





# BankAbility

With stricter regulations on community banks, a good balance sheet usually trumps a good idea.

By Lawrence Schumacher | Photography by John Linn

**W**hen Dean Koerner bought Dino's Southside Café in Richmond nine years ago, he sat down with the loan officer at the bank he'd worked with for 20 years. An hour later he walked out with the loan he needed to start his restaurant career.

This year, when Koerner contemplated buying a nearby restaurant that had gone out of business, it was a different story. He was told "no" by every bank he visited. "They weren't going to take the risk again, no matter what my credentials were," said Koerner. "The restaurant industry is high-risk in a good economy, and banks today really don't want risk."

Outstanding small business loans in Minnesota were down 13 percent in mid-2011, compared to three years prior—before the financial crisis broke, according to a review conducted for the StarTribune.

Restrictions on credit in this post-recession, post-financial crisis era are causing central Minnesota businesses to look for new solutions to the lingering problem of tight credit, even as the economy recovers.

Koerner eventually found another opportunity—a lake side supper club in Eden Valley—that was already a bank-owned property for four years and therefore a liability that the financial institution was more willing to get off its books. He had to put up his own house as collateral to secure the loan though.

"If I'd just been starting out today to buy my café, I doubt I would have been able to get into this business," Koerner said. "There's a guy who wants to buy my café in Richmond, but the bank wants him to come up with 30 percent down."



**Tight Times:** Two Rivers Enterprises owner Robert Warzecha (left) and American Heritage bank president and CEO Jay Johnston (right) worked together throughout the economic downturn. Today, Two Rivers Enterprises is poised to begin a \$1 million expansion.

## The New Normal

Robert Warzecha found a similarly friendly lending climate when he started Two Rivers Enterprises in Holdingford in 2001. But despite a good relationship with his banker, the stainless steel equipment manufacturer found that the credit market had changed since his last financing deal.

“Before the crunch, you’d go in and they’d shake your hand and give you the money,” Warzecha said. “Now, there’s a lot more documentation and scrutiny. You have to have a good relationship with your bank and know how they’re going to react to your needs.”

Warzecha’s bank—American Heritage National Bank in St. Cloud—helped his business through the economic downturn. Two Rivers Enterprises currently employs between 28 and 40 people, depending on the season, and is now poised to begin a \$1 million expansion.

## Tighter Regulations

In the wake of the collapse of national banks, several changes took place in the financial field, said Rob Ronning, CEO of Little Falls-based Pine Country Bank. The 2010 Frank-Dodd Act forced

all banks, whether large or small, stable or fragile, to institute new policies for evaluating loan applications and balancing their financial books.

“The biggest challenge for us today is how regulation has put a stranglehold on us,” Ronning said. “Small community banks like ours are especially hard-hit, because we have to live by the same restrictions as the big banks, but without the resources that they have.”

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Ronning describes diverting staff time to regulation compliance that would otherwise be spent on servicing clients, and says the new climate has left banks more unwilling to “go out on a limb” for clients in the same way they might have in the past.

“The pendulum had swung too far toward easy credit for businesses before the financial crisis, and now has swung too far toward preventing another meltdown,” said Jay Johnston, president and CEO of American Heritage Bank.

## Seeking Alternatives

Today, some banks are requiring three years of profitability from applicants, and some have raised the minimum personal credit score they’ll accept from 650 to 680, according to the Minneapolis-based Metropolitan Consortium of Community Developers, an organization that lends to higher-risk businesses who have been turned down by the banks.

In turn, some are relying on other sources of capital like the financing provided by federal programs, community loan funds, angel investors, venture capitalists and the Minnesota Initiative Foundations (MIFs), which provide a form of gap financing.

Even when a bank is willing to loan money to a rock-solid customer, they often can’t loan the entire amount that a business needs to buy a new piece of equipment or add on to their facility, said John Elden, director of business finance for the Duluth-based Northland Foundation, one of six Minnesota Initiative Foundations.

“Businesses that have a reasonable track record and are in an expansion mode aren’t having a particularly hard time financing, but they might need financing partners to get them all the way,” he said.

In response, the MIFs offer gap loans to make up the difference between the capital businesses have on hand and what the banks are able to lend.

“The goal of our lending program is simple: quality job creation or retention. We’re interested in working with business owners who want to create jobs that pay a living wage with benefits,” said Dan Bullert, business finance manager for the Initiative Foundation. “The Initiative Foundation’s focus has always been on economic growth, and partnering with companies who bring

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*Jay Johnston, President & CEO of American Heritage Bank*

in new revenue or keep it within the region is one of our key strategies.”

Warzecha said a past business financing package for Two Rivers included a loan from the Initiative Foundation, and he’s eager to repeat the process in the upcoming expansion. The Foundation does not compete with private banks in the small business loan industry, but typically partners with a bank to construct a loan package that leverages a variety of funding sources, added Bullert.

American Heritage and Pine Country Bank are among the 60-plus banks and community development partners that have worked with the Initiative Foundation to approve nearly 900 loans since the foundation began lending in 1987. “We probably lean more heavily on the Foundation now because there are more gaps that we can no longer fill,” said Ronning.

And if a business is looking for a smaller loan (under \$50,000) the Initiative Foundation will often direct them to microloan funds such as those managed by Region 5 Development Commission, St. Cloud State University, Southwest Initiative Foundation and other partners who are also focused on microenterprise development and support for entrepreneurs.

## Small but Vital

Many experts credit the Small Business Administration from keeping the business loan market from completely imploding

during the financial crisis. The guarantees it provided were essential to keeping businesses from folding, according to Johnston.

When the recession hit, Dubow Textile was in a strong enough financial position to look at expanding when the company started running out of space at its St. Cloud headquarters in 2010.

Because it had its finances in good order and a longstanding relationship with its lender, American Heritage Bank, the company was able to secure a

loan to almost double its headquarters, buy new equipment and add roughly 30 employees. But the expansion was much easier to accomplish because of favorable terms arranged through a Small Business Administration loan that American Heritage accessed. “We definitely took advantage of the favorable rates and terms of it,” said CEO Rob Dubow. “It wasn’t a moneymaker for us, but it made the difference between many businesses staying open and shutting their doors.”

## Outside the Mainstream

If a business has had recent economic troubles, or if an entrepreneur wants to start a new business, the picture can be more complicated though.

“There’s still money for a good idea, but it needs to be backed with a solid business plan and detailed, realistic estimates of its market and profitability,” said Barry Kirchoff, director of the Central Minnesota Small Business Development Center at St. Cloud State University. “Industries that have been hard-hit in the recession—banks are less willing to put up the money for them now than they were before.”

Nonprofits such as the Minnesota Initiative Foundations can provide some options, according to Elden. Gap loans that were typically directed toward helping a business expand went unused during the recession, and funds can sometimes be

# THE 5 C's OF CREDIT

Numbers aside, most lenders consider a handful of subjective guidelines when considering a loan application. Although the weight of each one may vary from bank to bank, the elements are the same: a profitable idea, financial stability and the borrower’s unwavering commitment to business success.

## CASH FLOW

Don’t confuse cash with profit. Lenders must be convinced that your business will have enough cash to pay its debts at any given time. This includes payroll, suppliers, utilities and, of course, your business loan.

## CAPITAL

How will you make it through the proverbial “tough times?” Will there be enough money to sustain and grow your venture?

## CHARACTER

Are you honest, competent, determined, savvy and adaptable? Prove it to your lender, and bring along a good credit score.

## COLLATERAL

Lenders are trained to protect their investments. By securing valuable assets, they can sell (or liquidate) them if you can’t repay the loan. Such assets include real estate, equipment, inventory and yes, even your personal property. In fact, a personal guarantee of repayment is non-negotiable. No collateral? No loan. It’s that simple.

## CONDITIONS

How healthy is the overall economy and the market for your product or service? Is your industry booming or sagging? Who are your competitors? In the razor-sharp minds of lenders, external conditions are equally as important as your business idea.



Rob Ronning, Pine Country Bank CEO

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redirected toward providing a lifeline to businesses that need working capital to sustain them until the economy picks up again. Despite the end of the recession, Elden said “the need is still there” for many of those sustaining loans.

And even though times are tough, experts remind businesses that the situation isn’t permanent. According to the Federal Reserve Bank of Minneapolis, Minnesota banks loaned out more money in the second quarter of 2012 than in the same quarter last year, the first time in three years that the state’s banks as a whole showed a quarterly gain.

“On the political side, they want you to lend to get the economy going again, but on the regulation side, they tell you not to lend unless it’s a sure thing,” said Johnston. “Eventually, things will balance out, but it’s taking a while.” IQ

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Across from Schaefer’s Grocery | [www.spiritofnisswa.com](http://www.spiritofnisswa.com)

**Nisswa Community Center | 218-963-0085**  
22x40 dance floor | 299 occ. cap. | smoke-free  
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