SMEs and credit scores: What to know about maintaining your business's creditworthiness

By Ben Bierman , issued by Business Partners Limited

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With Business Partners Limited's quarterly SME Index regularly listing funding as one of the key challenges faced by small business owners, most entrepreneurs will at some point most likely have to put in an application for small business funding or a line of credit. While you might be well aware of the importance of maintaining a healthy relationship with creditors in your personal capacity, it's important to know that a small business' credit score can be just as much of a 'make or break' factor when it comes to maintaining its financial viability in the long run.

What is a commercial credit score?

When entrepreneurs apply for funding, financial institutions may reference the personal credit score of the SME owner for businesses in their first few years. However, as the business begins to gain traction and develop a history with its creditors, it will obtain a commercial credit score. This score is determined by an algorithm that considers several data points related to the financial history of the business. This data is collected from a number of sources including debt collection services, debt review companies, public records from government institutions and banks or formal complaints laid by suppliers or other parties should SMEs not honour their debts in time and in full.

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The role that a good credit score can play in growing a business

A commercial credit score ranges from zero to 100, with zero representing the highest risk and 100 representing the lowest risk. Typically, SMEs should aim to maintain a credit score in the upper quartile (75 and higher). Doing so will have important implications on whether a business owner is able to obtain funding at the growth stage of their business.

The interest rate that a business will be offered by creditors will also relate directly to their creditworthiness and credit history. It is therefore in every SME owner's best interest to ensure that healthy debt management is a key component of their business's financial strategy.

Furthermore, an SME's credit score can also play a key role in its relationships with suppliers. Small businesses who are deemed more creditworthy may be granted more favourable payment terms by suppliers and will find a greater ease of business than SMEs who are overly-indebted or who have not managed their debt efficiently.

How to maintain a healthy credit score

Entrepreneurs should view their business's credit score in the same light as other important metrics, and should keep track of it, reviewing it at least three to four times a year. This can be done by requesting a full report from a commercial credit bureau and storing these records so that any fluctuations can benoted and corrected (or queried) if necessary. Currently, the major institutions that govern the determination and recording of commercial credit scores are Experian, TransUnion, XDS and Compuscan. These bureaus have access to full reports on all small business, including any default payments or judgements against an SME.

Investing in an efficient accounts payment system is key to maintaining a healthy credit record. Fortunately, there are a number of fintech companies that offer free or cost-effective accounting software tools that can assist in keeping track of bills and ensuring that debts are paid on time.

Part of an effective debt management system involves cashflow forecasting – which means determining whether your businessmay face any financial difficulty in the months to come and how to implement practical measures to mitigate the risks that may arise as a result. Accurate forecasting will give SME owners enough time to contact creditors and make alternative repayment arrangements before any financial trouble is compounded by a bad credit rating.

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