



Financing 101 for Small Business Owners

by Tom Ethen, Stearns Bank Director of SBA Lending



It doesn't matter if you've been a small business owner for decades – or just beginning the process of buying or starting a new business. Looking for business financing can feel like a daunting task.

Anyone going through the loan application process for business financing likely has questions running through their head.

As small business owners gain experience in financing, knowledge becomes power. Your experience and knowledge give you the ability to make informed choices about your business loan.

Here are some key things small business owners should be aware of.

1. Equity

Equity plays a very important role in the success of a small business. For existing businesses, the equity that is needed might already exist on the business' balance sheet.

If the business is properly capitalized, it is in a position to sustain various fluctuations in revenue and other market conditions. Well-capitalized business often times do not need to raise additional equity in order to complete equipment purchases, business expansions or debt refinances.

For start-up businesses, an appropriate equity injection provides for much more than checking a box with your lender. The equity injection reduces the amount of leverage on the business and also reduces the amount of the interest expense and debt service. New businesses, especially, need to be careful to be sure they are not over-leveraged.

2. Cash Flow

Cash flow is the amount of cash, either projected or historical, that a business produces in a given period.

The SBA Program is known as a "cash-flow lender," meaning cash flow takes a priority over things like collateral, net incomes and/or balance sheet ratios. These other credit components are still a factor, but not nearly as important as the business' ability to generate the cash needed to service the proposed debt and provide the salary the owner needs.



3. No Balloon Payments

There are no balloon payments or other early maturity dates associated with small business loans. As a result, with an SBA loan, you are assured to have a fully amortizing loan without the pressure of a balloon payment.

The SBA knows that balloon payments are not good for small businesses, especially newer businesses. It is much more favorable to know that you have a level payment over the entire term of the loan, without the pressures that come with a balloon payment.

Balloon payments require you to either come up with an abnormally large amount of funds at one time to satisfy the balloon payment, or it requires the small business to "requalify" for a loan they already have.

Small businesses also need to pay extensive fees to renew or extend a balloon payment -- such as origination fees, extension fees, searches, recording fees, appraisals and other reports. An SBA loan is truly permanent financing, with absolutely no balloon payments to cause a hardship on your business.

4. Loan Terms

The SBA loan program provides loan terms that are usually much longer than others. In most cases, SBA loans can be set up to fully amortize over a period of 10 years. For loans that include real estate, those terms can be extended as long as 25 years.

These terms are double what you can typically find with other types of loans. So what does that mean to you?

This means that the small business can make the lowest possible payment, thus freeing up cash flow for other important activities such as marketing, advertising and employee development. In addition to having the ability to make the lowest payment possible, there also isn't a prepayment penalty on most SBA loans, which means that you can pay more each month, if you wish, reducing debt at a faster rate and saving on interest expense without paying any sort of prepayment penalty to do so.

5. Bookkeeping

As a small business owner, recognizing the importance of bookkeeping should start right away. Whether you have the ability and skills to generate your financial statements yourself internally or if you need to employ outside bookkeeping and accounting services, it is critical that every small business keeps and maintains accurate, meaningful financial statements.

New businesses typically start with less sophisticated accounting systems/process, but over time, look for opportunities to enhance your financial statement management. There are many automated systems available today to do this.

Having reliable financial statements enables the small business to make decisions based on facts, rather than using "guess work." Creating financial statements over time also allows the small business owner to complete valuable trend analysis.

What is happening to your revenue, cost of goods sold, gross profit, operating expenses, net income and, ultimately, cash flow? By analyzing trends, you can react much quicker to changes in your business.

6. Finding The Right Bank

Remember, knowledge is power. Stay informed and be mindful of these items to take your small business to the next level with confidence.

If you are considering buying a business, starting a business or expanding your current business, you will want to connect with a qualified small business bank early in the process. It is essential to choose a bank that is experienced in SBA financing and one that takes a proactive and creative approach in business finance.

Make sure the bank you are working with not only has an innovative approach to loan origination, but also one with a culture of strong customer service.



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Tom started his career in banking in 1991 and has been a top-performing lender with Stearns Bank for more than 20 years. Throughout his career at Stearns Bank, Tom has been a mentor, helping others achieve success. He leads the SBA lending team at Stearns Bank, providing ongoing training and coaching. Tom and his team work with customers to learn about their specific needs and then structure transactions to maximize the benefits of the SBA loan program for business owners. He enjoys working with customers to learn about their specific needs. Having a deep understanding of his customers has allowed Tom to build long-standing relationships – connections that don't end on closing day.

If you're interested in learning more, contact him at

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