



INTRODUCTION TO COMMERCIAL LENDING

Brad Stevens

Stevens Risk Management



*Making Banking Better
Making Bankers Better*



COMMERCIAL LOAN



INTRODUCTION

Brad Stevens

BA, Degree Economics, MBA, Finance

30 Plus Years in Banking

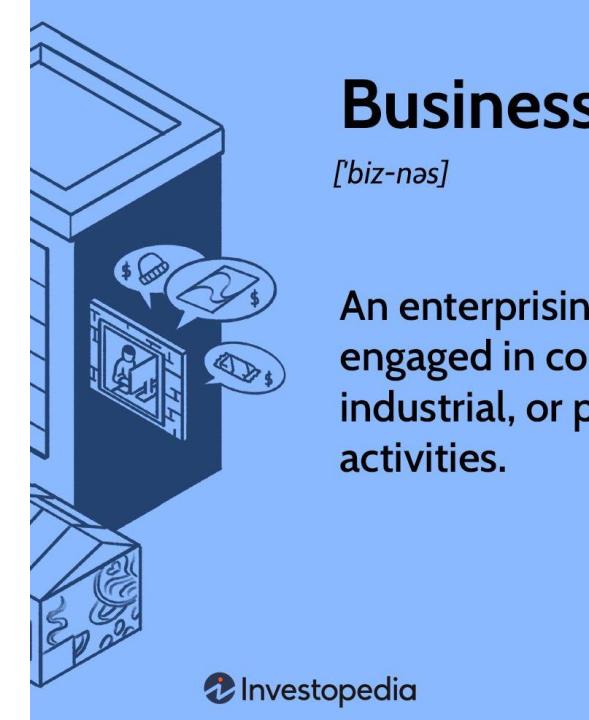
Managed over \$40 Million in Commercial C & I and
Commercial Real Estate Accounts

Senior Credit Officer of Two Troubled Banks

Nationwide Trainer and Bank Consultant

AGENDA

- Understanding Credit Risk
- Types of Borrowers
- Solving Your Clients Problem
- Analysis and Process
- Need for Structure
- After Closing



CORE CONCEPTS TO KEEP IN MIND

Yesterday's Loans Are Repaid With Today's Cash Flow

Today's Loans Are Repaid With Tomorrow's Cash Flow, Is There Enough?

Every Loan Request Is The Result of A Cash Shortfall



ending of the commercial

CORE CONCEPTS TO KEEP IN MIND

Business Loans Are Made to Business Entities For Business Purposes

No Good Deal Ever Comes Through The Front Door

Always-Match the Loan Repayment With the Self Liquidating Asset That Supports the Loan

You Are Not Paid to Make Loans, You are Paid to Manage Credit Risk!



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MANAGING CREDIT RISK

$$P \times C = \text{Credit Risk}$$

Probability of An Event Occurring Or Not Occurring As Expected

Inquisitive Underwriting is Required

Types of Credit Risk



MANAGING CREDIT RISK

$$P \times C = \text{Credit Risk}$$

The Consequences to the Client and The Bank If The Events Do Not Occur as Planned Are Mitigated By Proper Structure

Documentation
Pricing
Collateral
Covenants

Types of Credit Risk



ESSENTIAL CONCERNS

Essential Concerns in All Lending;

Assess the Needs of Our Borrower

Review the Financial Condition of the Borrower

Structure the Loan Properly

Close Effectively

Monitor Profusely



COMMERCIAL LENDING PROCESS

Request- Caused by A Cash Shortfall

Analysis- What Information, Why The Shortfall, Financeable?

Structure- Solving The Clients Problem

Monitoring- What To Look For After The Close



ANALYSIS

Marketplace Factors Impacting the Borrower

Plus

Managements Response to the Marketplace Factors

Equals

The Financial Statements



*M*ARKETPLACE *I*MPACTS

Local Economy

National Economy

Labor Requirements

Supply Chain

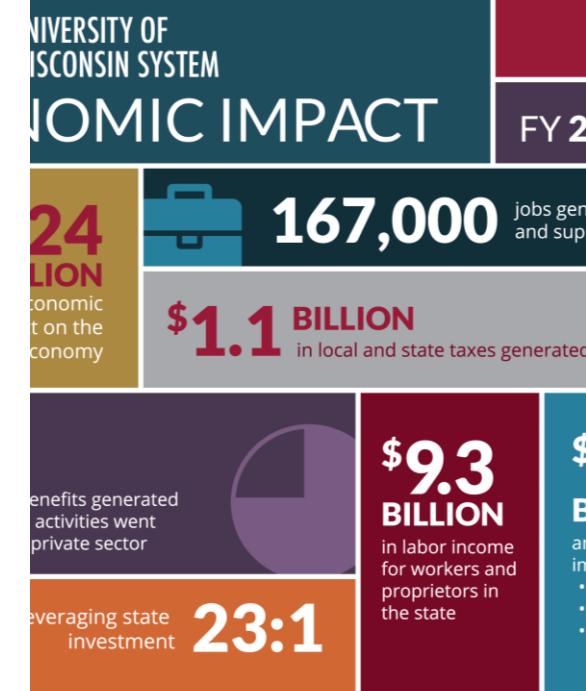
Regulations

Transportation

Economic Geography

Technology

Competition



MARKETPLACE IMPACTS

Type Of Industry;

Manufacturing

Wholesale/Distribution

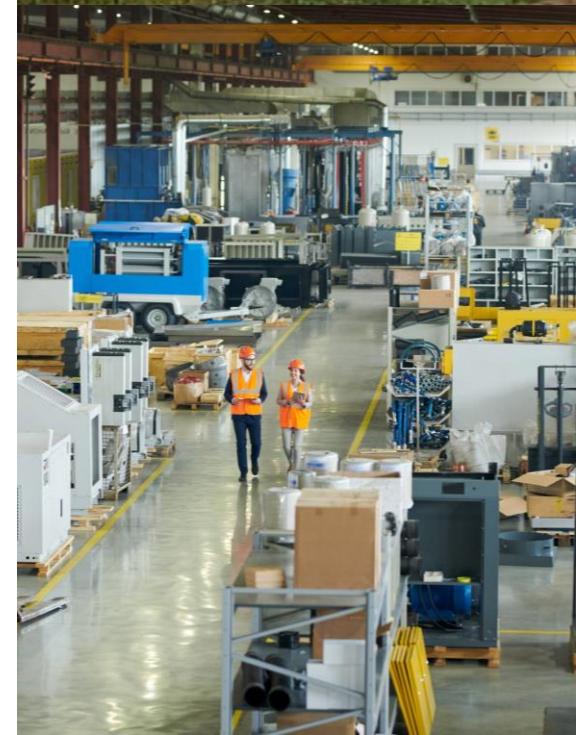
Service Sector

Retail

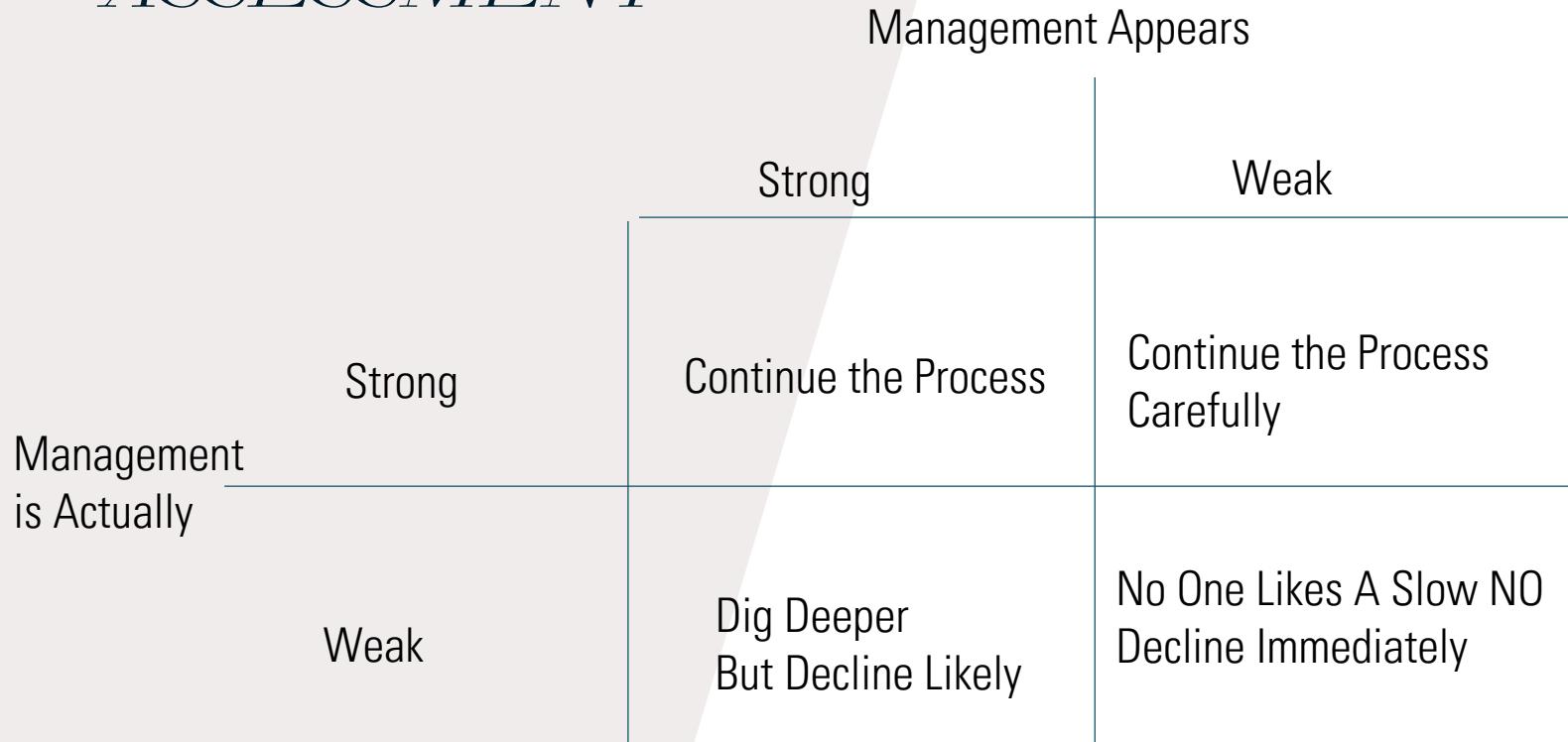
Hospitality/Food Service

Real Estate

Agriculture



MANAGEMENT ASSESSMENT



Organizing



Coordinating



MANAGEMENT ASSESSMENT

Core Abilities, Strengths and Weaknesses;

Breadth and Depth

Processes

Margin Control

Life Stage

Sales Management

Finance Acumen

Culture

agement Proces



Organizing



Coordinating



FINANCIAL ANALYSIS

BALANCE SHEET;

Details the Resources and Funding of the Firm

Assets or Resources

Liquid

- Cash
- Accounts Receivable
- Inventory

Long Term

- Equipment
- Intangibles

SAMPLE BALANCE SHEET

TS		LIABILITIES & EQUITY	
Assets		Liabilities	
Bank Account	5,000	Current Liabilities	
Checkings Account	1,000	Accounts Payable	
Cash	500	Line of Credit	
Inventory	22,000	Payroll Liabilities	
Intangibles	15,000		
Land Insurance	6,000		
Current Assets:	49,500	Total Current Liabilities:	35,500
Noncurrent Assets		Noncurrent Liabilities	
Accumulated Depreciation	-4,500	Long-term Debt (loan)	
Computer	7,000		
Furniture	65,000		
Land	60,000		
Noncurrent Assets:	127,000	Total Liabilities:	127,000
Total Assets:		Equity	
	177,000	Owner's Capital	
		Retained Earnings	
		Total Equity:	91,500
		Total Liabilities & Equity:	177,000

ce Sheet?

It is a financial statement that shows a company's assets, liabilities, and equity.



FINANCIAL ANALYSIS

BALANCE SHEET;

Details the Resources and Funding of the Firm

Liabilities or Funding Sources

Liquid

Accounts Payable

Line of Credit

Accruals

Long Term

Term Debt

Shareholder Debt

SAMPLE BALANCE SHEET

TS	LIABILITIES & EQUITY
Assets	
Bank Account	5,000
Checkings Account	1,000
Cash	500
Debts Receivable	22,000
Inventory	15,000
Health Insurance	6,000
Current Assets:	49,500
Invest Assets	
Accumulated Depreciation	-4,500
Computer	7,000
Equipment	65,000
Noncurrent Assets:	60,000
Total Assets:	127,000
Liabilities	
Current Liabilities	
Accounts Payable	
Line of Credit	
Payroll Liabilities	
Total Current Liabilities:	35,000
Noncurrent Liabilities	
Long-term Debt (loan)	
Total Liabilities:	35,000
Equity	
Owner's Capital	
Retained Earnings	
Total Equity:	92,000
Total Liabilities & Equity:	127,000

ce Sheet?

It is a financial statement that shows a company's assets, liabilities, and owner's equity.



FINANCIAL ANALYSIS

BALANCE SHEET;

Details the Resources and Funding of the Firm

Equity or Owner Funding Sources

Paid In Capital

Retained Earnings

SAMPLE BALANCE SHEET

TS		LIABILITIES & EQUITY	
Assets		Liabilities	
Bank Account	5,000	Current Liabilities	
Bankings Account	1,000	Accounts Payable	
Cash	500	Line of Credit	
Debts Receivable	22,000	Payroll Liabilities	
Inventory	15,000		
Bad Insurance	6,000		
Current Assets:	49,500	Total Current Liabilities:	38,500
Invest Assets		Noncurrent Liabilities	
Accumulated Depreciation	-4,500	Long-term Debt (loan)	
Computer	7,000		
Building	65,000		
	60,000		
Noncurrent Assets:	127,000	Total Liabilities:	127,000
Assets:		Equity	
		Owner's Capital	
		Retained Earnings	
		Total Equity:	50,000
		Total Liabilities & Equity:	177,000

ce Sheet?

It is a financial statement that shows a firm's assets, liabilities, and owner equity.



SOURCES AND USES OF CASH

Uses of Cash:

Increases of Assets/Resources

Repayment of Debt

Dividends

Losses



SOURCES AND USES OF CASH

Sources of Cash:

Decreases of Assets/Resources

New Debt

Paid In Capital

Net Income



FINANCIAL ANALYSIS

Income Statement;

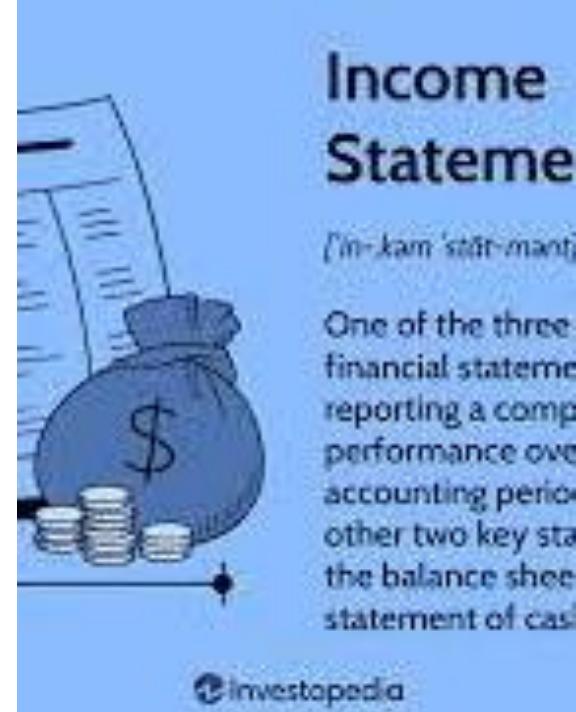
Sources of Revenue

Cost of Goods Sold To Create the Revenue

Gross Profit/Gross Profit Margin

Operating Expenses

Net Income/Net Loss



Income Statement

(in-kam 'stat-mənt)

One of the three financial statements reporting a company's performance over an accounting period. The other two key statements are the balance sheet and the statement of cash flows.

© Investopedia

Example Corporation Income Statement

Year ended December 31, 2023

Revenues

Expenses

Income

revenues, expenses, gains, losses

more income tax expense

Expense

See notes to the financial statements

FINANCIAL ANALYSIS

Key Ratios;

Current Ratio

Leverage Ratio

Gross Profit Margin

Cash Flow Coverage



Financial Analysis

[fə-'nan(t)-shəl ə-'nāl-ə-səs]

The process of examining the financial statements of a business, project, or other organization to evaluate their performance and suitability.

FINANCIAL ANALYSIS

Activity Ratios;

Accounts Receivable Days on Hand

Inventory Days on Hand

Accounts Payable Days on Hand



Financial A

[fə-'nan(t)-shəl ə-'nal-

The process of e
businesses, proj
and other finan
transactions to e
their performance
suitability.

CORE CASH DRIVERS

Sales Growth

Gross Profit Margin

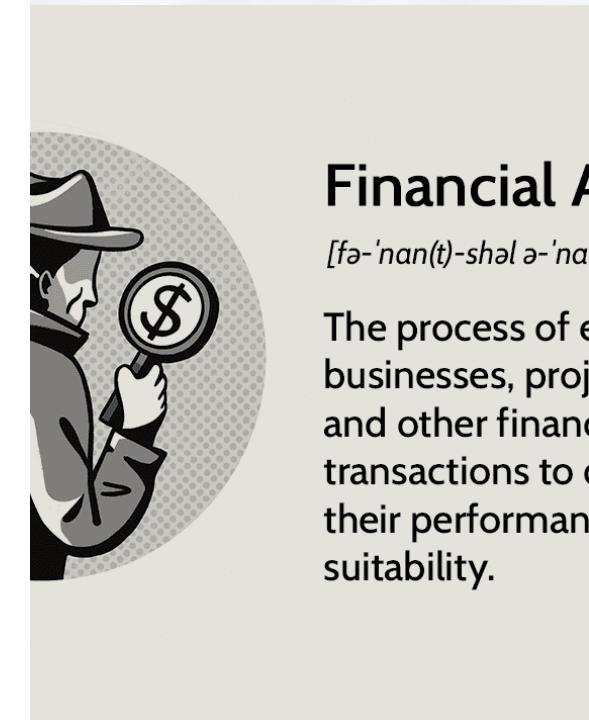
Operating Expense Margin

Accounts Receivable Days on Hand

Inventory Days on Hand

Accounts Payable Days on Hand

Fixed Assets Need



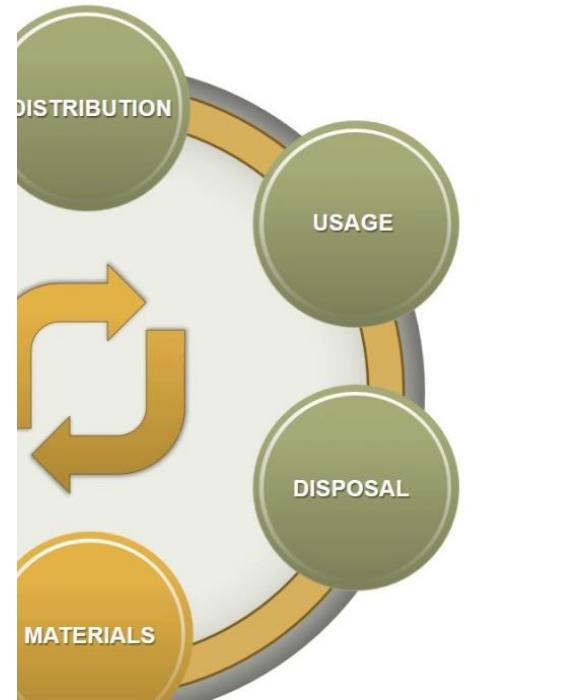
COMMERCIAL LENDING PROCESS

Request- Caused by A Cash Shortfall

Analysis- What Information, Why The Shortfall, Financeable?

Structure- Solving The Clients Problem

Monitoring- What To Look For After The Close



STRUCTURE CONSIDERATIONS

Managing Credit Risk is Primary

What Repayment Resources Does the Borrower Have?

What is The Self Liquidating Asset that Will Repay the Debt?

What Could Impair The Ability of Repayment?

What Guardrails Do I Need To have To Limit The Consequences of Impairment?

What is The Acceptable Repayment Term and Affordable Payment Amount



STRUCTURE CONSIDERATIONS

Types of Loans;

Lines of Credit

Term Loans

Balloon Loans

Interim/Bridge Loans

Long Term Working Capital Loans

Common Lending Options



Line of Credit

Cover planned or unexpected capital needs this year, in ten years or even twenty years.



Term Loan

Tailor a fixed-term loan to fit your exact needs before a high-cost purchase or renovation.



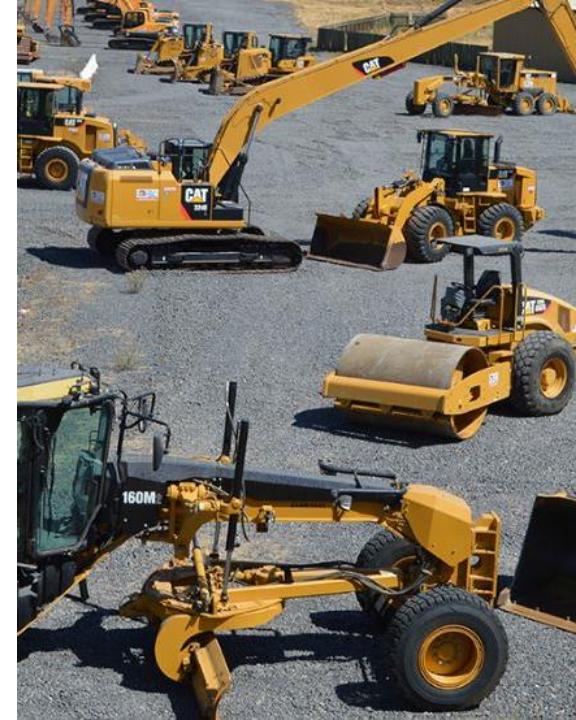
STRUCTURE CONSIDERATIONS

Documentation- The Right Documentation for the Right Loan

Pricing- The Right Return for The Risk

Collateral- The Alternative In Case of Default

Covenants- The Right Boundaries



STRUCTURE CONSIDERATIONS

Setting Financial Covenants;

Loan Type Specific

Providing a Road Map, Not a Hurdle

Targeted to The Key Risks You Want to Control

Two Will Do

Debt Covenants



Examples



STRUCTURE CONSIDERATIONS

Setting Control Covenants;

Management Concerns

Ownership Concerns

Collateral Concerns

Cash Flow Concerns

Reporting Concerns



Examples



POST APPROVAL, PRE CLOSING

Commitment Letters/Term Sheets

Negotiations, Best Alternative to A Negotiated Deal

Collect the Fees and Expenses

Preview of the Closing Documentation



CLOSING

Make it A Non-Event

No Surprises

They Are Busy-You Are Busy, Non-Real Estate Closings, 5 Minutes

Real Estate, Let a Qualified Title Company Handle It

Multiple Payee Disbursements



MONITORING/RELATIONSHIP ENHANCEMENT

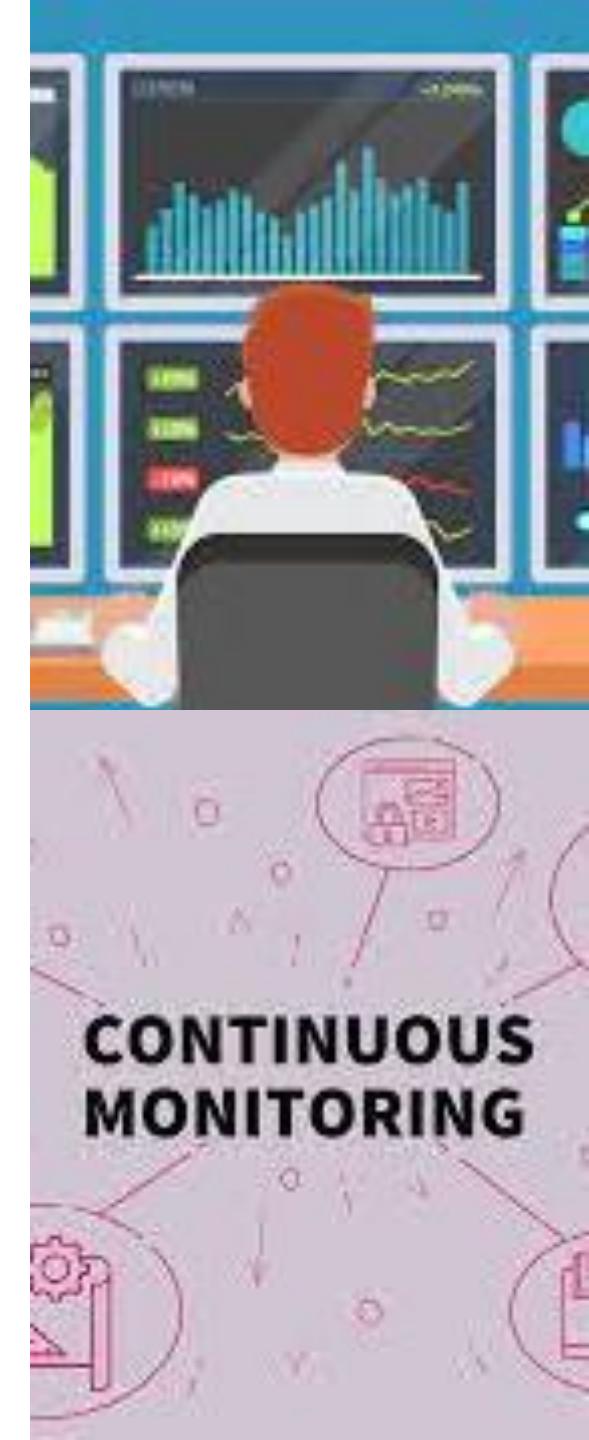
Tickler and Exception Reports

Financial Report Analysis

Looking for The Next Opportunity
Catching Early Warning Signs

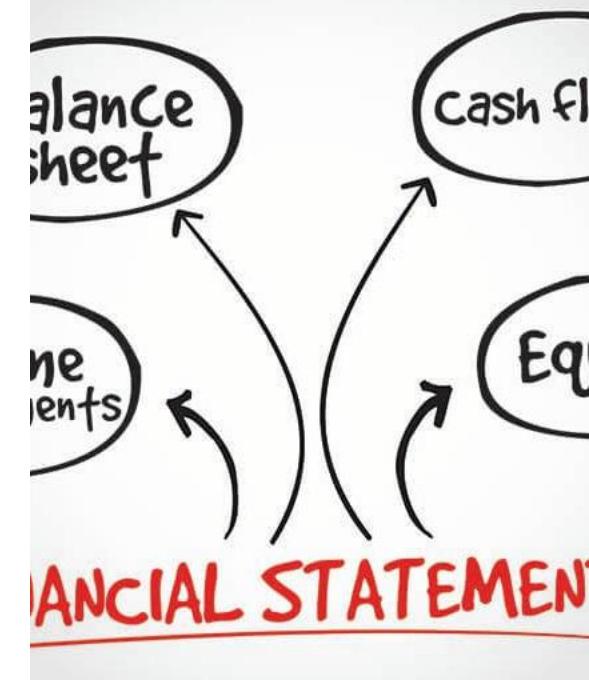
A, B and C Clients, Managing Your Portfolio

Mining Your Portfolio

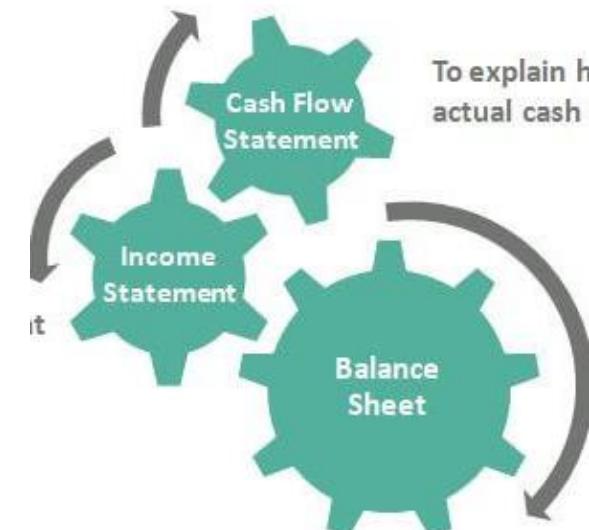


RECAP

- Develop a Efficient Process
- Credit Risk Management
- Understanding the Request
- Effective Analysis To Address The Key Risks
- Structure Properly
- Close Effectively
- Manage the Relationships Profitably

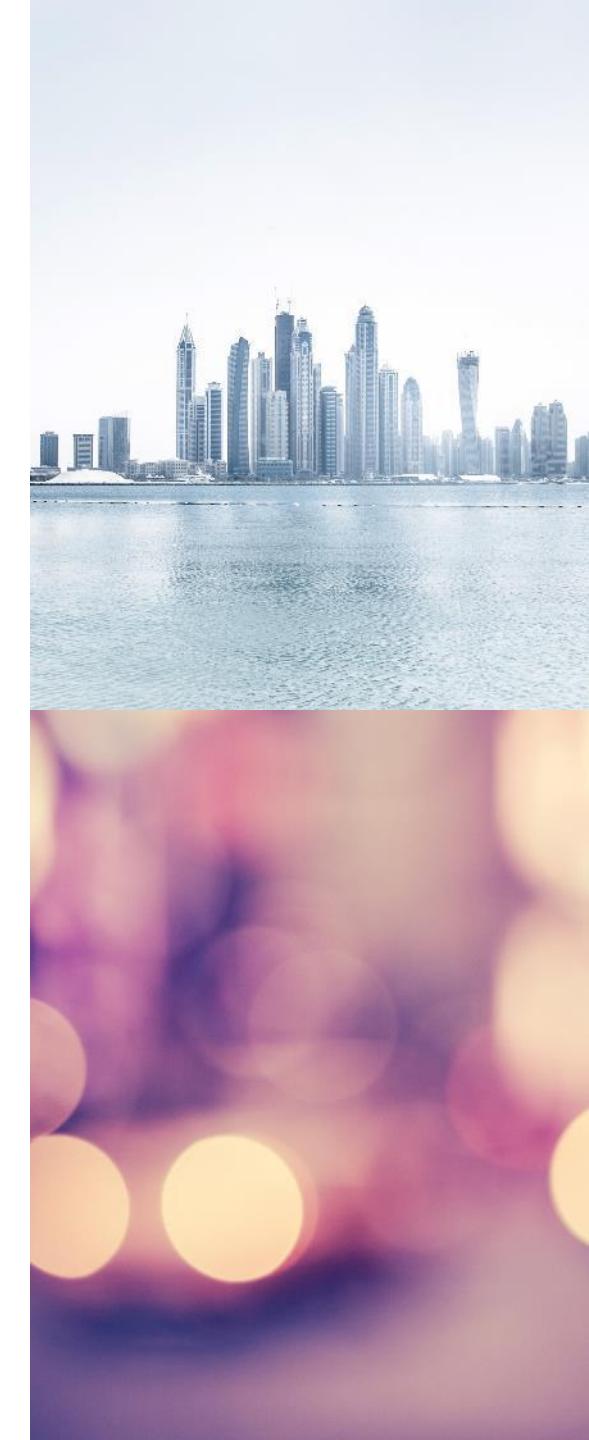


of Financial Statement



UPCOMING ICBA OFFERINGS

- Understanding C&I Lending, February 1, 2023
- February 22, 2023 Managing Troubled Loans
- March 28 ICBA Credit Analyst Institute





THANK YOU

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Making Bankers Better*

