

***Debt & Equity-Financing The Deal:
Considerations & Trends***

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IronHorse is a K.C. based special situation professional services firm with practice specialties in business valuation & appraisal, forensic services & litigation support, CFO services, due diligence, and complex financial & operations restructuring/turnaround consulting.

Tony is an Adjunct Professor of Accounting at Johnson Community College in Overland Park, KS and Rockhurst University in K.C. and serves on the Small Business Reorganization Committee as well as the Fraud Task Force with the American Institute of Bankruptcy.

IronHorse has performed numerous due diligence, valuation, litigation support and restructuring engagements for clients in a variety of industries. Tony has extensive M & A experience on dozens of transactions, especially with financially distressed enterprises.



Size Matters

- Easier to fund a \$ 15 million deal than a \$ 2 million deal.
- Private equity sources generally want to put at least \$ 5-8 million of their money to work.
- Universe of small capital providers is specialized, scattered and expensive.
- Costs about the same in terms of time to search, solicit, secure \$ 500,000 as it does \$ 5 million



Factors

- Quality of earnings
- Volatility
- Quality of collateral available
- Assessment of senior executive and management capability
- Demonstrated capability to service debt
- Degree of operating and financial leverage, liquidity and solvency
- Financial and internal operating control environment
- Conditions in capital markets
- Availability of guarantees, other assets to be pledged
- Valuation multiple trends.
- Commercial lending source; bank vs alternative capital provider.



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Changing Environment

- Loan to value limitations
- Covenants
- Access availability requirements (Collateral cushion)
- Stretch-pieces (over-advance)
- Balloons
- Subordinated soft notes
- Carry-backs
- Earn-outs
- Sub-debt
- Bank vs ABL : regulatory environment



Deal Trends

- (M&A) activity has accelerated meaningfully in the U.S. That trend is poised to continue, if not accelerate.
- Cash is flush
- Deal multiples climbing
- More leverage
- More creative leverage
- Covenant-light debt
- Stretch pieces & airballs
- Haircuts
- Hedge fund & other debt buyers
- Junior lien alternatives



Capital Structure Considerations

- Required rates of return & cost of funding
- Commercial collateralized debt
- Bonds
- Subordinated & convertible debt
- Preferred equity
- Common equity
- Eligible assets to pledge
- Guarantees



Typical Loan Covenants

- Debt service coverage ratio
- LTV limits
- Inventory collateral limits
- Ineligibles
- Equipment advance rates
- Real estate advance rates
- Borrowing base
- Leverage ratio
- Tangible net worth



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SBA Financing

- Small deals
- Tough/cumbersome to source & place
- Time consuming
- Advantages
- Alternatives:
 - Second tier ABL's
 - Conventional C and I debt with guarantees
 - Friends & family
 - Angel funding



Asset-based

- Bank sources
- Commercial finance companies
- Tiered providers based on size
- Pricing/costs
- Quasi factors
- Factors
- One-off sources
- P.O. financing



Subordinated (Mezzanine) Debt

- Usually unsecured
- Warrants
- Convertability
- SBIC's
- Costs
- Coupon
- PIC feature
- Fees
- Success fee



Equity

- Friends & family
- Angel funds
- Individual angels
- Private equity sponsor groups
- Control
- Size & critical mass matter
- Success rates in placing
- How to improve the odds



Special Situation Deals

- Debt buyers
- Turnaround sources
- Bridge capital
- Haircuts
- Subordinated soft notes
- Lender as equity player
- Carry-back financing
- Cleansing; article nine, going concern sales in receivership, section 363 deals, foreclosures