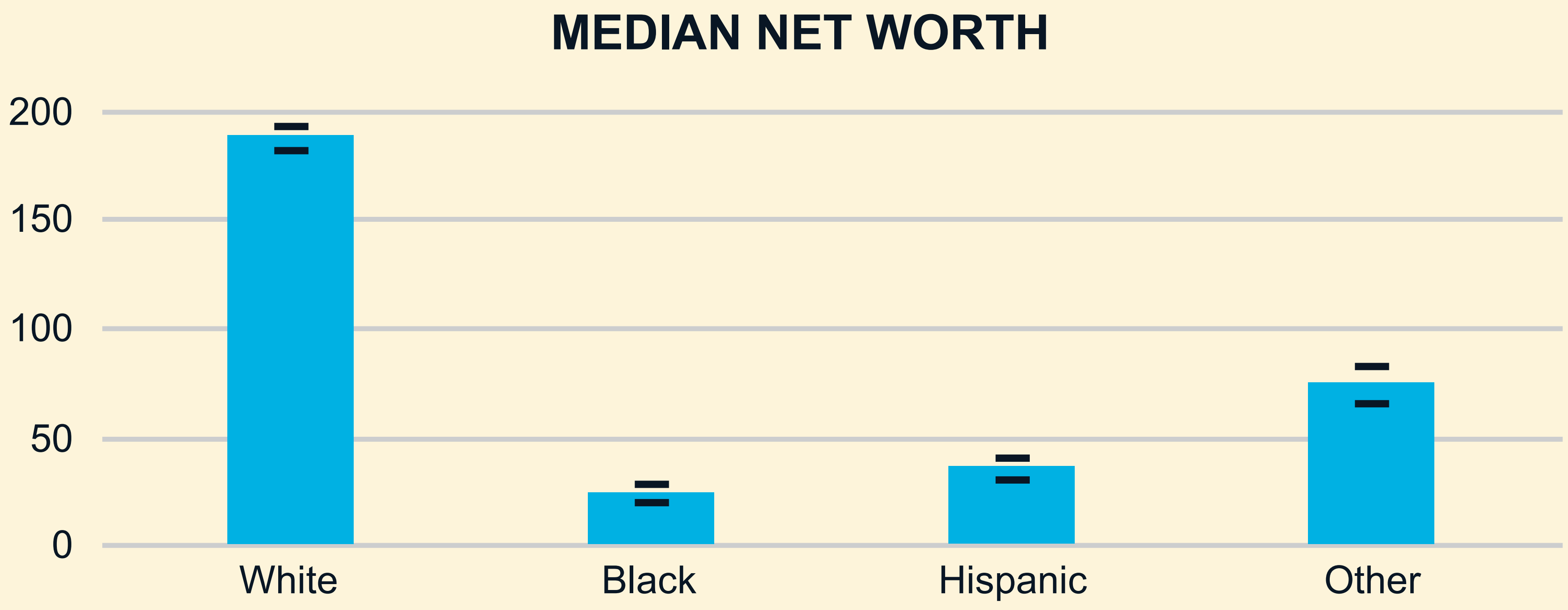
It can help you understand financing options for your business clients seeking capital.

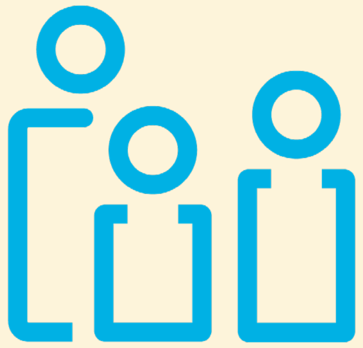
Why this is important: Inequality in Capital Access

- Although entrepreneurship is an arena of equal opportunity, there are major systemic barriers to realizing this ideal.
- A preexisting landscape of wealth, income, credit, and asset inequality is an important reason for differences in business ownership and capital access.
- Differing outcomes among small businesses reflect the racial/gender wealth and asset ownership gap, which have expanded.
- Let’s look at disparities in net worth by race and gender.
- National Community Reinvestment Coalition and Federal Reserve.

Median Net Worth by Race 2019

FIGURE 1. White families have more wealth than Black, Hispanic, and other or multiple race families in the 2019 Survey of Consumer Finances





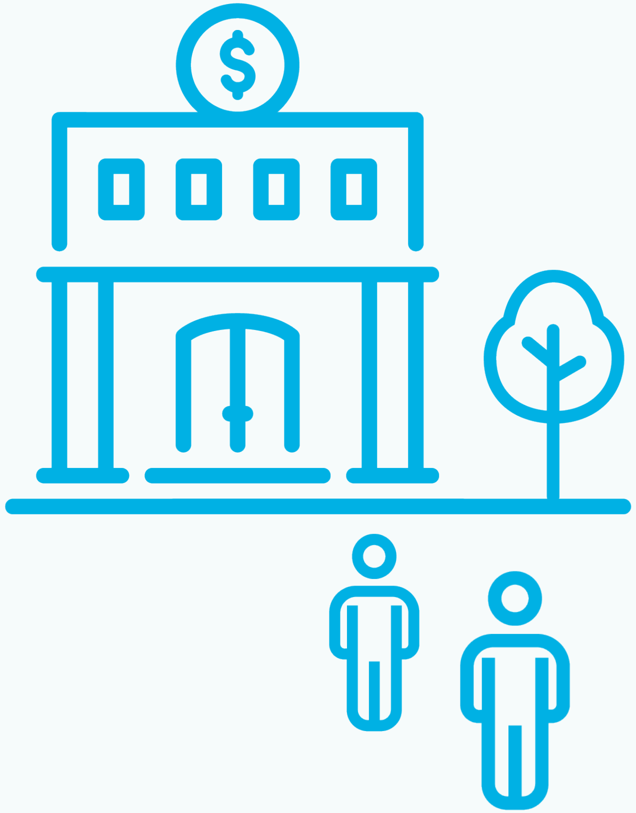
Federal Reserve: Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances

Personal Credit and Resources

- Most startups rely on personal credit. In 2020, 88 percent of firms used their owner's credit score to start the business.
- Of firms that had up to $100,000 in debt, a majority used an owner's personal financial resources as collateral.
- Given the racial and gender wealth, income, and credit gap, women and people of color face considerable disadvantage when accessing capital for entrepreneurship.

Community Banks

- A community bank primarily serves businesses and individuals in a small geographic area.
- Community banks tend to emphasize personal relationships with their customers.
- These banks are more likely to entertain loan applications from your clients.
- The very large banks, are generally not a good starting place for start-ups, young businesses, or people without significant wealth and assets.



Banks lend the most, often personal debt

- Banks remain the primary lenders for small businesses.
- In 2021, 45 percent of small businesses that received loans reported having taken a loan from a large bank and 49 percent reported having taken one from a small bank.
- Though these are not designed for business purposes, most small businesses are started with funds borrowed by their owner.
- Around 55 percent of firms were financed by their owner in 2014, using consumer loans, home equity, personal savings, or retirement funds.

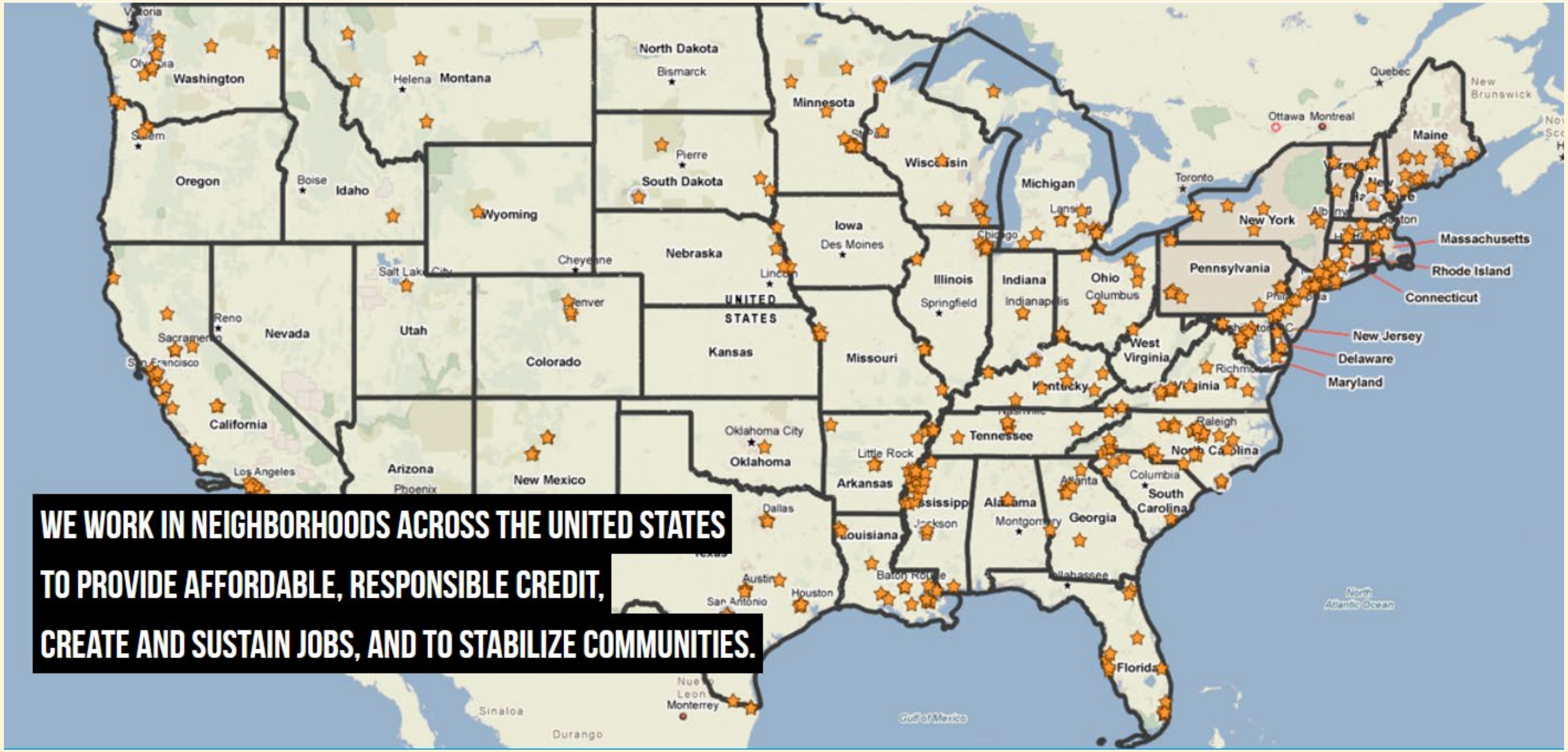
Credit Unions

- Credit unions are nonprofit financial cooperatives owned by their members.
- Small business loans make up an increasing part of their lending.
- Borrowers report extremely high satisfaction with this avenue of lending.
- Because credit unions currently specialize in consumer lending, they are an option for business owners seeking simply structured, relatively small amounts of capital over shorter periods of time.

CDFIs

- Community Development Financial Institutions (CDFIs) are nonprofit lending organizations that promote the economic development of low- and moderate-income areas.
- Mission-based lenders, who subsidize operations with grants.
- Less focused on profitability and can entertain higher-risk deals.
- Provide flexible terms and often provide technical assistance.
- Open to working out modifications when borrower is delinquent.
- Distribution across the U.S. isn’t even. CDFI Locator.

Map of CDFIs from OFN's Locator



Finance Companies

- Finance companies include lenders such as mortgage companies, equipment dealers, insurance companies, and auto leasers.
- Vehicles, equipment, credit cards, and factoring are common products.

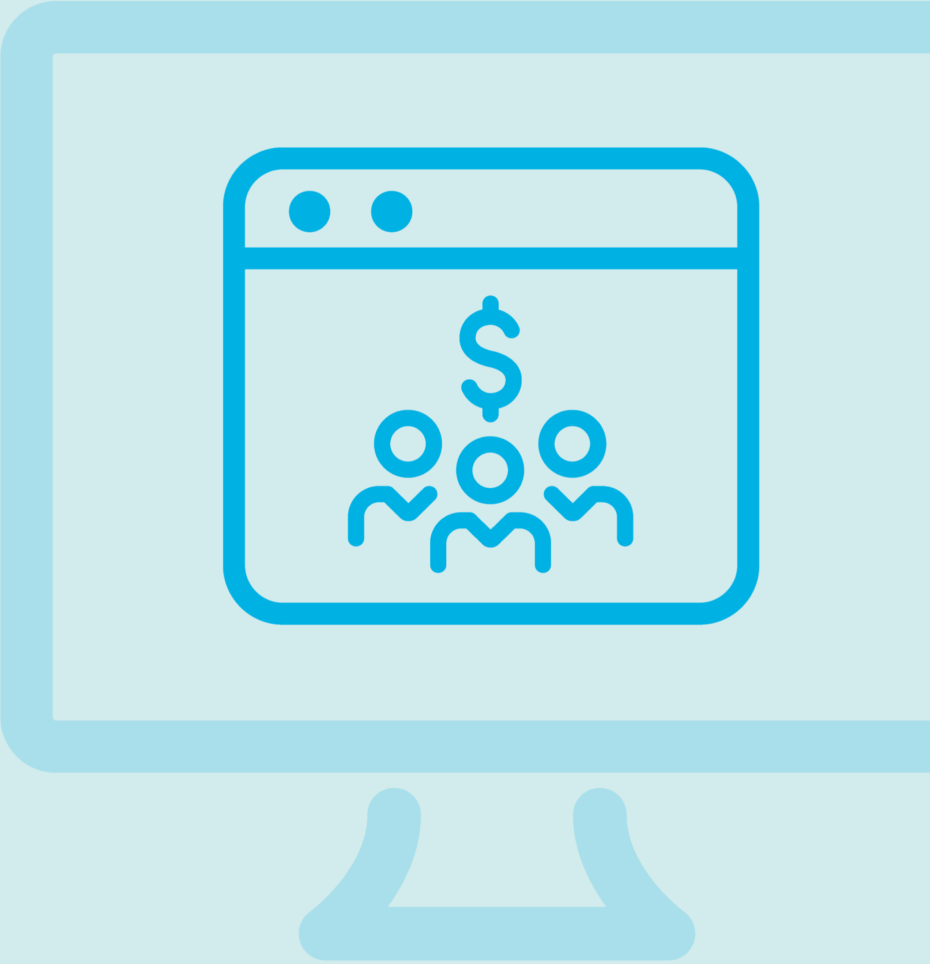
Fintech

- Companies that use technology and innovation to compete with traditional financial methods in the delivery of financial services.
- Biggest benefit: easy to apply and fast delivery of $$.
- But: high interest rates; repaid using electronic withdrawals directly from the borrower’s bank account (cashflow impact); and prepayment penalties.
- Nerdwallet has up-to-date information.

Please read:
Unaffordable and Unsustainable
report written by Accion Opportunity Fund.

Crowdfunding

- Funding a project by raising many small amounts of money from multiple people via the internet.
- Reward or donation-based crowdfunding: soliciting donations in exchange for a special, insider reward.
- Great opportunity for businesses that have or can readily build a large social media following.
- A successful crowdfunding campaign takes a lot of planning and time.

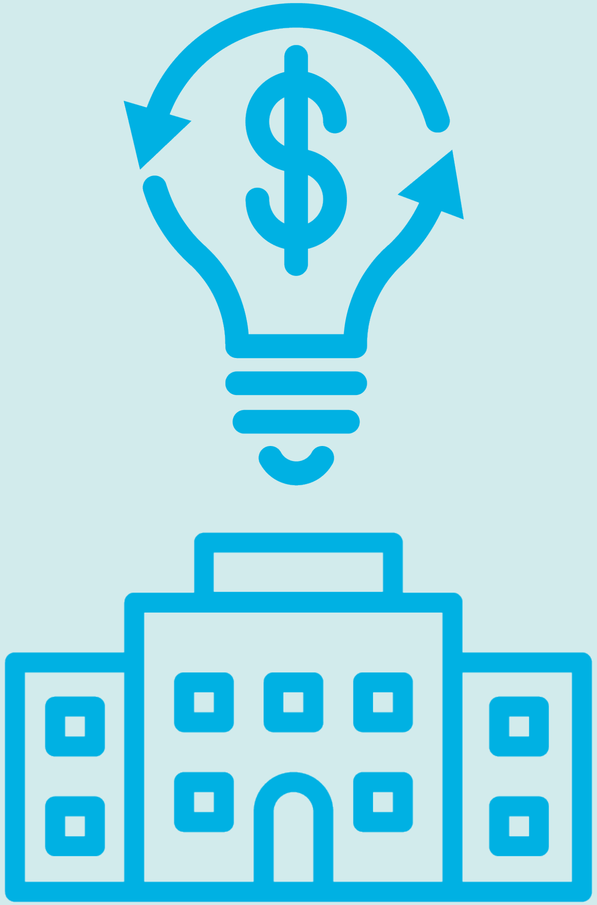


Small Business Administration Loans

- **Microloans**: Loans up to $50,000, though lending partners.
- **Community Advantage / 7a**: Run by some banks, credit unions, and CDFIs. Community Advantage up to $250K. 7a up to $5 million.
- **504 loans**: Real estate loans up to $5 million with bank participating in first position.

Venture Capital

- Venture capital makes up most of the equity investment in the U.S.; it accounted for 93 percent of the $346 billion equity market in 2018.
- Businesses with extremely high growth potential are usually the ones that receive equity financing from venture capital firms.



Benefits and Drawbacks

	Banks	Credit Unions	CDFIs
Benefits	• Reasonable interest rates • Dependable, regular monthly payments • Loans for many purposes, difference sizes • Banking relationship can grow owner's skills	• Highest borrower satisfaction rate • Low interest rates, regular monthly payments, patient terms (similar to banks) • Borrowers have greater control over their financials, more likely to get financial advice and closer relationship with institution	• Provide technical assistance and financial mentorship as standard practice • Many specialized programs that are effective for difference demographic groups and smaller businesses • More likely to lend without collateral
Drawbacks	• Discrimination in lending based on race, gender • More difficult to obtain, especially for sm. biz • Reluctant to lend to earlier stage & sm. Biz	• Primarily used for individual consumer credit (mortgages, credit cards, auto loans), limited capacity for small business lending • Not geared toward businesses seeking large, long-term loans for expansion	• Coverage is not well distributed across the U.S., concentrated in major cities with variable access in rural areas • Lack of local coverage limits ability to provide personalized business assistance

Benefits and Drawbacks *continued*

	Finance Companies	FinTech & Crowdfunding	Venture Capital
Benefits	• Relatively quick turnaround on a loan which can help with cashflow issues • More flexible on customer credit, less likely to have stringent collateral requirements	• Quick approval process • Peer-to-peer loans can fill need for smaller, quicker capital infusions • Anonymity between lenders and borrowers can reduce discriminatory practices • More individual lenders allows for borrowing more at lower risk	• Not loaned, carries no risk of defaulting on payments, collateral not required • Includes financial and operational guidance
Drawbacks	• Can be more expensive to obtain cash or working capital than through LOC or fixed-rate loans • Supply chain finance is not useful for retail biz or B2C biz, better suited for manufacturing or biz with profits from fewer customers • Failure to keep up with repayment can worsen owner's credit	• Often carry exorbitant interest rates • Lowest borrower satisfaction rates • Terms vary enormously between platforms, increased reliance on decentralized systems which can be difficult to navigate • Virtually no counseling services attached to this sort of lending	• Exclusive and highly concentrated in tech and economic hubs • Networks and social circles required are virtually impossible for sm biz owners to break into • Equity investments come with diminished control over company • Exclusionary toward women and people of color

Given this landscape…

The orientation of this training series will:

- Support BDO staff to gain skills and knowledge that helps clients improve their ability to access capital.
- Focus on how to access capital from CDFIs, community banks, and credit unions.
- Provide some ‘behind the scenes’ information about how lenders analyze loan applications.
- Offer suggestions for preparing for the ‘next level’ of financing.
- Provide resources for more information and training.

CHAPTER 1

Lending Landscape

(Modules 1 - 4)

UP NEXT

Bridging the Capital Access Gap Modules

CHAPTER 1

Lending Landscape

(Modules 1 - 4)

1 Lending Landscape
2 When to Borrow
3 Finding the Right Lender
4 Building Relationships with Lenders

CHAPTER 2

Underwriting Basics

(Modules 5 - 8)

5 What is Underwriting?
6 Five C's Overview
7 Understanding Credit
8 Debt Service Coverage

CHAPTER 3

The Best Version of the Business

(Modules 9 - 14)

9 Quality Applications
10 Startups vs Existing Businesses
11 Loan Ready vs Not Qualified
12 Improving Credit
13 Improving Debt Service Coverage
14 Collateral

CHAPTER 4

Preparing for the Next Level

(Module 15)

15 Preparing for the Next Level

CHAPTER 5

Resources for Professional Development

(Module 16)

16 Resources for Professional Development

Thank you for joining us!

Presenter: Susan Brown
Business & Nonprofit Development
Microlending & CDFI Capacity Building
Online Program Design
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LISC

Together with residents and partners, we forge resilient and inclusive communities of opportunity across America–great places to live, work, visit, do business and raise families.

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