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7 Ways to Get the Best Loan Pricing

1. Move deposits and other services to the lender

Other services you have at the bank, especially your deposits, are very valuable to the bank. The stock price of a bank is driven more by their deposit base than any other factor, even more than loans. Banks may require you to keep some deposits with them. These deposits are called “compensating balances” by bankers. Those balances increase profitability by reducing the reducing the risk of loss if you can’t pay back the loan and because your deposits are a cheap source of funding for your loan and other loans. If never hurts to ask if the lender will lower their rate if you move more deposits to them or use more services.

2. Reduce the length of the loan terms

Asking for a shorter repricing term, balloon term, or amortization term should reduce the interest rate on your loan. Think of banks as distributors who buy and sell funds. When they sell funds to you for 10 years, they have to buy or borrow money that’s locked in for 10 years. Their cost of funds, or cost for that money, go up as the length of the term goes up, and they pass that cost along to you. Shortening the amortization period also reduces their chance of losses if you have trouble paying off the loan in the future. On the other hand, don’t reduce the amortization period so much that it jeopardizes your current cash flow.

3. Trade off the costs of fees and interest

There are three major loan costs that you can negotiate: the origination fee, the interest rate, and the prepayment fee. In home mortgage lending, reducing the interest rate on a loan by increasing the origination fees (or “points” as they are called with home loans) or increasing the interest rate to reduce the origination fee happens all the time. Business loans are no different. If you expect to pay off the loan soon, you can reduce the origination fee by accepting a higher interest rate. It may save you in the long run. Don’t forget the cost of prepayment fees. If you are likely to pay off the loan soon, either through your cash flow or by the sale of the asset, make sure the prepayment fee isn’t too expensive or can be waived under certain conditions. Once again, lenders are more willing to reduce prepayment fees with shorter loan terms or reduce the fee with higher interest rates. I wouldn’t get too aggressive with this because most lenders already underprice the prepayment fee.

4. Refinance other loans with the lender

Like moving deposits, you can also reduce the loan cost by refinancing loans at other banks with the lender you are now approaching. If you are trying to get a commercial

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real estate loan, they would be very interested in your operating line of credit. The line usually comes with the operating cash accounts and other business services. Refinancing would also make sense if loan rates have gone down since you took out the loan at the other lender.

5. Move your personal accounts to the lender

Your business accounts aren't the only accounts you can move to reduce your loan costs. Moving your personal accounts also increases your overall customer profitability to the bank, which gives your loan officer greater flexibility in reducing your loan cost. Moving business operational accounts, like the line of credit, and personal accounts also signals that you are making a longer-term commitment to the bank, which increases your lifetime value to them. Once again, the more you give, the more you get.

6. Improve your financial health

Improving your financial health isn't something you can do overnight but over time it will reduce your pricing. The financially stronger you are, the less risky you are, which means you get better pricing. I'll explain exactly how lenders assess your riskiness in the underwriting section of this course. Your timeliness and completeness in your responses to the application process also build your credibility with the lender.

7. Refer customers to the lender

I wish I had a dollar for every time a loan officer justified low pricing on a loan by saying "the customer is a great referral source." It's like the punchline of a customer profitability joke. The officer knows the loan modeling system says the customer's profitability, which includes measures of the customer's riskiness, doesn't meet the return usually required for the lender to invest the loan funds. As a last act of desperation, the officer tries to point out the profits, or at least potential profits, from other referrals the customer has made to the bank. Actually referring customers to the lender can improve your chances of lower pricing and makes the pleas of the officer more believable.

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