



Annual Factoring Survey Report of Findings

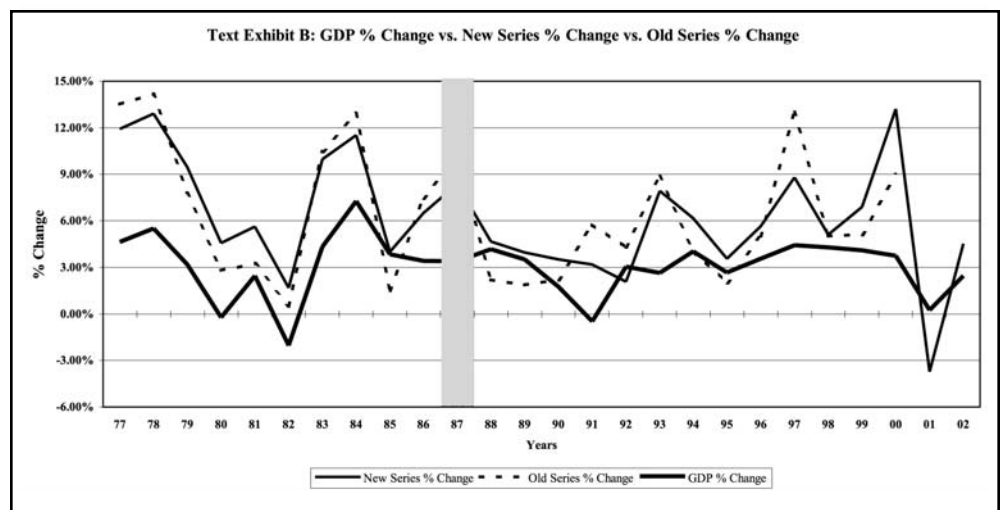
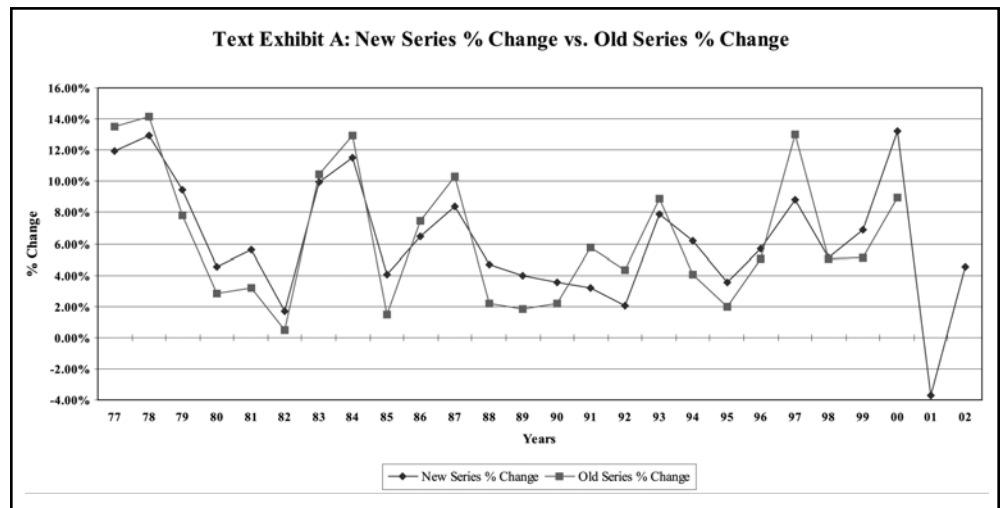
Part I — General Industry Results

The volume of factoring rebounded in 2002 from its first decline in the 27 year history since this data has been tracked. In 2001, a year in which this data was not previously reported, its volume dropped by 3.72%, or nearly \$3.6 billion from Year 2000. As shown in **Appendix Exhibit 1**, the industry grew by 4.52% over the previous year. As further shown in **Appendix Exhibit 2**, this increase put the volume of factoring back on its long-term growth track. (Also, see the related discussion on Page 4 in connection with **Text Exhibit D**.)

A revised data series is now being used to track the volume of factoring. The new series has been revised backward to 1976 in order to provide readers with a consistent report of comparable data. **Appendix Exhibit 2** contains the actual data for both series through 2000. However, only the new series is carried forward beyond that year. **Appendix Exhibit 3** presents the percentage changes from year-to-year in the two series.

In **Appendix Exhibit 3**, beginning in 1988 the new series tracks the impact of economic conditions on the volume of factoring. Prior to that time, movements among the two were highly similar. At that point the old data set became less reflective of the effects of economic movements on this industry. Furthermore, most of the changes exhibited there were flatter and, thus, less illustrative of these effects. The new series better reflects the changes that took place in and around the recession of 1990 - 91. Plots showing the percentage changes in both of these series are presented in **Text Exhibit A**.

Text Exhibits B and C compare changes in the movements of two important economic indicators that are thought to affect factoring volumes in both of these series — Real Gross Domestic Product (GDP) and Total Employment. A careful examination of the two exhibits indicates that, while both data sets show that changes in factoring volume tend to lead or be coincident with these economic changes, the new series foretells such changes in these broad measures of fiscal activity much more accurately and with much smaller variation. While movements in both series have



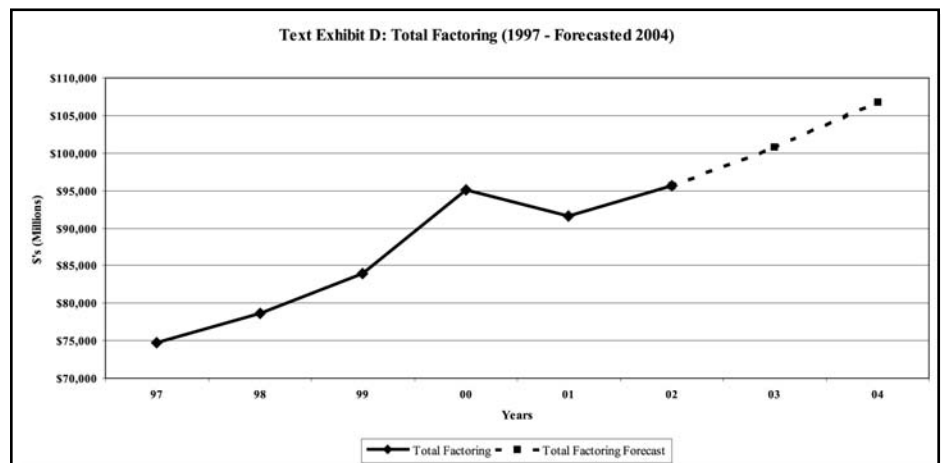
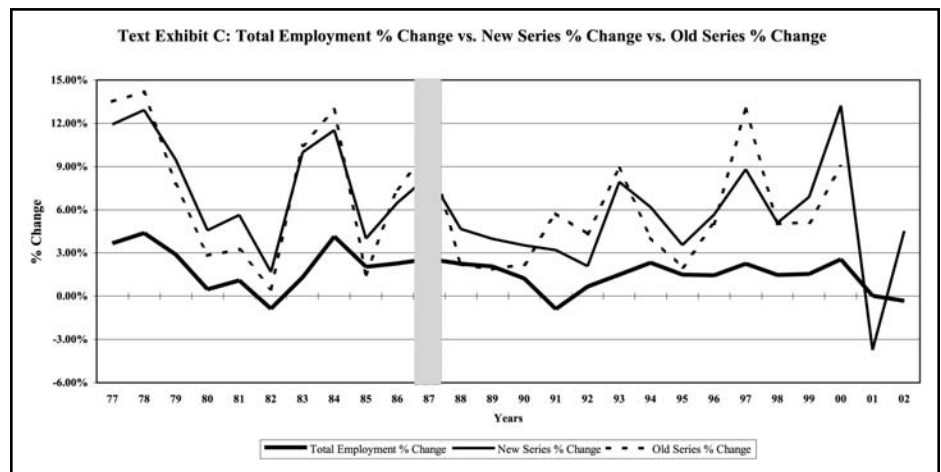
Annual Factoring Survey

tracked total employment coincidentally in almost all of the years since 1976, the new series has done so in a closer fashion. On the other hand, between 1987 and 1994 changes in the new series generally led those of the GDP. After that time, as can be seen in **Text Exhibit B**, and until 1998, movements in the volume of factoring

became less influenced by the GDP and, although not shown herein, much more affected by the very strong, upward pace of the stock market (▲45.38% between 1997 and 1999). This arose because the added personal wealth the market created caused consumers to demand more goods and services. Manufacturers and suppliers, therefore, required more financing to cover their receivables, resulting in the largest increase in total factoring. GDP was slow to respond. However, the huge decrease in the stock market by the fall of 2001 (▼17.99%) quickly dropped the GDP and caused the market demand for goods and services to rapidly decline, the economy to subsequently go into recession, and the customers and clients of factors to react to both. As presented in **Appendix Exhibit 1**, the combined effects of these caused the first decline in total factoring in recorded history (▼3.72%). In 2002, both the stock market and product demand have begun to increase. As seen graphically in **Text Exhibit B**, in general the factoring industry has partially corrected for last year's overreaction and has done so in response to the slow, but positive turnaround of the stock market (▲8.23%) and in the GDP (▲2.93%). Between 1987 and 2001, factoring grew at a compound rate of 5.01%. In 2002 it grew at a rate of 4.52%.

Based on estimates of both the GDP for 2003 of 4.01% and for total employment of 2.20%, and given the recent strong upward movements in the stock market of 8.23% through November 2003, we feel that it is very likely that total factoring in the industry will rise by 5.30% in 2003 to slightly over \$100 billion and by another 5.90% in 2004. This should put the level of total factoring well over \$100 billion. Our estimates are further bolstered by the Federal Reserve's continued pressure to maintain interest rates at a low level for the foreseeable future and by positive movements in other important determinants of factoring volume. **Text Exhibit D** presents a graphic view of the recent trend in total factoring with the inclusion of the two-year estimate we have just presented. If our forecasts are borne out, total factoring volume will return to the growth path that it has followed since 1992.

Appendix Exhibit 4 explores movements in factoring levels in comparison to those of its sister form of funding, asset-based lending. **Appendix Exhibit 4a** tracks total factoring advances in relation to asset-based outstandings over the last six years. During this period both seem to have moved together quite closely. Interestingly, while asset-based outstandings serve as the floor for its form of financing (and, thus, is often referred to as its "lending base"), total factoring advances represents the ceiling for its own segment of the industry. The latter is to be expected because such volume measures the speed at which various instruments of sale are purchased, collected, and new ones purchased again. Such activity, then, can be thought of as total factoring advances. A comparison of the two in this exhibit indicates that asset-based outstandings are approximately 3.5 times that of the factoring advances. (Note the differential size ranges presented on the right and lefthand sides of the exhibit). Even more interestingly, although both measure different aspects of their respective forms of financing, their identical movements appear to indicate that both are affected in a nearly identical manner by the various economic influences. Although otherwise incompatible as comparative measures of their respective forms of financing, both moved upward in a similar manner during the market run-up that occurred during the first four years and fell after that time when it dropped and slowly recovered thereafter.





Appendix Exhibit 4b shows the comparative movements of both asset-based and total factoring advances during this period. Although both measure the same aspects of each form of commercial financing, their growth patterns are much more out of sequence with one another than are those of the two non-comparable series pre-

sented in **Appendix Exhibit 4a**. Thus, the movements of the two more comparable measures appear to be anomalies. Part of the reason for this is the sheer size difference between asset-based advances and that of factoring advances. Over the last six years the velocity of asset-based lending has ranged between 22 and 34 times that of factoring. This provides a greater range over which swings in direction can occur.

The graph further indicates that not only is the volume of asset-based lending advances much larger than that of its comparable total factoring measure, it is also much more sensitive to changes in economic conditions. Asset-based deals tend to be much larger than those that are undertaken by factors. Factoring arrangements are generally much smaller in size and more focused on individual industries than are those of asset-based lenders. However, the smaller size of their deals allows them to better diversify their risk among their clients/customers than the larger asset-based providers. From this prospective, factors also have more flexibility to react to economic changes than asset-based lenders.

There are also other differences between these two industry segments that affect the reactions to changes in their operating environments. In part, these arise from the fundamental distinctions between buying, and owning, accounts receivables and other instruments of sale versus collateralizing them to protect more traditional lending arrangements. Ownership forces factors to be more directly involved with their clients/customers in order to protect their investments. To do this, they must continually monitor supply and collection conditions at both the latter and, as well, at the firms who purchased goods and/or services from its clients/customers. (Note that it is these buyers who are ultimately responsible for repaying these obligations.) This is especially true in nonrecourse arrangements. This unique approach to financing businesses and the development of more personal working relationships with these firms enhances the collection of factored outstanding instruments. Asset-based lenders also monitor those that finance through them, but not to the extent that factors must. Asset-based lenders focus more on loan repayment and the quality of their collateral. This difference further slows somewhat their response to changes in both economic and financial conditions.

The purchase of receivables and other instruments of sale versus their collateralization also has an impact on the speed at which

each type of financing reacts to changing external conditions. Instrument purchases are by their very nature more risky than the collateralization of them. Thus, factors tend to be less risk averse than are asset-based lenders. Collateralizers can call in loans faster under the threat of foreclosure and ultimate asset seizure. However, factors have to rely on their own collection capabilities and, in some cases, charge back their clients/customers to extinguish the payment obligations to them. Thus, they will tend to hang in longer in the financing process than will asset-based lenders.

A more tenuous explanation of the differential movements over time between asset-based advances and factoring advances shown in **Appendix Exhibit 4b**, is that which may occur because of the divergency of the types of industries on which each focuses. Asset-based lenders are more involved with durable and hard goods manufacturers. This is a result of their larger deal orientation. On the other hand, as discussed later in connection with **Text Exhibits H and I**, while 41% of factoring is carried out in manufacturing and manufactured products, only 9% is in heavier manufacturing. The remainder is concentrated in its more traditional business financing areas of textiles, apparel, and other lighter goods. Orders for heavier goods generally have much longer lead times than those for lighter ones and for firms supplying wholesale, retail, distribution and services. New orders transform themselves directly into requests for needed funding. The result is that the volume of asset-based lending is affected by changes in business activity earlier than is that for factoring.

Text Exhibit E expands upon **Appendix Exhibit 4** to illustrate the substantial difference in the magnitude of asset-based outstandings and that of both factoring advances and factoring lending base. **Appendix Exhibit 4** shows the comparative movements between these measures by changing right and lefthand scales appropriately. However, asset-based advances are so large in relation to that for factoring, we could not plot them on the same graph using the same axis increments. (Earlier we mentioned that they ranged between 22 and 34 times larger than that of factoring advances.) Thus, the magnitudinal differences can not be seen there. **Text Exhibit E** also includes a plot of the factoring lending base. As discussed in the SFNet's Annual Survey of Operating Statistics for the Asset-Based Financial Services Industry, outstandings represent the fundamental lending base upon which advances are generated. No direct data has as yet been collected on that aspect of factoring. However, we have attempted to estimate its size herein for the first time.

The huge difference in size between asset-based outstandings and that estimated for factoring is obvious in **Text Exhibit E**. The gap over the six-year period plotted there has also been as large as that for advances, nearly 34 times. Because the factoring lending base is so much smaller, it can sustain advance levels that are much smaller than that for asset-based lending. Thus, the huge differences between these two forms. **Text Exhibit E** also



illustrates the absolute size differences between factoring lending base and levels of its own advances. Between 1997 and 2002, the gap between them has widened almost continuously. Based on estimates, in 1997 factoring advances were \$67.7 billion larger than its lending base. In 2002 the difference stands at \$80.8 billion.

Thus, if estimates are correct, over this period factors have steadily improved the efficiency in which they have used their base of lendable funds.

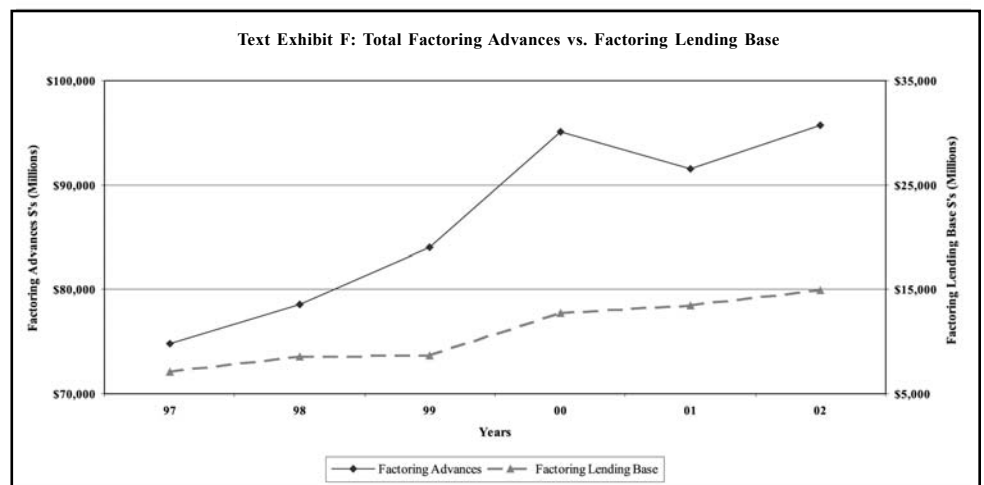
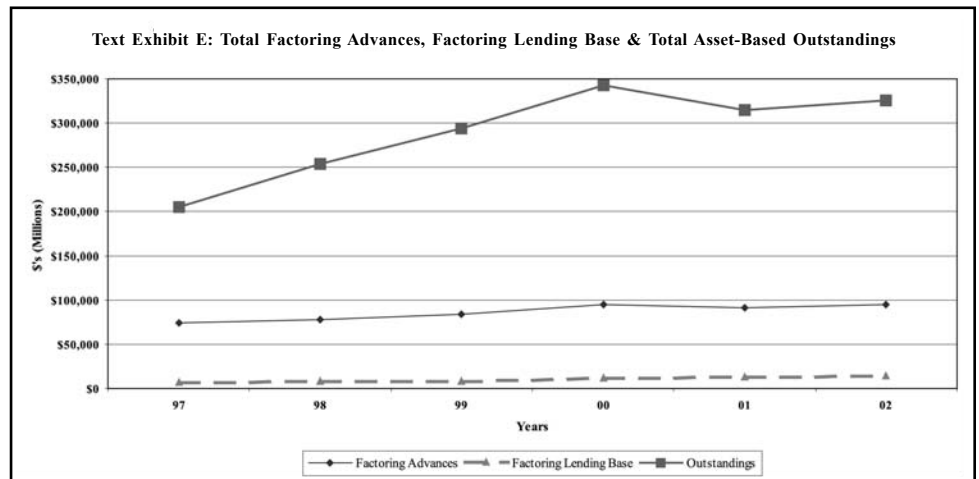
The data in **Text Exhibit F** focuses purely on the relative movements of factoring advances and factoring lending base. While they have moved away from one another in terms of their absolute size, on a relative basis the advances have grown at a much faster pace. Since 1997, the factoring lending base has risen at a compound rate of 16.17%. In comparison, advances increased at a rate of only 5.06%. In general, the two have moved similarly in response to changes in economic and other related conditions. However, factoring advances have been more volatile. Moreover, while advances dipped in 2001, the lending base continued to rise. Except for this one year, factoring advances have also risen. This is in contrast to asset-based advances that have fallen in 3 out of the last 5 years. Also, while asset-based outstandings fell in 2001, the factoring lending base continued to increase.

Appendix Exhibit 5 represents regional factoring activity. The area breakdowns are somewhat different than those presented in the Annual Survey of Operating Statistics for the Asset-Based Financial Services Industry. This is because factors tend to deal with clients/customers that are much smaller in size and, therefore, generally operate within more limited boundaries than do asset-based borrowers. We have broken the U.S. down into smaller, more economically cohesive areas. Thus, instead of splitting it into just 7 regions, we have divided it into 11.

The list of U.S. regions contained in **Appendix Exhibit 5** is ordered in terms of their 2002 factoring volumes. The volume of total factoring in the top two regions, i.e., the Lower Northeast and the Far West, were both larger than all of the remaining areas combined. This was nearly the case

for the previous year as well. In fact, the 2002 volume of factoring in the third-place region, the Eastern Southeast, was also larger than that of all of the remaining locations below it in the list. Together, these top 3 regions accounted for 83.6% of all factoring in the United States in 2002 and almost that in the previous year. The reason for the dominance of factoring in the Lower Northeast and in the Eastern Southeast is that they have long been the cradle of those industries that traditionally use factoring as one of their primary sources of short-term and seasonal funding — wholesale, retail, clothing manufacturing, and textile production. However, as these industries have been sluggish during the recent economic downturn and weak recovery, so too has been their factoring performance. At the same time, the Far West region has exhibited strong growth — the second highest at 10.38%. Many of the industries located there that were hard hit by the recession and stock market decline have remained slow to recover. However, certain other sectors have begun to rebound and, accordingly, so has their demand for short-term capital. This has been fueled especially by the importing and transportation industries.

In several regions growth rates in asset-based lending and in factoring have moved strongly in opposite directions. While the volume of factoring in the Eastern Midwest rose at the highest





rate in the United States this year (28.18%), in terms of asset-based lending it fell by nearly 16%. In Canada, factoring increased by the second highest rate (27.08%). However, asset-based lending there experienced the greatest rate of decline at -65.24%. Lastly, in the Western Midwest, where asset-based lending was the only location

to increase at a triple-digit rate (+114.18%), the volume of factoring fell at the fastest pace of any region, -35.33%. These differences may well be accounted for by the disparate types of industries that use each of the two forms of lending and by the overwhelming differences in the volume of asset-based lending versus factoring advances that take place there.

Another new area explored for the first time is the volume of spot versus continuous factoring. Spot purchases of various instruments of sale, especially accounts receivable, is a relatively new activity. Because no data on such factoring was collected before, it cannot determine at this time how quickly it has been growing. However, as indicated in **Appendix Exhibit 6**, it remains a very small proportion of the reported volume at only 3.26% of the total. In most of the areas it represents an even smaller proportion of the total volume. The areas with the largest factoring volume also do the most spot factoring. On average, factors in the top 3 regions carry out only 2.58% of their total trade obligation purchases using spot factoring. Factors in the South Central regions of the U.S., i.e., the Southwest and the Western Midwest, do the most spot factoring — 15.62% on average. However, between them their total volume amounts to only 5.6% of all U.S. factoring activity.

Spot factoring is often used to fill a gap in client/company needs for temporary financing where a large, one-time transaction with a single buyer has taken place. However, it is more risky and more expensive to carry out than continuous funding activities with regular clients/customers. Thus, it is not likely that spot factoring will comprise more than about 5.0% of the total volume advanced in the future.

Appendix Exhibit 7 presents an evaluation of the characteristics of the clients/customers that used factoring in 2002. In **Part II** of this report, i.e., that which deals with the specific attributes of the industry, more focus is offered as to the nature of some of the activities that has generated a need for this type of financing.

In **Appendix Exhibit 7**, the top 5 areas contain over 75% of the companies that do factoring in the U.S. (If Canada was placed in the list, it would rank 6th.) Furthermore, the clients/customers in these sections of the country accounted for 83.5% of the total U.S. employees who work for all such users of factoring services. The average factoring volume per company was \$6.70 million in the U.S. and \$4.52 million in Canada. Elsewhere in the world the

average was only \$1.90 million per company. This indicates that on average American companies make more use of factoring than other areas in the world. However, this instrument varies widely among overseas countries, especially those in Western Europe.

By far the heaviest volume of factoring per client/customer was in the Lower Northeast. Each firm there sold an average of \$11.13 million of its receivables and other instruments to factors in 2002. The volume of factoring was the smallest in the Southwest where the average “borrower” financed only \$1.65 million in this manner. (As already discussed, overseas it was even smaller at \$1.90 million per company.) The average size U.S. client/customer had 192 employees. Canada was close in size with 203 employees per company. Overseas firms averaged only 26 employees. Perhaps the most surprising find regarding these companies is that in those regions that would be expected to have the largest sized firms using factoring, those there were the smallest; and vice versa. The second highest volume of factoring took place in the Far West. Yet, users there were of the smallest size, averaging only 56 employees. On the other hand, the largest sized users were located in the Middle Atlantic states where the average firm had 525 employees. Over all, these results indicate that firms that use factoring are generally small to mid-size in their operations with somewhat modest short-term financing needs.

Employee productivity, if measured in terms of the volume of factoring needed to sustain activity, is substantially higher in the Far West than in any other region evaluated. In 2002, factoring by companies located there amounted to \$135,389 per employee. Evaluated from this perspective, it was 1.7 times higher than that of the next largest section of the U.S. and foreign areas surveyed. Surprisingly, given the sparsity of businesses located there, this second position was held by firms operating in the Plains States at \$79,040 per employee. Factoring volumes in Canada amounted to only \$22,249 per employee. On average, the volume of factoring per employee of a client/customer was \$34,936 in the United States in 2002.

Factoring activities in terms of clients/customers and their employees are much smaller than those who finance themselves through asset-based lending. This is to be expected since asset-based lending was nearly 22 times that of total factoring in 2002. A comparison with **Appendix Exhibit 12** in the Annual Survey of Operating Statistics for the Asset-Based Financial Services Industry indicates that asset-based lenders had 4.6 times as many borrowers as factors had clients/customers. And these asset-based lending firms had 7.2 times the volume of employment as did factors.

The average sized asset-based borrower in the U.S. and Canada had 289 employees. In comparison, those using factoring were significantly smaller in size, having only 192 people working for them. The asset-based borrower also financed themselves at 4.7 times the amount of those that sold their instruments of sales to factors in 2002 in these comparable areas — \$30.1 million versus



\$6.6 million. This is to be expected since, as mentioned earlier, many asset-based lending deals are very large, especially in relation to those carried out under factoring deals.

In terms of productivity, the volume of factoring used per employee was \$34,253 in the U.S. and Canada in 2002. By comparison, the figure for

employees of asset-based borrowers was \$104,381. Thus, firms that raise their short-term funds through the use of asset-based lending facilities required substantially more funding to conduct their short-term operations than did factoring companies.

In 2002 there were 3,982 people employed by the factoring industry. They produced an average of slightly over \$24 million in total factoring volume. In comparison, the 16,425 employees who worked in the asset-based lending industry on average produced \$127.2 million each

Part II — Results of Specific Attributes Portion of the Questionnaire

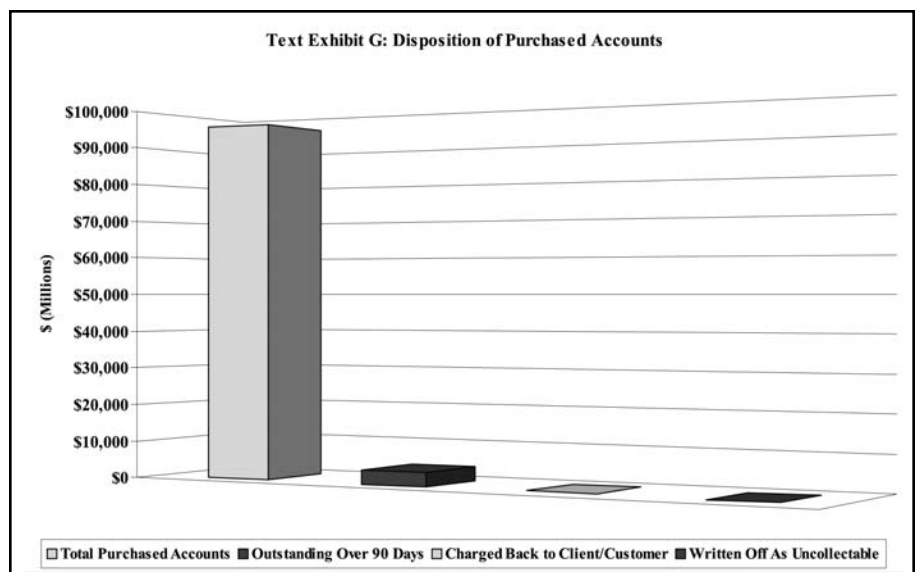
On average in 2002, purchased receivables were 5 days old at the time they were accepted by factors. Once purchased, it took an average of 42 days to collect them. At the time of their repayment the average age of the purchased receivables was 47 days. Typical terms offered by clients/customers to their buyers are net 30 days. Therefore, on average, factored receivables were 17 days past due at the time of their recovery. Outside studies have shown that on average 96% of new receivables will eventually be collected. At 30 days outstanding, the collection rate drops to 91%. Of those that remain uncollected after 90 days, only 74% will eventually be repaid. Based on these results, factors would be expected to receive only about 78.2% of the face value of the instruments of sale at the time of their initial purchase. By comparison, only 3.78% of the total factoring volume or \$3.6 billion were over three months old before they were collected. Thus, the industry's overall collection rate on its purchased receivables and other instruments of sale far exceeded that which has generally been experienced by the typical short-term lender. Of those instruments that remained outstanding at that time, 5.92% or \$214 million were charged back to firm's clients/customers, while 0.32% or \$ 12 million were written off as uncollectible by those firms. **Text Exhibit G** provides a graphic presentation of the magnitude of these differences.

Nearly 50% of those receivables that were charged back to the clients/customers were due to various disputes between the client's/customer's and their buyers that were made known to the factor. Some examples of these disputes are disagreements as to product price, differences upon receipt regarding its agreed upon specifications and/or quality, and dissatisfaction with the timeliness of delivery.

Of the remaining charge backs, about 40% were due to credit problems associated with the client's/customer's buyers. The balance of these returns, i.e., 10%, were due to disputes between

the two parties to the transactions that were not revealed to the factor. Hence, findings indicate that at the time of the charge back, the purchased receivables averaged 70 days past due. Typically, they were 100 days old when factors returned the uncollectible accounts to their clients/customers for payment. As will be discussed later in connection with **Text Exhibit J**, most factors offer their services on a nonrecourse basis. These latter instruments were written off much later. On average, they were nearly 4 ½ months past due when they were taken off the factor's books.

With the various types of instruments of sale in 2002, nearly all of the reported volume was comprised of accounts receivables. The remainder was accounted for by letters of credit (LCs) and banker's acceptance purchases. LCs are the fastest growing instrument of sale in the industry. Although response data for purchase orders is not statistically significant, anecdotal information indicates that they are the second fastest growing instrument of sale in the industry.





Typical accounts receivable transactions reported ranged from about \$25,000 to approximately \$3.5 million. Therefore, on average, the funds advanced per transaction to clients/customers ranged from \$19,640 to about \$2.95 million per deal. However, many such financing arrangements well exceed this range. On the other hand, many

factors, including the larger companies, generate their overall factoring activity through a high volume of small to medium size deals. This practice helps to reduce their overall exposure to the impact of collection risk on their businesses. It also creates added competition within the industry. This is particularly the case with small and medium size factors where the smaller size of the deals into which they typically undertake is not a barrier to entry.

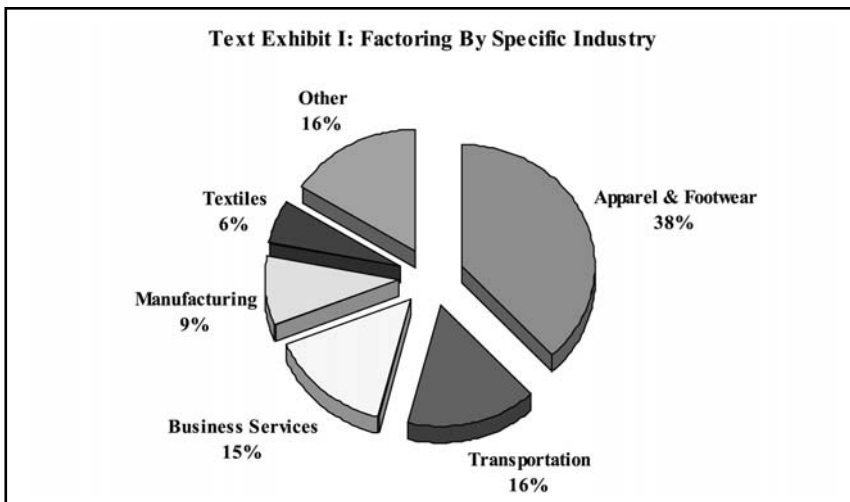
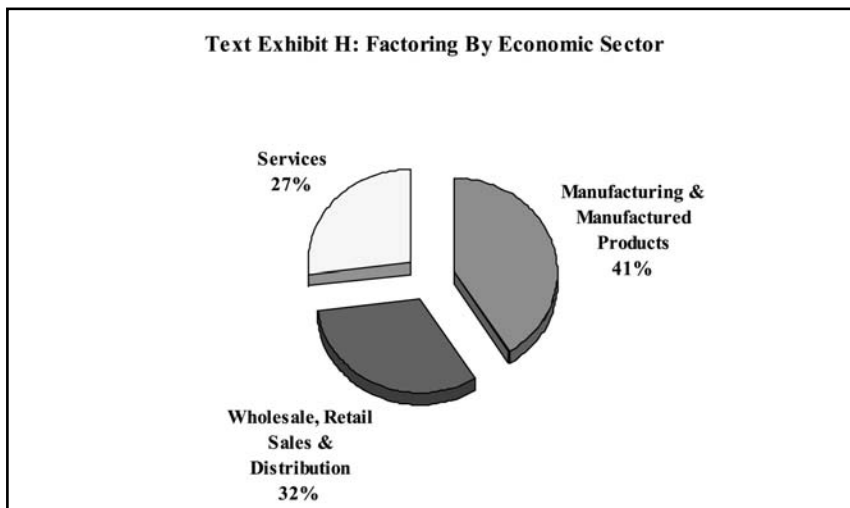
Nearly all of the factoring that was carried out among the various regions in the world was done within their own domestic borders. More specifically, 94.6% of the volume of transactions that were reported took place solely within their boundaries in 2002. The remaining portion involved export-import related activities.

Although not yet as significant a volume as domestic factoring, international trade financing based on factoring arrangements is growing significantly between the U.S., Canada, the United Kingdom and in other parts of Europe. These expectations are well founded, in part, by the history of commerce in both Western Europe and the U.K. who long ago developed this funding technique to facilitate trade both domestically and internationally.

In **Text Exhibit H**, factoring volume within these countries was derived from three primary sectors of the economy. The largest, manufacturing and manufactured products, includes both durable and nondurable goods. In 2002, this segment comprised approximately 41% of the total factoring volume. Wholesale, retail, and distribution of goods and products constituted 32% of the total. The service sector, which includes medical, dental practices, legal practices, various types of business consultants, temporary staffing and employment agencies, marketing and advertisers made up the remaining 27% of the factors' purchases of sales instruments.

Text Exhibit I provides a graphic overview of the specific industries that are contained in **Text Exhibit H**. As shown, there are 6 primary industries that factor their various instruments of sale. As has traditionally been the case, the apparel and footwear industry comprised the single largest group that made use of the factoring industry's services. In total, the

volume of financing generated by this source constituted 38% of total aggregate sales instrument purchases. This amounted to nearly \$36.4 billion in 2002. Of this total, 26% was utilized by clients/customers who manufactured these goods. The remaining 12% was utilized by firms involved in the retail sale of these goods and products. In **Text Exhibit I**, transportation was the next largest sector that used factoring as a short-term funding source. It represented \$15.3 billion or 16% of the industry's total volume. Business services constituted 15% of the total or \$14.4 billion. Within this group are firms that provide support to commercial and industrial enterprises. They include, among many others, employment services, temp agencies and printing services. The "Other" category represents 16% of total factoring which includes a diverse group of clients/customers involved in consumer-related activities. These include medical and dental practices, environmental services, fuel dealers, giftware, toys and sporting goods franchises. Nontextile related light and medium manufacturing comprised about 9% of the total volume of factoring. The remaining portion of factoring volume was derived from textile manufacturing. It constituted approximately 6% of the industry's total financing activity.





The first form in which factoring arrangements are offered is that involving the degree of recourse the factor has to the client/customer in the event that its goods and services purchasers do not pay their receivables obligations. Under nonrecourse financing the factor assumes the risk of nonpayment by the client's/

customer's obligator. Such agreements are happen only when the obligation has a strong credit rating, regularly does business with the client/customer, when there has been few if any disputes between the two entities, and/or a long-term supply contract has been consummated between them. In addition, the client/customer must be one who regularly finances through and/or is well known to the factor. As indicated in **Text Exhibit J**, this form of factoring constituted 56%, or \$53.74 billion in such financing in 2002.

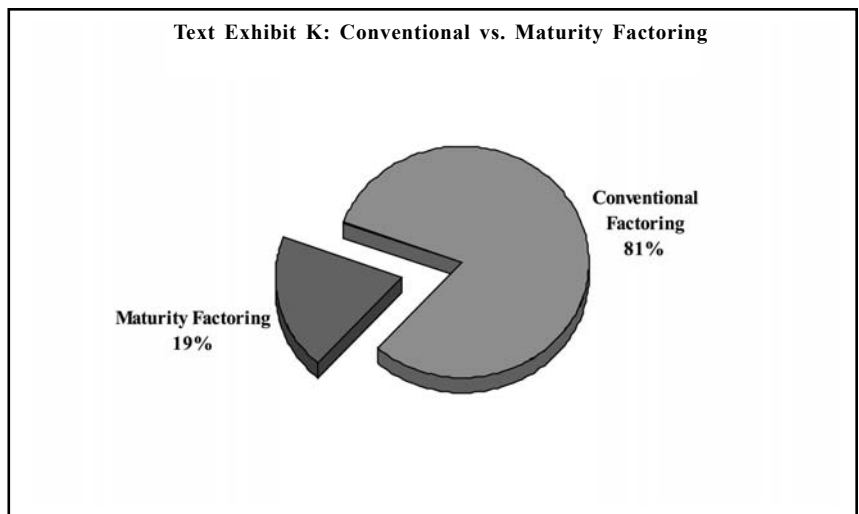
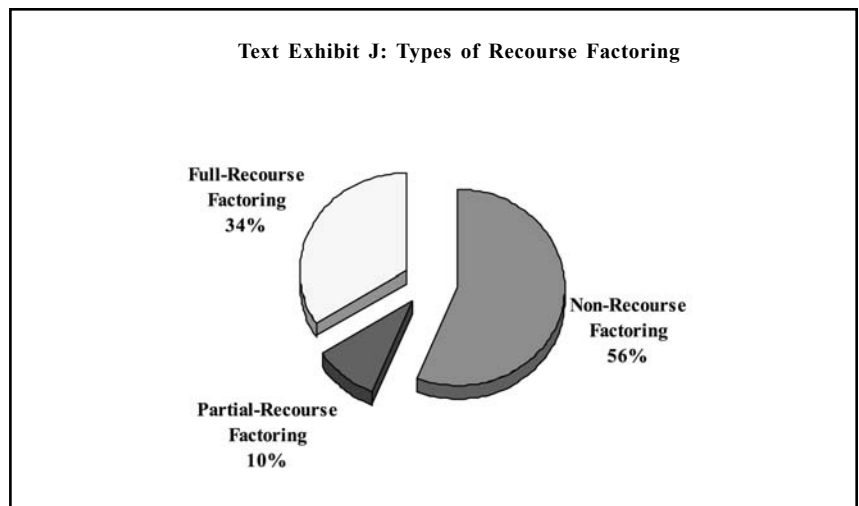
The second form in which such arrangements are carried out is that of full recourse factoring. The factor's client/customer is held ultimately responsible for all buyer defaults on the instruments of sale that it purchased. The factor includes this provision in its funding agreement with a client/customer when the latter is selling to a large number of firms considered to be poor credit risks and the client/customer itself has a good credit rating. It also includes this stipulation when such firms have had a prior history of default, are in weak financial condition, are unknown to the factor, and/or have purchased little or no products or services from the client/customer, and/or will only be doing so in the future. Finally, from the opposite end of such arrangements, the full recourse facility is required when the factor has done little or no business with the client/customer in the past. In **Text Exhibit J**, full recourse factoring accounted for 34% of this form of commercial finance in 2002. In total, this form of factoring generated \$32.40 billion in financing activity.

The last form of this type of factoring is a blend of the previous two arrangements. Known as partial recourse or modified recourse factoring, it is usually carried out in one of two ways. The first takes place when the factor and its client/customer agree to share the risk of non-payment by the buyer of the latter's goods and services. In this case, the factor has recourse against the client/customer up to a pre-set limit. Beyond that amount, the factor assumes the remaining loss. The second version utilizes an arrangement in which the factor segments the client's/customer's accounts into those from whom they will assume the nonrecourse risk and those from

whom they will not. The sales instruments generated by those accounts that have been segmented into the latter category will only be purchased by the factor on a full recourse basis. Thus, the client/customer assumes the risk of loss on the latter transactions. **Text Exhibit J** indicates that this form of factoring accounts for the remaining 10% of the volume of factoring conducted.

Text Exhibit K presents a breakdown of factoring activity based on the volumes of conventional and maturity funding. Conventional factoring is based on an initial advance of funds against a portion of the face value of the factored instrument. A discount is then taken upon receipt of full payment from the buyer to cover the commission for arranging the deal, the interest charged on the advanced portion, and the expenses involved in carrying out the purchase and collection process. The remaining collected balance is then returned to the client/customer.

Maturity factoring involves no financing to the client/customer. The factor takes no discount on the repayment of the obligation created under the instrument of sale. Instead, it receives a fee or service charge as a commission based on the face amount of that instrument. In return, the factor provides credit assurances to the





client/customer for all of a buyer's purchases under a particular sales instrument, collection services, bookkeeping, and other administrative services as is mutually agreed upon. In **Text Exhibit K**, maturity factoring made up the remainder of total factoring based on this breakdown in 2002. In terms of

dollar volume, conventional factoring accounted for \$77.75 billion and maturity factoring accounted for \$17.95 billion.

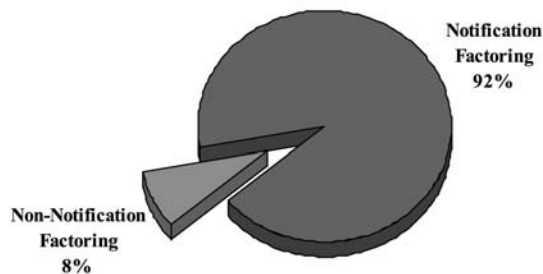
Notification factoring is considered to be one of the primary bases upon which factoring agreements are arranged. In nearly all cases, nonrecourse financing is accomplished under notification requirements. Notification occurs when those buying merchandise and/or services from a particular supplier are apprised that their trade instruments have been purchased by a particular factor. They are then directed to remit all payments made under the terms of their trade arrangement with that supplier, i.e., the client/customer of the factor, to remit all payments directly to the factor, rather than to the client/customer. Under nonnotification, the buyer is not apprised of the sale to the factor of its trade instrument with its supplier and, thus, instead remits all payments directly to the latter. In **Text Exhibit L**, notification factoring is the overwhelmingly most popular method by which factoring deals were carried out. Only 8% of all factoring was done without notifying buyers that their accounts were being factored. Thus, in 2002, nearly \$88 billion out of the total factoring volume of \$95.7 billion was conducted in this manner.

Factoring arrangements may also be broken down between those that are traditional and those that are not. Traditional factoring, also known as "old-line factoring", is carried out both with recourse and with notification to the buyers of the client's/customer's products and services. It is designed to facilitate continuous purchases of factored accounts over a long period of time. Nontraditional factoring focuses upon short-term dealings between suppliers and their buyers. As such, they are carried out on a spot basis and with recourse to the client/customer. Buyers may or may not be notified of this arrangement. Suppliers who fulfill their short-term financing needs are usually in a weaker financial condition than those who don't. Nontraditional factoring is not designed for long-term supply arrangements with product sellers.

Text Exhibit M presents the results of this aspect of factoring activity in 2002. More than three-fourths of all such deals were accomplished under the traditional form of factoring. This amounted to \$74.66 billion, while nontraditional arrangements accounted for just over \$21 billion.

The last aspect of factoring examined was that of refactoring. The term refers to the situation in which a smaller factor re-assigns all or some of its purchased contracts to a larger factor in order to improve its liquidity position. This is carried out by bundling together the instruments of sale they have purchased and selling them to a larger factor who serves as the provider of this service. This is done primarily to reduce the former's cost of servicing these accounts and to permit it to refinance itself. Users of this service, also known as refactors, remain responsible for the collection of its purchased instruments of sale. They earn their returns on the spread between the larger factor's commission fees and its own fees to its clients/customers.

Text Exhibit L: Non-Notification vs. Notification Factoring



Text Exhibit M: Non-Traditional vs. Traditional Factoring

