

# Financing

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# Reasons Companies Borrow

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- Large purchases
- Cyclical inventory build-up
- Pay suppliers before collecting from customers
- Tax incentives
- Leverage return on investment

# Sources of Financing

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- Banks
- Finance companies
- Factors
- Insurance companies
- Pension funds
- Venture capital groups
- Bondholders
- Government entities

# Characteristics

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- Amounts
- Repayment terms
- Costs
- Collateral
- Loan covenants/events of default

# Financing Structures

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# Factoring

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# Why Use Factoring

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- Bridge the funding gap
- Ready source of funds
- Outsource credit management

# Parameters

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- Terms of sale
- Average invoice
- Dilution
- Total sales
- Amount of financing needed



# Factoring Structures

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- Recourse vs. non-recourse
- “Upon collection” vs. “at maturity”
- Advances
  - advance rate
  - interest rate
  - overdraft privileges

# Factoring Structures

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- Notification
  - pay the factor
  - blind lock box
  - pay the seller (no change)
- Order-to-order vs. line of credit
- Including inventory
- Factor guarantees & letters of credit

# Finance Companies

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# Differences Between ABL and Factoring

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- Not a purchase, just a security interest
- Who takes the credit risk
- Who collects payments
- Rates
- Inventory included
- Non-notification

# Qualifying Assets

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- Receivables
- Work-in-process
- Inventory

# Parameters

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- Average book balances
- Business cycles
- Dilution
- Write-offs

# Structures

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- Advance rates
- Notification
  - blind lock box
  - pay the seller (no change)

# Banks





# Broad Range of Products

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- Repayment terms
  - short-term
  - medium-term
  - long-term
- Character
  - revolving lines of credit
  - bullet loans
  - installment loans

# Broad Range of Products

- Collateral
  - asset-based loans (receivables & inventory)
  - mortgages
  - loans secured by miscellaneous assets
  - equipment loans
  - unsecured loans
- Purchase of receivables
- Asset securitization

Banks try to match the structure to the use

# Leasing

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# Lessors

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- Manufacturers
- Banks
- Finance companies
- Leasing companies

# Types of Leases

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- Operating
- Capital
  - lease lasts most of the life of the asset
  - payments amount to a significant portion of the value
  - automatic transfer of ownership at end or option to buy
- Sale-leaseback arrangements

# Leveraged Buy-Outs

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# Government Programs

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# SBA Loans

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- Borrowers
  - small businesses
  - marginal credit-worthiness
- Structures
  - guaranteed loans (90%)
  - direct loans
- Special programs
  - minority-owned businesses
  - woman-owned businesses
  - low-income proprietors
  - change of equipment due to new regulations
  - exporters



# Exim Loans

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- Programs
  - working capital guarantees (90%)
  - medium-term & long-term guarantees (15% down, then 100%)
  - direct loans
- Borrowers
  - exporters
  - small businesses needing more money than SBA provides
  - companies providing goods to foreign projects
  - manufacturers of capital goods
- Restrictions
  - exportation of U.S. goods
  - military goods excluded

# Bottom Line

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- Financial statement analysis goes beyond balance sheets
- Some research into who a potential customer is borrowing from, for what purpose, and under what structure can provide insight into the company's financial stability

Tip: The type of financing should match the use of funds