Heartland
Economic Development Course

Basics of Finance for Economic Development

Brought to you by Tracy Brantner, Rebecca Gubbels, and Mark Stombaugh

Meet The Experts

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Today's Facilitator

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Vault Consulting quickly helps:

- Economic Developers
- Entrepreneurial Support Organizations, and
- Financial Institutions

meet their clients at the intersection of lending skills and genuine conversation!

Why Study Economic Development Finance?

- **Tools to support the basics of economic development:**
  - Grow the tax base
  - Help businesses create and retain good jobs
  - Develop and expand certain industries
  - Improve quality of life or key community initiatives
- Other uses could also include:
  - Real estate development or reuse
  - Funding projects and programs
  - Financing small business support, technical assistance or incubators with space and resources
  - Funding your organization

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Financial Capital is the Lifeblood Needed for…

- Business Expansion
- Business Attraction
- Small Business and Entrepreneurship

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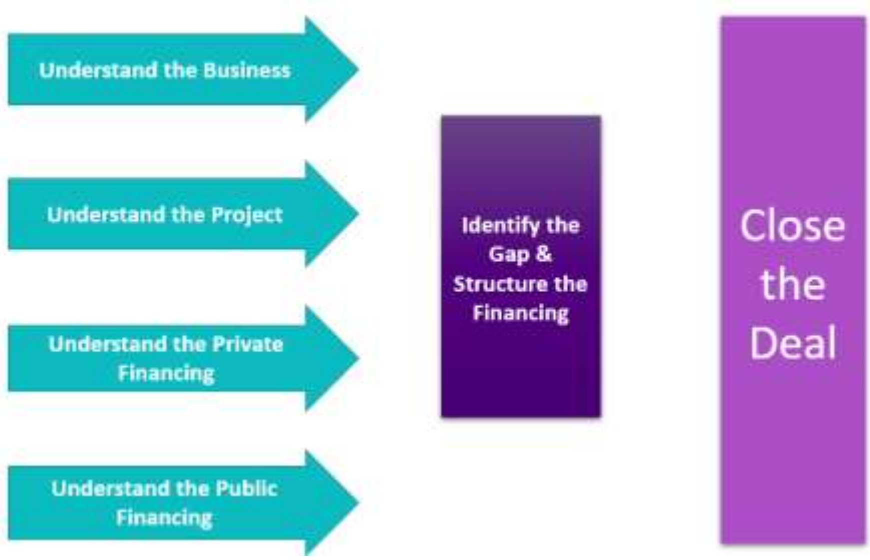
Steps in the Eco Devo Funding Process



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Understand the Business

Understand your Client's Business

1. **Assess Business Model & Market Position**
   1. Understand the company's core products/services and how they generate revenue.
   2. Research the industry landscape to determine market trends, competition, and potential risks.
   3. Evaluate customer base and pricing strategies to see if they're sustainable.
2. **Evaluate Leadership & Operational Capacity**
   1. Meet with the leadership team to understand their vision, experience, and management style.
   2. Examine business plans to determine strategic goals and scalability.
   3. Assess workforce stability, supply chain efficiency, and infrastructure readiness.
3. **Gauge Community & Economic Impact**
   1. Determine how the business contributes to job creation and economic development.
   2. Assess local partnerships, community engagement, or sustainability initiatives.
   3. Analyze alignment with economic development goals or incentives.
4. **Conduct a Thorough Financial Review**
   1. Analyze financial statements (profit and loss, balance sheet, and cash flow statements) to assess the company's financial stability.
   2. Review tax returns and credit history to gauge fiscal responsibility.
   3. Evaluate revenue streams, margins, and debt obligations.

Understand the Project

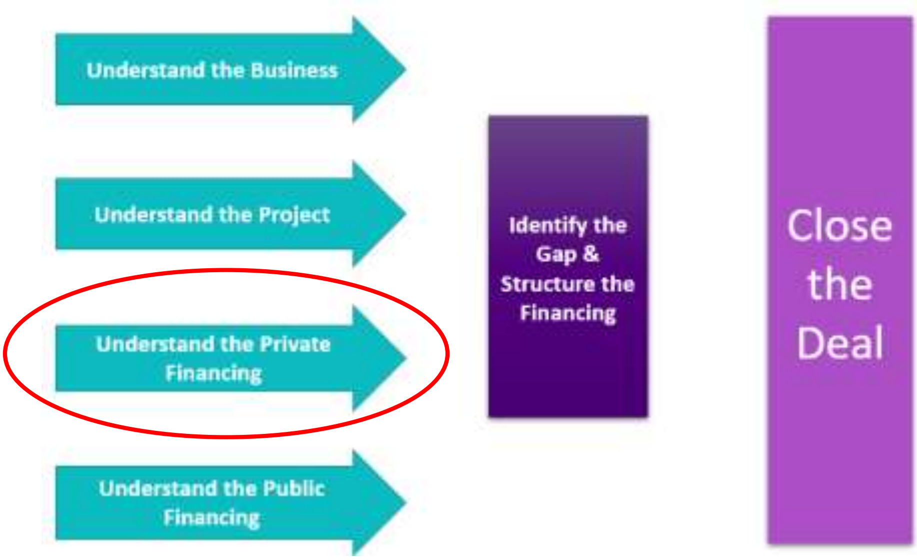
Understand Your Client and The Project

- **Business Cycle**
  - Start-up
  - Growth
  - Maturity
  - Reorganization
- **Use of Funds**
  - Working capital
  - Fixed assets
- Depending on the business stage and the use of funds, businesses will need different financing tools.

Understand your Client's Project

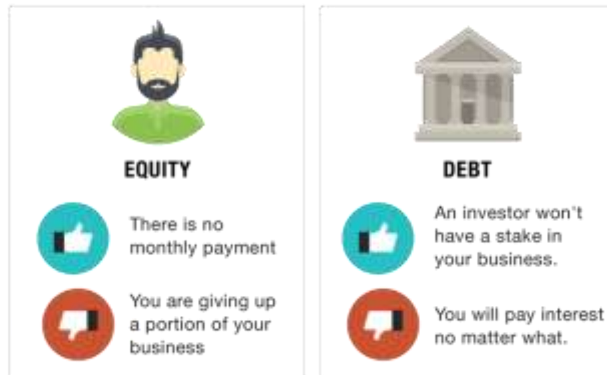
1. **Project Feasibility Analysis**
   - Assess whether the project is technically, operationally, and financially viable.
   - Review detailed project plans, including timelines, milestones, and deliverables.
   - Evaluate dependencies—such as supply chain availability, workforce readiness, or regulatory approvals.
2. **Financial Justification & ROI Projections**
   - Analyze cost breakdowns to ensure expenses are justified and aligned with the proposed budget.
   - Calculate expected revenue, profitability, or economic impact resulting from the project.
3. **Strategic Alignment with Business & Economic Goals**
   - Ensure the project fits within the company's broader strategy and future scalability.
   - Evaluate how the project supports regional economic development objectives—such as job creation, innovation, or infrastructure improvements.

Understand the Private Financing



Understand the Private Financing

- **Equity financing**
  - Does not require repayment
  - Investors receive partial ownership
  - Friends, family, angel investors, venture capital, etc.



- **Debt financing**
  - Must be repaid
  - Lenders receive fees and interest
  - Commercial banks, savings and loans, credit unions, etc.

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Private Source - Debt Financing

- Private funding comes from non-governmental entities, such as banks, credit unions, individuals, corporations, and venture capitalists.
- A bank loan is considered a private funding source.
- Bank loans are typically provided based on the borrower's creditworthiness and financial history.
- Key eligibility factors are based on what the business does to receive its income, its credit history, and where the business operates.
- These factors are often described as the **5 (or 6) Cs of Credit**!

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Private Source – Debt Financing

The 6 C's of Credit

- ❑ Character
  - Industry
  - Time in Business
- ❑ Credit
- ❑ Collateral
- ❑ Cash Flow
- ❑ Capacity
- ❑ Covenants

Small Business Administration Loans

- Called SBA loans, but they're not loans *from* the feds.
  - **They are loans from your local bank** where the feds (via the SBA) have provided a partial guarantee against losses to the bank.
- Can be underwritten by the bank and *then* sent to the SBA for their review, or can be underwritten a bank that has been given SBA underwriting authority.
  - SBA Preferred Lender Program – Banks with this authority will typically advertise themselves PLP lenders because of their comparative speed to SBA decision.
- Multiple SBA loan types.

SBA U.S. Small Business Administration

7(a) Loans

- **SBA's most common loan program**
  - The 7(a) Loan Program includes financial help for small businesses with special requirements.
- This is the **best option when real estate is part of a business *purchase***, but it can also be used for:
  - Refinance current Short- and long-term working capital
  - business debt
  - Purchase furniture, fixtures, and supplies
- The maximum loan amount for a 7(a) loan is $5 million.
- The SBA guarantees a portion of the loan, reducing risk for lenders and allowing them to offer more flexible terms and easier qualification processes.
  - Provides guarantee from SBA to the lender of up 85%... 75% is the norm.

504 loans

- The 504 Loan Program provides **long-term, fixed rate financing for major fixed assets** that promote business growth and job creation.
- 504 loans are available through Certified Development Companies (CDCs), SBA's community-based partners who promote economic development within their communities.
- The maximum loan amount for a 504 loan is $5 million.
  - For certain energy projects, the borrower can receive a 504 loan for up to $5.5 million per project, for up to three projects not to exceed $16.5 million total.

504 Loans

SBA U.S. Small Business Administration

A 504 loan can be used for:

- Existing buildings or land
- New facilities
- Long-term machinery and equipment
- Or the improvement or modernization of:
  - Land, streets, utilities, parking lots and landscaping
  - Existing facilities

A 504 loan cannot be used for:

- Working capital or inventory
- Consolidating, repaying or refinancing debt
- Speculation or investment in rental real estate

Photo by Tolu Olubode on Unsplash

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7(a) Express Loans

SBA U.S. Small Business Administration

- **SBA's fastest loan program**
  - The 7(a) Loan Program includes financial help for small businesses with special requirements.
  - Streamlined approval process. Loans can be funded in as little as a few weeks.
- Program works best for debt refinancing, working capital, and machinery and equipment (business expansion).
- Minimal to zero down payment (equity injection), and minimal to zero collateral requirements.
- The maximum loan amount for an Express Loan is $350,000.
- Provides guarantee from SBA to the lender of 50%.

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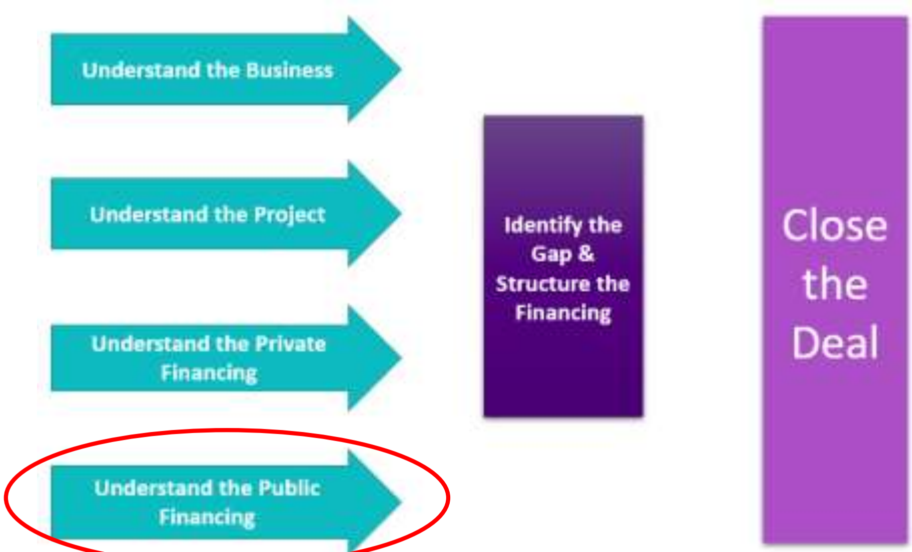
Express vs. 7(a) Comparison

U.S. Small Business Administration

	SBA Express	Standard SBA 7(a)
Maximum Loan Amount*	$350,000	$5 million
Average Decision Time**	36 hours	10 business days
Required Collateral	No *required* collateral under $25,000 Lenders can use their existing collateral policy for loans between $25,000 and $350,000	Typically requires collateral equal to loan amount
Guarantee Amount***	50%	75%

Understand the Public Financing



Principles of ED Finance

- Lower the cost of borrowing
- Lower the risk
- Flexible structures
- Package loans
- Technical assistance

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Understanding Public Sector Financing

- **Public financing can be provided by** - EDOs, utilities, non-profits, development authorities, state, federal, and more
- The public's participation in financing can **bridge the gap** for projects valuable to the community when private financing is insufficient.
  - Not for clients that can access and qualify for conventional financing
- Sometimes **access to capital** is more important than the **cost of the capital**

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What is Gap Financing?

Some projects are almost ready but need a final push to launch or expand… but they have a gap.

- Lack of feasibility is not a gap.
- Gap financing more relevant for different stages of business development
  - Growth-stage companies
  - Early-stage "search" companies
  - Mature companies avoiding "obsolescence"

- Can size of the "gap" change it from being a gap into a problem?
  - Has all but 10% of total project vs. still needs 70% of the project costs
- Ideally a final-dollar, not a first-dollar investment
- Only enough to get the deal done – protect the public dollars by pushing for more from private sources

Principles of ED Finance

Does the deal meet community's economic development goals?

- Job creation, retention, wages
- Support an industry
- Utility usage
- Land - redevelopment, repurpose, remove blight
- Other public goals in your area?
- Recommend identifying and then prioritizing your goals to know how to best value them in any proposed project

Will the assets stay in the community?

- Fixed assets vs. personal property
- Length and terms of any lease
- Other relevant ties to the community

Principles of ED Finance

ED Lending Process

- (Re)Create the programs – define priorities, rules and guidance
- Screen potential borrowers – fairly balancing community and consistency
- Underwriting – fairly balancing consistency and community
- Structuring the loan – rate, terms, and covenants
- Loan documentation – contracts to protect dollars and interests
- Loan servicing – after care to ensure repayment and relationships

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ED Underwriting

- **Underwriting – credit analysis, client's ability to repay**
  - Due diligence
    - Trust but verify what you're told about the company
    - Trust but verify what you're told about the deal
    - Trust but verify what you're told about others' commitments
  - Current/past financial statements
- **5 (or 6) Cs of Credit**
  - Character – borrower's reputation
  - Capacity – ability to repay the loan
  - Capital – enough financial resources to weather a storm
  - Collateral – pledged assets to secure the loan
  - Conditions – terms of the loan and general economic conditions

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Private Loans vs Public Loans

	Private, Bank Loans	Public, Eco Devo Loans
Character	• Industry and Time in Business	• Borrower's reputation and community impact
Credit	• History of personal and business obligation payment	• Relying heavily on private sector partners for this and/or asking for guarantees
Collateral	• 100% margined collateral	• Can choose to accept less and/or subordinate collateral
Cash Flow	• 1.2+	• Might have higher risk tolerance • Public finance can often reduce project's overall cash flow constraints to MAKE the cash flow
Capacity	• After all else fails, how can borrower still pay the loan?	• Pay as you go on larger deals reduces up-front disbursement risk… but after all else fails, • how can borrower still pay the loan?
Covenants		• Might offer a lower rate • Might offer a longer term • Must monitor the project to ensure it meets the promised eco devo results (jobs, wages, etc.)!

What are Covenants?

Loan covenants are conditions set by lenders in a loan agreement to ensure borrowers maintain financial stability and meet specific obligations. These covenants help mitigate risk and protect the lender's interests.

Types of Loan Covenants:

- **Positive (Affirmative) Covenants**: Require the borrower to take certain actions
- **Negative Covenants**: Restrict the borrower from certain activities
- **Financial Covenants**: Set specific financial benchmarks

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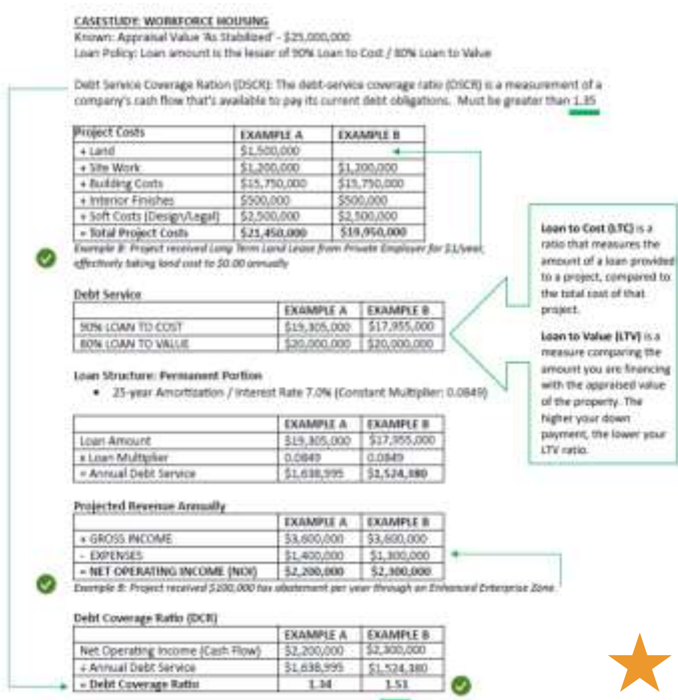
Private Loan vs Public Loan Covenants

	Private, Bank Loan Examples	Public, Eco Devo Loan Examples
Positive Covenants	Requirements to: • maintaining financial ratios • providing regular financial statements • keeping insurance coverage	Requirements to: • create or retain good jobs • be energy efficient • adhere to green building practices
Negative Covenants	Restrictions against: • taking on additional debt • selling key assets • making large dividend payments without lender approval	Restrictions against: • shifting industry focus • reducing wages or benefits • using land differently than stated
Financial Covenants	**Maintain financial benchmarks:** • minimum debt-to-equity ratio • ensuring a certain level of cash flow	**Maintain financial ED commitments:** • cannot repay loans early to avoid job creation or redevelopment commitments

Case Study: Workforce Housing

Impact of public finance tools and approaches:

- Long-term land lease
- Loan to Cost vs. Loan to Value
- Tax abatement



CASESTUDY: WORKFORCE HOUSING

Known: Appraisal Value 'As Stabilized' - $25,000,000

Loan Policy: Loan amount is the lesser of 90% Loan to Cost / 80% Loan to Value

Debt Service Coverage Ration (DSCR): The debt-service coverage ratio (DSCR) is a measurement of a company's cash flow that's available to pay its current debt obligations. Must be greater than 1.35

Project Costs	EXAMPLE A	EXAMPLE B
+ Land	$1,500,000	
+ Site Work	$1,200,000	$1,200,000
+ Building Costs	$15,750,000	$15,750,000
+ Interior Finishes	$500,000	$500,000
+ Soft Costs (Design/Legal)	$2,500,000	$2,500,000
= Total Project Costs	$21,450,000	$19,950,000

Example B: Project received Long Term Land Lease from Private Employer for $1/year, effectively taking land cost to $0.00 annually

Debt Service

	EXAMPLE A	EXAMPLE B
90% LOAN TO COST	$19,305,000	$17,955,000
80% LOAN TO VALUE	$20,000,000	$20,000,000

Loan to Cost (LTC) is a ratio that measures the amount of a loan provided to a project, compared to the total cost of that project.

Loan to Value (LTV) is a measure comparing the amount you are financing with the appraised value of the property. The higher your down payment, the lower your LTV ratio.

Loan Structure: Permanent Portion

- 25-year Amortization / Interest Rate 7.0% (Constant Multiplier: 0.0849)

	EXAMPLE A	EXAMPLE B
Loan Amount	$19,305,000	$17,955,000
x Loan Multiplier	0.0849	0.0849
= Annual Debt Service	$1,638,995	$1,524,380

Projected Revenue Annually

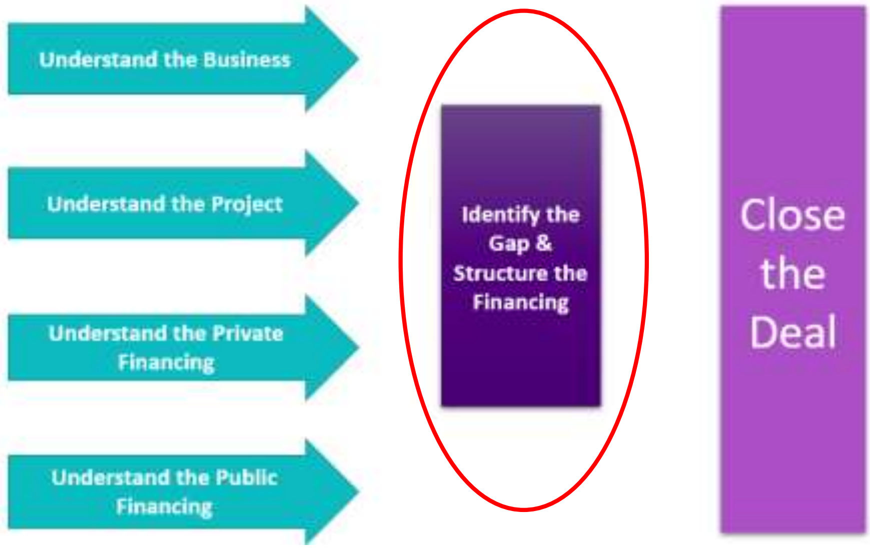
	EXAMPLE A	EXAMPLE B
+ GROSS INCOME	$3,600,000	$3,600,000
- EXPENSES	$1,400,000	$1,300,000
= NET OPERATING INCOME (NOI)	$2,200,000	$2,300,000

Example B: Project received $100,000 tax abatement per year through an Enhanced Enterprise Zone.

Debt Coverage Ratio (DCR)

	EXAMPLE A	EXAMPLE B
Net Operating Income (Cash Flow)	$2,200,000	$2,300,000
÷ Annual Debt Service	$1,638,995	$1,524,380
= Debt Coverage Ratio	1.34	1.51

Identify the Gap and Structure the Financing



Example: Business Retention & Expansion

Drivers:

- Ongoing relationships (BRE) is key
- Locally a long-time employer of choice
- Understanding all the partners and what defines their success
- Publicly traded global company
- Competitive – global search for a location
- Make a compelling case for why to re-invest in the community

Example: Structure of this Financing

Scope:
- $30 million in new production equipment
- $10 million in building and RE improvements
- 150 new FTE's at 130% of county average wage

Financing/Incentive Tools:
- State – BUILD bonds, Workforce Training, Missouri Works
- Local - Industrial Revenue Bond (IRB)(aka MO Chapter 100)

Say Hello to Carol!
It's about people…

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Beyond Loans – Other ED Finance/Incentive Tools

Other Tools
- Reduced price of land
- Technical assistance
- Tax abatement
- Tax credits
- Tax exemption
- Tax incremental financing (TIF)

EC
SizeUp
Overland Park Chamber
Network Kansas

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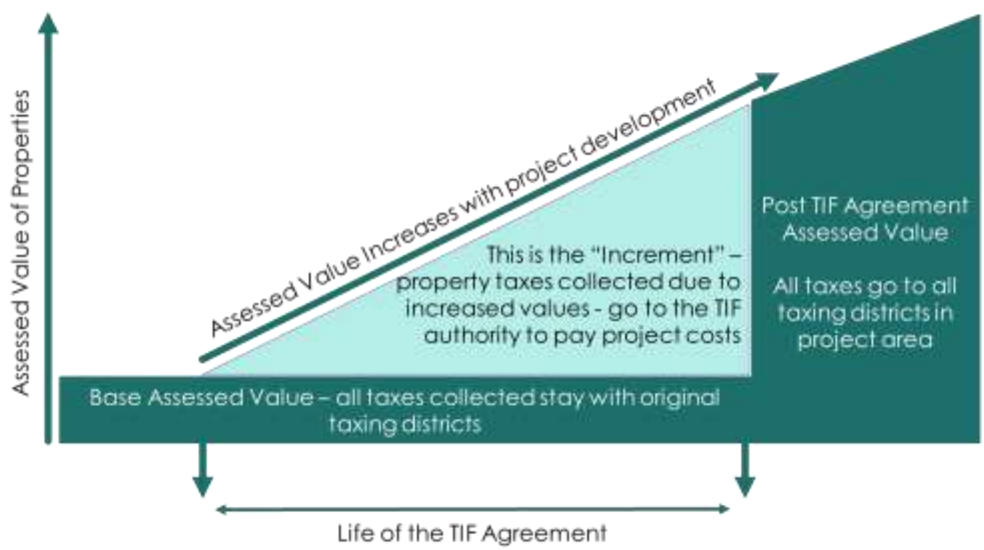
Tax Increment Financing – How it Works



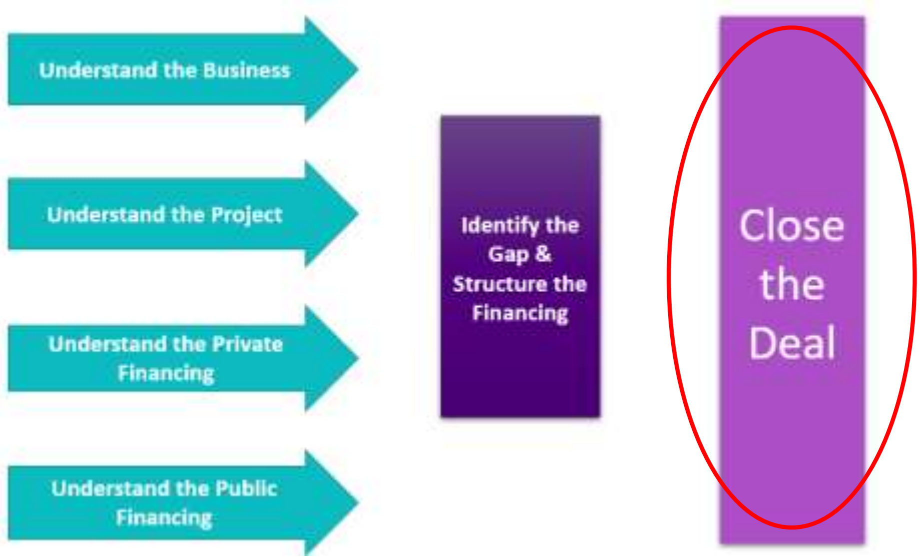
Financing/Incentive Tools

- Why use incentives?
- Who is involved?
  - There are a ton of players in finance and incentives
  - Government (local, state, federal), EDOs, utilities, investors, banks, etc.
  - Don't worry about learning them all today!
  - Develop your network of experts
- Understanding each player has a different perspective

General Rules

- Due diligence is a must
- Incentives and financing will never fix major project flaws
- Develop your network and create trust
- Confidentiality is a must
- It isn't about hitting a home run every time, singles & doubles win

Close the Deal



Close the Deal… If You Can!

- Find a responsible, ethical way to get to a YES!
- What can you do to safeguard success?
  - Educate stakeholders on role of incentives
  - Be consistent and fair
  - Under promise and over deliver
  - Maintain good accountability and transparency in program administration
  - Learn the art of saying “no”
- Why do some public/private deals fall apart?

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What Happens When I Get Home?

- This is just a start on your finance journey!
- Tools to use:
  - Utilize your Heartland Course glossary
  - Curiosity
  - Leverage AI to speed your learning
- Surround yourself with experts that can lend a hand
  - Today’s experts – Tracy Brantner and Mark
  - Referrals from Heartland Economic Development Team
  - Finance education resources like Grow America or Vault Consulting
  - Get to know your area’s finance players
- Fake it until you make it!

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Group Activity: Will This Fly?

Practice Evaluating Revolving Loan Fund Proposals

Instructions

- We’re having a *WORKING* lunch.
- During the next 45 minutes, please:
  - Use the Economic Development Finance: Group Activity Handout.
  - Work together with your tablemates.
  - Score each of the four loan proposals using the criteria provided.
  - Consider what, if any, covenants you’d recommend for each deal.
  - **Be ready to discuss your results at 12:15.**

  - Don’t forget to grab and eat your food, too!

GridIron Works

1. What Total Score number did you assign this proposal?
2. Did you vote to approve this deal?
3. Did you decide to attach any covenants or conditions?

Photo by Aarush Verma on Unsplash

GridIron Works - Considerations

- Contract in-hand triggers timeline urgency
- Corridor revitalization
- Creates skilled, long-term jobs
- Leverages two private funding sources
- Significant increase in utility use
- 5 Cs: good character, likely collateral (equipment), doubling revenue indicates possibly good cash flow

- If the revenue has doubled for this existing business and there is collateral in the use of funds, why is the bank only willing to extend $90K into this project?
- What if you fund this project and somehow the owners still miss the 120-day window to win the customer?

Root & Rise Market

1. What Total Score number did you assign this proposal?
2. Did you vote to approve this deal?
3. Did you decide to attach any covenants or conditions?

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Photo by Tara Clark on Unsplash

Root & Rise - Considerations

- Could be a catalytic retail anchor for downtown corridor
- Addresses food access and supports other microbusinesses
- Inclusive hiring plan
- Diversified funding stack
- Team has solid preparation, pre-orders, and vendor agreements

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- While diversified, the proposed funding sources are 94% from public sources. Is there something about this proposal that is turning off the private sector?
- Owners' first for-profit venture—but they are supported by advisors
  - Do we know the quality and strength of those advisors?
- Leasehold improvements—no real estate ownership
  - What are the long-term ties to the community?

Ember Ceramics Studio

1. What Total Score number did you assign this proposal?
2. Did you vote to approve this deal?
3. Did you decide to attach any covenants or conditions?

Photo by Earl Wilcox on Unsplash

Ember Ceramics Studio - Considerations

- Proven business and owner with track record
- Strong customer demand with clear growth potential
- Utility increase from kilns
- Cultural asset for revitalization corridor
- Owner is an artist and lacks experience with staff and facilities management
- HVAC permits not finalized
- Funds are likely premature without conditions

NextVolt Composites

1. What Total Score number did you assign this proposal?
2. Did you vote to approve this deal?
3. Did you decide to attach any covenants or conditions?

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NextVolt Composites - Considerations

- Visionary founder with technical credibility
- Utility impact could be substantial if the project advances
- Strong pitch and viral attention
- Leverages more than one private funding source = founder equity + angel investment

- No signed customers, team, or contractor bids
- Too early: speculative, undercapitalized, and unpermitted
- Risk of RLF being used for a first-dollar, not a final-dollar investment
- Public funds would be covering basic feasibility—not a ready gap
- No structural long-term commitment to the community – Lease allows 60-day exit providing zero site security

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Recommended Funding Strategy

Project	RLF Request	Recommended Allocation	Fund?
GridIron Works	$175K	$175K (Fully Fund)	Yes
Root & Rise Market	$75K	$75K (Fully Fund)	Yes
Ember Ceramics Studio	$85K	$42.5K (50% Fund)	Partial
NextVolt Composites	$210K	$0	No
TOTALS	$545K	$292.5K*	

Recommended Funding Strategy

- **Asterisk* - Recommended Allocation** of $292,500 does *NOT* include the other half of funds committed to Ember Ceramics if/when they meet their loan conditions. Must hold back the additional $42,500 now to ensure you can meet RLF's full promises to constituents.
- **Entire Allocation** (based on these terms): $335,000
- **Remaining RLF Capacity**: $165,000

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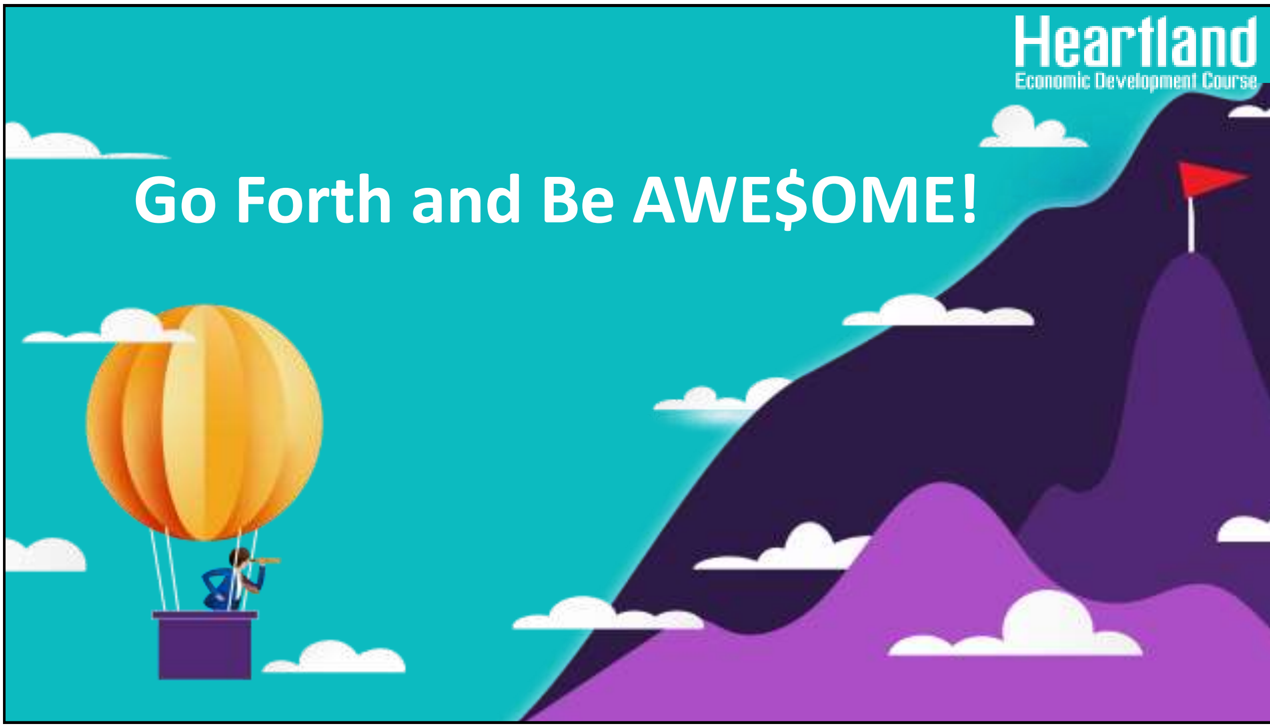
Finance Activity Wrap-Up Discussion

- Which project challenged your thinking the most—and why?
- How can public funds support, but not carry, private ventures?
- Were you provided enough information here to appropriately evaluate the 5Cs of Credit?
- How or where can you get training on economic development lending skills?
  - Build relationships with area lenders and other economic developers like Mark and Tracy
  - Ask the Heartland Economic Development Course team for referrals
  - Lending Skills trainers like Rebecca's Vault Consulting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Go Forth and Be AWE$OME!