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Stu's View

Contributing Editors:
Tom Williams, New Direction Partners and Stuart Margolis, MargolisBecker

Financing and Refinancing, Part 1: Bank Loans

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The print industry has experienced difficulty in attracting lender activity in recent months – but that doesn't mean that financing opportunities aren't out there. Industry-knowledgeable lenders still offer a variety of viable loan products. One excellent resource is People's Capital and Leasing Corporation ("People's"), a wholly owned subsidiary of People's Bank. People's experts like Mickey Urquhart, Senior Vice President, continue to work closely with the key vendors of sheetfed presses and finishing equipment, and offer a full gamut of loan and leasing products:

People's Loan Products			
Loan Type	**People's Terms**	**Recommended for**	**How It Works / Things to Consider**
Conventional	7 years, 10% equity	Most new printing equipment	Was 100% financing, 8 years. More collateral needed now in the short term.
SBA 504	10 years	Projects in excess of $1M	More streamlined process, lower fees. Longer loan period than conventional loans yields a lower rate.
Investor Revenue Bond	3.5% range if lending at 5%	People looking for low interest rate	Tax-exempt product provides lower rate to borrower (65% rate factor is applied to a commercial loan). Downside: No accelerated depreciation for the borrower (which this year is 100%), so borrower must depreciate the asset on a straight-line basis over 10 years. People's helps borrower determine best product from a rate and term standpoint.

Personal Guarantees and Asset Depreciation in a Changing Market

Whether a personal guarantee is necessary depends largely on two factors:

- The loan product selected. Personal guarantees are required by law for the SBA portion of the loan (40%). For the 50% advance from the senior lender—i.e., an entity like People's Capital—the call is discretionary. On bonds, personal guarantees are also discretionary.
- The business history. If a company is tightly held, has 2-3 owners, has been in business for less than 5 years, and has demonstrated the ability to provide personal guarantees to its primary lender, then an equipment lender is going to want the same personal guarantee. Exceptions can be made when the borrower has been in operation 6 or more years; has demonstrated the ability to retain some profits in the company; and can show balance sheet liquidity in tough times to support the balance going forward.

Discretionary personal guarantees may also be waived if the borrower has a hard asset to offer or puts more cash into the deal in lieu of a personal guarantee. People's uses orderly liquidated values on pre- and post-production equipment as their basis for lending. Historically, they went as high as 80% on day one in 2008 and prior. Today, their range is 65% to 70%, with much lower day one values, shorter terms, and more money in the deal.

Lenders have also changed their depreciation calculations on loans. People's formerly depreciated an asset by 10% per year, so a starting value of 80% on day one would be 72% at the end of the first year. Their starting value today is 70%, with a 12% to 15% depreciation per year. Clearly, there has been a major shift in a lender's valuation of printing equipment in response to economic changes.

Help the Lender Help You

Today's lenders consider not only the borrower's collateral position, but also the quality of the borrower's presentation. For a successful loan application, we recommend:

- Investing in an accountant-reviewed financial statement. This gives lenders more confidence than a hand written tax return or a verbal claim that the desired equipment will improve your profits by "X%".
- Providing financial projections that support the purpose of the investment and justify the loan. Lenders don't just want to know your collateral position. They want to see what this equipment will do for your bottom line, and how you have demonstrated that it is going to support you financially.

Refinancing

Printers with multiple loans and long-term debt who are not in a position to purchase or finance new equipment may find it advantageous to refinance all of their loans into one facility. Refinancing can reduce the cash flow requirement to service long-term debt while providing additional cash to run the business. While there will likely be prepayment penalties, the current low rates make this a good avenue to explore. For example, People's is currently lending on a 5-year term at an average of 4.5%. If an existing loan is at 6.0% or 6.5% with a 1.0% to 2.0% prepayment penalty, the inherent penalty is only 50 to 70 basis points in the form of a rate.

From an equity or collateral standpoint, lenders are actually better off lending against an existing loan. Eventually, the loan reaches a tipping or equity positive point. When financing a new piece of equipment, the lender probably still has a negative equity position based on the percentages noted above. By comparison, in term loans that are 2 to 4 years old, that equity has become positive, making it a better deal for the lender to refinance these loans provided that they can offer an attractive term and rate.

All in all, refinancing is something that every printer should look at for its potentially positive impact on the balance sheet. And regardless of whether a borrower is financing or refinancing, cleaning up the balance sheet and moving current debt into the long term will make for more favorable operating ratios.

Part 2 of this article will address Asset-based lending options that provide workable line of credits secured by receivables and inventory.

Stu's View is contributed by Stuart Margolis, CPA and Partner of MargolisBecker LLC to provide information that helps firms operate profitably. More information can be found at www.margolisbecker.com.

About MargolisBecker

MargolisBecker has long been recognized as the financial expert for the printing and allied graphic communications industry, assisting thousands of companies with strategic and financial management, valuation, mergers/acquisitions, accounting, audit and tax services. The firm is noted for its expertise in enabling printing companies to optimize profits. Proudly, it is the purveyor of the industry's *Cash is King*, and *Value-Added Principles of Management*, and compiles the annual Printing Industries of America Ratios, the industry's premier financial benchmarking tool.

About New Direction Partners

The team at New Direction Partners LLC has guided over 200 printing company owners through the sales and merger process. The advisory services reflect a full set of skills to help you sell or expand your business: valuation, management consulting, financial advisory and investment banking. The deep experience and industry expertise at New Direction makes it uniquely suited to serve printing, packaging and allied graphic arts businesses.