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MID-STATES ADVISORS
A Private Placement and Business Brokerage Firm
Newsletter

Mid-States Advisors, Inc.
Monthly Article & Updates

Good Morning,

Election day has passed and as usual, it appears that businesses, lenders, M&A professionals and the stock market are open for business. The typical quiet in the month or two preceding the election has now passed and we expect to see lots of activity. This should be buoyed by the announcement that Pfizer's vaccine is proving to be 90% effective.

Whether you are a Biden fan or still waiting to see how the Trump lawsuits fall out, business leaders around the world seem to be confident that the incoming administration will be more predictable. This should provide a calming effect after what is proving to be one of the most polarized elections in recent memory.

This week our content is focused on some of the lingering effects of Covid-19, specifically how to interact with bank workout groups and what you can expect. Every situation is different but this article is meant to provide general understanding to anyone who may be going through the bank workout process or expects it may be inevitable in the near future.

As always, if you are interested in learning more about this week's content or if we can help you or a client in any way please feel free to reach out to one of our team members.

Best Regards,
The Mid-States Team

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LESSONS LEARNED SHOULD NOT BE FORGOTTEN!

After almost 10 years of relative prosperity, many are forgetting the lessons learned during the “Great Recession” which arguably began in 2007 and lasted until sometime in 2010, in how to deal with a lender’s Special Assets, Managed Assets, or Workout Group. We had a recent experience in which our client and his professional advisers did not give proper consideration to the fact that a secured lender with a properly documented loan is the “800-pound Gorilla” in the room.

It is important to understand that a loan sent to workout is one that the lender no longer wants. As such, the borrower will rarely be treated as a customer, but rather as a problem. Workout specialists are often experienced lenders with a difficult job to do - recover as much of the banks money as they can. They are prepared to take losses, in fact normally a loan sent to these groups has already been either written off, or reserved, i.e. valued by the bank at less than the amount due. These people are usually highly skilled, and familiar with State and Federal insolvency laws. They know how to use the tools that “motivate” the borrower to leave their institution. Obviously, they are familiar with the loan documents, which are usually drafted solely for the benefit of the bank, leaving the customer at a distinct disadvantage.

What should be your first priority after notification that your loan is in Workout? Build a winning team!

Perhaps the most important advisor is an experienced Insolvency Lawyer. Unless your current attorney is highly experienced in this area of the law, retain someone who deals with these problems as part of his or her everyday job. Choosing the right person often makes the difference between survival and liquidation.

Next, supplement your attorney with a Financial Advisor who is familiar with the workout process. Hire your own before the bank chooses one for you. Your accounting staff will be burdened by numerous demands for information, far more than they have had in the past. The number of field audits will increase, building, equipment and perhaps even inventory appraisals will be updated on a regular basis, advance rates may be reduced, or a cap put on the amount of money that can be borrowed, if at all. The lender may do a Liquidation Analysis, which can be unnerving to business owners. Cash planning becomes paramount, and management tools must be formatted in the way that workout specialists are used to seeing the information. In the workout process CASH is king. Do whatever you can to conserve and maximize cash and cash flow. Forget long range planning. Focus on generating and conserving cash.

The cost of doing business will increase, sometimes dramatically. Attorney specialists, both yours and the banks, Financial Advisors, valuation experts, and the costs imposed by the lenders all eat into cash (and profit). The bank usually imposes a default rate of interest which is dramatically higher than your previous interest rate. Additionally, as you proceed through a series of forbearance agreements, there are fees imposed by the lender. Not much fun, but all part of the process.

Even though the lender’s workout specialists have a very different goal from that of the business owner, information supplied should be accurate and timely. With the degree of oversight exercised by the lender, a borrower would be foolish to misrepresent the condition of the business. While cash is king and the borrower needs to conserve it and maximize cash flow in the immediate term, the bank will want to see a long-term solution. The near-term needs can be managed using a 13 week cash flow analysis. Once the borrower and the lender get comfortable with the ability to sustain operations within that analysis, a longer-term focus and financial plan is important. This is true for both the existing bank and any potential refinancing prospects.

Management should be using this same information as a tool in their decision making. Remember the reason the company is in the workout department is because the bank concluded that it might not be able to meet its obligations and repay their loan. Everything you present to them, should point to a different conclusion. You want to control making decisions in the company's best interest, which should show the bank that you are striving to manage cash, return to profitability and that the business has competent decision makers on its management team.

Increasingly, commercial lenders are reviewing the customers in their own workout department for loan prospects. Be aware that you will have to go through an approval process as though you were not a current customer of the bank. Feelings often get bruised in dealing with the specialists, who can be single minded in their efforts to get the current loan off the books. As a result, most clients prefer to move on and find a new lender.

The Financial Advisor you hire must know how to present your business to a potential lender in a way that presents it as an attractive customer. Further he or she must know the lenders and institutions that are interested in funding businesses coming out of a workout department.

Hopefully, management can and will take the steps to restore profitability on a sustainable basis, and a new lender will bring this process to a close. How they do that is an article for a future Newsletter.

Obviously, this short article only hits the high points of the workout process. Feel free to call us if you want to discuss a specific situation or if you simply want additional information.

If you would like to discuss our services in more detail, please contact us to learn more about how we can assist your company or client. Below are the direct phone numbers and emails for a Mid-States team member who can answer your questions (yes, we answer our own phones):

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See our team at Midstates Advisors' website