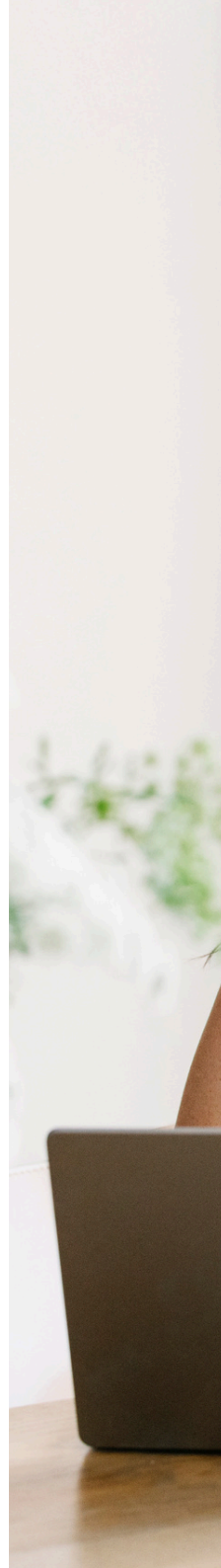


Finance to match
your business ambitions.



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Introduction to business loans

If you are an entrepreneur with a promising idea, a small business owner looking to expand, or simply seeking the financial fuel to propel your venture forward, understanding business loans is essential.

This guide is your compass in the vast landscape of business financing. We understand that the idea of applying for a business loan can feel like a big deal, with terms you might not know and important decisions that can really impact your company's future. That is why we have created this guide.

Whether you are thinking about a short-term line of credit to manage cash flow or a long-term loan to invest in equipment, this guide will provide you with the foundational understanding you need to make informed decisions.



Why would I need a business loan?

While the idea of taking on debt might seem like a big step, business loans are often a vital and smart tool for growth, stability and taking hold of opportunities for businesses of all sizes.

Here are some key times when a business loan can be helpful:

- **Funding startup costs:** Launching a new business needs a good upfront investment. Loans can provide the necessary money to cover initial expenses like buying equipment, getting inventory, making improvements to a leased space, marketing campaigns and initial running costs until you have consistent income coming in. It can help you get the business off the ground.
- **Managing working capital gaps:** Businesses often have ups and downs in cash flow. There might be times when expenses are more than the money coming in, creating a temporary shortage of working capital – the funds you have for day-to-day operations. Short-term loans like lines of credit or invoice financing can bridge these gaps, making sure your business can keep meeting its commitments (like paying suppliers and salaries) until money from customers comes in.
- **Expanding operations and growth initiatives:** Once a business is up and running, often the next step is to grow it. This could mean opening new locations, expanding products or services, entering new markets or making more of what you sell. Business loans can provide the necessary money to fund these expansion efforts, helping your business take advantage of growth opportunities that might otherwise be out of reach.
- **Purchasing equipment and assets:** Investing in new or upgraded equipment, machinery, vehicles or even real estate can help to boost your business's efficiency, productivity and long-term value. Business loans specifically designed for buying assets (like equipment financing or commercial mortgages) can make these important investments achievable.



- **Refinancing existing debt:**
Sometimes, a business might take out a new loan to pay off existing debt that has less favourable terms (for example, higher interest rates or shorter repayment periods). Refinancing can improve your cash flow, reduce overall interest costs or simplify managing your debt.
- **Acquiring another business:**
For businesses looking to grow by buying another company, loans can provide the substantial money needed to purchase an existing business. This can be a faster way to expand and grow your share of the market.
- **Navigating seasonal fluctuations:**
Businesses with income that changes with the seasons might have periods of low income followed by high income. Loans can help smooth out these changes, providing the necessary funds to cover expenses during quieter months until the busy season arrives.
- **Taking advantage of time-sensitive opportunities:**
Sometimes, unexpected opportunities come up that need money right away, such as buying inventory at a big discount or investing in a promising new technology. A readily available line of credit or a quickly approved loan can help your business make the most of these.

In essence, a business loan can act as a smart financial tool, providing the necessary money to overcome financial hurdles, take hold of growth opportunities and ultimately contribute to the long-term success and sustainability of your business.

However, it is important to remember that taking on debt is a significant decision that requires careful thought about your business's financial health, your ability to repay and the terms of the loan agreement, which we will look at in this guide.





Business finance glossary

- **Amortisation:**
The process of gradually reducing the value of assets like goodwill and intellectual property over a period of time.
- **Balloon payment:**
A final, large lump sum due at the end of the loan term. Loans with larger balloon payments often have lower regular payments.
- **Chattel mortgage:**
This gives your business immediate ownership of an asset, but you make regular payments. It often has the flexibility of a final 'balloon' payment to reduce regular costs.
- **Comparison rate:**
The comparison rate shows the total cost of credit, including interest charges and other specific credit fees and charges related to the loan.
- **Secured loans:**
These loans require you to provide something as security, like property or business assets. This often leads to lower interest rates and higher borrowing limits.
- **Unsecured loans:**
These loans do not require collateral. Lenders look at your business's creditworthiness and cash flow to decide if you can get one. They often have higher interest rates because there is more risk for the lender.

Types of business loans



There is not a one-size-fits-all when it comes to business loans. Depending on your financial position and goals, the type of loan you choose will vary.

In this chapter, we will break down the types of business loans most commonly available in Australia.

- **Term loans:** These are traditional loans where your business borrows a lump sum and pays it back over a set period with interest. They can be secured or unsecured and are used for various purposes like expanding, buying equipment or for everyday working capital.
- **Equipment finance (chattel mortgage):** This is specifically designed for buying business assets like vehicles, machinery or equipment. The asset itself often acts as security for the loan.

A term business loan offers the benefit of predictable payments and a structured repayment schedule with a clear end date, making budgeting straightforward. It is versatile, allowing you to fund various business needs, and can potentially come with lower interest rates compared to some other loan types. However, the repayment schedule is less flexible, and interest costs will add up over the entire loan term.

Also, eligibility requirements can be strict and the loan might need security depending on the lender and the specific agreement.

Equipment financing offers the benefit of immediate asset ownership and, because it is a secured loan using the equipment itself, it can be easier to qualify for than unsecured options. Your business could also potentially benefit from tax deductions on interest and depreciation (speak to your accountant about this). Repayment structures can be flexible, sometimes including a final balloon payment. However, the equipment acts as security and can be repossessed if you do not make your payments. You are responsible for ongoing maintenance costs, and the risk of the asset losing value over time is with your business.

Lastly, a potential balloon payment at the end of the term can be a significant financial hurdle.



- **Invoice finance:** This allows businesses to get funds based on their outstanding invoices. A lender might advance a percentage of the invoice value, which can really help with cash flow.
- **Business overdraft:** This is a flexible line of credit linked to your business transaction account. It allows businesses to withdraw funds up to a certain limit when needed, covering short-term cash flow gaps. Interest is typically charged only on the amount you use.

Invoice finance is often flexible, growing as your sales grow. This can help you grow faster and reduce reliance on traditional loans by using your sales ledger as a form of security. However, it can be more expensive due to fees and interest charged on the advanced funds. There is also a potential impact on customer relationships if the lender handles collecting payments.

Plus, it is not suitable for all businesses, especially those with inconsistent invoicing, and understanding the potentially complex fee structures is essential.

A business overdraft can be cost-effective for short-term needs as interest is usually only charged on the amount you use. It is also often easy to set up, often linked to existing business transaction accounts, and is particularly good for bridging temporary cash flow gaps. However, it can become expensive for long-term use due to potentially higher interest rates than term loans, and these rates can change as they are often variable, depending on the lender.

Furthermore, an overdraft facility can be called back by the lender, making it an unreliable long-term funding source, and various fees may apply for setting it up and using it.



What documentation is *needed*?

Depending on your business structure, needs and the lender you choose, the documentation you will need will vary.

- **Full doc loan:** A full doc loan (full documentation loan) is a type of loan where you need to provide comprehensive financial documentation to the lender to confirm your income, assets and financial stability. This is different from "low doc" or "no doc" loans, which need less paperwork but typically come with higher interest rates to balance the increased risk for the lender.

Here is a breakdown of what a full doc loan can involve in Australia:

- **Extensive documentation:** You will need to provide a range of documents to prove your financial situation.
- **Lower interest rates:** Because of the thorough checking process, full doc loans often come with more competitive interest rates compared to low doc options.
- **Higher borrowing power:** Lenders have a clearer understanding of your ability to repay, potentially allowing for larger loan amounts.
- **More favourable terms:** Generally, full doc loans may offer more flexible repayment options and other helpful terms.
- **Longer approval process:** The detailed checking process can sometimes mean it takes a bit longer for loan approval compared to loans with less paperwork.



- **Low doc loan:** A low doc business loan (low documentation business loan) is a type of financing designed for business owners who might not have all the extensive financial records typically required for a traditional business loan.

This is often the case for:

- **Self-employed individuals and sole traders:** They might not have the same formal financial statements as larger companies.
- **New businesses or startups:** They may not have a long financial history yet.
- **Small businesses with fluctuating income:** Their earnings might not show a consistent pattern over the past few years.



Instead of relying heavily on years of tax returns and detailed financial statements, low doc loans typically use other ways to assess your ability to repay. These methods can include:

- **Bank statements:** Showing recent cash flow and account activity.
- **Business Activity Statements (BAS):** Providing evidence of sales and GST collected.
- **Accountant's letter:** A declaration from your accountant confirming your income.
- **Asset declarations:** Listing business and personal assets.
- **Revenue verification:** Focusing on current sales and income.



- **No doc loan:** A no doc loan (no documentation loan) takes the idea of less paperwork even further than a low doc loan. As the name suggests, it aims to provide business financing with minimal to no traditional financial documentation required from you. No doc business loans may offer/require:
 - **Extremely limited paperwork:** You typically do not need to provide tax returns, detailed financial statements or extensive proof of income.
 - **Very fast approval times:** Because there is no in-depth financial review, approvals can often be obtained very quickly, sometimes within 24 to 48 hours.
 - **Highest interest rates and fees:** No doc loans are considered the riskiest for lenders because there is no traditional financial checking. As a result, they come with significantly higher interest rates and fees compared to both traditional and low doc loans.
 - **Short repayment terms:** Loan terms are usually very short, often ranging from a few months up to a year. This means you need a quick repayment strategy.
 - **Strong emphasis on security/collateral:** Lenders heavily rely on tangible assets, primarily property (commercial or residential), to secure the loan and reduce their risk. The loan amount is often determined by the equity in the property.
 - **Income declaration:** While formal income proof is not required, you may still need to declare your ability to repay the loan.

The lender's main focus is on the value and how easily the security property can be sold, and your plan to repay the loan (your "exit strategy," such as selling the property or getting other financing). Traditional banks and credit unions are less likely to offer true no doc loans due to their rules and risk management policies. Private lenders and specialised finance companies are the more common sources.

In Australia, no doc loans used for business or investment purposes may not be covered by consumer credit protection laws. This means fewer regulations and potentially higher risks for you.





The broker advantage



In the past, you might have gone straight to your bank manager for a business loan, but times have changed.

Choosing a business loan broker can offer some significant advantages compared to directly approaching banks and other lenders.

1. Access to a wider range of lenders and loan products:

- **More options:** Brokers have established relationships with a diverse group of lenders, including major banks, credit unions, online lenders and niche financiers. This gives you access to a broad range of loan products and terms.
- **Specialised lenders:** Brokers often work with lenders who specialise in specific industries or types of financing, increasing your chances of finding a loan tailored to your unique business needs (for example: equipment finance, invoice finance, commercial property loans). Whatever your industry, you will have specific needs, and a broker can find you a suitable loan plan from the right lender.

2. Saves you time and effort:

- **Streamlined process:** Applying for loans can take a lot of time, involving research, preparing applications and talking with many lenders. A broker handles much of this work for you.
- **One point of contact:** Instead of dealing with several different lenders, you work with a single broker who manages the process on your behalf.
- **Potentially faster turnaround:** Brokers understand the application processes and requirements of various lenders, potentially speeding up the approval process.



3. Expertise and guidance:

- **Market knowledge:** Brokers have in-depth knowledge of the current lending market, interest rates and available products. They can provide valuable insights and advice to help you make informed decisions.
- **Matching you with the right lender:** Brokers understand what different lenders are looking for and can match you with those who are more likely to approve your application based on your business profile.
- **Understanding lender criteria:** Brokers know what different lenders are looking for in an applicant and can help you put together a stronger application.
- **Navigating complexity:** The world of business finance can be complex. Brokers can simplify the jargon and guide you through the details of loan agreements.

4. Potential for better rates and terms:

- **Negotiating power:** Experienced brokers often have strong relationships with lenders and can negotiate interest rates, fees and repayment terms on your behalf, potentially securing a better deal than you could get on your own.
- **Access to broker-specific deals:** Some lenders offer exclusive rates or products to brokers.

5. Ongoing support:

- **Long-term relationship:** A good broker can become a trusted adviser for your business's future financing needs, helping with refinancing or securing additional funding as your business grows.

6 tips

to keep on top of your loan repayments



Understand your loan terms inside and out:

Be very familiar with the specifics of your business loan. This includes knowing whether your interest rate is fixed or variable and how it is calculated. Understand how changes in market rates could impact your repayments. Importantly, be clear on the due dates, how often you need to pay (monthly, bi-weekly, etc.) and the exact amount needed for each payment. Note the total length of your loan term.

Finally, be aware of any fees or penalties for late payments or paying off your loan early, and understand if you can make extra payments without penalty.



Create a robust repayment plan and budget:

Include your loan repayments as a top priority expense within your business's monthly budget. Make sure you set aside enough funds each period to cover the full payment amount every time. Regularly project your business's incoming and outgoing cash to anticipate any periods where cash flow might be tight.

This proactive approach will allow you to plan for loan repayments ahead of time. It is also helpful to set up a dedicated loan repayment schedule, outlining all payment dates and amounts in a calendar or spreadsheet that you can easily access for consistent tracking.



Implement effective payment strategies:

Make your repayment process smoother by setting up automatic payments from your business bank account directly to the lender. This simple step significantly reduces the risk of missed payments and the related late fees. If your business has predictable income cycles, try to align your loan repayment due dates with these periods to ensure funds are readily available.

You can also explore the possibility of making smaller, more frequent payments (for example, fortnightly instead of monthly) if your cash flow allows. This can speed up how quickly you pay down the main loan amount and reduce the total interest paid over the loan's life, but always check with your lender if this option is available.



Proactive financial management:

Keep a close watch on your business's financial health by regularly monitoring cash flow. Tracking income and expenses will help you spot potential financial challenges early. Build a strong cash reserve or emergency fund to provide a financial cushion against unexpected costs or temporary dips in income, protecting your ability to meet loan obligations. Aim for a reserve that covers at least 3 to 6 months of operating expenses.

Regularly review and adjust your budget as your business grows, making sure loan repayments remain a high priority in your updated financial plan.

If you expect or experience cash flow difficulties, proactively identify and cut non-essential expenses to ensure loan payments are covered. Finally, optimise your accounts receivable processes through efficient invoicing and diligent follow up on outstanding payments to improve cash flow and your ability to make timely loan repayments. Consider offering incentives for early customer payments.

**Communication is key:**

Keep open lines of communication with your lender. If you think you might have any difficulties making a scheduled payment, reach out to them straight away. Do not wait until a payment has already been missed.

Lenders may be willing to work with you on temporary solutions such as deferred payments or loan restructuring, especially if you have a good repayment history.

When you communicate, be honest and open about your situation, clearly explaining the reasons for the potential difficulty and your proposed plan to get back on track with repayments.

**Explore options if you are struggling:**

If your business faces significant challenges in meeting loan obligations, explore the available options. Refinancing your loan to a potentially lower interest rate could reduce monthly payments, especially if market rates have dropped or your creditworthiness has improved. If you manage multiple business debts, consolidating them into a single loan with a more manageable payment structure might provide some relief.

Talking with your lender to restructure the terms of your existing loan, such as extending the repayment period (which would lower monthly payments but increase the total interest paid), is another avenue to explore.

Importantly, seek professional advice from an accountant or financial adviser who can give you an objective assessment of your financial situation and help you develop a sustainable repayment strategy. In Australia, the Small Business Debt Helpline offers a free service for guidance in such situations.

The wrap up

Remember that securing the right financing is not just about getting money; it is about making informed decisions that align with your business goals and what you can afford. Whether you are a budding entrepreneur taking your first leap or an established business owner, embrace the power of informed financial decision making and use business loans strategically to fuel your growth and overcome challenges.



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