ABL ADVISOR

SERVING ASSET-BASED LENDING DECISION MAKERS

New Trends Emerge Across the Entire Asset-Based Lending Spectrum

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As *ABL Advisor* enters its third year of publication, we are pleased to present our annual industry leaders market segment overview. In the following four-part article, we catch up with five industry professionals from four leading asset-based lending and factoring institutions. As has been our custom, we approach the industry from varying market perspectives ranging from the large corporate marketplace to small business lending. This year we hear that there are detectable trends evolving across the entire spectrum of commercial finance. We invite you to explore the perspectives offered in the interviews that follow.

Speaking of this year's participants, we extend a hearty thanks to Michael Murphy of Union Bank's Asset Based Lending Group, Michael Scolaro and Jay Schweiger at BMO Harris Bank's Asset Based Lending Group, Darren Latimer at Gibraltar Business Capital and Jeffrey Goldrich at North Mill Capital for their valuable time and invaluable contribution to this overview.

As always, the questions are tuned to best fit the different market sectors, yet our five executives agree that both ABL and factoring continue to play a prominent role in financing today's economy.

Feel free to read these four perspectives in any order you prefer.

MUFG Asset Based Lending Group: Crafting Customized Solutions
Michael J. Murphy

As asset-based loan borrowers continue to expand on a global basis, Union Bank's Michael Murphy notes his institution is poised to leverage those opportunities.

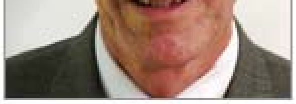
The MUFG Union Bank Asset Based Lending Group serves corporate, commercial, and investment banking clients across the United States and Canada. Last July, Union Bank's parent Mitsubishi UFJ Financial Group (MUFG) merged its subsidiaries and affiliates in the Americas, creating MUFG Union Bank. In the Americas, the group services its corporate and investment banking customers under the MUFG brand, and goes to market with its commercial banking customers under the Union Bank brand.

ABL Advisor: By what measure does Union Bank define the transactions and/or relationships that fall under Union Bank's Commercial Finance group? Are your borrower's primarily middle-market ABL borrowers or large corporate borrowers?

Michael Murphy: The MUFG Asset Based Lending Group specializes in formula driven revolving lines of credit and term loans based on eligible assets including accounts receivable, inventory, equipment, and owner-occupied real estate. The asset-based loan product provides flexibility for rapid growth, acquisitions, and turnarounds with commercial clients with borrowing needs as low as $15 million and corporate clients with revenues greater than $2 billion.

MICHAEL J. MURPHY
Managing Director &
Head of Asset Based Lending
MUFG Union Bank, N.A.

MUFG is a full service provider with national and international capabilities with 1,100 offices in more than 40 countries. One stop financing with junior debt and non-control equity capital is provided by UnionBanCal Equities and access to debt and equities securities are handled by our affiliate, Mitsubishi UFJ Securities (USA), Inc.



MICHAEL J. MURPHY
Managing Director &
Head of Asset Based Lending
MUFG Union Bank, N.A.

ABL Advisor: From your perspective, what are these corporate borrowers looking for these days from their lending relationships? As a follow up, how do those needs differ from what they sought in the pre-recessionary years?

Murphy: Our ABL corporate borrowers are looking for solutions to increase their liquidity position and to extend the maturity profile of their debt at competitive rates. Improved financial flexibility can be used to deploy capital for acquisitions to diversify platform, capital expenditure alternatives, and shareholder distributions.

Borrowers want their lender to bring creative financing solutions to their attention including securitization products or matching high yield bonds or institutional term loans with an ABL facility to complement the capital structure with limited amortization and flexibility to pay down debt.

The ability for an institution to commit to various tranches of debt for an acquisition is a key differentiator in the market today versus the pre-recessionary years. Asset-based lending survived through the recession as a predictable source of financing with a low loss given default and is now viewed as a flexible form of mainstream financing versus a last resort option used by troubled borrowers.

ABL Advisor: What other things come to mind as areas these borrowers are paying close attention to these days?

Murphy: ABL borrowers are looking for their lender to be a “trusted advisor” to strategically craft customized solutions and differentiate by demonstrating improvements to their current cost/fee structure and providing incremental borrowing capacity. Borrowers want regular market updates tailored for their business with creative capital solutions to position for the next refinance. The asset-based loan product in the corporate market generally comes with a limited covenant structure tied to springing liquidity trigger -- a very attractive solution for borrowers looking for flexibility and financing predictability in executing their business plans.

ABL Advisor: Are there any examples in the way of recent transactions that demonstrate that an asset-based loan proved to fit the bill in getting the deal done in the best way possible?

Murphy: As we continue to see ABL borrowers expanding on a global basis, we are leveraging our international capabilities with our parent to lend in foreign jurisdictions that have favorable laws in perfecting collateral and enforcing liens as well as cross-selling other services in these jurisdictions. Also, we are leveraging our industry verticals in food and beverage, oil and gas, technology, transportation, retail, and equipment rental to focus on acquisitive borrowers where we have industry expertise.

ABL Advisor: Give us your take on today’s syndicated loan market. How robust is this market for asset-based lenders these days?

Murphy: Refinancings continue to dominate the market at 75% of all asset-based lending volume in 2014, which is creating an inadequate supply of new ABL assets to utilize robust lender liquidity. As the leveraged loan issuance hit record highs in 2013 and continues its robust pace, the asset-based share of overall leveraged loan volume has shrunk to 9% in the first half of 2014. Pricing levels for high quality ABL deals and club deals based on relationship lending have gone to market on a pricing grid from L + 125-175.

The asset-based loan market is currently encountering competition from cash flow lenders since there is an abundance of liquidity in the market. High yield bonds continue to pay down revolvers, which is decreasing credit line utilization on ABL facilities.

BMO Harris Bank ABL: Poised for Growth in All Directions
Michael W. Scolaro & Jay L. Schweiger

BMO Harris Bank’s Michael Scolaro and Jay Schweiger see positive signs for asset-based lenders in terms of opportunities on the horizon.

Michael Scolaro and Jay Schweiger have seen the asset-based lending business at BMO Harris Bank grow from less than $1 billion in commitments to more than $5 billion within a seven-year period. Presently, the group has more than 130 clients and works with commercial lenders within the bank’s central U.S. footprint with officers in Wisconsin, Minnesota, Kansas, Illinois, and Indiana. The group structures ABL deals for clients with loan needs ranging from $10 million to over $1 billion. BMO Harris ABL mines lending opportunities from the customers of both BMO Capital Markets and BMO Harris clients as well as direct asset-based borrowers resulting from the group's direct calling efforts.

MICHAEL V. SCOLARO
Managing Director & Group Head
Asset Based Lending
BMO Harris Bank

ABL Advisor: When considering the middle-market, what would you say borrowers are primarily seeking from their asset-based lenders these days?

Michael Scolaro: Essentially, our borrowers want three things, which can be summed up in one phrase: they want the most money for the lowest cost with the fastest delivery. Frankly, it’s a borrower’s market with the supply of asset-based loans outstripping the demand. Initially this caused pricing to decrease to all-time lows and today, it’s trying to drive structures to be more accommodating to borrowers. That’s where we and other asset-based lenders need to be more selective in terms of who we choose to lend money to.

ABL Advisor: In your estimation, has competition in the asset-based lending intensified, stayed at the same level or decreased in the last year or so?

JAY L. SCHVEIGER
Director – Business Development
Asset Based Lending
BMO Harris Bank

Jay Schweiger: I think the competition is aggressive these days. Pricing has remained relatively consistent over the last year or two. On a deal-by-deal basis in certain locales or deal specific opportunities, you might see a lender go below the market.

Typically one encounters the most aggressive terms when an asset-based loan is paired with other parts of the debt capital structure.

With that said, we see that pricing has been aggressive and you’re certainly not winning any deals today by overcharging. Still, I think the competition with regard to pricing has been relatively rational and as Mike said, we think that competition is turning toward the terms of the financing. We all will need to be selective on what we do and when we do it.

ABL Advisor: What are your observations on the ABL market from a geographic standpoint?

Scolaro: I can say this. We recently opened up a direct calling office in Atlanta, so as you can see, we are stepping out of our footprint. Within the next 12 to 18 months, we have plans to open other offices throughout the country. At BMO Harris, we have continued growth plans for the upcoming years and we have plans to double the business within the next three years.

Schweiger: We really haven’t seen any area of the country or one geographic region standing out as stronger than the others. From our standpoint, things have been pretty consistent and I think it all goes back to the flexibility of asset-based loans … the product pairs well with other parts of the capital structure. Our customers appreciate that flexibility.

ABL Advisor: Among ABL borrowers, are you seeing and/or anticipating any growth in any particular sectors? Do you see any pulling back either now or in the near term?

Scolaro: Historically, BMO Harris has always been a big player in the food and agriculture business. We’ve got great corporate and investment banking coverage in the area and as an institution; we are well regarded in that space. Over the last 12 to 24 months we have also spent a good deal of time in the industrial manufacturing space working with metal distributors in addition to basic manufacturing companies. We are putting significant effort in helping to finance the manufacturing expansion currently happening in the United States.

ABL Advisor: What is your outlook for the asset-based lending marketplace as we head into 2015?

Schweiger: I recently saw that the GDP 3.5 over the 3.2 estimate and I think that bodes very well for us. There has been a lot of positive news with regard to companies re-shoring their businesses. On the consumer side, I’ve read some reports that indicate incomes are beginning to grow and it’s clear that businesses are growing. We are very excited and we have some very strong goals being put down in front of us now. We think that 2015 could turn out to be a good year for many people … a strong year for the U.S.

Scolaro: I concur with that line of thinking. I think we’re going to see similar loan demand that we’ve seen over the last couple of years but it might actually increase a little bit later into the recovery.

ABL Advisor: Is there anything you would like to add in closing?

Schweiger: We’re pretty positive for ABL guys. I think the thing I would like to add is our growth has been across a number of spectrums and that’s the exciting part of being at BMO Harris. We’ve grown or presence in the smaller end of the middle market and we’ve increased our penetration into the large cap corporate ABL market. We have also increased our penetration into the food and industrial sectors through our direct calling effort. Our growth is broad based and not dependent upon any one source of business. The industries we serve are fairly diverse and the size of companies we serve is diverse as well. In addition, the number of buyouts versus non-buyouts isn't skewed one way or the other. We are poised for growth in the near future and beyond.

Scolaro: Jay said it correctly. At BMO Harris, we are expecting growth and we are ready for it.

Gibraltar Business Capital: Watching the Trends
Darren Latimer

These days, Gibraltar Business Capital's Darren Latimer is staying on top of the trends he sees emerging in loan origination.

Northbrook, IL-based Gibraltar Business Capital seeks to serve under-banked ABL and other borrowers through its three businesses: an asset-based lending group, a factoring group and a merchant cash management business. Darren Latimer, president and CEO of Gibraltar, notes its group of asset-based lending borrowers is divided roughly into thirds: private equity backed companies, small owner occupied or small group owned businesses, and small publicly owned companies.

ABL Advisor: Please share what in your estimation makes Gibraltar Business Capital unique among its peers.

Darren Latimer: We have built our commercial finance business by diversifying across various asset classes taking risk, gross return, credit profile, and loan size into consideration which we believe will serve us well over time. Today, we have a diversified customer base which drive strong revenue, earnings and ROE for our shareholders. We think our three products working in unison do that and at the same time, providing a lot of cover for each other. For example, we are able to earn premium returns in our merchant capital business, which allow us to be competitive for our best ABL clients.

DARREN LATIMER
Chief Executive Officer
Gibraltar Business Capital

ABL Advisor: From your perspective and based on the borrowers you finance, what are the chief concerns those borrowers have in today's environment?

Latimer: From a wide perspective, we recognize that our borrowers and prospects are most concerned with their lender's ability to understand their business … the ups and downs of their business and the assurance that they will have access to liquidity at all times. Many of our borrowers have had the unfortunate experience where a bank may have called a minor covenant default … thus limiting their access to capital when they need it most.

We react to those borrowers by setting the ground-rules early and laying out our expectations upfront, and given that, a borrower has transparency into their liquidity. That has worked out well for us.

ABL Advisor: What concerns do they face when it comes to their business operations?

Latimer: There are two main concerns. Given we specialize in serving smaller customers with less than $50 million of revenue, the chief concern is their ability to maintain and grow gross margins, but that's nothing new. The other big concern is how wide the gap between payable and receivables are and how much stress that puts on the working capital cycle.

Another concern for our customers today lies in the fact that more and more buyers are "just in time" buyers and that makes our borrowers' who aren't looking to hold a lot of inventory thus stressing their ability to forecast.

ABL Advisor: On the flip side, what are the primary concerns lenders in your space have these days?

Latimer: Besides being competitive with the liquidity in the market, our major concerns haven't changed too much over the years. We are looking for integrity in the collateral and reporting, working with good managers who can forecast, and of course maintaining our ability to enjoy what we do.

ABL Advisor: How would you characterize the competition among lenders of your ilk in the markets you serve?

Latimer: The competitive nature of this business is hard to gauge — it's very wide. The amount of liquidity in today's marketplace among unregulated non-public money is enormous. It comes from private equity firms, business development companies and from private client funds as well as from our regular competitors. The abundant liquidity in today's market is a big concern for our growth.

ABL Advisor: What is your outlook as we head into 2015?

Latimer: On the smaller ABL front – from $1 million to $10 million in loan size – we are concerned with the liquidity in the market and what this will do to gross returns. We are bearish on material growth for small companies, albeit there appear to be a lot of small and early stage companies, so the prospect pool may be wide but average loans may stay low. Overall, I don't see the liquidity ending right now ... it's all a crap shoot and when the economy rolls a seven, we'll be here.

ABL Advisor: Is there anything more you would like our readers to know?

Latimer: At Gibraltar, we are really focusing on the tools we use to originate loans, mainly driven by new liquidity and technology. Data show that originations for loans less than $250,000 are trending towards direct call, mail, SEO, and radio response. The ground rules for this sub $500,000 market are being completely re-written all toward a direct calling method.

And as information becomes more plentiful, who's to say that we won't be able to develop a list of 1,000 or so potential ABL candidates and call directly on them some day? The origination source is a huge discussion point for us right now. We're pretty excited about the changes we're seeing.

North Mill Capital: Taking the Time to Listen
Jeffrey K. Goldrich

Jeff Goldrich and his staff at North Mill Capital work hard at fully understanding their borrowers' needs ... and that makes all the difference in his firm's ability to think "outside the box."

North Mill Capital is both an asset-based lender and factor with two full-service offices in Princeton, NJ and Minneapolis, MN. The company has business development officers in various parts of the country and offers its products on a nationwide basis. Asset-based loans range from $400,000 to $15 million in three primary sectors: manufacturing, wholesale distribution and service companies. In its factoring business, transactions range from financing startups at near zero dollar levels to $15 million.

ABL Advisor: From your perspective, what would you say are the chief concerns small business owners face when it comes to meeting their financing needs? Other than capital, what are these entrepreneurs seeking from their finance company?

Jeff Goldrich: Our borrowers are most concerned with the cost of money and beyond that, having a lender that is flexible in terms of structure. They want a lender who is willing to provide financing that is "out of the box," so to speak. For lenders, it's easy to fit things into conventional advance rates on receivables, inventory, and machinery and equipment. Trying to force a borrower's financing into a cookie-cutter model rarely meets their needs. They are looking for a lender who tries to find a way to go over and above that. We find our borrowers are looking for a lender that is willing to spend the requisite amount of time required to listen to them and really get to know their business. Because we do that, we can generally find a way to be more flexible and in turn, meet their needs.

JEFFREY K. GOLDRICH
President and CEO
North Mill Capital LLC

ABL Advisor: In what other ways do a small business owner's needs differ a middle-market borrower's needs?

Goldrich: Small business owners' needs are very different from those of a middle-market borrower in a number of ways. For one thing, there is really no difference between the person who owns a small business and the business itself. Middle-market borrowers have more influence over their lender. They get more competitive financing, and the world – perhaps unfairly – takes middle-market companies more seriously. Small business owners have to work harder to get more attention and flexibility from their lenders. And for the most part, forman projections and business plans can sometimes be lacking on the part of small business owners. As a lender in this end of the market, you need to spend the time listening to small business owner articulate their needs.

ABL Advisor: In considering today's economic environment, what are the realities finance companies face when it comes to securing their own financing?

Goldrich: I think the environment is very good for finance companies in this regard. Lending to finance companies is clearly a niche, but there are several options with highly competitive terms.

ABL Advisor: In your estimation, how much control are these lenders exercising on opportunities finance companies can pursue these days?

Goldrich: I'd say there's a certain amount of control … there are eligibility criteria that any sophisticated lender to finance companies uses to finance their borrowers. I don't see that control as being more or less than it has been in recent times. For us, it's at an appropriate level and when we need something that falls outside of those criteria, we typically can get it. The fact of the matter is that if you can't live within the broad eligibility criteria offered by these lenders, your risk level is probably excessive.

ABL Advisor: What matters most to your lenders?

Goldrich: I think it's reliance on our team members. We give our lenders access to our entire team and there's no one at North Mill who serves as a gatekeeper. Our lenders speak with our portfolio manager, our chief financial officer, our chief operating officer and they speak to me. Transparency and sticking to our standards matter most to our lenders. That's why they can be flexible with us when we need them to be.

ABL Advisor: What's your outlook for the markets you serve?

Goldrich: I think we're in for exciting times for the next few years. We do quite well when banks are in a tighter environment and I see that happening now. Furthermore, we think that is likely to continue and because of that, we've already seen an uptick in our pipeline in terms of quality. As banks stay appropriately conservative, there will be many more opportunities for us in the entrepreneurial independent finance company arena. We are starting to see that now and we feel really good about it.

In terms of competition, there are terrific finance companies and factors out there and without a doubt, we are in a competitive market. We are maintaining our standards and we'll only compete to the extent that opportunities fit within our criteria. I think the level of competition today is healthy. There's always someone out there who is overly exuberant. For the most part, our competitors are smart people and are competing in an intelligent manner.
