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A Global Perspective...
What in the World is Going On With Factoring?

So, what in the world is going on in the factoring industry? Thomas Siska of FactorHelp.com tells us simply: just about anything and everything — and just about anywhere and everywhere. But, as the statistics reveal, it's no longer about growth for growth's sake. Factors will continue to explore new territories and when all is said and done, the endgame for players will be to "stake their own claim."

By Thomas G. Siska

The rate of growth of factoring around the globe is slowing down. The good news is that we are still talking about an industry that is growing, not shrinking. And while statistics can be misleading, there is no fooling around with the fact that growth is slowing down both in percentage terms as well as real dollar terms.

Worldwide Total Factoring Volume

VOLUME*	1999	2000	2001	2002	2003
Global	€557	€624	€686	€724	€760
>	22%	12%	10%	6%	5%
>>	€100	€67	€62	€39	€36

Key: * Annual volume in billions (Euros)
> Percentage change from prior year
>> Change from prior year (Euros)

Source: Factors Chain International (FCI) at www.factors-chain.com

The statistics coming from the U.S. are decidedly worse. Not only has growth basically come to a screeching halt, but it has been stagnant since the dawn of the new millennium.

United States Total Factoring Volume

VOLUME*	1999	2000	2001	2002	2003
United States	$84	$95	$91	$95	$96
>	7%	13%	-4%	5%	1%
>>	—	$11	-$4	$4	$1

Key: * Annual volume in billions (Dollars)
> Percentage change from prior year
>> Change from prior year (Dollars)

Source: Commercial Finance Association

There is no secret as to the reason for the slowdown in the U.S. as compared to the continued growth on the global scale. Many U.S. firms in the garment and textile industries (America's most prolific users of factoring) are continuing their migration offshore, attracted by the lower cost of doing business, especially labor costs. The result of this recent phenomenon is that international factoring has come to center stage with almost triple the growth rate of domestic factoring and appears to be one of the best opportunities for future growth.

Domestic vs. International 2003 Growth Rates

FCI MEMBERS ONLY	2002	2003	% CHANGE
Domestic Factoring FCI	€311	€341	10%
Int'l Factoring FCI	€23	€30	34%
Grand Total FCI	€334	€372	11%

WORLDWIDE	2002	2003	% CHANGE
Domestic Factoring	€681	€712	4.6%
Int'l Factoring	€43	€48	11.2%
Grand Total	€724	€760	5%

Key (from FCI): Annual volume in billions (Euros)

The entrepreneurial nature and structure of the recourse factoring market allows these nimble risk takers to react quickly and "stake their claim" as they blaze new trails across the landscape.

It is clear that with domestic factoring stagnating in the U.S. and growth slowing around the globe, cross-border factoring may present the best opportunity for growth in the traditional factoring niche. And while U.S. factors are presently behind in penetrating the international factoring market, there is an excellent opportunity now to challenge the leaders.

2003 Domestic Factoring Volume

RANK	# OF FACTORS	COUNTRY	DOMESTIC
1	110	United Kingdom	€158
2	45	Italy	€125
3	213	United States	€77
4	20	France	€68
5	15	Japan	€60
6	20	Spain	€36
7	18	Germany	€27
8	5	Netherlands	€16

2003 International Factoring Volume

RANK	# OF FACTORS	COUNTRY	INTERNATIONAL
1	45	Italy	€8.00
2	18	Germany	€7.95
3	20	France	€5.00
4	20	Taiwan	€4.30
5	213	United States	€3.20
6	110	United Kingdom	€2.50
7	4	Belgium	€2.00
8	9	Denmark	€2.00

Key (from FCI): Annual volume in billions (Euros)

At the end of 2004, U.S. import quotas for textiles expired. This will surely change the landscape of this global industry since producers will now relocate to the most advantageous areas. The movement already started in late 2004 in anticipation of this industry-changing event. The migration will involve the severing of established factoring relationships in favor of firms more familiar with the manufacturer's new country of residence. The country that stands to be the biggest beneficiary of this movement is, of course, China.

In addition to the many local Chinese and Hong Kong factoring divisions of banks, several familiar entities have already established their presence in China, such as CIT, GE Commercial Finance (even though GE sold its U.S. factoring operation to CIT) and UPS Capital. In turn, at least one China-based factor already has a beachhead in the states, DBS Bank Ltd. As evidenced in the previous charts, China (together with Hong Kong) does not rank in the top eight in factoring volume for either domestic or international factoring. As such, it is fertile territory waiting to be harvested.

The one ray of hope in the domestic U.S. traditional factoring market is the recent success some of the established players have shown in taking their core competency, retail credit and collection services, to industries outside of garment and textiles. CIT has established a position in the seafood industry while most every traditional factor has made a push into electronics, housewares and toys. It is expected that these factors will continue to attack any and every product category coming out of retail.

Another clear and continuing trend can be summed up in three words: consolidation, consolidation and consolidation. Within the last two years, CIT accomplished its version of "addition by subtraction" by purchasing the seventh and fifth largest competitors by volume at the time, GE Commercial Services and HSBC's factoring unit. GMAC, SunTrust and Wells Fargo Century (second, third and fourth, respectively) can't be too far behind in making moves of their own. And while it's "out with the old," there was actually a new entrant, First Capital Corporation, which began its foray into non-recourse factoring.

The net effect was another decline in the number of individual players competing in this space, resulting in a reduction of people employed as well. The offset to the drop in traditionally trained personnel is the hiring of people in the international departments, those with knowledge of non-traditional industry niches and ABL trained credit executives to manage the inventory exposures that are growing due to competitive deal structuring. The long-term employment effect of these initiatives won't be known until sometime in the future when it can be determined if the players can truly succeed in these new areas.

Non-Traditional, Recourse Factoring

There has been very little attention paid to cross-border transactions by the recourse factors in the U.S. While the number of recourse factors is estimated to be above 1,000, the number of these factors that focus on international transactions is less than a dozen. Even these tend to work in concert with either an independent credit insurance company or the Export-Import Bank of the U.S. Both of these insurance sources cater to a more balance-sheet oriented borrower, eliminating the lion's share of clients the recourse factors target. So it is doubtful that recourse factors, as a whole, will make a global push any time soon. However, 2005 and beyond should find several recourse factors carving out a niche in not only cross-border trade, but in just about every other facet of trade receivables known to man. The entrepreneurial nature and structure of the recourse factoring market allows these nimble risk takers to react quickly and "stake their claim" as they blaze new trails across the landscape.

Even the largest and most institutional of recourse factors, Wells Fargo, is quietly making a market with its factoring product that didn't exist just five years ago. The largest of recourse factoring clients used to have maybe $25 million in annual sales. A few clients may have been as large as $50 million in sales. Incredibly, Wells Fargo has funded a couple of clients with factored volume exceeding $250 million annually. With a low cost of funds, Wells finds its recourse factoring product to be, in certain cases, a more efficient substitute for receivable securitizations.

There are now factors that fund sales commissions (mostly post-contract fees of real estate brokers). A few will pre-fund retail sales (such as advancing one week's worth of receipts to a restaurant). Many more will now provide leasing, inventory advances, purchase order financing or other such accommodations to secure the "bread & butter" factoring business. Several are venturing into the construction industry. Medical receivable factors, both entrepreneurial as well as large institutional firms, are popping up everywhere. Similarly, both institutional and independent factors specializing in a single industry continue to thrive in transportation and staffing. The staffing niche is so saturated there are now factors that will advance on permanent placement fees (one firm only factors permanent placement). Another new entrant specializes in the slow pay, contingent fee area of advertising agency paper.

An even more interesting development in recourse factoring is the targeting of a particular sales channel, as opposed to a particular client industry. There is a factor that specializes in its ability to work through CPAs. Several specifically target banks. Another is trying to own the DIP attorney referral space.

As mentioned earlier in this article, even traditional factors are once again looking at the recourse market as a way to leverage its existing sales channel. So it is safe to say that where there is a slight hole in the marketplace, someone will no doubt step in and try to fill it. And while filling a need is good, "owning" a piece of the market is much better.

Lastly, banks continue to push forward with recourse factoring variations. From the largest of banks, such as Wells, to small independent community banks, factoring remains a popular product. Even though quite a few banks have been exiting the space recently, that number is still more than offset by the banks jumping in. Further, if history is a guide, the restrictions that the federal government just lifted on credit unions is an invitation to a whole new wave of competitors. When the same thing happened to the savings and loan industry in the 1980s, the S&Ls moved into factoring faster than any bank did. While credit unions probably won't move quite as fast as their S&L predecessors, they are sure to make a splash in the future.

Conclusion

So what in the world is going on in the factoring business? Well, just about anything and everything. And just about anywhere and everywhere. Expect to see almost every traditional factor spreading out beyond its core industry segments and beyond the border in its established niches, thus creating growth for the firm and overall employment. And what is good for the goose will be good for the gander. In other words, we'll see foreign factors coming to the U.S. (such as the already established factor from the UK, Bibby Financial). Recourse factors will be doing bigger deals (it is now fairly routine to fund outstanding receivable balances between $2 million and $5 million through newly created participation arrangements) and smaller deals (there is one factor that has amassed $2 million in A/R in less than 18 months with the average client below $10,000 in monthly volume). They will broaden their product offering and venture into uncharted industry segments. Overall employment should continue to grow at a fairly robust pace. And the name of the game is no longer to grow for growth's sake. Factors will pick something they can establish a presence in and push to own their space. These pioneers will no longer accept simply blazing the trail. They'll continue to explore, but the endgame will be to stake their claim. Happy trails in 2005! abfj

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