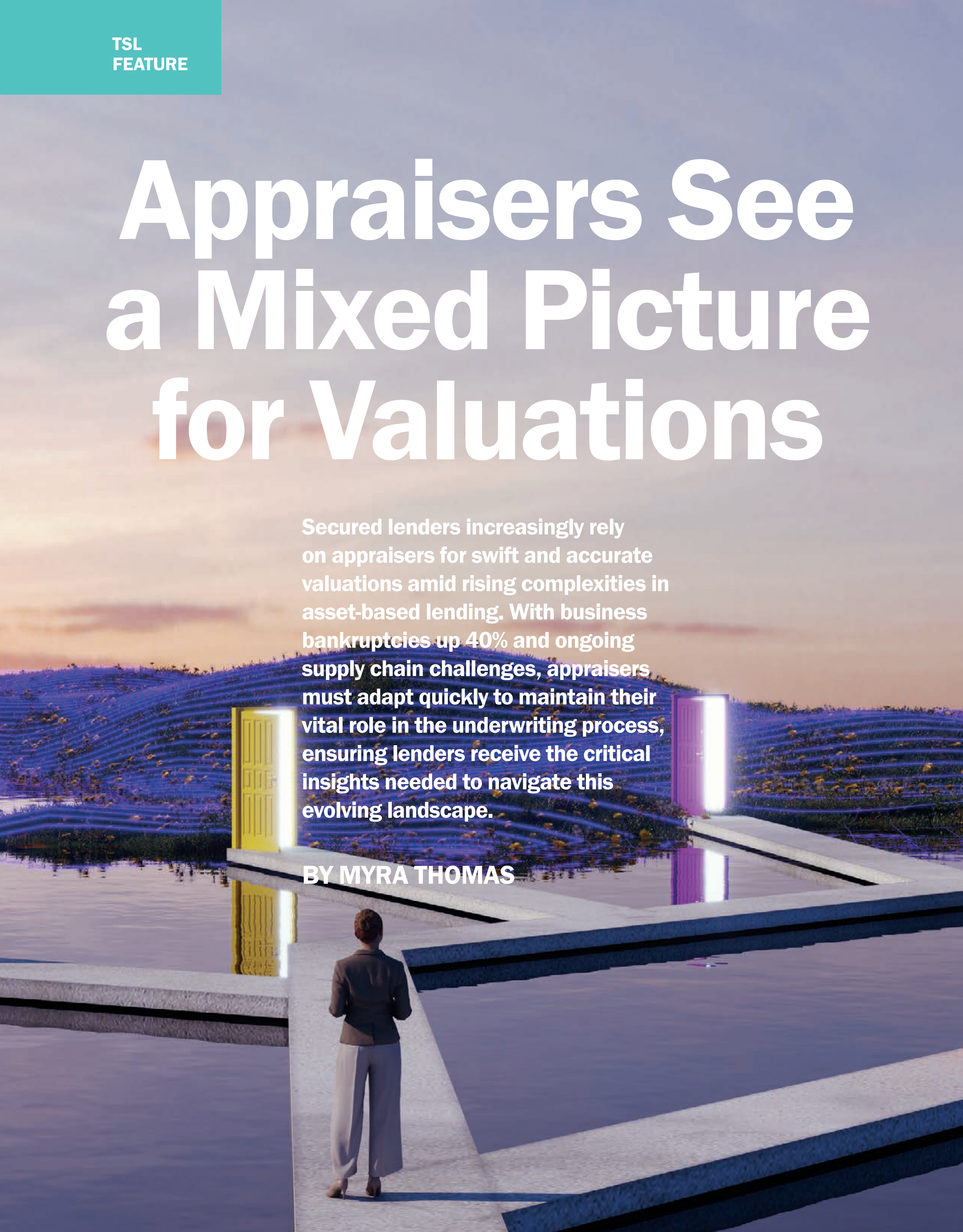


Appraisers See a Mixed Picture for Valuations

Secured lenders increasingly rely on appraisers for swift and accurate valuations amid rising complexities in asset-based lending. With business bankruptcies up 40% and ongoing supply chain challenges, appraisers must adapt quickly to maintain their vital role in the underwriting process, ensuring lenders receive the critical insights needed to navigate this evolving landscape.

BY MYRA THOMAS

Secured lenders are increasingly dependent on appraisers providing accurate valuations and those assessments are needed quicker than ever. As deals become more complicated and competitive, asset-based lenders rely on adept and knowledgeable appraisers to help facilitate the underwriting process no matter the product or economic cycle. In turn, appraisal costs are on the rise, and secured lenders are feeling the pinch.

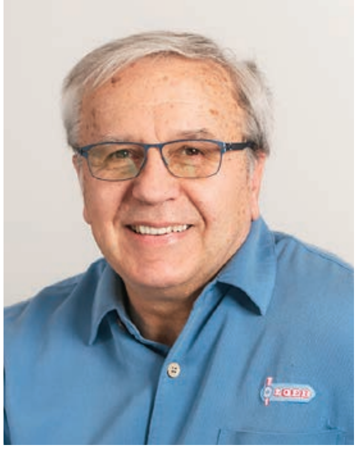
Whether it's COVID-19 or geopolitical conflicts impacting the supply chain, or the recent rise in corporate and personal bankruptcy filings, appraisers are constantly adapting to the new normal. According to data from the Administrative Office of the U.S. Courts, US business bankruptcy filings were notably higher for the year ended June 30, 2024, up 40% from the year prior. But despite the uptick in bankruptcies, Alex Sutton, managing director, head of research, at Gordon Brothers, argues that the majority of companies remain healthy and are "benefiting from increasing availability of capital from the secured lending market."

Of course, there are lingering effects of the pandemic and the supply chain crisis. According to Sutton, aerospace, in particular, is still experiencing long lead times and capacity shortages. Certain building product sectors, such as lighting and hardwood flooring, have been active in the distressed space. Dollar stores are also seeing a decrease in consumer demand. Most would suspect that these lower-end retailers would benefit from inflation and the rising costs of goods. But Sutton notes that dollar stores are simply sitting on too much inventory, making the mistake of ramping up too much during the pandemic. Overexpansion in the dollar store space and price increases on items in the stores have also added to the oversupply of inventory.

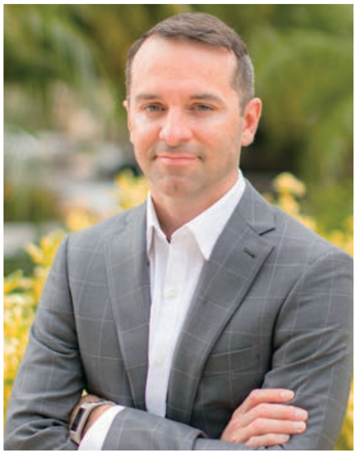
And, as Americans went back into the office and the pandemic cloistering in the home ended, the demand for alcoholic beverages, especially higher-end distilled bourbons and whiskeys, slowed. Sutton notes that a decade of increased production in this industry and the flood of new brands into the marketplace couldn't have come at a worse time. "We are seeing too much inventory and a weakness in pricing," he adds. Plus, many new entrants in the space are sitting on extensive amounts of bulk inventory, leading to the question as to where it will end up.

Supply chain problems did serve to temporarily and artificially inflate the value of some in-demand items, says Stan Czupryna, senior appraiser at Loeb Equipment. He notes that mask and some test making lines are now sitting in warehouses with little to no hope of recovery. Czupryna explains it's the charge of appraisers to constantly educate the secured lending community, especially when industries experience a boom and then demand for their products wane. "We all have a duty to elevate this industry and let the banks

TIM ANDERSON
Hilco Valuation Services



STAN CZUPRYNA
Loeb Equipment



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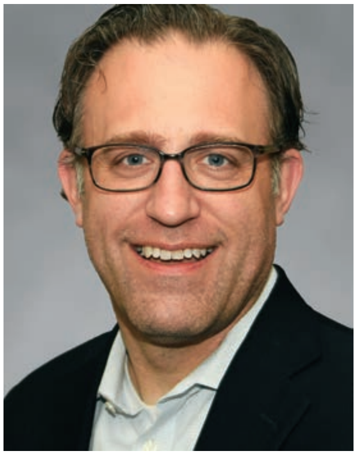

JONATHAN DEPTULA
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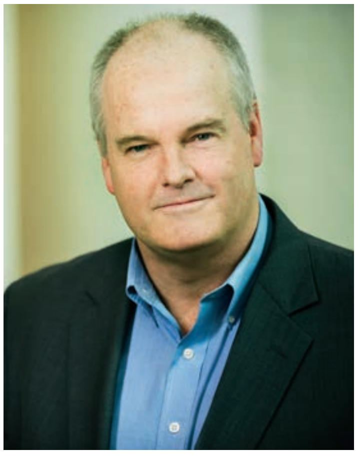
RICHARD HAWKINS
Atlantic Risk Management



ALEX SUTTON
Gordon Brothers

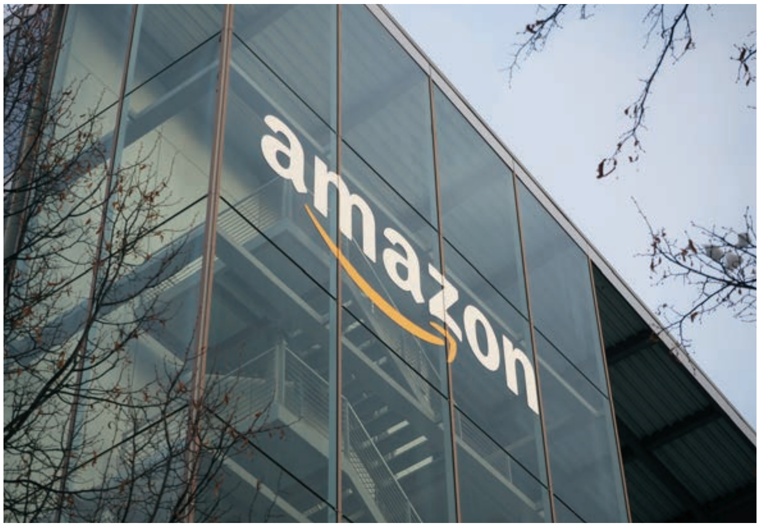
and all lenders know they are getting the right information each and every time," he says. "We go in with a blank canvas and come up with an opinion on value that we have to support."

Czupryna notes that appraisal firms, large and small, served the secured lending industry during the lockdown, despite limited access to businesses, by using an in-depth knowledge of inventory and historic and last-minute valuations. Appraisers are now benefiting from being back on the ground 24-7, when needed. But he is noticing other trends in valuations. Light equipment and microbreweries are struggling for the moment, with a glut of inventory and machinery. On the other hand, valuations remain strong for nutraceuticals and pharmaceutical manufacturing equipment. Post-pandemic, and as always, appraisers are adjusting to the new normal.

For instance, order cancellations and a slowdown in supply has caused some retailers to adjust their thinking, and appraisers as well. "There was a reactionary surge in demand for some products and a valley of supply," notes Ryan Davis, executive managing director of Tiger Valuation Services. Now, some industries are oversupplied, and liquidation may be the inevitable next step. Discretionary items are certainly more at risk, Davis says. "Our expertise is knowing price elasticity and really knowing how to liquidate items. But retailers and manufacturers are working through the pendulum swing." He credits appraisers for not overvaluing inventory when demand was artificially inflated from temporary pandemic demand. "We knew this was a short-term event," he says.

Tim Anderson, executive vice president at Hilco Valuation Services, remains surprised by the number of secured lenders who are still shocked by the lasting impact of the pandemic across certain industries. Companies ramped up production of home goods and hobby supplies, like fishing gear and exercise equipment, but now the market for it has cooled. "Some companies thought the good times would never end, and they did, and now they're still dealing with over-inventory positions," Anderson adds.

But there are headwinds in the economy, and Anderson is expecting to see an increased frequency of appraisals. "It's harder to liquidate items, like fashion brands, if we head into a recession," he says. "Consumers stop buying and that will impact asset values." It's an expected cycle, and not unprecedented. In that environment, companies like Peloton and Bowflex, will be harder to value. "This isn't simply equipment that can be easily appraised," Anderson notes. "These are really technology companies that rely on connectivity. It's the customer lists and the online library that are important, and the equipment is useless without them." The same is true for home monitoring systems that require monthly subscription fees. "There's not a ton of worth in the security cameras, and we have to get lenders to get beyond thinking this is just an inventory deal," he adds.



Smaller companies are turning to Fulfillment by Amazon to quickly put their items into the consumers' hands. Amazon handles the inventory in their own facilities and does all of the fulfillment. The implications of "using another company's intellectual property platform and warehouse space means that Amazon holds all the cards, and that can have an impact on appraisals and liquidation," Anderson explains.

And while retail can be highly volatile and item specific, it's also subject to the vagaries of consumers and changing economic cycles. Anderson notes that appraisers are at the ready to appropriately analyze subsectors in it to provide a more complete perspective. Fulfillment by Amazon, for example, is giving secured lenders pause. "We really all need to understand the risks associated with it," he says. Smaller companies are turning to Fulfillment by Amazon to quickly put their items into the consumers' hands. Amazon handles the inventory in their own facilities and does all of the fulfillment. The implications of "using another company's intellectual property platform and warehouse space means that Amazon holds all the cards, and that can have an impact on appraisals and liquidation," Anderson explains.

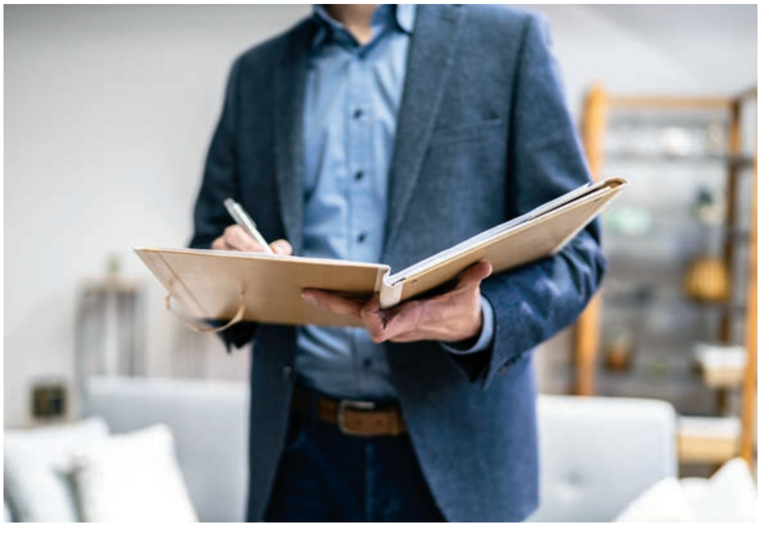
Amazon may be complicating the retail sector, but according to Jonathan Deptula, president at Hyper Valuation Services, some retailers are less problematic than others. "Certain industries, like furniture and home décor, are struggling, after the pandemic," he notes. Americans are no longer looking to the comfort of home amidst the lockdown. But the direct-to-consumer space and higher-end luxury items are holding value. He credits much of that growth to younger shoppers who are staying put with parents longer and, as a result, have more disposable income to spend.

Deptula does see an uptick in disposition activity across industries, and appraisers are working extra hard to respond quickly to their secured lender clients. "We are trying to execute better than ever, yet be the least intrusive to businesses," he notes. The larger appraisers benefit from data sharing with the big banks, larger independent secured lenders, and private equity. But technology cannot facilitate every deal. "It's harder to use as much technology as we would want because every deal is unique," he adds. Deptula predicts the 4th quarter will be stronger than the period before for secured lenders and, consequently, appraisers. He points to the benefit of a drop in interest rates for some industries, as well as the impact of economic uncertainty for others. "The appraisal business allows for lenders to understand values during distressed times, but also is able to help fast growing business to monetize assets to fuel growth."

But as lead times increase on some products, appraisers are becoming quite circumspect in their valuations. The shipment of raw goods is part of the problem. It's always a challenge to come up with fair market value, but the pressure is on for appraisers to move more quickly than ever, says Richard Hawkins, CEO at Atlantic RMS. He adds that "the result of extended lead times is that companies are carrying more inventory than they used to." The pandemic and supply chain issues are certainly to blame, but he notes that some sectors are faring better than others. "It's all related to load, demand, cyclical issues, and then geopolitical pressures in relation to commodities, and specifically to energy," he adds.

Hawkins notes that the pressure is always on the appraiser to come up with a valuation, but the increase in private credit in secured lending is complicating the process. "They have a different perspective, and they also have different timescales in relation to the execution process," he says. "There is going to be more pressure put on third-party organizations." Private equity is, simply put, quicker to execute than banks. So, appraisers have to respond to those new demands.

Despite those pressures, appraisers are reaping the rewards of a growth in secured lending players, as well as a shift in the types of companies they lend to. "Retail has always been a large part of secured lending, but the growth and shift into industrials, as well as the increase in products and machinery related to the green economy, are expanding the market," Sutton notes. The increasing sophistication of appraisers is making it much easier for secured lenders to underwrite new products and goods or value more complex items, including work in process or intellectual property. Whether it's green products, the internet of things, or digitally-native brands, the marketplace is constantly changing, and, for now, appraisers are meeting the demands of their clients. Sutton notes, "At the end of the day, it's all about the ability to execute."



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Myra Thomas is an award-winning editor and journalist with 20 years' experience covering the banking and finance sector.