COMPETITORS WITH LIMITED PRODUCTS

There are several financial firms that compete with or complement banks, but with a narrower range of products.

Commercial finance companies

Operating within the larger group called "asset-based lenders," commercial finance companies specialize in making working capital or investment capital loans to small businesses secured by accounts receivable, inventory or, on occasion, equipment. These firms can compete with banks to provide working capital financing, but can also complement bank financing where increased risk is present.

Asset-based lenders make loans based primarily on the value of the assets or collateral the borrower agrees to pledge, instead of financial condition of the company. Asset-based lending can include dealer floor plans (secured by inventory) and some leasing arrangements.

Collateral for commercial finance loans usually is monitored daily or weekly, and this extra handling, on top of additional risk, results in pricing that is generally higher than what is charged by banks. The specialized nature of getting updates on accounts receivable and inventory, plus staffing to make periodic collateral audits, makes this a difficult financing package for community banks to offer. Nevertheless, banks can partner with commercial finance companies in situations where the customer needs a permanent working capital line of credit. The commercial finance company can provide the line of credit, while the bank retains various deposit accounts and other types of loans, such as term loans for equipment. This type of arrangement is particularly useful when lending to a rapidly growing business. In addition to independent commercial finance companies, many larger banks may have separate commercial finance subsidiaries.

Factoring

Another way to support working capital needs for growing or young firms is via factoring—where accounts receivable are sold at a discount to a factor, which then assumes the credit risk of the account debtors, and receives cash as the debtors pay. The factor makes a profit by collecting the full amount due or more than the discounted purchase price paid for the accounts. Factoring is prevalent in some industries such a garment and textile manufacturing. The financial condition of the business selling the accounts is not a key issue, and the focus of the factor (purchaser) is the credit quality of the account debtors. The factor can determine to whom and for how much total exposure a business can make sales, and essentially become the credit department of the business.

Commercial sales or "captive" finance companies

Finance companies tied to large manufacturer's industrial or agricultural equipment and compete with banks for term loans and sometimes provide lease financing. These firms can make direct equipment loans and leases, or can support a dealer by purchasing loans or leases made by the dealer. These firms attempt to support the sales of the manufacturer and often have sources of funding that are different from bank funding. Subsequently, they can offer competitive terms such as 100 percent financing, a lower interest rate, or longer amortization period than typically offered by a community bank. In consumer banking, similar firms dominate the financing of automobiles.

Credit card issuers

Many credit card issuers offer business lines of credit that can be used for any type of purchase. Although the interest rates may be high compared to a bank loan, the convenience of a one-time application for credit has value to the small business owner.

In recent years, business credit card marketing has intensified, with programs offering new levels of information, such as categorized spending summaries and improved spending control. Cards can be restricted to selected employees, with customized limits put on the types of transactions, dollar amounts and participating merchants.

Both Visa International and MasterCard International have launched separate divisions for the following types of cards:

- Corporate—travel and entertainment cards issued to very large companies, and they are similar in concept to cards issued for years by American Express and Diners Club International
- Business—targeted at smaller businesses, generally less than $10 million in annual sales or fewer than 100 employees. The cards are designed to offer discounted rates on hotels and insurance programs worldwide, rates these businesses could not get on their own. Many start-up businesses use these cards or personal cards for some of their initial financing
- Purchasing—sometimes known as procurement cards, are designed to save companies time, offer them better control over minor purchases, and provide them with better record keeping

Banks—even community banks—can serve as issuers of these cards, although larger banks tend to dominate this area.

Leasing companies

Leasing companies are a major source of credit for financing equipment for businesses. Leasing is an attractive alternative because the initial capital outlay is often smaller, and there may be tax benefits to deducting the full lease payments versus deducting depreciation and only the interest expense portion of the loan payments. Also, equipment with quickly changing technology is often leased. Companies with rapid growth can choose to lease equipment in order to use their capital to fund the growth rather than down payments on equipment. Many large banks have leasing company subsidiaries.

Life insurance companies

Non-recourse (no personal guarantee), long-term, fixed-rate financing for large commercial real estate (CRE) projects has been provided for many years by life insurance companies. Life insurance companies are more of a competitor for larger banks than for community banks. The general terms provided by life insurers are usually more favorable than those offered by banks. Within the last decade, commercial mortgage-backed securities (CMBS) have become the largest provider of financing for large CRE projects. In consumer finance, property and casualty insurers have become more active in automobile finance.