

Startup operations face financial obstacle

Brand new ventures difficult to finance, seen as unproven by lending institutions

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THOMAS DOYLE - Victoria Advocate

It's not easy to get money to start a new business in these parts.

"Accessing small business capital is not necessarily easy anywhere," said Carole Parks, director of the Small Business Development Center at the University of Houston-Victoria.

Victoria is in an area of the state where startup capital lending is rather conservative, she said.

"From a pure banking standpoint those are the more difficult to finance because they are unproven. It's a brand new venture," said Kenneth Vickers, executive vice president of First Victoria National Bank.

About 5 percent of the commercial lending at Wells Fargo is to start up companies, noted said David Edwards, business banking manager.

About a third of the startup loans to businesses in the region come from non-bank lending institutions outside of the area such as government programs, Parks noted.

But other factors unique to the area have a greater cooling effect on accessing startup capital than bank loans, Parks said.

Businesses seldom get all their startup capital from traditional commercial banking, Vickers noted.

"We are short on venture capital here," said Keith Mudd, associate director of the SBDC. That shortage serves as a bottleneck for small business development.

"It would seem to have a bit of a dampening effect," Parks agreed.

Only a small number of the startup borrowers at Wells Fargo have other creditors who put money into the deal, Edwards said. Venture capital increases the total amount of money a business can borrow to start, Mudd said.

A new company with around \$50,000 in venture capital can use that money to leverage an additional \$50,000 from the bank, he said as an example.

Investments in a business by venture capitalists may also not have payments like a bank loan would, allowing a business more time to generate cash flow, Mudd said.

Venture capitalists generally have higher risk tolerances than banks do in terms of who they will give loans to, Vickers said. But he noted venture capitalists also expect more in return than banking institutions.

The shortage of such venture capital in the region leads many prospective entrepreneurs to use what is known as "boot strap capital," Parks said, such as using personal credit cards, home equity loans, retirement funds or loans from family members to start a business.

"Basically the people are tapping into every asset they've got," Parks said. This can tie an entrepreneur's entire financial fate to the success or failure of the enterprise.

That level of risk is usually not the safest or best way to fund a new business, she said.

Mergers of large banks have also had a cooling effect on commercial lending in general, Parks noted.

A recent study by the Small Business Administration found that when a bank holding company buys another bank, lending to small business as a percentage of total assets drops, she said.

If a holding company acquires a bank and doesn't merge it with other banks owned by the holding company, the drop is not as bad, she said.

In terms of lending for small business startups, small banks can be more flexible in lending decisions, she said.

Smaller banks can rely less on credit scoring and can use factors like personal character in lending decisions much more so than multinational banks, Parks said.

With larger banks lending decisions many times must be finalized by someone in another city, she said. Since banks make money by lending it out, she said, smaller banks also have more incentive to invest in the local economy.

Edwards disagreed with Parks' evaluation, stating that while the local office may seek advice from other offices that specialize in a certain type of loan, lending decisions are made locally.

"Wells Fargo can't run this corporation from San Francisco," Edwards said. "They've got to run it in the local markets that they serve."

That means even a giant banking institution can use criteria like personal reputation when making a loan.

Larger banks can often offer products and services that smaller banks can't, he said, pointing as an example to people in the Wells Fargo organization who may have

experience in lending to the type of business a local person wishes to start. Those employees can advise the borrower on methods to structure their debt in a way that a smaller bank might not be able, he said.

Parks noted most of the banks in Victoria are still regionally based, and do make a fair amount of startup loans.

Vickers described his bank's lending philosophy as "opportunistic," neither conservative nor aggressive. The amount of capital the bank will require a business to have available before making a loan varies from enterprise to enterprise. The bank will take a larger risk on a company with a very strong business plan, for example.

Edwards said his bank's lending standards are about the same as they are anywhere else.

In contrast to startup capital, business expansion capital is fairly easy to access in this region, Parks said.

If a company has a good track record and financial history, coupled with strong management, "I think expansion money is pretty readily available," Vickers said.

• **Thomas Doyle is a business reporter with the Advocate. Contact him at 361-580-6511 or at tdoyle@vicad.com.**