# Phoenix Management Services
# "Lending Climate in America" Survey

PHOENIX

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## 4th Quarter 2022
## Summary, Trends, and Implications

# PHOENIX
# "LENDING CLIMATE IN AMERICA"
# 4th Quarter 2022

## SUMMARY, TRENDS AND IMPLICATIONS

(Survey results were tabulated on December 7, 2022)

1. **The annual inflation rate for the U.S. is 9.1% for the trailing 12-month period that ended in June'22. That represented the largest annual increase since 1981. In an effort to curb inflation, the Federal Reserve has increased interest rates by 4.25 percentage points in 2022. American wages have increased over the past year by approximately 5.1%. A report released in June found that, even with the increase in wages, 61% of Americans (roughly 157 million adults) are living paycheck to paycheck. The survey also found that the average savings dropped to $10,757 in June from $11,274 in May, as people struggled to afford their lifestyles and increased credit card debt, making them more financially vulnerable. As the holiday season approaches, how do you think the average consumer will approach their spending:**

   The majority of lenders, sixty percent, believe an increase in prices will result in less holiday spending, but will not result in a material decrease from prior years. The other forty percent of the lenders surveyed believe that consumers will reduce their Q4'22 spending, which will have the greatest effect on small business relying on holiday revenue.

2. **How are borrowers allocating excess cash (if any)?**

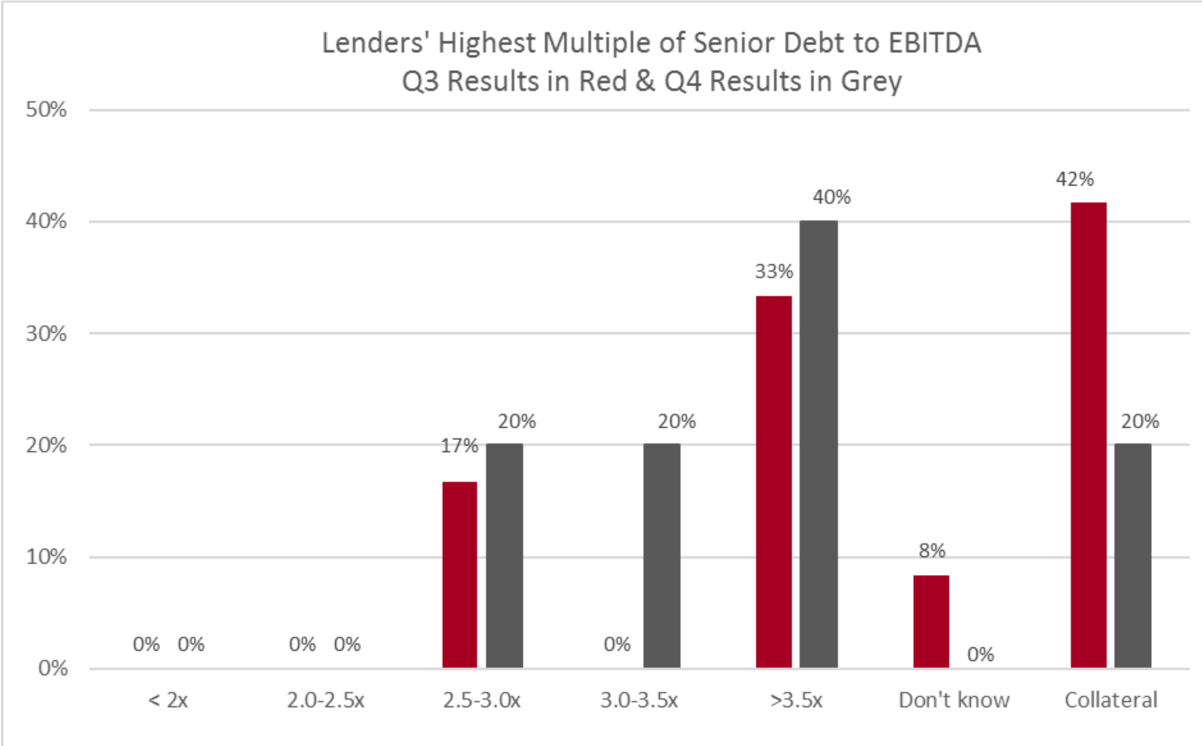
   When asked how their borrowers are allocating any excess cash, sixty percent of lenders expect any excess to go towards building a cash reserve to defend against any further downturn. However, forty percent of lenders believe their borrowers will use excess cash to catch up on payments to any of their stretched vendors.

3. **Approximately, 99.9% of businesses in the United States are considered small businesses, meaning the employee headcount is less than 500 (according to the Small Business Administration). 88% of small business owners said inflation was currently impacting their business. On average, these businesses have had to raise prices by more than 9% to offset the impact of inflation. How do you see the remainder of FY2022 and the beginning of FY2023 trending for small business owners?**

   Eighty percent of lenders expect inflation to continue to impact the economy well into FY2023, which will cause already tight margins to be squeezed even more if prices are not raised to offset any increased costs. Twenty percent of lenders believe inflation is at its peak and the economy will begin to normalize, giving relief to the increased commodity prices and material costs.

4. **Leverage multiples slightly shifted in Q4 2022.**

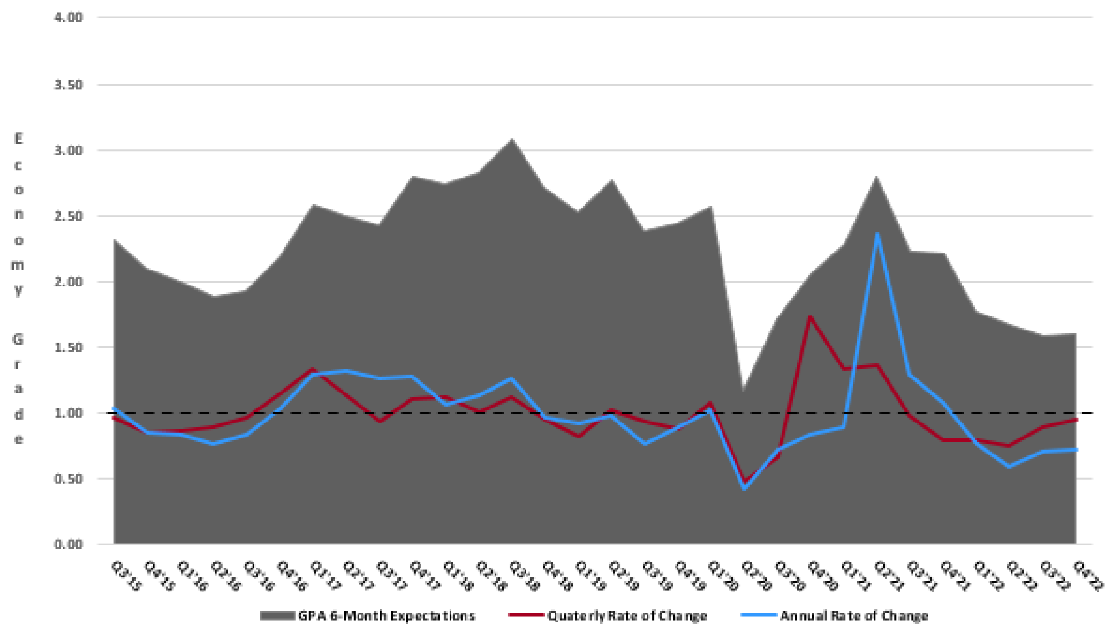
   Leverage multiples slightly shifted in Q4 2022 with 40% of lenders indicating that the >3.5x range would be the highest EBITDA ratio they would consider versus 33% in Q3 2022. The percentage of respondents who would consider a debt to EBITDA ratio of 2.5-3.0x slightly increased to 20%. Twenty percent of lenders responded that they were collateral lenders and therefore do not make decisions based on cash flow/leverage multiples.




5. **Near-term and long-term economic performance expectations decrease in this quarter's survey.**

   Lenders' optimism in the near-term U.S. economy slightly increased by 2 points this quarter from 1.58 in Q3 2022 to 1.60 in Q4 2022. In this current quarter, the majority of lenders (60%) believe the economy will perform at a "C" level during the next six months. Of the lenders surveyed, 40% believe the economy will perform at a "D" level, while 0% believe the economy will perform at a "B" of "A" level.

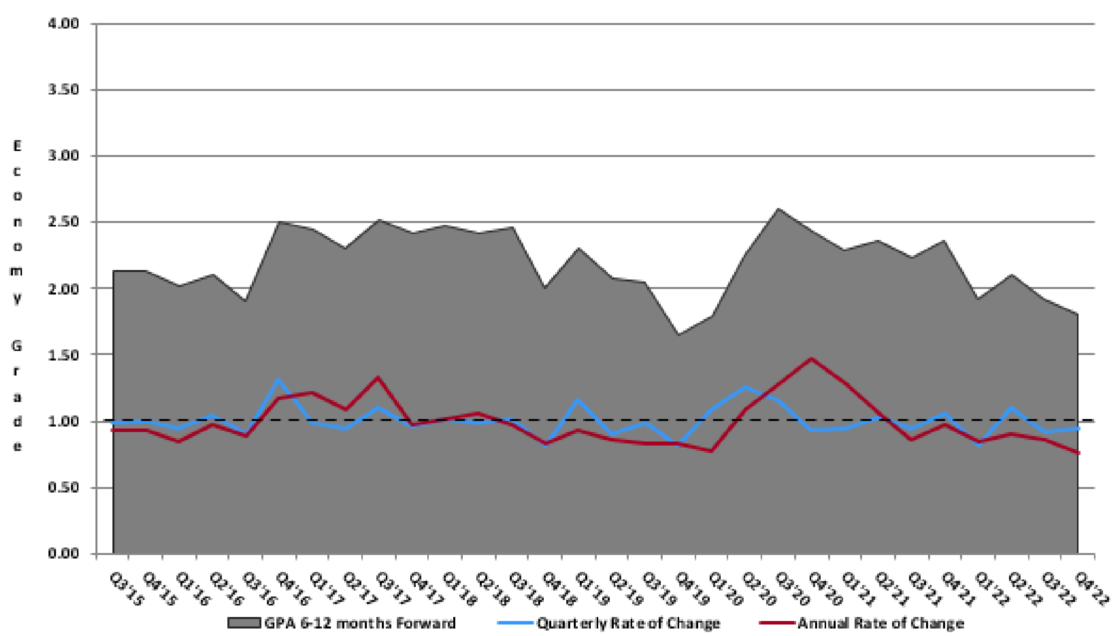
**Lender Expectations for Economy (Forward Six Months)**
**4.0=A, 2.0=C. 0.0=F**




** Rate of Change of 1.0 is at equilibrium and signifies "no change" from the corresponding prior period of comparison.*

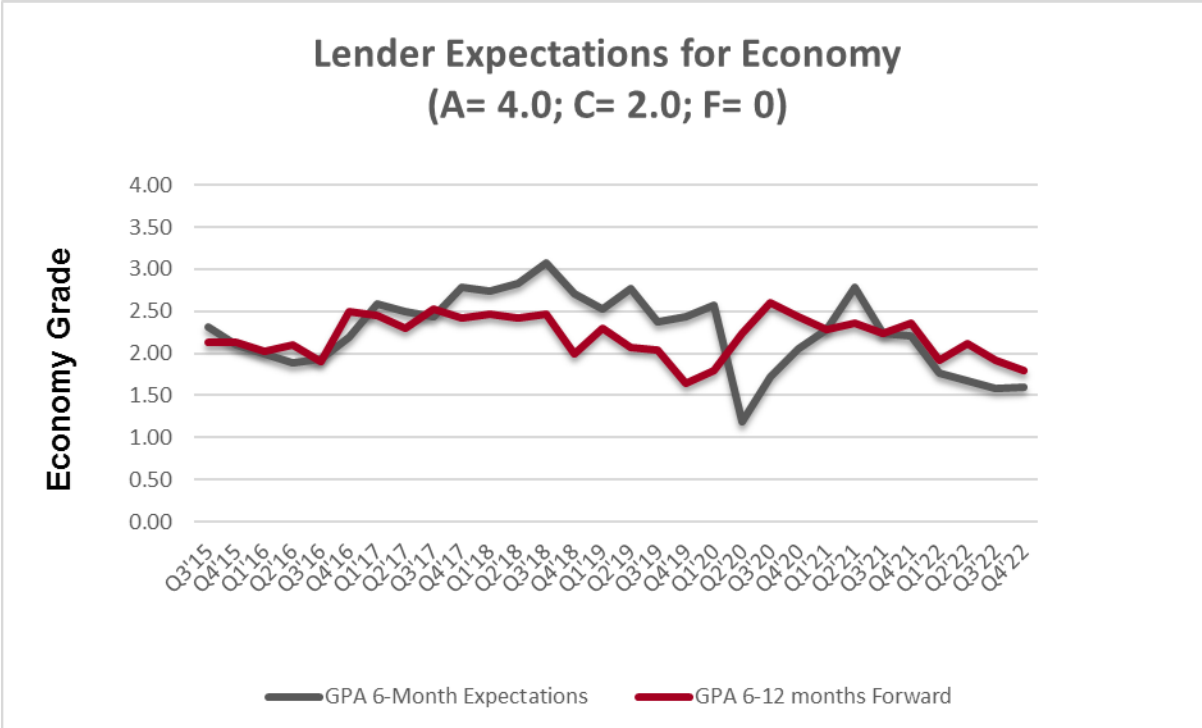
Lenders' growth expectations for the U.S. economy beyond six months also decreased from the prior quarter. The weighted average GPA decreased 12 points from a 1.92 in Q3 2022 to 1.80 in Q4 2022. Of the lenders surveyed, 80% feel as though the U.S. economy will perform at a "C" level beyond the next six months, while 20% expect the economy to perform at a "D" level, a decrease of 5 percentage points from Q3 2022.

**Lender Expectations for Economy (Forward Six-Twelve Months)**
**4.0=A, 2.0=C. 0.0=F**




** Rate of Change of 1.0 is at equilibrium and signifies "no change" from the corresponding prior period of comparison.*

In Q4’22, it seems lenders are still feeling pessimistic about the U.S. economy in both the near and longer-term.



# "Lending Climate in America"
# 4th Quarter 2022
# Survey Results

(Survey results were tabulated on December 7, 2022)

1. **The annual inflation rate for the U.S. is 9.1% for the trailing 12-month period that ended in June'22. That represented the largest annual increase since 1981. In an effort to curb inflation, the Federal Reserve has increased interest rates by 4.25 percentage points in 2022. American wages have increased over the past year by approximately 5.1%. A report released in June found that, even with the increase in wages, 61% of Americans (roughly 157 million adults) are living paycheck to paycheck. The survey also found that the average savings dropped to $10,757 in June from $11,274 in May, as people struggled to afford their lifestyles and increased credit card debt, making them more financially vulnerable.**

Lenders were asked: As the holiday season approaches, how do you think the average consumer will approach their spending?

| | |
|---|---|
| Consumers will reduce their Q4'22 spending, which in turn will affect many small businesses relying on holiday revenue. | 40% |
| Higher prices will result in less holiday spending, but not a material decrease from prior years. | 60% |
| Other | 0% |

2. **How are borrowers allocating excess cash (if any)?**

| | |
|---|---|
| Building Cash Reserves | 60% |
| Catching up on payments to stretched vendors | 40% |
| Other | 0% |

3. **Approximately, 99.9% of businesses in the United States are considered small businesses, meaning the employee headcount is less than 500 (according to the Small Business Administration). 88% of small business owners said inflation was currently impacting their business. On average, these businesses have had to raise prices by more than 9% to offset the impact of inflation.**

Lenders were asked: How do you see the remainder of FY2022 and the beginning of FY2023 trending for small business owners?

| | |
|---|---|
| Inflation will continue to impact the economy well into FY2023. Small businesses will need to continue to raise prices to offset the increases in costs or their margins will continue to shrink. | 80% |

| | |
|---|---|
| Inflation is at its peak and the economy will begin to normalize. Small businesses should soon experience some relief to commodity prices and material costs. | 20% |

## 4. Highest Senior Debt to EBITDA Leverage Institutions Would Consider

Respondents were asked the highest multiple of Senior Debt to EBITDA their financial institution would consider with regard to a loan request.

| EBITDA Level | 3Q 2022 | 4Q 2022 |
|---|---|---|
| Greater than 3.5x | 33% | 40% |
| Between 3.01x and 3.50x | 0% | 20% |
| Between 2.51x and 3.00x | 17% | 20% |
| Between 2.01x and 2.50x | 0% | 0% |
| Less than 2.0x | 0% | 0% |
| Collateral lenders | 42% | 20% |
| N/A | 8% | 0% |

## 5. Anticipated Change in Senior Debt to EBITDA Multiple

Respondents were asked, over the next six months, how the Senior Debt to EBITDA multiple would change at their financial institution.

| Change in Senior Debt to EBITDA Level | 3Q 2022 | 4Q 2022 |
|---|---|---|
| Increase greater than 0.5x | 0% | 20% |
| Increase less than 0.5x | 0% | 0% |
| Decrease less than 0.5x | 17% | 20% |
| Decrease greater than 0.5x | 0% | 0% |
| No change | 33% | 40% |
| Collateral lenders | 8% | 20% |
| N/A | 42% | 0% |

## 6. Factors with Strongest Potential to Affect Near-Term Economy

Respondents were asked, over the next six months, which two factors had the strongest potential to affect the economy.

| Factors Affecting Near-Term Economy | 3Q 2022 | 4Q 2022 |
|---|---|---|
| Unstable Energy Prices | 58% | 40% |
| Other | 42% | 60% |
| Stability of Stock Market | 33% | 20% |
| Constrained Liquidity in Capital Markets | 25% | 40% |
| U.S. Budget Deficit | 25% | 20% |
| Supply Chain | 0% | 20% |
| Sluggish Housing Market | 17% | 0% |

## 7. Industries Expected to Experience Greatest Volatility

Respondents were asked, over the next six months, which industries will experience the most volatility (i.e. Chapter 11 filings, mergers and acquisitions, declining profits, etc.). Respondents were asked to select the top three industries.

| Industries Experiencing Most Volatility | 3Q 2022 | 4Q 2022 |
|---|---|---|
| Retail Trade | 75% | 60% |
| Arts, Entertainment, and Recreation | 0% | 20% |
| Construction | 42% | 80% |
| Transportation & Warehousing | 33% | 0% |
| Real Estate & Rental/Leasing | 33% | 60% |
| Accommodation & Food Service | 33% | 20% |
| Mining | 25% | 0% |
| Manufacturing | 25% | 20% |
| Wholesale Trade | 0% | 20% |

## 8. Customers' Plans in the Next Six to Twelve Months

Respondents were asked which of the following actions their customers planned in the next six to twelve months. Lenders were asked to designate all potential customer actions that applied.

| Customers' Plans | 3Q 2022 | 4Q 2022 |
|---|---|---|
| Hiring New Employees | 55% | 20% |
| Introducing New Products or Services | 45% | 40% |
| Raising Additional Capital | 36% | 80% |
| Capital Improvements | 36% | 20% |
| Making an Acquisition | 36% | 20% |
| Entering New Markets | 18% | 60% |
| "Other" Initiatives | 18% | 20% |

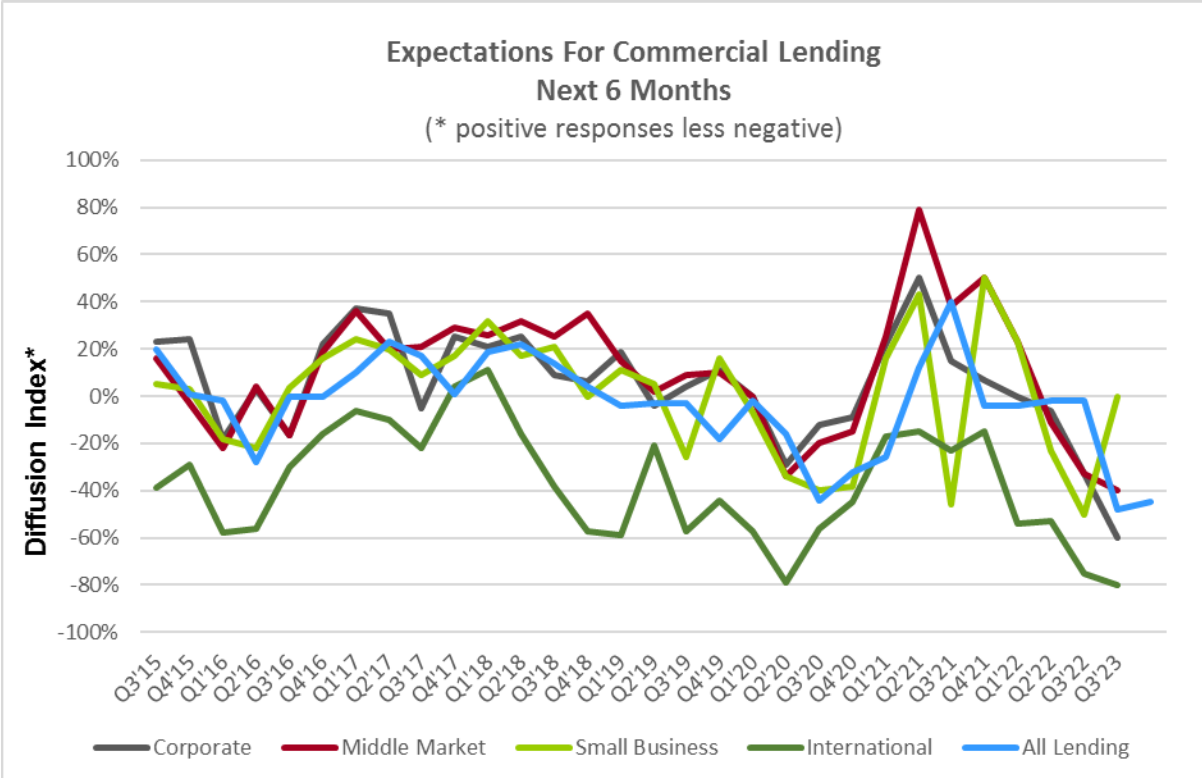
## 9. Economic Indicators

Respondents were asked whether they expected the following economic indicators to be up, down, or remain the same over the next six months.

- In Q4 2022, lenders optimism continued to decrease in large corporate (-60%) and middle market (-40%) lending, but remained neutral in small business lending (0%).

| | 3Q/2022 | | | | 4Q/2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Up | Down | Same | Diffusion Index | Up | Down | Same | Diffusion Index |
| Corporate Lending | 17% | 50% | 33% | -33% | 0% | 60% | 40% | -60% |
| Middle Market Lending | 17% | 50% | 33% | -33% | 0% | 40% | 60% | -40% |
| Small Business Lending | 0% | 50% | 50% | -50% | 20% | 20% | 60% | 0% |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| International Lending | 0% | 75% | 25% | -75% | International Lending | 0% | 80% | 20% | -80% |




- In Q4 2022, there was an increase in the bankruptcies diffusion index from 83% in Q3 2022 to 100%. The unemployment diffusion index increased to 100% in Q4 2022 compared to 58% in Q3 2022. In addition, the loan losses diffusion index increased to 100% in Q4 2022, and the bank failures diffusion index increased to 20% in Q4 2022.

| | 3Q/2022 | | | | | 4Q/2022 | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Up | Down | Same | Diffusion Index | | Up | Down | Same | Diffusion Index |
| Loan Losses | 92% | 0% | 8% | 92% | Loan Losses | 100% | 0% | 0% | 100% |
| Bankruptcies | 83% | 0% | 17% | 83% | Bankruptcies | 100% | 0% | 0% | 100% |
| Interest Rates | 83% | 8% | 8% | 75% | Interest Rates | 100% | 0% | 0% | 100% |
| Unemployment | 58% | 0% | 42% | 58% | Unemployment | 100% | 0% | 0% | 100% |
| Bank Failures | 17% | 0% | 83% | 17% | Bank Failures | 20% | 0% | 80% | 20% |

## 10. U.S. Economy Grade – Next Six Months

Respondents were asked how they expected the U.S. economy to perform during the next six months on a grading scale of A through F.

- Lender optimism on the U.S. economy increased 2 points this quarter from 1.59 in Q3 2022 to 1.60 in Q4 2022. In this current quarter, the majority of lenders (60%) believe the economy will perform at a “C” level during the next six months. Of the lenders surveyed, 40% believe the economy will perform at a “D” level, while 0% believe the economy will perform at a “B” or “A” level.

| **Grade** | **3Q/2022** | **4Q/2022** |
|---|---|---|
| A | 0% | 0% |
| B | 17% | 0% |
| C | 33% | 60% |
| D | 42% | 40% |
| F | 8% | 0% |
| Weighted Average Grade | 1.58 | 1.60 |

## 11. U.S. Economy Grade – Beyond the Next Six Months

Respondents were asked how they expected the U.S. economy to perform beyond the next six months on a grading scale of A through F.

- Lenders’ expectations for the U.S. economy’s performance in the longer term decreased from the prior quarter. The weighted average GPA decreased 12 points from a 1.92 in Q3 2022 to 1.80 in Q4 2022. Of the lenders surveyed, 80% feel as though the U.S. economy will perform at a “C” level beyond the next six months, while 20% expect the economy to perform at a “D” level, a decrease of 5 percentage points from Q3 2022.

| **Grade** | **3Q/2022** | **4Q/2022** |
|---|---|---|
| A | 0% | 0% |
| B | 17% | 0% |
| C | 58% | 80% |
| D | 25% | 20% |
| F | 0% | 0% |
| Weighted Average Grade | 1.92 | 1.80 |

## 12. Customers’ Future Growth Expectations

Lenders assessed their customers’ growth expectations for the next six months to a year.

- The percentage of respondents indicating their customers have “moderate” growth expectations for the next six months to one year increased 10 percentage points to 60%. In Q4 2022, there was a decrease in the percentage of lenders that ascribed to strong growth (0%). Fourty percent of lenders ascribed to no growth.

| **Indication** | **3Q/2022** | **4Q/2022** |
|---|---|---|
| Very Strong | 8% | 0% |
| Strong | 8% | 0% |
| Moderate | 50% | 60% |
| No Growth | 33% | 40% |

## 13. Loan Structure

Respondents were asked whether their financial institutions planned to tighten, relax, or maintain their loan structures (collateral requirements, guarantees, advance rates, loan covenants, etc.) in each of four different-sized loan categories.

Half of the surveyed lenders plan to maintain their current loan structure. In Q4 2022, the other 50% of lenders plan to tighten their loan structure and 0% plan to relax their loan structure.

| | 3Q/2022 | | | 4Q/2022 | | |
|---|---|---|---|---|---|---|
| | Tighten | Maintain | Relax | Tighten | Maintain | Relax |
| Loans> $25 million | 36% | 64% | 0% | 40% | 60% | 0% |
| $15 – 25 million | 45% | 55% | 0% | 40% | 60% | 0% |
| $5-15 million | 40% | 50% | 10% | 60% | 40% | 0% |
| Under $5 million | 64% | 27% | 9% | 60% | 40% | 0% |
| Overall Average | 46% | 49% | 5% | 50% | 50% | 0% |

## 14. Interest Rate Spread

Lenders were asked whether their financial institutions planned to reduce, maintain, or increase their interest rate spreads and fee structures on similar credit quality loans.

A majority of lenders (55%) plan to increase their interest rate spreads and fee structures. In Q4 2022, the percentage of lenders that plan to maintain their interest rate spreads decreased to 40%, and 5% plan to reduce their interest rate spreads.

| | 3Q/2022 | | | 4Q/2022 | | |
|---|---|---|---|---|---|---|
| | Reduce | Maintain | Increase | Reduce | Maintain | Increase |
| Loans > $25 million | 0% | 82% | 18% | 20% | 20% | 60% |
| $15 – 25 | 0% | 80% | 20% | 0% | 60% | 40% |
| $5-15 million | 0% | 70% | 30% | 0% | 40% | 60% |
| Under $5 million | 0% | 82% | 8% | 0% | 40% | 60% |
| Overall Average | 0% | 78% | 22% | 5% | 40% | 55% |

## 15. The Fed and Interest Rates

Respondents were asked in what direction they thought the Fed would move interest rates and by how much in the coming six months.

100% of respondents in Q4 2022 believe the Fed will increase interest rates by + 1/2 point or more.

| **Bps Change** | **3Q/2022** | **4Q/2022** |
|---|---|---|
| + 1/2 point or more | 84% | 100% |
| + 1/4 point | 0% | 0% |
| Unchanged | 8% | 0% |
| - 1/4 point | 0% | 0% |
| - 1/2 point or more | 8% | 0% |
| Weighted Average | 0.85bps | 0.95bps |

## 16. Current Competition

Respondents were asked to identify the segment of the industry from which they were experiencing the most competition.

- Regional Banks place at the top of the survey, garnering 60% of responses. Money Center and Local Community/Commercial Banks garnered the next highest amount of responses with 20% each.

| | **3Q/2022** | **4Q/2022** |
|---|---|---|
| Regional Bank | 33% | 60% |
| Commercial Finance Co. | 25% | 0% |
| Local Community/Commercial Bank | 25% | 20% |
| Money Center Banks | 8% | 20% |
| Other | 8% | 0% |
| Factors | 0% | 0% |