The 5 C's of lending for development

By: Al Rogers, USAmeriBank

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Obtaining bank financing for a commercial real estate development deal isn't necessarily impossible, even in this tough economic environment. But, certainly, much has changed since the heady days of the boom.

Lenders will tell you that - from the bank's perspective - making a successful loan is all about doing a quality job of mitigating downside risk. With the economy in turmoil, and with consumer demand soft in so many business sectors, this is no easy task.

Still, there is lending being done for the right kinds of deals. Here are "5 C's" to be aware of if you're thinking about approaching a financial institution to help finance your development deal:

Collateral

Even for the most favorable development deals, borrowers are being asked to put a significant amount of cash down, in many cases as much as 30% to 40% of the loan amount. While collateral doesn't always pay back a loan, it surely helps.

Don't take this personally - it's simply the cost of getting a deal done in this economic environment. In particular, additional collateral is often required for speculative deals or for those that require belief in "projections" to repay the debt.

Cash flow

More than ever, a stable, predictable cash flow is critical for a deal to work. That's why the only retail development deals being done right now are in sectors that have the healthiest and most consistent customer demand, such as grocers, drugstores and dollar stores.

And, of course, the lower the leverage in the project, the less pressure there will be on the borrower to prove up front that cash flow will be adequate.

Character

Having a personal and a business relationship with the bank can help tremendously. The most recent real estate cycle proved that there were plenty of "characters" in the business - many were too highly leveraged and too aggressive with projections. While every loan will not go perfectly as planned, having open, honest, and frank communication will go a long way toward resolution.

We strongly encourage applicants for business loans to also bring us their personal banking business and other business. This helps build a true overall relationship, one that allows the bank to have a deep understanding of the borrower's capabilities and needs. Banking is about relationships. Having a significant level of personal deposits with a bank can count in your favor when the institution considers your loan.

Confidence

Over time, the bank may grow its financial commitment if the loan performs well. We are doing a number of deals where our involvement in the deal grows as we confirm that the level of risk is proving to be acceptably manageable from our perspective. In other words, make the first request easy and increase leverage as the projects perform. Bankers don't mind hearing, "I told you so!"

This isn't something you should assume will happen, but it's a good idea to talk to your lender about that possibility, to see whether the lender is willing to consider certain parameters for growing its level of involvement over time.

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Composition

You have to do your homework before bringing a deal to the bank, because the viability of the project is the most important factor. Certainly, it will help your cause if you are a quality borrower, but if the bank doesn't have confidence that the project will work, it doesn't matter what the bank thinks of the borrower.

The composition of a solid business plan for the venture is critical, and the plan needs to be based on facts - not conjecture and hope that things are going to get better. A lender needs to see that projects like yours are showing quantifiable success, even in this environment.

Long-term, this return to fact-based decision-making, along with a lower risk profile on loans, will result in a healthier lending environment, as fewer borrowers go into default and lending increases while the economy improves.

It's a fact that banks cannot survive long-term if they don't lend money to businesses, so it's in everyone's best interests for financial institutions to lend and for borrowers to bring them deals that will work for everyone involved.

Al Rogers is executive vice president and senior loan officer for USAmeriBank, a fast-growing Largo, Fla.-based bank with close to $1 billion in assets that focuses on business lending.