Case Study #1

Bill & Mary are very excited to be buying their first house. They come to you as a referral from a broker who has worked with you in the past and you did such a great job she is sending another client to you. Bill is the Athletic Director at a local college where he started 3 years ago and loves his job, which is why they have decided to settle down in this area and no longer commute over an hour just because their parents want them to stay close to them. Mary also has been working in this area for 1.5 years and prior to her current job did some part time work while she was looking for about 8 months, she is also at the local college as an administrator in the financial aid department. Their parents aren't thrilled with the move which takes them an hour away but are supportive and willing to help them with whatever they need.

Here is their financial information:

Purchase Price: $270,000
Loan Amount: $243,000

Principal, Interest, Taxes and Insurance payment on new home $1,658.36

If Private Mortgage Insurance is needed that monthly payment is $85.42

All other monthly payments $47.75

· Closing Costs $4,000 ·

Income: Derived from current
paystubs

Bill $7,500
Mary $2,000

Credit Scores:
Bill 802
Mary 797

Liquid Assets $ 22,000

Does the credit score meet the standard requirement?
Could this be considered a Qualified Mortgage?
Does this loan require Private Mortgage Insurance?
There are other things to consider in this case study so pay attention to the synopsis and all the numbers that have been given on this page, each one has a reason for being there

Case Study #2

Jim & Kelly are looking to buy a new primary residence in a quieter part of town. Their kids are grown and they have no use for all the square footage in their current home which they own. They have found a condo in town and are excited about moving there, it is right near restaurants, theatres and shops which they love going to. Jim is a Computer Engineer who has been in the business for 20 years however did just switch employers a little less than a year ago that has more bonus potential but a lower base salary, he has historically received bonus payouts but they have varied quite substantially over the past two years. Kelly is self-employed and works as an interior designer with a lot of real estate brokers you know to stage homes for sale and has been doing it for 7 years.

Here is their financial information:

Purchase Price: $725,000
Loan Amount: $455,000

Principal, Interest, Taxes and Insurance payment on new home $3,675.91

If Private Mortgage Insurance is needed that monthly payment is $157.62

All other monthly payments $1,109

Closing Costs $6,000

Income: Derived from current
paystubs and Tax Returns

Jim $10,400
Kelly $-500

Credit Scores:
Jim 705
Kelly 739

Liquid Assets $1,589,331

Does the credit score meet the standard requirement?
Could this be considered a Qualified Mortgage?
Ifit doesn't meet Qualified Mortgage Standards do you still do this loan?
Does this loan require Private Mortgage Insurance?
There are other things to consider in this case study so pay attention to the synopsis and all the numbers that have been given on this page, each one has a reason for being there

Case Study #3

Borrower	ABC Industrial Fasteners Inc.
Company Age:	0
Size:	Start up
Ownership/Management	Joe Jones
Industry	Industrial Fasteners-nuts, screws, bolts, washers, clips, etc
Market:	Domestic
Request:	1) $400K Asset based line of credit
	2) $ 20K Equipment loan -

Background:

Joe Jones is an experienced, highly qualified engineer who has been involved in his family owned business which was the manufacturing of industrial fasteners in New Jersey and doing $15 million a year in sales. Joe realized that the nature of his family business was changing, it was being affected by the world economy and lother factors. After trying convince the family that things in the fastener industry were changing he decided it was time to open his own fastener business, with a different twist. He would <u>not</u> be manufacturing, but he would be selling his "value added services" (consulting, problem solving, research, custom engineering and design) to some major manufacturers and distributers of equipment in the U. S. He came to a community bank that was growing their commercial loan portfolio and asked for 2 credit facilities that are mentioned above. The line was requested to support the need for a significant inventory of fasteners of various shapes and sizes, and the growth of accounts receivable. He provided the bank with a very well done business plan complete with projections, a market analysis, and his own personal financial information. The bank agreed to provide these facilities as requested. The company opened on time, and acquired four or five customers in the first year, four or five more in the second year, and a few more in the third year. Margins were good, the company grew, and it is still in business today.

How did the bank get to a level of comfort that convinced them to approve this loan request? What information did they require?

What research or due diligence did the bank do?

Why did the bank "believe in the future success of this business? Why was the business successful?

Case Study #4

Borrower	Foodie Inc.
Company Age:	10 yrs.
Size:	Annual sales $8 million
Ownership/Management	Bob and Regina Smith 50% each
Industry	Manufacturing- Food products, condiments, sauces, marinades,
Market:	Domestic
Request:	1) $3 million term loan for the purchase of another business, (a leveraged buyout) including equipment, recipes, inventory, licenses and goodwill. 2) $ 1.0 million Line of credit to support growth in A/R

Definition: A **leveraged buyout (LBO)** is a transaction when a company or single asset (e.g., a real estate property) is purchased with a combination of equity and significant amounts of borrowed money, structured in such a way that the target's cash flows or assets are used as the collateral (or "leverage") to secure and repay the borrowed money. Since the debt (be it senior or mezzanine) has a lower cost of capital (until bankruptcy risk reaches a level threatening to the lender[s]) than the equity, the returns on the equity increase as the amount of borrowed money does until the perfect capital structure is reached. As a result, the debt effectively serves as a lever to increase returns-on-investment.

The term LBO is usually employed when a financial sponsor acquires a company. However, many corporate transactions are partially funded by bank debt, thus effectively also representing an LBO. LBOs can have many different forms such as management buyout (MBO), management buy-in (MBI), secondary buyout and tertiary buyout, among others, and can occur in growth situations, restructuring situations, and insolvencies. LBOs mostly occur in private companies, but can also be employed with public companies (in a so-called PtP transaction - Public to Private).

As financial sponsors increase their returns by employing a very high leverage (i.e., a high ratio of debt to equity), they have an incentive to employ as much debt as possible to finance an acquisition. This has, in many cases, led to situations in which companies were "over-leveraged", meaning that they did not generate sufficient cash flows to service their debt, which in turn led to insolvency or to debt-to-equity swaps in which the equity owners lose control over the business and the debt providers assume the equity

This a leveraged buyout situation. A major food conglomerate, located in the U.S, but doing business internationally, decided to sell off one division of the company, even though it was profitable, it did not fit their new business model. The division they wanted to sell is their "pickle division".

Foodie Inc., a successful domestic, privately held company, is aggressively trying to grow and would like to buy this pickle division from the publicly traded conglomerate. They have accumulated some equity (cash) from both private investors, family, and their own resources, and have gone to a large financial institution for financing. They have prepared a significant business plan, complete with projections, and historical financial information from the pickle division of the seller. They are willing to pledge all business assets, their own personal assets, and utilize all cash resources that are available to secure the proposed loans. The loans were approved, the sale was completed. However, in just 9 months, the company was in trouble.

In fact. Shortly thereafter they filed for bankruptcy because they could not service debt and could not pay suppliers.

The bank had done significant due diligence. They used sophisticated financial analysis methods on all the numbers, they did research on the markets, analysis of the management team, testing of the products, review of regulatory issues, FDA regs, licenses, all kinds of research. There was no reason why Foodie Inc. should not be successful. Income projections were based on the new operating company and the historical performance of the pickle division, proven markets, - it all made sense.

What caused the company to take a sudden downturn?

Had the market changed? Did the product change? Did cost of goods and profit margin change? Did the labor markets change? Did new minimum wage requirements hurt profitability? Federal regulations?
Cost of new or replacement equipment? Lack of an adequate supply of raw materials?
Utility costs? Energy costs?

What if any could the bank have done sooner to prevent a loss? As banker how can you insure you are prepared to meet the challenges facing business at it relates to consumer habits, spending, the economy and seasonality.