THE VALUATION & APPRAISAL ISSUE

JIUNE/JULY 2021 WWW.SFNET.COM

THE SECURED Lender

Putting Capital To Work

FEATURE STORY:
PART 1 OF 2

Allou: A Firsthand Account of a Massive ABL Fraud

One of the biggest frauds ever perpetrated against ABL lenders.

A publication of: Secured Finance Network

ADAPT. RENEW. GROW

SFNet Returns to Live Events

For over a year now, I've used this space, as well as all mediums at our disposal, to connect with the SFNet community. Like all of us, I've missed being able to meet in-person. But despite the loss of these interactions, we've been patient and creative and managed to stay connected in our socially distanced environment. Having a strong community to rely on in good times and challenging times is a vital part of what SFNet is about. We've had thousands of members participate in our virtual events, our Crucial Conversations Webinar series, our virtual education and on-demand courses, as well as our discipline-specific, peer group Member Forums. We're a resilient bunch who found innovative ways to keep business moving forward despite the obstacles that the global pandemic presented.

As we emerge from all this, our Innovation Conference: The Future of Work, to be held live-online on July 14 and 21 will dive into what our new world will look like going forward. From the social, technological, and legal issues around our return to the office (or not), to accelerating adoption of emerging technologies that are transforming secured lending – this highly interactive, unlimited-attendance-for-member-company meeting should not be missed.

At long last, I'm excited to now be able to discuss our upcoming live and hybrid events, starting with SFNet's YoPro Leadership Summit, August 3-4. This hybrid event will bring together the young professionals of the secured finance industry for opportunities to hear from industry leaders, connect with peers, and discover how to succeed in our changing industry environment. The live component will include activities in Chicago, including golf at Medinah Country Club, a cocktail reception, and a dine-around event. Please reach out to Eileen Wubbe ewubbe@sfnet.com for further details.

Our first fully in-person event will be the SFNet Independent Finance Roundtable, August 17-19 in Chicago. Panelists and attendees will come together to discuss the state of M&A, legal issues impacting our industry, and other timely topics that may affect your business. This is an invitation-only event for senior executives. Please reach out to Rob Meyers, our event chairperson, if you are interested in attending.

For our SFNet 40 Under 40 Awards celebration on September 9, we'll be trying something new: hosting the event virtually in conjunction with the opportunity to attend an exclusive reception during SFNet's Annual Convention. This will be a joint event celebrating the classes of 2020 and 2021. We look forward to honoring these outstanding future leaders. Details will follow soon!

RICHARD D. GUMBRECHT
SFNet Chief Executive Officer

Of course, the industry's most-attended event is the Annual Convention. SFNet's 77th Annual Convention: Adapt. Renew. Grow! will be held in-person at the JW Marriott Desert Ridge in Phoenix, AZ, November 3-5, 2021. The venue is fabulous and affords plenty of outdoor gathering space as well as world-class golf and recreation. For those who are not ready to interact face-to-face, or not yet able to travel, we'll provide a virtual attendance option supported by our SFNet Connect platform. With a hybrid structure, we're poised to have the most inclusive Convention ever. Please visit www.sfnet.com for registration details.

The pandemic had a significant effect on so many sectors of our industry, particularly appraisals and valuations, which is the focus of this issue. In *Challenges and Opportunities Along the Road to Electric Vehicle Proliferation* on page 18, Keith Spacapan of Hilco's automotive practice provides an overview of the electric vehicle industry and tips for lenders involved in the space.

On page 22, get a rare glimpse into a major ABL fraud. Mark Fagnani, who was directly involved from day one in the Allou Healthcare case, reveals how the fraud was perpetrated and how it was discovered. It's a riveting story.

Despite the devastating effects of the ongoing COVID-19 pandemic, the construction and building products industries in the U.S. adapted and many sectors experienced significant growth during 2020. Turn to page 30 for an overview of the industry by Erick Beaudoin of Gordon Brothers.

The COVID-19 pandemic caused ecommerce to transition from "convenient" to "essential," but what does the post-pandemic world hold for this sector? Executives from HYPERAMS cover this sector on page 34.

On page 38, in *Restaurant Rebound Tests the Limits of U.S. Food Distributors*, Eric Schloemer of Tiger discusses how foodservice distributors generally adapted well to the massive disruptions triggered by the pandemic, but the sector is feeling the strain of the rapid return of tens of millions of Americans to in-person dining.

Looking forward to seeing you in person soon!

THE SECURED Lender
A PUBLICATION OF SECURED FINANCE NETWORK

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Secured Finance Network

An association of professionals putting capital to work

The Secured Finance Network is the trade group for the asset-based lending arms of domestic and foreign commercial banks, small and large independent finance companies, floor plan financing organizations, factoring organizations and financing subsidiaries of major industrial corporations.

The objectives of the Association are to provide, through discussion and publication, a forum for the consideration of inter- and intra-industry ideas and opportunities; to make available current information on legislation and court decisions relating to asset-based financial services; to improve legal and operational procedures employed by the industry; to furnish to the general public information on the function and significance of the industry in the credit structure of the country; to encourage the Association's members, and their personnel, in the performance of their social and community responsibilities; and to promote, through education, the sound development of asset-based financial services.

The Secured Lender, magazine of the asset-based financial services industry (ISSN 0888-255X), is published 8 times per year (Jan/Feb, March, April, May, June, September, October and November) $65 per year non-member rate, and $105 for two years non-member rate. SFNet members are complimentary.

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Axiom Bank, N.A. Hires New AVP, Marketing Manager

Victoria Lowe was appointed AVP, marketing manager. Lowe brings more than three decades of experience in branding, advertising and communications for banking and finance enterprises.

Axiom Bank N.A. Promotes Joe Dear to SVP, Commercial Market Executive for Orlando

In this role, **Joe Dear** will be responsible for leading and growing the bank's Orlando Commercial Banking unit, including Treasury Management.

CapitalPlus Launches New Materials Financing Product

CapitalPlus Construction Services has launched a new Materials Financing product to help contractors and subcontractors in all trades access mission-critical materials without tying up their capital. CapitalPlus purchases materials on the contractor's behalf, the order ships directly to the job site, and contractors have extended terms to repay CapitalPlus.

CIT Names Business Development Leaders for Northeast, West and Southwest Regions

CIT Group Inc. announced that its Equipment Finance business, part of the Business Capital division, has hired new business development leaders for the Northeast, West and Southwest regions.

Wayne Wagner, Mark Johnson and **JP DeStefano** join CIT as vice presidents for business development on the Industrial team, where they will be responsible for developing dealer relationships throughout the Northeast, West and Southwest, respectively.

CIT Names Business Development Officer in Commercial Services

CIT Group Inc. announced that it has named **Christopher DeRosa** as a business development officer in the West Coast office of its Commercial Services business. DeRosa, a vice president, will be based in Los Angeles and will focus on business development across a wide range of verticals supported by Commercial Services.

Citizens Business Bank Hires President

CVB Financial Corp., the holding company for Citizens Business Bank, is pleased to announce the appointment of **Brian T. Mauntel** as the president of CBB. In his new position, Mauntel will be responsible for overseeing the Bank's 57 business financial centers, specialty lending groups including Dairy & Livestock and Agribusiness, sales support groups, and its wealth management division, CitizensTrust.

Crestmark, a division of MetaBank, Names Rick Pierman as Crestmark Equipment Finance Senior Vice President, Business Unit President

Based in Troy, **Rick Pierman** will report to division president, Christopher Soupal. In this new role, he is responsible for overseeing CEF's equipment finance portfolio, succeeding Tom Rutherford, who remains with the company in support of division special projects.

Encina Business Credit Adds Garett Figueroa to its Business Development Team as a Managing Director

Garett Figueroa is an asset-based lending finance professional with over nine years of business development and credit risk experience at bank lenders and non-bank private debt funds. In his role, Figueroa will be responsible for expanding business development efforts in Wisconsin, Ohio, Missouri, Kansas, and Minnesota, while also joining forces with Steve Beriau, an existing Encina business development executive, to cover the Chicago market.

Fifth Third Bank Bolsters Asset-Based Lending Team

Fifth Third Bank, N.A. announced that **Wanda Alverio** and **Andre Lemons** have joined the Fifth Third Business Capital team as vice president, ABL principal. In addition, **John Littrell** was promoted to group head portfolio management. Alverio joins as vice president, ABL principal and brings nearly 25 years of banking experience to Fifth Third, including more than a decade in asset-based lending. Lemons joins as vice president, ABL principal and has seven years of industry experience. Littrell is a 33-year veteran of the ABL industry with a focus on serving middle-market companies.

Nick Bassi Joins FrontWell Capital Partners as Vice President, Underwriting and Portfolio Management

Nick Bassi, an industry veteran with more than two decades of asset-based lending experience in underwriting, origination and portfolio management, will be based in the firm's Toronto headquarters.

Gordon Brothers Promotes Evren Ozargun to Head of Credit

Gordon Brothers has promoted **Evren Ozargun** to the newly established head of credit role. Ozargun and his growing Credit team will work in close partnership with Gordon Brothers' deal professionals and play an integral role in structuring, underwriting and monitoring all investments involving both debt and equity transactions. Additionally, Ozargun will continue to oversee Corporate Development activities.

Gordon Brothers Welcomes Carolyn D'Angelo as Managing Director, Brands & President of Laura Ashley

Gordon Brothers, the global advisory, restructuring and investment firm and owner of the British heritage brand Laura Ashley®, has welcomed **Carolyn D'Angelo** as managing director, Brands and president of Laura Ashley.

Haversine Funding Announces Andrew Bae Joins as Senior Director of Underwriting and Portfolio Management

Andrew Bae has 20 years of experience in the industry, will be responsible for underwriting, asset management, credit

policy and overall portfolio performance. Previously, Bae focused on ABL origination with White Oak Commercial Finance.

Hitachi Business Finance Expands to Upper Midwest, Hires Heather Rachel as Origination Leader

Hitachi Business Finance has announced that **Heather Rachel** has joined its business development team, where she will focus her efforts on supporting business owners and trusted advisors across the United States.

IDS Adds Four New Customer Wins in Q1 2021 and on Record Pace for Go Lives in First Half

IDS, a leading provider of enterprise mission-critical solutions for secured finance, announced it added four new customer wins during first quarter of 2021. They include two start-up equipment finance operations: Metropolitan Capital, a universal bank expanding into asset-based lending (ABL); and a top five U.S. bank, which implemented IDS | ABL. The company is also on record pace to complete 14 go lives by the end of the first half, representing a 40% increase over 2020.

Kristen Palmer Joins Iron Horse Credit as Business Development Officer

Iron Horse Credit, a leading stand-alone inventory lender, is proud to announce that it has hired **Kristen Palmer** as business development officer. In her role, Palmer will be responsible for identifying new territories, partnership channels and building new client relationships.

JPMorgan Chase Commercial Banking Launches Specialized Green Economy Team

JPMorgan Chase Commercial Banking announced the new Green Economy specialized industry team, which will provide dedicated banking services and expertise to companies that produce environmentally-friendly goods and services or focus on environmental conservation. **Brian Lehman** was named as the head of Green Economy.

MidCap Business Credit, LLC Announces the Addition of Terry Dougherty and Jay Cunningham to its Risk Team

MidCap Business Credit, LLC is pleased to announce the addition of **Terence (Terry) Dougherty** and **James (Jay) Cunningham** to its risk team. Dougherty has joined MidCap Business Credit as a SVP and head of Underwriting. Cunningham has joined MidCap Business Credit as an SVP and head of Credit and Diligence.

Monroe Capital LLC Adds to Marketing Team by Hiring Jayro Yoo

Jayro Yoo has joined the firm as director based in Texas. Jayro will serve on the firm's Marketing & Investor Relations team.

Moritt Hock & Hamroff (MHH) Launches Closely Held/Family Business Practice Group

Moritt Hock & Hamroff (MHH) announced that attorneys from its Corporate/M&A, Estate Planning and Employment Practice Groups have joined forces to create its Closely-Held/Family Business Practice Group. The new practice group is comprised of six MHH attorneys, (**Brian Adelman, Jill T. Braunstein, Keith J. Frank, Stephen J. Ginsberg, Louis P. Karol** and **Tina M. Kassangana**). The group will combine their considerable experience and collaborate to provide creative and effective solutions to the broad array of legal issues that family enterprises encounter on a day-to-day basis and as they evolve over generations.

MUFG Union Bank Appoints Head of New Healthcare Commercial Banking Team

MUFG Union Bank announced that **Anvar Hodjaev** has been named head of Healthcare for its Commercial Banking division. Based in Los Angeles, he will lead the bank's Healthcare industry team and report to Adam Feit, managing director and head of Financial Sponsors, Healthcare, and Life Sciences.

MUFG Appoints Neal Holland Chief Financial Officer of MUFG Americas Holdings Corporation and MUFG Union Bank, N.A.

Mitsubishi UFJ Financial Group announced that **Neal Holland** has been appointed chief financial officer for MUFG Americas Holdings Corporation and its primary banking subsidiary, MUFG Union Bank, N.A., effective June 1, 2021.

Anne Mask Joins Sallyport Commercial Finance, LLC

Anne "Annie" Mask has joined Sallyport Commercial Finance, LLC's team as a partnership associate to help better serve its referral partners and assist prospects with sound finance solutions. Mask is a tenured finance professional who is passionate about helping Sallyport's entrepreneurs find the right cashflow solutions to grow their business.

Sidley Adds Prominent Restructuring Partner Tom Califano in New York

Sidley Austin LLP is pleased to announce that **Tom Califano** is joining the firm's global Restructuring group. Califano will be a partner in the New York office and joins from DLA Piper where he was the global co-chair and U.S. chair of the restructuring group.

Siena Lending Group LLC Announces Addition of Joe Panico

Joe Panico joins the Siena team as director of Originations, based in Cleveland, where he will focus on providing asset-based lending (ABL) solutions for middle-market companies in Ohio, Michigan, Pennsylvania and Western New York.

Signature Bank Announces Management Appointments, Promotions and Transitions

After 21 years of dedicated service, **Mark Sigona**, senior executive vice president and chief operating officer, announced his retirement, effective June 30, 2021. Sigona, a founding member of the executive management team, joined as senior vice president and chief financial officer.

Eric R. Howell, senior executive vice president-Corporate and Business Development since 2013, will assume the COO role, including his current duties overseeing certain of the Bank's national businesses and West Coast operations.

Peter Quinlan, executive vice president and treasurer, also announced his retirement, effective June 30, 2021. In this capacity, Quinlan managed the Bank's investment portfolio, interest rate risk and liquidity management functions since 2003.

Kevin Hickey, senior vice president and chief risk officer for the past five years, will return to the Treasury Department as senior vice president-chief investment officer and treasurer.

Keisha Hutchinson has been named senior vice president and chief risk officer, effective June 1, 2021, joining Signature Bank from KPMG in Short Hills, NJ, where she was audit partner for five years.

Executive vice president and chief financial officer **Vito Susca** will move into the newly created post of EVP and chief administrative officer, and assume various operational responsibilities, including overseeing risk and compliance, facilities, security and special projects as well as serving as a liaison for internal audit and regulators.

Stephen Wyremski, senior vice president and controller since joining the Bank in 2015, will be promoted to senior vice president and chief financial officer, managing all financial-related activities, effective June 30, 2021.

Catherine Donald-Grove, senior vice president and director of Product Management Services, was promoted to chief products officer, also a newly established position for the Bank.

Dawn Juliano was named to the newly created position of senior vice president and deputy chief Lending officer, reporting to executive vice president and chief lending officer Thomas Kasulka.

Webster Expands Focus on Healthcare Financing

Webster Bank is pleased to announce that it is increasing its commitment to its Healthcare industry vertical by naming **Steve Dowe** senior vice president, to lead Webster's Middle Market Healthcare vertical focused on privately owned health care providers and senior housing operators.

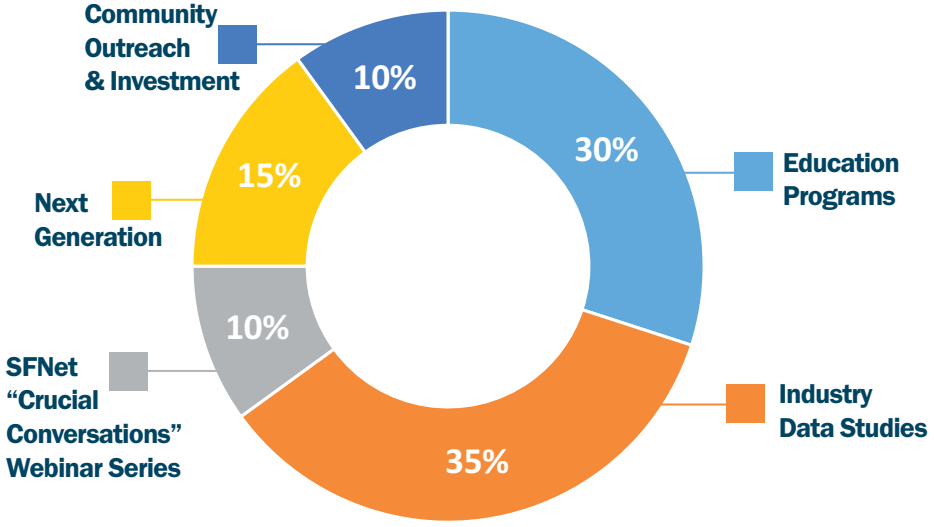
The Secured Finance Foundation's Campaign 2021 Is Underway

This year's goal is $350,000 – your support can get us there.

Networking, Industry data, Education, NextGen, Community and Webinars/ Roundtables

When faced with unprecedented challenges, SFFound is there to help
A strong network is more important than ever in times of uncertainty. That's why the Secured Finance Foundation helps unite our industry for crucial conversations, delivers actionable data to inform smart business decisions and prepares individuals for what comes next with our Education Focus 20/20 initiative. But none of this is possible without your support.

Where does your money go?



For more information or to make a donation, please visit SFFound.org

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure	Service Provider (Type)
Abacus Finance Group, LLC	Non-bank	**N/A**	To support the refinance of LifeSpan Biosciences, Inc. (LSBio) by Thompson Street Capital Partners	Pharmaceutical	Senior debt financing	Legal counsel was provided to Abacus by Goulston & Storrs, PC
Accel-KKR Credit Partners, Centre Lane, and Wells Fargo Capital Finance	Non-bank and Bank	**$67 Million**	Salary.com, Waltham, MA	Technology	Funding	
Access Capital	Non-bank	**$3 Million**	Next Move, Inc. a healthcare staffing company that specializes in the placement of travel nurses at assignments throughout the Midwest, based in Kansas City, MO	Healthcare staffing	Facility	
AFC Gamma, Inc.	Non-bank	**$21 Million**	FarmaceuticalRX, to provide capital to allow FarmRX to purchase and complete the build out of its +/-120,000 square foot Class 1 cultivation and processing facility	Cannabis	Credit facility	
Alleon Healthcare Capital	Non-bank	**$25 Million**	Infusion pharmacy that specializes in Infusion pharmacy services for homecare patients, New Jersey			
Amerisource Business Capital	Non-bank	**$12 Million**	Distributor of construction materials, California	Distribution: Construction	Senior credit facility	
Amerisource Business Capital	Non-bank	**$4.5 Million**	Field services firm, Texas	Field services	Senior credit facility	
Ameristate Bank in conjunction with the U.S. Department of Agriculture's (USDA) Business & Industry Loan Program	Bank and Non-bank	**$10 Million**	Stabilis Solutions, Inc. a leading provider of energy transition services including hydrogen and liquified natural gas (LNG) fueling solutions	Energy	Credit facility	
Antares	Non-bank	**N/A**	To support the acquisition of 80/20 Inc. by MPE Partners. 80/20 Inc. is the originator and manufacturer of "The Industrial Erector Set," a modular aluminum T-slotted building system for various applications and end-markets	Manufacturing	Senior secured credit facilities	
Assembled Brands	Non-bank	**N/A**	InStyler, a high-tech hair and beauty company, Culver City, CA	Beauty	Revolving line of credit	
Associated Bank	Bank	**$12,255,100**	VK Industrial V, LP, an affiliate of Venture One Real Estate, for the acquisition of a Chicago-area logistics portfolio and billboard site	Real estate	Term loan	

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
Ares Commercial Finance (ACF)	Non-bank	**$45 Million**	Southern States Cooperative, Inc. (SSC), Richmond, VA, a retail agricultural cooperative serving the agronomy, energy and farm supply needs of its members and customers across eight states in the Southeastern United States.	Agriculture	Senior secured revolving line of credit
Atalaya Capital Management	Non-bank	**$50 Million**	Opportunity Financial, LLC (OppFi), a U.S.-based fintech platform that powers banks to help the everyday consumer gain access to credit	Fintech	Corporate credit facility
BofA Securities, Inc. and Coöperatieve Rabobank U.A., with Bank of America, N.A. acting as Administrative Agent	Bank	**$500 Million**	Phibro Animal Health Corporation, an animal health and mineral nutrition company	Pet care	Amended and restated credit agreement consisting of Term A loans in an aggregate principal amount of $300 million and a revolving credit facility in an aggregate principal amount of $250 million.
BofA Securities, Inc., JPMorgan Chase Bank, Barclays Bank PLC, Citibank, N.A, Deutsche Bank Securities Inc., and BNP Paribas	Bank	**$2.7 Billion**	General Mills, a leading global food company	Food	Revolving credit facility. BofA Securities, Inc. is acting as the Sustainability Coordinator.
Bank of America	Bank	**$150 Million**	Gibraltar Business Capital, an industry leader in asset-based lending for lower middle-market businesses	Lender finance	Line of credit
Bank of America, N.A. and JPMorgan Chase Bank, N.A	Bank	**$300 Million**	Carpenter Technology Corporation, a recognized leader in high-performance specialty alloy-based materials and process solution	Metals	Syndicated credit facility
BHI	Bank	**$41.86 Million**	Oasis at Coral Reef, a new 217,123-square-foot luxury senior living facility under development in Miami, adjacent to Jackson South Medical Center	Real estate	Construction financing
BMO Harris Bank N.A.	Bank	**$200 Million**	Digi International Inc., a leading global provider of business and mission critical Internet of Things ("IoT") connectivity products, services and solutions	Internet	Amended and restated senior secured revolving credit facility with an option to increase the size of the facility by an additional $75 million. BMO Capital Markets Corp. was joint lead arranger and sole book runner; Silicon Valley Bank, as joint lead arranger and syndication agent, and U.S. Bank and Citizens Bank were lenders
Cadence Business Finance	Non-bank	**$20 Million**	NuBridge Commercial Lending LLC, a small-balance commercial bridge lender, Diamond Bar, CA	Lender finance	Senior secured revolving credit facility

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
CIBC Bank USA [Agent] and Texas Capital Bank [Joint Lead Arranger]	Bank	**N/A**	Context Business Lending, LLC, a leading, national asset-based lender focused on providing flexible working capital for lower middle-market businesses that do not qualify for traditional bank financing	Lender finance	Warehouse line increase
Cambridge Savings Bank (CSB)	Bank	**N/A**	Worcester Envelope Company, Auburn, MA	Paper and printing	Expanded credit facility
CapitalPlus Construction Services	Non-bank	**$200,000**	Self-performing commercial general contractor to take on large Housing Authority projects, Texas	Construction	Construction factoring facility
CapitalPlus Construction Services	Non-bank	**$450,000**	Painting and drywall contractor to take on several large contracts, South Carolina	Construction	Construction factoring facility
CapitalPlus Construction Services	Non-bank	**$400,000**	Existing steel fabrication and erection contractor client	Steel	Construction Factoring Facility
CapitalPlus Construction Services	Non-bank	**$5 Million**	Mechanical, electrical, and plumbing service contractor address accounts payable and expand their payroll, Ohio	Construction	Construction factoring facility
Car Capital	Non-bank	**$20 Million**	Medalist Partners LP, a private institutional investment management firm, New York	Finance	Credit line
Celtic Capital Corporation	Non-bank	**$4 Million**	Developer of software that automates the arrangement of property management and renovation services for REITs and property managers, software	Software	Accounts receivable line of credit
Chicago Atlantic Group, an affiliate of Green Ivy Capital, and a group of lenders	Non-bank	**$23.5 Million**	Vireo Health International Inc., the leading physician-led, science-focused multi-state cannabis company	Cannabis	First tranche of debt financing, non-convertible with a three-year term
CIT Group, Inc.	Bank	**$20 Million**	GEE Group Inc., a provider of specialized staffing solutions and is the successor to employment offices	Staffing	Asset-based senior secured revolving credit facility
CIT Group Inc.	Bank	**$39 Million**	To finance the Jefferson Health medical office building adjoining the Philadelphia Navy Yard Corporate Center	Real estate	Loan
CIT Group Inc.	Bank	**N/A**	Construction of a new 730,000-square-foot logistics center and campus, North Las Vegas, NV	Construction	Financing
CIT Group Inc.	Bank	**$15.9 Million**	Financing for two medical office buildings in Littleton, CO	Real estate	Financing
CIT Group Inc. - Healthcare Finance unit	Bank	**$18.5 Million**	To finance the acquisition of the Singing River Cancer Center in Florence, AL	Healthcare	Loan
CIT Northbridge Credit	Bank	**$23 Million**	Nova Compression, LLC (a successor company to MGC Equipment Company, LLC), Kilgore, TX)	Gas compression	Credit facility

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure	Service Provider (Type)
CIBC Innovation Banking	Bank	**$10 Million**	MayStreet Inc., an industry-leading market data technology and content provider, New York	Technology	Credit facility	
Citizens Bank, N.A. [administrative agent, lead arranger and bookrunner], BankUnited, N.A. and Silicon Valley Bank	Bank	**$65 Million**	Fluent, Inc., a leading data-driven performance marketing company, New York, NY	Technology	Consisting of a $50.0 million term loan and a revolving credit facility of up to $15.0 million	
Citizens Financial Group, Inc.	Bank	**$300 Million**	Moda Midstream, a infrastructure company that stores and handles liquid products, Houston	Storage	Senior credit facility	
Credit Suisse and Hudson Cove Capital Management	Bank and Non-bank	**$100 Million**	Fora Financial, a leading provider of flexible working capital to small- and medium-sized businesses nationwide	Lender finance	Revolving credit facility	Sector Financial Inc., an affiliate of Credit Suisse, provided access to the debt facility, which will give the company up to $150 million of borrowing capacity over the next two years.
Crescent Capital Group LP	Non-bank	**N/A**	To support the refinancing of DMC Group, a leading global platform of needlecraft brands and a portfolio company of Lion Capital	Retail	Unitranche facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$3 Million**	Freight broker, Minnesota	Transportation	Ledgered line of credit facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$300,000**	Refrigerated trucking company, Georgia	Trucking	Accounts receivable purchase facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$2 Million**	Backup power supply and distribution company, Oregon	Power supply	Ledgered line of credit facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$4 Million CAD**	Transportation company, Alberta, Canada	Transportation	Ledgered line of credit facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$250,000**	Freight-all-kinds trucking company, California	Freight	Accounts receivable purchase facility	
Crestmark's Asset-Based Lending and Factoring Division	Non-bank	**$1 Million**	Precision manufacturing company, Massachusetts	Manufacturing	Ledgered line of credit facility	

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
Crestmark Equipment Finance	Non-bank	**$2,223,746**	Wholesale food company, Midwestern U.S.	Food	New lease transaction
Crestmark Equipment Finance	Non-bank	**$1,955,811**	Energy management company, Midwestern U.S.	Energy	New lease transaction
Crestmark Equipment Finance	Non-bank	**$697,993**	Aesthetic clinic, Western U.S	Healthcare	New lease transaction
Crestmark Equipment Finance	Non-bank	**$2,665,599**	Video telematics company, Western U.S.	Video	New lease transaction
Crestmark Vendor Finance	Non-bank	**N/A**	Healthcare company, Midwestern U.S.	Healthcare	Equipment finance transaction
Crestmark Vendor Finance	Non-bank	**N/A**	Transportation company, Midwestern U.S	Transportation	Equipment finance transaction
CrowdOut Capital LLC	Non-bank	**$20 Million**	Lane Gate Advisors, a boutique investment management practice focused on certain segments of the specialty finance market	Finance	
Deutsche Bank AG	Bank	**$100 Million**	Newtek Business Services Corp.	Lending	Credit facility
Eastward Capital Partners	Non-bank	**$17 Million**	Augmedix, Inc., a leading provider of remote medical documentation and live clinical support	Medical technology	New loan facility consisting of a $15 million secured term loan and $2 million available in 4Q21 upon the achievement of certain financial objectives
East-West Bank (EWB	Bank	**$40 Million**	Drip Capital, a leading Fintech provider of cross-border trade finance	Fintech	Committed credit facility
Encina Business Credit, LLC	Non-bank	**$10 Million**	Designer, marketer, and distributor of mid-priced and premium bicycles	Bicycle	Senior secured revolving credit facility
Encina Lender Finance, LLC	Non-bank	**$35 Million**	Uown Leasing, a technology-enabled, consumer leasing platform focused on partnering with retailers of durable consumer goods	Technology	Senior credit facility
Entrepreneur Growth Capital	Non-bank	**$1.8 Million**	Distributor of building materials, New Jersey	Construction	Financing
Express Trade Capital	Non-bank	**$2.5 Million**	Organic spice importer in business since 2010, Nevada	Food	Accounts receivables facility
Fifth Third Bank, N.A.	Bank	**$22 Million**	American Shared Hospital Services (NYSE American: AMS) (the "Company"), a leading provider of turnkey technology solutions for stereotactic radiosurgery and advanced radiation therapy equipment	Healthcare technology	Credit agreement, composed of three loan facilities: a $9.5 million term loan that will refinance $6.8 million of domestic Gamma Knife debt, $1.6 million will primarily be used for two Gamma Knife reloads with two customers that have recently extended their agreements, and the remaining $1.1 million will be available for future projects. A second term loan of $5.5 million will refinance the Company's PBRT Orlando equipment debt as well as provide additional working capital.

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
Fifth Third Business Capital	Non-bank	**$6 Million**	Cosmo Films, Inc., Addison, IL	Specialty flexible packaging films	Revolving credit facility
Flatbay Capital LLC	Non-bank	**$5.6 Million**	Logging company with multiple locations in Arizona, secured by an owner-occupied commercial/ industrial property with direct highway and rail access	Logging	CRE Loan
Gateway Trade Funding	Non-bank	**$500,000**	Maéstro Watch Co. a watch company based in Canada	Watches	Purchase order facility
Gordon Brothers	Non-bank	**N/A**	Nicole Miller, the eponymous fashion and lifestyle brand founded and led by Nicole Miller	Retail	Secured credit facility
ING [Sole Mandated Lead Arranger and Bookrunner] with participant lenders BNP Paribas, Rabobank, MUFG and Wells Fargo Bank N.A.	Bank	**$650 Million**	Supports Pilot Company's oil product purchase and storage, energy and wholesale marketing, logistics and merchant activities	Oil	Inaugural syndicated secured loan
Haversine Funding	Non-bank	**$3 Million**	Infusion pharmacy going through a management buyout and needed capital to execute on the transaction	Pharmacy	Participation in a medical receivables asset-based loan
Haversine Funding	Non-bank	**$150,000**	Telecommunications infrastructure services firm	Telecommunications	Factoring participation
Haversine Funding	Non-bank	**$1 Million**	To support the growth of a staffing factor which experienced growth recently due to various nurse staffing and cleaning service clients in which they specialize	Staffing	Subordinated debt facility
Haversine Funding	Non-bank	**$6.5 Million**	Sawmill, Southwest	Real estate	Senior secured funding for a commercial real estate loan
J D Factors	Non-bank	**$120,000**	Transportation company, Illinois	Transportation	Factoring facility
J D Factors	Non-bank	**$400,000**	Transportation company, Iowa	Transportation	Factoring facility
J D Factors	Non-bank	**$75,000**	Transportation company, Virginia	Transportation	Factoring facility
J D Factors	Non-bank	**$250,000**	Transportation company, Illinois	Transportation	Factoring facility
J D Factors	Non-bank	**$120,000**	Transportation company, Wisconsin	Transportation	Factoring facility
J D Factors	Non-bank	**$150,000**	Transportation company, New Jersey	Transportation	Factoring facility
J D Factors	Non-bank	**$150,000**	Transportation company, Illinois	Transportation	Factoring facility
J D Factors	Non-bank	**$150,000**	Transportation company, Ontario	Transportation	Factoring facility
J D Factors	Non-bank	**$100,000**	Transportation company, California	Transportation	Factoring facility
J D Factors	Non-bank	**$500,000**	Underground drilling company, Arizona	Transportation	Factoring facility
J D Factors	Non-bank	**$100,000**	Transportation company, Ontario	Transportation	Factoring facility
J D Factors	Non-bank	**$100,000**	Transportation company, California	Transportation	Factoring facility
J D Factors	Non-bank	**$75,000**	Transportation company, Nova Scotia	Transportation	Factoring facility

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure	Service Provider (Type)
J D Factors	Non-bank	**$200,000**	Transportation company, New Jersey	Transportation	Factoring facility	
J.P. Morgan, funds managed by Oaktree Capital Management, L.P., and investment funds managed by Morgan Stanley Tactical Value	Bank and non-bank	**$265 Million**	NN, Inc., a diversified industrial company, Charlotte, NC	Industrial	J.P. Morgan acted as administrative agent, sole bookrunner and sole lead arranger on the asset-based credit line, advised on the term loan, and served as sole placement agent on the preferred issuance.	Bass, Berry & Sims PLC served as legal counsel to the Company on the transaction. Gibson, Dunn & Crutcher LLP served as legal counsel to Morgan Stanley Tactical Value.
JPMorgan Chase Bank, N.A.	Bank	**$800 Million**	Dillard's, Inc.	Retail	Amended and extended senior secured revolving credit facility. . A $200 million expansion option remains in place.	
KeyBanc Capital Markets as Coordinating Lead Arranger, along with Rabobank and Wells Fargo, each Joint Lead Arrangers	Bank	**$50 Million**	Scout Clean Energy, a Colorado-based renewable energy developer, owner, and operator	Energy	Letter of credit facility	
Kudu Investment Management, LLC	Non-bank	**$300 Million**	Massachusetts Mutual Life Insurance Company (MassMutual)	Insurance	Credit facility	
Lighthouse Financial Corp.	Non-bank	**$5 Million**	Importer and distributor of premium quality, responsibly-sourced crab meat, Florida	Seafood	Credit facility	
LSQ	Non-bank	**$3 Million**	Existing textile manufacturing client, Tennessee	Textiles	Accounts receivable credit line	
LSQ	Non-bank	**$7.5 Million**	Resurging marketing services firm	Marketing services	AR facility, including a $3.1 million payoff to the first position lender	
LSQ	Non-bank	**$1.5 Million**	Growing manufacturing company distributing DIY products to one of the largest home improvement retailers in the U.S., South Carolina	Manufacturing	Facility	
Marco Capital Inc.	Non-bank	**$600,000**	Staffing company specializing in providing global technology firms with temporary personnel, New York	Staffing	Factoring facility	
MidCap Business Credit	Non-bank	**$8 Million**	Manufacturer of precision components and assemblies	Aerospace and defense	Asset-based credit facility	

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure	Service Provider (Type)
Monroe Capital LLC	Non-bank	**N/A**	To support the acquisition of Lulu's Express. In October 2018, Mammoth partnered with Red Dog Equity LLC, an Atlanta-based private equity firm			
Monroe Capital LLC	Non-bank	**$120 Million**	To support the recapitalization of an infusion therapy business by a private equity sponsor	Specialty pharmacy	Senior credit facility	
NXT Capital	Non-bank		In support of Wind Point Partners' acquisition of Zone Mechanical, one of the largest providers of commercial and industrial refrigeration installation and maintenance services	Refrigeration and HVAC	Senior credit facility	
Old Hill Partners	Non-bank	**$12 Million**	ByzFunder NY, a provider of working capital solutions in the form of merchant cash advances, New York	Lender finance	Increase to committed credit facility	
Oxford Finance LLC	Non-bank	**$125 Million**	Kala Pharmaceuticals, Inc., a biopharmaceutical company focused on the discovery, development, and commercialization of innovative therapies for diseases of the eye	Biopharmaceutical	Senior secured term loan	
PNC Bank, National Association	Bank	**$120 Million**	Universal Stainless & Alloy Products, Inc., Bridgeville, PA	Steel	Amended and restated that includes a revolving credit facility of $105 million and increases the term loan facility to $15 million	
Rosenthal & Rosenthal, Inc.	Non-bank	**$7.5 Million**	Food distributor serving restaurants up and down the East Coast, based in the Midwest	Food distribution	Revolving credit facility	
Rosenthal & Rosenthal, Inc.	Non-bank	**$2.75 Million**	Importer and distributor of recreational sporting products, Georgia	Sporting goods	Joint $2 million factoring and $750,000 inventory production finance deal	
Runway Growth Capital LLC	Non-bank	**$25 Million**	Allurion Technologies, a pioneering leader in the development of innovative, scalable and trusted weight loss experiences	Technology	Senior secured term loan	Armentum Partners served as the financial adviser to Allurion in connection with this financing.

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
Sallyport Commercial Finance	Non-bank	**$500,000**	To assist the turnaround of this flourishing health food manufacturer in Canada	Manufacturing	Accounts receivable facility
Second Avenue Capital Partners, LLC	Non-bank	**$10 Million**	Northern Reflections Limited, one of Canada's largest privately-held apparel retailers of women's apparel	Apparel	Senior secured credit facility
Second Avenue Capital Partners, LLC	Non-bank	**$30 Million**	UNTUCKit, one of the fastest-growing retail apparel brands in North America, New York, NY	Retail	Senior secured term loan
SG Credit Partners	Non-bank	**$1.25 Million**	Single-asset real estate holding company owned by a prominent carwash company in the Midwest	Real estate	Financing
SG Credit Partners	Non-bank	**$1 Million**	Privately-held family investment vehicle	N/A	Loan structured around the Guarantors' personal assets and diversified income streams
Siena Healthcare Finance	Non-bank	**$35 Million**	Home health company, New York	Healthcare	Asset-based line of credit
Silicon Valley Bank	Bank	**$13 Million**	Zoom Telephonics, Inc., doing business as Minim, the creator of innovative internet access products	Telecommunications	Credit facility
Silicon Valley Bank	Bank	**$50 Million**	Humacyte, Inc., a clinical-stage biotechnology platform company developing universally implantable bioengineered human tissue at commercial scale	Biotechnology	Secured debt financing facility
Sky Business Credit	Non-bank	**$75,000**	HVAC contractor, Arkansas	HVAC	A/R factoring line
Sky Business Credit	Non-bank	**$100,000**	Telecommunications contractor, Minnesota	Telecommunications	A/R factoring line
Sky Business Credit	Non-bank	**$200,000**	Manufacturer, Illinois	Manufacturing	A/R factoring line
Sky Business Credit	Non-bank	**$1.5 Million**	Healthcare staffing company, Pennsylvania	Staffing	A/R factoring line
SLR Business Credit	Non-bank	**$2.5 Million**	Producer of high-quality fresh and frozen ground meat out of bankruptcy via a 363 sale, Midwestern U.S.	Food	Asset based facility
SLR Business Credit	Non-bank	**$12 Million**	Distributor of veterinary medicine and supplies	Veterinary medicine	Asset-based revolving line of credit
SLR Healthcare ABL	Non-bank	**$4 Million**	Medical staffing company	Staffing	Asset-based revolving line of credit
SLR Healthcare ABL	Non-bank	**$3 Million**	Skilled nursing operator	Healthcare	Asset-based revolving line of credit
TAB Bank	Bank	**$5 Million**	Factoring company, Michigan	Factoring	Rediscount credit facility
TAB Bank	Bank	**$3 Million**	Beverage company, Idaho	Beverage	Revolving credit facility

Lender/Participant	Lender Type	Amount	Borrower	Industry	Structure
TD Securities and Bank of America	Bank	**C$1.05 Billion**	Navacord Corp., one of Canada's largest insurance brokerage firms and fastest growing multi-line brokers	Financing	Financing. TD Securities is acting as administrative agent on the revolving credit facility and first lien term loan and Bank of Montreal is acting as administrative agent on the second lien term loan.
Texas Capital Bank, N.A.	Bank	**$20 Million**	Natural Gas Services Group, Inc., a leading provider of gas compression equipment and services to the energy industry, Midland, TX	Energy and Gas	Senior secured revolving credit facility
TradeCap Partners	Non-bank	**$2.5 Million**	Consumer packaged goods company, West Coast U.S.	Packaged goods	Purchase order finance facility
Webster Bank	Bank	**$34 Million**	In support of The Metro Group Inc.'s acquisition of Response Electric	Water treatment, HVAC mechanical contracting, and electrical services	Senior secured credit facilities increase
Wells Fargo, N.A., including Bank of America N.A., U.S. Bank N.A., PNC Bank, N.A., Bank of the West, and Northern Trust, N.A.	Bank	**$1.2 Billion**	TTEC Holdings, Inc. (NASDAQ: TTEC), one of the largest, global CX (customer experience) technology and services innovators for end-to-end digital CX solutions	Technology	Amended credit facility by exercising its accordion feature to increase the total commitments by $300 million to $1.2 billion.
White Oak ABL, LLC	Non-bank	**$10 Million**	Hunt & Sons, Inc., a third-generation, family-owned diversified petroleum products distributor, Sacramento, CA	Petroleum	A second $10 million line increase and extension, bringing the total ABL credit facility to $95 million
White Oak Healthcare Finance, LLC	Non-bank	**N/A**	ViaQuest Holdings, Ltd. and affiliates, to support the acquisition by Council Capital, a Nashville-based private equity fund. ViaQuest is a provider of services for individuals with intellectual and development disabilities ("I/DD"), hospice services, and other behavioral health services to individuals.	Behavioral Health	Senior credit facility
Wingspire Capital LLC	Non-bank	**$46 Million**	Worldwise, Inc., a leading designer and supplier of pet products	Pet	Senior secured credit facility. Transaction includes a $30 million revolving line of credit and a $16 million term loan to replace the previous credit facilities and enable Worldwise to meet the growing demand for cat and dog toys, beds, carriers and other pet products as the pet category continues to grow both in the U.S. and worldwide.
Wingspire Capital LLC	Non-bank	**$45 Million**	Large private industrial mining company	Mining	$45 million senior secured credit facility which included a $35 million revolving line of credit and a $10 million term loan
Wintrust Receivables Finance	Bank	**$4.75 Million**	Provider of logistics and transportation management services	Transportation	Line of credit
Wintrust Receivables Finance	Bank	**$4.5 Million**	Growing paper bag manufacturer	Manufacturing	Accounts receivable line of credit

FEATURE STORY

Challenges and Opportunities Along the Road to Electric Vehicle Proliferation

BY KEITH SPACAPAN

Keith Spacapan of Hilco's automotive practice provides an overview of the electric vehicle industry and tips for lenders lending in the space.

Takeaways

1. Ensure that a company's strategic plan anticipates the continued emergence of EV technology.
2. Assess the sense of urgency of a company's leadership with respect to EV technology.
3. Determine the percentage of a company's R&D budget that is related or dedicated to EV technology.
4. Determine the percentage of a company's capital expenditures that are related or dedicated to EV technology.
5. Become as knowledgeable as possible about the details of the strategic partnerships that a company has formed or is considering in the future.

KEITH SPACAPAN
Hilco Global

Over ten years ago, Nissan launched its all-electric Leaf automobile, becoming the first automaker to mass produce such a vehicle. Since that time, a plethora of legacy manufacturers from Toyota and Honda to Mercedes, Audi and Ford, have introduced a host of hybrids and electric vehicles (EVs). General Motors has announced that it is making a $27-billion investment in electric and autonomous vehicles and has committed to introducing a minimum of 30 EV models through 2025. Volvo recently revealed its aggressive plans to transition to an all-EV company by the year 2030. And Volkswagen has put a stake in the ground, publicly stating that its mission is to become the world's largest manufacturer of electric vehicles. While multiple automakers plan to eliminate new vehicles with gasoline and diesel engines entirely in the next 15 years, it is worth noting that many longstanding brands have yet to fully commit to an EV platform-based future.

Historical Perspective

The reluctance to commit is somewhat easier to understand when we consider the evolution of personal vehicles overall, dating all the way back to the transition from horses to the first automobiles. With advances in technology in the 1800s came experimentation with not only gasoline, but steam and even electric-powered engines. Steam was, in many ways, the most promising technology of the time because it was so widely used to power train locomotives, ocean-going ships, mining and factory equipment. An engine powered by steam is, in fact, widely believed to have propelled the world's first "automobile" in the late 1800s. Steam engines, however, had a number of drawbacks, including the time needed to warm up prior to use and their constant need for water, which limited the distance they could travel in many circumstances.

Electric cars of the time lacked many of the issues that plagued steam and gasoline-propelled vehicles. They didn't make a lot of noise, they were comparatively simple to operate, and they did not generate excessive heat or emissions. Some popular electric models were actually produced as early as the late 1880s in Germany and in England, where an entire fleet of electric taxicabs filled the streets. The popularity of electric cars continued to grow, particularly in urban areas, as more cities became electrified for the first time and charging became a less arduous task. As a result, auto pioneers, notably Ferdinand Porsche, continued to experiment with electric and even early hybrid creations. Around this time in the U.S., Thomas Edison was busy developing vehicle batteries that could deliver better performance. He and Henry Ford even partnered together in an effort to develop a viable low-cost electrical car. Ultimately, however, many consider the introduction of Ford's own $650 Model T in 1912 — a credit to the efficiencies of his innovative production-line process — as the pivotal event that stalled the future of electric vehicles of the era and led to the meteoric rise of the combustion engine. In fact, it wasn't until over 80 years later, in 1996, that the first production electric vehicle was brought to market by General Motors. Toyota's Prius hybrid was introduced the following year, and in 2004 Tesla motors was founded.

The Modern Era

As referenced above, the past several years have featured numerous announcements by manufacturers across the globe pertaining to their plans for EV rollouts. Even under the restrictions of COVID-19 conditions, since the start of 2021 we have seen GM release its completely redesigned 2022 Chevrolet Bolt EV and a compact sport utility variant badged the Bolt EUV. Production is scheduled to begin later this fall on GMC Hummer's highly anticipated EV. According to Stellantis, by year end it plans to introduce up to ten hybrid or electric models across its brands, among them a highly anticipated Jeep Wrangler plug-in. The latest front page news for electric vehicles is Ford's introduction of an electric-powered version of the iconic Ford F-150 pick-up truck to be badged the Ford Lightning. Only five years ago, Ford used its iconic F-150 pick-up to make headline news when it jettisoned the rugged, conventional steel body in favor of a lightweight, all-aluminum body. There is no better way for Ford to demonstrate its commitment to the cause than to introduce a zero-emission variant of the most popular vehicle in America, the Ford F-150.

The new car market in China is by far the largest in the

world. According to estimates by global automotive firm LMC Automotive, China will produce over eight million electric cars annually by the year 2028. Europe and the U.S. will be hard pressed to ramp production at anything approaching a competitive rate. Meanwhile, China's projected rate of growth for "new energy" vehicles in 2021 is 40%, with total sales expected to climb to 1.8 million units, based on data from the China Association of Automobile Manufacturers. At present, there are 22 EV makers doing business in China. All but Tesla are home-grown China-based companies, including one which is joint venture with Volkswagen. While U.S.-based Tesla is the only outlier, the company actually leads the market in units shipped to-date.

The new administration has prioritized a national EV charging network, with a goal of installing at least 500,000 devices nationwide by the year 2030. Similar efforts have been proposed, with some well underway in countries around the world. This is an aggressive undertaking for the U.S. and one that clearly looks toward the future of a carbon footprint-friendly roadway.

Technological Crossroads

Reducing emissions is a top priority for most major automakers today, but determining how best to accomplish that task remains a topic of some significant debate. While hybrid electric vehicles (HEVs) have paved the way for the industry since Toyota's Prius debuted nearly 25 years ago, their reliance on petroleum-driven combustion engines makes HEVs an unlikely long-term candidate for survival in an increasingly environmentally conscious, sustainability focused world. With this in mind, meeting consumer expectations and achieving zero emissions - which states including California have now mandated be accomplished by specific future dates - will require further refinement of two notably different technologies: battery electric vehicles and hydrogen fuel cell vehicles.

While both harness electricity to generate vehicle propulsion, the way each stores that electricity is dramatically different. In battery-electric cars, that power is stored directly in a vehicle's battery packs. Storage is accomplished quite differently, however, in hydrogen fuel cell cars. Here, a car's fuel cells store electricity in the form of gaseous hydrogen, which, when released via a chemical reaction in those cells, generates propulsion.

In a recent self-funded study, "Automotive Industry 2035 – Forecasts for the Future", management consultancy firm Horváth & Partners explored which of these technologies is likely to become most established in the years ahead. Its findings indicated that based on the specific model, a battery-powered electric car is capable of achieving a level of efficiency somewhere between 70% and 80% percent. This means that approximately three quarters of the total electricity generated by the car's own grid is actually able to be applied to vehicle propulsion.

By comparison, the study found that losses are significantly more extensive in hydrogen-powered electric cars, which are only capable of attaining an efficiency range between 25% to 35% percent. The study also showed that, when alternative fuels to hydrogen are burned, efficiency drops even further. So, while hydrogen and other fuel cell-based electric cars can offer extended range, fast refueling and reduced weight over their battery-on-board counterparts, they would appear to have one distinct disadvantage: their comparative inefficiency. That said, while current offerings from Volkswagen, BMW and Ford underscore those manufacturers' commitments to battery-electric cars, others including Hyundai, Toyota and Honda strongly support fuel-cell technology, with each currently offering such a vehicle in the California market where that fueling infrastructure currently exists.

Commodities Impact

With the pace of electric vehicle adoption overall increasing at a rapid rate, major implications lay ahead for industries that supply the automotive industry. This includes the mining and metals as well as the energy sectors. Demand for metals, including lithium and cobalt, can be expected to dramatically increase as more widespread adoption of electric vehicles takes place across the globe in the coming

years. Furthermore, as automakers are being regulated into reducing the emissions footprint along their supply chains, the pressure will be on for greater use of renewable energy and sustainable manufacturing techniques such as electrification of mining operations and implementation of green initiatives.

Some have expressed concern for the steel market, as penetration of electric vehicles continues to advance. According to Ernst & Young, automotive sector demand for steel can be expected to remain relatively flat with the incremental volume of EVs produced offsetting the reduced volume of steel needed for each unit. A demand increase is also forecast for aluminum as the push to reduce vehicle weight continues. Both metals will be essential in the growth of the global charging infrastructure and EV battery production. Copper demand is also expected to grow at a significant rate, given that an EVs construction involves approximately five times more of that metal than an equivalent combustion engine vehicle. Copper is also an essential component in the expanding EV-charging infrastructure. Demand for cobalt, graphite and nickel is also expected to grow alongside the lithium widely utilized in EV battery technology.

Infrastructure

The new administration has prioritized a national EV-charging network, with a goal of installing at least 500,000 devices nationwide by the year 2030. Similar efforts have been proposed, with some well underway in countries around the world. This is an aggressive undertaking for the U.S. and one that clearly looks toward the future of a carbon footprint-friendly roadway. With EVs and hybrid electric vehicles currently accounting for only about 2% of the new vehicles sold domestically in 2020, demand for a large network does not exist today. Yet, adding future capacity is clearly critical as evidenced by a recent *Consumer Reports* survey. Findings indicated that about half of drivers would be interested in an EV that could travel further than 300 miles between charges, yet most offerings on the road today do not deliver that range. Less than half of those surveyed, who indicated that they definitely do not plan to obtain an EV as their next vehicle, indicate that an inadequate charging infrastructure is a key factor holding them back. 28% state that they lack a place to charge an EV at home.

Not surprisingly, while automakers are heavily vested in evolving their EV offerings to meet consumer expectations and government regulations, they are not as zealous about following the Tesla model of building out, owning or operating their own charging networks. As a result, most have entered into partnerships with third-parties to provide those capabilities. Companies such as ChargePoint and EVgo have adopted distinct business models in building out large charging networks, both of which place the majority of the cost burden on area businesses. While these and other suppliers/operators have, to-date, concentrated on installations at highly trafficked urban and suburban shopping and entertainment locations, we expect to see a growing number of fast charger installations at intervals between major population areas to make longer trips more practical for EV owners and EV ownership more appealing to the masses.

Consumer Acceptance

With mounting legislation and regulation worldwide supporting clean initiatives and the reversal of climate change, automobile manufacturers have little choice but to continue the acceleration of their efforts toward an EV-focused future for their vehicle offerings. The risks, however, at least in the near-term are very real. EV sales comprise under 2% of new vehicle sales in the U.S. and only 3% globally. While overall awareness of EVs and their distinct benefits is high among consumers here in the U.S., multiple studies indicate that current range limitations, charging station scarcity and expensive pricing continue to inhibit many from making the leap to EVs. As a result, while a global production shift to EVs is all but certain over the course of the next decade, the rate of future adoption remains more in question.

For more than a century, man has toyed with the concept of electric vehicles. Ironically, electrification of the industry is anything but the flip of a switch. Swamy Kotagiri, the newly appointed chief executive of Magna International, likened the process to a marathon. All the work up until now should be viewed as training for what now is the race. With that in mind, Hilco urges lenders with current portfolio exposure to the industry to actively engage with their borrowers to 1) ensure that a company's strategic plan anticipates the continued emergence of EV technology; 2) assess the sense of urgency of a company's leadership with respect to EV technology; 3) determine the percentage of a company's R&D budget that is related or dedicated to EV Technology; 4) determine the percentage of a company's capital expenditures that are related or dedicated to EV Technology and; 5) become as knowledgeable as possible about the details of the strategic partnerships that a company has formed or is considering in the future.

Keith Spacapan is vice president of Hilco's automotive practice. He has been directly involved in the automotive industry for more than 30 years, including 15 years with General Motors. Keith can be reached at kspacapan@hilcoglobal.com or 847-313-4722.

FEATURE STORY

PART 1

Allou – A Firsthand Account of a Massive ABL Fraud

BY MARK FAGNANI

Allou Healthcare was one of the biggest frauds ever perpetrated against ABL lenders. What follows is a description of the case from an individual who was directly involved from day one. *TSL* will be publishing the entire article in two installments. In Part One, you will read how the fraud was perpetrated and how it was discovered. In the second installment, to be published in our September issue, you will read all the steps taken by the lenders and their team of professionals to recoup the loan and to punish the wrongdoers. This is a rare firsthand account of a significant fraud and you won't want to miss it.

MARK FAGNANI
Clear Thinking Group

This story begins in 2001. By that time I had been in asset-based lending for 25 years and had risen through the ranks of my company to be a senior leader and the person with oversight over all problem loans. While I would never say that I've seen it all, I had seen a lot. The same could be said for every member of our senior management team, many of whom had more than my 25 years in the industry. Despite that, this is a story about how a massive fraud was perpetrated against our company and our numerous co-lenders, right under our noses beginning with the day the loan was booked (and, as it turned out, many years before that). But it is also a story about our reaction to the circumstances and how we assembled a world-class team to uncover all the facts, recover as much of our loan as possible and ultimately send the perpetrators to jail. This is a story about lenders who, once the fraud was discovered, were tireless and aggressive and willing to spend substantial amounts on professionals in pursuing their remedies, which ultimately resulted in over $130 million in recoveries (better than 60%). This is also the story of how the agent and its co-lenders collaborated in developing and implementing a comprehensive strategy to gain control of the situation, manage recoveries from every available source and assist in the prosecution and conviction of the wrongdoers. The story began in 2001, but all court-related activities only recently ended and the last convicted felon was released from jail in 2020. So, yes, it has gone on for a very long time and at great expense. The mistakes made by us in 2001 can easily occur today and the lessons learned are as relevant now as ever. My hope is that the reader will not only enjoy the story, but learn from it.

Allou was one of the biggest ABL frauds ever documented and, to my knowledge, there has not been another one like it. It is a cautionary tale for all lenders.

In September 2001 my employer, then known as Congress Financial Corporation, (and subsequently to become Wachovia Capital Finance), closed on a $200MM loan facility for Allou Healthcare and its subsidiaries. Allou was a distributor of health and beauty aids and essentially sold everything you would have then expected to find in a drugstore, from shampoos and cosmetics to tissues and diapers. Through a subsidiary called Sobol, they also distributed prescription medicines. Winning the deal was somewhat of a coup for us as our head of marketing, Barry Kastner, had tracked the company for some time without success, but finally broke through and signed Allou to a multi-year credit agreement. We were thrilled. Up until this time, Allou had financed with other bank-owned ABL shops for at least the preceding 10 years. Our co-agent was Citicorp and we each held $50MM in the loan facility. In addition, there were several other co-lenders in the deal and some of them had actually sold participations to smaller lenders. In total, there were 10 lenders sharing in the facility. A few of the lenders in our group had been lenders in the previous loan facility as well. The deal was structured as a revolving facility with a blanket lien on all of Allou's assets. We advanced 85% against A/R and 50% against the inventory. Allou was the 16th largest publicly traded company on Long Island and was listed on the NYSE. Annual audits had been prepared for years by a relatively small local CPA firm. At our insistence, the company engaged a large national firm for annual certified statements and, when that firm failed, another Big 8 firm was engaged as the lead partner went over to the new firm. Interim quarterly financials continued to be prepared by the small local firm. We also had personal guarantees from the three primary officers other than the CFO. The PGs were joint and several and limited to $10MM.

The company CFO was an individual we will call David S. He was a very polished, very charismatic individual, dressed in expensive suits and ties and was very articulate. It was David S. who met with the Wall Street analysts to discuss results and plans and it was with David S. that the agent had all interaction. He negotiated the entire loan agreement and signed the loan documents. He was the face of the company, but we were later to discover that David S. had little to do with the actual running of the company and primarily acted as a shield for the other officers who we later discovered had previous financial difficulties. This was mistake number one. We failed to familiarize ourselves with and meet all of the officers of the company. Today, in 2021 all regulated banks and most non-regulated lenders are required to perform KYC procedures and that is all well and good but is not a replacement for actually meeting and getting to know your clients. Harder in this COVID era, but still very relevant.

In the early days of our relationship, all seemed well. The company reported A/R and inventory on a weekly basis and interim financials reflected modest profits. A/R turnover trends were in line with those revealed in our initial survey field exam as were dilution trends. The company had hundreds of customers and thousands of small-dollar invoices. WalMart was the largest customer, making invoice verifications difficult and inconclusive, as the results of any testing we did were small as a percentage of A/R. However, other than the fact that the company consistently used the full credit line and did not maintain significant liquidity, nothing appeared to be out of the ordinary and this was attributed to the company keeping A/P very current.

On September 21, 2002, one year into the deal, the company reported to us that they had had a massive fire in their warehouse in Brooklyn (there was also a warehouse on Long Island) and that almost all of the inventory had been substantially destroyed. This was obviously distressing news; however, the company informed us that the inventory had been fully insured so, despite the fact that inventory with a cost of $100MM had been destroyed, insurance proceeds were expected that would more than make both the lenders and the company whole. We had a Lenders Loss Payee Endorsement

in our favor and accordingly assumed we would receive a check in due course. Our advance against the inventory had been $50MM and we now had an overadvance in that amount, which would have to be repaid with the insurance proceeds. At this time, we believed the company had been the unfortunate victim of an accident and accordingly we planned to support them through this troubling period. A salvage expert was retained by the insurance companies to dispose of any inventory that survived the fire and that could be sold albeit in a soiled or damaged state. He was also responsible for removing all inventory/rubble from the warehouse. During this effort, 15 to 20 40-foot dumpsters were filled with waste. This is important as it validated that there was merchandise in the warehouse at the time of the fire. This turned out to be very important based on future events. However, insurance personnel on site during this removal process were concerned that certain items or the remains of items that should have been present based on inventory reports were not found.

On September 21, 2002, one year into the deal, the company reported to us that they had had a massive fire in their warehouse in Brooklyn (there was also a warehouse on Long Island) and that almost all of the inventory had been substantially destroyed.

Shortly after the fire, the Fire Marshall issued a report stating that, in their opinion, the fire was of a suspicious nature and they suspected arson. This report, combined with the suspicions noted above, prompted the insurance carriers to withhold payment on the claim pending further investigation. Allou maintained that vandals must have broken in and started the fire.

At this juncture (mid-to-late October 2002) we still had no reason not to believe the company or to discontinue our support. We continued to finance on a daily basis based on new sales and new purchases of inventory. As the days turned into weeks and we received no payments on the insurance policies, the lenders obviously became concerned. The insurers began conducting EUOs (examinations under oath) of certain members of Allou management, causing further delays. The insurers also challenged our lender loss payee endorsement, an argument we eventually won but which caused even further delays and was not achieved without first having to litigate with the insurers. (A sign of things to come.) We pressed the company to come up with an alternative solution to clear the overadvance. David S. informed us that he was negotiating the sale of Sobol (the prescription drug distributor) to a well-known entity that we knew had the wherewithal to close a deal. He represented that the purchase price would be roughly $40MM and would substantially clear the overadvance and that, once the insurance proceeds were finally received, the company would clear the balance and have significant availability. We were relieved to hear this news and awaited further developments.

In March of 2003, Otterbourg, as counsel for the lenders, and Proskauer as counsel for the company, initiated a lawsuit against the six insurance companies in state court as following, their investigations, which were inconclusive, they continued to withhold payment. A word about the insurance carriers: While there was one policy, there were numerous carriers, with each having liability under the policy at a different dollar level so the first carrier was responsible for claims up to their limit, then the second carrier up to their limit, then the third, etc. The carriers involved were household names: Travelers, Seneca, Lloyds, Royal, Chubb, and Zurich.

Also in March we elected to conduct a field examination to insure that the remaining collateral was still performing and that reporting was accurate. In addition to examiners at the borrower's main location, we arranged a site visit to a satellite warehouse in Nyack, NY. We were not aware that the Nyack location existed until our examiners at the company's HQ discovered the existence of this location on the inventory perpetual. The company's failure to inform us of this location was another red flag. Under the terms of our agreements, all borrowers were required to notify us in advance whenever they opened a new inventory location so that insurance could be updated, landlord waivers obtained and, in those days, UCCs filed covering the location (no longer required under the UCC). On the very first day of our visit to Nyack our examiners called to say that they had been denied access to the warehouse and that the warehouse personnel were being uncooperative. I will never forget this call. Our entire senior management was together in a conference room as we had convened credit committee. When the call came in, we had it transferred to the conference room. We all heard the news at the same time. You could have heard a pin drop for a few seconds and I believe the hair on the back of each person's neck went up as lack of cooperation is always a red flag, and especially given the current situation. The examiners were instructed to let the warehouse manager know that they would be returning the

next day accompanied by senior personnel and then to leave, but to return the next day to meet in the parking lot. The following day, we were once again denied access. I had a brief closed- door meeting with warehouse personnel, explained that we were in the midst of what we regarded as a possible criminal investigation and that, if our worst fears were confirmed, anyone assisting the company would be regarded as colluding with the wrongdoers. This was a complete bluff on my part, but seemed persuasive as we were ultimately allowed to enter the premises.

The inventory was in a shambles. It appeared that what was there had just arrived and been unloaded without any order or system and was just piled in a heap. There were no aisles and there was no way we could perform test counts. Another conversation with warehouse personnel persuaded them to restack the inventory in some semblance of order so that we could return and do some testing. We returned a few days later and indeed the inventory was now organized such that it could be inspected. Almost immediately it became apparent that all was not well. For certain items, our counts went well and proved accurate, but the costing was completely out of line. For example, while we accurately counted almost 130,000 room deodorizers that typically sell for about $1.99 each, we found that they were costed at $8/unit, an overstatement of roughly $1,000,000. We found cosmetic containers that should have had powder in them that were empty, yet valued as though they were full. We found items marked as "for export only." We found old, outdated inventory and, when we tested the perfume, while the quantities were generally right, we discovered that we were counting the little gift items that are given away for free, not bottles of perfume. Just as bad, these were off-brand perfumes that were no longer popular. I vividly recall counting thousands of samples of Baywatch, swearing under my breath the entire time. In a nutshell, it was a mess and our conclusion was that the inventory reported at this location was overstated by at least $16MM. After several hours, during which things went from bad to worse, we elected to stop, thanked the warehousemen for their efforts and left. I called the office from my car and spoke to our CEO and chief credit officer, who were obviously not pleased. I told them I was driving directly to company HQ to confront the CFO with our results and ask if there were any explanations for this seeming overstatement of our collateral.

The inventory was in a shambles. It appeared that what was there had just arrived and been unloaded without any order or system and was just piled in a heap. There were no aisles and there was no way we could perform test counts. Another conversation with warehouse personnel persuaded them to restack the inventory in some semblance of order so that we could return and do some testing.

Upon arriving at the company's location, I was left to wait for over an hour before being greeted. I went and spoke with our examiners on site at this location. They were having similar cooperation problems and had been instructed not to walk in the warehouse without supervision. The company also insisted on receiving our test count selections in advance, yet another red flag. To our examiner Robert Morelli's credit, he refused to provide selections in advance as he knew this would compromise our findings. He and I toured the warehouse together and it was pretty obvious to us both that inventory levels at the Sobol section (caged and segregated as these were pharmaceuticals) were drastically low. This called into question the legitimacy of the claims that this unit was being sold. I should note here that it came to my attention that previous examiners had indeed "cooperated" with company personnel by furnishing our count selections to the company in advance of the actual counting. We should not have done this, as a company with the intent to defraud a lender will insure that those items selected for the test miraculously appear. Since ABL lenders typically only count a small fraction of the inventory and then extrapolate the results over the total inventory, successful counts of the test sample usually result in an assumption by the lender that the entire inventory report is correct, a fact that Allou, having been financed for years, knew quite well. Finally, David S. came to get me. I was introduced to all the other officers of the company by David S., who promptly left the meeting. I presented our findings to the assembled management team, who first denied everything and said we must be mistaken and who finally asked that they be given a few days to look into it and come back to us with a full report. Their demeanor during the entire meeting was disturbing. They were arrogant, dismissive, talked among themselves without addressing me and downplayed my concerns. I was by now completely distrustful of anything management

said. For those of you who know me, you can only imagine my temperament at this point. I believe it is safe to say that all antennas were up at Congress. I steadfastedly believed we had been defrauded and for the first time worried in earnest about the fire marshall's findings. Others shared my view, but we agreed to allow the company a chance to explain. Declaring a fraud is not something a lender should do lightly and, while we were all anxious now, we needed more information.

I returned to our offices and gave a full report. We determined that we would give the company a few days to explain our findings while our team in the field continued the exam. Several days later the management of Allou came to our offices for a meeting. They explained that at holidays, Valentine's Day, Mother's Day, Christmas, etc., they assembled gift baskets for some of their customers and that all the components we found that we thought were overpriced or valueless were used in assembling these baskets. We asked that they provide purchase orders and a sampling of invoices that would corroborate these claims. Call this "trust, but verify" if you will, but we were no longer taking their word for anything. The company asked for a few more days to provide the requested documents. In the meantime, our examiners continued to have difficulty gathering information or getting cooperation. People that they needed made themselves unavailable; requested reports or documents were slow in coming or not provided at all. This is never a good sign and we all knew it. I, for one, was now convinced that the company was lying through their teeth and just stalling us and had committed a massive fraud on the lenders. At this point, we determined that we needed a consultant as eyes and ears on the ground. We introduced Dick Sebastiao of RAS Management Advisors (RAS) to David S. and suggested (read insisted) that the two meet in person.

During these discussions, Dick requested authority from David S. to shut the warehouse down for the weekend to perform a complete physical inventory. He also asked for permission to change all of the locks in the office and warehouse and David S. approved. The timing of the inventory count was perfect because it was the month and quarter end for SEC reporting purposes.

Dick had dinner with David S. to discuss RAS's services and potential involvement. Dick then went to the company headquarters the following day with David S. to get the assignment started. He was joined by 2 of his RAS staff. David S. introduced Dick and his associates to the company staff in accounting, warehouse and sales management and other departments and said RAS was going to help the company deal with the banks. While standing in the doorway to the conference room, Dick noticed a young staff member from Allou going into the president's office and coming out with a personal computer tower over his shoulder. He immediately asked the head of warehousing and sales if he could please get the computer back and he did so. Upon receipt of the tower, Dick turned it over to RAS staff members for safe keeping. RAS kept the computer in the trunks of their cars for several days until we had the authority to examine it, which occurred after certain other events described further in this article. They rotated who had the computer and brought it into their hotel rooms at night. Talk about not trusting anyone. Dick was on red alert.

During these discussions, Dick requested authority from David S. to shut the warehouse down for the weekend to perform a complete physical inventory. He also asked for permission to change all of the locks in the office and warehouse and David S. approved. The timing of the inventory count was perfect because it was the month and quarter end for SEC reporting purposes. Dick called the accounting firm partner, whom he knew from his days in accounting (at Anderson), and told him it would be in his best interest to send over at least three staff people to observe the counting and take test counts over the weekend. He agreed and provided assistance. The RAS staff was also increased for this testing. Collectively, almost 80% of the inventory was counted by RAS and the accounting firm teams and they actually retested around 50% of those counts. We were certain the counts recorded were accurate and had been correctly reconciled.

RAS controlled all of the paperwork to ensure no tampering and controlled the input into the mainframe computer of all inventory counts into a separate file and then compared their counts to the company's inventory system. When completed on Tuesday morning, we noted an approximate $70 million shortfall as compared to the inventory reports submitted to the agent. By this time, the head of IT and the controller had stopped coming in, so Dick located and engaged an outside computer firm (SBI) to monitor the computer system until

we could get authority to control the system. Little did we know that, while the head of IT and the controller were no longer present at the company, they had remote access to the company's computers.

When Dick called me to tell me about the inventory shortfall, I think he could hear me gasping for breath. (I was on the treadmill at the time, but this was shock, not being out of breath.) I immediately asked Dick to take a look at accounts receivable. He went to the accounts receivable manager and asked to see his aging. That gentleman handed Dick a stack of greenbar paper that was only about a half inch thick and totaled just $29 million. Dick asked him where the other $100 million was and he got defensive and said this list was all he knew about. The total receivables reported to the banks was $129 million. Dick instructed his staff to look deeper into this inconsistency and asked us to supply him with the receivable aging that was last reported to us. That report was over six inches thick and, as indicated above, totaled $129 million. Over the next several days, RAS tore into that report and found some extraordinary disparities. When they found these discrepancies, they increased their staff to around nine people for about three weeks, then cut back to a core group of three to four people. I determined that, while we were pursuing answers, we would not skimp on professionals, no matter the cost. We needed answers and fast.

Walmart was listed on the bank aging as owing $14 million. RAS determined that they really owed just $1.4 million and that their total sales volume for the prior year was just $14 million. The IT department had written a program to create invoices of varying dollar amounts, some as much as $2.7 million as recorded in the company books, but transmitted to Walmart electronically as $.01. In doing so, the invoice appeared in the Walmart system as valid. The way invoices were verified by the field examiners was to locate the invoice number in the Walmart system and check it off. We presumed that the fact that the invoice number was in the portal meant it was legitimate. The RAS staff went a step further and went into the Walmart payment system where they show what is scheduled for payment. It was there that they saw the $.01 invoices, which added up to nothing on Walmart's books, but which fraudulently totaled around $13 million on the Allou books. The company had fabricated support documents for each of these phony invoices. This is an important lesson. We were a big firm, we had over 500 clients, we did thousands of field exams. We were not amateurs. Yet, verifying invoices as being in the portal stopped one step short of truly verifying their legitimacy and authenticity. We had failed to take that extra step.

RAS then went into more of the details and found the remaining $87 million of fictitious billings to other fictitious customer names. When making calls to verify those accounts, we received totally non-responsive answers such as "go ask the CEO what that is all about if you want to know, etc." The IT department had recorded all of these sales as being made by Salesman #2. Sales made by Salesman #2 were not included in the sales report given to the sales management team so as to hide that volume and were not included in the aging that the accounts receivable manager used for making collection calls, but were all included in the reports given to Congress. During these investigations RAS also reviewed cash receipts in detail. They discovered that checks received from "ABC Company" were shown as paying WalMart or other customer invoices. As we all know, only WalMart pays for WalMart and using a WalMart account. These were simply phony receipts making a round trip to pay off phony invoices, thus making it appear as though there was significantly more sales activity than there really was and this also explained why turnover (or DSO) always looked consistent. The company would create phony invoices, borrow against them and use some of those proceeds to pay down phony A/R. And do it over and over again. Our failure to examine actual checks and remittance stubs was another shortcoming on our field exams. We examined cash receipts registers and bank statements but, as with the A/R portal, did not take the extra steps.

While some of RAS staff were reconciling the receivables, others were investigating how the inventory fraud was perpetrated. They determined, with the help of SBI, that there was a non-existent Warehouse #8. The only way to access Warehouse #8 was, when you went into the inventory system, you had five seconds to notice a flashing box and then insert an A in that box. That gave you access to the details in that warehouse, all of which appeared to be fictitious. The purchases that were entered into Warehouse #8 were supported by fictitious invoices generated by the senior management, together with fictitious purchase orders and receiving reports. Sales and inventory management personnel did not receive information that included Warehouse #8 because it would have caused confusion on what to buy to fill real customer needs.

The company was making payments to these non-existent vendors through the accounts payable system by way of manual checks. Those payments would be debited to a prepaid account in the general ledger until month end when the controller would request (by email) support for each payment and then make a general ledger adjustment to transfer the prepaid balance to inventory. It was now clear that the company was maintaining two sets of books: one with the actual business and one created just for the lenders to inflate the borrowing base. Because the company had been financed by ABL lenders for so many years, they had learned what our field exam protocol was and knew what documents they needed to create to satisfy our testing.

As an example of the magnitude of the testing and analysis being done, I submit this excerpt from an RAS report: RAS examined all disbursements in the six years prior to the BK filing that were greater than $15,000, totaling ~$2.275B in disbursements.

RAS' initial focus was on 42 entities believed to be affiliated with management. RAS examined ~$687MM worth of disbursements and, using a developed set of evaluation criteria, found that 70% ($475MM) of the disbursements were false purchases of inventory. The majority of these false purchase disbursements were round-tripped from the affiliated entities back to Allou to support AR collections to support the fraud.

Another 5% ($26MM) of the total disbursements were related to otherwise suspicious general ledger accounts (Loans & Exchanges, Officer 1099 & Donations). Some of these disbursements were for false purchases of inventory but many others were sent to third parties with no round-tripping, with the funds often moving overseas.

In addition, RAS examined another ~550 transactions totaling $64MM with ~400 different parties (different from the initial 42 noted

above) that were deemed suspicious according to our evaluation criteria. The vast majority of these transactions were all deemed to be fake transactions with little or no physical backup. The same suspect general ledger codes were used as above and a majority of these funds were also moved overseas. As the reader can see, this was fraud on a huge scale and it took a firm the caliber of RAS to sort it all out.

While all of this was going on, the senior management, together with a few of their accomplices, broke into the warehouse/offices over the weekend when the counts were being made and took troves of documents out with them. The head of security was approached at home to give them keys for the new lock and refused, so they went to the warehouse manager's house and got them from him. We had the break-in on the security cameras/tapes and presented them in court at a later date. More on that later.

While all of this was going on, the senior management, together with a few of their accomplices, broke into the warehouse/offices over the weekend when the counts were being made and took troves of documents out with them...We had the break-in on the security cameras/tapes and presented them in court at a later date.

On April 1, while the work described above was ongoing, the senior officers of the company met with senior management at Congress along with counsel. They offered to pay us $10,000,000 under their PGs in return for full releases. That request received a swift and resounding NO. I think at that point we all knew we had a huge problem; the question was, just how big.

On April 8, Dick met with two of the partners at the company's law firm to tell them what we had found and the extent of the fraud so they could deal with the necessary SEC reporting. Allou's counsel was shocked and couldn't believe our reports of the total amount involved. Dick left them to discuss it internally with their internal SEC counsel. They subsequently met with the senior management and filed an 8-K with the SEC and all trading was stopped.

Shortly after this meeting, while Dick was in the Company's conference room with his team late in the evening, he received a call from the CFO with a menacing message. Having learned of the Brooklyn fire and related allegations, it made Dick nervous enough that he actually called his wife and told her to keep the alarm on in the house at all times and don't ask any questions until this situation resolved itself, which did not happen until April 14. We were dealing with bad people.

Part two of this article will appear in TSL's September issue.

Mark Fagnani is senior managing director, Clear Thinking Group, a boutique advisory firm focused on turnarounds and restructurings, process and performance improvement and creditors rights. He has more than 30 years of hands-on experience working with large bank groups, private equity sponsors, turnarounds, workouts and insolvencies. Over the course of his lending career, Fagnani has worked with companies in a multitude of industries including steel and aluminum, coal mining, transportation, plastic injection and blow molding, beverage distribution, retail, lighting, and generic pharmaceuticals.

Fagnani was formerly a managing director and the chief credit officer of Wachovia Capital Finance, a unit of Wachovia Bank. After leaving Wachovia, he helped form HVB Capital, a subsidiary of Hudson Valley Bank, and subsequently spearheaded their sale to EverBank, resulting in EverBank Business Credit. More recently, Fagnani was recruited to help establish an asset-based lending business for Bank Leumi USA, serving as first senior vice president and group head of Leumi Business Credit.

Fagnani is a frequent lecturer and panelist. Most notably, he spoke on behalf of the World Bank and the Secured Finance Network in China, instructing over 250 bankers on asset-based lending.

FEATURE STORY

Construction Continues to Adapt Amid Increasing Costs and Labor Shortages

BY ERICK BEAUDOIN

Despite the devastating effects of the ongoing COVID-19 pandemic, which have weighed on the global economy, created volatile indexes, clogged supply chains, shuttered factories, disrupted shipping and limited the sale and movement of goods worldwide, the construction and building products industries in the U.S. adapted and many sectors experienced significant growth during 2020.

Takeaways

1. Despite the devastating effects of the ongoing COVID-19 pandemic, the construction and building products industries in the U.S. adapted, and many sectors experienced significant growth during 2020.
2. Demand for new construction increased in the U.S. and Canada during the pandemic as homeowners considered a transition to less densely populated geographies.
3. At the same time, homeowners are investing in existing homes, and repair and remodel spending continues to strengthen.
4. While demand for new construction and repair and remodeling activities will continue in the near term, the price of certain building materials is skyrocketing amid a growing labor gap.
5. Gordon Brothers conducted an internal survey of its building products clients and found 100% of respondents were bullish on the current expansionary trend continuing in the near term or through the end of 2021.

ERICK BEAUDOIN
Gordon Brothers

As the industry recovers from pandemic-related downturns, the spike in building material and labor costs, attributed to shortages and delays from supply chain disruptions, is expected to continue throughout 2021. Companies across a range of industries are currently navigating higher commodities pricing for lumber, roofing supplies and other building materials while grappling with product delays and labor shortages.

The broader commercial and residential construction market has performed remarkably well despite the pandemic and ongoing building supply challenges, and Gordon Brothers has seen several trends accelerate, many of which we expect to continue during and post-pandemic.

Housing Market and Construction Spending Strengthens During Pandemic

With homeowners spending more time working and overseeing remote learning at home, repair and remodel spending continues to strengthen as they invest in existing homes. Additionally, the pandemic is improving the demand for new single-family residential construction as homeowners consider a transition to less densely populated geographies.

By mid-to-late summer 2020, new construction had increased upwards of 30% year over year (YoY) in new home demand and the numbers are still coming in strong.[1] Although housing production in 2021 has softened since January as rising lumber prices continue to affect the housing industry, both private and public residential spending is up 21% YoY.[2]

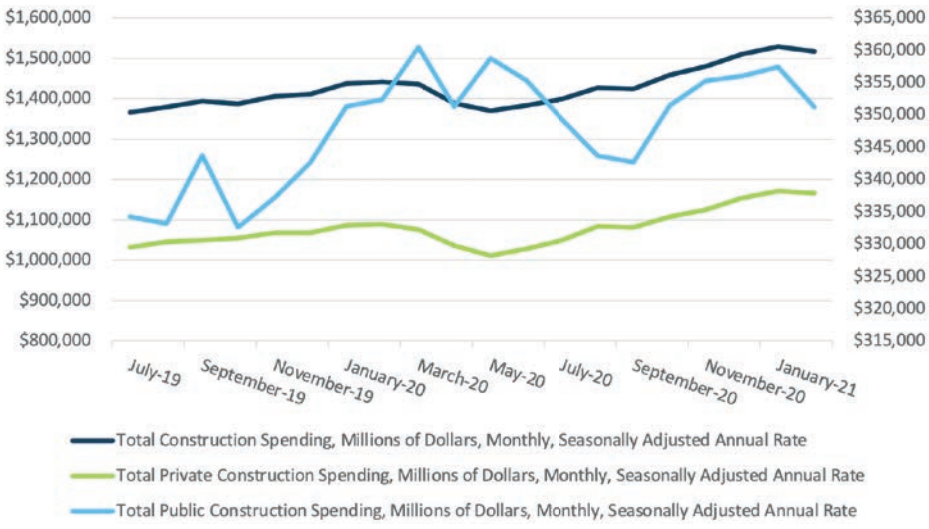
Despite a slight decrease in construction spending in February because of bad weather and pricier materials, it's still higher than it was last year. Overall U.S. construction spending is up 5.3% versus prior year levels and private construction is up 7.1% year over year. In January, spending hit a record high of $1.528 trillion.[3]

These trends are also strong in Canada with the total value of Canadian building permits issued in February setting a record and breaking the $10 billion mark for the first time. Additionally, the non-residential sector jumped 14.2% to $3.3 billion in February.[4]

Another positive indicator is mortgage interest rates, which hit historic lows in January, with the average interest rate on a 30-year fixed-rate mortgage at only 2.65%.[5] Since January, mortgage rates have risen by more than 30 basis points, and demand has been affected. Housing activity should remain strong with mortgage rates at record lows, strong federal stimulus spending trends and low housing inventory rates.

Based on the underlying market fundamentals and trends, Gordon Brothers believes demand for new construction and

Public & Private U.S. Construction Trends



[1] Based on SFNet Asset-Based Capital Conference, March 9, 2021.
[2] U.S. Census Bureau Economic Indicators Monthly Construction Spending February 2021 Released April 1, 2021 https://www.census.gov/construction/c30/pdf/release.pdf
[3] U.S. Census Bureau Economic Indicators Monthly Construction Spending February 2021 Released April 1, 2021 https://www.census.gov/construction/c30/pdf/release.pdf
[4] Statistics Canada https://www150.statcan.gc.ca/n1/daily-quotidien/210401/dq210401a-eng.htm?HPA=1
[5] Freddie Mac, Primary Mortgage Survey http://www.freddiemac.com/pmms/#

repair and remodeling activities will continue in the near term and current trends represent a sustained, rather than temporary, shift in consumer behavior.

Building Products & Material Costs Rise Amid Growing Labor Gap

For certain parts of the country, the industry is a very seasonal business that had been growing over the five-year period ended December 2019 at an annual growth of 1.8%, supported by a housing market that had been expanding steadily since the recovery from the previous 2008 Recession.[6]

Prior to the pandemic, revenue for the building products industry was forecasted to decline slightly in 2020, based primarily on the expectation the housing market and the North American economy would soften.[7] However, building product distributors and retailers were deemed essential, allowing these businesses to remain open during the pandemic.

A variety of trends including home office construction, finishing basements, home improvement because of boredom and moving to suburbs have increased renovation and remodeling spend and have all contributed to the strength of the cycle today.

Additionally, an increase in proposed government spending on infrastructure development should positively impact public construction spending trends and a variety of related building products including aggregate, structural steel, communication and electrical wire, and others.

Gordon Brothers provides appraisals, disposition opportunities and financing in the building supply market. We recently conducted an internal survey of our building products clients and found 100% of respondents were bullish on the current expansionary trend continuing in the near term or through the end of 2021.

A chief operating officer of an upper Midwest building materials dealer noted the following, which summarizes the respondents' collective sentiment.

"While we do not think the repair and renovation market will persist indefinitely at the elevated levels created by the COVID-19 pandemic, our conversations with retail customers and remodeling contractors indicate this will continue for some time," the chief operating officer said. "Many of the remodeling contractors are booked with projects for the rest of 2021 and, with the scarcity of homes for sale on the marketplace, repair and renovation should remain strong for some time."

Pandemic-driven supply chain issues, shipping delays and tariffs are all affecting the price spike in materials. Factories that decreased production when demand dropped in early 2020 with the onset of the pandemic are still not running at full capacity.

Adding pressure to the jump in material prices is a labor gap. Construction companies will need to hire at least 430,000 more workers this year than they employed in 2020. Additionally, construction spending is likely to reach $1.45 trillion in 2021, up 1.3% from 2020.[8]

In terms of home improvement, Gordon Brothers does not expect to see much change in the high prices of building materials, other than temporary impacts and commodity pricing issues, until supply chain issues alleviate. Construction material shortages are likely to continue throughout 2021 and pricing will accordingly not likely be alleviated anytime soon.

Below is an overview of specific building materials sectors that are affecting the construction and home improvement industries.

Lumber

Many regions in the U.S. and Canada are facing lumber shortages, and there were several events in 2020 that disrupted an otherwise relatively steady industry.

The sector is recovering from shortages caused by mill lockdown orders and shutdowns, new safety protocols that slowed production, wildfires and lingering timber beetle issues that created shortages and contributed to high lumber costs.

Lumber prices were up over 90% in 2020 and will continue to be in high demand with the increase in new construction. The May 2021 Random Lengths Futures Contract price reached $1,129 per thousand board feet on April 9, which was more than double the price for the front month lumber futures contract from January.[9]

A U.S. manufacturer of hardwood veneer and hardwood plywood Gordon Brothers partners with expects the current market conditions to exist through the rest of 2021 but expects a trail off in mid-2022 and a return to "normal" levels.

The manufacturer does not believe current supply chain issues will ease anytime soon and has had to make some hard decisions regarding cost structure.

A second privately held lumber production company in Canada explained, while the pandemic has affected lumber prices in their market, it was not the only driver.

The fundamentals for a run on prices were in place before the pandemic started, according to the lumber producer, citing years of just-in-time inventory practices, lumber shortages because of wildfires, beetle infestation and plant closures in recent years.

Additionally, the company noted "70% of the U.S. softwood lumber consumption is in residential construction, and housing starts before the onset of the pandemic were not keeping up with demand." According to the producer, "pricing was going to increase in 2020, pandemic or not."

[6] Gordon Brothers, Building Materials & Supplies Trends Industry Insight https://www.gordonbrothers.com/insights/industry-insights/commercial-and-industrial-residential-building-products

[7] Gordon Brothers, Building Materials & Supplies Trends Industry Insight https://www.gordonbrothers.com/insights/industry-insights/commercial-and-industrial-residential-building-products

[8] Associated Builders and Contractors analysis of U.S. Bureau of Labor Statistics https://www.abc.org/News-Media/News-Releases/entryid/18636/abc-the-construction-industry-needs-to-hire-an-additional-430-000-craft-professionals-in-2021

[9] Source is Wall Street Journal, market data center from April 9, 2021 https://www.wsj.com/market-data/quotes/futures/LB00?mod=md_cmd_overview_quote

[10] Roofing Marketing Outlook 2027 https://www.alliedmarketresearch.com/roofing-market#:~:text=The%20global%20roofing%20market%20size,rain%2C%20and%20other%20atmospheric%20conditions

Roofing

The residential roofing market was forecasted to remain stable in 2020 and, although there were short-term challenges with weather events and demand falling across multiple segments because of the ongoing pandemic, a rebound is expected in 2021. Weather events, especially in the southern states, can have a significant effect on roofing material prices.

The global roofing market size was valued at $92,942.3 million in 2019 and is projected to reach $132,775.6 million by 2027, an almost 43% increase.[10]

Demand for roofing was strong in 2020. Owens Corning, which accounts for approximately 20% of the U.S. market,[11] noted the asphalt roofing market grew 8.6% in 2020 driven by a 13.2% increase in weather and storm driven repairs, a 6.3% increase in repair and remodeling demand, and a 9.1% increase from new construction activity.[12] The company expects "continued strength in the U.S. residential housing market with commercial and industrial markets recovering at a slower pace."[13]

Granite and Flooring

Fueled by consumer growth in building and remodeling, the granite sector is expected to rise at a considerable rate over the next few years. The global flooring market size was valued at $388.24 billion in 2020 and is expected to grow at a compound annual growth rate of 6.1% from 2021 to 2028.[14] Respondents to the Gordon Brothers survey in the flooring sector had a bullish outlook, believing their customers "will continue to use their discretionary budgets to invest in their properties and home quality."

At the same time, they were concerned about a growing labor shortage, which is creating difficulties in responding to strong customer demand, continuing supply chain challenges and an unprecedented increase in transportation costs.

A large U.S. granite and natural stone tile distributor noted net revenue declines of 3.5% in 2020, citing weakness on the west and east coast driven by COVID-19-related disruptions and the closure of two branches. Despite the drop in revenue for 2020, this company had a positive outlook for 2021, noting a double-digit growth forecast for repairs and renovations published by the National Kitchen & Bath Association[15].

Another respondent to the Gordon Brothers survey agrees with the industry sentiment and expect the growth and interest to remain strong on the repair and renovation side in addition to new construction.

Housing Market Recovery Uncertain with Volatile Building Supply Market

After an initial period of disruption to demand and the supply chain last year, residential building products have been resilient. Continued uncertainty and supply chain issues in the short term continue to challenge the building supply sector and, ultimately, the new construction and housing markets.

From an outlook perspective, how the housing market recovers from the pandemic is uncertain. The building products distribution market continues to be affected by supply chain issues, tariffs and to some extent, weather. Current interest rates are likely to continue to have a positive effect on the housing market. As the pandemic ebbs and more of life returns to normal, some the impacts on the building supply market that are pandemic-specific may subside.

From an inventory appraisal perspective, Gordon Brothers expects to see continued strength in building products markets, especially as product shortages continue to roil markets and both public and private construction demand remain robust.

In a rising-price environment, liquidation discounting tends to contract as buyers try to secure supply and lock in low pricing. However, there is the potential for a sharp price correction at some point as these high market prices increase capacity utilization and the supply chain issues eventually get sorted out.

Given the volatility in the building supplies market, lenders should be aware of the target company's costing methods and should consider incorporating a mark-to-market or lower-of-cost-or-market reserve. A mark-to-market reserve account will adjust the cost basis to market and ensure an advance rate, based on a percentage of cost, remains relevant even in a volatile market.

Erick Beaudoin is director, valuations for Gordon Brothers. With over 15 years of valuation experience, Erick Beaudoin has appraised billions of dollars' worth of industrial inventory collateral for financing purposes. His areas of expertise include building products, fabricated metal products, plastics products, automotive inventory, agricultural food products and fracking sand.

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FEATURE STORY

Trends in E-commerce During and Post-Pandemic

BY JONATHAN DEPTULA AND THOMAS PABST

The COVID-19 pandemic caused ecommerce to transition from "convenient" to "essential," but what does the post-pandemic world hold for this sector?

E-commerce is defined as the buying and selling of goods or services using the Internet, and the transfer of data and money to execute these transactions. Essential is defined as something which is extremely important or necessary. E-commerce has always been viewed as a disrupter in the retail industry because of its convenience, growing ease of use for the customer and consumer-centric policies. The dent e-commerce has made into the retail landscape has been obvious for all to see over the past decade, and there is no doubt that its influence will continue to grow. But to term it as "essential" would have been a stretch some 16 short months ago. That all changed with the rapid spread of the COVID-19 pandemic and the physical shutdown of our economy. Suddenly, these two words became synonymous, as e-commerce became the safest way for consumers to shop for virtually all of their most basic needs. As a result, the distribution center workers, truck drivers, and others who kept the industry humming were all deemed essential as well.

JONATHAN DEPTULA
HYPERRAMS

THOMAS PABST
HYPERRAMS

Now that we are reaching critical mass in the vaccination effort and consumers have been returning to stores and other activities, it made me wonder whether the pandemic floated the boats of all e-commerce retailers, and to what extent. We all have seen that Amazon the industry giant, posted sales increases of 40% or more, and record profits during the last couple of quarters. But what about the smaller, less-established players in the industry? Did they benefit as well?

The answer is absolutely, and not in just a couple of categories. We have completed the appraisal of twenty plus e-commerce retailers since the beginning of 2021, and all but two of those companies posted sales increases of 20% or more. The two that did not fit this positive criteria operate in industries where sales declines during the pandemic would be expected, including one that caters almost exclusively to support the in-classroom educational sector. Most of these winners also took advantage of less discounting to achieve these sales increases, with gross margins escalating in the majority of those companies for which we completed collateral monitoring assignments. Inventory levels, by and large, have remained in a range close to the prior year or have increased, as these companies have proven their ability to procure stock to help support the significant rise in sales. Furthermore, an increase in customer traffic to their websites, as well as third-party shopping sites as a result of the pandemic, enabled some of these companies to clean up excess inventory. That said, not all e-commerce companies took advantage of this opportunity, and some may still need a push to markdown that slow-moving inventory to provide increased liquidity for new inventory.

The real question now is: What happens to those sales volumes as the pandemic eases and physical retail stores reopen? Our initial read is that sales volumes have held during the first four months of 2021 and, while we cannot predict the future, it seems unlikely that e-commerce will yield ground to brick and mortar going forward. This indicates to us that borrowers will need to continue the maintenance of higher inventory levels in order to support their sales volumes. If the need for increased borrowing by your customers has not already taken place in order to build or rebuild inventory, it may be forthcoming in the very near future. This need can potentially create more opportunities to those lenders that already have e-commerce-based customers and those that are trying to enter the space.

Recent and continuing supply chain issues are forcing all retailers — and not just e-commerce businesses — to reassess their purchasing habits. The delay in the receipt of inventory from overseas, the lack of shipping containers, the shortage of chips required to make smart products, and a general increase in the need to replenish consumer goods has to be accounted for in your borrower's purchasing habits. The need to purchase earlier, and potentially in higher quantities to offset future supply-chain delays, has to be considered by all e-commerce retailers. Of course, this always represents a fine line between building inventory in the wrong places and being in stock all the time on those products the customers need. However, if you haven't asked the question of your borrowers, you should proactively gain a better understanding of what their plans are heading into any upcoming high seasons. Most e-commerce businesses are all about growth and, in order to sustain that growth, increased inventory levels will need to be supported by their lenders. Additionally, the risk of increased pricing for the purchase of consumer goods is real, and it begs the question as to whether or not the increased cost of inventory can be passed along to the consumer. If the inflationary trends continue, and consumers ultimately pull back on purchasing because of price increases, pressures on gross margin could become a factor in the back half of this year.

The other big question is: what does this all mean for collateral values in relation to your customer's current borrowing base? Increasing sales, higher gross margins, and reduced weeks of supply and excess inventory levels are all positive indicators when it comes to recovery values. Sales increases during the pandemic were driven by many types of customers, including an influx of buyers who were either new or infrequent users of the e-commerce channel. Gaining new customers, and new customer email addresses, is an incredibly valuable thing during an e-commerce liquidation. In the event of a

meltdown, the ability to solicit established customers to purchase products they are already familiar with, through a website they are comfortable with, is critical. Liquidations on the Internet are not like retail store liquidations, where the physical placement of a going-out-of-business banner on the building can generate an increase to store traffic on its own. Every customer gained during the pandemic is a potential customer if a liquidation were to take place. Additionally, the increase in gross margins witnessed during the pandemic means that such customers have grown more accustomed to purchasing at those higher price points, even if on the surface they seem insignificant. The perceived value of a ten or twenty percent discount off of a slightly higher original selling price could mean an overall improvement to recovery values. And, if your borrower is one of those that took advantage of increased e-commerce traffic during the pandemic and reduced its excess inventory and weeks of supply, they should be sitting on fresher, more desirable inventory in the event of a liquidation.

Sales increases during the pandemic were driven by many types of customers, including an influx of buyers who were either new or infrequent users of the e-commerce channel. Gaining new customers, and new customer email addresses, is an incredibly valuable thing during an e-commerce liquidation.

A few other things to consider, that are not necessarily pandemic-driven, but always at the forefront of an e-commerce liquidation. For those companies whose inventory is solely sold through Amazon or through another third-party channel, the ability to create a true sell-to-the-walls mentality does not exist. There can be no going-out-of-business theme, no selling to the bare walls mantra to drive sales – but only changes in price. A sale through Amazon will benefit through the tremendous amount of traffic that its website alone drives, but it will likely be more of an orderly event that will take more patience. To ensure an extensive inventory sell-through, a more methodical approach to discounting may be required. Company support, particularly from those businesses whose prices are driven based on algorithms and other computer-generated methods, is even more essential to properly manage a sale. A lender will need to be patient in terms of expense rationalization to ensure the proper support is in place to achieve the sale's goals. There will also need to be more patience as the accounts receivable from the third-party sites turn into cash. Additionally, in a retail store liquidation, you can reduce prices to get to a total sell through of almost any category of inventory. It is less than certain, however, in a sale solely driven through e-commerce if inventory can ever be discounted far enough to sell-through to the last piece. Companies with very high weeks of supply, and significant amounts of excess inventory, will struggle even further to achieve an extensive sell-through. Do not be surprised if the bottom third of the inventory must be sold through a wholesale channel at significantly reduced recoveries if a total liquidation were to take place.

E-commerce, as an "essential" element of the retail landscape, is truly here to stay. Based on early data, it appears that e-commerce businesses will continue to thrive post-pandemic, and at least a portion of those sales gains derived in the last year or so will become permanent. It is also our belief that e-commerce liquidations, if there are to be any, would only perform better in this environment; lenders might just have to be a bit more patient to get to the end result. Although nothing changes faster than inventory as a collateral base, especially in a direct-to-consumer setting, the need to monitor never changes, even if current indicators are trending positive. So, remember, collateral monitoring is an essential business too.

Jonathan Deptula is senior managing director of appraisal services for HYPERAMS. He is responsible for managing the day-to-day operations of the appraisal practice, along with business development, inventory appraisals and supporting all other HYPERAMS business operations. Deptula works with asset-based lenders, commercial lenders, private equity firms and companies to help understand asset values. Deptula has completed hundreds of appraisals for firms in the US, Canada, United Kingdom, Netherlands, Belgium and Germany.

Thomas Pabst is president and founder of HYPERAMS. Specializing in asset disposition for middle-market companies, Pabst has a consistent history of increasing productivity and profits for manufacturers, distribution companies and retailers. With over 25 years of experience, he uses a unique combination of investigative, analytic planning and team building skills which have been proven very effective in identifying profit opportunities and driving their achievement for stakeholders.

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APPRAISER'S INSIGHTS

Restaurant Rebound Tests the Limits of U.S. Food Distributors

BY ERIC SCHLOEMER

Foodservice distributors generally adapted well to the massive disruptions triggered by the pandemic, but the sector is feeling the strain of the latest shift—the rapid return of tens of millions of Americans to in-person dining.

Historically, foodservice inventory and M&E have been good, stable forms of collateral, and the prospects of this "safe haven" sector remain quite strong over the long term. However, closer monitoring is always required when any form of collateral faces headwinds, which is the case in today's food-distribution sector due to shortages of truck drivers, refrigerated trucks, warehouse personnel and even some staple menu items in American restaurants. While these dynamics may be temporary, lenders in this space would do well to give the overall health of foodservice distribution borrowers a second look.

A little background: most foodservice distributors serve a variety of customer types, including independent and chain restaurants, healthcare facilities, schools and other government-funded entities like prisons and foodbanks, and supermarkets and small grocers. Typically, restaurants make up around 70-80% of a given distributor's customer base. During the pandemic, foodservice distributors shifted to grocery, which was deemed "essential."

As Covid-19 hit and restaurants closed, distributors were forced to either rapidly adapt to the changing landscape or shutter their operations. During 2020, companies like Sysco ramped up sales to grocery stores and other non-restaurant customers as consumers shifted from dining out to eating at home. As noted in the company's annual report, total overall sales fell by about $7 billion in fiscal 2020. But Sysco reportedly managed to win more than $1 billion in new business during the crisis by focusing on non-restaurant customers. Along with other successful distributors, the food giant was also able to decrease operating expenses at the start of the pandemic to remain profitable despite the sales decline.

In conversations we conducted with smaller distributors earlier this year, they expressed confidence that their inventory positions would hold steady. Most distributors keep a 2–3-month supply of inventory so, when sales slowed at the start of Q2 2020, this short length of supply helped protect them from becoming over-inventoried.

ERIC SCHLOEMER
Tiger Valuation Services

Distributors reduced sourcing and continued to maintain that same 2-3 months' supply even as sales remained lower. This meant that, in appraisals conducted prior to the restaurant rebound, their inventory collateral values were similar to pre-pandemic levels.

Challenges and Headwinds

But the situation is changing quickly. We're now seeing a dramatic shift in consumer behavior as Americans start traveling, patronizing entertainment venues, and eating out once again.

This past April, per preliminary U.S. Census Bureau data, total monthly sales at eating and drinking establishments reached $64.9 billion. This figure is about $2 billion higher than the prior month and $35 billion above the pandemic low, set in April 2020, of $29.9 billion.

This third consecutive month of rebounding restaurant sales was "driven by rising vaccination numbers and the easing of restrictions in many parts of the country," according to a press release from the National Restaurant Association. This shift means that distributors will need to pivot back to making more deliveries to restaurants, and less to retail operations like grocers.

At least for now, the dramatic surge is testing the limits of the U.S. food supply chain. Citing shortfalls of chicken and other basic food supplies; difficulty in finding workers, and mushrooming transportation costs, *The Wall Street Journal* on May 21 quoted Mark Allen, head of the International Foodservice Distributors Association, on the gravity of the situation: "Over the last six weeks, we have seen the market come roaring back faster than anybody would have anticipated," he told the newspaper. "The startup has been, in many ways, as difficult as the shutdown…Everybody is trying to turn it on immediately and the capacity might not be there."

The supply chain has reportedly been rocked by erratic

deliveries, in part because distributors reallocated so much of their capacity to grocery stores as a response to the pandemic. Formerly highly predictable, the availability of many basic elements in U.S. food distribution—corrugated cardboard, plastic packaging, staple foods and more—is now uncertain.

Other headwinds are presenting themselves. Labor costs have spiked and are expected to stay elevated due to both an increase in wages and labor scarcity, which should further drive wage growth. In a May 11 press release, The National Federation of Independent Business (NFIB) said 44% of owners had reported job openings that could not be filled. It was a record high reading and 22 percentage points above the group's 22% historical average for this labor measurement over the past 48 years. "Small business owners are seeing a growth in sales but are stunted by not having enough workers," stated NFIB Chief Economist Bill Dunkelberg. "Finding qualified employees remains the biggest challenge for small businesses and is slowing economic growth."

Food costs are also rising, resulting in an increase of prices at the operator level. Many CPG companies, including General Mills, Hormel Foods, and J.M. Smucker Co., reportedly have either implemented price increases or are planning to do so. Prices are expected to increase between 2.5-3.5% for the balance of 2021, per the USDA's April forecasts.

Faced with these pressures, some "on the bubble" food distributors (particularly smaller independent operators) may be poorly positioned for the future. During the height of the pandemic, their survival strategy could have included furloughing truck drivers and warehouse personnel to cut costs.

Inventory and Equipment Value

With any shift in the balance of supply and demand, lenders need to reassess collateral value. With respect to foodservice inventory, food prices increased by 0.4% in April due to higher costs for the likes of eggs, fish, dairy products, and fruit and vegetables, according to government data. Meanwhile, certain equipment used by food distributors—such as refrigerated trucks—is now in higher demand as well. On this latter score, it is worth noting that, when food distributors pivoted from restaurants to grocers, they were able to maintain smaller fleets of rolling stock. After all, there are far fewer grocers than restaurants in a typical market, and so a strategy focused on supplying grocers can mean less time on the road and fewer delivery stops made.

Now that the pendulum is swinging back to restaurants, those trucks (and drivers) are sorely needed once again.

Other collateral in this sector can include the shelving, material-handling and storage equipment found in warehouse and distribution facilities, and the buildings themselves. Here, too, a reappraisal could be beneficial: The value of some of this collateral may be on the rise as food distributors scramble to meet the demand triggered by the restaurant reboot in the United States.

Borrower Health

Faced with these pressures, some "on the bubble" food distributors (particularly smaller independent operators) may be poorly positioned for the future. During the height of the pandemic, their survival strategy could have included furloughing truck drivers and warehouse personnel to cut costs. Those personnel may now be either unavailable or too expensive to hire back. In addition, some distributors may lack the rolling stock, distribution facilities or operating capital needed to meet the resurgent restaurant demand.

In our experience, many of those regionals that could not stay afloat in 2020 were quickly acquired by other food distributors with stronger balance sheets.

If today's pressures prove to be too great for some distributors, their better-positioned competitors are likely to snap them up as well. Further consolidation seems likely because healthier regional food distributors know that growing their footprint and leveraging economies of scale is the best way to compete. Yet they are physically limited by radius: Making deliveries beyond a certain distance may no longer be cost-effective. These operators cannot go toe-to-toe with heavy-hitters like Amazon for new warehouse and distribution real estate built from the ground up. The only real way to expand is to acquire another company with its own territory,

facilities, equipment, customers and personnel. In particular, the value here is in the routes and customers of these targets: By making acquisitions, distributors either gain routes in new markets or increase their productivity and efficiency by bolstering the density of the routes they already serve.

These dynamics bode well for collateral value. In some markets, demand could be high enough that multiple food distributors could engage in a bidding war for the assets of other foodservice distributors.

What Comes Next?

Distributors that have successfully weathered the pandemic may be well-positioned to thrive as more states fully reopen their eating and drinking establishments. As costs increase, many distributors will be able to adjust their prices and pass through these costs, which is a necessity in this historically low-margin business. (Operating margin for Sysco, for example, has trended around 3.9% in the four years prior to 2020, and last year it was less than half that number.) Other operators, experiencing some extended disruptions, may need to be more closely monitored by their lenders to better position them to regain solid ground. Under normal circumstances, appraisal firms recommend that food distribution asset appraisals occur around every six months. That is to ensure that inventory stays in line with demand and to confirm the borrower remains healthy.

What are the red flags and areas to watch out for? Length of supply of inventory should remain in line with prior years; even if sales remain suppressed in the short term, successful companies should be able to adjust their sourcing strategies accordingly.

Last year, food distributors with efficient approaches to inventory management deftly scaled back their sourcing in response to lower sales. As a result, they are now well-positioned to bring on more inventory in response to the spike in restaurant sales. (This assumes, of course, the actual availability of that inventory. For now, certain basic items, including the likes of chicken, pepperoni, peanut butter and ketchup packets, are in short supply.)

In assessing borrower health, lenders would do well to scrutinize the distributor's overall length of supply. Companies that allowed length of supply to get too extended in 2020 may not yet have corrected the problem. As a result, some of that product could be nearing its expiration date. In other cases, distributors may be stuck with too much of certain low-demand products. Because they have too much capital tied up in that inventory, acquiring higher-demand products will be much harder for them.

Margins should also remain steady: Since higher costs are typically passed through in the form of higher prices, higher costs should not affect profitability. And last, a high route density is important, as maximizing sales relative to delivery expense is a key component of distributors' profitability. Make sure routes have been optimized, and personnel and rolling stock are at the right levels. Distributors with too much rolling stock, inadequate personnel, poor route-planning or some combination of the three make less money than their better-run competitors.

More and more states are easing restrictions and allowing restaurants to reopen and increase capacity. This is a positive development for an industry hard hit by the pandemic and lockdowns. Successful distributors will have the wherewithal to nimbly adjust to this great rebalancing.

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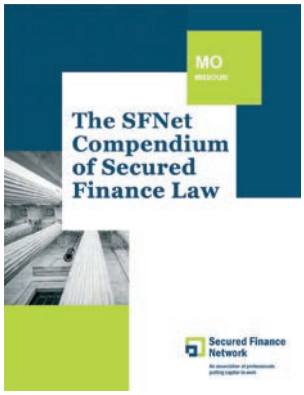

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CEOs IN TURNAROUND

Recognizing and Dealing With Overly Emotionally Vested CEOs in Turnarounds

BY MICHAEL WESLEY

CEOs of distressed companies deal with the stress in a myriad of ways, some more helpful than others. One of the less-than-optimal reactions is to become overly emotionally vested, which can cloud their perception of reality. Michael Wesley, of Clear Thinking Group, discusses the red flags to look for.

If you have been in the turnaround industry for long enough, you realize that CEOs handle the stress of turnaround situations in different ways. Some rise to the occasion and tackle the situation head on using a fact-based approach. Others shut down and try to just avoid the problem while focusing on protecting their own interests. Both of these types of reactions have distinct advantages and disadvantages to the ultimate outcome of a turnaround situation. But there is a third type of reaction to distressed situations that often leads to a worse result for lenders. This third reaction, which I call the "overly emotionally vested response", is a combination of the two, where the CEO appears to be tackling the situation head-on, but is, in fact, knowingly or unknowingly, acting to protect their own self-interest often at the expense of the lender's recovery.

The CEO may be the owner/founder of the company or they could have been hired by the Board or a sponsor. Sometimes the traits are inherent in their personalities, while others may only appear during distressed situations. However, there are several characteristics of the overly emotional CEO that need to be identified early on so that they can be effectively managed.

Externally, there are a few signs to look out for as you work with the company and the CEO that could indicate that they are overly emotionally vested. They tend to overstate the chances of success and underestimate the possibilities of negative outcomes, subscribing a higher probability of success to favorable outcomes than experience and history would warrant. They make the numbers "work" for them to address the situation instead of basing them on trend, probability, and other factors (e.g., "hockey stick" sales curve). They grasp at any and all opportunities that might address their "emotional needs," often keeping critical discussions with potential investors, lenders, etc. secret.

MICHAEL WESLEY
Clear Thinking Group

Internally, there are even more signs that might indicate the CEO is overly emotionally vested. They feel that the burden to "save" the company is solely on their shoulders. They tend to only want to listen to their internal team members who have been with them since the distressed situation was created and who they believe are personally loyal to them. They often challenge and do not take the advice of their external professionals who have the knowledge and experience to help the company through the turnaround situation. They view their lenders as the enemy and believe they are trying to ruin their business by adding more blocks, reserves and requirements in order to push them into bankruptcy. They tend to want to pursue "homerun" options (e.g., new lenders and or investors) which they believe can solve all of the Company's and "their" problems at one time versus systematically "hitting singles" to address specific problems that usually are quicker and easier to achieve.

Identifying that the CEO is overly emotionally vested is not an easy task. But once you have, the question is how to manage them and the distressed situation best in order to improve results.

Some believe the best solution would be to replace the CEO with one better suited to the situation; however, that is not always possible to do. If replacing the CEO is not an option, lenders should look to implement guard rails in order to improve results. These guard rails should include:

1. Setting clear milestones that define the ramifications if they are not met in a timely manner and sticking to them as best as possible. This can be difficult for a lender who is looking to work with the company in order to pursue every possible opportunity to improve the situation while not eroding their position any further. The key is to ensure that they do not exploit the opportunity being provided by their lender to pursue an agenda regardless of the probability of success.

2. Installing a set of advisors/professionals with the ability and, if needed, authority to check the CEO's actions. As consultants, we deal with overly emotionally vested CEOs all the time. We are often mistrusted, challenged, ignored and viewed as "spies for the enemy (lenders)." In these situations, it is critical that we are retained with the ability to enact needed change.

Recognizing that CEOs will react differently in distressed situations and being able to identify and manage their actions/reactions is key to the ultimate success of a turnaround and maximizing recovery. While not without its challenges, identifying an overly emotionally vested CEO is particularly important, since it can help lenders address these distressed situations better and typically insures improved results.

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Michael Wesley leads the Value Creation Practice Group at Clear Thinking Group LLC.

Wesley has over 20 years of consulting and management experience within the manufacturing, food and beverage, service, wholesale, and retail industries. He has worked in all areas of operations including finance, manufacturing, supply chain, warehousing/distribution, inventory management, planning/allocation, and IT. As a consultant, Wesley has been retained by numerous companies as the financial advisor in several turnaround and Chapter 11 engagements as well as those seeking value creation assistance. Wesley holds a BS in Mechanical Engineering and a Master of Engineering Management from Duke University. He also received his MBA from Duke's Fuqua School of Business where he was named a Fuqua Scholar.

FINANCE INSIGHTS

AI In Secured Finance

BY BRIAN RESUTEK

"We're a technology company that happens to do biology."
— Stephane Bancel, CEO, Moderna.

While lenders and financial institutions are not looking to discover the next vaccine or medical breakthrough, artificial intelligence (AI) and machine learning (ML) have been reshaping traditional business processes at a rapid speed. Many decision makers in the C-Suites, while still responsible for ensuring everyday "blocking and tackling" is done, are dealing with how best to integrate AI/ML into their companies, and at what cost. This article takes a deeper dive into how AI and ML are being utilized in the industry along with the factors leaders must consider with AI/ML integration.

AI and ML are not synonymous. ML should be thought of as a subset of AI, although ML is by far the largest subset, followed by others such as Deep Learning. Artificial Intelligence covers the broad landscape of creating intelligent machines while ML can learn from these creations and continuously improve performance when correctly implemented. As an example, the intelligence of the AI machine of a credit underwriting scoring model will provide a decision or outcome; however, through ML, which runs and depends on receiving continuous, updated inflows of data, the credit scoring system can be "learned" and smartly evolve or to improve the model and further benefit a company.

Not surprisingly, in the financial world, AI/ML was first used in the consumer finance space where troves of data are readily available. Areas such as credit card fraud detection and chat-box services, which many of us use daily, have grown quickly and are continuously enhanced as these models learn and train on data literally received every second of each day. Movement from the consumer financial channels to the commercial channels hasn't taken long as the benefits of AI/ML become more mainstream.

BRIAN RESUTEK
Rosenthal & Rosenthal

Philip Armstrong of Mo Technologies, a credit as a service (CaaS) fintech with proprietary technology in the ML and AI space, has seen the impact of AI/ML in both the consumer and commercial financial sectors. He gave the example that in Latin America, over 2 billion credit card transactions are declined annually due to non-sufficient funds (NSF). "The data showed that the average NSF was just $6 or 10% of the $60 attempted spend; this represented over $120 billion of gross dollar volume left on the table. Through appropriate scoring, we could determine that 40 – 50% of these should be processed because the default risk is extremely low," Armstrong stated. "This allows for improved overall customer and brand loyalty with the credit card company, not to mention capturing future revenues that were not available prior to the implementation of the scoring model."

In the commercial lending space, Mo Technologies used its ML capabilities to help credit-score smaller farming businesses that agricultural banks could not underwrite using traditional credit models. Armstrong cites that "the part of the model that is dynamic is the feedback loop, which constantly refines the model with appropriate frequency." Working with the agricultural lender, Mo Technologies could capture and train (and retrain) its model for the lender, showing default rates much lower than originally thought. This ultimately opened a whole new sector of borrowers for the bank and access to capital to farmers.

This new access to information through AI is rapidly moving through all sectors in the financing world largely for two simple reasons:1) Low cost and 2) It works. According to a recent Gartner Inc. forecast, AI will be involved in 75% of venture capital decisions by 2025, up from less than 5% today. Take the case of Correlation Ventures, a San Francisco-based early-stage VC firm with over $360 million under management. The firm internally developed a machine-learning tool that reviews information extracted by humans and pitch decks and other materials from startups to decide whether the firm should invest in a company. This information is then fed into an algorithm trained on data from more than 100,000 venture financing rounds according, to managing director David Coats of Correlation Ventures. But AI/ML projects do not churn out overnight or the next fiscal quarter, but rather the investment into ML must have a long-term outlook with support and understanding by C-Level leadership.

Daniel Faggella, the CEO and head of research at Emerj, a leading AI research and advisory company, puts heavy emphasis on this long-term outlook objective. "Businesses should avoid AI toys," states Faggella, meaning that "toy" applications are technologies or projects taken on because they use AI, not because they solve a business problem. Companies need to be careful not to just get into AI for the sake of getting into AI. Faggella believes that it is critical for companies to map out AI projects and to begin with the end in mind. Expanded further, "Leadership must understand that AI is an investment in a new paradigm of skills and resources, so not all experiments will prove immediately valuable in financial terms; initiatives that build towards core strengths and skills are ultimately valuable to creating transformation, not just surface-level solutions."

Going back to CEO Stephane Bancel's quote of calling Moderna a technology company that happens to do biology, illustrates a paradigm shift that took less than a decade to complete. Less than ten years ago, a 20-person Moderna firm was still manually entering nucleotide sequences into Excel spreadsheets per the standard industry practice. Today, because of Bancel shifting Moderna into full digitalization, it has become one of the leaders in the coronavirus vaccine development.

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In summary, AI/ML, along with deep learning networks, will serve to benefit the lending spaces not only in efficiency areas, but also in creating opportunities that might not even exist today. The ability to apply AI methodology to multiple segments within a corporation and continue to apply year after year and project after project are where the real benefits of the shift into AI are made.

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CapitalPlus: Helping Construction Businesses Succeed with an Infusion of Working Capital

With over 20 years in the construction factoring business, CapitalPlus has put almost $1 billion in funding into the hands of contractors and subcontractors seeking cash-flow support.

BY EILEEN WUBBE

BRENT CHAMBERS
CapitalPlus

In 1998, Scott Applegate saw firsthand a funding gap that left construction businesses without working capital. He founded CapitalPlus in Knoxville, TN to respond to that need with spot, contract and long-term factoring. The company now has offices in Atlanta, New York and Phoenix.

Like so many other industries, the construction industry has had its share of challenges due to the coronavirus pandemic. When the pandemic first hit in March 2020, the construction industry, which often serves as a barometer of the overall economy, was considered an essential business. The immediate challenge was keeping the workforce healthy and on the job. If a worker contracted the virus, job sites had to shut down and the crews had to quarantine, causing huge delays and a ripple effect on schedules. As the pandemic lingered, conditions in the market worsened.

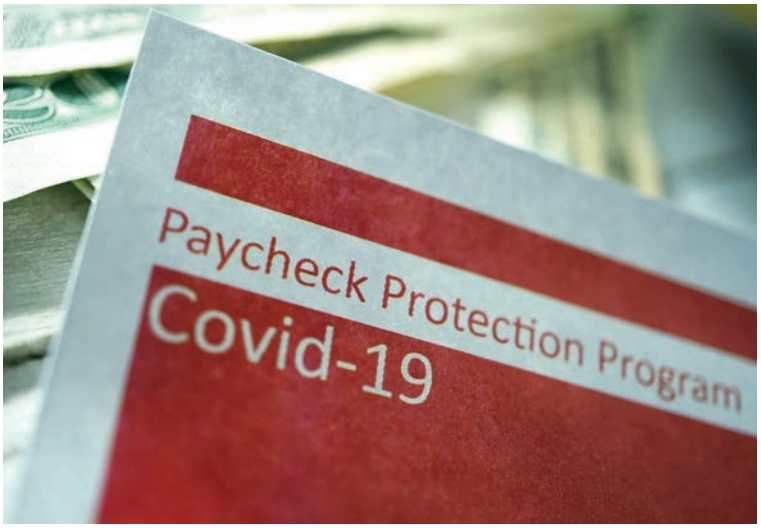
"We noticed our customers' backlogs were being greatly reduced, mainly projects that hadn't started yet," explained Brent Chambers, executive vice president, CapitalPlus. "In other words, contracts were signed, but our clients weren't due to start the projects for some time in the future. In those cases, the owners and/or investors were uncertain how COVID-19 would develop and what its ultimate impact on the economy would be. As a result, they cancelled projects outright or, at a minimum, stalled open-endedly. This affected contractors' pipelines, and, subsequently, the pipelines of non-traditional lenders."

The pandemic's impact on supply chains

delivered another blow to the construction space. Construction requires large amounts of materials such as wood, steel, concrete and finish materials. Many, if not most, manufacturers and suppliers were closed or running at reduced capacity for months. The drop in supply caused a large spike in costs that had to be absorbed, coupled with a related cost surge when demand returned.

"Pre-pandemic, a contractor may have bid on, and won, lump-sum contracts for projects to be executed in the future. Those bids were estimated using pre-pandemic costs, and as much as 35% to 50% of a project cost is in materials," Chambers explained. "A year into the pandemic, those materials are costing 30-40% more. Contractors and subcontractors are faced with three choices: seek cost modifications from their general contractor; try to absorb the added costs; or pass on the job altogether. At the same time, general contractors and owners have to decide how to cover the extra costs, or whether the project should be parked or terminated." Altogether, this is creating impacts up and down the chain, including project postponement or cancellation.

As in all recessions, most of the bigger construction companies could weather the storm, but a lot of smaller companies could not.



The SBA's PPP Loans and the Emergency Injury Disaster Relief loans were free or extremely low-cost government-backed loans and were very attractive to construction firms, which reduced demand for alternative financing. CapitalPlus has managed to weather the storm well.

Launching a new product

Mid-pandemic, CapitalPlus saw another way to help construction firms. They launched a materials financing product, a short-term capital solution in which a third-party lender, such as CapitalPlus, purchases the materials contractors and subcontractors need and gives them extended terms to pay it back.

"The industry was hurting, and it was not the time to shy away from challenges," Chambers said. "By offering materials financing for construction firms, we gave clients the strategic advantage of being able to order materials sooner than their current cash flow allowed. As a result, they can work faster, invoice sooner, and stay on or ahead of schedule. In the construction industry, completing a project on time is crucial to success. The funding also enables them to take on larger jobs, take advantage of vendor early payment discounts, and improve their supplier relationships, all without impacting any existing bank relationship or loan."

Impact on non-traditional lenders

In addition to the construction industry, the pandemic affected nearly all of the non-traditional lending industry. The SBA's PPP Loans and the Emergency Injury Disaster Relief loans were free or extremely low-cost government-backed loans and were very attractive to construction firms, which reduced demand for alternative financing. CapitalPlus has managed to weather the storm well.

"As a factoring company, we are rather diverse in our overall services," Chambers explained. "We offer spot and contract factoring, but we also offer a long-term revolving factoring facility that provides a flexible credit facility to our larger clients. For these larger clients, the PPP funds weren't enough to handle their cash-flow needs, and they've continued to fund with us. So, we've been fortunate in that aspect."

Looking forward

Another factor to consider for the future of the construction and lending industries is the seismic shift to remote work. Businesses quickly figured out how to make it work and now see it as a way to reduce cost.

"There's a tremendous glut of real estate and commercial office space available now. I don't know why you would return to the office if you can be just as efficient working from home, and that will have a long-term effect on both the construction and lending industries," Chambers said.

While no one has a crystal ball and no one could have predicted the pandemic would go on for more than a year, CapitalPlus is expecting some rebound in late 2021.

"Like most of the financial community, we expect to see some light at the end of the tunnel in Q3, and more in Q4," Chambers said. "We have a strong bench of repeat clients that have kept our overall portfolio in good condition. We are looking forward to the day when it is in a great condition."

Chambers is also hopeful that a planned large investment into the country's infrastructure will come to fruition, which will have a positive impact on the construction space for some time to come.

Eileen Wubbe is senior editor of The Secured Lender.