FINANCE TERMS

Fighting Misinformation:

Don't believe Everything You Read on the Internet

BY LEE HASKIN

Borrowers face an uphill battle when conducting an internet search for capital. Lee Haskin of Crossroads Financial discusses the misinformation out there and offers clarifications concerning certain types of finance products.

I began my career in the finance industry in the early eighties. Times were far simpler then. It was a time when a phone was something that didn't have a screen; you put a dime into it to make a call. Cameras used film and it took days to develop to see the pictures. Your news came from a newspaper or a journalist on TV and a business loan was defined as what it was.

Today, information overload takes place from any number of so-called media channels. Instagram, Facebook, Twitter and an ever-growing number of Internet platforms bombard us with fake news and misinformation on a daily basis.

The catalyst for this article came from an internet search I conducted for the definition of "inventory lending", which happens to be the business I have been perfecting for over 16 years. I also searched the internet for "receivable finance." I was dumbfounded to find any number of non-inventory and non-receivable lending companies defining themselves as lenders in those arenas. Further, through these searches and during many conversations with borrowers and loan brokers/referral sources, I learned that many have a hard time differentiating between a cash-flow loan and a revolving collateral-backed loan.

Back in my day, if you were lucky enough to have all 25 volumes of an encyclopedia, you may have been able to find the answers to most questions. Today, a definitive go-to source on the internet is an online encyclopedia called Wikipedia. The content found on this site comes from the submissions of individuals who might – or might not - have a background or knowledge of the topic for which they are contributing definitions. There is no way for a common person to know whether the source of information is reliable or even credible.

With today's technological advances, information sources are endless and immediate. All one has to do is type – or ask Siri or Alexa - on their phone or computer a question and an answer is provided within seconds. Where that information comes from is often an unreliable source. This is why I caution that you, "Don't believe everything you read on the internet."

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Most funding sources hire outside firms to handle their search engine optimization (SEO) as well as their online marketing. Many of these companies unwittingly spread misinformation simply due to their lack of industry knowledge. It is their job to increase the "hit rate" or "click rate" on the funding company's web site in order to achieve success. The SEO companies have knowledge about, well SEO, and very little knowledge of the definitions surrounding the funding programs offered by their clients. Thus, they utilize the entire myriad of words and phrases that describe any form of funding in order to attract "clicks." This begets a whole new generation of newcomers to the asset-based financing world who are left questioning the true nature of asset-based financing and the differences between them.

Circling back to my recent search using the most popular internet search engine, I found some disturbing results. Results that are not only a disservice to funding sources, but also a disservice to anyone entering the borrowing arena. My search for inventory lenders resulted in two pages of results before I found an actual inventory lender.

According to the results, all forms of financing are covered by lenders like Amazon, OnDeck and Cabbage, along with a myriad of other cash advance businesses. Further, these companies turn out to have the highest results with all of my searches.

Using all variations of words imaginable related to asset-based financing proffers results that makes one believe that every type of funding is covered by some form of cash flow loan. This makes it very difficult for a borrower to navigate through the internet to find the financing relating to their specific needs. One size does not fit all.

To the best of my knowledge, there are two categories under which most financing companies fall. The first is "collateral-backed asset-based financing" and the other is "noncollateral-backed financing." Let's define further:

Noncollateral-Backed Financing: A cash-flow loan (or cash-advance loan) is one where the lender performs due diligence on the historical cash flow of the borrowing company to ascertain that company's ability to pay back the loan.

Accounts Receivable Financing: A/R funding is provided by both the factoring business and receivable financing industry. Whether the funding against the account receivable is based on the purchase of same is with or without recourse, the principle remains the same. Receivables are generated by a seller or borrower based upon the completed delivery of goods and/or services (not future delivery) creating an obligation being due from debtors who have the ability to pay. The key word is "delivered" and never has it been for services or products to be delivered in the future.

Equipment Financing: An equipment lender or bank will make an advance against an often-appraised piece of equipment. This funding would be underwritten at a loan-to-value that would anticipate a full recovery based upon the possibility of liquidating that piece of equipment at the worst time possible and under the most likely scenario that the borrower is going out of business. In many cases, if there is a limited life expectancy of the equipment then the lender would amortize that equipment based upon loss of value as it becomes older. Time frames for equipment could range from as short as two years and as long as ten years from the date of acquisition.

Real Estate Lending: In similar fashion, as applied to the equipment lending business, the loan is made based upon the recovery value of the real estate established at the time of the loan. In almost all cases there will be an applied amortization schedule or repayment schedule as a feature of the loan that is often set at 10 years or greater even if the asset appreciates in value over time. Commercial real estate lending can be for income-producing property, raw land or owner-occupied property that domiciles the borrower's business.

The finance world has gone through many changes since I got into the factoring business 40 years ago, but the basics have remained the same. The definition of each of the lending programs have remained consistent through the years.

Inventory Revolving Lines of Credit: An inventory loan functions in many ways like an accounts receivable line of credit, where a loan is made on inventory already owned by the borrower. The loan-to-value, or how much is to be lent against the Inventory already owned by the borrower, is determined by an industry expert appraisal company that evaluates and provides recovery values for the inventory based on market value and forced liquidation values. The most common value needed is the net orderly liquidation value (NOLV), which gives an estimate of how much could be recovered from the sale of the Inventory in an orderly liquidation over a 90-day time period. The value is net of expenses required during the liquidation period including rent to landlords, payroll and fees to the liquidator as identified in the appraisal. From that appraisal, a borrowing base will be established and provided by the borrower once a week or once a month showing the lender the most current inventory levels, including what inventory was purchased and sold. This allows the lender to adjust the loan value based on the actual collateral to remain "in formula" as inventory levels change during the normal course of business. Companies that borrow are ones that need to hold inventory for sale. They are comprised of companies that sell direct to consumers, like e-commerce and brick-and-mortar retailers as well as companies who sell to other businesses like manufactures or distributors. The important criteria of this type of lending is to have access to the proceeds of the sale of inventory so that the lender can stay in formula as inventory comes in and gets sold over the course of the month and year.

The finance world has gone through many changes since I got into the factoring business 40 years ago, but the basics have remained the same. The definition of each of the lending programs have remained consistent through the years. If a simple internet search delivers three pages of cash flow lenders before a typical borrower is able to find a true receivable or inventory finance company, then it is not just misinformation that concerns me, it is the realization that this is jeopardizing the integrity of the industry by making it such that a borrower or consultant new to the industry may never find the lender who can provide the financing that is needed.

We all need to do a better job of disseminating information on the internet.

Lee founded Crossroads in 2006 to provide inventory and purchase order financing to lower and middle market commercial customers. Prior to Crossroads, Lee was a senior managing partner with Capital Access Group, arranging lines of credit averaging a total $200M per year. Prior to that, Lee was an EVP and co-founder of Great Western Financial Services Inc., a factoring and ABL provider. Lee has over 30 years' experience in the commercial finance industry starting at Allstate Financial as head of sales and marketing. From his career in asset based lending, Lee brings a unique knowledge and understanding of inventory lending. Under his direction and guidance, Crossroads has successfully funded over $240 million in credit facilities with less than a 1% loss ratio.