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Debt and Equity Market Updates

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A New Take on NMTCs: Meet Lendistry's Small Business Loan Fund

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A lack of low-cost, nonpredatory capital is still a significant hurdle for underserved small and medium-sized businesses and our small business loan fund (SBLF) can help address that.

As a small business lender, community development financial institution, community development entity and capital provider, Lendistry is seeking solutions to the systemic barriers underserved borrowers face, and one practical avenue includes using Lendistry's new markets tax credit (NMTC) allocation to create an SBLF that provides below-market rate loans to disadvantaged small-business owners. It's a strategy that others can embrace.

The move comes after Lendistry significantly increased the dollar volume and number of transactions it deployed in 2020 and 2021 due to the COVID-19 global pandemic, which exposed historic disparities in capital deployment and allocation to diverse-led businesses and nonprofits.

An Impactful Product for Undercapitalized Businesses

While NMTCs are effective in spurring investment in disadvantaged communities, small businesses have a hard time accessing NMTCs because the loan capital they need is lower than most minimum NMTC thresholds. Transaction costs can be prohibitive and discourage small businesses with capital needs of less than $5 million from accessing NMTCs. An SBLF leveraging NMTCs makes a lot of sense for small businesses, allowing entities such as Lendistry to make below-market-rate loans to small businesses by leveraging the equity generated by NMTC allocation contained within the fund.

To the end user, this offering is just a loan. Because its complexities are behind the scenes, businesses can worry less about understanding all of the nuances involved with NMTCs and instead focus on their core competency–running a successful business.

The Lendistry SBLF has a specific approach: Lendistry will use 50% of its NMTC allocation to fund at least 50 innovative qualified low-income community investments in the form of debt through the NMTC SBLF, which is capitalized by Lendistry capital and NMTC equity. These loans will be made to small businesses and nonprofit organizations located in highly distressed areas that do not meet Lendistry's traditional underwriting standards.

The SBLF is an evergreen fund, meaning all repayments will be recycled continually. This will allow minority-owned businesses in low-income communities to fund their growth and expansion, including working capital, inventory and equipment purchases. The SBLF will satisfy several indicia of flexible or nontraditional rates and terms, including below-market rates, longer-than-standard period of interest-only payments, higher-than-standard loan-to-value, longer amortization periods, more flexible credit standards, nontraditional collateral and lower-than-standard debt-service coverage ratio.

A commitment to traditional nonbankable, disadvantaged businesses is a breakthrough in the NMTC market, especially in a pandemic-affected economic down market. Lendistry intends to recycle these small NMTC loans more than two times within the seven-year period to increase the impact of the NMTC subsidy to at least 100 businesses in critical need of capital. These businesses will include professional services, retail, restaurants, multiservice community organizations and other underserved businesses.

Overcoming Historic Market Challenges

Markets in America's inner cities and distressed rural areas possess enormous untapped economic potential. However, growing businesses in these communities are unlikely to attract the attention of venture capitalists who generally work within their existing relationships and communities. The smaller local venture funds that exist in some communities may have difficulty raising capital, developing deal flow, providing the requisite investment and management expertise, and managing the risks inherent in less diversified local economies. Greater distances required in rural areas often mean that capital providers may incur higher costs for travel and information.

That is even more true of businesses in isolated rural or inner-city communities that are cut off from mainstream business networks. In urban markets, information barriers may prevent investors and lenders from discovering and fully appreciating business opportunities.

Equity capital can provide small businesses with "patient" capital–capital that can be used to grow a business before a return on the funds is due to the investor. A healthy equity capital base in a business relieves some short-term cash flow pressures, allowing the firm room to innovate and introduce new products, cultivate new sales leads and hire and train new staff. In addition, equity capital can increase a small business's creditworthiness, which can lower its cost of financing and make it better enable it to leverage additional sources of financing. Finally, an equity cushion helps a firm absorb unforeseen setbacks and weather temporary economic downturns.

The SBLF at Lendistry has already funded several businesses with many more in the pipeline. Some examples include a Black-owned paper company in Pennsylvania, a brewery in Fresno, California, and a community co-manufacturing workspace in Chicago.

We encourage other lenders to join in the mission to push innovation in the financial industry to meet the needs of the fast-evolving small business ecosystem. ❖

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