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Getting to 57

How to convince a lender to say 'yes' - or at least, not to say 'no'

By Dennis Monroe

There is no question that trying to obtain bank financing, equipment or even financing from a national finance company is now about as difficult as it has ever been; however, all is not lost. The most important approach to finding financing for a franchise business in today's environment is persistency. It is what I'll call "Rule 57." "Harry Potter and the Sorcerer's Stone" was rejected by 56 publishers until J. K. Rowling brought the manuscript to the 57th publisher. That same persistency is required today by a franchise business owner.

More than sheer persistence and numbers, the key is perseverance in dealing with banks and financial organizations, and even lenders with whom you have a relationship and have done business in the past.

What I have come to believe is that you just don't let them say "no." Keep coming up with ideas and approaches until something seems to stick. Even if you do not feel that you are making much progress, ask the lenders what they can live with, even if it is based on the use of cash collateral or marketable securities; at least you have kept the ball in the air.

To be more specific, let's look at ways you should approach lender situations. The following are the key elements needed when meeting with a lender:

Historical financials

1. Don't avoid historic financial information, but only give historic financial information that is detailed with line-by-line explanations for everything on the financial statement that may be somewhat problematic. Even if your statements are reviewed or audited, it is very important to define:

- Extraordinary items on the profit and loss statements;
- Unusual aberrations as they relate to expenses;
- Start-up expenses;
- Your capital expenditure accounting rules, specifically what dollar amount gets capitalized and what amount gets expensed;
- Negative net worth needs to be clearly addressed (which may have been a result of shareholder buyouts, some type of extraordinary loss, asset impairment or something that can be explained away);
- Look at all liability items and explain things such as deferred rent, deferred revenue, gift card issues, anything that can be of concern on the liability side.

These clarifications should be done in a systematic way with detailed explanations so when the lending institution is looking at historic financials, they are looking at all the detail in the best light.

2. If there was progress from 2008 (which was obviously one of the worst years possible) and 2009, and if there has been progress already in 2010, this progress should be highlighted. Show your actual performance to your budget; hopefully your budgeting process is effective, which provides more reliability for a strong 2010.

3. Do not leave any rock unturned; explain and expose everything you think the lender may have issues with.

Long-term view

Provide a clear understanding of the strength of your company on a long-term basis. For example, "We have been in business for 25 years and have not had store closures." "We've had a string of profitability, probably only offset by 2008 or 2009." Also, you may want to highlight a strong performance in 2010.

Debt repayment

Explain to the lender how the debt will be repaid. Do a detailed analysis for the lender of the fixed charge coverage ratio (which is the cushion of cash flow over what your fixed obligations). Show in detail how your existing debt and the debt you are asking for (on a store-by-store basis) will be repaid and the cash flow cushion for the repayment. Lenders like to see a fixed-charge coverage in the 1.4-plus range on a proforma basis. Make sure this debt repayment schedule includes 2010, 2011, 2012, 2013, or the term for your requested loan.

Guaranties

Be up-front and present guaranties as a requirement versus waiting for the lender to come back to you for the guaranties. Provide the guarantors' personal financial statements and tax returns in the initial package. Also explain away any issues as to the guarantors' personal financial statement. Further, if one of the significant assets in a guarantor's personal financial statement is the business that is the proposed borrower, make sure the value reflects a conservative approach. Create as much transparency as you can.

Structure

Take care of any legal structural issues or concerns about collateral or shareholder loans or any items that could legally create some problems before you make your loan request. A clean balance sheet is key. Personal assets, intercompany loans, and uncollectable receivables are all problems for your lender.

Proformas

If your request is for new-store development, make sure the proformas are very detailed, show monthly cash flows and also show a very explicit understanding of start-up costs, preopening costs and other expenditures you are asking the lender to finance. The proformas should also reflect the fixed charge coverage on an individual store basis for repaying the debt requested. Further, it is important to have an opening balance sheet for any new store, even though it may be consolidated on the overall company's financial statements.

Tenacity

If the lending institution comes back and says they cannot loan money to you based on your last two years of performance, look them in the eye and ask them how you can structure this to get around the last two years of performance. Ask them if they can make the loan directly to the guarantors. Can a new entity be created that starts out with a clean balance sheet? Can we look at putting the collateral of strong stores into a "special purpose entity" in order to provide additional collateral for the loan requested?

Pursue all of the above ideas. You have to keep the ball in the air with a number of different financing sources. It is a juggling act, but the key is to not let any balls drop; keep them up in the air until you can catch the one that is going to provide financing. It is a tough world out there, but it is doable. So don't let the lender say "no." Learn how to get them to say "yes." FT

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