Construction: Out of the Ashes

Brad Peterson
Channel Partners

October 2008 was our best month to date in our short seven month-old business unit and our $18 million dollar backlog of open approvals pointed to even better months ahead. Little did we know that 30 days later we would be strategizing the best ways gracefully exit the market. That was the beginning of some dark days that descended on the economy and the equipment finance industry. That's also the environment in which we began building Channel Partners.

At the time, construction was possibly the hardest hit industry among all the industries we serve. Total construction spending in the U.S. dropped a staggering 35% between 2008 and 2011—that's $400 billion annually. The industry crumbled around us, with defaults sky rocketing and equipment values plummeting. Many leasing companies prudently exited the construction market. Equipment brokers and lessors had few, if any, options to fund their construction related clients.

Construction Has Risen Again

"ELFA/The ALTA Group Rate Construction as the Best Equipment Leasing Opportunity."

We began funding construction related business loans in 2011. Our financing in the segment has continued to grow over the past several years to the point where construction business loans represented over 17% of our 2014 volume.

According to an ELFA and The Alta Group study of 400 equipment leasing managers and consultants (What's Hot, What's Not In Equipment Leasing 2014), construction equipment ranked highest in both Future Leasing Volume and Positive Change in Residual Position. For the first time in eight years construction equipment was rated "the best equipment leasing opportunity", replacing medical equipment, which had been the perennial first place winner.

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Gary Souverein, Pawnee Leasing Corporation

As reported by the Federal Reserve, construction spending has rebounded over 26% from 2011 through 2014. In addition, a recently released report (11/14), Dodge Data & Analytics predicts the total U.S construction starts for 2015 will rise 9%, almost double the 5% of 2014.

Today's Equipment Financing Environment – Good News

The good news is that brokers, lessors, and funding sources are again benefiting from the volume and margin generated from servicing the construction industry.

The industry rebound has translated into renewed interest from many funding sources. Some industry veterans were among the first to come back into the construction business. The benefit of the early "re-adopters" has been strong growth and portfolio performance.

"We've historically had good performance in this industry which is generally helped by having strong assets in this segment."

Terey Jennings, Financial Pacific Leasing

The continued growth in the construction industry along with rising equipment valuations will certainly draw other funding sources to re-enter the market.

THE FUTURE HAS POTENTIAL

I reached out to some leasing colleagues for their insights into the construction industry and have included some of the observations below.

"Over the past four years Financial Pacific has seen an increase each year in our concentration in the construction industry. The bulk of the equipment we finance in the construction industry is either yellow iron or vehicles like dump, bucket and water trucks. We've historically had good performance in this industry which is generally helped by having strong assets in this segment."

Terey Jennings, Financial Pacific Leasing

"Construction equipment financing since 2012 has run at twice the growth rate of our overall business. Performance in this segment of business we believe may continue to have runway ahead of it due to underlying trends in home supply and in the macro-economy. That said, we are becoming more cautious in regional economies that have exposure to the oil and gas production industry and believe the recent cyclical effects of oil & gas may have an adverse impact on the construction segment."

Gary Souverein, Pawnee Leasing Corporation

"TEAM Funding Solutions' construction customers are typically small to medium sized businesses that are sub-contracting to General Contractors and other larger entities. The 4 hardest hit states from the Great Recession being Arizona, Florida, California and Nevada have bounced back and are performing fine. We are guarded about all oil patch transactions and see continued growth in real estate construction in most of the country. There are a few Midwest states, especially Michigan, that continue to have slower growth and depressed real estate values."

Ted Reynolds, TEAM Funding Solutions

"Several key indicators suggest continued growth in construction industries. One of those indicators, the amount of requests for working capital to support existing and new contracts, cause us to be very optimistic that the positive trend over the last 4 years will continue."

Jason Sinclealr, Dakota Financial

Another Opportunity to Provide Financing to Your Construction Industry Clients

In today's environment, multiple factors make it challenging for banks to lend to small businesses, including construction related businesses. The cost of processing a transaction due to regulatory and compliance issues, the higher risk profile of small businesses and the difficulty of assessing creditworthiness make it difficult for most banks to profitably provide loans for less than $250,000.

As a result, the non-bank lending market has grown significantly over the past three years and has provided more than $6 billion in small business lending in 2014.

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In particular, general contractors and contract specialty businesses (HVAC, plumbers, electricians, etc.) have become a significant portion of Channel Partners' loan volume. Most of the companies in this segment have a strong credit profile (A or B credits) and are seeking $25,000 to $150,000 to complete a specific project. According to Adam Peterson, sales manager at Channel Partners, most construction borrowers find that the short-term nature of the loans matches well with their needs. "The borrowers are using the working capital as a revolving line of credit to help bid on additional projects, as well as startup capital for materials, payroll, or other related costs when beginning a new project. Our product allows them to have the flexibility to borrow and payback the notes as needed and is easily available to support their future projects."

Working capital loans are a compelling and important option to offer for brokers and lessors wanting to provide solutions for the financing needs of their construction business customers and prospects.

The re-emergence of the construction industry and further projected growth is a great sign for our economy and our businesses. Your financing support will help "pave the road" to further growth and success of the construction business. With you, we are pleased to be a part of growing the economy by helping your clients gain access to the capital they need to engage in new projects.

ABOUT THE AUTHOR | Brad Peterson is the Managing Member at Channel Partners LLC.