Lead Left Interview – Barry Bobrow (Part 2)

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This week we continue our conversation with Barry Bobrow, Managing Director, head of Loan Sales and Syndications, Wells Fargo Capital Finance. Wells Fargo Capital Finance is one of the largest providers of asset-based loans to large, middle market and small companies in the United States.

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***The Lead Left**: How about favored industries right now?*

Barry Bobrow: Thomson Reuters reports that the number one industry for ABL is retail. That represents about a third of the syndicated loan market. Retailers, given their large base of easily liquidated assets, work well in our business. Other sectors where ABL continues to see activity includes metals, chemicals, and transportation, which of course are more cyclical. Energy is a strong ABL sector; we don't lend against reserves, but are pretty comfortable with the commodity in storage and pipelines, and can lend against fixed assets.

***TLL**: Speaking of energy, how has the fall of oil prices impacted ABL?*

BB: ABL is an ideal structure to use since the borrowing base adapts automatically to falling prices of your inventory. You just need to track values carefully. I would expect some of the stronger oil-field service businesses may migrate to ABL.

***TLL:** Barry, talk about noteworthy deals you're seeing in the market.*

BB: There are a couple of leveraged retailers in market right now that I don't want to name. We haven't seen a lot of M&A in general and certainly not in the retail space. Leverage is relatively high so there will be interesting deals to watch. Despite the high level of global M&A last year much of it was high grade and corporate to corporate debt and not a lot of it found its way to the asset based market. I'm hoping we see more event driven financings this year.

***TLL:** Are smaller middle market lenders consolidating?*

BB: Because of the cost structures of the larger banks, many are moving away from smaller transactions. The breakpoint is going to be different for every bank. To take advantage of this, several BDCs are buying small-end ABL firms. That's a real trend. As more capital flows into the BDC space, I would expect you'll see more of that activity.

***TLL:** A big change since 2011 is the regulatory pressure on banks regarding "risky loans." How is that affecting asset-based lenders such as Wells Fargo Capital Finance?*

BB: Many good old fashioned asset-based loans are now being labeled as leveraged loans under the new guidelines. Because of overall leverage and cash-flows, there's a risk that many of these may encounter difficulties in approval due to their potential regulatory rating. Just the fact that banks are also so focused on

Leveraged Lending Guidelines has the risk of causing slower processes and uncertainty. There are a lot of non-banks looking to see if there are opportunities to fill a void.

TLL: *Are these regulations having a chilling effect on ABL? Is that the intention?*

BB: The intention of the regulators is to make sure that the banks they regulate are not engaging in unsafe and unsound practices. The challenge is that many asset-based loans are getting caught up in this from a definitional standpoint. It's certainly not the intention to stop banks from making good loans. As one of my industry friends said, some of the impact on asset based lending from the leveraged lending guidelines is really "collateral damage".

TLL: *What about from a syndication perspective?*

BB: Most of the market will not be impacted by the guidance. Having said that, the guidance could definitely put a chill on syndication market for certain deals. In the past, new asset-based deals which might not have been rated "pass" by the regulators could often be syndicated, but given the new guidance they cannot. For existing portfolio names that are not pass rated there may still be some syndication market, but the new deals will need to show some sort of structural improvement. Every bank needs to formulate its own policies, which will take some time and in the meantime syndication could become a bit more challenging.

TLL: *What worries you about the market this year?*

BB: Regulatory changes could certainly dampen M&A related deal activity, which could reduce volume. Also, until banks are on a better footing with respect to their own leveraged lending policies, there will be more uncertainty. One member of a panel I was on recently said that the traditional drivers to asset-based lending are not driving it right now. It's not M&A activity. It's not LBO flow. Certainly not a lot of restructuring going on. Much of the refinancing from last year won't be back in market soon so I guess I wonder what will be the drivers this year. It's a bit early to say.

TLL: *And what was your biggest surprise of 2014?*

BB: Looking back, it was the impact of jumbo deals. It was a record year for new money – almost all of the jumbo deals were upsizings. As a result, Thomson Reuters reports that 2014 was the biggest new money deal year. We probably won't get that again this year. I suspect we'll continue to see companies seeking to lengthen maturities while rates are attractive and potentially converting their higher-cost of capital to asset-based facilities wherever possible. That will still keep us very busy, but I don't think we'll see a repeat of 2014 for a while.

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