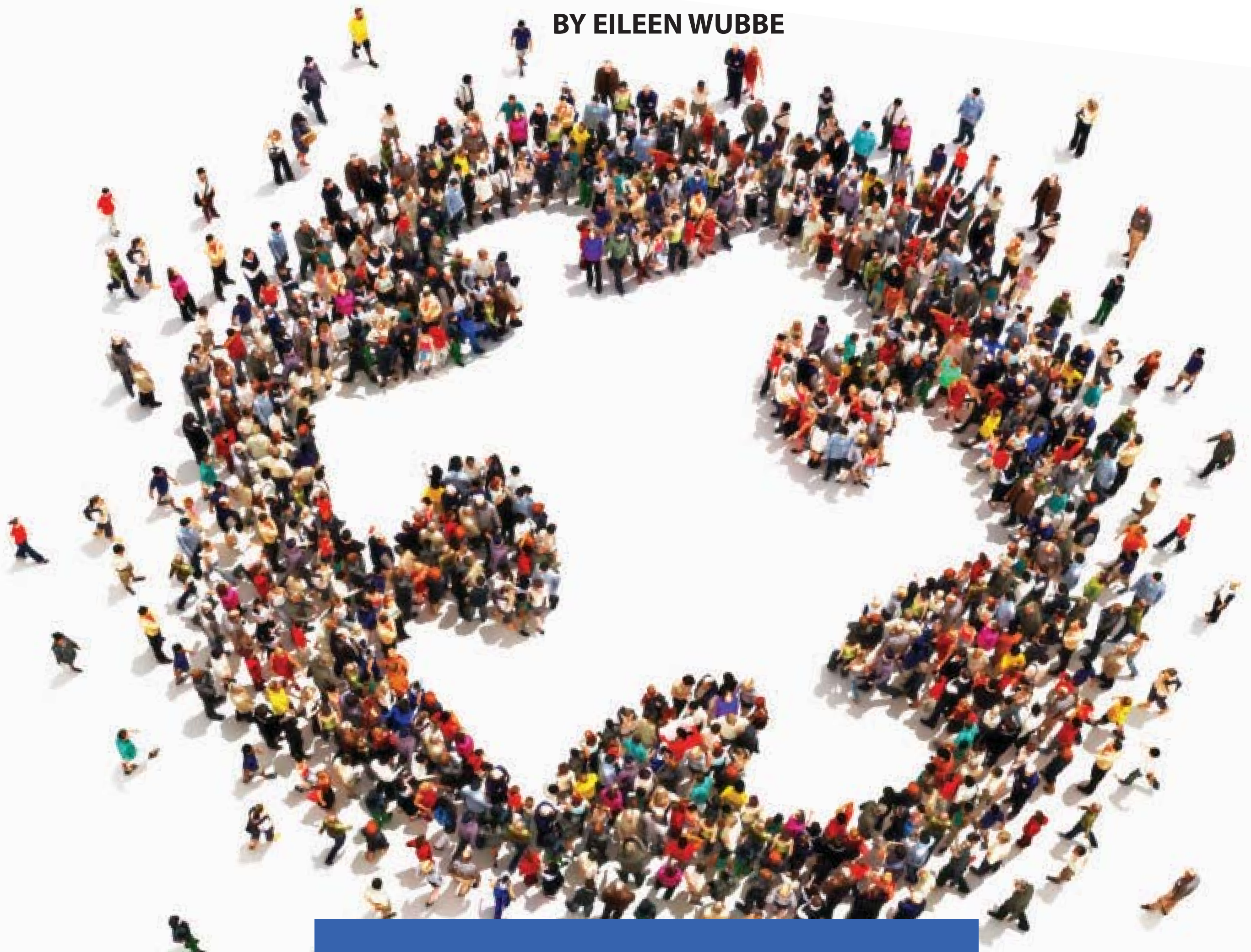
Entrepreneurial Roundtable:

Lenders Discuss Challenges, Competition and What's Next

BY EILEEN WUBBE



The Secured Lender's senior editor sat down with some of the industry leaders in the entrepreneurial ABL, factoring and FinTech space to take the pulse of the industry. Secil Baysal, chief operating officer, FastPay; David Grende, president, Siena Lending Group; Betty Hernandez, shareholder, EVP and chief credit officer, North Mill Capital, LLC; Michael Monk, managing partner, Amerisource Funding; Kwesi Rogers, president and CEO, Federal National Commercial Credit, and Scott Winicour, co-founder and co-president, Gibraltar Capital Holdings, LLC, discussed the challenges and trends they're seeing, efforts to attract and retain talent and their thoughts on merchant cash advance.

Secil Baysal
chief operating officer,
FastPay

David Grende
president,
Siena Lending Group

Betty Hernandez
shareholder, EVP and
chief credit officer,
North Mill Capital, LLC

Michael Monk
managing partner,
Amerisource Funding

Kwesi Rogers
president and CEO,
Federal National
Commercial Credit

Scott Winicour
co-founder and co-president,
Gibraltar Capital Holdings, LLC

Please give our readers a general overview of the industry, from an entrepreneurial lender's perspective. What are some of the challenges and trends you are seeing?

BETTY HERNANDEZ: We're seeing the effects of the easing of credit from the new entrants in the marketplace. We've all been talking about FinTech and online lenders, and the MCAs of the world. They're obviously affecting all of us, especially in our factoring portfolio. They're able to produce and give credit faster and easier with less covenants, and, of course, that's impacting us on the factoring side.

On the ABL side, we're seeing some of the trickle down from the decline in the scrap metals market and oil and gas-related borrowers are starting to filter down from larger banks into the independent finance company level. As you can imagine, they're weaker credits at this point after everything they've gone through, so we really need to accept and understand the turnaround strategy in place and determine whether the borrower can survive, and ask ourselves, are they one of the survivors at the end of this?

MICHAEL MONK: The major trend over the last several years (since the banking/economic crisis) has been the vast imbalance of the "supply" and "demand" for money.

On the "supply" side, the extended period of historically low interest rates, coupled with quantitative easing by the Fed, has created excess liquidity in the financial markets. This translates to a huge supply of money – lots of lenders with lots of money to lend.

On the "demand" side, the lack of significant economic growth translates to reduced "demand" for money by borrowers.
This imbalance has led to increased competition by lenders for a smaller pool of borrowers – i.e., more aggressive loan structures and pricing. Sure, there are plenty of deals getting done in the marketplace. But much of it has been refinance business, with borrowers looking for a better to deal to lower their cost of capital. This imbalance has made things challenging for both bank and nonbank lenders. But it's been even tougher for banks, which have the additional burden of a tight regulatory environment. So that's given nonbank lenders like us a competitive advantage in this market.

As a 30-year-old business, for us, it's all about market share. We're committed to the ABL market for the long term, so we haven't really worried too much about pricing – if we see a deal we like, we are going to do everything we can to win and maintain that relationship. As a result, we've been able to continue to grow our business even under these difficult macroeconomic conditions.

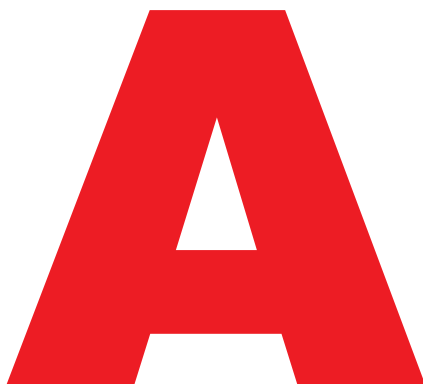
However, I think it's been much tougher for some of our lender/competitors who are newer to the business and don't have an established customer and revenue base, nor the scale to provide a

lower cost of capital and value proposition to potential borrowers.

KWESI ROGERS: While none of the industry participants have enjoyed the lower yields, limited deal flow and hyper-competitive environment, I believe it has strengthened the industry. Industry participants now have to find ways to lower costs and deliver their product with greater speed, efficiency and cost competitiveness than I ever recall over my 24-year career. The growth of the FinTechs and the availability of new technology continues to apply pressure on the market participants to achieve greater efficiencies.

is feeling some of the effects that Betty mentioned on the factoring side. It's been a challenge to grow the portfolio, but this isn't something new, at least in my experience. The biggest challenge we're facing is on the ABL side, as this is our core business and our existing borrowers' availability has decreased. So, I may have the same amount of borrowers, but their loan balances are down, and new business development is probably as competitive as I've ever seen it.

DAVID GRENDE: I echo Scott's comments. We're in essentially two businesses: asset-based lending and a servicing platform of our ABL business that we use for community banks to be able to participate in ABL



s a 30-year-old business, for us, it's all about market share. We're committed to the ABL market for the long term, so we haven't really worried too much about pricing – if we see a deal we like, we are going to do everything we can to win and maintain that relationship. — *Michael Monk*

with our help as an outsource provider. On the ABL side, from an industry perspective, it is super competitive. There are more players in the space now than there were at the beginning of the year.

So, with all the competition it creates, every new deal that we're looking at has four-to-seven term sheets that are involved, and some of them are just ridiculous term sheets that we won't even compete with because it just doesn't make any sense. So structures and pricing are deteriorating.

From the business-flow perspective, we're seeing more business than we have seen. We're winning less and we're bidding on more. I think there is more business coming into the space, either being trickled down from the banks because they're getting out of the sectors that Betty talked about, or just because the banks and all the issues that they're going through have moved more away from the lower middle market.

So, the challenges that we have are continuing to grow the business year over year, and part of that also has to do with retention of existing portfolio accounts because we see a tremendous amount of attrition. We're more expensive than traditional banks, so customers will take the first opportunity they get to repay our debt with cheaper money. Probably a third of what we do is financing companies as a bridge to a sale of the business.

SECIL BAYSAL: We cater to digital new economy verticals that are inherently high growth and finding new origination opportunities hasn't been the primary challenge. We are more concerned about maintaining our credit quality and increasing our penetration of our target market.

Our clients' funding needs move in line with how the venture capital community looks at the different verticals, whether it's ad tech, digital, online or mobile. Their sentiment is, in turn, influenced by equity markets and recent exits. The last couple of quarters have been pretty jumpy, with a lot of venture capital money drying up in some of these verticals, which impacts the number of new entrants. On the other hand, this pull-back increases our clients' need to borrow more.

On the competitive front, we seem to be in a period where big financial institutions have differing opinions in terms of where the credit cycle is going. We see some of the larger players already starting to tighten credit, believing we are entering that next cycle. On the other hand, we see some newcomers who don't want to miss out and who are looking at potential deals more opportunistically.

SCOTT WINICOUR: We have two balance sheets with three different products. One has factoring and asset-based lending, and another has merchant cash advances. While our merchant cash advance business continues to grow rapidly, we've seen the largest surge in growth over the last four months, even though we have been providing MCA facilities for more than four years, since our inception.

We're pleased with our ability to originate these deals, and we've been able to manage some losses well under industry averages. The real test will be when the next credit downturn comes, as to whether or not our underwriting process is sound enough. But, since we have a solid executive team with many years of experience, knowledge and a deep understanding of this business, we feel confident and well prepared that they will hold up.

However, Gibraltar Business Capital

What are some of the changes or challenges that have had the most effect on your business over the last five to ten years?

MONK: Everyone is faced with the challenge of growing their portfolio and business in this less-than-optimal economic environment. We've been fortunate to have a very seasoned management team and outstanding employees who place tremendous value on client relationships, yet have the credit expertise to avoid/minimize losses. This has translated into a very low client attrition rate for us, with our average client tenure well in excess of four years. This has allowed us to grow our earning assets every single year, even in years when new business opportunities are less abundant. And it allows us to spend more time focusing on ways to improve and streamline our origination and underwriting processes.

ROGERS: Finding personnel with the attributes required to propel your company to achieve its goals and objectives continues to pose a challenge. The internet and new market entrants have made the entrepreneurial factoring and small-ticket asset-based lending marketplace a more efficient market for the consumers of these products, forcing the participants to step up our game and become more competitive. In many respects this hyper-competitive environment has placed extreme pressures on market participants to offer structure that was not available in the marketplace five years ago. Technological advancement has had the biggest impact on our business in the past 5-10 years. For example, I'm providing this response as I sit on an airplane. This was not a possibility five to ten years ago. If I board a plane today without Wi-Fi, the expression on my face resembles a child who has been prohibited the privilege of Trick or Treating on Halloween. Technology provides the tools required for the industry to close deals faster and manage them with greater efficiencies. The other variable causing a great deal of change in the market compared to the market, ten years ago is the amount of liquidity in the marketplace.

WINICOUR: I would say the flatness of the economy. If you go back the last 30 or 40 years, the credit cycle seemed to be about three years on average. Banks would get in, banks would get out and, depending on the timing of all that, asset-based lenders would have plenty of chances to prosper. As we all know too well, the economy has been relatively flat since 2008-09 when the global economic crisis hit. We haven't seen a lot of revenue and the credit cycles seem to be longer than usual. There's still a ton of excess capital and probably more capital available for specialty finance businesses today than there ever has been; but, when you look at simple supply and demand, supply is up but demand is still much lower than the supply. I think that is what has had the largest effect on our business overall in the last seven years or so.

BAYSAL: For us, the main changes have been around capital markets and data. We fit in the category of next-generation FinTech-based lenders, and probably one of the big changes in the last five years has been the entry of a lot of new investors into the space, players who previously were not necessarily exposed to this type of asset class. With the growth of marketplace lenders, whether it's business-to-business or consumer, there is a whole new class of investors who got educated in various lending models and became very active, increasing the supply of capital. Secondly, the availability of big data in real-time allows us to reinvent a lot of the traditional processes in a way that is much faster and much more scaleable. Whether it's for invoice verification or collections, we can leverage third-party data sources, to underwrite and service faster and more efficiently.

GRENDE: I think regulation and what's come out of the environment post-2009 has had a big effect on our business. I believe the banks no longer want to dabble in anything close to a criticized asset, whereas in the past, before the great recession, many banks were dabbling and playing in the ABL space around criticized assets. They would designate a portion of their book that they were comfortable with, having it rated as substandard credits.

With the onslaught of all the regulation post-2009, the banks don't want to come near substandard assets.

HERNANDEZ: There are such a limited number of good deals out there, and we're all chasing the same ones. We're over-equitized, and that leads to all of us in the ABL and the independent finance world to chase the same deals, liberalizing the standards a little bit, and lowering the yields in order to gain market share.

Man vs. Machine - Should we use better technology or find the right salesperson?

MONK: We are always looking for ways to improve our processes with technology, whether that is lead acquisition, underwriting, approval, client service, reporting or risk management. But in our core market space ($1-10 million factoring and ABL deals), there is still no replacement for the human business development officer, as these lower middle-market borrowers still place a very high premium on "relationships". Our clients are not going to fill out an online form to request a $10 million line of credit. These companies normally have a controller or CFO charged with vetting financing options – and it's critical that they are comfortable with the lender relationship.

However, in the "small ticket" market I think technology has been very disruptive and is making very big inroads with automated credit scoring and approvals. For many small borrowers, the individual completing the application is the actual business owner, who has many time constraints – so a quick, easy online application can be appealing. Unfortunately for many of these business owners, time constraints can lead to lack of due diligence in understanding how these online lenders work. And many of these business owners find themselves trapped with exorbitant fees and interest rates charged by online lenders, simply because they went online and clicked "Agree" to have their advance wired to them, without reading the fine print.

ROGERS: I prefer a combination of man and machine. Even in the most technology-

enabled underwriting and onboarding processes, I have seen key personnel use their expertise to provide their firms with a competitive advantage. I am a firm believer that, when this expertise is properly paired with technology, it allows key personnel to underwrite and disqualify deals faster than they otherwise could. On the sales side, I prefer a mix of man and machine here, as well. In speaking with industry colleagues whose target markets support a more technology-driven sales process, such as transportation factoring, there is still an inflection point in the process where the prospect demands to speak with a knowledgeable person who can immediately structure a deal for the prospect.

approach, engage and retain new customers in this changing environment.

HERNANDEZ: I think Scott is correct. I think we're trying to do the same thing here. I think the younger borrowers are definitely more social-media savvy. They prefer an online, less personal touch. There's always going to be that pool of borrower that likes the human touch; but, in order to get a shot at looking at deals, I think we all need to focus more on the social media strategies and data analytics like Scott mentioned. It's just a new playground now. It's not just networking and shaking hands – that's not enough anymore. The same players are there at events and you have to distinguish yourself somehow.

At the same time, when you're dealing with a more-established company to discuss a multi-million dollar credit facility, I don't think you'll ever completely eliminate the human touch part of the equation because people still want to know whom they're dealing with.

So, our approach is to figure out how to best segment and use technology to make the process much smoother for everyone, but always maintain the option to be able to talk to our prospects and clients, especially larger ones.

What efforts are your organizations doing to attract talent? What are some of the challenges you face in attracting and retaining employees and how are you addressing them?

e're pleased with our ability to originate these deals, and we've been able to manage some losses well under industry averages. The real test will be when the next credit downturn comes, as to whether or not our underwriting process is sound enough. — *Scott Winicour*

WINICOUR: We're trying to strike a healthy balance that works for us. This involves figuring out how to best use technology and marketing elements, in order to generate a higher and better quality type of deal flow. I think the days of the ABL shops putting 50 bodies on the street may be over, but not disappearing completely. We believe that the human factor is still an essential part of the experience for our clients. We want one of our sales experts to properly close the deal, especially in a larger ABL transaction. However, we have also embraced and implemented new technology and marketing resources to improve our efficiency and results when we originate deals.

There's a shift going on, and I think we're right in the middle of it, and Gibraltar recognizes all sides. We actually just hired a new salesperson, and are currently talking to a few others. But we're also working with marketing and technology experts that can help us figure out more definitively, how to

GRENDE: I agree with that one hundred percent. As you're going through time, your CFOs and CEOs today are Millennials looking for financing. As the generations move on, people are going to use social media and other online networks and portals to start shopping for money.
On a lot of these transactions, you still need a person that's physically going to be there to direct or close the transaction, especially on the larger, more complex ones. For finding new opportunities, there needs to be a technology or data marketing component to it as opposed to just a salesperson.

BAYSAL: We're obviously coming from a technology angle, but we believe the right mix is a hybrid. We do have an SMB version of our product, which is fully automated, providing next-day funding, and that works well for the app developer or online publisher who actually prefers to go through that type of low-touch process.

GRENDE: We've got 21 employees, and, out of this, probably four or five are Millennials. In attracting talent, it's really all about the workplace culture and having people enjoy coming to work and working with each other. It's an atmosphere where there is complete transparency. Obviously, we're a small company, and this probably is true for a lot of small companies, but there isn't any politics. Everyone knows what's going on.

There's a constant review of goals and the progress we've made against our goals. Everyone knows where this company is on a weekly basis and its stages as it's going through from a startup to a more mature company. No one's worried about someone doing something behind their back because nothing is done behind anybody's back.

We've also have had luck with the transformation of GE Capital's multiple businesses being sold off, especially since we're also based in Connecticut. It's created

a tremendous opportunity for us to find extremely talented people. We've taken advantage of that opportunity, even ahead of where our hiring matrix was. We had the opportunity to hire some very talented people that wanted a change of lifestyle, moving from a huge organization to a small organization and something that was very local to them.

HERNANDEZ: At North Mill, we're fortunate that many of us have worked together before in prior organizations. We are like a family. We have 30 employees and two locations and several salespeople that work remotely.

We try to improve morale here all the time. In the summer we try to offer summer hours and people really look forward to that. We also try to cross-train. We have collateral specialists that have indicated in the past they may be interested in field examination. So, since we have inside field examiners, we gladly take them out on a field exam and show them what a field examiner's role is.

We have a monthly portfolio review meeting where everyone in the company is involved. Everybody knows what's going on with all the accounts.

BAYSAL: We are about 70 people, mostly in Los Angeles, with offices in San Francisco, New York and London. We do have a relatively young workforce, which helps us speak the language of our clients.

From a recruiting angle, we are looking for people who come with a mindset to innovate; dispute and challenge the status quo. If we just do the same job banks do, then we won't have a reason to exist. So we have to do better on all fronts.

MONK: We have roughly 50 employees and are fortunate to have a very tenured management team, but we are continuously building our bench!

As a general rule, we don't hire "seasoned" credit personnel in our back office. Instead, everyone starts at entry level and works their way up through the business. And our shop is a meritocracy, so if they don't cut it, they're moved out pretty quickly. As a result, all of our key management personnel are 10-15+ year veterans.

So, we just look to keep our benches full and make sure we constantly have new candidates coming in that are upwardly mobile; so, as we go through our normal employee attrition, we have great candidates who are ready to move up into those roles and take on increasing responsibility.

Hiring sales people is a different story entirely! Over the years, we've discovered that there is no magic formula to predict who will make a great sales person (if you have this formula, please share it with us!). So, instead, we only look for proven producers, the best of the best – top producers in the industry with an established track record. To attract these producers, our pay and comp plans are the highest in the industry. We're generally not interested in people that have hopped around from job to job. And once we identify a good candidate, we get them down to tour our back office as quickly as possible. When a top producer is looking for a new job, it's usually because of challenges with their existing employers' ability to do deals. Once they meet our management team and back-office staff and understand our corporate culture and "pro-client" mentality, the recruiting process is 90% complete.

ROGERS: We are constantly assessing our personnel needs and exploring the market for talent that will assist us in achieving our goals. Additionally, we offer referral bonuses to existing employees who refer us to resources who eventually become employees of the firm. One of the biggest challenges I face in retaining employees is the wide array of diversity in our employee base and the job functions they fulfill. The type of person who is going to be a successful BDO is much different than that of a successful account executive or underwriter. While all of the varying positions generally have distinct personalities, it is sometimes difficult to ensure they all are satisfied with their job. In order to address this particular challenge, we do our best to communicate clearly to the staff and keep them informed. If we are forced to make adjustments that certain staff members do not like in order to remain competitive, we simply provide the why behind the action. Typically, people are much more inclined to accept changes that adversely affect them if they understand it is for the greater good of the firm.

WINICOUR: I could talk about this subject for hours, as this is something our management team focuses on an ongoing basis. We spend more time with our co-workers than we do with our own families, so we work on creating and maintaining a cohesive company environment that understands and embraces our mission, values and purpose. Our company culture is based on trust, loyalty and respect throughout all facets of our business, and among each of our team members. We also recognize that Millennials have an increasingly a strong presence in the workforce, and we are very mindful of making sure all team members, regardless of their experience level or age, can contribute in their own way.

GRENDE: We are actually hiring a couple of college graduates without any experience in our business and putting them through a training program and a career path that we think excites them. That has been a tremendous opportunity for some of the young folks. The opportunity for everybody, no matter where they are in the organization, to be able to move around and move up is something else that gives you the ability to retain employees over some of the larger businesses, because they get to see many different aspects of the business that they would never get to see if they were working for a larger business.

WINICOUR: It's great to hear that you're doing that, Dave. In the past five years, we started an internship program, and every year after that intern graduated, they have come back and started a full-time job with us. We're combing the job fairs and college fairs to find these Millennials who are about to graduate and looking at what their career move is going to be. We bring them in on an internship level, and they get to test the waters. It's really exciting to work with new people this way.

We're looking more for a cultural fit than a specific background, and over the summer we put them in variety of positions within the company.

In your opinion, is merchant cash advance a friend or foe to this industry and why? What are your predictions of the long-term effects of alternative financing to this industry?

WINICOUR: We have a sister business called Gibraltar Capital Advance, which is a separate balance sheet that provides online lending and merchant cash advances. We built the organization from the ground up with two senior professionals who were in this space in their previous careers, and brought them onboard to start and grow this sector of business. Over the last four years the MCA business has evolved tremendously, but if you're not staying ahead or on top of what's going on on a day-to-day basis, you're going to get left behind.

There's been a lot of noise in the specialty finance space about MCAs. As is in any industry, my feeling is that there are always a few bad apples that spoil the bunch. They might not have the best ethics or may just be trying to make as much money as they possibly can and ride the wave, so to speak. But, I would say the majority of the people I've met in this space are truly professional, smart, entrepreneurial, serious finance people who are providing a good service and a good product to companies that need it.

Online lending and small business lending, in general, has yet to experience a true downturn, and a lot of these companies consider themselves as technology companies that just happen to be in the lending space. My concern is that they don't have the true lending experience to manage the ups and downs of a full credit cycle. On the contrary, the experienced lenders who utilize digital and technology platforms, are better equipped to manage their portfolios in a downturn than many of these tech businesses who just 'happen to be lenders'. I expect there will be some consolidation in the industry in the next couple of years as credit starts to tighten up, and that's going to be a game-changer for some of these new guys.

GRENDE: From a small factoring perspective, there's no question that it's disruptive technology that is kind of knocking on the door of the factoring world. I think the merchant cash advance industry is continuing to migrate up size-wise in what they're doing.

In one vein, I think they can be a friend because companies with seasonal issues or one-time events will find this type of financing extremely helpful to them. On the other hand, when you look at companies that are failed business models just waiting to liquidate or are going to liquidate, and really have no reason to exist, I don't think that it's positive for them to be able to put more debt on.

At the end of the day, it goes back to how you look at generating new business. There's a lot that everybody can learn from these organizations in regards to how they market and generate the leads that result in closed financings.

HERNANDEZ: Certainly the stackers are not giving the legitimate MCAs a good image in the industry. In some cases having a merchant cash advance lender in the deal is beneficial, like Dave said, as long as all of the proper intercreditor agreements are in place. We're not funding the same account being debited by the MCA. We have a good understanding of the cash flow of the borrower; and, if we're not in conflict, it could be good. But from my selfish perspective, in instances where a stretch piece is needed, I'd rather do it myself and realize the higher yields on that piece rather than allowing an MCA lender to step in. Life can be a little more complicated in a liquidation if you don't have the proper bells and whistles.

As far as predicting long-term effects, I think the MCA lenders are here to stay. I think the stronger ones are going to survive--the ones that have sensitized their analytics and have taken the proper outside factors into consideration and use some common sense. I don't think it's any different than when purchase order finance companies began to spring up. All can survive in the marketplace, but you need to be the strongest and most adaptable lender to survive.

rom a small factoring perspective, there's no question that it's disruptive technology that is kind of knocking on the door of the factoring world. I think the merchant cash advance industry is continuing to migrate up size-wise in what they're doing. — *David Grende*

ROGERS: I will answer this question just like I answered most of the questions in my accounting class…it depends. I have done deals with MCAs where they provided the additional financing required to get a deal done based solely upon the borrower's cash flow, which we would never have done. In this instance, MCAs have helped my firm and others close deals we would have not otherwise closed. On the other side, I believe MCAs are placing tremendous pressure on the small-ticket factors that typically provide financing to micro enterprises, whose owners are generally not sophisticated financial managers. Many of the firms that typically relied upon small-ticket factors to provide their working capital are turning to MCAs who can generally provide financing faster and with less paperwork. We have received inquiries from

a number of small firms who were saddled with debt from MCAs (I have seen as many as four on one small deal). Unfortunately, in some of these cases the borrowers have ended up on Chapter 11 and/or Chapter 7. I predict that marketplace pressures and events will cause the two industries to merge closer, with the end result being the two industries will more closely resemble one another.

MONK: The positives of the industry are that they're bringing some fairly exciting technology in the form of underwriting metrics on the front end. It's hard to say that they're really competitors because their credit lines are not really "monitored" collateral lines. I certainly wouldn't call them "asset-based lenders", although a lot of them call themselves "factors" because they claim to be purchasing future receivables. But a purchase of something that does not yet exist is certainly not a true sale from an accounting standpoint.

Still, these lenders are offering money, which competes with asset-based lenders and factors insofar as it provides businesses with capital that they might have otherwise sought from an asset-based lender or factor. But these cash advance lenders aren't monitoring collateral day to day; they're just hitting the borrower's checking account every day for repayment. There have been problems with these lenders because many borrowers don't understand the structure and incredibly high cost they've agreed to…until it's too late. The borrower usually figures out within a few weeks that the financing cost is well in excess of 100% APR, when all the money starts getting drained from their bank account. And when 3 or 4 or 5 or 6 of these cash advance lenders "stack" on top of each other, the borrower has virtually no chance for survival. As a result, the attrition rate for these cash advance lenders is very high (typical client tenure of 4-5 months), and default rates are astronomical. This high attrition/runoff rate makes it very difficult for these companies to accumulate assets without huge origination platforms, which is a big challenge for most of those cash advance lenders looking to grow.

For asset-based lenders and factors, the daily debiting of your borrower's bank account can be a real problem when you wire the client funds for payroll on Thursday night, and the cash advance companies initiate their debits at 12:01am Friday morning, cleaning out all the funds before payroll checks can clear. This can cause big problems for your borrowers, as account debtors who might be required to pay the unpaid workers could offset these funds from your accounts receivable collateral.

But the real struggle in the cash advance industry right now is the cash advance lenders fighting amongst themselves – i.e. "stacking". The "right" to debit the daily repayment from the borrower's bank account is not based on any sort of "collateral priority". So, when there are multiple cash advance lenders stacked on top of each other, it becomes a race to be the first one to debit the borrower's bank account each day (to get repaid ahead of the other cash advance lenders…before the money in the bank account runs out). This is why "stacking" has become such a huge problem within that industry, as they are cannibalizing each other and increasing the likelihood of default by their own borrowers.

WINICOUR: Before we were in the MCA space, we actually had a watch list credit that we were worried was headed to a liquidation. We had a well-known MCA provider, who provided $650,000 on Christmas Eve to that borrower. Ultimately, it didn't save the company, but it allowed this business to extend another couple of months so that they could properly align themselves and prepare for a sale. This not only gave the ownership more value, but also allowed Gibraltar to get out of the deal 100% without having to go through a liquidation. So, in terms of friend or foe, of course there are a lot of good professionals in the industry, but clearly there are also some stackers and players who are just trying to squeeze every nickel that they can out of this higher yielding paper. As a client, you have to make sure you're working with MCA companies that have a solid reputation and can give you the help you need.

GRENDE: I'd like to ask Scott and Secil whether they believe that the MCA industry is heading eventually towards a regulated environment.

WINICOUR: It's really hard to say. The CFPB is coming out with new payday lending rules and has been dancing around MCA/online lending for a while. For many years, people were saying that factoring was going to get regulated at some point in time, and ABL was supposed to be regulated, and it never happened. If we regulate every specialty finance business, well, then we might as well all be banks. I think there has to be some balances for private entrepreneurs who are not regulated and using their own capital, to decide whether or not they want to take the risk that banks don't want to take. So I don't want to say it will never be regulated, but I do think it will be a challenge to regulate, as small businesses need access to unregulated capital.

BAYSAL: I agree with that. There's definitely more pressure on the category. There seems to be increasing concern about the regulatory arbitrage and the fact that these advances are not considered loans. It's very much a state-by-state regime so I don't think we're going to see any federal solution yet.

But I think that the biggest pressure is really going to come ultimately from the market, and that's why you see a lot of these players trying to reduce their effective cost-to-borrow. I think transparency is also a big issue and, quite frankly, many borrowers don't fully appreciate how much these loans actually cost.

Rates are coming down on average, but that has been largely driven by longer terms offered on these MCA products. That obviously increases the credit risk in a downturn scenario. **TSL**

Eileen Wubbe is senior editor of *The Secured Lender*.