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# trekking

a newsletter on practical strategic thinking and action  
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## who's got money?

Before my time as a Principal of Trek Consulting, I spent seventeen years of my career as a commercial lender, and in that time I went through my share of lending crises. Just as we were learning about inflation-based accounting in the U.S. at Bank of Boston in the early '80's (the birth of FIFO and LIFO valuations?), I was transferred to Buenos Aires, Argentina with the same bank and learned how to make local currency loans in a triple-digit inflation environment and with wild fluctuations in foreign exchange rates.

Today's lending environment in the U.S. isn't quite that bad, but it also bears no resemblance to that of a couple years ago. If businesses can find loans from banks these days, the loan rate and fees are higher. The covenants and advance rates are also tighter, a far cry from the "covenant-light" loans that were made in 2005 and 2006.

The capital injections by the Bush and Obama administrations have averted a total meltdown of the U.S. banking system, but have created some "zombie" banks by deferring their inevitable insolvency (liabilities exceeding assets, exacerbated by declining asset values - <http://online.wsj.com/article/SB123560389732776681.html>). The injected capital has supported some key internal ratios, but no conditions to lend were attached, so the funds did not create much market liquidity.

So who's lending? Let's look at eastern Massachusetts, where I spoke with some bankers off the record this week.

The lenders who are booking new lending relationships are re-financing relationships that exist at other banks. There is little expansion of lines of credit. There is no merger and acquisition activity.

At some of the biggest banks in the area, here's what we're seeing. B of A is in the papers every day because of the disastrous acquisition of Merrill Lynch. An explanation of their lending approach in the lower and middle market is that the Bank would lend, but there is concern about the credit quality of the borrowers—so not many loans are being made there. Citizens just announced huge losses for the last quarter of 2008 and for the year as a whole. Sovereign was recently acquired by Banco Santander from Spain, which is now instituting tighter credit standards and overhauling the culture, making its lenders more cautious. And TD Banknorth appears to be the most active in lending at that end of the market, but can be selective when reviewing credits from these other banks.

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One tier down, Middlesex Savings Bank and Eastern Bank seem to have avoided the toxic assets found at B of A and Citizens and are lending more aggressively, albeit selectively. Even in this sector, banks are establishing higher floors to loan rates, requesting more security, and tighter covenants.

Even mezzanine lenders, who were shut out when senior debt lenders were making more aggressive loans a few years ago, are getting involved—in response to the request by senior lenders to have more capital.

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## a different approach

Now is not the time to take your lender's word on the safety of your financial relationship. It is time for your company's finance people to meet with other bankers and get them familiar with your company—just in case your current banker pressures you to refinance elsewhere.

Some businesses are trying to avoid banks that took TARP money, not wanting their fate to be in the hands of the government overseers (as Northern Trust learned this week with the flap over the sponsorship of the PGA tournament in Los Angeles - [http://www.huffingtonpost.com/2009/02/24/northern-trust-bank-threw\\_n\\_169674.html](http://www.huffingtonpost.com/2009/02/24/northern-trust-bank-threw_n_169674.html)). If your business needs a multi-million dollar loan facility, working with larger banks may be unavoidable. But if your loan needs are smaller, you might be better off looking at community or medium sized banks that rejected the government's funding offer.

Also, owners should consider other forms of capital, such as injecting more equity or shareholder loans, as well as better trade terms from suppliers.

Business owners should become accustomed to the idea of more collateral needing to be pledged, higher rates and fees, requests for personal guarantees from the owners and tighter covenants. At all costs, loan defaults must be avoided because banks will not show much appetite to forbear. If your company's revenues are declining, you must be ruthless in cutting costs in response (or in advance) to avoid this possibility.

At some point, from the lessons learned in Argentina, it is likely that inflation will return to the U.S., and business owners and investors will need to be ready to adjust their financing practices. However, at least for the near term, Fed chief Bernanke has downplayed the threat of inflation (<http://www.reuters.com/news/video?videoid=98951>).



## reading list

### *The New Capitalists:*

### *How Citizen Investors are Reshaping the Corporate Agenda*

By Stephen Davis, Jon Lukomnik and David Pitt-Watson

This sounds like a do-good kind of book about how activists can change the world. But it is actually much more down to earth. And it has a point that is very important to understand, especially as we make our way through and out (yes, we will eventually get out) of our current recession.

The authors assert that change will be driven by the significant shift in the ownership of public companies. They point out that as recently as 1970, the market was controlled by a small number of wealthy individuals. Small investors owned just 19% of stock. Today, more than 50% of the U.S. market and more than 70% of the UK market is controlled by institutions investing the money of regular people. This trend has been steady over the past few decades.

How will this change the markets? If you own diversified portfolios rather than individual stocks, the authors assert, you will have a greater interest in the health of the system. Does our current crash prove them wrong or show us the pattern that will emerge after we get through these tough times?

Read more about this book (<http://www.amazon.com/New-Capitalists-Investors-Reshaping-Corporate/dp/1422101010>).

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## announcements

On Tuesday, March 17, the Exit Planning Exchange (XPX) will hold a full-day program at Babson College in Wellesley, MA. The XPX Summit '09 will draw many practitioners from the world of advisors to business owners, including: wealth managers, investment bankers, business brokers, consultants, coaches, estate planning attorneys, corporate attorneys, and insurance specialists. You will get to hear three keynote speakers and attend up to three of nine breakout sessions, all related to exit strategy planning for owners of closely held businesses. The goal of this event is to provide a day of learning and networking for those involved in helping business owners with exit strategy.

If you are interested in participating, visit the XPX Summit '09 web site (<http://www.exitplanningexchange.com/>).

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An upcoming issue of CEO Refresher will carry an article of mine entitled, "Strategic Conversations Will Help You to Work Smarter in Difficult Times" (<http://www.refresher.com/amcoconversations.html>).



## about trek consulting

Trek works with owner-managed businesses to develop action plans for growth. Trek also works with the owners to prepare for their successful exit by coordinating the resources necessary to increase and preserve the firm's value, creating the succession plan and assembling the right transaction team, financing and post-transaction plan.

Our clients report improved market focus, greater revenues, better margins and increased profits. To learn more about Trek Consulting and how we can help you improve your company's results, visit us on the web at [www.trekconsulting.com](http://www.trekconsulting.com) or call us at 781.729.1008.