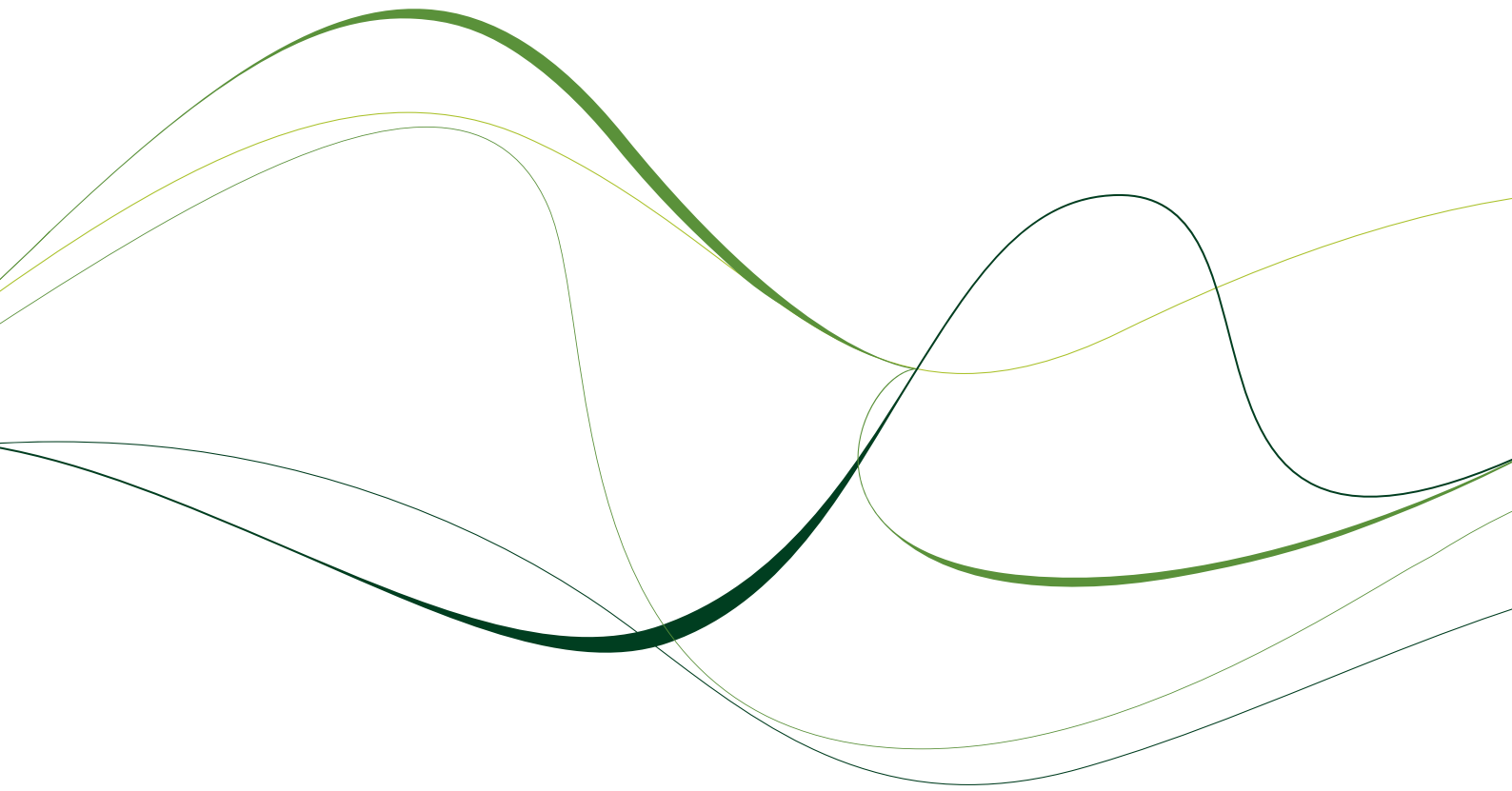


Helping your Business

Understanding the

Bank Funding Criteria

our practical guide



Introduction

Gaining access to finance is critical to the success of any business. This guide is designed to help you get a better understanding of what the high street banks look for when assessing any lending decisions. We identify the top six pieces of information required and explain why the banks value this information - also explain why you need to look at these yourself to effectively manage your business.



1. Cash flow forecasts
2. Aged Debtors and Credits Lists
3. Management Accounts / Information
4. Historic Trading Accounts
5. Profit and Loss Forecasts
6. Balance Sheet

At the back of the guide there is a directory that has been compiled to provide you with additional information at your fingertips.

“I am a great believer in keeping everyone you do business with informed. Openness, honesty and integrity with your bank, suppliers and customers is the only long-term way forward for success”.

Sir Alan Sugar, Government Enterprise Champion

Cash Flow Forecasts

Why you need them:

It is essential for all businesses to know (usually on a monthly basis) when income will be received and bills are going to be paid. This helps ensure that sufficient cash/working capital is available. Planning your cash flow will help you identify the cash needs of your business. Similarly, it will enable you to review actual figures each month in comparison to your budget. This will help highlight any variances to allow corrective action to be taken if required.

From a co-ordination point of view, decisions made today are almost certain to affect future cash flow. Cash flow forecasts will help you appreciate the impact of your decisions on the business and its financing needs.

What banks are looking for:

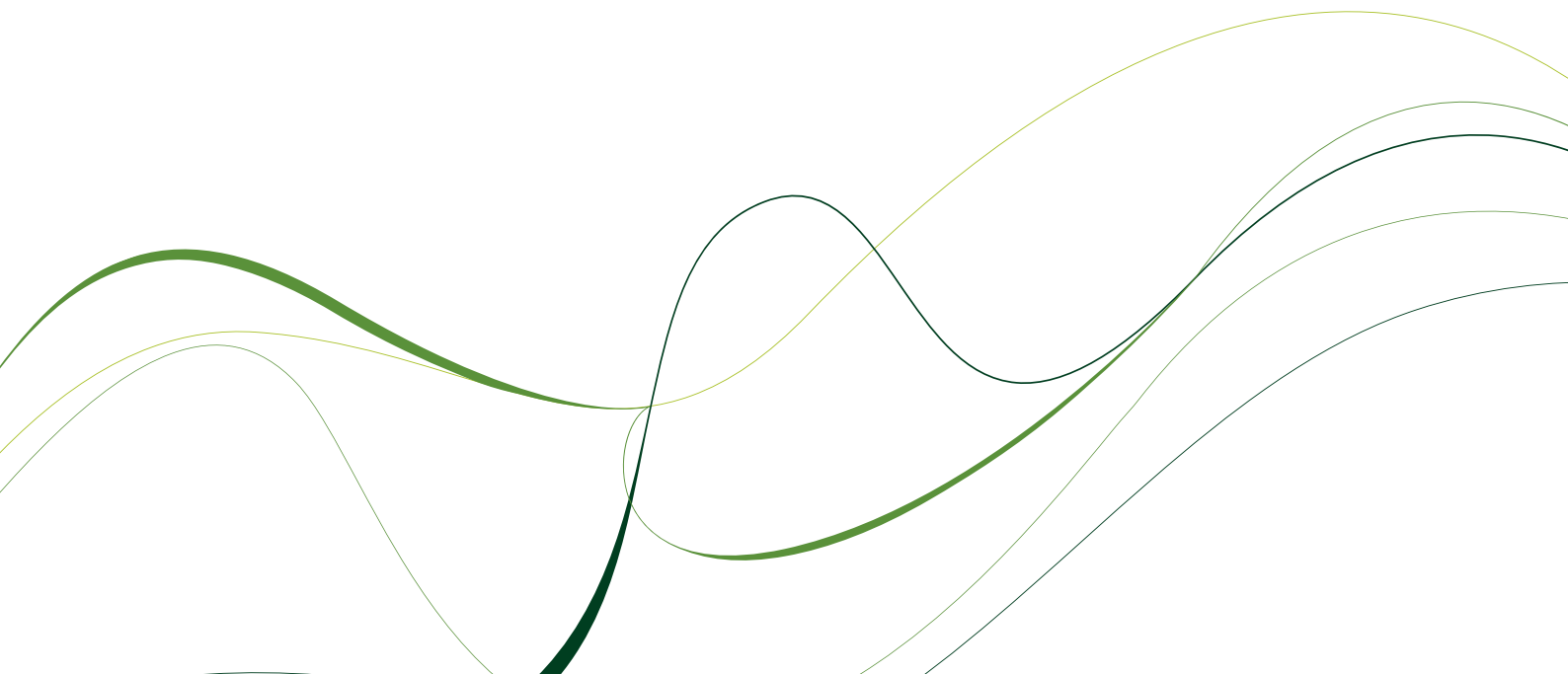
Banks will need simple financial projections detailing payments you need to make and income you will receive.

- Evidence to support your turnover forecast.
- Historic trading accounts, vendors accounts, or (if you are buying a business) new contracts.
- Details of potential and pipeline income and how it has been calculated.
- Details of loan repayments and interest, VAT, dividends, remuneration, drawings, tax etc.

They will also assess your cash flow assumptions and consider what might happen if things don't go quite as planned.

- Sales are lower than planned
- Debtors pay later than anticipated
- Bad debts are higher than forecast
- Interest rates rise
- Costs increase

Given the time involved in preparing this data, we strongly recommend you speak to your bank before any meeting and confirm what information is required. After your initial meeting, you may be asked to provide supplementary information to help assess your lending proposal before a formal decision and offer can be made.



Aged Debtors & Creditor Lists

Why you need them:

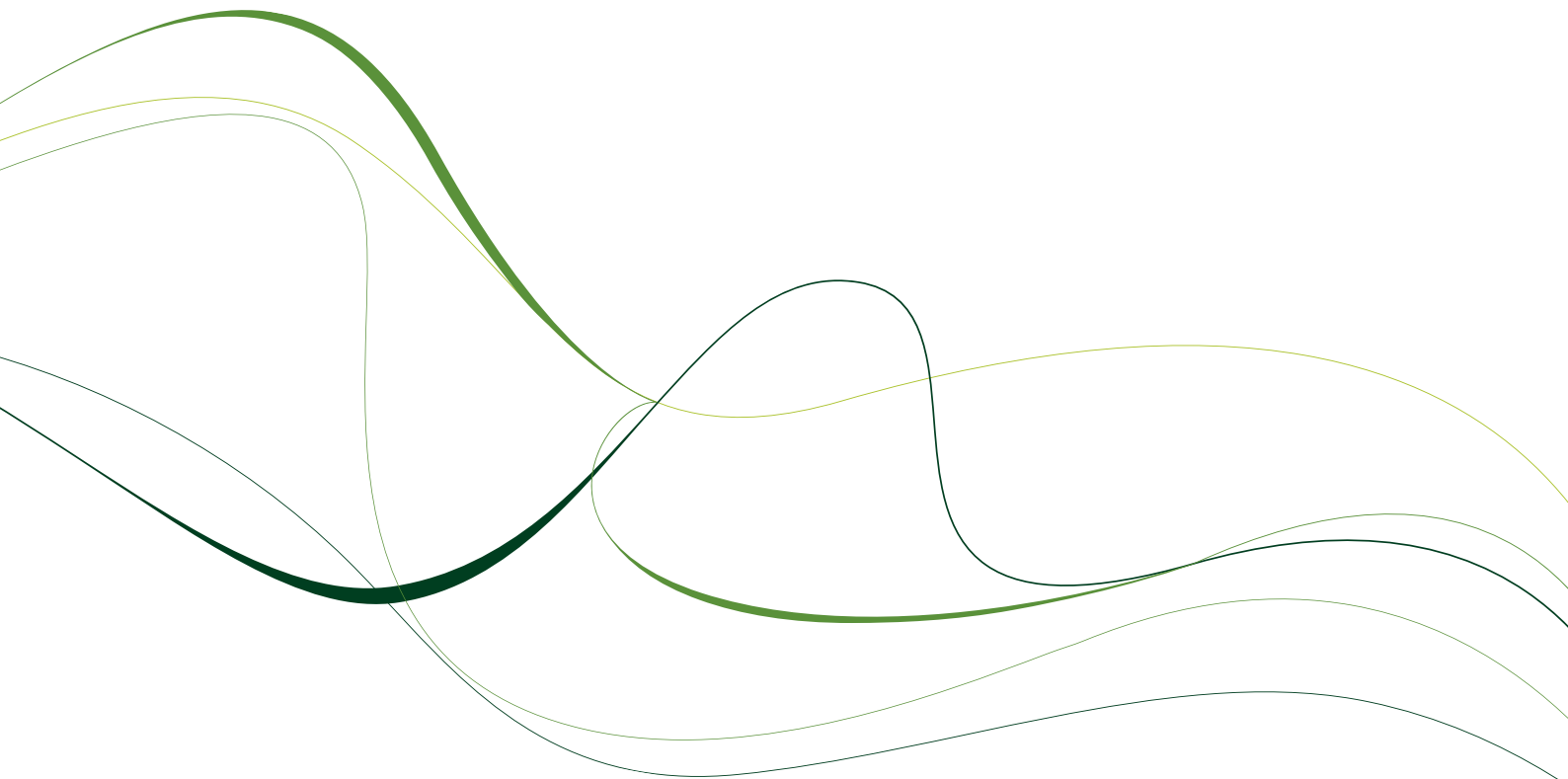
To make sure your business is not over-exposed to a single customer and the risk of non-payment, it's vital to keep tabs on who owes you money and who you owe money to. You should also consider the risk to your business if, for example, a larger debtor went bust or a major customer switched to a competitor.

Applying terms of trade and undertaking credit checks will reduce your exposure to any one customer. It is also good practice to list the balance per debtor/creditor, showing when the payment is due to be received/paid out. It's a good idea to categorise all debtors and creditors according to settlement timeframes, i.e. 30, 60 or 90 + days.

What they are looking for:

The banks will be interested in the same things you are - when will payments come in and when will they go out? They need to know that the terms you're trading under are realistic given your overall debtor/creditor picture. Be ready to answer the following questions:

- Are settlement terms with debtors/creditors agreed in writing?
- Are there any trends of late/non payment?
- Are debtors outside the agreed terms of trade?
- How do the current month's figures compare with previous months?
- Can you provide an explanation for any changing trends?
- Do you have quality assurance (of product/service) from suppliers?
- Have you run credit checks on customers/suppliers?
- Do you have agreed dispute resolution processes in place?
- Is bad debt insurance in place?



Management Accounts/Information

Why you need them:

These will outline your business's track record, providing relevant trends and forecasts on which funding decisions can be based. Historic accounts are often used to provide evidence of previous business success or a track record. This is especially useful if you need to talk to your bank about finance for the first time.

What they are looking for:

The bank will seek to understand how your business is performing relative to historic trends or projections. They will also compare performance against your last set of certified year-end figures. VAT returns provide a useful way of demonstrating current and more recent levels of turnover.

Items such as depreciation, drawings, directors' remuneration and finance costs need to be included to provide an accurate financial picture. If they are not included, the bank will aim to factor in their likely impact on your business and on cash flow.

Clearly, the more up-to date your management accounts and information are, the easier it is to evaluate your business for funding.

Historic trading Accounts

Why you need them:

These will outline your business's track record, providing relevant trends and forecasts on which funding decisions can be based. Historic accounts are often used to provide evidence of previous business success or a track record. This is especially useful if you need to talk to your bank about finance for the first time.

What they are looking for:

Ideally your trading accounts will cover three years for all parts of your business. For Limited Companies, these should be within the statutory timescales for lodging with Companies House.

The bank will seek to understand various trends i.e. sales, gross margin, overhead growth/decline. This will create an accurate financial picture of your business and the sector in which it operates.

As part of their discussion with you, they may need to ask you about data such as: year-on-year trends, single notable figures on your balance sheet, remuneration, dividend and/or drawings requirements which appear out of line with reasonable requirements.

For some smaller businesses, Income Tax returns may be used to demonstrate income received if formal trading accounts are not produced.



Profit & Loss Forecasts

Why you need them:

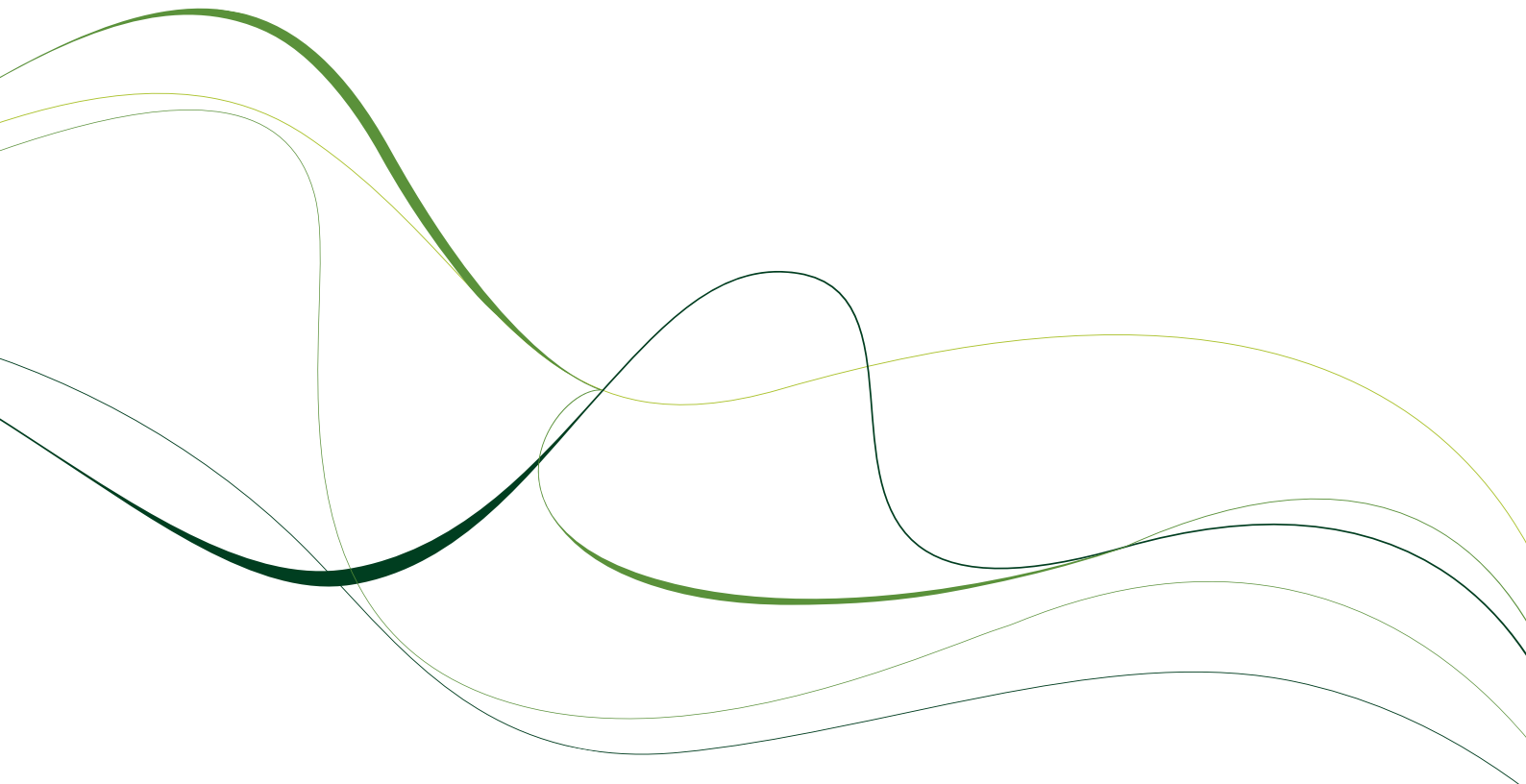
Profit and Loss forecasts enable you to demonstrate future profitability. This is particularly relevant when a business operates in changeable conditions or is exposed to variations in gross margins or overheads.

What they are looking for:

Your bank will need to understand the likely impacts of changes to income and costs on your business. This will contribute to building a realistic picture of future profitability.

Profit and Loss forecasts are often produced for just 12 months forward. Where ongoing growth is assumed for the business, projections for 24 months and even 36 months can be useful.

Given the time involved in preparing such data, it's always a good idea to check with your bank beforehand what information will be needed at your meeting. They can then let you know precisely what is required initially. They may request extra information subsequently – before they make a formal loan decision and/or offer.



Balance Sheet

The Balance Sheet provides a summary of:

- What your business owns or is owed (assets)
- What it owes (liabilities)

This in turn shows how the business is funded and how these funds are being used. The Balance Sheet provides a snapshot of assets and liabilities at a given point in time. It is important to be consistent when making comparisons over time - for example, by comparing year-end figures in the current year with year-end figures in the previous year.

What they are looking for:

First and foremost, the bank needs to ensure that your business is solvent. They will calculate some accounting ratios in order to assess your business's performance and compare these to previous results and/or industry standards.

The ratio analysis is likely to focus on some of the following areas:

- Liquidity - has the business enough cash to cover its immediate liabilities and how is this changing?
- Solvency - how much of the business is funded by borrowed capital and how is this changing? The higher ratio, the more vulnerable the business is to increasing interest rates.
- Efficiency - how quickly does the business pay its suppliers, how quickly do customers pay and how long is stock held before being sold?
- Profitability - what is the return on the capital employed in the business? This could be compared to the return made by investing the capital in stocks and shares or in a deposit account.

This information, together with the Profit and Loss Account and cash flow forecast, will provide a robust picture of the business - enabling a well-informed lending decision to be made.

(With thanks to the RBS Group plc)



Help Directory

www.britishchambers.org.uk

The British Chambers of Commerce (BCC) is the national body for the network of Accredited Chambers of Commerce across the UK.

Every Chamber sits at the very heart of its local business community providing representation, services, information and guidance to its members.

www.businesslink.gov.uk / www.bgateway.com

Whether you are already running a business or looking to grow and develop, Business Link/Business Gateway has been developed in partnership with government experts and business support organisations to help with regulations and improve performance.

www.companieshouse.gov.uk

Hosting company information and accounts, the Companies House website provides access to a wide range of company information plus supplementary advice and guidance for businesses.

www.nfea.com

The National Federation of Enterprise Agencies (NFEA) is the membership body for Local Enterprise Agencies, and other like-minded organisations, in England. It forms a network of independent, not-for-profit local agencies committed to responding to the needs of small and growing businesses by providing a comprehensive range of quality services.

www.cbi.org.uk

The Confederation of British Industry (CBI) helps create and sustain the conditions in which businesses in the United Kingdom can compete and prosper for the benefit of all working with the UK government, international legislators and policymakers to help UK businesses compete effectively.

www.fsb.org.uk

The Federation of Small Businesses (FSB) is the UK's largest group promoting and protecting the interests of the self-employed and owners of small firms. Formed in 1974, it now has 215,000 members across 33 regions and 230 branches. In addition, it is committed to delivering a wide range of high quality, good value business services to members of the FSB.

www.fpb.org.uk

The Forum of Private Business (FPB) was established in 1977 and represents 25,000 UK-based private businesses, which in turn employ more than 600,000 people. Funded by its members, the FPB offers a range of products and services aimed at saving money for members and providing practical help with all aspects of running a smaller business.

