

The Fundamental Benefits of Today's Asset-Based Finance



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Companies in an array of industries and at varying stages of their lifecycles use asset-based loans for a multitude of reasons including mergers and acquisitions, debt refinancing, capital expenditures, working capital, leveraged buyouts and even employee stock ownership programs.

What is an Asset-Based Loan?

An asset-based loan is a secured loan that is backed by a company's property such as accounts receivable and inventory, and typically structured as a revolving line of credit. The borrowing base is usually calculated at between 70 to 85 percent of accounts receivable and up to 65 percent of inventory. The borrower is required to make interest payments only and the revolving loan balance increases and decreases in concert with the borrower's assets.

In addition to the revolving line of credit, an asset-based facility may include a term loan secured by fixed assets such as machinery, equipment and real estate. The term loan portion generally carries a repayment schedule that is equivalent to the useful life of the fixed assets.

While asset-based loans traditionally are secured with tangible assets, borrowers may be able to generate additional liquidity using trade names, patents and intellectual property as collateral. Looking beyond traditional

inventory and receivables toward intangibles is what lenders refer to as an "overadvance" or "stretch loan." An overadvance, a loan based on a company's earnings, is a highly versatile structure.

Borrower Benefits

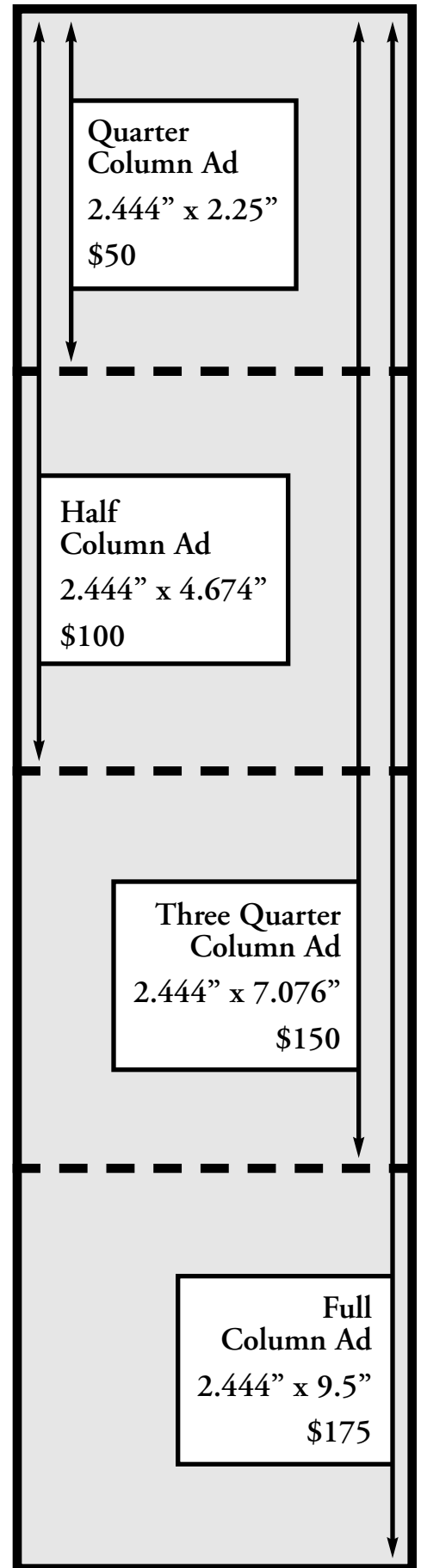
Asset-based finance is used by financially healthy borrowers as well as companies that have experienced diminished or inconsistent cash flow due to seasonal needs, a weak economy or a cyclical industry. Borrowers often choose asset-based finance because it offers a number of advantages over cash flow loans.

Enhanced Liquidity: If a company borrows against a multiple of EBITDA (earnings before interest, taxes, depreciation and amortization) and its earnings decline, its borrowing capacity is diminished. Borrowing against assets may result in greater liquidity and more predictable availability.

Greater Flexibility: Asset-based loans generally require one or two covenants whereas cash flow loans typically have four or five. Asset-based lenders aren't as concerned about certain financial performance metrics since their loans are tied to collateral value. This flexibility frees management to focus on executing the operating plan rather than worrying about violating quarterly covenants.

More Versatile: Asset-based loans tend to be more flexible when it comes to how the company can use the proceeds. Unlike cash flow loans, asset-based loans may permit a company to buy back a portion of its bonds, repurchase shares of stock or provide more freedom to pursue potential acquisitions.

Lender Patience: With collateral securing the credit facility, an asset-based lender is usually willing to give the borrower more time to turn around the company in the event of financial difficulty. Often forward-thinking



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Financial Discipline

Asset-based loans carry some monitoring and reporting disciplines that are related to the borrower's credit profile. As a general rule, healthy companies have more leeway when it comes to reporting while distressed companies need to check in more frequently.

In addition, the lender has dominion over the borrower's cash by establishing a deposit

