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Guyana Economic Opportunities

How to Approach Banks
A Guide for Small and Medium Enterprises

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TABLE OF CONTENTS

Introduction

Small business operators see banks as unfriendly, uncaring institutions that are reluctant to lend to small businesses. Especially in lesser-developed countries these perceptions create an air of mystery surrounding the operations and the personnel of lending institutions. Potential borrowers are intimidated by these establishments, their people and their requests for what seem like unnecessary and unavailable information. They feel that bankers do not appear to understand the workings of small businesses and entrepreneurs. Business owners tend to be optimistic in their predictions. Bankers are analytical, cautious and mathematical.

Banks, on the other hand, perceive small businesses as being disorganized and mismanaged. Business decisions are made by emotions rather than by rational analysis. Their owners seem to be indisciplined; they manage by instinct and are excited by and unafraid of risk. They dislike paperwork and are believed to be capable of withholding information from the banks. Because of these misconceptions bankers and small and medium business enterprises initially do not speak the same language. They eventually come together in a forced courtship that is characterized by mistrust and anguish until credit is disbursed.

Universally we speak of "the business sector" and "the banking sector'" as though they are distinctly different and unconnected. Banking is like any other business; it buys and sells money from and to different people just like any other supplier of products and services. Banks and their borrowers depend on each other to generate revenues and to provide a profit to their owners.

Experience is showing that the small business sector plays a vital role in developing countries. The relationship between lenders and the small borrower is improving. While bankers have studied and gone a far way in understanding their clientele, considerable misunderstanding still exists in the entrepreneurs' perception of the banking sector.
A better understanding of the banking culture will assist entrepreneurs in improving their relationship with the banks and increase their opportunities for financing.
This guide has been developed specifically to assist small businesses when they approach the Banks for financing.

Profile of a Bank

A bank is another business operating in your community. It provides financial and related products and services to the business and private sectors while making a profit for its shareholders. It is very specific and distinct in its operations. While it may provide mentoring and advisory services, trading in money is its core business, the business for which it is licensed.

A bank is like any other business. It trades in money. It buys money in smaller volumes (retail) and sells it in larger volumes (wholesale). It buys deposits and sells loans and overdrafts in local dollars. In addition to buying and selling foreign currencies, it can also lend in foreign dollars. Banking can also be explained as a business that rents funds (money) on short terms from depositors and then leases the funds on longer terms to borrowers.

Banking is based on confidence. Depositors invest their money with the bank where they know that it will be safe, earn interest and be available whenever they need it. The bank puts these funds to work and the revenues that are earned are used to pay depositors, the bank's expenses and a profit for bank's shareholders. Everyone has something to gain in these relationships.

Banking or lending is referred to as one of the oldest business institutions. Two other institutions that we are familiar with are the medical and the legal institutions. These have many similarities to banking. They are legislated, regulated, tell us what we can or cannot do and even have their own language. Consumers tend to misunderstand these businesses. These misunderstandings are our reaction to the policies and procedures that are unfamiliar to us and have been put into place to protect everyone. Some of these policies and procedures are self-imposed and have been created because of past experiences. Lenders, like the medical and legal professionals, follow a strict code of conduct.

As borrowers we are required to develop a relationship of understanding with the banker, so that the bank may invest depositors' funds with us. While the lender is learning about your business, you need to understand why the lender needs a variety of information and proof of the accuracy of the information. While bankers work with depositors and borrowers, their code of conduct is designed for one overall purpose. Banks protect depositors.

The Business of Banking

Banks must not be confused with Trust Companies or Building Societies. These are different entities. A Trust Company is a financial organization that acts as an agent for its customers in many capacities. It administers trust funds, executes Wills and acts as the custodian of property. Some trust companies provide lending services. A Building Society is a cooperative association owned by its members who are the depositors. Deposits buy shares in the operation. A building society usually lends exclusively for the acquisition and construction of residential real estate. The maximum amount it lends is in keeping with the needs of its membership.

A Bank's main activities provide investment opportunities to depositors, and sources of financing for borrowers. In addition, it moves funds and makes payments for its customers in and out of its country of operation. Some banks are also involved in providing general assistance and guidance to the business sector.

Trading of "paper" is another form of business. It may buy, for a discounted amount, negotiable documents such as bills, contracts and other "paper of value" making the cash available up-front to the business. While it can also trade in financially related services and information, it is not allowed to hold nor trade in other assets. Specifically a bank cannot trade in real estate or the stock (shares) of other businesses. These restrictions safeguard banks from the possibility of speculation or conflict of interest when lending against collateral held as security.

Banks are controlled by a Board of Directors, which sets the policies and guidelines for its management. The Government assures the safety and soundness of a bank's operation by enacting legislation and regulations which control licensed Financial Institutions. These two entities are the major factors that affect decision making in a bank. By understanding these guidelines and regulations you will be able to better understand banks and develop a good and beneficial relationship with your banker.

Even though Banks operate under strict External guidelines and stringent Internal procedures, they treat each customer on an individual basis. They are flexible and accommodate the needs of their clients. Their revenues and profit come from your success. The relationship you develop with the bank is of the utmost importance. Your skills at negotiating and the strength of your business are what will determine the terms and conditions of your dealings with the bank.

Banks are in business for profits. . . . .banks therefore develop relationships with winners.

The Lender

The lenders' job is to predict the future. The bank's loan officer must gather sufficient information from the client and analyze these to predict the future of the business. If the analysis indicates that the borrower could attain a comfort level that is acceptable to the bank then the loan application is encouraged. If in their opinion the business is capable of doing what it says it can do, then a loan becomes possible. The analysis will include investigations to determine, the integrity of the borrower (individuals), and the ability of the business to repay the borrowed funds with interest, in a prompt and businesslike manner.

All information you provide or claims that you make, must withstand testing. Lenders do not like uncertainty and by nature are cautious. All applications for financing are examined with regards to the risk to depositors' funds. Assessing these risks is the tool of the banking trade. A bank is made up of a number of levels of credit and management personnel. Analysis, recommendation and approval are conducted sometimes at different levels within the organization. All approved credit applications are reviewed at a more senior level. In some instances persons not involved in the original approval process carry out the disbursement of the loan funds, which must follow an approved program.

The consequence of these processes is that the information supporting a loan and the loan are analyzed or reviewed in a number of different ways and by many individuals. All information that supports a loan are checked and crosschecked by the collective expertise of the organization. As a potential borrower you must appreciate and understand these requirements so as to develop a good relationship with your banker and to assist him in helping you. The banker represents the bank. You are their business. The banker needs to trust you and have confidence in your business skills. Help the banker to help you by providing all information that is required.

The Borrower

Dictionaries define an entrepreneur as a person in effective control of a business with the chance for profit or loss. In real life, an entrepreneur is a "risk-taker" who engages in business opportunities with the chance for profit or loss. In essence the small business owner is this entrepreneur. The owner is also manager and is responsible for all aspects of the business, from dealing with the bank to cleaning of the premises. The small business owner is a risk taker. Bankers on the other hand are cautious and are perceived to be averse to risk.

As a business owner, you believe in getting things done now and doing the paper work later. A bank does paperwork first. You make decisions based on gut feelings and instinct. A bank analyses risk, recommends the approval of, then approves a loan. You are confident of the success of your plans for the future. The bank wants proof that what you predict will happen. You know in detail, in your memory, what your plans are for the future. The banker knows only what you have told him or her.

Most times you and your banker do not speak the same language and you see things differently. Developing a relationship with your banker is no different from your relationship with your doctor. He speaks a different language. There is an interview, an examination, verification by laboratory results, and then treatment and prescriptions are set in place. You trust and confide in your doctor so that he understands and more easily addresses your needs.

Your banker requires similar trust.

As a borrower you need to "lease" money from the bank. Convince the bank that you will be able to take good care of it and return it in good condition, with all costs (interest) on the agreed date.

Do You Need To Borrow?

The main reasons for borrowing are:

1. To start a new business;
2. To purchase an existing business;
3. To expand or upgrade an existing business.

Whether you intend to start a new business, purchase an existing one, or upgrade your current operation, you need to decide if borrowing is the best option for you. Borrowing comes with a cost. This cost can be a significant burden on a small start-up business. Minimize your borrowings by seeking alternatives to purchases. You may also consider the addition of a silent partner or investor into your plans. For a small start-up business, these opportunities may be limited to family, relatives and friends.

Starting a new business

When starting a new business, you should examine the possibility of renting or leasing, instead of purchasing any asset. Consider the purchase of used instead of new equipment.

It may be difficult for a new entrepreneur to get supplier credit, but you should investigate the possibility of purchasing raw materials on 30 days credit.

Remember borrowing has a cost, which is currently in the 17-20% range and interest expenses can be a drain on future profits.

Purchasing a current business

For the purchase of an on-going business, you need to investigate the following options:

- Would the vendor assist you in financing the business by giving you a loan or mortgage against the assets?
- Do you need all of the assets currently owned by the business?
- Will you have access to the same credit arrangements that were available to the previous owner?

In the sale of a business, payment is generally made for the Goodwill of the business. Goodwill is the dollar value of the business' reputation and the relationship it has developed with customers and suppliers. Determining what is goodwill and assessing the value of it is extremely difficult. It depends on your negotiating skills with the vendor. The vendor of the business should be prepared to take back a loan for the amount of the goodwill. This loan could be at a preferred (reduced) or no interest rate.

Expanding or upgrading a business

If you are expanding your current operations, you may consider, in addition to the above, the idea of selling non-productive assets. Another option is to sell an asset and then lease it from the purchaser. Let us assume that you are operating from your own building and would like to expand to another location. Consider selling the current building to an investor, from whom you will lease it. The proceeds of the sale may then be used to finance the expansion.

Personal requirements

Before you borrow, consideration must be given to your future income and your personal and family's well being. If you are currently employed and are contemplating entrepreneurship, your business will have to pay your family's bills. Determine what is this amount? Carefully assess the forecasted profits of the proposed business. Will the business be able to support your family's needs and repay the bank?

Lending Criteria

Lending institutions have standards which are used to assess and judge loan applications. These are referred to as the bank's lending criteria. They are designed to assess the risk on a loan and the likelihood of its repayment.

Depending on their ownership and corporate objectives, banks will emphasize different criteria for credit approval. For example an agricultural developmental bank with International and Governmental funding may favour loans that create jobs and develop the agricultural sector. But, like any other commercial lender, it must be convinced that borrowers will be able to repay the loan principal plus all interest, on a timely basis.

All financial institutions use a common set of criteria to assess proposals for financing. These criteria are as follows[1]:

1. MANAGEMENT'S ABILITY
2. EARNING POTENTIAL
3. INVESTMENT OF THE OWNER
4. SECURITY

For most business lenders (1) Management's Ability and (2) Earning Potential are the most important factors in their credit analysis. The level of Investment of the Owners is used to determine their commitment to the business.

Financial institutions do not lend solely on the value of security. The sale of collateral pledged, as security is the "insurance policy" for repayment. The bank would cash in the collateral in the event that the business is unable to make its payments or if it "dies". Lenders apply a rating process for assessing each criterion and while the yardstick may differ most institutions generally follow a common practice. Years of similar institutional experience and the guidelines of the country's laws and regulations promote this common practice. During the interview and loan investigation, you will be asked questions generally in these four areas. Your preparation for your interview therefore, should follow these same guidelines.

1) Management's Ability

The success of a business depends on the skills of its management personnel.

The effective management of a business requires experience generally in the following areas:

- Proven and/or successful experience as a business manager/supervisor.

[1] Some institutions utilize these criteria under different names. In some instances they are called the 5 "**C**"s of credit. The 5 "C"s refer to the assessment of credit in the following areas**: Conditions, Collateral, Capacity, Commitment and Character**. Other financial institutions may refer to their lending criteria as the 4 "**P**"s of a loan proposal. The 4 'P's are **Purpose, Payment, Protection and People.** Do not be confused by these. These are similar to the four basic criteria listed here.

- Experience and/or qualification in the technical or trade skills required by the business.

This criterion is one of the most important factors that can influence the success or failure of a business. Management's ability is ultimately reflected positively or negatively in a business' performance. It can make or break a good business. Management's decision making, whether at the executive, operational or technical level, charts the course for the short and long-term prospects of any business.

2) Earning Potential

You need to paint a financial picture of your business. This picture should include answers to the following questions:

- What is the make up of your business?
- What has it done?
- What will it do in the future?

Financial statements for current or new businesses must be prepared and presented.

A **Balance Sheet**, which is a statement of assets and liabilities, will state what you own, what you owe and how much you are worth. The **Profit and Loss** statement will show your sales, expenses to generate those sales, and the net result, **Profit**. For a new business, the profit and loss will be a **Forecast** and will contain estimates, footnotes, and additional information to support your sales, expense and profit figures. The bank will assess your forecast, adjust the figures based on their own experience, and most likely, arrive at a different level of profit.

This figure is the earning potential of the business. It must be enough to provide you with a fair annual income for running the business and most importantly, provide for the monthly loan installments. The forecasted level of activity and profitability must be sustainable over the length of the loan.

3) Investment

Only in special situations will banks finance 100% of a new project. The lender "**co-invests"** with the borrower so as to share the risk. It is in the borrower's best interest to protect his or her investment by working for the business' success. The level of investment influences the level of commitment by the borrower and offers similar protection for the bank's investment.

The amount of investment that is required depends on a number of factors. The purpose of the loan and the value of the collateral pledged as security, would determine what percentage of investment is required from the borrower. The loan to investment ratio can range from 2:1 to 4:1. This means that the bank will advance two dollars or four dollars for each dollar that the borrower will invest. By protecting his or her one-dollar investment, the borrower also protects the bank's two to four dollar loan. Your investment does not have to be cash, but can be the value of assets you are putting into the project. When the investment is in the form of cash, you will be required to spend your money first, before drawing on the loan.

4) Security

"How much money can I borrow against my property valued at $X Million?"

Many bankers in Guyana cite this often-asked question as a common occurrence during interviews. The answer is "Zero". The pawn broking sector lends entirely against the value of an asset. The ability to repay determines the amount of a bank's lending. However, as explained in another chapter, the country's financial regulations encourage the banks to make loans that are fully secured.

Collateral, which are the assets pledged as security, take many forms and are valued quite differently depending on the purpose of the evaluation. Construction or replacement cost, today's sale price and the estimated sale price three years into the future are vastly different. The conditions under which an asset will be sold in the future and the status of the vendor (the lender) of the asset, influence the sale price.

When a bank has to dispose of collateral held as security for a loan, it occurs after a considerable period of time, during which it incurs legal and other costs. The bank in most instances has to seek the Court's approval for disposal of the assets. The assets could be in a deteriorating condition and require maintenance and repairs prior to offering for sale. The assets are sold by a bidding process, a process that attracts bargain hunters. Experience shows that selling by public auction yields selling prices considerably lower than private sales. A bank therefore must consider the liquidation value, under distressed sale circumstances, when it evaluates assets. This valuation is therefore considerably lower than the current market value.

The following is a list of typical collateral. Included in the appendix is a format for the recording of all moveable assets.

- Cash.
- Guarantees from other banks.
- Mortgage on Land and Building.
- Charge on Vehicles.
- Charge on Machinery and Equipment.
- Charge on Receivables, Inventory and Raw Materials.

Overall assessment

The layman thinks in terms of borrowing against the value of security. Good, high-valued security does not make a business more profitable. Good collateral does not make a weak loan application a better loan prospect. High valued collateral does not offset weak management and earning abilities.

A business with good profit potential and under strong capable management is very appealing to a lender. These are the indicators that the business would be able to repay its debts.

Meeting the Banker

So you are nervous, and quite rightly so!

Remember, a banker is another person working for a business that has strict regulations and procedures. If you satisfy their requirements, the banks will invest in your business.

Your initial meeting may be with a front line credit person who will assess the general nature of your request. You may then be requested to complete an application or be referred to a credit officer. Once the information has been submitted a substantial interview will occur. Most banks operate with a very tight schedule during opening hours. Loan interviews may be arranged after the bank is closed to general transactions. If you are already in business, meeting at your location can be very helpful.

First impressions count. In the initial stages of your meeting you will need to establish that you are honest and reliable. Regardless of the information you provide, the interviewer **must trust you as a person**. You must fully understand any information that you are presenting, as you will be answering questions related to that information. The bank has years of experience and as a result is able to estimate potential markets, sales, and the value of equipment and other assets. They will adjust your estimates and your forecast, as you may be too optimistic. You stand to gain from this exercise, as it is a test of your estimates by experienced persons.

The bank will reformat the information to fit their procedures. This will result in a number of questions and the way you answer these will establish your knowledge of the business and show your ability to manage it successfully. Answer questions honestly and if necessary, ask for time to get the correct information. Practice full disclosure.

This is not an interrogation. Questions asked will cover basically two areas. Firstly, how you expect to achieve forecasted revenues and secondly, how you expect to control expenses. There is no suspicion or hidden motives in these questions. The interviewer wants to be convinced that your forecasts are realistic and attainable. He/she wants to be assured that you will be prepared for any eventualities.

Types of Financing

There are many kinds of financing available to a business. One basic distinction is the length of the repayment period. The purpose for which the loan is required also determines its length. There are short, intermediate and long term financing agreements that you can negotiate with the bank.

Short Term Financing

During a 12-month period, a business buys raw materials or services, pays expenses, sells finished products and collects receivables on a recurring basis. Short term financing bridges the gap between the outlay for purchases and the receipt of cash from sales.

In some countries, as in Guyana, "OVERDRAFT" financing is available. This is an approved amount by which a business may draw cash over the balance in its chequing account. Interest is calculated on the daily balance. The overdraft must show significant fluctuations in its usage and must be reduced to zero during the year. It is available for 12 months and is generally renewable annually.

Loans, generally for a period of 12 months or less, are also a source of short-term lending. This type of financing is used to assist a business in meeting unusual or unexpected demands.

Intermediate Financing

Loans with a repayment period in the two to five-year range are considered intermediate financing. Used to purchase assets such as machinery, equipment and buildings. Repayment may be delayed to commence when the acquired assets become productive and start to generate revenues. The new assets are usually lodged as collateral for these loans.

Long -Term Financing

This financing is used to finance the acquisition of major assets such as land and buildings. Terms are generally in the five to ten year range. Longer terms are also available. Conditions similar to intermediate financing applies.

Loan Application

There is always an initial interview during which a decision will be made whether or not your application has potential and will be encouraged. For consumer and smaller business loans, applicants complete an application form and attach supporting information. During the interview the banker will record additional notes for future reference and analysis.

You have about thirty minutes to convince the interviewer that you have a bankable proposal. A proposal which shows that you will be successful and that the loan will be repaid. A proposal, into which depositors' money can be safely invested.

You need to explain your proposition, as simply as possible, by answering the following questions.

- What is your business background or experience?
- What do you need?

- Why do you need it?
- What will it cost?
- How will it be paid for?
- How will the loan help your business?
- How do you expect to repay the bank?
- What security will the bank have for the loan?

For example, imagine that you are a farmer who has ten years of experience and now would like to buy your own tractor. You will explain to the banker your successes as a farmer. Justify the size and type of tractor that you require because of the size of your acreage. State the cost of the tractor, and the amount that you are able to put towards its purchase. How much do you need to borrow? Show that the tractor will help you to prepare your fields on time and make your business more profitable. As a result, you will be able to repay the bank in four crops or two years, and as security the bank can take the tractor as collateral for the loan.

This example answers all of the above questions and gives the banker a good understanding of who you are and what you need. Be prepared to answer all of the above questions before you make your appointment. The banker will encourage your application by requesting further clarification or additional information. This is when you should provide further details. This is the start of the paperwork phase. You may be asked to provide a Financial Requirements statement as well as a Forecast. A brief background on the owner/manager will be required. Examples of these follow.

Remember, to work with you, the bank needs to understand your business. No two private businesses are alike. Even though the bank may have financed a similar business, yours is different. Each business has its own brand of products and services, a unique culture, and its own pricing and quality practices….just to name a few differences.

Financial Requirements

This document puts your basic ideas into a financial format for the lender to get a feel for the type and size of your request and also to assess the bank's exposure.

Let us assume that you need financing to start a small business that will manufacture wooden furniture. The business intends to purchase land and building, a vehicle, production equipment and raw materials to get started. This information presented in a simple format will show the source of funds and how the funds will be applied (spent).

Financial Requirements		**Proposed Financing**	
Purchase land and building	$150,000	Bank loan	$170,000
" vehicle	20,000	Overdraft	30,000
" equipment	50,000	Owner's investment	50,000
" raw materials	20,000		
Start-up Expenses	10,000		
TOTAL	**$250,000**	**TOTAL**	**$250,000**

This table shows the cost of the items needed to start the business and how the cost would be split between you and the bank. You will be required to provide more detailed information on the items that you have listed.

Land and Building
Describe the location, size, and type of construction, the age and reason for choosing this location.

Vehicle
State the age, make, specification and reason for this selection.

Equipment
State the age, make, specification and reason for each selection.

Raw materials
State the quantity and source of the intended purchases. Why do you need a certain level?

Start-up expense
These are items such as legal fees and mortgage fees, insurance, utilities deposits, first month's salaries and all one-time or prepaid expenses.

Bank loan and Overdraft
Propose the term of the loan and the anticipated interest rate on both of these debts.

Owner's investment
What is the source of your investment? Be specific, be able to show proof that you have access to cash or will be able to convert an asset to cash. Investment could be in the form

of assets. For example, you may be able to put a vehicle or equipment into the business. Money that you borrow privately, cannot be considered as your investment as it has to be repaid.

Preparing a Forecast

All of us make decisions based on our prediction of the future. We do this based on assumptions, our personal experience, our interpretation of information and society at large. We do this to set objectives and long-term goals for our lives.

When this exercise is done for a business, a Financial Forecast is the result. For someone to understand your forecast, they will need to know what assumptions you have made. These assumptions and any other information that you have utilized must be part of the forecast document. Your assumptions must be clear, justifiable and easy to modify. The Banker may see things differently and would want to modify your estimates. Everyone will know exactly what is behind your forecast and will be able to make changes if your assumptions or basic information require adjustments. For example, the bank may have a different opinion on the number of customers you have forecasted or the sale price of your products. Keep it simple. The loans analyst will be required to reformat this information to conform to the bank's internal reporting style.

The Forecast is one of the most important exercises that you will perform. You need to spend a great deal of your time researching and preparing this document. It is worth the time and the effort. The results will tell you if your business will provide enough profit to satisfy your livelihood. It must also show the lender that you will be able to repay the loan.

A ***forecast is the profit and loss statement of the future*** i.e., the next 12 months. It contains three main sections which are as follows:

- Sales
- Expenses
- Profit

Sales estimates will have assumptions about the need and demand for your product or service. How much is the consumer prepared to pay? Information on your competition must include comparisons with your business. If you have considered advances in technology or any other factors in your prediction show your reasoning. Be prepared for eventualities, it is better to be very conservative in the prediction of sales.

Expenses are the costs incurred by a business during the normal course of its operation. Forecasted expenses are the anticipated cost of doing business at the volume you have predicted in your sales estimates. This will include the Cost of Goods Sold, Selling, General and Administration expenses. Do not forget Financial Expenses and Taxes.
Be prepared for the unforeseen. Be liberal in your assessment of expenses.

Profit is what remains when all the expenses have been paid from the receipt of the sales for a specified period.

Here is an example of a financial forecast:

FORECAST
For 12-month period ending Dec 31st xxxx

Sales		$1,000,000
Cost of goods sold	$400,000	
Gross profit		600,000
Expenses		
Selling expenses	100,000	
General expenses	150,000	
Administrative expenses	250,000	
Financial expenses	40,000	
Total expenses	540,000	
Profit before taxes		$60,000

Selling, General and Administrative expenses are categories of expenses that combine all expenses associated with a business. You will need to provide a list of all expenses. The following is a list of some common expenses

Cost of Goods Sold
- Raw material costs
- Labour
- Overhead

Selling General and Administrative Expenses
- Advertising
- Depreciation
- Entertainment
- Insurance
- Interest and Bank charges
- Office supplies
- Postage
- Professional fees
- Rental expenses
- Repairs
- Salaries
- Travel
- Telephone
- Utilities

Budget

The amount that you have allocated to each expense category will become one of your most important management tools. These figures will become the basis for your budgets.

Cash Flow

During the course of its operation, cash flows through a business in a cycle. Cash flows into and out of a business like water flowing in and out of a tank. If the flow is not managed properly the tank can run dry. Cash in the bank and in the business is used to purchase inventory, pay salaries, all expenses and produce sales. When the finished products are sold and the cash collected, the cycle restarts.

The amount of cash flowing through on a monthly basis is referred to as the cash flow. As the selling and production cycles overlap, a shortage of cash may occur. These shortfalls are known as "the cash flow requirements". This is one of the most important issues for the survival of a business. A business can be rich in assets, but if there is insufficient cash to meet daily or monthly bills it can soon be out of business. Similarly, a business can be profitable but does not have enough cash to pay bills on a day-to-day basis.

Preparing a cash flow statement is a complex exercise and requires experience. Most banks prepare a cash flow statement based on the information you supply. This exercise shows the need for and decides the size of the overdraft that is required.

Management's Ability

The bank will need to know that you have the technical and management skills to make your business a success. Be prepared to provide information to show that you have what is needed. State your age and any special qualifications that you have. Describe your practical experience and show how it will be useful to the business.

Let us assume that you are opening your own motor repair shop. Tell the bank that you have "a mechanics certificate from GTI and 10 years experience as a mechanic at Guysuco, followed by five years as a supervisor at the Demerara Motor repair shop. During this time I was responsible for estimates, purchasing raw materials and the supervision of four employees in the engine and transmission department". You may add that your spouse is a bookkeeper at John's Hardware Store and that she will be assisting with your book keeping.

Is there any personal information or issues in your past, which the bank must be aware of? Do you have current debts or a borrowing record with another organization?
The business will have to provide for your personal needs. What are your personal financial needs?

The lender will be interested in your personal affairs such as your previous employment, income, debts and your personal net worth. This information is provided in a Statement of Personal Affairs. A sample is in the Appendices.

Documents And Fine Print

Most borrowers are excited by the approval of their loan application and cannot wait to sign documents and receive the funds. The bank will require signatures on a number of documents. Before you sign these take the time to understand their content. If in doubt seek advice from a private source. It is advisable that you obtain independent legal advice.

The following is a list of some of the more common documents. A full explanation of each is in the glossary.

- Promissory Note.
- Loan Agreement (Offer of Credit).
- Guarantee.
- Mortgage.
- Bill of sale.
- Assignment of insurance.

Choosing a Bank

Think of your bank as a supplier of a product or service to your business. Find a bank with a banker who has a reputation for working with businesses similar to yours. Imagine that you are seeking medical or legal services. You would attempt to find a person who has experience in dealing with your case. You would look at the track record of the doctor or lawyer.

Banks usually have a preference for certain industries or types of business. While one may favour the manufacturing sector another may excel in agricultural loans. Some may assume a developmental role for small and micro-businesses. The key is to learn about the financial institutions and decide what is best for your needs. If you are a very small start-up business with minimum assets and require a low level of financing you should consider one of the Micro-credit organizations.

Your choice must also consider factors such as the size of the bank, its location and the authority of the lender. There are advantages and disadvantages for each. A local branch will be familiar with your business and it is easily accessible. However the manager's authority may be very limited. Match your business needs with your banker's authority. A major disparity in size can lead to misunderstandings and poor relationship. If you require access to foreign trade and safe depository services a small rural branch may be unable to serve you.

Interest Rates and Fees

The banks main source of revenue is interest received on loans. Interest paid on deposits is the major cost of doing business.

The difference between the lending and the deposit rates is known as the interest rate spread. As at August 2003, the Statistical Abstracts published by the Research Department of the Bank of Guyana shows, the average deposit rates paid by banks was in the 2.98-3.73 % range. The average prime lending rate was 14.88 %. Prime lending rate is the base for calculating general lending rates. Actual customer borrowing rates quoted by the banks were in the 17.0- 19.5 % range. This spread pays all the operating expenses and costs for running the bank. It also generates the profits for the shareholders.

Interest Rates

The level of the interest rate depends on the level of risk to the bank. The higher the risk the higher is the rate. Rates are generally floating or fixed. Rates are negotiable and are based on the bank's Prime rate. This is the rate at which a bank lends to its no-risk (prime) customers. It is based on the total cost of the funds to the bank.

- **Floating Rates**
  The floating rate is set at 1-3% above the bank's prime rate. It varies with the prime rate. Most short-term loans and overdrafts have floating rates.

- **Fixed Rates**
  Most long-term loans have a fixed rate with a fixed monthly repayment.
  The rate is set for the life of the loan. In some instances it may be renewable after a 5-year period.

The lending rate varies with the bank's assessment of each loan. You may be able to negotiate a better rate if your business will provide other sources of income to the bank. This may be foreign currency exchange if you are an exporter/importer.

Fees

It is common practice for the banks to charge fees for providing most services to customers. Fees are charged for various specific services such as, safe depository, ATM, chequing account operation and the issuing of drafts and payments.

Fees related to borrowing may be charged prior to the approval of the credit, during the approval process and annually thereafter. Ensure that these are discussed thoroughly with your interviewer. The following is a list of some of the more common fees associated with borrowing:

- Application Fee - this is a fee for the application.

- Processing Fee - the cost of conducting the investigation and analysis of your proposal.

- Inspection fee - the cost of inspecting and evaluating the collateral offered as security.

- Appraisal fee - for the professional evaluation of collateral.

- Legal Fees - paid to the bank's lawyer for preparation of security documents.

- Mortgage Fee - a percentage of the loan value paid to the bank's lawyer for preparation of a mortgage.

- Registration Fees - the cost of registering the security documents with the relevant authorities.

- Insurance Fees - a blanket life insurance plan for all borrowers.

- Commitment Fee- a fee for keeping the approved funds available for a period.

- Annual Renewal Fee - for the continuation of an overdraft.

Lending Limits

Banks have established upper and lower lending limits. While the upper limit is based on the strength of the bank, the lower is an amount fixed by the management of the institution.

The bank sets the lower limit based on the cost of doing business and the location of the branch. This amount varies by institution. The minimum amount is decided by the initial cost of processing a loan and the month-to-month cost of keeping it on the books. The bank through its in-house lawyer sometimes absorbs the cost of legal fees on smaller loans. Remember the monthly cost of servicing a loan is the same regardless of its size, and adequate compensation is expected for the time and effort spent on each transaction.

Many banks are reluctant to process loans lower than $100,000.00. Some banks have established special lending programs for micro-businesses as an opportunity to harvest businesses as they grow. However, the amount that any bank will authorize depends on factors described under Lending Criteria. The business' ability to repay, your investment and the collateral offered decide each borrower's limit.

APPENDICES

STATEMENT OF PERSONAL AFFAIRS

Name			Date of birth
Spouse's Name			Date of birth
Address			
			Tel
Employer			Tel
			Salary
Spouse's Employer			Tel
			Salary

PERSONAL FINANCIAL STATEMENT

ASSETS	Amount	LIABILITIES	Amount
Cash (Home & Bank)		Bank Loans (Balance Owing)	
Life Insurance (Cash Value)		Mortgages (Balance Owing)	
Real Estate (Present Value)		Other Liabilities	
Automobile			
Stocks, Shares, Bonds			
Household, Personal Effects		Total liabilities (B) Sub-total	
Other Assets		Net Worth (A-B)	
TOTAL (A)		TOTAL	

Cash: total of all cash held at home and in the Bank.
Life Insurance: the present cash value of the policy.
Real Estate: the fair present day sale price.
Automobile: state the Make, age and present sale value.
Stock, Shares: the present sale price of any shares or stocks.

Bank Loans: state balance, purpose, security and monthly installments.
Mortgages: initial and present balance, purpose and installments.
Other Liabilities: all debts e.g., hire purchase payments.
Net Worth: the difference between total asset and total liabilities.

Additional Information
Provide additional information that you feel may be applicable. Do you have any debts to collect or other sources of income? What about personal loans or guarantees that you have given?

Who should complete this form?
If appropriate both spouses are required to provide this information, especially if the real estate is the matrimonial residence. Provide reason(s) if one spouse is omitted.

LIST OF MACHINERY, EQUIPMENT & VEHICLES

Name: ______________________

Date: ______________________

Description (Manufacturer's name, capacity, etc)	Model #	Serial #	Age	Purchase price	Present value	Outstanding loan

GLOSSARY

This list contains the definitions of some of the topics that may arise during your discussion with a lender.

Assets
This is defined as any physical property, object or rights, which are owned and have a money value.

Assignment Of Insurance
Assets pledged as security to the bank will require insurance coverage. The policy will be assigned to the bank. This offers you protection in the event of a loss, as the proceeds of the policy will be used to repay your indebtedness. In some instances life insurance coverage, on you and all co-borrowers, may be required for the same reason.

Balance Sheet
This statement is like a photograph of the business at a specific time. The photograph contains a listing of and the value of all assets owned and all liabilities owed at a specific time, which is usually the business' year-end. It also shows the net worth of the owner(s).

Bill Of Sale
The most common form of lien on vehicles is the Bill of Sale. The Bill of Sale is advertised and registered. However, it empowers the lender to seize the asset anywhere and to dispose of it at anytime.

Business Plan
Your business plan contains your view of the future. Even if it is in your memory or "in a little black book", this plan covers sales, markets, competition and budgets. It may contain your thoughts, assumptions and perceptions.

For the plan to be prepared for a business loan, you may need to refocus your ideas to make them presentable to a lender. The main focus should be details on financing, profits and your ability to make monthly payments

Collateral
Collateral is the tangible asset or property that is lodged by a borrower as security for a loan.

Chattel Mortgage
A chattel mortgage registers a lien against personal moveable property, which are called chattels. It provides security to the bank on moveable assets such as vehicles, equipment, and furniture and in some instances buildings or structures.

Cost of Goods Sold
This is the total of all costs associated with sales such as raw materials and labour. In manufacturing, it is the total of all costs for acquiring and converting raw materials into a finished product.

Depreciation
This is an expense that provides for the decline in value of an asset caused by normal usage and aging. It is loosely referred to as "wear and tear" costs. A business is allowed to allocate, as an expense each year, part of the cost of an asset. The annual allowance depends on the life span of the asset.

Discount
The purchase of a Bill on discount, is to buy it for a reduced price by paying cash for it now.

Equity
This is the net worth of a company, or the excess of assets over liabilities. It provides information on the amount invested by the shareholders and accumulated profits.

Forecast
A statement prepared by the owner, which predicts the future performance of a business over the next 12 months. It is the Profit and Loss statement of the future.

Goodwill
The value that is placed by the owner, on the reputation of a business and the relationship that it has developed with its customers, suppliers and the authorities.

Guarantee
A guarantee is a written agreement to be responsible for the payment of the debt of another person who is a borrower. When the business is a limited company, the owner will be required to guarantee all or a portion of the company's debt. When residential property is used as collateral for a loan and one spouse is the borrower, the other may be required to guarantee the loan, even though the property is registered to one person only. This allows for easy settlement of the debt, if the property becomes an issue in a divorce settlement.

In the event of a shortfall by the borrower, the guarantor will be responsible for repayment. The bank will also have access to the assets of the guarantor upon default.

Liabilities
A liability is a debt or obligation owing by a person or business. The liabilities on a balance sheet will contain a listing of all debts and the net worth of the business.

Loan Agreement
The loan agreement supplements the promissory note.

It contains the conditions under which a loan will be made available, the purpose for which it is to be used and how it is to be repaid. Designed to protect the lender, it establishes limits in some areas. Some conditions will establish agreement on issues such as limiting the creation of further debt, the disposal of assets, the protection of the environment and other relevant issues. This is the area in which negotiations are possible.

Mortgages
A mortgage is a legal document that pledges a borrower's asset to a lender by creating a charge or lien against the asset. This lien can be created against real estate and is known as a "real mortgage" or is generally referred to as a mortgage. A charge against moveable assets such as a vehicle or equipment is a chattel mortgage.

A real estate mortgage is advertised in the Official Gazette for the public's knowledge and then recorded in the Deeds Registry. Many mortgages may be recorded on the same asset, with each being assigned a number showing its ranking. Some properties are known to have a first to a fifth mortgage. When used to secure a loan, a mortgage includes the principal amount, the rate of interest, and in some instances restrictions and conditions that normally form part of the loan agreement.

It is the understanding that the assets will be released on repayment of the debt by a certain time. The mortgage does not transfer ownership to the lender nor does it allow the transfer or sale of the asset to anyone. The lender has to secure the court's authority to enforce any recovery of its debt or to dispose of the asset.

Net Worth
The difference between total assets and total liability is the owner's net worth. If the value of your home and all other assets is $150 and your mortgage and loan balances together are $90, then your net worth is $150 - $90= $60.

Overdraft
An overdraft is a fluctuating credit on a chequing account. A borrower is allowed to write cheques up to a pre-approved limit. Interest is calculated on the daily balance.

Prepaid Expenses
The payment for something to be received in the future. Examples are the portions of a lease or insurance policy that have been paid in advance.

Profit and Loss Statement
This statement shows the Revenues or Sales with all Expenses for a specific period of time. The profit or loss for the period is also shown. Profit and Loss statements are prepared annually, quarterly or monthly.

Pro Forma Statement
A Pro Forma statement is one that is prepared in advance. A pro forma balance sheet contains an estimate of the assets and liabilities of the business on the proposed start up date. The pro forma income statement is known as the Forecast.

Promissory Note
Commonly referred to as the Pro-note. The promissory note is an unconditional written promise to pay a given amount with interest, to the bank. A Loan Agreement usually accompanies this document. The Pro-note is the IOU of business financing. It is the single most important document that you will sign. It establishes the debt and your promise to repay with an agreed interest rate. Terms and clauses are fixed by the bank and are not negotiable. These allow the bank to proceed against you legally when it needs to recover all unpaid balances. Most Pro-notes are "on demand" documents and are sometimes referred to as "demand notes". The bank can demand the full repayment of the loan at any time regardless of the status of your payments.

Receivables
Sales that are made on credit to customers are recorded as receivables. Depending on the business, terms are generally in the 30-days range.

Refinancing
The repayment of a loan or debt, by the same lender, from the proceeds of a new loan.

Regulators
This is the Central Bank, whose Bank Supervision Department is responsible for supervising the country's licensed financial institutions.

Security
This is generally a number of official documents that pledge assets to the lender as assurance for a loan. Mortgages, promissory notes and loan agreements are examples.