



Transitioning to Working Capital Lending

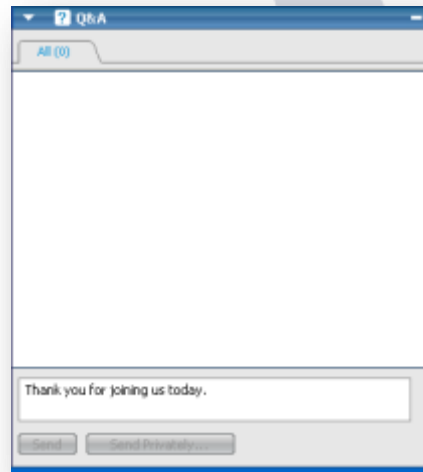
Tips for Making the Pivot from CRE to C&I

October 5, 2011

Housekeeping Details



The event is
being recorded



Use the Q&A
window



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Agenda & Speakers



Todd Williams
Chief Credit Officer
Fidelity Bank



David Stott
VP, Product Marketing
Covarity

- The New Reality – A Look at the Landscape
- Working Capital Lending Overview
- Making the Pivot? What are the Challenges?
- Best Practices
- Covarity Overview
- Q&A

Key Takeaways

1. Market data indicates a decline in CRE and growth in C&I, particularly in some segments
2. There are well-known benefits and challenges to C&I lending for those considering the pivot
3. Consider best practice changes throughout your own pivot



Introducing David Stott

VP, Product Marketing
Covarity

The New Reality – The Headlines

BofA to sell \$880 m
loans: source

Number of U.S. Bank failures in August
cools off following July's
By SA Commercial Prop News 14,000

Recommend

By Iaina Jona
Thu Sep 22, 2011

(Reuters reached
estate l
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Bloomberg

Banks to Sell \$20 Billion of European Real Estate Loans

September 28, 2011, 12:33 PM EDT

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By Simon Packard

(Updates with Royal Bank of Scotland's sale of loans in seventh paragraph.)

Sept. 28 (Bloomberg) -- Banks will sell about 15 billion euros (\$20 billion) of loans secured by commercial property in Europe through 2012 as they anticipate tougher capital regulations, debt adviser Situs Cos. said.

MORE FROM BUSINESSWEEK

RBS, Patron Pay Administrator \$173 Million for 24 Jarvis Hotels

Maybourne Holder McKillen 'Concerned' After Nama Debt Sale

W.P. Carey Acquires 20 Italian Store Fund for \$408 Million

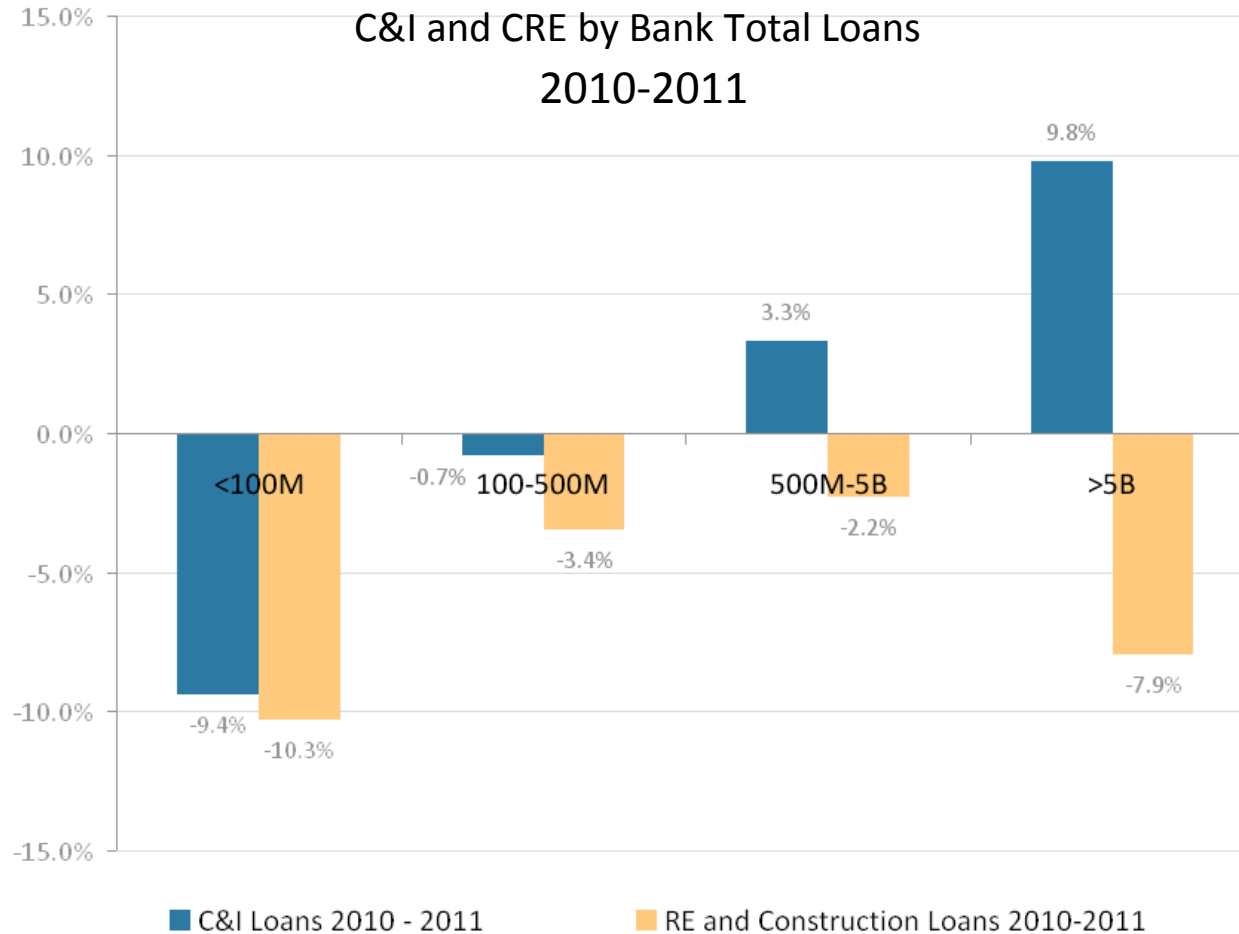
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1st with
\$56 million in
a record

The New Reality – The Facts

Changes in Outstanding Loans

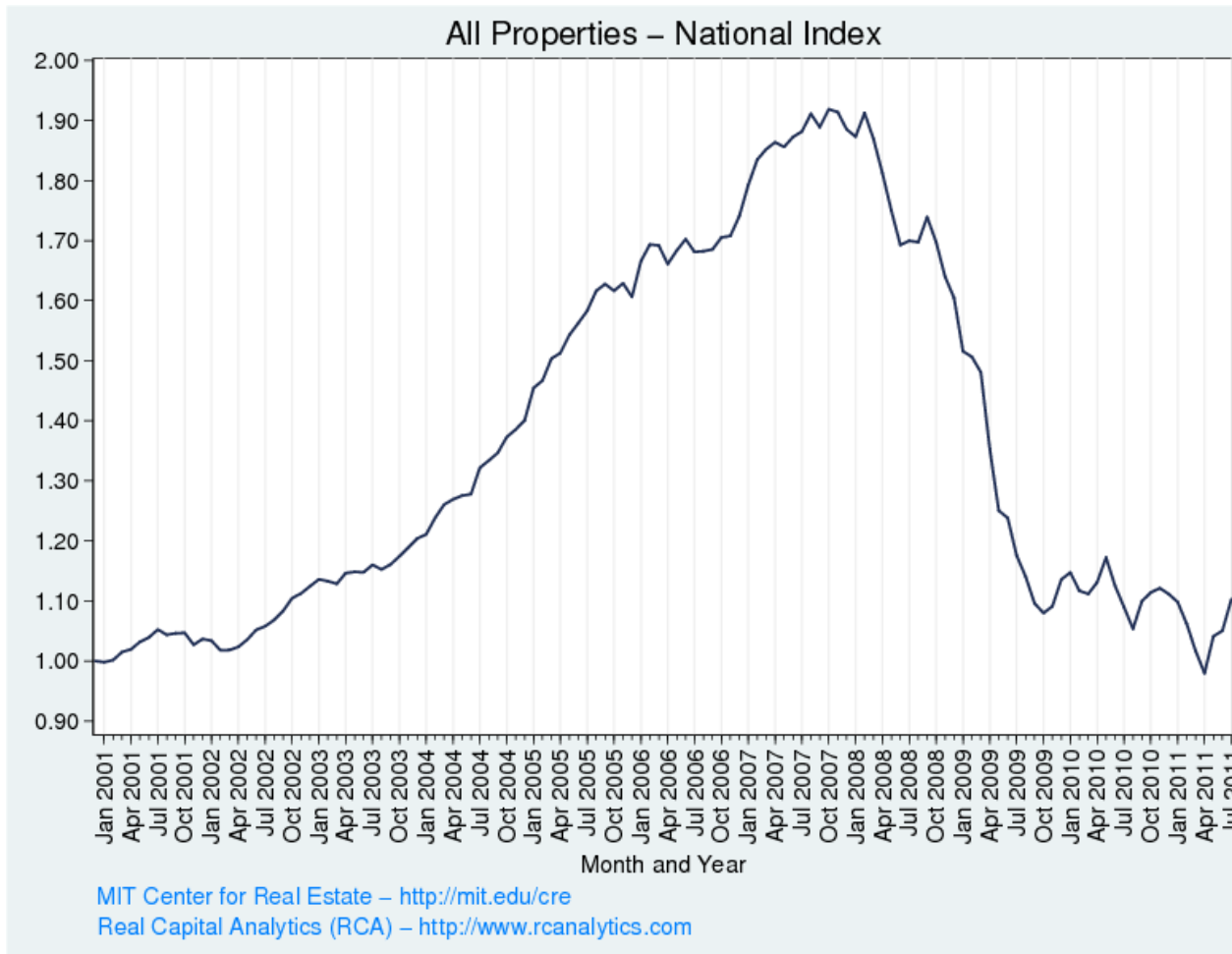
C&I and CRE by Bank Total Loans

2010-2011



Source: FDIC

The New Reality – The Facts



Source: Moodys/REAL Commercial Property Price Index (CPPI)

Poll Question

Where are you with your current portfolio?

1. Comfortably in CRE
2. In CRE, but considering a pivot to Working Capital
3. Currently pivoting
4. Recently pivoted
5. Comfortably offering Working Capital Lending

A close-up photograph of a hand holding a pen, poised to write on a document. The document has a grid pattern and some text, including the word 'X' and 'The following'. The background is blurred, focusing attention on the hand and the pen.

Working Capital Lending Overview

- Not ABL, but a ‘hybrid’ lending product based on financials and pledged collateral
- Offers higher advances of funds against a company’s assets due to a **significantly higher degree of monitoring** of the borrower’s collateral

Working Capital Lending Overview

- Ideal for growing businesses or those in transition
- Less emphasis on ratios and financial covenants – risk profile is more generous due to the collateral security
- Compared to CRE, credits are normally individually smaller

Why Working Capital Lending is Complex

Lender

- Deep understanding of client business needed
- Keeping the borrowing base lending formula current and accurate
- Monitoring can be time intensive
- Burden of collecting and analyzing statements

Borrower

- Due diligence process - very detailed, field analyst costs, appraisal costs
- Collateral reporting - generally more frequent
- Loan documentation

Introducing Todd Williams

Fidelity
BANK

LOBBY HOURS

Monday - Friday
9:00 a.m. to 4:00 p.m.

AUTO BANK HOURS

Monday - Friday Saturday
7:30 a.m. to 6:00 p.m. 9:00 a.m. to 12:00 p.m.

- Senior Vice President and Chief Credit Officer at Fidelity Bank in Edina, MN
- Began his banking career in 1987 following his graduation from the Carlson School of Management

Key Challenges in Making the Pivot



Challenge #1: Changing your Business Acquisition Model



- Common client characteristics i.e. mall A vs. mall B vs. mall C
- Marketing approach includes developer communities, builders and conferences
- More transactional

- Diverse client characteristics across many industries
- Marketing approaches focus on local boards of trade, word of mouth, social media
- More relationship driven

Challenge # 2: Obtaining the Right People and Experience

1. You need a certain combination of characteristics & experience
2. Take inventory of who is on your staff
 - Make changes or pair up for mentoring
3. Must have people who can understand and interpret your client's business – data, business cycles, industry focus etc.



Inquisitive & able to engage a client throughout their working capital cycles



Able to recognize & interpret trends

Challenge #3: Changes to Loan Structuring & Origination Processes

Loan structure is fundamentally different.



CRE



Working Capital Lending

- Based on debt service and cash flow as governed by rent, occupancy rate and lessor quality and maturities

- Borrowing base formula in the loan agreement based on risk profile
- A/R and inventory characteristics are different for each deal
- Look for people capable of managing assets

Challenge #4: Instituting Effective Credit Monitoring Processes, Systems & Tools

Most processes and systems will be affected by your pivot.



- Rent rolls and lessor maturities
- Vacancy rates
- Financial statements
- Cash flow and financial covenants



- More regular borrowing base – aged A/R, A/P, inventory listings
- Financial statements
- Ratios and financial covenants

Challenge #4: Instituting Effective Credit Monitoring Processes, Systems & Tools

- Think through changes to monitoring tools, processes and systems (data management)
 - How will you schedule and track new documents?
 - How will you collect borrowing base information?
 - How will this information be analyzed and reported?
 - How will new exceptions be managed?

BEST

PRACTICE

A close-up portrait of a woman with shoulder-length blonde hair, smiling warmly. She is wearing a dark blue collared shirt under a light-colored blazer. The background is a blurred office or conference room with other people in the distance.

#1 People Pay You Back, Not Their Collateral

- The relationship is paramount
- Your proactive, transparent, partnering approach is what helps you manage risk, not the 80% security on your clients' receivables



#2 You have to Invest the Time to Understand Your Client's Business

- Each client's business evolves over time
- Working capital is not transactional
- Intellectual capital
- Must dedicate time to educate your clients

#3 Active Monitoring is a Critical Discipline



- Regular monitoring means you can better see trends, hold relevant discussions and reduce risk
- Analyzing borrowing base and financial statements frequently will enable you to have relevant conversations – eliminating surprises from the processes
 - Required systems, people and processes to read, analyze and interpret results
- If borrower doesn't like this process, it's not a good sign

Introducing Covarity

- Covarity measurably improves its clients' **Commercial Loan Portfolio** health and performance through the breadth of our loan **monitoring** and **analysis** capabilities:



Operational Efficiencies:
Accuracy, Consistency & Savings



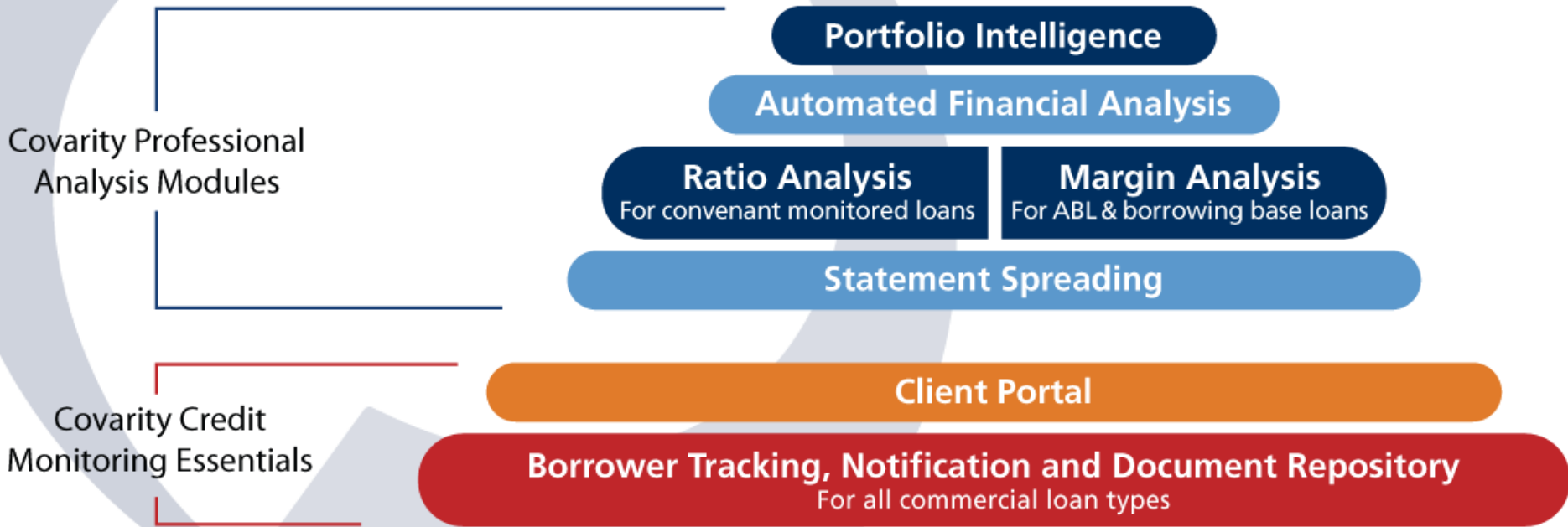
Portfolio Insight:
Reduced Loan Losses



Improved Borrower Relationships:
Value-Added Service

- **Customers include:** RBC Financial Group, BMO Financial Group, Fidelity Bank, Libro Financial, Crestmark Bank

The Covarity Solution



Key Takeaways



1. Market data indicates a decline in CRE and growth in C&I, particularly in some segments
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3. Consider best practice changes throughout your own pivot

The logo for Covarity, featuring the word "COVARIETY" in a bold, white, sans-serif font. The letter "O" is stylized as a blue circle with a white arrow pointing clockwise, suggesting a cycle or process.

COVARIETY

Thank You

Q&A

Additional comments or questions can be
emailed to info@covarity.com