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Juggling 101

How to get a bank to say 'yes' to a loan, despite the fact you're a restaurant

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TRYING TO OBTAIN BANK financing, equipment leasing or even vendor financing for a restaurant is one of the biggest challenges in the business world. Each week I hear from local restaurateurs who have either hit the wall and need some liquidity because it's a slow time of year or have been undercapitalized from the start. Others are looking to expand. They all want to know: "How do I get funding?"

In the past, help has come in the guise of individuals who like to invest in restaurants. Unfortunately this key investment group is getting older and hasn't necessarily been replaced by younger, affluent business people, particularly millennials. So restaurateurs still need to look to banks, equipment leasing groups and others to provide the funding. Equity will always be a part of the equation, and there will always be people who will want to invest, but the industry needs more bank debt, (or "senior debt") for the non-mega chain restaurant companies, such as operators with a first location trying to finance their second, or have five units and are trying to finance two more, or have 10 or 15 different concepts to finance.

So when you don't have friends and family willing to invest, it's important to be persistent, to keep looking at options, to always keep your ears open. Talk to your service providers: attorneys, accountants and others in the industry who might be making loans. With persistence comes hearing a lot of "no's." So when the answer to your question, "Do you do restaurant loans?" is "We've done some, but we don't make a habit of it," you'll need to be extra persuasive.

Here are some rules and things that you should look at to get yourself ready for traditional lenders. These apply not just to the banks, but to the other lender sources. They will all want to see your overall credit, ways you run your business and, most importantly, your present and historic financials.

Historic Financials: When you give historic financial information, include detailed 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 important to define any type of extraordinary items, such as non-reoccurring expenses. Clearly define start-up expenses and inform the lender of your capital expenditure accounting rules, specifically what dollar amount gets capitalized and what amount gets expensed. Negative net worth (which means your liabilities on your balance sheet exceed your assets) needs to be succinctly addressed (which may have been a result of shareholder buyouts, some type of extraordinary loss asset impairment or something that can be explained). Also look at all liability items and explain things such as deferred rent, deferred revenue, gift card issues and anything that can be a concern. This should be done in a systematic way with detailed explanations so that when the lending institution is looking at historic financials, it is looking at all detail and explanations to put you in the best light when reviewing the restaurant's lending package.

Long-Term View: Provide a clear understanding of the strength of your restaurant company on a historic, long-term basis. For example, stress you have been in business for 15 years and have not had store closures. You may have had some recent problems, but always focus on long-term. Also, make sure you emphasize your background in the restaurant industry, that you've been in it for a certain amount of time and you are not a newcomer.

Proformas: If your request is for new-store development, make sure the proformas are detailed, show monthly cash flows and also have an explicit understanding of start-up costs, pre-opening costs and other things you are asking the lender to finance. Further, it is vital to have an opening balance sheet for any new store, even though it may be consolidated on the overall restaurant's financial statements.

Debt Repayment: Don't expect the lender to understand how they are going to be repaid: explain it. You need to 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 are). Spell out how the debt that you have and are requesting (on a store-by-store basis) will be repaid and what the cash flow cushion is for the debt repayment. Lenders like to see a fixed-charge coverage in the 1:4+ range (this means you have a cushion of about 40 percent of your cash flow to pay your fixed-charge obligations) on a proforma basis and also see historically that you perform at that level.

Guaranties: Be up front and present guaranties as a requirement versus waiting for the lender to come back to you for them. Provide the guarantor's personal financial statements and tax returns in the initial package. Also explain away any issues as to the guarantor's personal financial statement. Further, if one of the significant assets in the 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.

Legal Structure: If there are any legal structural issues or concern about collateral or shareholder loans or any type of items that could legally create some problems, like many separate companies, make sure those are taken care of before you make your loan request. A clean balance sheet and understandable legal structure are key.

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

Know Your Sources: If you are going to grow, always consider equipment-leasing companies that specialize in restaurants, which may also include leasehold improvements. Their rates are higher but their credit requirements are more favorable. Also look at vendor financing, which is debt but is used to finance the vendor's specific piece of equipment, like an ice-maker or walk-in cooler.

Another source is what we call mezzanine financing. These are unsecured or second-position loans that carry a high rate of interest. In many cases, they carry an equity component so that the mezzanine lender can get a higher return. In many cases, with an equity component for a higher return. There are a number of these sources in Minnesota. Sometimes they are called SBICs, small business investment companies, which is part of the SBA, and some are specifically charged with making minority loans. In addition to these funds, there are also a select group of individuals who are willing to make high yield debt loans to restaurants.

Just remember: It's 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." Juggle until they say, "yes." FSN

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