STEPPING UP

An increasingly diverse finance landscape has given rise to asset-based lenders, many of which are capturing opportunities posed by the economic downturn. Fiona Haran reports

In the face of inflationary pressures and the rising cost of borrowing, many small to medium-sized enterprises (SMEs) are starting to consider how they can leverage the assets within their business.

"An asset-based lending (ABL) finance package is often ideal for when business owners are looking to fund growth ambitions, free up capital to buy or sell businesses or purchase equipment, but need fast decision-making processes and manageable, affordable repayments," says David McIntyre, corporate manager at Bibby Financial Services. "This type of funding can be especially valuable in situations when a clearing bank might find it difficult to provide the correct solution."

This has opened several doors for players in the alternative lending space, including Leeds-based Reward Finance Group. Managing director for Yorkshire and the North East, Gemma Wright, says: "Any time there's uncertainty in the market, the mainstream lenders increase their level of caution. They are still lending but are taking longer to do it or have changed stance on sectors, for example.

"Equally, there's been tightening on pricing and we've seen the base rate move as well, which means that SMEs are looking at a broader market."

The latest research from UK Finance shows that total invoice finance (IF) and ABL advances increased by £1.7bn (8.7 per cent) between the quarter ended March 2022 (£19bn) and June 2022 (£20.7bn) – the eighth consecutive quarter-on-quarter growth in total IF/ABL advances since June 2020. Client numbers in retail, manufacturing, construction and transport have increased.

The primary appeal of ABL is flexibility. Ben Milner, regional business development director at the Leeds office of specialist asset-based lender BREAL Zeta CF, says: "ABL is traditionally counter-cyclical with the economy because when there's a downturn, the flexibility to take a view on financial performance and be able to leverage the assets on the balance sheet means that more businesses use it. ABL gives management teams comfort that if something comes out of the blue or trading performance isn't as strong because there's another unforeseen event, like the Covid-19 lockdowns, they know they've got more headroom in their borrowing facility than they might have with a non-ABL facility."

Gemma Wright

> "If your revenue and working capital assets increase, you can borrow more."
> **Ben Milner**
> Breal Zeta CF

Measuring performance

To make an ABL finance offer, lenders take a "whole myriad" of considerations into account, says McIntyre. "In addition to asset value, the typical lending criteria will focus on the people in the business, their background and their experience, the sector in which they operate, who their buyers and suppliers are and their financial performance, now and in the future."

The nature of ABL means that funders tend to be sector-agnostic. Wright says: "Every SME has different circumstances, so even what's perceived to be a challenging sector still has good businesses and individuals operating within it.

"This is the case for a lot of people in the alternative lending space. It allows us to do more common-sense lending because we're sitting in front of people and talking to them. It's not a 'computer says yes or no' decision, so we've not shied away from any sectors and we've seen some good opportunities."

This has driven ABL's transition from a historically perceived 'last resort' solution to a first port of call for many businesses, says Wright. "While traditionally it was the working capital solution, it's now leveraging from invoice finance, plant and machinery and property to allow people to acquire businesses.

"As a result, people have more experience of using it, which improves the product image," she adds. "It makes private equity houses and corporate finance advisers realise that ABL could be a first-choice solution for some of their transactions."

BREAL Zeta's arrangements often have private equity involvement. Milner says: "Our minimum facilities start at £5m and go up to £200m-£250m-plus. The clients in our portfolio are predominantly private equity-backed and also privately owned businesses. They're typically going through a transformational period, so it might be a management buyout or they're funding growth or executing a turnaround plan.

Weighing up costs

The specialist nature of ABL means that higher loan rates are to be expected compared with mainstream lenders. Wright says: "The alternative lending market has to be able to borrow itself to be able to pass on the funds. We don't have our own cash to lend out, so that comes at a premium. But increasingly, ABL is being used by people to take advantage of opportunities, whether it's an acquisition, property purchase or move into a new market."

Additionally, Milner says that potential borrowers should be aware that ABL may result in a reduction in cash availability if their working capital assets (such as receivables and inventory) are reduced.

"Compared with a property or plant and machinery, those assets move on a daily basis. As a result, the availability of funds moves in tandem," he says. "That can be hugely positive because if your revenue and working capital assets increase, you can borrow more, but conversely, it can go the other way. So you need to forecast for it."

Tech adoption

The growing use of technology is also reshaping the ABL space, with the ability to embrace change and incorporate new platforms said to be critical to enhancing the lending process. The most progressive companies are adopting technology such as software-as-a-service (SaaS) in the cloud, data analytics, artificial intelligence (AI) and open finance platforms.

Wright has seen an increase in providers adopting new technology. She says: "Historically, ABL was perceived as quite cumbersome with a lot of admin, whereas cloud-based solutions and open banking have changed that perception.

"Smaller providers have turned to fintech to speed things up and the big players have automated a lot of the process removing the admin burden. It enhances the relationship with the client rather than replacing it."

'HAVE COURAGE IN YOUR CONVICTIONS'

Leeds-based Procurement Supplies received an ABL package of £250,000 from Reward Finance. The company provides a complete design, manufacture and 'stock and serve' service for environmentally responsible transit packaging materials.

Owners Paul and Stella Sykes leveraged the loan against their own residential property. Paul tells *Insider*: "We started the business in the middle of the pandemic. Unfortunately, two previous lenders weren't appropriate for our business model. We required a significant amount of cash to fund stock purchases to raise our sales.

"Having looked at various options, there was a serious conversation about whether we were prepared to risk putting our residential property up as security," he continues. "Both my wife and I decided it was worth the risk. It unlocks significantly more working capital for our business than we could have ever imagined compared with traditional lending methods."

(From left): Stella and Paul Sykes with Simon Micklethwaite at Reward Finance and Mark Storey at BHP

The couple was introduced to Reward Finance by their accountant BHP. Paul says: "We supplied them with the proprietary information on background and forecasts.

"The onus is on you as a director of your own business to make a calculated and measured decision about whether you've got sufficient courage in your convictions to risk an asset," he continues. "Because we crunched all our numbers very thoroughly in conjunction with our accountants, we understood where the growth was going to come from. I knew that as long as I could make the sales happen, which we are well underway with already, that the success would follow."

The couple were pleased with the application process. Paul says: "We found the people at Reward easy to work with and approachable. It made the whole process much smoother."

The funding has helped the business procure more stock to raise sales, says Paul, who adds that he would definitely consider further asset financing in future. "It gives you options. That's not to say that you should enter into a funding model such as this lightly, because you absolutely shouldn't. You've got to go into it with your eyes fully open and thoroughly understand your business model to give it the best opportunity for success."

Eleven months into the ABL process, Paul says the company's trajectory is in line with expectations. "We consider our relationship with Reward a stepping stone for the growth of our business. When we started with Reward, everybody was still preoccupied with Covid, but here we are now 12 months on and our business is flourishing."