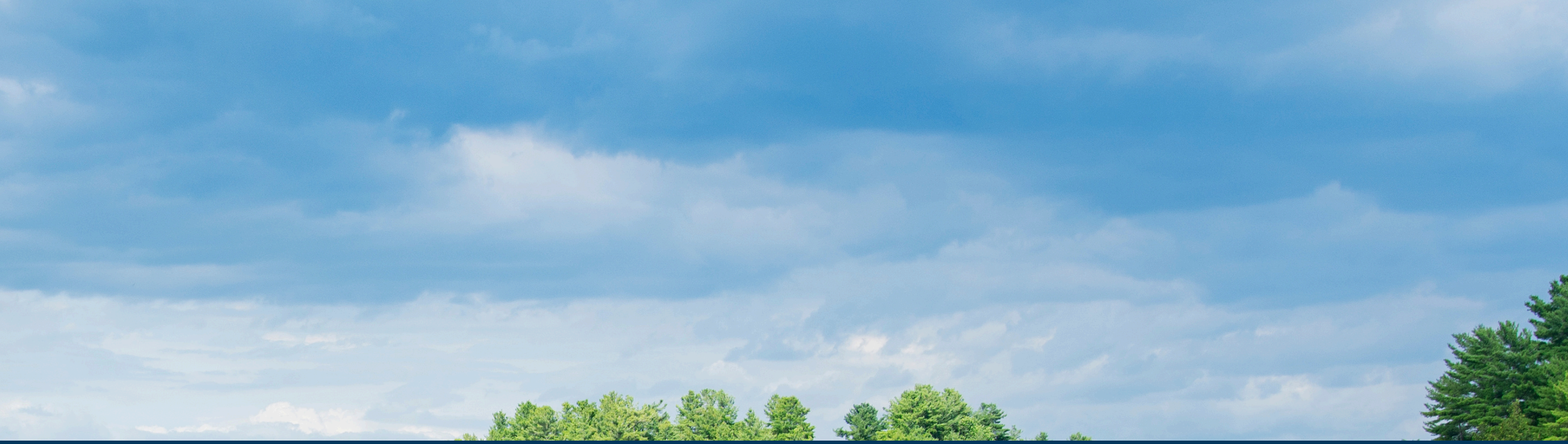
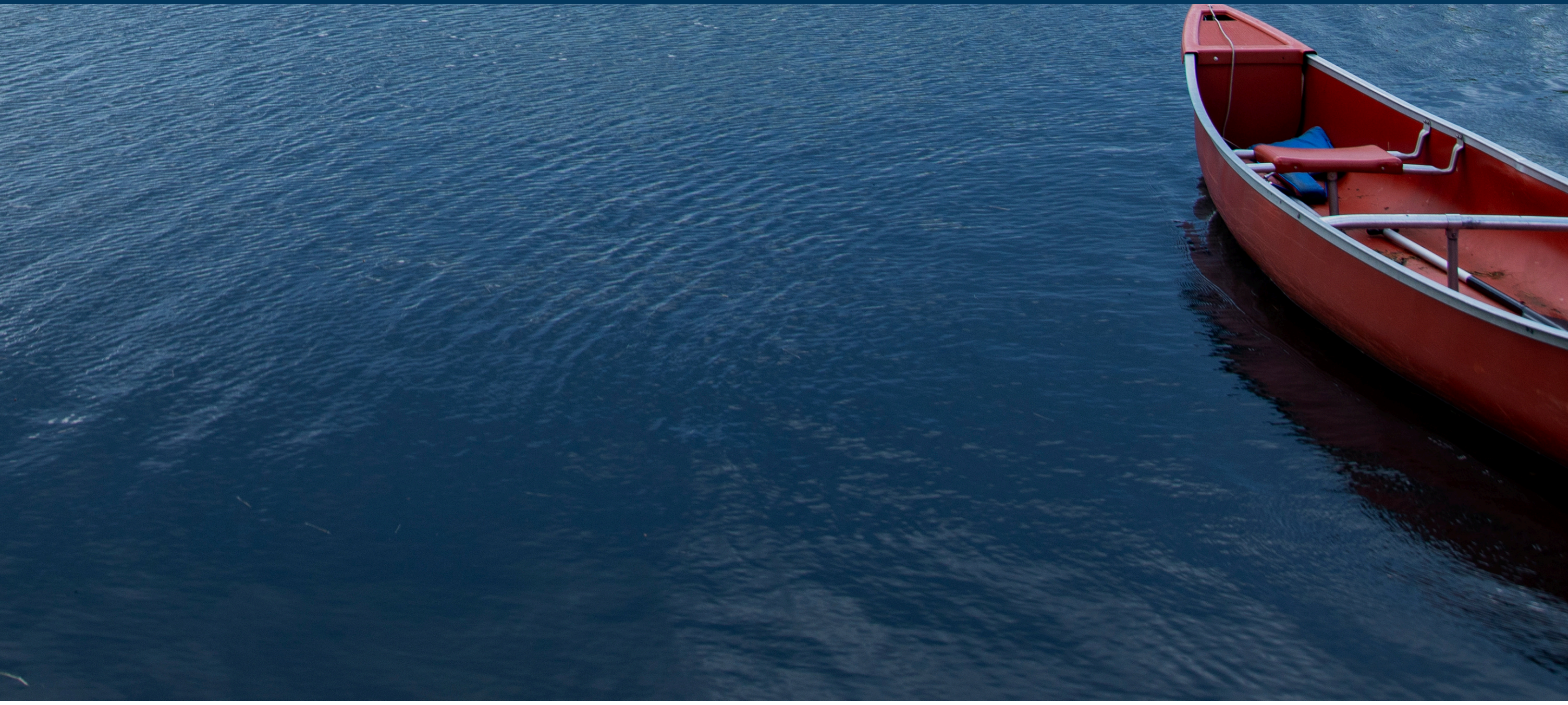


AMERICA'S SBDC MINNESOTA

Small Business Basics

Your Easy Guide to Business Lending and Finance



A product of the North Central Small Business Development Center at Central Lakes College

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Understanding Common Lending Words

Amortization: The process of paying off a loan with regular payments over time

Annual Percentage Rate: The yearly cost of borrowing money, including interest and fees, shown as a percentage

Assets: Things that a person or business owns that have value, like money, property, equipment, or products

Balance Sheet: A summary that shows what a business owns (assets), what it owes (liabilities), and the value of the company (equity)

Balloon Payment: A large final payment due at the end of a loan term, after making smaller payments

Breakeven: The point where a business's revenue equals its costs, meaning it's not losing or making money

Bridge Loan: A short-term loan used to cover expenses until long-term financing is available

Business Credit Cards: Cards issued to businesses to make purchased or pay bills, with the money being repaid in a shorter amount of time than a loan

Business Line of Credit: A flexible loan that lets a business borrow up to a set limit and only pay interest on what's used

Business Loan Terms and Rates: The conditions and interest rates a business agrees to when taking out a loan

Capital: Money or assets a business uses to operate or invest

Cash Flow: The money coming into and going out of a business, showing how much cash is available

COGS: Cost of Goods Sold; the cost of producing or buying the goods a business sells

Collateral: An asset (like a car or property) that a borrower offers to secure a loan

Credit History: A record of a person or business's borrowing and repayment activities

Credit Limit: The maximum amount you can borrow on a credit card or line of credit

Credit Line: Another term for a line of credit, where a borrower can use up to a set amount

Credit Score: A number that shows how well someone has handled credit in the past

Debt Instruments: Contracts or agreements where one party lends money and the other agrees to repay it, such as bonds or loans

Debt-to-Income Ratio: A comparison of how much money a person or business owes to how much they earn

Equipment Financing: A loan used to buy business equipment, like machinery or vehicles

Equity: The value of ownership in a business, or the difference between what a business owns and owes

Gap Financing: A loan given to fill the gap between what the bank lends and what the business needs

Gross Income: The total money earned by a business before subtracting expenses

Income Statement: A report that shows a business's earnings, expenses, and profits over time

Interest: The cost of borrowing money, usually shown as a percentage

Invoice Financing: A loan where a business borrows money based on its unpaid customer invoices

Lien: A legal claim on an asset (like a car or house) used as security for a loan, until the debt is paid

Loan Agreement: A contract between a borrower and lender outlining the terms of the loan

Loan Covenant: Rules or conditions a borrower must follow as part of a loan agreement

Loan-to-Value: A percentage coming a loan to the value of an asset being purchased

Maturity: The date when a loan must be fully paid back

Net Income: The amount of money a business has left after subtracting all its expenses

Net Worth: The total value of a business's assets after subtracting its liabilities

Origination Fee: A fee charged by a lender for processing a new loan

Personal Guarantee: A promise made by a person or company to pay back a loan if the business that borrowed the money can't. It's like a backup plan for the lender

Prime Rate: The lowest interest rate banks offer to their most trustworthy customers

Principal: The original amount of money borrowed in a loan, not including interest

Pro Forma: A financial statement that projects future income, expenses, and profits

Profit/Loss Statement: A report that shows how much money a business made or lost over time

Promissory Note: A written promise to repay a loan by a certain date

Revolving Credit: A credit line that allows a business to borrow, repay, and borrow again up to a certain limit

Secured Loan: A loan backed by collateral, like a car or house, to reduce the lender's risk

Underwriting: The process where a lender reviews a loan application to decide if the borrower is credit worthy

Unsecured Loan: A loan where a business borrows money without having to offer anything valuable, like a house or a car, as a guarantee.

Variable Interest Rates: Interest rates that can change over time, depending on market conditions

Working Capital Loan: A loan used to pay for everyday business expenses, like salaries or rent

The 6 C's of Credit

These are 6 things that a lender (like a bank) typically looks at to decide if they should give a business owner a loan.

1. **Character:** This is about the business owner's trustworthiness. Lenders what to know if you've paid back loans before and if you're responsible with money. They might check your credit history to see if you usually pay your bills on time

2. **Capacity:** This is about how much your business makes and if you can afford to pay back the loan. The lender will look at your business income (or projections) to see if you have enough money to make monthly payments.

3. **Capital:** This is the money or assets (like equipment or property) that you already have in your business. Lenders like to see that you've invested your own money because it shows that you're serious about your business.

4. **Collateral:** This is something valuable (like your car, building, or equipment) that you promise to give to the lender if you can't pay back the loan. It gives the lender security because they can take the collateral if things go wrong.

5. **Conditions:** These are about the loan's purpose and the overall state of the economy. Lenders want to know why you need the loan (like to buy new equipment or expand) and if the economy is doing well enough for your business to succeed.

6. **Cash Flow:** This is about ensuring that you have enough money to fund potential growth. If it looks tight, or if there are signs of not having enough cash, lenders may decline new credit or find the need to restructure existing credit.

Understanding Your Balance Sheet

ABC Gift Shop Balance Sheet December 31, 2023				
Assets			**Liabilities**	
Current Assets			Current Liabilities	
Cash		$32,800	Accounts Payable	$49,000
Accounts Receivable		$300	Accrued Expenses	$450
Prepaid Rent		$1,000	Unearned Revenue	$1,000
Inventory		$39,800	Total Current Liabilities	$50,450
			Long-term Liabilities	$99,950
Total Current Assets		$73,900	**Total Liabilities**	$149,995
			Owner's Equity	
Long Term Assets			Owner's Equity	
Leasehold Improvements	$100,000		Retained Earnings	$11,950
Accumulated Depreciation	($2,000)	$98,000	Common Stock	$10,000
Total Long-Term Assets		$98,000	Total Owner's Equity	$21,950
Total Assets		$171,900	**Total Liabilities and Owner's Equity**	$171,900

A balance sheet is like a financial picture of a company at a specific moment. It shows three main things:

1. **What the business owns:** These are called assets. Think of them like the business's stuff-- like cash, buildings, or computers.
2. **What the business owes:** These are called liabilities. These are the business's bills or debts that need to be paid, like loans of money they owe suppliers.
3. **What's left over:** This is called equity: This is what's left after paying off the bills. It's the company's value for the owners.

Here's the formula that's used to make balance sheets:

Assets = Liabilities + Equity

This formula means that everything the company owns (assets) is either paid for with borrowed money (liabilities) or money from the owners (equity). Just like this formula, balance sheets must always "balance."

Definitions from Balance Sheet Example

Cash: Money that a business can use right away. It could be paper money or money in the bank

Accounts Receivable: Money that customers owe a business, but haven't paid yet

Prepaid Rent: Rent that a business has paid in advance before it's due

Inventory: The items a business has ready to sell

Leasehold Improvement: Changes or upgrades made to a rented space to make it better for the business using it

Accumulated Depreciation: The total loss in value of something a business owns over time, like how a care becomes worth less the more you drive it

Accounts Payable: Money that a business owes to others, like bills they need to pay later

Accrued Expenses: Costs that a business has to pay but hasn't paid yet

Unearned Revenue: Money that a business gets before doing the work or delivering the product

Retained Earnings: Money that a business has made over time that it keeps to use later

Common Stock: Shares in a business that people can buy, giving them part ownership

Understanding Your Profit & Loss Statement

ABC Bookstore January 1- September 20, 2024

Description	Q1 (Jan-Mar)	Q2(Apr-Jun)	Q3(Jul-Sep)	Year-to-Date	
Revenue					*This is the total amount of money the business earns from selling things. It shows how much money the business brought in before paying for any cost or expense*
Book Sales	$25,000	$30,000	$35,000	$90,000	
Coffee & Snack Sales	$5,000	$6,000	$7,500	$18,500	
Stationary Sales	$1,000	$1,200	$1,500	$3,700	
Total Revenue	$31,000	$37,200	$44,000	$112,200	
Cost of Goods Sold					*This is the amount of money a business spends to buy or make the products it sells.*
Cost of Books	$15,000	$18,000	$21,000	$54,000	
Cost of Coffee & Snacks	$2,000	$2,400	$3,000	$7,400	
Cost of Stationery	$400	$480	$600	$1,480	
Total COGS	$17,400	$20,880	$24,600	$62,880	
Gross Profit	$13,600	$16,320	$19,400	$49,320	*This is the money the business has left after it sells something and pays the cost of that product*
Operating Expenses					*These are the everyday costs of running a business. It's all the things a business has to pay to stay open, even if they don't sell anything*
Rent	$3,600	$3,600	$3,600	$10,800	
Salaries & Wages	$6,000	$6,000	$6,000	$18,000	
Utilities	$900	$900	$900	$2,700	
Advertising & Marketing	$450	$500	$600	$1,550	
Office Supplies	$300	$350	$400	$1,050	
Total Operating Expenses	$11,250	$11,350	$11,500	$34,100	
Net Profit	$2,350	$4,970	$7,900	$15,220	*This is the money the business has left after paying for everything. It's the amount of money the business actually gets to keep*

A profit and loss statement (also called an income statement) is a financial report that shows the business's income, expenses, and overall profitability. It's like a snapshot of your business's financial health.

It is a way to track how much your money is making and spending. By understanding your profit and loss, you can make informed decisions about how to grow and improve your business. Here are a few ways that you can use your statement:

1. **Determine Profitability:** The statement shows whether a business is making a profit or a loss. This information is crucial for determining the overall health of the business and identifying areas for improvement.
2. **Track Financial Performance:** By comparing the profit and loss statement to previous periods, you can track changes in your financial performance over time. This can help identify trends, such as increasing or decreasing revenue or expenses.
3. **Identify Cost-Saving Opportunities:** This statement can help identify areas where expenses are higher than expected. By reviewing the statement, you can pinpoint areas where costs can be reduced, such as by negotiating better deals with suppliers or streamlining operations.
4. **Evaluate Business Strategies:** The profit and loss statement can be used to evaluate the effectiveness of different business strategies. For example, if a new marketing campaign resulted in a significant increase in revenue, the statement can help measure the success of the campaign.

Understanding Your Cash Flow

ABC Hair Salon for the Month Ended September 30, 2024

Cash Flows from Operating Activities		*These are the daily tasks a business does to make money, like selling products or providing services*
Cash Inflows:		
Cash Receipts from Customers	$12,000	
Other Income (ex, Product Sales)	$1,500	
Total Cash Inflows	$13,500	*Cash Inflows are the money a business receives, such as from customers who buy things*
Cash Outflows		
Employee Salaries	$4,000	
Rent	$1,800	*Cash Outflows are the money the business spends, liking paying bills or buying supplies*
Utilities (Electricity, Water, Internet)	$350	
Product Purchases (Supplies for Hair Services)	$1,200	
Marketing and Advertising	$400	
Insurance	$200	
Miscellaneous Expenses	$250	
Total Cash Outflows	$8,200	
Net Cash Flow from Operating Activities	**$5,300**	
Cash Flows from Investing Activities		*Investing Activities are when a business spends or makes money by buying or selling things like equipment, buildings, or other investments*
Purchase of Equipment (ex, Hair Dryers)	($1,000)	
Proceed from Sale of Old Equipment	$300	
Net Cash Flow from Investing Activities	**($700)**	
Cash Flows from Financing Activities		*Financing Activities are the ways a business gets or repays money, like taking loans or paying back debts*
Loan Repayments	($500)	
Owner's Capital Contribution	$2,000	
Net Cash Flow from Financing Activities	**$1,500**	*Owner's Capital Contribution is the money that the owner of a business puts into the business to help it run or grow*
Net Increase in Cash	**$6,100**	
Cash at Beginning of Period	$10,000	
Cash at End of Period	**$16,100**	

A cash flow statement is like a report that shows how much money is coming in and going out of your business over a certain time. Think of it like a bank statement, but just for your business. It helps you see if you have enough money to pay your bills, save for the future, or invest in growing your business.

Here are a few ways a cash flow statement can help your business grow:

1. **Understand how much money you have:** It shows if you're making more money than you're spending, so you know if your business is healthy or needs improvements.
2. **Plan for future expenses:** You can spot when bills are coming up and make sure you have enough money saved to pay for them.
3. **Identify opportunities to save or invest:** It helps you find places where you might be overspending or if you have extra money to invest in new equipment or advertising.
4. **Make better business decisions:** You'll know when it's safe to hire new employees, expand your services, or buy better tools because you'll see exactly where your money is going.

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