

2 ANNUAL FACTORING SURVEY 4

Report of Findings

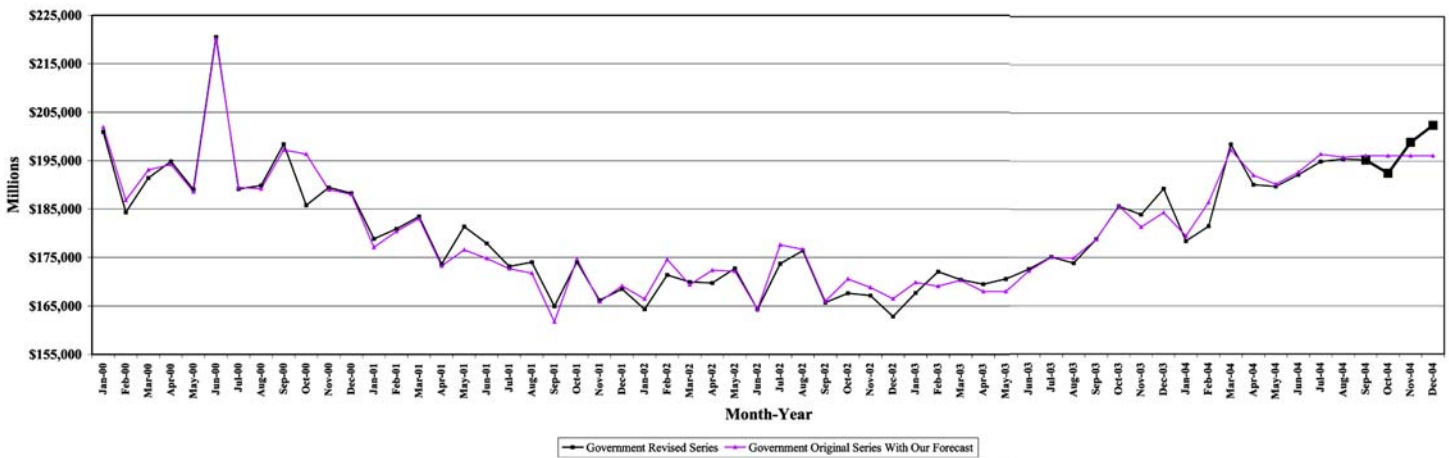
1) 2004 marks the first time in the long history of factoring that its volume crossed the \$100-billion barrier. The prediction in Part III of 2003's survey was for a modest gain of between 1.75% - 2.75% for 2004. In fact, as shown in **Appendix Exhibit 1**, the actual growth rate was 7.49% year-over-year to a total of \$103.23 billion, the largest increase since the final pre-recession gain of 13.22% in 2000.

What caused this unanticipated growth in 2004 and will it occur again in 2005? The best way to review the first part of this

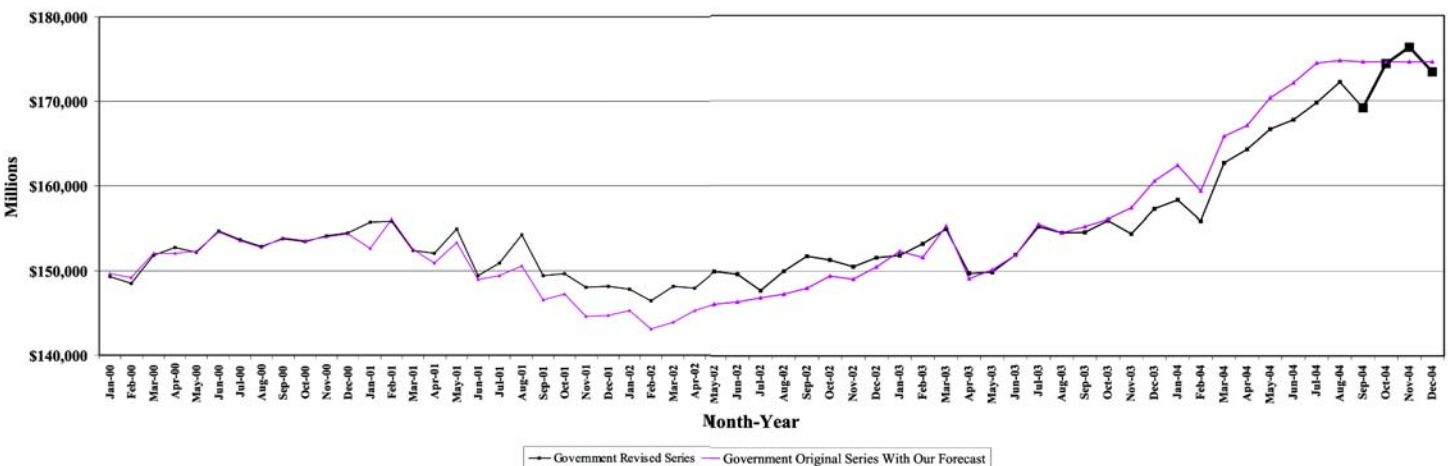
question is to examine the differences between the economic forecasts for 2004 and that which actually occurred at that time. The last part of our query will be addressed in the final section of the report.

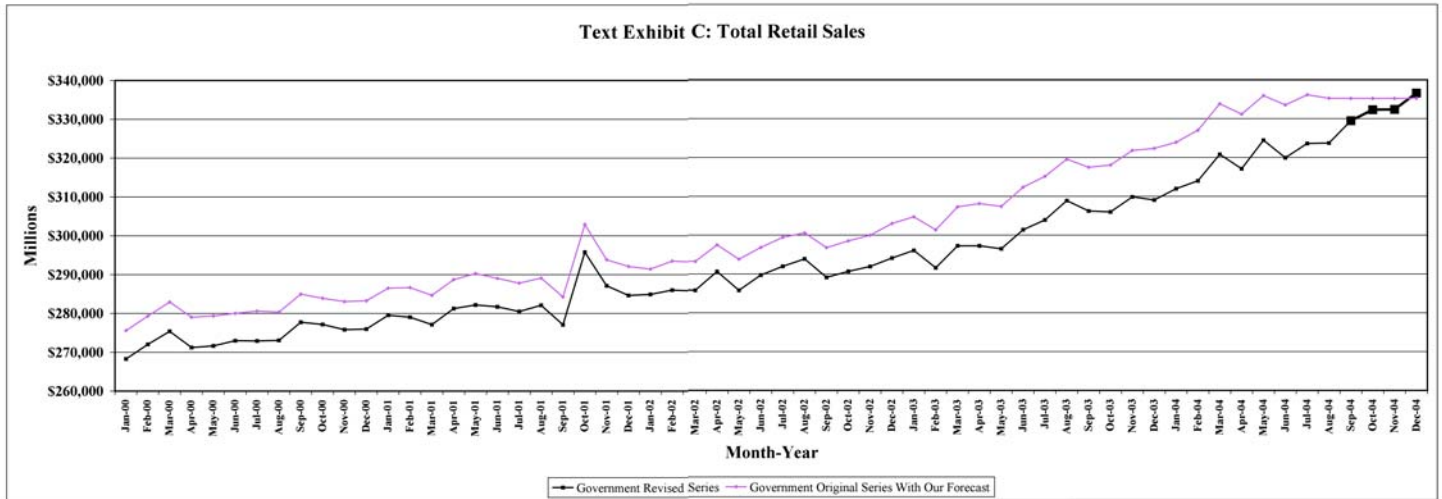
2) As shown in **Text Exhibit A and B**, there was an unexpected jump in non-durable and durable goods new orders in the last four months of 2004. In total, these orders were up by \$11.65 billion over the forecast amount and that difference played an important role in increasing factoring volume. Additionally,

Text Exhibit A: Manufacturing Durable New Orders



Text Exhibit B: Manufacturing Nondurable New Orders



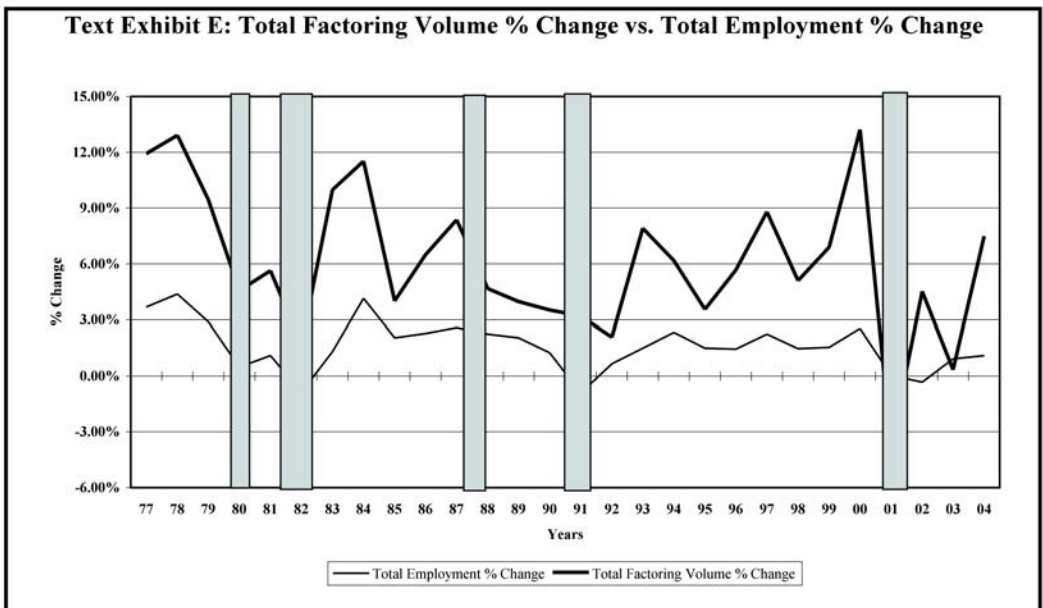
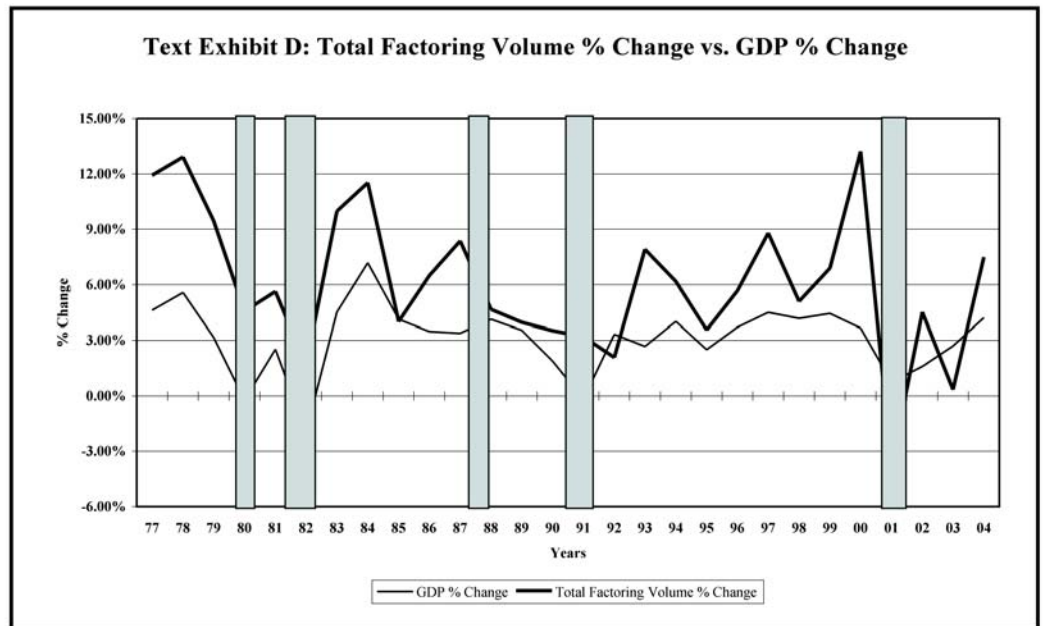


continued movements in these measures through the first eight months of 2005 will be shown at the end of this report to be important indicators of the direction of factoring volume.

Similarly, as shown in **Text Exhibit C**, retail sales also moved ahead briskly in the last four months of 2004 while the forecast was for virtually flat sales during that period.

Consumer demand for goods and services remained very strong despite the substantial rise in gasoline and housing prices, healthcare costs, and the moderate rise in interest rates that continued during the final four months of 2004. And, given the strong focus of commercial factors on lending to the apparel, textile, footwear, and furniture industries, traditionally strong consumer-oriented segments at between 53.3% (2004) and 63.3% (2003) of total volume, one can see why these drove the industry's total volume to its new record high.

As shown in **Text Exhibits D and E**, over the years, gross domestic product and total employment have been strong coincident leading indicators of changes in factoring volume. However, as shown in the exhibits, coming out



of the 2001-2002 recession, factoring volume declined sharply in 2003 although GDP and total employment did not. At the time, the analysis was based on excessive cash hoarding by businesses, low interest rates, slow job growth, lowered wage, ever-rising fuel costs and the strong movement of textile, apparel and furniture manufacturing overseas. As it turned out, some of these conditions changed during the year while others, such as the fuel price increases, did not have the expected impact on the economy.

3) Turning next to **Appendix Exhibit 2** we examine another aspect of our factoring results — the variability of its volume over time. The top graph shows the volume of factoring that has been generated by the industry over the 29 years that the SFNet has been tracking it. As you will notice, the last five years have been more erratic than in the past. Year 2000 exhibited the highest rate of growth ever — +13.22% — just prior to the recession and 9/11 that occurred in 2001. That year produced the first decline experienced by the industry (-3.72%). As shown in the exhibit, 2004 shows an increase that tracks at a higher rate of increase than the long-term trend. However, the atypical variability of these movements since 1999 makes prediction of factoring volume more difficult than in the past. The high variability is shown to be even more pronounced and more unusual in the bottom graph in **Appendix Exhibit 2**. There, changes in each year's factoring volume are presented.

4) As indicated earlier in this report, the outward movement of textile, apparel, footwear, and furniture manufacturers to East Asia and Mexico as well as the impact of their resultant export competition in the United States have cut into the Upper and Lower Northeast as well as the Eastern Southeast regions. Nevertheless, in 2004, all three of these regions followed the overall industry trend by exhibiting growth in Total Factoring Volume, from growth in other manufacturing and retail business segments as well as service related fields. **Appendix Exhibit 3** breaks down 2004's volume of factoring into all of our regions and compares the changes that have occurred in each since 2003.

Overall, performance in the volume of factoring across the United States and Canada has been overwhelmingly positive. The only region in North America that had a decline in factoring volume in 2004 was the Plains States, the smallest region in the survey. While total factoring volume grew by 7.49% throughout the world in 2004, in the United States, it rose at a rate of 10.09%. Canada increased by 63.32%. The Other International regions experienced a significant loss of -37.21%. However, the estimates for this area are not statistically reliable due to limited available data regarding the industry's activities in Europe, the Far East, and elsewhere overseas.

As can be seen in **Appendix Exhibit 3**, the regions generally fall into three tiers. The top three areas — the Lower Northeast, the Far West, and the Eastern Southeast, — account for 77.38% of the total volume. The second tier — the Southwest, Canada, the

Eastern Midwest, the Western Southeast, and the Other International (overseas)— comprise another 18% of total volume. And, finally, the smallest group — the Upper Northeast, the Middle Atlantic, the Western Midwest, the Northwest, and the Plain States — make up the remainder of the volume.

Below is the detailed discussion of the volume of factoring activity that took place in each of these locales. They are presented in order of the total volume of factoring which they generated in 2004. However, the "Other International" delineation that contains all of the other areas of the world is included last because of the broad and general boundaries it covers. The list of the volumes of factoring accounted for by each region in 2003 and 2004 as well as the percentage changes in them over these years is presented in **Appendix Exhibit 3**.

5) Lower Northeast: This is the most dominant of the 13 regions. It comprised 41.86% of all factoring volume in 2004, more than twice that of the second largest region, the Far West, which accounted for 20.83% of 2004's total. As shown in **Appendix Exhibit 3**, volume here rose by 6.48% over 2003. The decline in textile and soft goods manufacturing located there was the primary cause in its somewhat muted performance. This was offset to some extent by the increase in other manufacturing activity that rose moderately in the region, especially among firms producing plastic products, electrical equipment and food items. In addition, stronger growth in other retail and wholesale industries as well as in the service sector helped to boost the volume of factored lending that took place there in 2004.

Far West: The second largest of the 13 regions examined. Factoring in the Far West is quite different than that carried out in its counterpart above. Factoring volume in this region was half that of the Lower Northeast and had the slowest growth rate of any region at 5.45%. This region had a large concentration of defense contracting and manufacturing, technology and services. Although these manufacturing and service-related industries grew in 2004, their growth there was tempered somewhat by high tax rates, skyrocketing energy costs, and rising health insurance costs that especially impacted California and Hawaii.

Eastern Southeast: This region, which had been flat in 2003, grew much more briskly in 2004 at a rate of 13.12% or nearly \$1.8 billion. Although it was hurt by the same weakened apparel, textile, footwear, and especially furniture industries as were both the Upper and Lower Northeast Regions, growth in other manufacturing industries, distribution and transportation, and in service industries boosted this region's overall performance. Positive economic conditions in North Carolina and Georgia had a strong impact on the level of factoring activity in this region. In 2004, North Carolina exhibited fairly strong growth in its Gross State Product(GSP), rising at 6.32% in 2004 over 2003. In addition, North Carolina had a drop in its unemployment rate from 6.5% in 2003 to 5.5% in 2004. Georgia also had strong growth with its GSP increasing by 6.08%. The unemployment rate in Georgia has remained fairly low at 4.6%.

Southwest: This region had the third highest growth rate of any United States region, rising by 39.12% or \$1.15 billion in 2004. This area is characterized by the wide variety of businesses that operate there — oil and gas, farming and livestock, and a mixed assortment of manufacturing businesses. However, high production costs, primarily driven by fuel, shipping, and raw material prices, have hindered firms in this region, especially in Texas, which most likely has the highest level of factoring in this region. 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 it fell 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. On the other hand, the strong growth in factoring in this region appears to have been the result of companies there shortening up their liquidity financing by switching from asset-based lending to factoring, especially given the continued weakened economic climate in Texas, its principle member.

Canada: In total, the volume of Canadian factoring is nearly as large as that carried out in the Southwest. However, the types of businesses that use this financing tool are different there. Canada is much more of a service-oriented economy than is the United States. Approximately 68.7% of its real GDP is accounted for by this sector. Manufacturing and construction make up 22.88%; wholesale, retail, and distribution comprises 16.81%; while services constitute 51.93% of its total GDP. (The remainder is accounted for by minerals extraction, utilities, and agriculture and forestry, in that order.) As indicated in **Appendix Exhibit 3**, Canada had the second largest growth rate of any of the 13 regions rising by 63.32%, or nearly \$1.6 billion in factoring volume in 2004.

Eastern Midwest: Known primarily as the center of heavy manufacturing in the United States as well as being an area that is also dominated by agriculture, livestock, and light manufacturing businesses, factoring in the Eastern Midwest grew by \$500 million or 20.05% in 2004. This was a rebound from the -10.79% decline that this region suffered in 2003. The Eastern Midwest comprises 2.92% of all factoring.

Western Southeast: Often considered to be a part of the Deep South, this region is characterized by traditional crop production. Such production remained steady in 2004 due to stable demand and weather. However, factoring there continued to grow as a result of the movement of businesses to this area and their consequent demand for financing. Thus, factoring volume rose by 20.15% or \$385 million in 2004.

Upper Northeast: This area of the United States also rebounded from 2003's large decline. Although it was hit by its portion of the same losses indicated in the soft goods manufacturing industry in the Lower Northeast, growth in nontraditional factoring industries were enough to lift the region's use of factoring by 7.83%, or \$107 million over 2003.

Middle Atlantic: For the second year in a row, the Middle Atlantic region had the highest growth rate of the 13 locales examined. By far the smallest in physical size, it is nevertheless located strategically in the hub of the East Coast. It contains businesses of all sizes and types including vegetable, livestock, crop production, high technology, consulting, chemical manufacturing, electronics, and tool and industrial machinery manufacturing. The use of factoring there is small because of the relatively few number of businesses located there. There are only 501 client/customers there that fund a portion of their business activities with factoring (**see Appendix Exhibit 4**). Nevertheless, this number represents an increase of 169.35% over the number of clients in the region in 2003. Because of the small size of the states located there and their strategic locations, real estate costs are very high and they assess very high business and income tax rates. This has the effect of limiting the number of firms that might otherwise use factoring. Despite that, this relatively high growth in the number of businesses using factoring there produced the highest rate of growth in factoring volume among all regions this year at 113.89%, or \$697 million.

Western Midwest: Like its neighbor, the Eastern Midwest, this region recovered from a substantial decline in 2003. Improved economic conditions gave the Western Midwest the second highest growth rate of any United States region, 51.48%, or \$348 million in 2004. Growth took place despite the general trend of declining clients/customers that occurred throughout the industry in 2004. The region accounts for only about 1.00% of all factoring activity.

Northwest: The Northwest region had a growth rate of 6.99% or \$54 million in 2004. The total volume of factoring generated by the region was only \$826 million.

Plains States: This area makes the smallest use of factoring of any of the regions tracked. Its volume in 2004 was only \$137 million, and it experienced the only decline of any United States region. Factoring there fell by 48.11%; \$127 million below that of 2003. This region accounts for only 0.13% of all factoring activity. (**See Appendix Exhibit 4**)

Other International: We receive only very limited information as to the factoring activities that are generated throughout this massive area and estimates are not statistically reliable.

Also assessed by region is the number of client/companies that have factored funds in 2004. This information is presented next in **Appendix Exhibit 4**.

6) As indicated by the data compiled there, the number of such firms declined by 1,915 or 11.73% between 2003 and 2004. Although drops occurred in six of the eleven United States regions as well as in Canada and the Other International area, five United States regions did experience gains.

The Far West Region, which has had the most clients/customers using factoring over the past two years, fell into second place in 2004 as this region lost 1,580 firms, a decline of 35.68%. This resulted in the Lower Northeast, an area in which the volume of factoring has remained roughly flat, to move into the top spot in terms of the number of clients/customers.

The most significant growth rates in terms of clients/customers took place in the Middle Atlantic and Western Southeast regions with growth rates of 169.35% and 48.58%, respectively. A comparison with **Appendix Exhibit 3** reveals that within both of these regions, the factoring per client/customer ratio fell by about 20%.

Part II — Special Attributes Section

7) Weighted Average Length of Time to Accounts Receivable Collection:

In 2004 it took the industry an average of 53.71 days to collect its factored receivables, or approximately seven days longer than in 2003. This was back to about the same level (54 days) as the post-recession year of 2002.

8) Weighted Average Advance Rate on Purchased Receivables:

The average advance rate on such receivables in 2004 was 84.27%. In 2003, it was 80.99%. In combination, these two sets of results indicate that while the Industry was willing to lend more against the typical value of each instrument, its collection success was more protracted. Furthermore, these data imply that the industry was willing to take somewhat larger risks due to the continued strong economic atmosphere.

The next two attributes of 2004's factoring activity involve both the sectors and industries in which its financial services are provided. A sector represents a general economic division into which individual industries are grouped according to the similarity of the business activities in which they are engaged.

9) Factoring by Economic Sector:

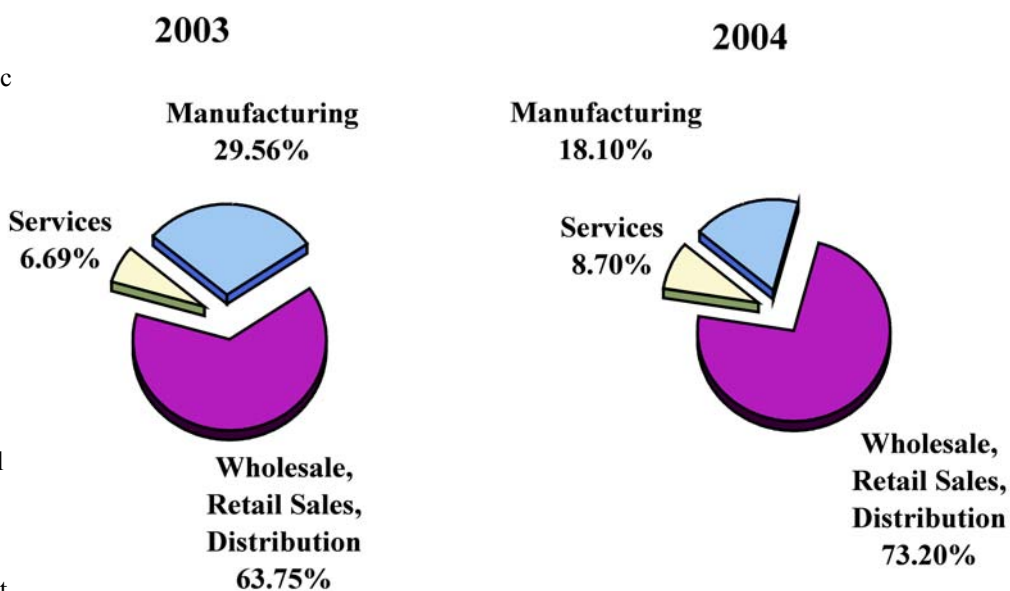
Text Exhibit F below provides a pie chart comparison of the volumes of factoring that were directed to three broad categories of industries in 2003 and 2004 — Wholesale, Retail Sales, and Distribution; Manufacturing; and Services. As can be seen there, by far the largest portion of factoring is generated within the first

sector. It includes sales at all levels of textiles, apparel, footwear, furniture and other goods, the warehousing and distribution of such goods, other forms of intermodal transport, and other related types of businesses. In 2002 and 2003, the first two years in which this breakdown was prepared, this broad-based segment of business comprised between 63.75% and 65.27% of total factoring volume. However, in 2004 it jumped to 73.20% of the total. As a whole, this segment accounted for \$75.6 billion of all factoring.

The manufacturing sector is composed of both durable and nondurable goods production, chemicals, shipbuilding & repair, mineral extraction, construction, medical equipment and electronics. Production items range from heavy machinery to that sold over the counter, including those which are provided to customers in the above sector. Factoring in this spectrum has moved in the opposite direction from that of the first grouping. After having comprised a steady portion of such borrowing at approximately 28.5 - 29.5% of the total in 2002 and 2003, manufacturing slipped to only 18.1% of the total volume in 2004. As such, it represented \$18.7 billion in factored financing in 2004. However, as shown in **Text Exhibits C and D** earlier, the strong growth in new orders especially in the second half of 2004 appears likely to propel factoring in this sector back to its former volume in 2005.

The remaining sector, i.e., services, includes communication, printing, information technology, medical and dental practices, legal practices, various types of business and other consulting, temporary staffing and employment services, and marketing and advertising agencies. It has continued to account for a small, but growing portion of such borrowing. Over the last three years it has grown at a compound rate of 22.14% to nearly \$9.0 billion.

Text Exhibit F: Factoring By Economic Sector



10) Factoring by Specific Industries:

By far the largest decline in factoring volume occurred in the apparel, textile, footwear, and furniture industries combined. Traditionally the most important industries that factor their various instruments of sale, such borrowing in these segments fell substantially as a proportion of 2004's total. It fell from 63.32% to 53.33% between the two years. In 2003 these industries accounted for \$60.8 billion of the industry's total lending. In 2004 it fell to \$55.1 billion. All of this decline was in the manufacturing phases of these industries and was the reason why the sector experienced the reduction in factoring volume discussed earlier. In combination, the remaining manufacturing segments increased their use of factoring by 40.46% from 2003's total of \$8.29 billion (8.64%) to 2004's \$11.65 billion total.

Two other industries that also make significant use of factoring are in the related areas of distribution and transportation. The second in size was that grouped in the two exhibits into "Other Services". Firms involved in communication, printing, healthcare, law, consulting, and marketing and advertising are included herein. Although they, in total, represent only a small fraction of factoring by the industry, between 2003 and 2004 their volumes grew by \$2.4 billion.

With the exception of the industry's more traditional business segment borrowers, i.e., apparel, textiles, etc., all of the remaining industries exhibited increases in their use of factoring. These include information and technology (\$365.1 million), other wholesale (\$1.08 billion), other retail (\$1.14 billion), staffing (\$884.6 million), and unidentifiable other industries, i.e., that which was not specifically identified by survey respondents, (\$861.3 million).

11) Domestic Versus Foreign Factoring:

As can be seen in **Text Exhibit G**, the overwhelming majority of factoring that was reported for 2004 was conducted within the lender's local country. Virtually all of the volume that was reported upon was issued to local United States or to local Canadian businesses. In total, this accounted for \$96.6 billion, or nearly the total volume of factoring from all locations reported in 2003. As shown in the pie chart, this amounted to 93.57% of all factoring in 2004, almost identical to 2003's 93.66%. As also shown there, factored financing to firms

importing from foreign countries comprised only 4.46% of 2004's total. Factoring for purposes of exporting accounted for only 1.65% of the total. The small remainder, factoring to firms whose activities were conducted solely outside of their country of origin amounted to only 0.32% of all factoring.

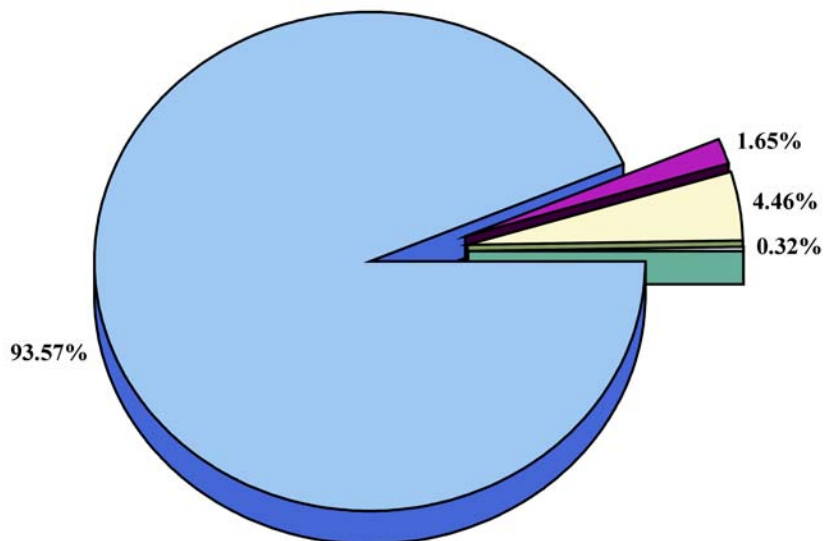
12) Levels of Recourse Factoring:

Under full recourse, the client/customer is held ultimately responsible for all buyer defaults on the instruments of sale that the factor purchased. At the opposite extreme, the factor assumes full responsibility for all collection losses associated with its sale instrument purchases from its client/customer. As can be seen in **Text Exhibit H**, there has been a substantial switch in the degree to which factors have been willing to finance sale instruments over 2004. Between 2003 and 2004, non-recourse factoring fell from 74.55% of all transactions to only 59.00% of them. At the same time, both full and partial recourse arrangements rose substantially. Between 2003 and 2004 the portion of factored sales for which client/customers were held at least partially responsible nearly doubled. In 2003, they totaled \$25.45 billion, against \$41 billion in 2004. The shift is a reflection of the increased risk of the economy, the longer collection times and the number of business bankruptcies that took place during the year.

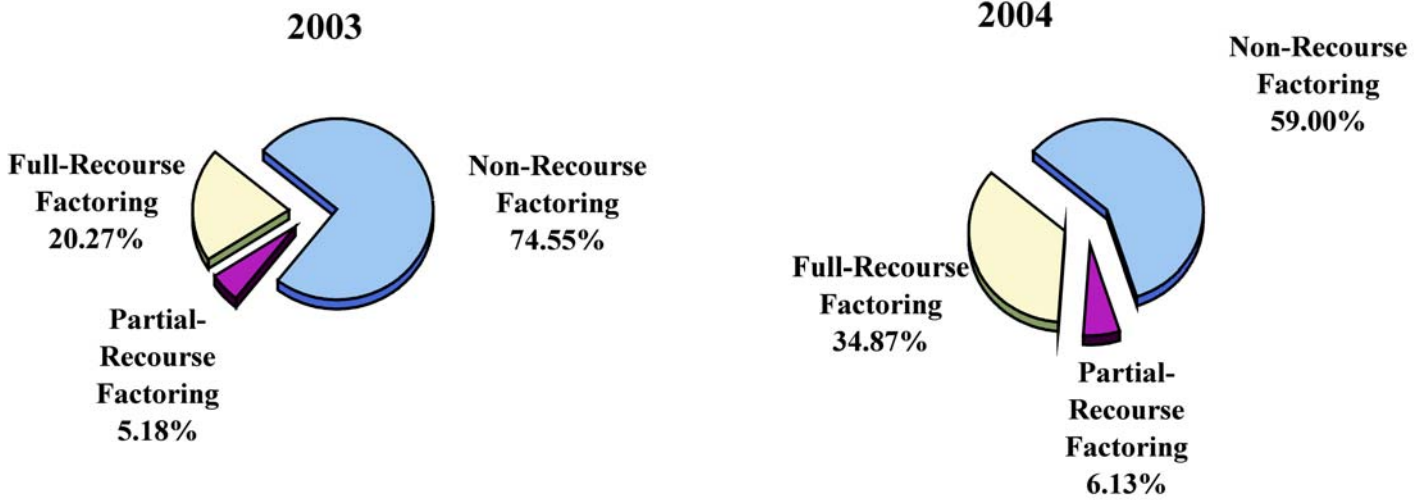
13) Forms of Notification Factoring:

As indicated in **Text Exhibit I**, notification factoring continues to be a much more popular arrangement for factoring deals than that based on non-notification. In 2003, 82.14% or nearly \$78.9

Text Exhibit G: Domestic vs. Export, Import & Foreign Breakdown For 2004



Text Exhibit H: Types of Recourse Factoring



billion of all factoring was done with notification. In 2004, it grew to 88.29% of the total, or over \$91.1 billion.

Having completed our review of 2004's factoring activity, we turn last to the forecast for 2005.

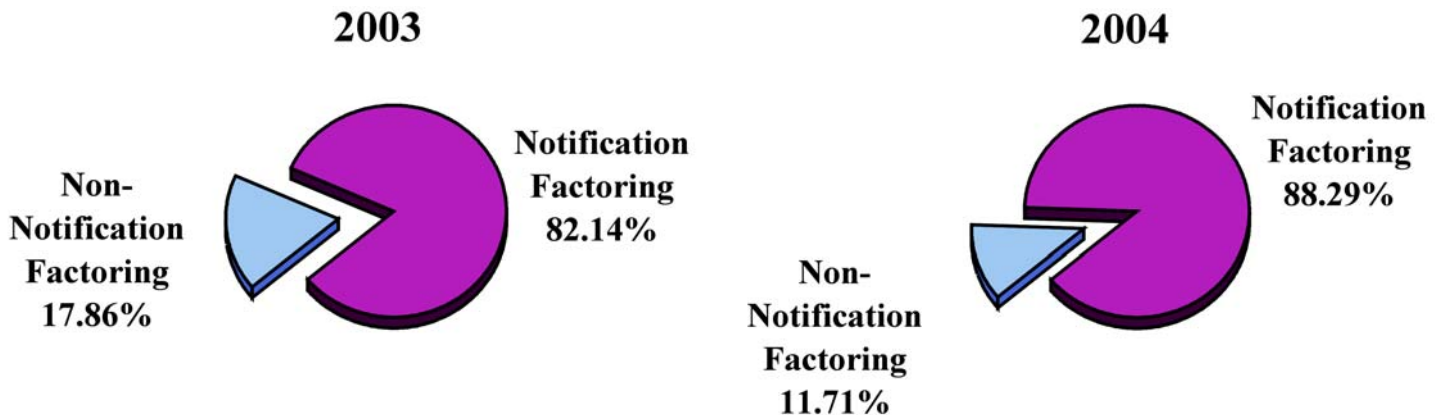
Part III — Forecast for 2005

While the outlook for the economy in the United States is somewhat cloudy for the final quarter of 2005, as of this writing the outlook for factoring for the whole of 2005 is not. In fact, it is quite positive. It is also similarly so for Canada, although its

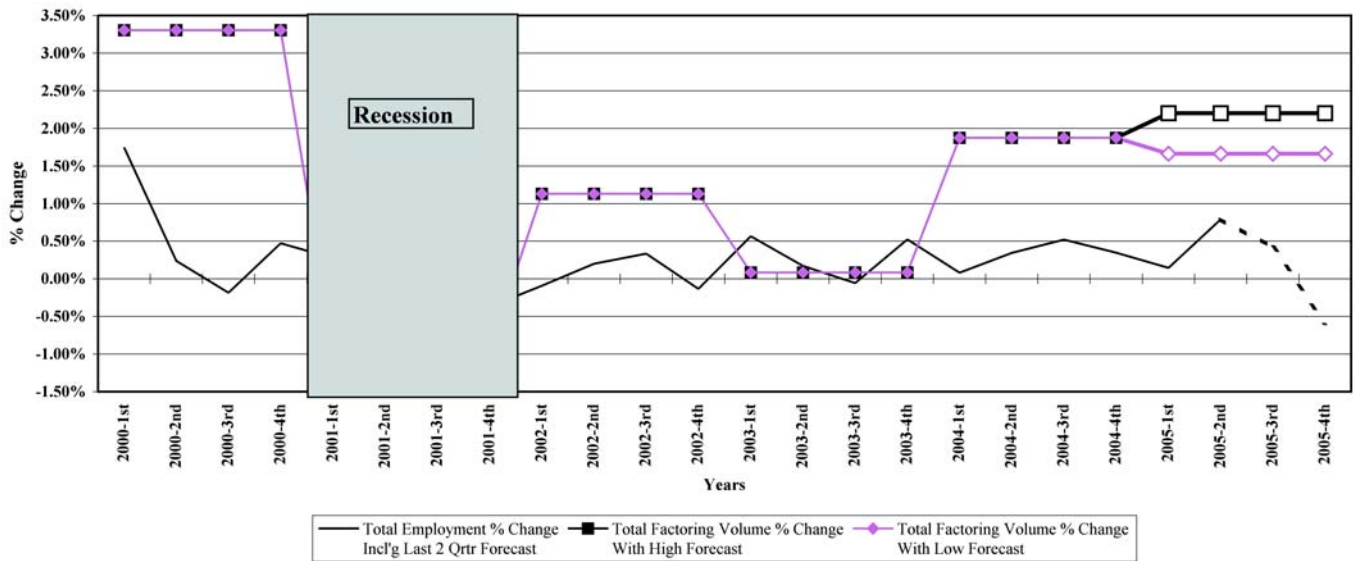
available data is much more sparse. Preliminary data for the first half of 2005 indicates that, overall, 2005 will be a strong economic year. And although both Hurricanes Katrina and Rita, coupled with continued very high gasoline prices and the ever-draining war in Iraq, have weakened somewhat both the 3rd and 4th quarters of 2005, we estimate that total factoring volume will rise by between 6.56% and 8.80% over that of 2004. Thus, we anticipate its reaching between \$110.0 - \$112.3 billion in 2005.

Even though we expect manufacturing durable new orders to peak in the second quarter of 2005 at \$623.4 billion, the decline thereafter will not cause factoring demand to fail to reach a new all-time high, especially after the second quarter's strong rise.

Text Exhibit I: Non-Notification vs. Notification Factoring



Text Exhibit J: Total Factoring Volume % Change vs. Total Employment % Change, INCLUDING 2005 FORECAST



Furthermore, we do not expect non-durable new orders to peak until the third quarter of 2005 at \$539.6 billion. Another reason for the positive outlook for factoring demand, total factoring volume moves coincidentally with non-durable new orders and with somewhat of a lag behind that of durables. Also total retail sales will not peak until the third quarter of 2005. However, this will be for a somewhat convoluted reason. As gasoline and the prices of other products made from crude oil rise, there will be a substitute of this price change for the quantity drop off in demand. Furthermore, we feel that building product shortages, that for home furnishings, and other related scarcities resulting

from the Gulf Coast devastation will also cause similar substitutions to take place. The need for the financing of these demands will cause factoring to finish 2005 at a fairly strong pace.

Changes in GDP and total employment have an important influence on factoring volume. The anticipated declines in both GDP and total employment, especially the slowdown in GDP that started early 2004, have led us to estimate a range in the gain in factoring volume between 6.56% and 8.80%. We feel that the level of factoring volume will reach a new all-time peak of between \$110 billion and \$112.3 billion in 2005.