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Identifying and Retaining High Growth Small Businesses during their “Awkward Teenage Years”

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Matt Scarborough and Bridgeforce

- Started in banking after finishing grad school in the 90's
- Founded or joined early three different businesses, two of which grew enough to experience the transitions we'll talk about, and I informally advise several entrepreneurs
- Bridgeforce:
 - We are a highly-specialized consulting firm that focused fully upon consumer and small business banking while employing a different model than most: the vast majority of our team was in the industry for a decade or two before joining us
 - We have gone through these transitions ourselves
- So we are going to start by thinking about this process from the entrepreneur's perspective and then transition to the banks' perspective

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Stages of small business life



- As the title of this presentation implies, we use analogies to human development as we discuss stages of Small Business life (and how different businesses go through stages differently)
- How to identify those stages as their lender
- What to do about it

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Planning stages – the beginning



- The early stages (pre-teenage)
 - During the planning stages we are all relatively rational but with a strong emotional component:
 - There is of course a sense of the importance and seriousness of the decisions about to be made
 - For those who go forward with it, there is also frequently a sense that this is what we are supposed to do at an emotional level: many people feel a pull to parenthood, and many people feel a pull to entrepreneurship (and they are related through the joy of creation)
 - Developing plans, understanding the market, and thinking about the resources needed (people, product, financial, etc.)
 - Formal debt financing is limited at this point
 - Owner(s) may take out debt against personal assets
 - Equity investments from friends & family, others (perhaps introduced through lawyers or accountants)
 - Growing movement and options for crowdfunding (the kick-starters of the world)
 - At this point, the entrepreneur is in information-gathering/planning

mode, and if you have relevant solutions then you have a chance to get some mindspace, but historically banks are not very relevant yet at this stage

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Birth and infancy – existence and survival



- You've now stepped onto the roller coaster
- You are sleep-deprived, your friends are all saying "Aren't you glad you did this?" and while you are supposed to say yes, the reality is that you are saying to yourself "I think it will be ok, but no book can prepare me for this and I'm pretty stressed out."
- You are certainly paying attention to cash flows, but you don't know what you don't know yet and this would be a very difficult time for a bank to get your attention (unless you are in a cash crisis and need a loan, in which case you likely do not fit a traditional lending risk profile)
- At this point, the business is highly likely to continue with whatever relationships it has unless a major exogenous event forces a change
 - Recent NFIB survey showed financing and interest rates as the top concern of only 2% of small business.

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Teenage years – success and...



If all went well, you went through a fairly blissful period for a little while

- You are sleeping through the night
- You are feeling like “We’ve done a good job – this is great.”

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...transition



- Then the teenage years hit
 - Lots of great new possibilities are opening, but
 - Lots of transition becomes necessary, which is scary
- For the entrepreneur, you may no longer be
 - The lead sales person
 - Knowledgeable of every last detail of your business
 - The person signing all of the checks
 - The person signing all agreements
- You are now building processes to enable reliability that is not dependent upon any one specific individual – building for durability
- This time of transition is a time of risk and opportunity for the bank (and all other vendors) – you can get the entrepreneur's attention again, but they will act based upon what they see.

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- A few more key things to consider regarding the mindset of the small business owner¹
 - Optimism: 63% expect revenues to rise in the next 12 months
 - Dedication: 67% say that they would reduce or delay their own compensation
 - Majority work over 50 hours per week
 - Leveraging social media

¹Bank of America Small Business Owners' Report 2015



Over one in three (and nearly half of Gen-X and Millennial respondents) says that social media has provided feedback that has prompted a change in business.

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Identifying these stages as a lender...



Marketing

Underwriting

Renewals

How much do you learn about each small business' growth plans, and what do you do with that information? How do you stay in touch with those plans?

It starts with thinking about the sorts of information you would like to have, and what you might do with it. Perhaps use some illustrative examples:

- fast-casual BBQ (single location vs. starting a franchise),
- professional services (small number of professionals forever vs. plans to become global),
- small manufacturing (machine shop vs. producer of designs for 3D printing)

“Given where you are and what you are trying to accomplish, are you having challenges with...?” vs. “what banking products do you have or need?”

Then, start to think about how to capture that information:

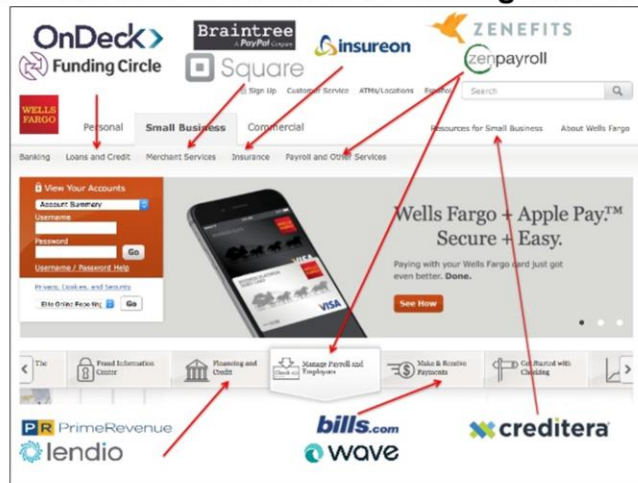
- Directly from the entrepreneurs (through application and renewal, but

also through their transactional data)

- Various lead/referral sources (and the greatly different mix that comes from each)
- Data for purchase

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...while lots of others are focusing here too



Created by RRE Ventures



Funding for small businesses has long come from many sources, with banks providing perhaps half of the total, but now there are new entrants being added to the mix.

In many cases those entrants are aimed at small businesses before their teenage years, but others (like Forex services) are quite relevant.

What are the barriers that prevent banks from serving 100%?

- Risk tolerance (affects debt/equity tradeoffs plus the acceptable risk levels for debt)
- Awareness
- Other? – what prevents them from helping with finding equity financing (perhaps through their wealth management arms)?

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So What Should We Do?

- Focus on the customer experience
 - Speed matters – Lots
 - So do paperwork requirements
- Be the trusted advisor
 - Mean it
 - Address the P&L implications
- Help their evolution
 - Controls over spending
 - Forex and cash management



We've been doing instant decisions in consumer since the 1990's. What about small business?

Actively search for ridiculous paperwork requirements – my favorite example from personal experience was needing to provide two separate Board resolutions to get online banking access and to be able to move funds.

Be the trusted advisor – do not lead with products (about you, not them) lead with understanding their business (about them, not you). This requires spending at least a few minutes to do research on their business and their sector.

Controls over spending: help me to avoid being the one signing every check while also being confident that we have the right controls in place. Handing over signing authority scary – emotionally like handing car keys to a teenager – and having the right bank systems and reporting to work with is very helpful.

Forex – According to UPS (“Perceptions of Global Trade” survey), 24% of small businesses are engaged in exports, and according to the Census Department 35% of US exports are done by small to medium enterprises. This

is a non-trivial minority, and it is expected to grow.

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The Key Point:

- During the transition of the “teenage” years you are more likely to get the entrepreneur’s focused attention
- Think about it from their perspective and make sure that they like what they see



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