Information and Insight for the ARM Industry July 2012

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Obtaining Attractive Debt Capital for ARM Firms

Debt capital financing is a vital component for all types of ARM firms, including debt purchasers and debt servicers, in order to fund portfolio and asset purchases, working capital, expansion, and acquisitions, among other things. The availability, requirements, and preferences for banks and lenders continue to change. Below, we offer insight about the current environment for raising debt capital, as well as the key factors that help determine a lender's "Go/No-go" decision regarding a funding request.

For Asset Acquirers / Debt Purchasers

Many large financial institutions have pulled back from providing financing for debt purchasers, as some were burned by overly aggressive lending during the last several years.

What many debt buyers are not aware of, however, is that there are a wide variety of specialty lenders and banks that are interested in the ARM industry. These groups are well-versed in lending based upon the characteristics and collateral profile of ARM firms. They seek ARM opportunities from $1 million to $20 million, and they offer attractive terms in today's market. Perhaps best of all, these groups generally do not seek costly back-end profit sharing. However, most of them are not known to industry participants.

Many of the well-known "industry lenders", as well as some European and U.S.-based hedge funds, have played a significant role filling the gap left by the large financial institutions, but often demand profit sharing arrangements, as well as more stringent covenants and reporting requirements.

Regardless of the type of lender, critical factors that they assess for debt purchasers include sourcing pipelines, analytics and underwriting, technology and compliance infrastructure, licensing, asset class, collateral, long-term performance and liquidity history, servicing model (e.g. in-house vs. outsource), credit history, and equity contributions for new purchases. The better a firm scores in these and other important areas, based upon lender preferences, the more likely that financing will be approved and favorable terms will be obtained.

For Debt Servicers / Collection Agencies

The sustainability of EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization), or similar cash flow metrics, is a focus of lenders while reviewing service companies, as it is a good proxy for the free cash flow which is available to pay back the loan.

Lenders tend to be more conservative than in the past, and utilize structures involving senior debt, and in cases where more debt is required, may also provide subordinated or mezzanine capital. Preferential terms and leverage amounts may be given to more financially stable, larger, and/or institutionally-backed firms. As well, companies with long-term contracts, long-term client relationships and consistent financial performance are generally seen as better credit risks.

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Obtaining Attractive Debt Capital for ARM Firms (cont.)

For example, companies servicing the U.S. Department of Education student loan collection contract have the rare security of a multiyear placement and income stream, and thus lenders are interested in funding existing vendors, as well as new vendors who will incur significant ramp-up costs before they even begin working on this contract. This is but one example. Lenders will fund ARM firms with clients in most any segment as long as they can conservatively project repayment of the debt.

Lenders also view compliance and data security as critical areas for assessment in the underwriting process. This is important from the standpoint of limiting a lender's downside risk in case of a breach, but also because larger firms are often better equipped to handle additional compliance costs.

Make Informed Decisions

Debt capital financing for ARM firms is most certainly available today, however finding the best terms for your particular circumstances often requires expertise and relationships that go beyond a local bank.

Greenberg Advisors is skilled at helping clients explore their options and secure the best terms from among the many dozens of lenders interested in the industry. Our capital raising process includes those who participate in industry conferences, but also includes a broader set of lenders which seek investments in the ARM and related Specialty Finance sectors, and which may provide considerably more attractive capital. Please contact us to discuss your capital needs, and we'd be happy to provide you with our feedback.

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