

# TAKING STOCK

PERSPECTIVES ON WHOLESALE & RETAIL  
FROM INDUSTRY TO INVENTORY

## A WHITE PAPER BY BZ

Specialists in structured asset-based lending facilities  
for Wholesale & Retail businesses

[WWW.BZCF.CO.UK](http://WWW.BZCF.CO.UK)

# INTRODUCTION

**BZ invited a panel of leading senior advisers to discuss the post-COVID environment facing businesses that hold large inventory levels, in particular the Wholesale and Retail sectors, and the challenges and opportunities that confront businesses as they navigate the uncertain and volatile market ahead.**

The COVID-19 pandemic has sent shockwaves throughout the Retail industry, forcing the closure of physical stores, dislocating supply chains and transforming operating models. With near-term liquidity a critical concern, Government aid has provided swift and significant support but the financial repercussions of the crisis on the retail market will be felt for years to come.

This Industry Focus Paper, 'Taking Stock', reveals timely insights on a range of issues surrounding both the industry and its inventory. Here, an expert panel explores the dramatic shift towards online retail, the impact of the pandemic on supply chains and the role of brands as an asset class. This report also identifies fresh perspectives on funding dynamics and trends, examines the reintroduction of crown preference and outlines potential strategic options for businesses with substantial inventory holdings.

**Our special thanks go to the following industry experts for their participation and invaluable contributions to this study:**

**Martin Carr** – EY Parthenon  
**Mike Denny** – Alvarez & Marsal  
**Paul Flint** – Alvarez & Marsal  
**Milton Guffogg** – Retail Realisations  
**Matthew Holt** – Hilco Capital  
**Andrew Knight** – Crowell & Moring LLP  
**Andy Miller** – Sentio Partners  
**Adam Sookia** – Deloitte  
**Lyn Vardy** – Alvarez & Marsal  
**Matt Warrilow** – Alvarez & Marsal  
**Alex Williams** – EY-Parthenon  
**Lucy Winterborne** – EY-Parthenon

*“During the pandemic the shift to online retail has been accelerated due to restrictions in physical stores opening. As lockdown measures ease and government support is withdrawn, retail and wholesale businesses must deal with the financial, logistical and legislative challenges that have impacted the sector. The post-pandemic landscape is far from certain and those businesses that can continue to adapt will stand the best chance of recovery.”*

Ben Milner, BZ

## What, in your opinion, are the greatest challenges the wholesale and retail markets are facing today?

**Lyn Vardy:** *The key challenge will be to respond to the structural changes facing the sector, all of which have been accelerated by COVID-19 – this will include forecasting customer demand and implementing the right footprint and delivery channels to deliver this. These markets will also need to ensure they have the right funding mix and headroom levels to rebuild stock levels, which will largely be a ‘leap of faith’ until normalised demand levels become clearer. Finally, the sector is likely to face cost pressures through enforced changes to supply chains and rising global logistics costs.*

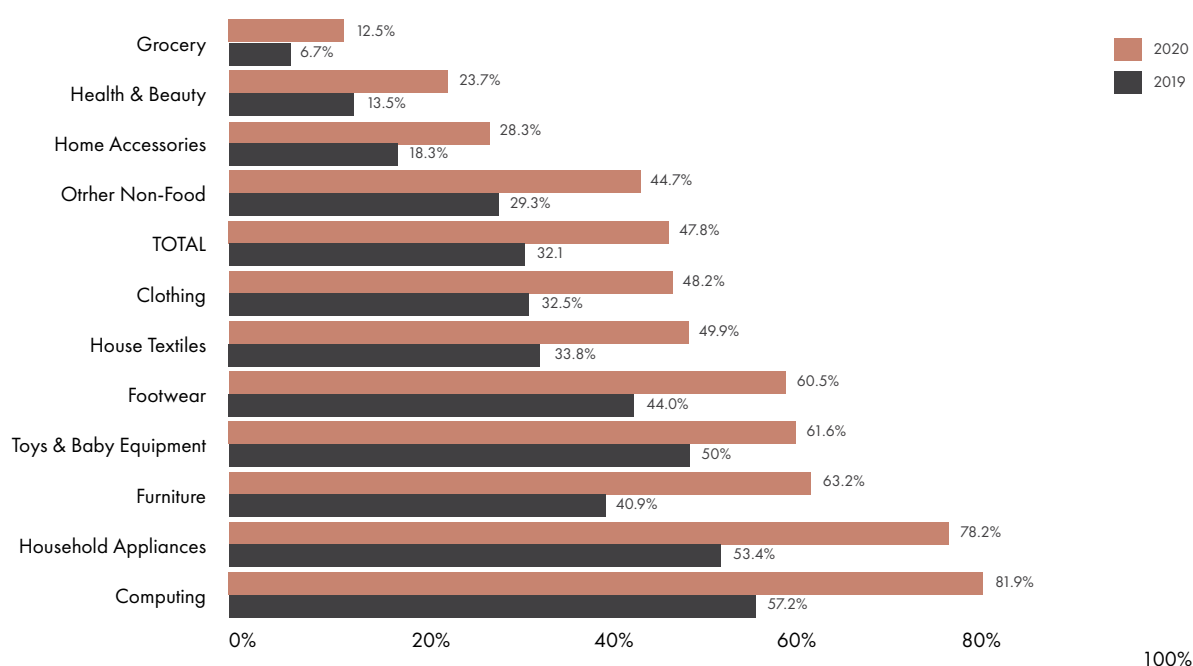
**Alex Williams:** *The channel shift, especially the speed of this shift through the pandemic, is both the greatest challenge and greatest opportunity for retailers. In addition, the coming months and years will provide economic challenges for consumers, which are likely to suppress overall retail spending causing further stress to the sector.*

## MAKING THE SHIFT TO ONLINE

The relationship between retailers and customers has changed fundamentally, with a demonstrable power shift in favour of the customer. Increasingly, the location of preference is online, prompting a shift from bricks and mortar to digital in order to remain relevant to today’s consumer. As retailers double down on digital to remain agile and meet consumer preference, a permanent shift either to purely online or omnichannel experiences to supplant the single in-store channel is an inevitability. It is likely that those that fail to make the leap will not survive.

With stores either closed or operating at reduced capacity and shoppers seeking to avoid indoor spaces, all retail categories shifted markedly to digital during 2020, particularly in December with the impact of lockdown. In January 2021, this trend intensified further as non-essential stores were closed.

## UK ONLINE PENETRATION BY CATEGORY – DECEMBER 2020 VS. DECEMBER 2019



Latecomers have found the move to online particularly challenging, while 'new' online retailers, such as ASOS and Boo Hoo, have been actively engaged in pursuing and acquiring assets of retail giants with traditionally large physical footprints, including Arcadia Group and Debenhams.

Almost every facet of online retail is changing. For traditional retailers, the migration to online has created a new set of logistical challenges such as managing returns and cancelled orders. Navigating the return to physical shopping as the market re-opens raises the problematic issue of forecasting demand as retailers look to manage their stock levels and supply lines.

While there have been undeniable challenges, there are also opportunities for a new breed of retailers ready and willing to embrace technology. Customer behavioural data allows for hyper-targeting and personalisation.

Virtual appointments and live streaming content are now starting to bring an in-store feel to the customer experience online. Augmented-reality (AR), machine-learning, and computer-vision techniques will further serve to de-risk digital-purchasing decisions by allowing consumers to see how items such as clothes, shoes and jewellery will look on them.

**For businesses that have been slow to move to online retail, is there still time or have they missed the boat?**

**Lucy Winterborne:** *Yes, but it is becoming more challenging and expensive. Many businesses have already developed online businesses but are suffering from a lack of brand presence, effective marketing and differentiation. In many cases, traditional bricks and mortar retailers have online competitors that are more established and offer a better digital proposition (range, price, website, logistical efficiency).*



## SUPPLY ISSUES

COVID-19 has put significant pressure on supply chains, particularly during the initial shockwaves of the outbreak in which many items were out of stock for extended periods.

The pandemic has also highlighted previously unseen supply chain vulnerabilities. Many wholesalers and retailers have risen to that particular challenge by responding quickly to assess supply chain risks and identify any indirect exposures, while seeking to diversify supply lines away from single source models.

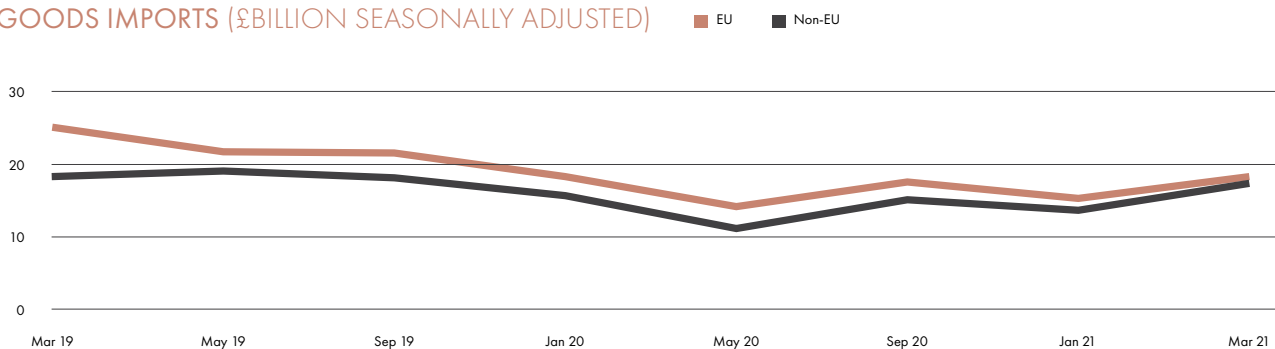
Preparations in advance of Brexit prompted both wholesale and retail businesses to build inventory levels as a contingency measure in Q3 and Q4 last year. They now face the challenge of unwinding their inventory positions at a time of uncertain demand. Increased input prices due to Brexit tariffs, foreign exchange and shipping costs have served to compound the issues facing these sectors, putting further pressure on margins and profitability.

The new post-Brexit trading environment has also made life difficult for UK firms trying to export to the EU, evidenced by figures showing reduced levels of imports and exports with the EU due to increased bureaucracy. Research from manufacturing trade group Make UK has shown that 74% of firms are facing delays with EU imports and exports.

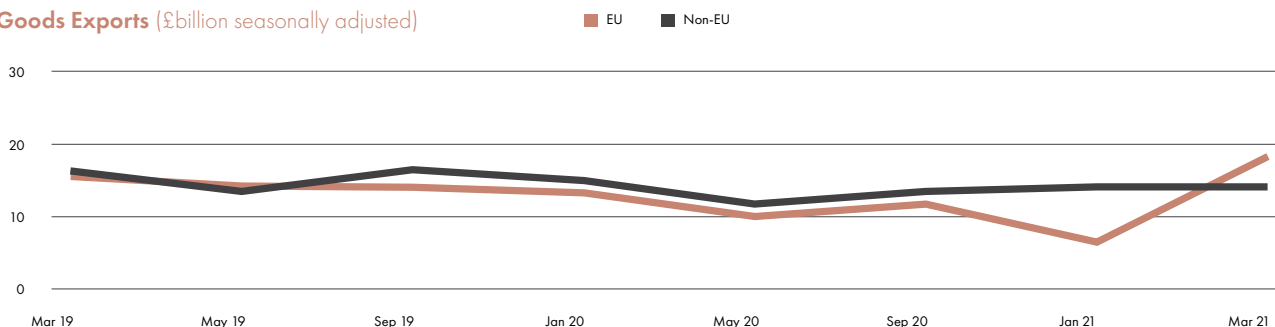
A survey conducted by the Chartered Institute of Procurement & Supply (CIPS) with UK supply chain managers has found that 63% of respondents have experienced delays of at least 2-3 days getting goods into the UK as new customs paperwork continues to cause problems.

According to the latest available ONS figures at the time of publication, exports and imports of goods with the EU, excluding precious metals, increased by £1.0 billion (8.6%) and £0.8 billion (4.5%) respectively in March 2021.

### GOODS IMPORTS (£BILLION SEASONALLY ADJUSTED)



### Goods Exports (£billion seasonally adjusted)



Source: Office for National Statistics – UK Trade Statistics, current prices, seasonally adjusted.

### In the context of the M&A market, have you noted any change in buy side due diligence around supply chains since Brexit and/or the disruption caused by COVID?

**Andy Miller:** Yes, a strong focus on sustainability of earnings, in cases where businesses have both benefitted and suffered through the pandemic. Impact on supply chains is a key focus; whilst some disruption might be temporary, buyers are keen to understand permanent impacts. The disruption (good and bad) has been and will continue to be a challenge to assess through diligence. Inevitably, we are seeing more earn out type structures and/or equity rollovers to protect some of these downside risks.

### How has COVID-19 impacted the operational requirements and costs of moving and holding stock?

**Milton Guffogg:** Most retailers rely on international supply chains, with goods manufactured overseas and imported into the UK. A shortage of containers and a bottleneck at UK ports triggered by surges in demand and huge shipments of PPE has caused freight costs to more than quadruple. This has eroded margins at a time when companies are already struggling to grapple with declining sales due to COVID-19.

Additionally, the shift of consumer demand to online during COVID-19 has forced retailers to drastically adjust their supply chains. Many have struggled with logistical capacity issues associated with a surge of online orders and in tandem, returns. As a result, there have been severe delays with dispatch and delivery, often culminating in cancelled orders and loss of revenues.

There is also the added problem of seasonal stock and how this is treated. Some retailers have chosen to try to clear stock at discounted levels, to either generate much needed cash or to save on warehousing costs. Others have chosen to re-categorise stock into the following season or store it for the following year. In any scenario, the solutions have a cash/profit impact for the retailer.

**Lyn Vardy:** Many businesses that we have worked with in the last 12 months have been extremely pro-active in managing supplier risk in the wake of the COVID-19 impact. The focus has been on reducing reliance and therefore the risk of a single country (i.e. China +1/+2 models) and single supplier strategy. Businesses are increasingly putting risk ahead of cost in many supply decisions, to create a broader and more localised supplier base that is resilient and fit-for-purpose in the context of increasing geopolitical volatility and pressures around ESG.



## THE ROLE OF BRANDS

The COVID-19 crisis has accelerated the expansion of e-commerce and has provided customers with access to a considerable variety of products from the convenience and safety of their homes, enabling businesses to continue operation in spite of contact restrictions and lock downs.

Ecommerce brands have benefited during the pandemic. Amazon, unsurprisingly, has been the biggest single beneficiary, focusing on essential household and medical items.

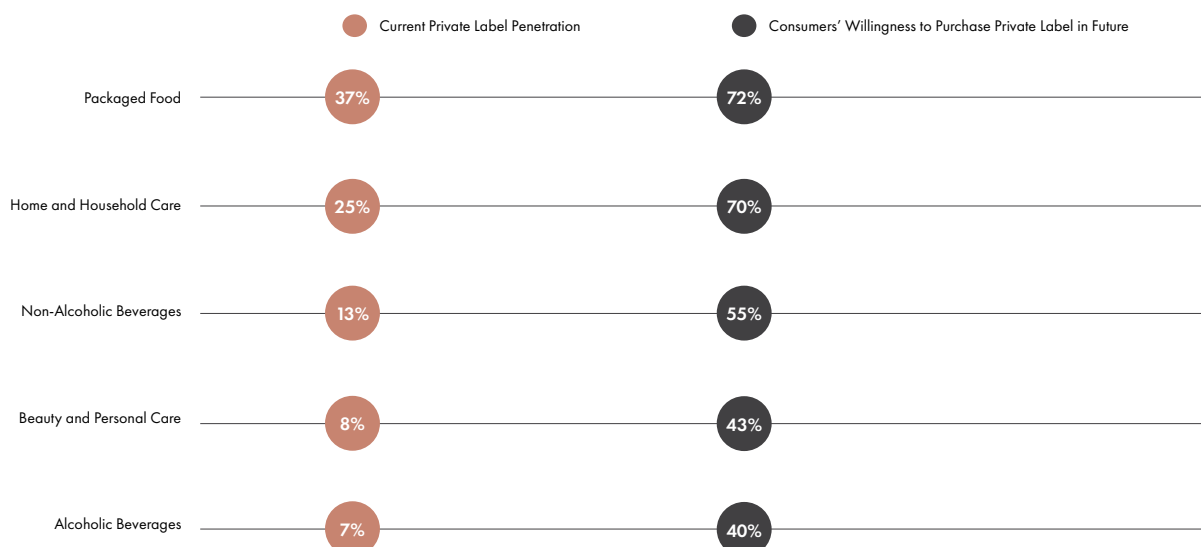
Ecommerce transactions have also made a notable shift from luxury goods and services towards everyday necessities. Due to consumers becoming focused on value they are also more likely to purchase private label products.

Strong brands may help businesses gain access to funding as they are increasingly viewed as boot collateral or an asset which can be lent against in its own right by specialist lenders. They will also attract higher valuations for businesses looking sell or raise equity.

### To what extent do you think the importance of brands has changed during the last 12 months? Are they more or less important and why do you feel this is the case?

**Martin Carr:** EY's Future Consumer Index survey indicates that consumers are becoming increasingly focussed on value as a driver of spend and as a result more likely to buy private label products rather than recognised brands. This is expected to have a larger impact on FMCG products sold through supermarkets and general merchandise retailers. However, brands will remain important and a driver of sales and traffic. In apparel categories, especially casual fashion and streetwear, there is no sign that consumer appetites towards 'must-have' brands is waning, whilst other brands have struggled to remain relevant, especially through the rapidly changing consumer market we've seen over the last year.

### SHARE OF UK CONSUMERS WILLING TO PURCHASE STORE BRAND/PRIVATE LABEL VS. CURRENT PENETRATION



Source: EY – Reshaping UK Retail: New Horizons for 2021.

### Do you think using the brand as collateral for debt facilities is something that will become more common?

**Andrew Knight:** *There is evidence that brands are increasingly being treated as borrowing base collateral, but this continues to be seen as a specialist activity, which must be approached with great caution. The largest obstacle to the development of IP lending in an asset-based lending context is the material difference in lenders' and borrowers' perception of the value of the brand. Borrowers tend to overvalue the brand, whereas experience has shown that brands become devalued quite quickly when they change hands and especially when they are acquired in private equity transactions. Consumers are highly attuned to changes in quality of service and product that may result from a PE owner's attempts to streamline costs.*

*In addition, the COVID-19 pandemic has had a material and adverse effect on UK retail brands in particular. The issue is not simply that shops have been compelled by law to remain closed and that retailers lacking an established online route to market have underperformed. There is also real uncertainty around the possible changes in retail consumers' behaviour and choices once 'normal life' resumes. For example, the market for formal business attire such as suits, shirts and ties was already under pressure before the pandemic, as 'business casual' became more widely-accepted. It now appears possible that, post-pandemic, people will go into the office much less frequently than before and that their need for business attire will reduce accordingly.*

### Have you noticed any change in acquirers' valuation of brands or demand for well established brands during the last 12 months?

**Andy Miller:** *Strong ecommerce brands have benefitted significantly through the pandemic as consumers have switched from traditional to online retail. Demand for strong brands has always been there and helps command a higher valuation. The pandemic will have enhanced that value, subject to the assessment of sustainability!*





## THE RETURN OF CROWN PREFERENCE

The re-introduction of Crown Preference and the subsequent change in the order of priority of creditors on insolvency was originally due to come into force on 6 April 2020 and was delayed until 1 December 2020. As a result, certain tax debts are now treated as 'secondary preferential debts', placing HMRC ahead of other floating charge holders for amounts owed under VAT, PAYE and employee NICs.

This change is particularly relevant for wholesale and retail businesses with debt facilities where the lender has placed value on the inventory. The new legislation has come into force when HMRC payment arrears have been at an all-time high due to Government support. This may have had the impact of softening the impact of the change as lower levels of trading have resulted in businesses drawing far less on their ABL facilities.

The impact of the change in legislation will be felt to a far greater extent as we emerge from lockdown and the level of borrowing required increases, while HMRC deferrals remain high, affecting the ability of businesses to access cash.

Key impacts include:

- Lenders reviewing their security structure in line with the changes
- A move away from high street banks to more flexible independent ABL providers
- An increase in borrowers leveraging other balance sheet assets such as P&M and property
- Increase in cash flow lending.

### How have you seen lenders respond to the new Crown Preference Legislation?

**Adam Sookia:** *We've actually seen some quite different responses and behaviours from lenders since the change in legislation became effective, in particular for new refinancing processes. An important consideration is the timing of working capital pinch points against*

*the timing of peak HMRC arrears build up; we have seen examples of the inventory borrowing base being completely unaffected as the peak crown arrears timing coincides with a minimal inventory hold position. There is then a polarisation of lenders between those who are able to take the commercial view on the risk profile and quality of the underlying credit (and not increase reserves or security requirements) and those that are required to apply the relevant borrowing base reserves in line with their credit requirements.*

*Whilst the impact has been negligible on more traditional invoice discounting/fixed charge facilities, there remains a reasonable volume of revolving cash flow facilities that are monitored by way of debtor base loan to value covenants. These were slightly under the radar initially given their hybrid nature, but lenders are now seeking to strengthen the security requirement if the borrower wishes to preserve the LTV covenant ratios.*

*A potential positive side effect for lenders and businesses with material HMRC liabilities, is that we are seeing case studies of HMRC being more tolerate on payment plans given their improved creditor status, which could be an important lever is cash flow forecasting is looking tight.*

**Milton Guffogg:** *There has been increased focus on the quality and accuracy of company forecasts which predicates future tax liabilities. It goes without saying that companies with large outstanding tax balances will see their collateral value depleted and may find it difficult to obtain traditional asset-based financing facilities.*

*Potentially there will be changes in the price and quantum of debt available to a would-be borrower if there is less security available for a floating charge due to deferred tax balances. In layman's terms, debt will be more expensive and there will be less of it on offer, especially for rescue finance, which will become more difficult and more complex. The other impact of large tax balance deficits is on the reaction of credit insurers; many have reduced the available credit/insurance compounding the cash constraints on a business.*

**Andrew Knight:** *The initial reaction of most lenders in the months leading to the reintroduction of Crown Preference was to increase floating charge reserves in steps, with a view to restricting availability gradually in the hope that borrowers could adapt over time. While this has been a successful strategy in some cases, in others it has not been feasible and a different approach has been required.*

*In a number of these cases, borrowers have refinanced with lenders who are prepared to apply a more generous lending formula to floating charge assets such as inventory. In others, borrowers have been able to find lenders who are prepared to include within the borrowing base other asset classes, such as real estate, plant and machinery and (in extremis) intellectual property.*

*Quite a few asset-based lenders appear to have restricted their appetite for inventory lending in response to the changes and this has been a particular problem for borrowers in the retail sector specifically. These borrowers often cannot offer material collateral in any other form. We have seen more well-known retail brands attempting to borrow against the intellectual property in their brand names, but this is not universally acceptable to asset-based lenders and more often than not, funding against IP has had to be sourced from alternative and specialty finance lenders.*

### **How have lenders responded to the new Crown Preference Legislation where inventory makes up a significant proportion of their collateral?**

**Matt Warrilow:** *Inventory lending is not a large part of the SME market, but before crown preference, this often provided good security ("boot collateral") to enable more flexible and creative lending to be put in place to support a turnaround/transaction. Larger manufacturing companies (with more bespoke inventory financing) are already starting to feel the impact of this, which is effectively pushing shareholders into a position of needing to access more flexible sources of debt finance, or be prepared to "equity cure" a funding problem much earlier now than before this legislation.*

**Paul Flint:** *It is also worth noting that Work in Progress can take a variety of forms, many ABLs have provided very high advance rates as they have been able to get good recovery on unbilled time sheets in the manpower/recruitment sector. Advance rates of 95% plus have not been unusual, going forward the floating charge value of unbilled time sheets ("work in progress") could be significantly reduced and impact on funding levels. The crux is more likely to come as business needs working capital for emergence and growth and the debt capacity is limited due to the lack of a floating charge security cover.*

### **What actions have lenders taken to protect themselves as a result of these changes?**

**Andrew Knight:** *While gradually increasing floating charge reserves was a common strategy in the months leading up to the reintroduction of crown preference, this achieved mixed results. More recently, asset-based lenders have started to consider ways in which their collateral over floating charge assets such as inventory can be reconfigured to eliminate or reduce the impact of crown preference.*

*Where inventory is stored in third party warehouses, it is relatively straightforward to create fixed security although care needs to be taken to ensure that the lender is able to exercise the correct degree of control that is a prerequisite for a fixed charge.*

*Where inventory is kept in premises that the borrower controls, such as its own warehouse or in its retail shops, this is a more difficult proposition but much depends on the exact facts. For example, it may be possible to create a pledge over imported goods and then to permit the borrower to hold the goods pending their sale in the UK.*

"Since the introduction of crown preference, we have seen advisors discuss a number of different options to allow inventory to be lent against. Each option typically lends itself to a particular set of circumstances that could help a borrower leverage funding from its inventory base."

Robert Wakeford, BZ

## FUNDING DYNAMICS

Headroom will be key for businesses looking to manage the uncertainties that lie ahead.

However, high street banks may find themselves further constrained by CBILS and Recovery Loan Scheme activity and raise the threshold for new to bank lending.

Asset-based lending (ABL) is therefore likely to experience increased demand as businesses and their advisers look to independent and challenger bank ABLs for flexible solutions to navigate the route out of lockdown.

Wholesale businesses will predominantly use receivables facilities to meet their working capital requirements. The changes in the sector may also necessitate leveraging property and brand assets to provide lenders with the security to deliver the level of funding that businesses require to emerge from the pandemic, allowing them to stabilise, innovate and drive growth.

For retailers the options are more restricted as they often have no receivables. Inventory lending in some sectors such as fashion will be further hampered by seasonal stock which has not sold in line with normal patterns over the last 12 months and may therefore be valued at a lower level.

Increasingly, cash flow loans are being provided alongside asset-based lending to generate additional headroom, a flexible option to support businesses over the coming years.

This combination is already becoming a staple of a growing number of private equity sponsored deals.

Restructuring in the sector will be likely for those businesses that have struggled with the challenges identified. As Government support unwinds, ABL is ideally positioned to support a business through a restructuring process.

For businesses that require inventory funding there may be challenges resulting from the change in the Crown Preference legislation and lending criteria in the market. The following structures can be explored to increase access to funding by reducing the need for lenders to apply reserves against ABL facilities:

- **Fixed Charge Structure** – if goods are stored in a third-party warehouse the lender may be able to demonstrate sufficient control to establish a fixed charge over inventory.
- **Inventory Purchase Structure** – the lender purchases the inventory from the supplier or from the client. Title is passed back to the client upon sale of the goods and the lender is then repaid via cashflow or by transferring the exposure to an invoice finance facility.
- **Ring fenced SPV Structure** – floating charge assets are moved into an entity with no employees and no VAT liability.

**Government support has been at an all-time high in the last 12 months. To what extent do you think the unwinding of this support will be a key driver for businesses looking for new or increased funding?**

**Matt Warrilow:** *The (March) budget provided further extensions of support, which particularly for SMEs, will provide more time and flexibility to assess how they can cope with the new environment post-lockdown. Larger companies with more complex capital structures (restricting access to Government loans) need to now work out whether they can 'stand on their own two feet' without any refinancing/restructuring plans being put in place. Many will need new external funding for growth sourced from outside the traditional banking market, underpinned by a clear articulation of the merits of the post-lockdown business plan and the quality/flexibility of the asset base.*

## How have you seen the volumes of businesses needing new funding change over the last 12 months? How has Government support impacted this?

**Adam Sookia:** We've seen changes both for better and worse depending on the nature of the transaction:

**M&A** – we saw a clear slowdown in M&A linked activity and Acquisition Finance in Q1 and Q2 2020, with shareholders either deferring the process (helping to drive a bumper Q3/ Q4) or choosing to complete a refinancing to enable Shareholders to take cash out or repay higher yielding loan notes. Q3 and Q4 2020 then saw a surge of M&A driven financing activity and a return to Pre-Covid levels of commercial terms and competitiveness – especially across ABLs and Private Debt Funds. This continued into Q1 2021 as vendors were seeking to pre-empt potentially adverse changes to CGT.

**Liquidity** – naturally there was a significant uptick in businesses requiring access to liquidity for headroom or to manage working capital needs, however the impact of government support schemes meant the size and timing of liquidity requirements became quite an iterative process. Within a month of the implementation of government support schemes (e.g. furlough), c.50% of our clients that had started investigating liquidity options were comfortable they no longer required this.

**Working capital** – one common theme across our clients when forecasting working capital requirements was the need to make payments above and beyond what was commercially required to suppliers to ensure their survival. Certain sectors (e.g. door and interior manufacturers in Italy) were reliant on continued payment (or payment in advance) to ensure viability and continuity of supply – often in capacity as a sole supplier to a UK distributor. The other interesting feature from a working capital perspective is that some sectors are now thriving under pandemic conditions, causing unprecedented levels of growth and associated pressures on cash management.

**Pricing** – businesses have been paying a significant premium for freight following supply/demand imbalances caused by Covid and Brexit. This has driven either a strain on margins or a need to consolidate SKUs – both of which have led to cashflow challenges.

**Government funding** – there's no doubt the various government funding schemes have been hugely helpful in supporting businesses over the past 12 months. Not just in terms of accessing new funding, but also in allowing incumbent lenders to be more supportive than they otherwise could have been. That said, equally helpful was incumbent lenders providing access to liquidity within the confines of existing docs, e.g. capital repayment holidays or deferring cash flow sweeps.

## What role do you think asset-based lending will play in the recovery of retail and wholesale sectors in the next 24 months?

**Matthew Holt:** Whilst the new preference rules will make inventory financing difficult for a number of ABL's, there will still be an important role for ABL's / Alternative Lenders in financing these sectors as they recover and work through the inevitable working capital challenges the pandemic will have left them with. As businesses seek to rebalance their inventories and credit terms become even harder to secure from Asian supply chains, the demand for creative lending packages, secured on real assets is likely to increase. It remains uncertain, how changes in the statutory environment will impact on this need, however, ABL financing has always been highly adaptive to such changes.

**Andrew Knight:** Retail and wholesale businesses ultimately depend on one thing: consumers buying products. In that respect, they have faced a perfect storm over the past 12 months. The COVID-19 pandemic has severely impacted their route to market, with non-essential retail outlets being either closed or, when open, operating under capacity restrictions. Only those businesses with a strong online presence have been able to keep goods flowing out of the door at the same rate as before. Meanwhile, the end of the transitional Brexit period has seen many businesses struggle with increased import and export paperwork and significant delays in the supply chain.

The UK Government's VAT deferral scheme, which was a vital policy intervention to help businesses deal with the cash flow impact of these issues, has created difficulties of its own by causing a massive build-up – estimated at over £30 billion by the end of 2020 – of unpaid taxes which now fall within the scope of Crown Preference and therefore operate as a material disincentive to secured lenders who may find their claims rank behind those of HMRC.

The core collateral class for most UK asset-based lenders has always been, and remains, a business's unpaid receivables. Where these are purchased, as they frequently are by UK asset-based lenders, the impact of Crown Preference is nil or negligible. Problems begin when asset-based lenders need to offer additional finance availability to their customers on the basis of assets such as inventory, which have classically been floating charge assets.

The issue is exacerbated in the retail sector: most retailers have very few receivables over and above card payment receivables which are usually paid in a short time and in contrast they often hold significant quantities of inventory.

Asset-based lenders can play a meaningful role in assisting the recovery of retailers, but only if they can obtain the security they need. Retailers in turn need to recognise that their business model may need to change if they require access to finance. In particular, the tendency to hold high levels of goods in retail shops and in warehouses controlled by the retailer is not helpful to lenders or to their borrowers.

Wholesalers may be in a more favourable position, especially where goods are supplied in bulk and sold on credit terms to retailers. Asset-based lenders will view especially favourably any wholesale business that imports goods and holds them in third party logistics warehouses, a methodology which opens up a range of possibilities for taking security in such a way as to protect the lender from the impact of Crown Preference.

### **What are the main factors for businesses carrying large levels of inventory to consider when seeking funding?**

**Milton Guffogg:** The quality and age of inventory held is of paramount importance. As a result of COVID-19, many retailers are holding large quantities of legacy inventory which they have been unable to sell given the prolonged closure of all non-essential stores.

A higher level of discounting is required to sell legacy inventory, decreasing the value of collateral available to lenders.

Further, the value of inventory is largely impacted by the capacity to sell through available channels, which is

driven by consumer demand. If footfall in physical stores continues to wane as lockdown eases, and web sales do not make up for the loss of sales in stores, different sales channels will need to be considered, often leading to much lower recoveries.

Lastly, the importance of brand value should not be underestimated. Inventory backed by a good brand will increase achievable recovery levels and can also be used to lend against as fixed asset collateral.

### **Do you expect to see an increase in the restructuring of these businesses over the next 12 months?**

**Alex Williams:** As Government support for business reaches an end, there are likely to be numerous businesses that will require significant restructuring. Many of these will be retailers who have been unable to manage the rapid channel shift as well as those with a market proposition significantly less relevant than it was 12-18 months ago.

### **Do you anticipate seeing high levels of restructuring for businesses with large inventory holdings within the next year?**

**Mike Denny:** I think that will depend on the sector, the rationale for the inventory build and the ability to turn stock quickly if required. We saw a number of manufacturers choose to build stocks over Q3 and Q4 2020 given the Brexit uncertainty. In normal market conditions this could be unwound in a controlled manner, but customer demand schedules remain very difficult to predict and inflationary raw material prices, under-supply and escalating freight costs are each weighing hard on supply chain strategies.

By contrast, the stock overhang for fashion retailers is involuntary. The nature of product is such that in many cases this cannot now be shifted until at least Q3 / Q4 2021, and in all likelihood at the expense of margin. Across all sectors, a clear understanding of how to manage and fund working capital will be key over the next 12 months. Getting this wrong will stymie the ability to recover quickly and risk creating cash issues that are insurmountable.

**How do you think the role of ABL will change in the corporate finance market after the disruption caused by the pandemic?**

**Matthew Holt:** *ABL financing will become an even more important component in a number of companies' financing structures, as they look to free up cash flow tied up within their working capital to facilitate recovery and growth post pandemic. In addition, the economic shock caused by the pandemic, and its consequential impact on earnings will mean that traditional leverage finance will be harder to secure. Accordingly, it is likely that the relative attractiveness of ABL finance vs other financing routes will be enhanced.*

**Andy Miller:** *I suspect we will see more activity as businesses encounter working capital issues as they build back their businesses and Government support initiatives are phased out. ABL facilities will undoubtedly help cash flow problems for certain, asset rich business in that regard, particularly where business are unable to secure cash flow lending.*

**“Unsurprisingly given the special situations nature of our lending, BZ has seen a large number of retail business seeking funding in the last 12 months. We have completed 3 transactions totalling £155m of facility limits where maximising the funding availability from inventory was a key initial request from our client.”**

Robert Wakeford, BZ



## CONCLUSION

COVID-19 has had an immense impact on an already challenged retail sector, accelerating many of the structural changes already under way. Even before the crisis, many retailers and high street stores were struggling to survive with rising overheads, high rental costs, declining store footfall and the ease and convenience of online shopping all contributing to the well-publicised decline of the high street.

There have been huge changes and challenges facing the sector and doubtless more lie ahead as businesses emerge from the pandemic. The heightened focus on supply chain resilience will stand the industry in good stead in the long term.

Government support has been key to survival for many businesses, particularly in the retail sector, and this will need to be extended and unwound carefully when the time is right to support businesses adapting to post lockdown trading.

Forecasting will continue to be difficult and liquidity will be key to navigating uncertainty in the months and years ahead.

Funding options for the sector have been impacted by legislation, however, there remains a strong independent lending market to provide flexible and innovative solutions.

### CITATIONS

**CIPS. Delays at the UK/EU Border increase as new customs paperwork continues to cause problems. (2021 February 24)** from <https://www.cips.org/who-we-are/news/delays-at-the-ukeu-border-increase-as-new-customs-paperwork-continues-to-cause-problems/>

**Scott, D. ONS. UK trade: February 2021 (2021, April 12)** from <https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/bulletins/uktrade/february2021>

**Make UK. Govt urged to address border delays and red tape. (2021, February 1)** from <https://www.makeuk.org/news-and-events/news/govt-urged-to-address-border-delays-and-red-tape>



## ABOUT US

Management teams, leading advisers and private equity groups trust BZ to deliver innovative, multi-jurisdictional asset-based lending and cashflow solutions that make a difference.

BZ's experienced team brings trusted expertise and a relationship-driven approach to every aspect of deal execution, ensuring certainty and creativity.

### MAXIMISING VALUE. MINIMISING EXECUTION RISK.

- Up to £150m full underwrite and hold
- No asset class mix restrictions
- Sector agnostic
- Additional cashflow lends considered
- Cross border
- Flexible facility terms

**If you have a debt capital opportunity you would like to discuss with us, please contact us today.**

+44 (0)20 3786 6101

[WWW.BZCF.CO.UK](http://WWW.BZCF.CO.UK)



## LATEST SECTOR LENDING NEWS

### BZ LEADS INNOVATIVE 'CLUB DEAL' TO SECURE £90M FUNDING LINE FOR EVO BUSINESS SUPPLIES

Specialist asset-based lender, BZ has completed a £90m refinance of EVO Business Supplies ('EVO'). The facility included a £9m structured term loan. BZ led the structuring and financing of the substantial facility, working with club partner, Leumi ABL. The flexible asset-based lending deal will see EVO, the UK's largest multi-channel distributor of business supplies and services with sales in excess of £450m, focus on driving further rapid growth.

EVO is a portfolio company of Endless, a transformational UK private equity investor. The business provides sourcing, storage, specialist and value-added fulfilment services to over 2,000 resellers, in addition to retailers, large public sector bodies and corporate organisations through its trading brands VOW and Banner. The product offering spans the full range of business critical supplies, from traditional office supplies to EOS, facilities supplies, technology, furniture and specialist consumables. EVO has recently added new infection control lines such as face masks, sanitising gel and gloves to its extensive product offering and has seen its online business expand significantly since the onset of the pandemic.

**Andrew Gale, Group Finance Director, EVO Business Supplies Limited, said:** *"The requirement to transact quickly is critical to EVO as we continually look to maximise strategic opportunities to drive scale. From our first meeting with BZ, the team's credibility, professionalism and experience was evident and the process just flowed. Their short lines of communication, openness and transparency and the involvement of the wider team were refreshing and brought us confidence from the outset. They understood what we were looking to achieve and put a compelling offer and 'club deal' structure on the table that would provide both the optimal funding mix and the platform and capacity for EVO to support further organic growth and future acquisitions. In just a few months, we believe we have built the foundations for a strong, long-term partnership that will enable us to move forward and grow together."*

**Andrew Ross, Partner, Endless LLP, said:** *"BZ responded positively with a deliverable ABL 'club deal' structure to ensure that EVO is appropriately capitalised to take maximum advantage of opportunities in its evolving marketplace. The additional headroom created by the combined facility will enable EVO's management team to concentrate on further accelerating P&L growth and enterprise value in the medium term without constraint. The team at BZ was very straightforward to work with and having direct access to the decision makers and influencers, including their credit function, figured strongly in the successful completion of the deal."*

**Commenting on the deal, Robert Wakeford, Managing Director, UK Sales at BZ, said:** *"We never forget that today businesses have many and diverse financing options available to them and we are delighted to have structured an innovative funding solution in support of EVO's growth objectives. The business has a highly efficient operating model and has grown to be a market leader in each of its chosen market segments. We were excited to have the opportunity to lead this substantial transaction, which will allow the business to maximise opportunities for expansion within its £19bn addressable market."*

**Ben Milner, Regional Business Development Director, BZ, commented:** *"The team at EVO Business Supplies is dedicated to the UK and Ireland office supplies market with a clear strategy and an uncompromising focus on the sector. It has been a pleasure to support the management team and Endless and we look forward to working closely with them as they take the business to a new level of growth."*





## KEY CONTACTS



### PETER JAFFE

Chief Executive Officer  
[pjaffe@bzcf.co.uk](mailto:pjaffe@bzcf.co.uk)  
+44 (0)7769 640965



### RUSSELL GILLING

Managing Director  
[rgilling@bzcf.co.uk](mailto:rgilling@bzcf.co.uk)  
+44 (0)7305 535562



### BEN MILNER

Managing Director  
[bmilner@bzcf.co.uk](mailto:bmilner@bzcf.co.uk)  
+44 (0)7500 771186



### CEM YASLAK

Director  
[cyaslak@bzcf.co.uk](mailto:cyaslak@bzcf.co.uk)  
+44 (0)7908 653067



### DUNCAN MAYBURY

Associate  
[dmaybury@bzcf.co.uk](mailto:dmaybury@bzcf.co.uk)  
+44 (0)7377 437740