2004 Asset-Based Lending Survey

Report of Findings

(1) Year-end outstandings between 2003 and 2004 rose by 8.39%. This is the largest increase since the pre-recession year of 2000. Based on the new definition of outstandings, the volume of asset-based lending grew from $334.1 billion in 2003 to over $362.1 billion in 2004. (**See Appendix Exhibit 1.**)

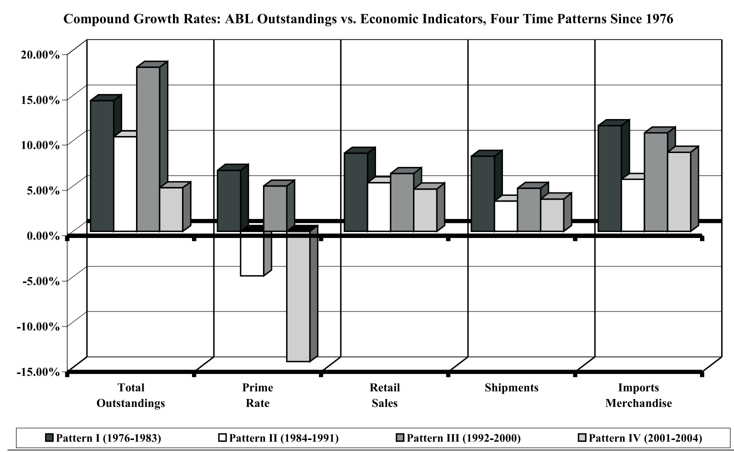
Given that the collected data for the cross-over definition year, i.e., 2003, under both definitions, it has observed some seasonality in the outstandings data. Data based on “year-end totals” are 1.75% smaller than those based on the former “average monthly” definition.

(2) **Appendix Exhibit 2** provides a traditional graph of the movements of outstandings over time. Overlaid is the 2003 graph with the 2004 in order to make comparative tracking easier. The trend in outstandings since the 2001 recession is noticeably flatter than that which took place after the previous recession period of 1990-1991. Compound growth between 1991 and 2000 was 16.94% compared with only 2.91% for the period between 2001-2004.

In the four years immediately following the 1991 decline (1992-1995), outstandings rose by 11.80%, a compound growth that was four times that which has taken place during the current take-off. From there they skyrocketed with another five years of growth at 19.37% through year 2000. The implication of this is that the present strengthening provides a much weaker base for the industry’s future growth than did the former one in the 1990’s.

(3) **Appendix Exhibit 3** shows these changes even more clearly on a year-by-year basis. The graph here illustrates four distinct patterns of change since SFNet began the modern era of data collection in 1976. More specifically, growth between 1976 and 1983, which is called Pattern I, is mixed but all positive. Pattern II, which took place between 1984 and 1991, exhibited strong year-to-year growth but one whose rate was clearly falling. In contrast, Pattern III, which occurred over the period 1992-2000, was characterized not only by strong growth, but also one that was moving almost consistently upward. Finally, Pattern IV —the one in which the industry is currently involved. So far, it shows one of weakness. Annual changes in growth rates begin-ning in 2002 are shown there as being the lowest of any of the other three historical growth patterns. The concern, then, is that this may forebode more long-term weakness in the growth of future outstandings volume. **Text Exhibit A** focuses on the comparative movements of several important economic indica-tors during these four patterned periods.

Text Exhibit A



Gathered are data for eight bellwether economic measures during each of these four growth time frames. This is the calculated compound annual rates of change for each. These rates were then compared to those for the total volume of outstandings during each of these four patterned time periods. Although many economic variables could have been assessed, these are the measures that strongly reflect a variety of aspects of economic performance. Accordingly, the GDP measured in terms of real dollars, the All Urban Consumer Price Index, interest rates as represented by the prime rate of interest, both merchandise imports and exports, total retail sales, and both new orders and shipments involving durable and non-durable goods manufacturing.

Four of the eight indicators exhibited changes in compound growth rates that were similar to those of total outstandings over these four patterned periods and are shown in **Text Exhibit A**. These were the prime rate of interest, retail sales, shipments, and merchandise imports. On the other hand, the remaining four measures’ compound growth moved in different directions from that of asset-based lending outstandings. Compound growth rates in real GDP were relatively low at around three percent over each of these four selected periods, and changes in them have been almost flat from pattern to pattern. Movements in both the CPI and new orders were also relatively low and moved in a flat pattern with the exception of their high rate of growth between 1976 and 1983. Merchandise exports moved mostly in an opposite direction to that of the total outstandings over the whole time period. However, a close examination of **Text**

Exhibit A indicates that changes in the growth patterns of the remaining measures of economic performance moved closely with that of the industry's asset-based lending outstandings.

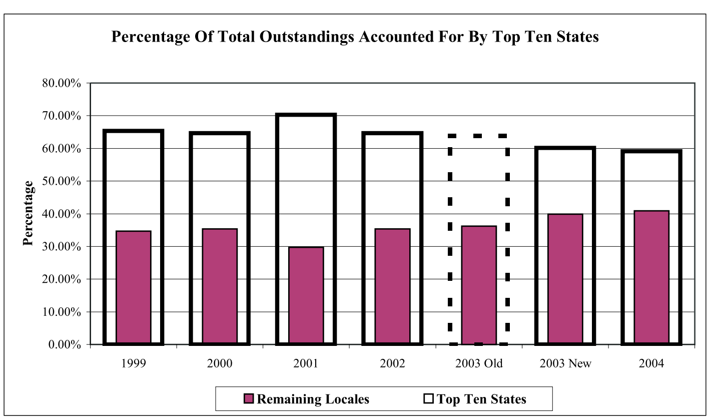
(4) Turn next to **Appendix Exhibit 4** where the volume of outstandings accounted for by the top ten states (and provinces) is presented. The comparisons made in the table respecting asset-based lending activities in 2003 and 2004 are assessed in terms of 2004's new definition of year-end total outstandings. As shown in the exhibit, California and New York continue as the leading states in the survey. Together, they captured $72.9 billion of the total market for asset-based lending, or about 20.1% of total outstandings. In 2003, they accounted for only $67.9 billion, but about the same percentage of the total. New Jersey jumped two positions over Texas and Illinois to no. 3. New Jersey's lending volume grew by $2.5 billion while that of Texas fell by about $1.3 billion and that of Illinois remained almost flat. In addition to California and New York, the positions of four other states remained unchanged — Ohio, Pennsylvania, Florida, and North Carolina. However, only Pennsylvania's outstandings remained flat. Those in the other three states rose by between $727 million (Florida) and $1.81 billion (North Carolina). Ohio's increased by $1.30 billion.

Georgia and Massachusetts traded the no. 9 and no. 11 spots versus 2003. Although Massachusetts grew by a respectable $892 million, or 8.02%, North Carolina rose by the largest amount of any locale, $3.86 billion, and at one of the largest growth rates, 38.0%.

In total, the top ten states accounted for 59.11% of all asset-based lending in 2004, down slightly from 2003's 60.08%. Nevertheless, these states generated over $13.3 billion or 6.64% more in volume than in 2003. But the lending base of their smaller counterparts rose by $14.71 billion, an 11.0% increase.

In an attempt to clarify discrepancies resulting from the new definition of outstandings, **Text Exhibit B** has been prepared . The exhibit compares outstandings for 2003 under the old definition as a dashed bar. Next to it stands a solid bar for the top ten states under the new definition. Thus, the bars to the left of the dashed one are as presented in past years' surveys under the old definition, while those to the right of it are as presented in 2004's survey under the new, year-end outstandings definition. The solid bars contained inside of each respective years' bars are defined similarly, but represent the collective remaining locales not falling within the top ten at those times.

Text Exhibit B



A cursory examination of **Text Exhibit B** implies that the trend in the dominance of the biggest states over the smaller ones in the last three years has been falling. However, there is strong reason to believe that the decline in their dominance has, in fact, been leveling off. This is because the true trend is masked to some extent by both the change in our definition of outstandings from average monthly outstandings, to that of year-end outstandings adopted in 2004 and by certain critical reporting differences among the set of respondent companies between 2003 and 2004. As shown in **Text Exhibit B**, the heights of the two sets of righthand bars are nearly identical, indicating that there was almost no relative change in the dominance of the top ten states between 2003 and 2004.

(5) **Appendix Exhibit 5** presents a breakdown of 2004 outstandings as they were generated within each of the 50 individual states and the District of Columbia and within those Canadian provinces and other regions in the world for which such estimates could be prepared. During this period, 33 states, two of the five Canadian provinces that reported outstandings, the United Kingdom, and other Europe had volume increases Assessments could not be made for Alaska and four of the nine Canadian provinces. In comparison, in 2003 there were 27 states, 5 Canadian provinces, the United Kingdom, and other Europe that showed outstandings increases. Thus, there appears to be an overall, worldwide improvement in asset-based lending activity. Despite the fact that three Canadian provinces had double-digit percentage declines in 2004, Canada had the largest percentage growth of any region at 38.47%. This was primarily due to Ontario's growth in outstandings of just over $3 billion, representing a gain of 55.73% over 2003.

Overall, asset-based lending in 2004 was stronger than in 2003 as nearly twice as many states had increases versus declines in their outstandings volume. In addition, every United States region, with the exception of the Middle Atlantic states, exhibited growth during 2004. Although the Canadian provinces of Quebec and British Columbia had strong growth in 2003, they struggled over 2004. However, Ontario's especially strong performance provided a significant overall boost to Canada's overall outstandings volume in 2004. Ontario's improved results are in line with statements from many economic experts that the very positive business, healthcare, educational, and operating climate there is attracting many United States and other foreign based companies there.

The next two charts, **Text Exhibits C** and **D**, compare for each of the two years the states with the greatest upward and downward changes in outstandings. Accordingly, the two charts make direct comparisons of data that were included in 2003's report with that newly presented in 2004's report.

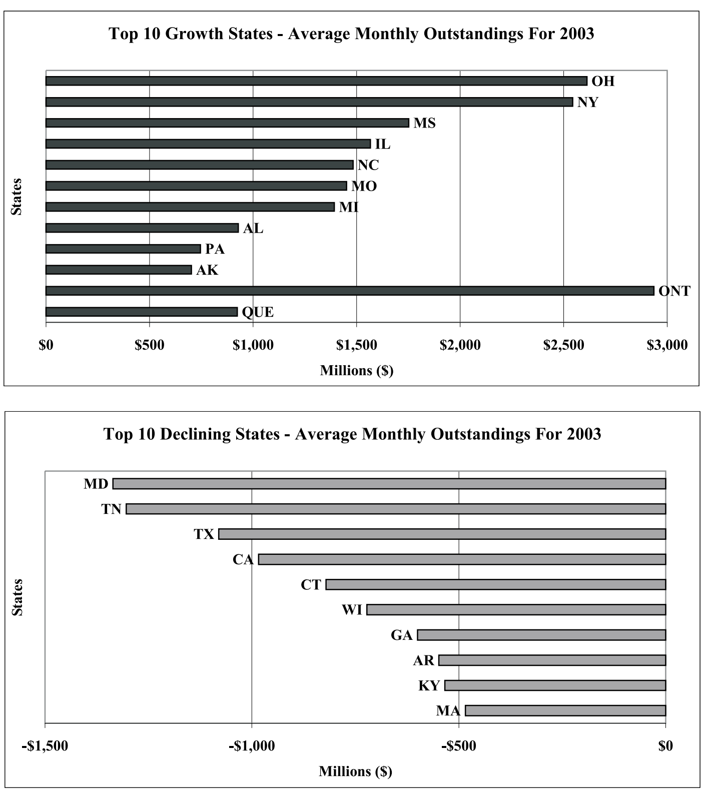
Text Exhibit C is a repeat of 2003's graph and was included for the first time there as Text Exhibit F. It shows both the top ten growth states and the top ten declining states based on average monthly outstandings. **Text Exhibit D** does the same for 2004, except that it is based on year-end outstandings. Although the 1.75% overall difference between the two alternate definitions may have had some differential impacts on individual states, it could not adjust for this due to lack of individually comparative information. However, the comparisons of these states' performance between the two years discussed below are significantly strong to outweigh the definitional differences. It is also important to note that these two exhibits focus on distinctive changes in volume within each locale. **Appendix Exhibit 4** and **Text Exhibit B** focus upon leadership based on total volumes themselves.

Turn to the analysis of the data contained in **Text Exhibits C** and **D**. Most obvious among the leadership changes is Georgia. In 2003, it had the seventh largest decline in average outstandings. In 2004 Georgia completely reversed the trend, showing the largest volume increase of any state, $3.9 billion, or 38%. California and Connecticut also rebounded to move from the top ten declining states list to that of the top ten growth states. Three of the top growth states in 2003, New York, Michigan, and North Carolina, continued their strong upward trend in 2004.

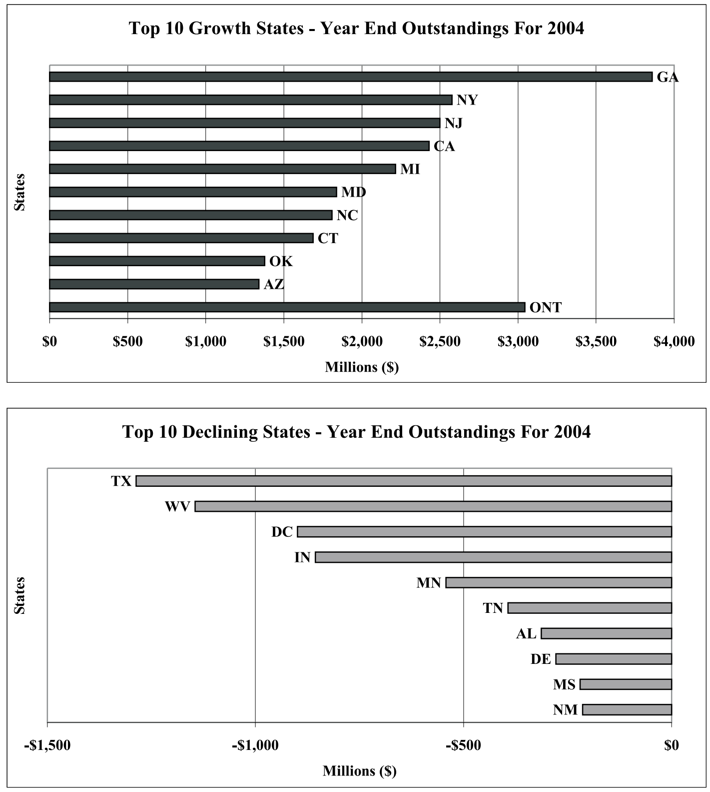
Two disturbing trends have been taking place in Texas and Tennessee. These are the only two locales out of the 59 worldwide areas that in 2004 exhibited continuing declines in asset-based lending in 2003 and 2004. Both are centered in the heart of the southern region of the United States, an area that most demographic and economic experts consider to be part of America's vibrant "sunbelt". Texas' asset-based lending performance has continued to be quite weak. It had the third largest reduction in outstandings volume in 2003, and in 2004 it fell even more. More specifically, it had the largest drop in the dollar volume of its outstandings of any of these 59 local areas in 2004. Its decline of nearly $1.3 billion was 5.65% lower than that of 2003. Furthermore, despite strong growth in its gross state product due to high oil prices, Texas' economic atmosphere has been weak in recent years. The unemployment rate for Texas, although dropping somewhat from 2003, still remained high at 6.1%. In addition, the Industrial Production Index for Texas fell for the fourth year in a row, reaching an eight-year low in 2004.

Tennessee's asset-based lending activity also displayed a continued downward decline. In 2003 it had the second largest drop in outstandings, falling by $1.3 billion or 19.27% from 2003. In 2004, although the decline softened somewhat, it still recorded a 9.1% dip from its 2003 level. From an economic

Text Exhibit C



Text Exhibit D



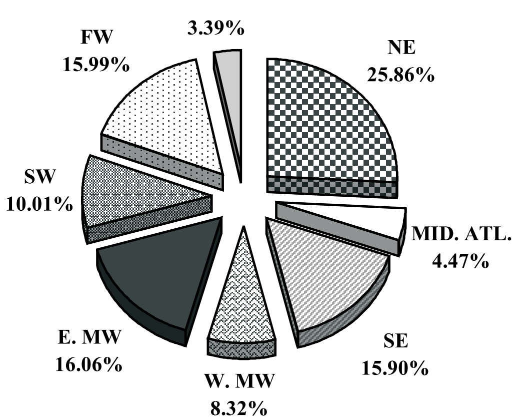
standpoint, conditions in Tennessee are puzzling. While its GSP rose by 6.83% in 2004, employment there has been stagnant. Its unemployment rate dipped only 0.1% in 2004 from a ten-year high of 5.5% in 2003.

(6) From the above state and other locale specifics, take a broader look at the wider, regional outstandings activities that took place. These are presented in **Appendix Exhibit 6**. The regional rankings changed somewhat from 2003 as the southeast region moved from fourth place to second with a growth in outstandings volume of $7 billion, a gain of 13.22% over 2003. The far west section of the United States had the second largest upward movement in outstandings. Volumes there rose by nearly $5.5 billion, a $10.20% over 2003. Seven of the nine states within this region had gains in outstandings including California and Arizona, which were top ten growth states in 2004 (see **Text Exhibit D**). The northeast region remained the highest volume locale in the world growing at a rate of 8.8%, or $7.6 billion. Continued improvement in the economy of this region since 2001 has helped strengthen the traditional industries that utilize asset-based lending.

As in 2004's survey, there is a pie chart of the proportions of outstandings volume accounted for by each region of the United States. This appears in **Text Exhibit E**. The results there are designed to depict the data contained in **Appendix Exhibit 6** so as to provide a clearer picture of the manner in which outstandings were distributed throughout the country in 2004. Also there is a chart for 2003 based on the year-end outstandings. This is labeled as **Text Exhibit F**. This has been done to provide an illustrative regional performance comparison of the two years based on the changed measure of asset-based lending outstandings. Areas along the eastern seaboard continue to account for nearly half of all of the asset-based lending done

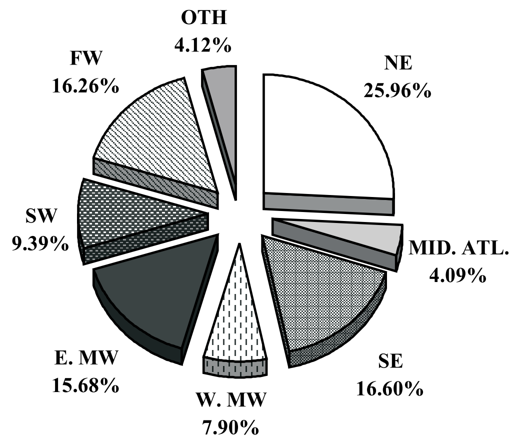
Text Exhibit E

Year-End Outstandings By Region For 2003 (%)



Text Exhibit F

Year-End Outstandings By Region For 2004 (%)



in the United States. It is in these regions that such traditional industries as textiles, apparel, footwear, and other manufactured soft goods are located. And, it is these industries that have served for many years as the primary clients/customers of the asset-based financial services industry. Outstandings along the seaboard increased only marginally to 46.65% in 2004 from 46.23% in 2003.

However, a comparison of **Text Exhibit F** with that denoted as Text Exhibit G in 2003's survey report, and which is based on average monthly outstandings by region, shows a decline in the percentage of lending activity along the East Coast from 50.66% to 46.23%. However, this difference is most likely due to reporting differences from 2003 and to a lessor degree by the change from average monthly outstandings to year-end outstandings.

There is an examination of the regional volumes and their compound growth rates over the last five years. This appears in **Text Exhibit G**. In particular, the table there presents the compound growth rate and trends in outstandings volume by region from 2000 through 2004. This recovery period has been somewhat weak with growth rates in real GDP in 2002 of 1.86%; 2003 of 3.04%, and 2004 of 4.44%.

It is apparent from the data in this table that asset-based lending activity in nearly all of the United States regions has been sluggish. Only the western midwest exhibits solid growth over the five-years. This confirms the forecast in 2002 that this region had excellent growth prospects for the foreseeable future. Elsewhere, two United States regions suffered compound reductions in volume, it was flat in two of them, and moved weakly upward in the remaining two locales.

(7) Because of the changes in the design of the 2004 survey, there are no participations data either by regions, based on advances, or by a fully detailed breakdown. Instead, more limited information is presented in **Text Exhibit H**. The exhibit presents summary data on these transactions based on the changed definition of year-end outstandings and has been prepared under this definition for both 2003 and 2004 for comparative pur-

poses. However, data collected for and used in prior surveys is not comparable to this new series.

As can be seen in this exhibit, participation activity rose by 0.75% and sole + lead lending fell by that rate. The total net difference between them was $20.52 million over 2003 and 2004.

(8) Next, turn to **Appendix Exhibit 7** where a breakdown of the number of companies that have raised funds through asset-based lending is presented. As indicated by the data compiled there, the number of such firms declined by 20.27% between 2003 and 2004.

Text Exhibit I also shows this phenomenon in terms of the trend over this period in United States versus non-United States totals. The number of companies using asset-based lending fell by 6.76% during the recession year of 2001, but rebounded strongly through 2003. In 2004, the number declined by 21.09%. Outside of the United States, clients fell by 18.23%.

Although client company size in terms of employees, a measure used in the past to assist in measuring the latter, (i.e., “number of employees per company”), could not be assessed this year due to lack of sufficient data, less directly they have been evaluated in terms of volume of asset-based lending per company. A comparison of the data contained in **Text Exhibit I** with that in **Text Exhibit J** indicates that outstandings per client company rose from an average of $4.52 million in 2003 to $6.25 million in 2004 in the United States and from $2.10 million in 2003 to $3.31 million in 2004 outside of the United States.

(9) Finally, the last feature contained in 2004’s survey is a new entry — an analysis of the asset-based lending industry’s activities by business segments. These contributions are presented in **Text Exhibits K** and **L**.

These exhibits examine total outstandings in terms of specific industry usage of asset-based lending instruments. The

Text Exhibit H

VOLUME OF YEAR END OUTSTANDINGS
SOLE + LEAD LENDING VS. PARTICIPATIONS BOUGHT

	2004 ($,000,000)	2004 %	2003 ($000,000)	2003 %
Sole + Lead Lending	$297,165	82.06%	$276,658	82.81%
Participations Bought	$64,980	17.94%	$57,446	17.19%
Total Year End Outstandings	$362,145	100.00%	$334,104	100.00%

Text Exhibit G

VOLUME OF LOANS OUTSTANDING BY REGION
2000 - 2004 ($000,000)

REGION	AMOUNT ($) 2000	2001	2002	2003	2004	COMPOUND GROWTH RATE (%)
NORTHEAST	$93,442	$86,530	$91,762	$94,918	$93,994	0.15%
SOUTHEAST	$56,972	$56,368	$63,330	$65,213	$60,126	1.36%
FAR WEST	$58,905	$52,786	$45,021	$45,564	$58,888	-0.01%
EASTERN MIDWEST	$49,820	$50,983	$54,256	$59,118	$56,794	3.33%
SOUTHWEST	$37,902	$29,246	$30,497	$28,884	$34,016	-2.67%
WESTERN MIDWEST	$21,819	$14,892	$22,440	$23,148	$28,605	7.00%
MIDDLE ATLANTIC	$16,100	$13,752	$13,032	$12,135	$14,801	-2.08%
CANADA	$2,320	$5,951	$2,976	$7,564	$10,457	45.71%
EUROPE	$2,631	$3,819	$2,493	$3,327	$4,463	14.12%
OTHER INTERNATIONAL*	$2,775	$87	$98	$184	$1	-86.22%
TOTAL	$342,686	$314,414	$325,905	$340,055	$362,145	1.39%

* Not Statistically Reliable

Text Exhibit I

NUMBER OF CLIENTS BY REGION (2000 - 2004)

	ESTIMATED NUMBER OF CLIENTS					COMPOUND GROWTH RATE
REGION	2000	2001	2002	2003	2004	(%)
NORTHEAST	19,232	16,089	18,850	19,402	14,574	-6.70%
SOUTHEAST	11,730	11,439	12,511	14,553	10,913	-1.79%
FAR WEST	9,735	10,232	10,470	9,228	9,708	-0.07%
EASTERN MIDWEST	9,411	11,471	10,441	11,389	7,544	-5.38%
SOUTHWEST	7,111	4,957	6,379	6,221	4,486	-10.88%
EUROPE	4,486	5,823	5,137	4,988	4,396	-0.51%
WESTERN MIDWEST	5,335	3,992	5,610	5,333	4,375	-4.84%
MIDDLE ATLANTIC	2,501	2,478	2,366	3,887	3,646	9.88%
CANADA	1,852	2,522	1,676	2,153	1,860	0.11%
OTHER INTERNATIONAL*	496	11	20	66	66	-39.60%
TOTAL	71,889	69,014	73,460	77,220	61,568	-3.80%
U.S. Total	65,055	60,658	66,627	70,013	55,246	-4.00%
Non-U.S. Total	6,834	8,356	6,833	7,207	6,322	-1.93%

*Not Statistically Reliable

Text Exhibit J

VOLUME OF OUTSTANDINGS PER CLIENT (1999 - 2004)

Year	Number of Clients	Number of Clients % Change	Volume of Outstandings (Old Def'n) ($000,000)	Volume of Outstandings (Old Def'n) % Change	Outstandings Per Client (Old Def'n) ($000,000)	Volume of Outstandings (New Def'n) ($000,000)	Volume of Outstandings (New Def'n) % Chang	Outstandings Per Client (New Def'n) ($000,000)
1999	65,749		$293,773		$4.468			
2000	71,889	9.34%	$342,686	16.65%	$4.767			
2001	69,014	-4.00%	$314,414	-8.25%	$4.556			
2002	73,460	6.44%	$325,905	3.65%	$4.436			
2003	77,220	5.12%	$340,055	4.34%	$4.404	$334,104		$4.327
2004	61,568	-20.27%				$362,145	8.39%	$5.882

results are based on a summary of responses regarding the top four industries whose firms have secured funding from them in 2004. **Text Exhibit K** presents that summary in the form of a pie chart broken down into the nine most frequently cited primary industry segments. The remaining portion was placed in a 10th category labeled as "unidentifiable other." In total, these 10 components accounted for the total volume of outstandings generated in 2004. Only the top four industry clientele information was provided, most of the activity in total among them appears to have taken place in their less active segments. As a result, the single largest percentage of outstandings ended up in the "unidentifiable other" category. In total, it comprised 54.05% or nearly $196 billion of the total volume in 2004. Nevertheless, in this format one can see in **Text Exhibit K** the substantial proportion of asset-based lending that took place in total among the top four industries mentioned.

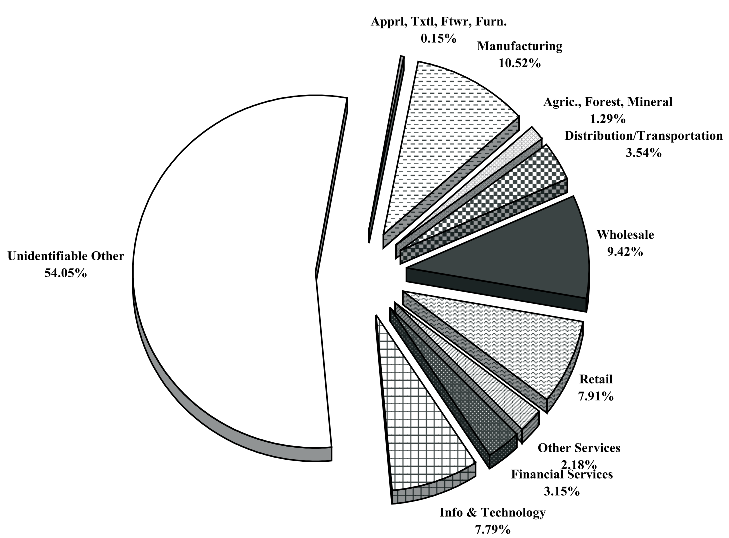
Also prepared in **Text Exhibit L** to highlight more clearly the relative usage that these most frequently mentioned nine industries have made of asset-based lending instruments in 2004. In particular, the exhibit presents a specific breakdown of the asset-based lending activities of these "identifiable industries" only. Thus, the percentages presented there are in terms of 100% of these nine "identifiable industries". This closer examination reveals the dominance of the previously indicated three traditional asset-based borrowers — manufacturing, wholesale, and retail. In total, the three segments accounted for 60.61% of the identified portion.

Before closing, it is also important to note that the trend in usage by industry is also probably changing. In 2003 some industry data was collected for the first time, but it was not analyzed for various reasons. However, in another study, other data was collected and evaluated for 2003 and 2004. Although the data are not directly comparable to that collected for this report, they do yield some insight into the year-to-year changes that took place between 2003 and 2004 in these industries' dominance. In particular, although the traditional manufacturing, wholesale, and retail industries remain the primary users of asset-based lending in 2004, all three made less use of it than in 2003. Comparable data for the two years reveals that manufacturing (and minerals) usage dropped from $57.4 billion in 2003 to only $42.0 billion in 2004, a decline of 26.80%. Use by the wholesale industry dropped even more, and on both an absolute as well as a relative basis. In particular, funding fell from $80.8 billion to only $34.1 billion, a decline of 57.79% between the two years. Retail dropped by less than $1.0 billion, only a 3.70% decline. Among the top four industry users, only information & technology showed a significant increase. It rose 253.82% between 2003 and 2004, an increase of nearly $17 billion. The only other industry segment that exhibited a significant positive increase in asset-based lending usage was that composed of service-oriented businesses. In fact, as a full sector, the group includes financial and other services. And the latter includes healthcare services, temporary staffing, employment services, and marketing and advertising specialists. Between 2003 and 2004, the group in total grew by 568.41% from $3.4 billion to $19.3 billion. These results indicate that while the three traditional industries remain the primary users of asset-based lending, they may be losing their dominance to those that are newer and less traditional such borrowers.

The three sets of findings — that exhibited in **Text Exhibit K**, in **Text Exhibit L**, and the results presented above — strongly suggest that more data collection is needed, and in a more industry definitive fashion, in order to examine the future directions into which the industry is headed.

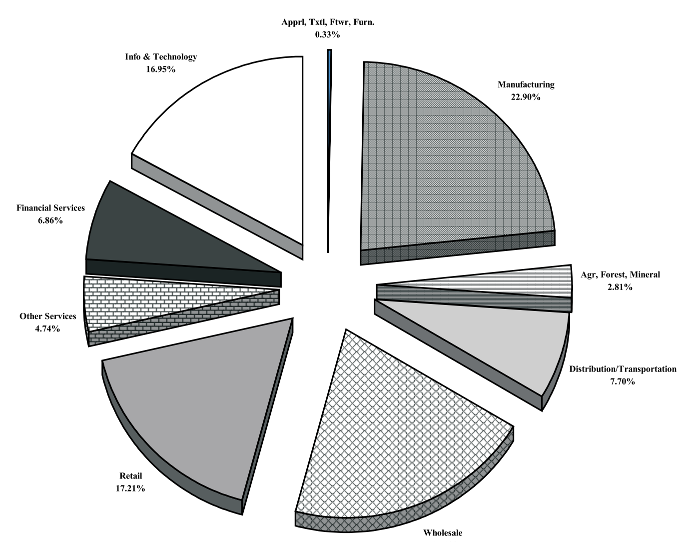
Text Exhibit K

Outstandings By Specific Industries



Text Exhibit L

Outstandings By Specific Identifiable Industries



A FINAL LOOK TOWARD THE FUTURE ...

Although there is not a forecast of the future movement of the industry as in 2003, an examination of a few of the economic indicators that seem to have some impact on the volume of financing carried out annually by the industry was conducted. An initial look at these is in section (3) earlier in the report.

Where will the industry be in 2005? Preliminary data for the first half of 2005 is mixed. Seasonally adjusted real GDP data for the first two quarters of 2005 is down only slightly from that in 2004. And, although over the same periods the CPI is higher, surprisingly it has not risen significantly, despite the sharp increase in fuel prices. The real concern appears to lie more in that of healthcare costs and the so-called “bubble” in housing prices. 2004’s growth in imports was significant, averaging in double-figures. So far in 2005 they have begun to drop. Retail sales are sluggish and the growth in shipments is falling off. Perhaps the strongest indicator in favor of a positive year for asset-based lending are interest rates. Having risen in every month since July 2004, the prime rate jumped even more to 6.25% this past July. So, what does all this tell us? Expect the total volume of outstandings to rise somewhere around 4.6% to 5.4% in 2005.

This report is based on statistical information supplied by members of the Secured Finance Network and estimates from other sources involved in the asset-based lending industry. The final figures are derived by using advanced statistical estimation and modeling methods and are the best estimates of the activities of the industry available.