# What do Banks look for when assessing a lending proposition?

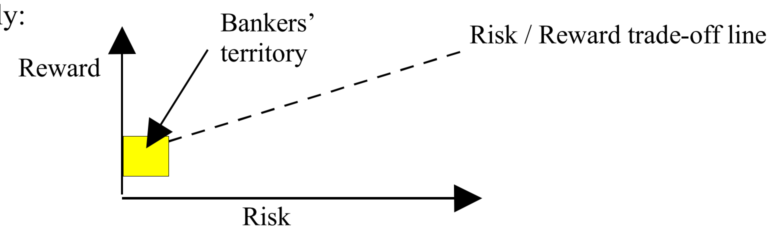
When making a lending decision a bank's first priority is to its shareholders not to you the (potential) customer. When lending money to any customer the bank's overriding concern is to ensure that the funds are at some time repaid, preferably in the way set out in a formal contract (facility letter) with the customer at the time the funds are lent.

In looking at any proposal a **bank is looking for repayment from an identifiable and credible source** be it by on-going trading / profits of the business or the financial fruits of a specific project. Then the bank will want some form of back up, **an alternative repayment source**, just in case the original plan does not work – view this as built in redundancy. For a large company the alternative source might be the strength of the overall business – its balance sheet but for many smaller businesses this inevitably means providing extra security – a personal house or other assets. If there is no additional security the bank may consider the option of a Small Firms Loan Guarantee. Speak to your bank / business adviser for more information.

Is this fair? Well look at how the bank sees it.

- If a bank lends £100,000 on a 3% margin over base it takes over 20 years to double its money. An equity investor looks to double their money in 2 - 5 years.
- If the bank loses £100,000 to a bad debt they need to lend £3,333,333 for a full year at 3% over cost of funds to merely cover the loss. **Banks by necessity are risk averse** with a low risk threshold.

Shown graphically:




Is your proposal a good risk?

When assessing any proposal each bank has as its guide a set of principles of good lending – Canons of Lending, which are often made into a mnemonic, one such is 'CAMPARI'. In making a presentation to a banker you need to provide them with sufficient information and reassurance so that they can mentally tick off each element of their aide-memoire and hopefully agree your proposal. If need be speak to your business adviser to ensure your proposal addresses the issues that the bank will consider.

CAMPARI – Canons of lending

- Character – Can you the customer be trusted, what is your track record, your historic actions will be considered here, have your previous projections been optimistic / conservative.
- Ability – What key skills does the organisation's management possess for the proposal presented. Are there areas of weakness in the management team?
- Margin – Set to match perceived level of risk; including commission, interest margin and fees.
- Purpose – Is bank prepared to lend for purpose stated, is it against bank policy, is it illegal or is the bank wary of the market sector? Could the bank consider that the proposal is too risky, development capital will often attract a premium margin when compared to normal working capital or owner occupied premises finance.
- Amount – Is the amount being asked for appropriate? Too much or too little, here the bank will look in detail at your projections, and challenge your assumptions. They will also be interested in the customer's stake in the presented proposal?
- Repayment – The crucial element, a source of repayment needs to be established at the outset – trading profits turned into cash-flow, trade sale, asset disposal, market quotation, what ever the source this needs to be set out for the bank. It must also be identifiable not merely a promise. This is their real risk assessment task and a major component is usually the assessment of the historic trading figures and the projections. Early stage companies with no or minimal sales and no chance to establish credibility in financial forecasts can have problems here.
- Insurance – In case something goes wrong the bank will normally seek some form of appropriate collateral – ideally something that is easy to take, value and if necessary realise.