



Building Success. Together.

Evaluating the Commercial Borrower's Business Strategy

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You had a request from a prospect, not a
current customer, declined by your
underwriter/approver even though debt service coverage was
>2x.

What likely was the cause?

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Credit Risk Triangle



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- Does your institution have a formal business target?
- Does your institution have a formal restricted or prohibited business list?

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Target

To understand Business Risk you first need to know your target audience:

- Borrower Characteristics
- Loan Types
- Industries

What's your target?

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Macro



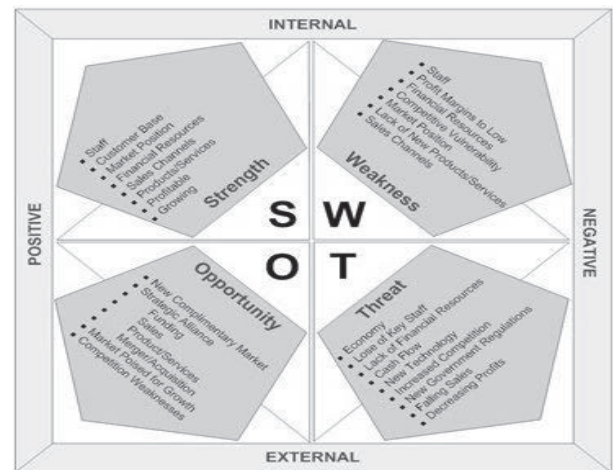
Industry Analysis

Porter's 5 Forces

Porter's five forces



SWOT



Industry Analysis

- Must understand external factors that impact a borrower's business.
- How will these factors impact a seasonal or cyclical business?
- Geographic Area – local, regional, statewide, national, international – Why & How?

Competitive Position

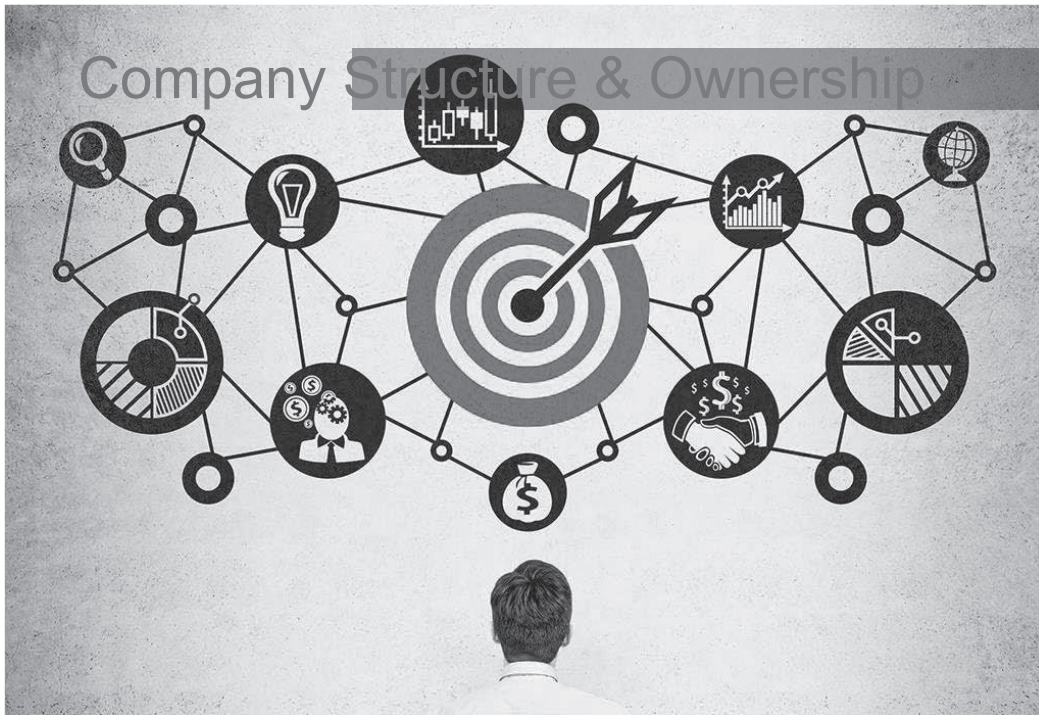


Case Studies

Review the three short case studies in your Resource folder:

Write three Macro, Industry and Competitive Position questions you think need to be addressed in the credit memo for each case.

Company Structure & Ownership



Management Capability & Strength



Management

Classic Credit Considerations

The Five C's of Good Credit

- Character
 1. Willingness to perform
 2. Integrity
 3. Attitude
 4. Good credit history
- Capital
- Capacity (Cash Flow)
- Collateral
- Conditions

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Management

- The Five C's of Bad Credit
 - Complacency
 - Carelessness
 - Communication
 - Contingencies
 - Competition

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Management

The Five D's of Credit

- Death
 - Disability
 - Divorce
 - Disagreements....Dissolution
 - Drugs
-
- +1: Disasters Pandemic!

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Fastest Growing Small Businesses

- Residential Remodeling
- Home Health Care
- Animal Care and Services
- In-person and Digital Fitness
- Tutoring and Online Learning
- Food Delivery
- Online Plant Nurseries
- Digital Events
- Cybersecurity Business
- Digital Content Creators

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Business owners have a lot in common

- Pride in their business
- Belief in serving the customer well
- Talent, interest, or skill to share a story about their business
- Acceptance of risk
- Strong work ethic
- Desire for respect and good relationships

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Risk Management

- Performing adequate due diligence prior to introducing a new product, new territory or expansion.
- Have developed and implemented controls to ensure risks are properly measured, monitored, and controlled.
- Have the appropriate performance and review systems.

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Non Financial Credit Considerations

- Ownership/Management
- Length of time in business
- Lines of business
- Competition
- On what basis do they compete
- Trade markets
- What is their market share
- Operating cycle
- Industry characteristics
- Pertinent government regulations
- Economic sensitivity
- Demographics
- **Psychographics** – Lifestyle information, tastes, preferences, and buying habits

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Non Financial Credit Considerations

Evaluate the Industry

- At What Stage in the Business Cycle?
 - Growth, Mature, Declining
- Seasonal or Cyclical
- Subject to Regulation
- Capital Intensive
- Estimated size of the industry
- Establish trends in sales over recent years
- What types of marketing strategies are prevalent within the industry?
- Is the industry sensitive to economic fluctuations?

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Best Practices

- Face to Face, visit the borrower, look at the operations, talk with their customers
- Rapid growth, from real estate construction to selling widgets, can be good but can also be a problem
- Technology and our changing world. How does it impact your customer? How does it impact the bank?

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Contact Information

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