A PRIMER ON NON-BANK LENDING

A PRESENTATION FOR MBDA

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The Market we are Discussing Today ….

	Small Balance Commercial	Larger Balance Commercial Lending	Commercial Real Estate
Market Description	Businesses seeking credit for working capital, liquidity, equipment or expansion in amounts less than $500K	Businesses seeking credit for working capital, liquidity, equipment or expansion in amounts of $500K or more	Businesses seeking capital for real estate purchase or refinance in any amount

The Non-Bank Small Balance Commercial Lending Industry

- **Highly diverse universe of businesses** in the United States - ~1,100 classifications of businesses according to the North American Industry Classification System (NAICS) resulting in substantial differences in:
  - Cyclicality (exposure to the boom and bust of economic cycle)
  - Growth prospects
  - Profitability / profit margins
  - Capital intensity (machinery, inventory, etc.)
  - Regulatory influence

- Resulting, in **highly diverse needs for capital**
  - "Working capital" / manage uneven cash flow
  - Accounts receivable financing (liquidity)
  - Inventory financing
  - Investments for capital improvements or expansion
  - Equipment finance
  - Real estate finance

- Resulting, in a **highly diverse ecosystem of products and business models** serving the debt capital needs of the business community

The Market for SMBs Seeking Credit for Working Capital and Expansion

Large Ticket ($250k - $500k)

Annual Origination Potential
$64B

~10% of market demand unmet by banks

Mid Ticket ($100k - $250k)

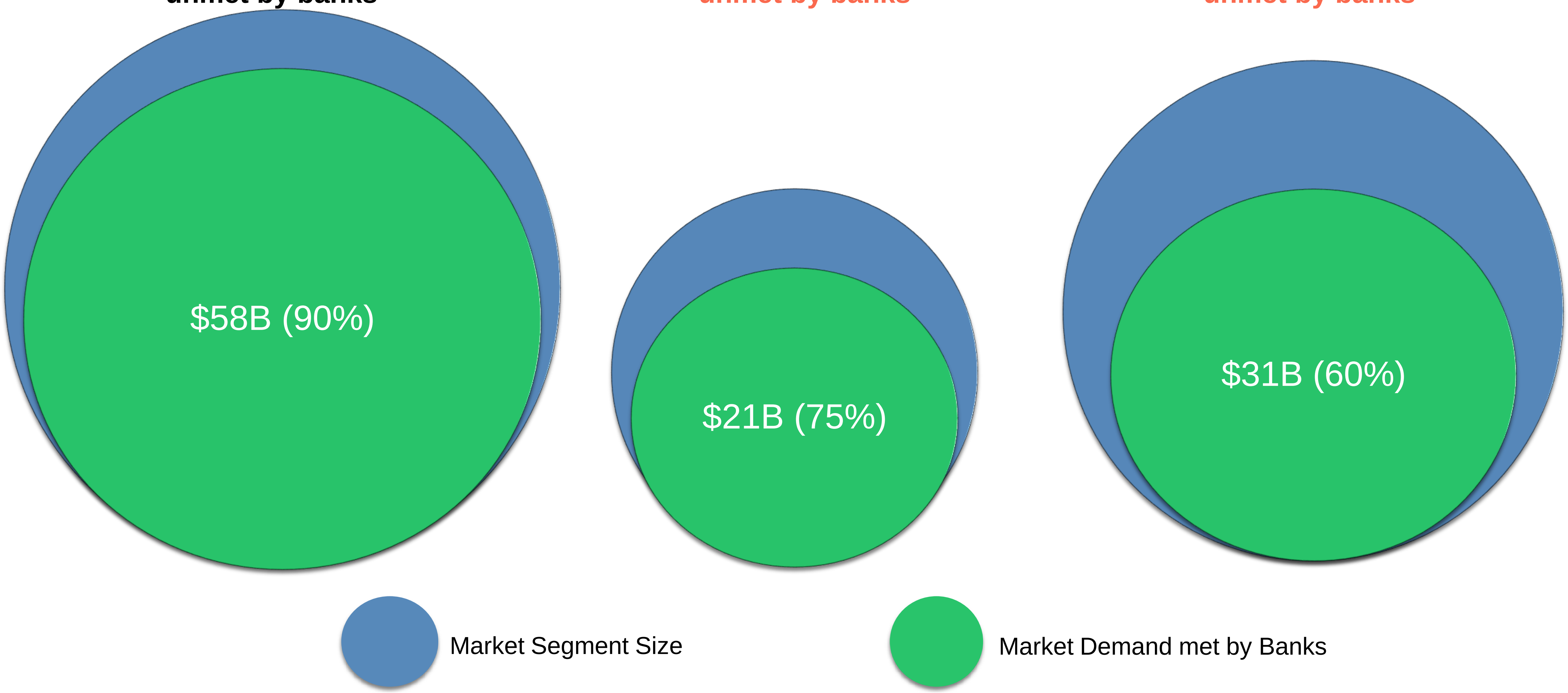
Annual Origination Potential
$28B

~25% of market demand unmet by banks

Small Ticket (less than $100k)

Annual Origination Potential
$52B

~40% of market demand unmet by banks



The small ticket segment has the largest 'credit gap' of demand not met by banks

Figures are estimates based on the Federal Reserve's most recent joint study on SMB finance

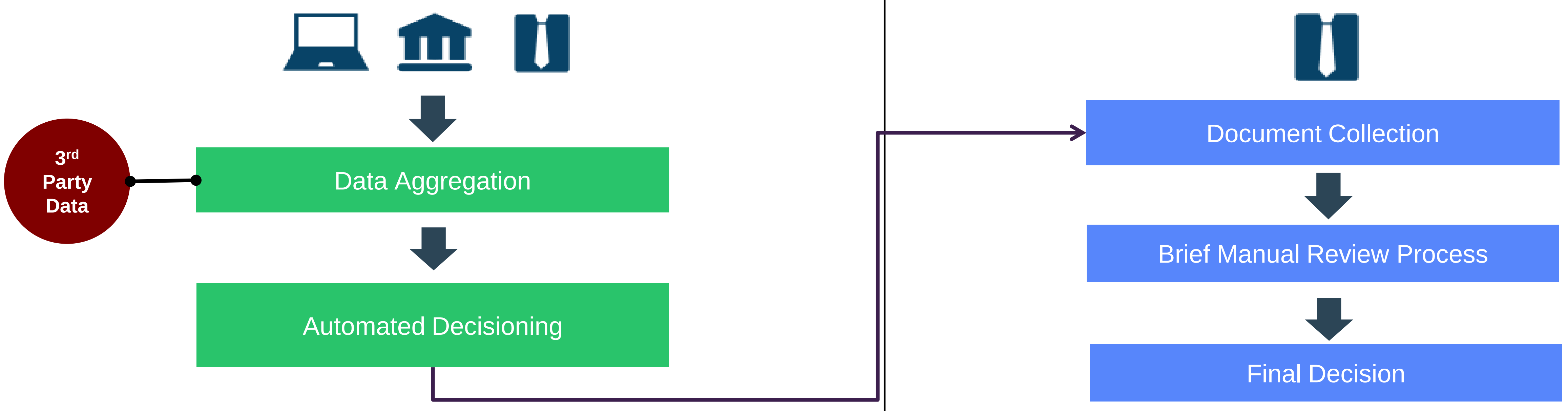
Putting Business Lending in Perspective

	SMB Balance Commercial	Larger Commercial	Commercial Real Estate
General Deficiency of Collateral	✓		
Extremely Heterogeneous Customer Population	✓	✓	✓
Relatively High Volatility of Loan Performance Across Economic Cycles	✓		
Most Predictive Third Party Data is Still in a Maturation Stage (e.g., Commercial Payment Data)	✓		
‘Thin File’ Customers (lack of availability of audited financial statements, budgets, business plans)	✓		
Manual Underwriting is Cost Inefficient Relative to Revenue Potential on Lending	✓		

These challenges are most acute for transactions less than $250K

Technology is Making Small Balance Lending More Efficient

AUTOMATION | **MANUAL (when necessary)**



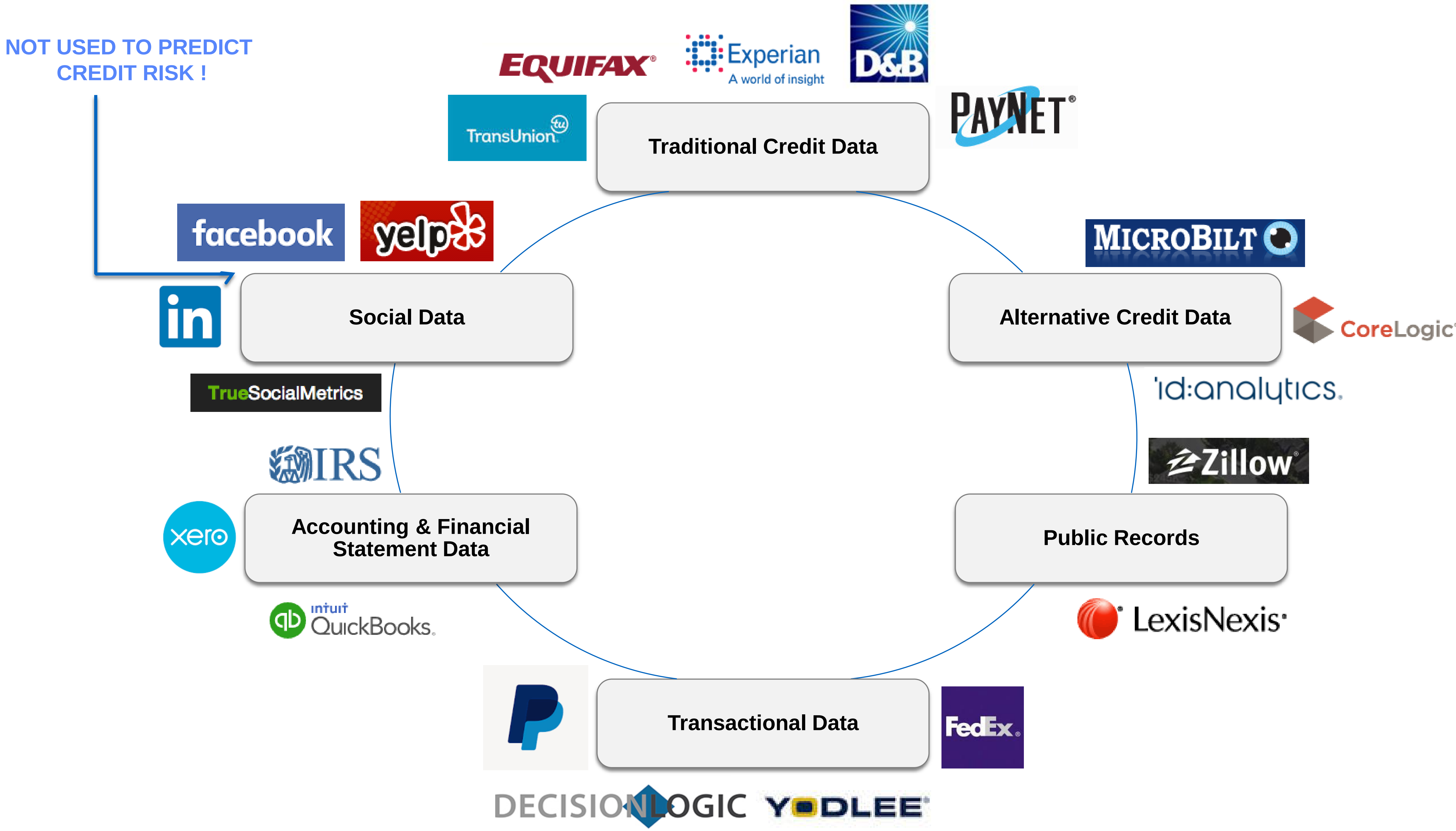
AUTOMATION

- Personal credit history
- Business credit history
- Personal and business related public records
- Business verification and fraud related data
- Industry performance related data
- Quantifies / scores risk using proprietary algorithms
- Some automated systems deliver offers in real time

MANUAL (when necessary)

- Verification of information
- Review of key risk factors found during automated process
- Depending on the company or size of the loan requests, a cash flow analysis may be performed

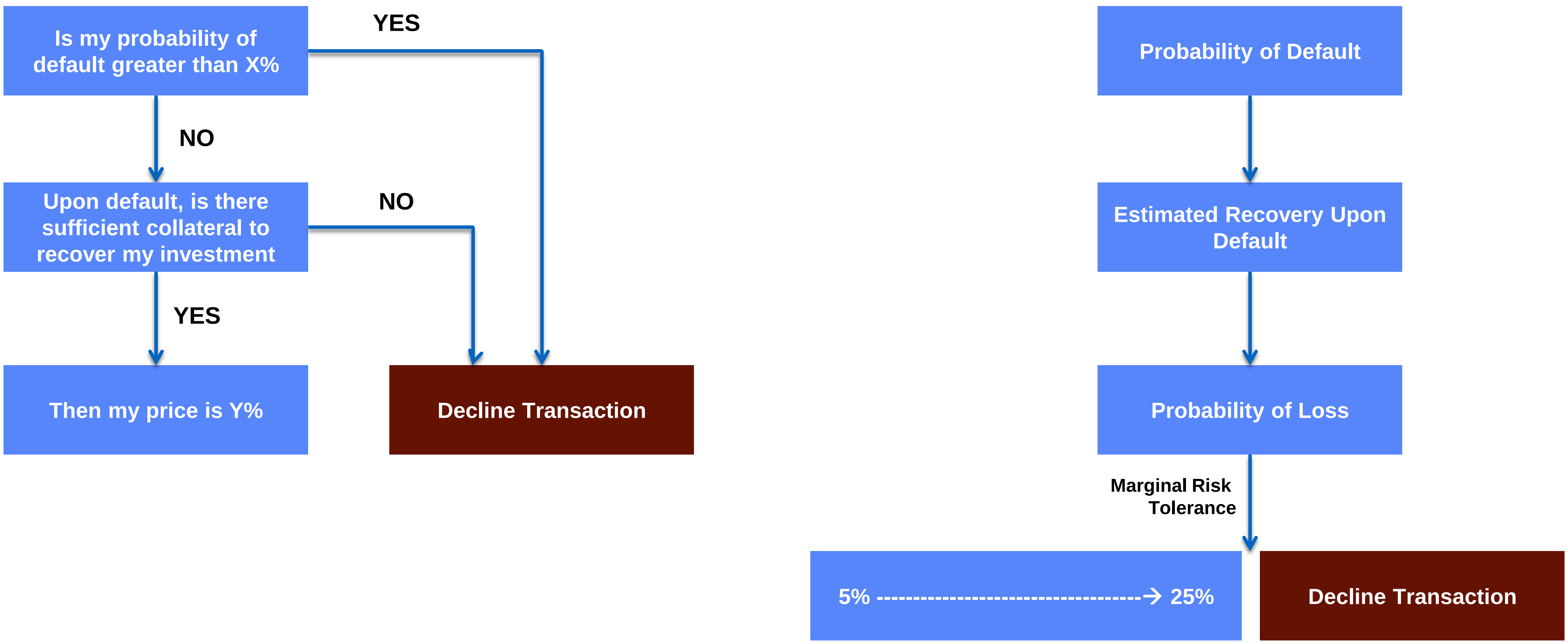
Data Aggregation – Capturing Data Available on You and Your Business



THERE IS A LOT OF DATA OUT THERE BUT NOT ALL OF IT IS USEFUL !

How Does a Non-Bank Lender Decide to Lend?

“*Risk* Based Pricing” (Banks)	Risk Based Pricing (Non-Bank Lenders)



**NON-BANK LENDERS HAVE DIFFERENT RISK TOLERANCE THAN BANKS DO ……
BUT THEY PRICE FOR RISK**

Business Models

Sourcing Customers	Underwriting & Risk Management	Servicing & Collections	Capital	Who
AGGREGATOR				lendio fundera BoeFly lendingtree
"MARKETPLACE LENDERS"	"MARKETPLACE LENDERS"	"MARKETPLACE LENDERS"		Funding Circle LendingClub BOND STREET OnDeck Dealstruck
DIRECT LENDERS AND CASH ADVANCE COMPANIES	DIRECT LENDERS AND CASH ADVANCE COMPANIES	DIRECT LENDERS AND CASH ADVANCE COMPANIES	DIRECT LENDERS AND CASH ADVANCE COMPANIES	CAN SWIFT CAPITAL Kabbage STRATEGIC FUNDING DIRECTCAPITAL
	"CREDIT SOLUTIONS PROVIDER"	"CREDIT SOLUTIONS PROVIDER"	"CREDIT SOLUTIONS PROVIDER"	FUNDATION WWW.FUNDATION.COM

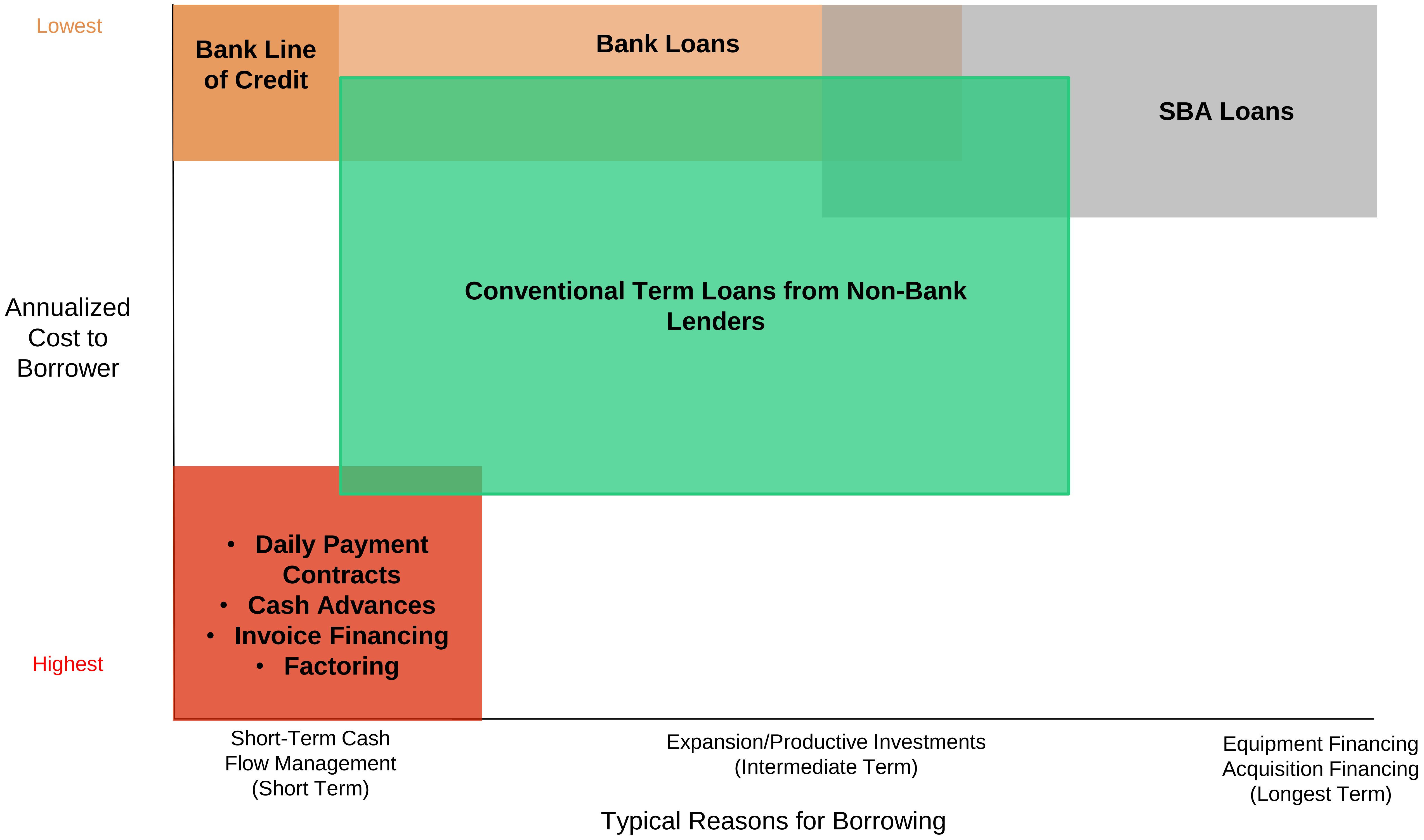
Hybrid Models
(Aggregators that also Deploy a Balance Sheet)

bizfi
BUSINESS FINANCING
Biz2Credit
THE BUSINESS BACKER

Simplifying the Business Models

	Agents or Intermediaries	Principals
Description	Provide advice or other services to businesses seeking capital, generally including preparing their applications and obtaining offers from lenders (Principals)	Businesses seeking capital for <u>real estate purchase or refinance</u> in any amount
Economic Model	Receives a transaction fee (commission) from the lender (and, in some cases, the borrower) for rendering these services	Earns interest, fees and other income from investing its own capital in a loan (or other form of credit)

Product Landscape



Product Vocabulary

Cost Measurement and Fees

- 'Cents on the Dollar' – A fixed amount of money to be paid back on every dollar borrowed
- Factor Rate (aka: Total Payback) – A quote on the total cost of a loan (ex: 1.30) – Multiplying the factor rate by the amount borrowed will give you the total amount a borrower must pay back
- Total Interest Percentage (aka: Simple Interest) – the total amount of interest paid as a % of the principal balance of t he loan
- Annual Percentage Rate – The amount of interest charged depicted as an annualized rate that is inclusive of all fees
- Prepayment Fee – A fee charged to a customer when a loan is paid off in full or partially before its maturation date

Types of Contracts

- Conventional Term Loan – Fully amortizing loan with fixed payments comprised of principal and interest
- Line of Credit – A specific amount of credit a borrower is given access to that can be used at its discretion – the most common types are "revolving lines of credit" and "term lines of credit"
- Merchant Cash Advance – An advancement of capital against a business's credit card receivables and collected by taking a fixed percentage of daily credit card transactions – loan costs are typically quoted as a Factor Rate or Total Interest Percentage. These products are technically not a loan.
- Fixed Repayment Loan – A loan agreement that requires a fixed payment amount typically with daily or weekly paym ent terms and loan costs quoted using a factor rate or Total Interest Percentage

Products in the Market

	MERCHANT CASH ADVANCE	FIXED REPAYMENT LOANS	CONVENTIONAL TERM LOANS	LINES OF CREDIT
Loan Amounts	~$5,000 - $150,000+	~$5,000 - $500,000	~$10,000 - $1,000,000	~$10,000 - $150,000+
Terms	3 – 18 month	3 – 24 months	1 – 5 years	N/A
“Type of Interest Charged”	Factor Rate	Factor Rate / AIR	APR	APR
APRs	~40% +	~30% +	5% - 30%	5% - 30%
Payment Frequency	Daily	Daily or Weekly	Twice Monthly or Monthly	Monthly
Security	All Asset Lien + PG (Lender Dependent)	All Asset Lien + PG (Lender Dependent)	All Asset Lien + PG (Lender Dependent)	All Asset Lien + PG (Lender Dependent)
Approval And Funding Timeline	~24 – 48 Hours	~24 – 48 Hours	~24 – 48 Hours (Some lenders take 7 days +)	~24 – 48 Hours

Things That Sound Alike are Actually VERY Different …..

	MERCHANT CASH ADVANCE AND PAYMENT CONTRACT LOANS	CONVENTIONAL TERM LOAN
Loan Amount	$100,000	$100,000
Repayment	1 Year	1 Year
Interest Rate	**$1.20 on the $1.00 Quoted as 20% "interest"**	**20%**
Total Interest Over Life of the Loan	$20,000 20% of the original loan balance	$10,745*
Total Payments if Paid Through Maturity	$120,000	$110,745**
Total Payments if Paid Back the Next Day	$120,000	$100,056
Effective Annual Percentage Rate if paid through maturity	**~45%**	**20%**

* Based on semi-monthly payments instead of one payment per month. 1 payment per month would result in $11,161 total interest over the life of the loan

** Based on semi-monthly payments. One payment per month would result in $111,161 total payments if paid through maturity

Practices to Be Aware of

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- "Stacking" – when lenders (often merchant cash advance companies) will seek out businesses that recently took on debt, pressuring the borrower to take on more debt, often at a higher cost over a shorter period of time putting borrower's in a challenging economic condition

- "Wholesaling" – a practice where brokers will obtain a financing rate from a lender and then seek to 'mark-up' the price (cost) of the loan to the borrower

- "Double Dipping" – for contracts that have a <u>fixed repayment</u>, some lenders will proactively influence borrowers to refinance early, allowing the lender to accelerate their income and thereby capture more income over a shorter period of time

<u>Our advice</u>

- Read a contract before executing and make sure you understand all terms

- Ask your Agent or Principal about
  - All costs in the contract
  - The costs of early prepayment
  - Your financing rate expressed as a % of the original balance and on an annualized basis

Conclusions

- The non-bank lending market is incredibly diverse because the businesses that need capital are diverse, as are their needs for capital

- There are a lot of different types of businesses that can facilitate your needs for capital – some serve as agents or intermediaries, and other lend directly

- Be prepared for the application process with the documents you may need to provide and a good explanation of why you are seeking funds

- Don't be discouraged if you are not successful with the first firm you work with. There are a lot of options out there

- There are a lot of very ethical companies in the non-bank commercial lending market but, like in any market, there ar e some bad actors – protect yourself by asking the right questions and understanding the financing arrangement yo u may enter