LEVERAGED LOAN AGREEMENTS

HELPING SMALL BUSINESS GROW

Western Economic Diversification Canada (WD) partners with financial institutions on leveraged loan agreements designed to start businesses and help them grow.

These loan programs target industry sectors important to Western Canada and provide flexible debt capital on terms suited to the unique needs and cash flow requirements of small businesses. The loan programs are provided on commercial terms by financial institutions, such as credit unions, trust companies and the Business Development Bank of Canada. Each lending institution funds its own program and makes the decision on all loan approvals.

By providing a "loan loss support contribution" that shares the higher risks associated with eligible loans, WD enables these financial institutions to supply loan capital to clients who would not otherwise have access to funding.

Leveraging private sector investment

The leverage ratio reflects the relative risk of the specific target of the loan agreement. For example, the Knowledge and Growth Loan Agreements vary between 5 and 10 to 1 ratio of financial institution funds to WD funds while the Urban Micro-Loan Agreements have a 5 or 6 to 1 ratio. In other words, the financial institution provides $5 to $10 for every dollar provided by WD.

In many cases, the loans provided under this program are part of a larger financing package that can include other equity and debt capital investment. As a result, the true private capital leveraged can be considerably greater than the loss reserve direct leverage ratio.

Increasing the capital available to small business

For every loan disbursed to a client, WD makes a loss support contribution at the negotiated rate. This rate is usually between 10 and 20 per cent of the value of the loan. As more loans are made, the loss support contribution grows in size.

Individual loan losses are shared between WD's loss support contribution and the financial institution at a negotiated rate, but the financial institution's share is generally at least 20 per cent of any loss. At the end of the agreement, any contribution exceeding WD’s share of losses is returned to WD.

Interest rates charged by the financial institutions are higher than prime because of the higher risk factors associated with targeted sectors of the economy. These higher interest rates help ensure the program only benefits companies unable to qualify for traditional loans.

Analyzing results to date

From June 1995, when the first loan agreement was implemented, to March 2006, 43 loan agreements were established, involving 20 separate capital providers.

During this time, 2,862 loans totaling over $218 million were approved. Only $33 million from WD leveraged the $218 million in loans.

The micro-loan agreements established with credit unions are doing extremely well. They provided 1995 loans averaging about $13,000 and totaling $26.6 million. These loans are made to very small and start-up businesses, with insufficient assets and credit history to obtain traditional financing. The program has also had success in helping to develop knowledge/technology-based, conservation and agricultural value-added companies. Loan agreements targeting these industry sectors are responsible for over $165 million in loans, averaging $340,000 per loan.

For more information on WD-sponsored loan programs, call WD at 1 888 338-WEST (9378) or visit www.wd.gc.ca/finance/xnetwork_e.asp.