Your Guide to Short-Term Financing

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What is short-term financing?

Short-Term Financing includes financing with terms less than 24 months.

In this eBook, we're going to focus on short-term financing with payback terms from three months to one year.

Whether it's a term loan or a line of credit, the best use case for a short-term loan is for projects where the business need has a clear short-term ROI.

Traditional lenders, such as banks, do not typically offer short-term small business loans. Online lenders, like OnDeck, offer short-term loans and lines of credit to meet a variety of small business use cases. Some business owners, especially those with long-standing relationships with their banks, sometimes have questions about short-term loans.

With that in mind, here is a brief explanation of typical use cases for successfully leveraging short-term financing for your business.

What business needs are a good fit for short-term financing?

The first question you should ask yourself when you begin the process of securing financing for your business is: **what is your business need?** Your answer to this question will determine what type of financing and loan term is appropriate for your business. Do you need the funds quickly? Do you need the funds for a project that will capture additional ROI in a short period of time? Different types of financing are appropriate for different business needs.

Most Common Reasons for Seeking Business Loans*

54%
Equipment Purchase

&

51%
Inventory Purchases

Examples of business needs for short-term financing to fuel growth or increase ROI are: a physical expansion or renovation, hiring a new employee, buying inventory quickly, or purchasing equipment. These and similar initiatives can help your business growth long term, and generally provide realized gains fairly quickly. The loan term should match the useful life of the asset just as you wouldn't take a 30-year auto loan for your car, even if the payments were smaller.

Would you want to take out a long-term loan and continue to pay for that business case over time if its business use is realized in the near future?

*Source: Electronic Transactions Association 2016

Example

Real businesses that used short-term financing to their advantage.

Expansion & Renovation

Jungyae Martial Arts

$50,000 borrowed over a 9 month term

With the help of OnDeck, Michael was able to snatch up a prime location and turn it into the full-service martial arts academy it is today. And thanks to additional financing from OnDeck, he's able to offer a variety of new programs for the active community of Kirkland, WA.

Marketing

The Juice Cellar

$15,000 borrowed over a 6 month term

"I increased my customers by 15% from a radio campaign I paid for using my loan from OnDeck."

Purchasing Equipment

Lowery Smiles

$10,000 borrowed over a 9 month term

With her funds, Dr. Lowery was able to make a major equipment purchase that better serves her patients and keeps her practice on the cutting edge. She was also able to hire new employees, and is looking to expand her practice

.

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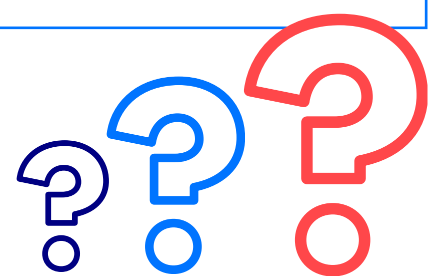
What costs make sense? APR vs. Cents on the Dollar

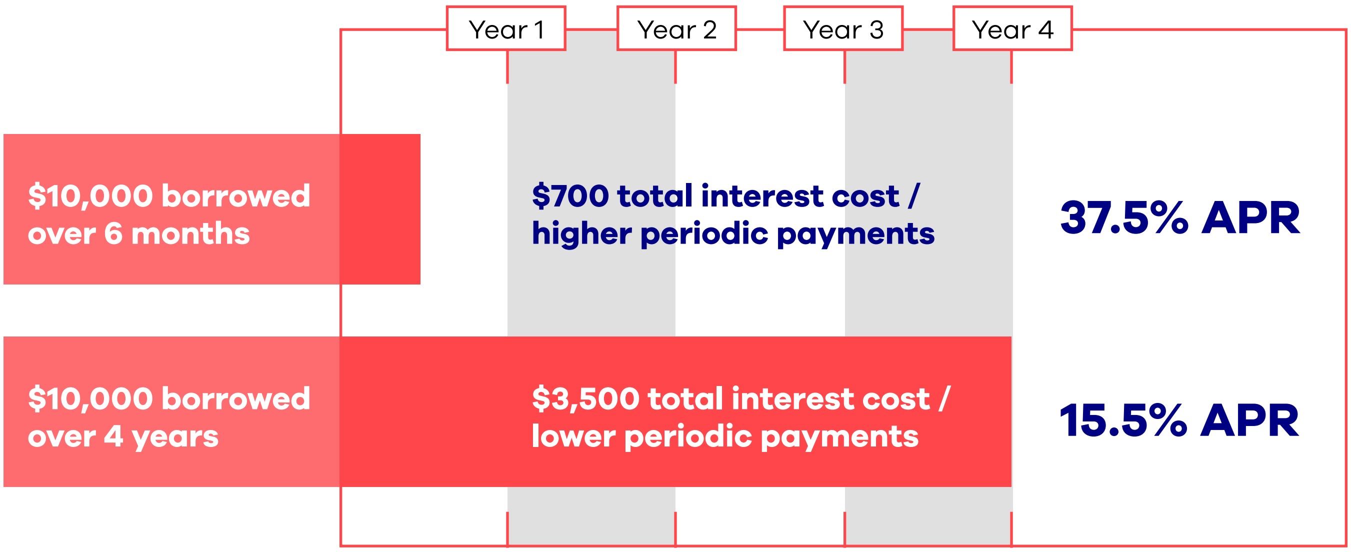
Annual Percentage Rate (APR) is only one way to compare your financing options and doesn't represent the total cost of a small business loan. In many cases, the APR of a short-term loan can be much higher than the APR for a longer-term loan. But when you consider other factors, such as total cost of the loan and your business need, you can see a short-term loan could be a better fit for your business. As you see in the above example, the shorter-term loan has a higher APR, but a lower overall cost than the longer-term loan with the lower APR.

Let's run some numbers to illustrate the point.

Which would you prefer?	**37.5% APR**	**OR**	**15.5% APR**
What about?	**$700 interest cost**	**OR**	**$3,500 interest cost**



It really depends on the term length of your loan:



Another metric to consider is the overlap between your periodic payments and the returns on your investment.

For example: If you are planning to use your loan to make an equipment purchase, then the equipment you buy might start generating returns immediately. In that case, consider comparing your daily or weekly payment on the loan to the daily or weekly income your investment will generate. That difference represents your net gain from the investment in the short-run.

Paying down your loan quickly allows you to see your ROI faster, like the example on the next page.

Calculating ROI

Time Is Money

Traditional lenders, like banks, can take weeks to process your business loan application and for you to receive the funds. Short-term online lenders, like OnDeck, often have an answer to your loan application in under an hour and funds in your account as quickly as the next business day. The Federal Reserve Bank of New York reports it takes the average small business owner **33 hours** to apply for a loan at the bank.

How much do you value your time?

The average business owner thinks their time is worth $170/hr*

Considering ROI When You Borrow

For short-term loans with a defined ROI target, APR might not be as important a metric as the total cost of the loan relative to the return on investment. Particularly when purchasing inventory or equipment, the total cost of financing might be a relevant number when calculating ROI.

Considering the total cost of financing, in addition to APR, when calculating ROI can be a good way to determine if the financing being considered will help meet the ROI objective or become too expensive—even with a lower periodic payment or lower APR.

**Source: Electronic Transactions Association 2016*

Example
Calculating ROI

Let's make it simple:

Example A

If you plan to purchase new equipment and that will yield you $5 for every $1 spent over the course of its lifetime, short-term borrowing could make sense.

Example B

If you have the opportunity to purchase discounted inventory in bulk, you may receive a 70% discount on the inventory. Even if the cost of the loan reduced that discount down to 55% it could still make sense to borrow to capture the extra profits.

Some business owners are concerned the with higher periodic payments often associated with a short-term loan. If your business has the cash flow to sustain the payments, the lower total dollar cost of capital can be cheaper, in the long run, with a short-term loan. Even if the term loan has a lower periodic payment or a lower APR.

Remember

Match your loan term to the useful life of the asset you are purchasing.

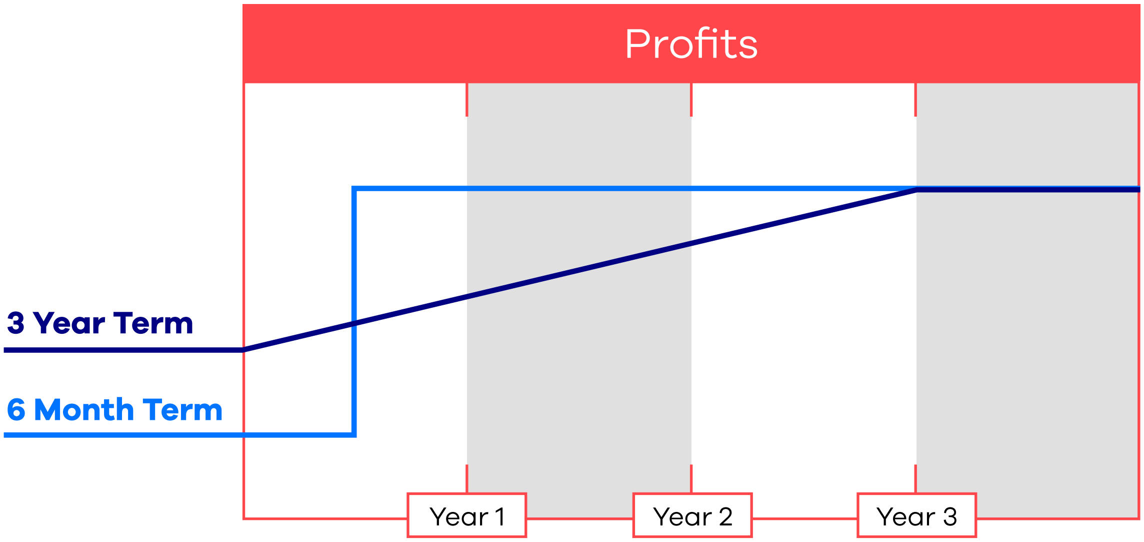
If you're turning over the inventory in six months, it might not make sense to borrow the funds over a four-year term.

Example

How Can a Short-Term Loan Affect My Cash Flow?

A laundromat buys 10 new washing machines.

From the day they install the new machines, they generate $540 per day ($3 per cycle, 180 cycles per day). If they bought the machines with a 6-month loan for $10,000 at 1.19 Cents on the Dollar (CoD), their daily payment would be $95/day. So, over the short-term, their net gain would be $540-$95 (minus the cost of the water and electricity to run the machines).



Once they've made all 126 payments they get to keep all $540 (minus utilities) for the remaining lifetime of the machines. That might be more appealing to some business owners than a loan with a longer payback, because they might be willing to take a short-term hit in exchange for a greater ROI, faster.

57%

of small businesses choose a shorter-term higher-APR loan over a longer-term lower-APR loan in order to minimize total fees & expenses*

**Source: Electronic Transactions Association 2016*

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Choosing The Right Lender

When it's time for you to make a decision on choosing a lender, there are some things you should consider.

Transparency

The first and most important issue is **transparency**. If the lender you're speaking with is not forthcoming regarding their rates, fees, and Terms & Conditions, you should look for another lender. If the lender has nothing to hide from you, they will most likely not hide it.

- **Fees**
- **Rates**
- **Terms & Conditions**

SMARTBox®

A growing group of lenders are utilizing the SMARTBox®, a tool developed by a coalition of online lenders, a non-profit, along with an industry trade group, including OnDeck. The SMARTBox® was developed to make it easier to understand and compare different loans, different loan types, and different terms, to help you make the best financing decision for your business. If a lender is part of the SMART Coalition, the box will appear on your loan offer enabling you to make a true apples to apples comparison of your loan amount, terms, rates, fees, and the total cost of your loan.

SMARTBOX™

Capital Comparison Tool

Next:

We'll tell you what questions you should be asking.

Regardless of the lender you choose, here are some questions you should ask yourself:

Q: What do I need the money for?

Why? Knowing the business need for the funding will help you with is the most important step in your search for financing. The answer to this question will help the lender get you the right offer, as well as help you make the best financing decision for your business.

Q: How much money do I really need?

Why? Know the actual amount of funds you need. There are costs associated with borrowing, so borrowing more than you really need can become very expensive. What's more, not every lender will offer you the full amount you request, and if you have good credit, some lenders may offer you too much.

Q: How quickly do I need the money?

Why? Do you need the money tomorrow, this week, or next month? The time frame in which you need the funds can drastically cut or shape the options that work for your business.

continued...

Regardless of the lender you choose, here are some questions you should be asking yourself:

Q: What types of financing can I qualify for?

Why? Your personal credit score, business credit profile, cash flow, time in business, annual revenue, and several other factors are all considered by lenders to determine the funds and terms you will qualify for. Know the minimum requirements for each lender before you put in an application. That way, you won't waste your time applying with lenders that won't work with your business.

Q: Do I have all the information I need to make a decision?

Why? The simplest way to know you're getting the best financing for your business is to have all of the information beforehand. Do your research, so you spend your time applying with lenders who will lend to you and will meet your business needs.

Click here to find out more about short term financing with OnDeck.