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Question 1: What are the risks in lending to manufacturing that supports the oil and gas industry?

One major risk when lending to manufacturing that supports the oil and gas industry is the volatility of prices for oil and gas. As stated in the document, significant downturns such as the one that happened in 2021 put many capital expenditure plans on hold. Although prices have recovered, there is no guarantee that they will continue to be stable for the foreseeable future. As such, volatility is a huge risk for banks when lending to the oil and gas industry. This is because when banks loan money, it is considered an asset for the bank and a liability for Atkinson's company. If oil/gas prices suddenly fall, the borrowing firm's liabilities will increase in real terms while not increasing the real value of the firm's assets. Thus, the borrowing firm's net worth will decline, thereby increasing the risk of default. Therefore lending to manufacturing in the oil and gas industry leaves the loan vulnerable to changes in asset price, making the loan highly risky.

Question 2: Atkinson Widget has lots of debt. What will the overall debt to net worth look like (leverage ratio), and is this a risk?

Atkinson Widget's financial leverage, or its debt-to-net worth ratio, is a key measure of how much debt it can handle. The company has previous liabilities, including a $400,000 officer loan.The $2,000,000 loan would increase the company's debt which would increase its leverage ratio. A high ratio means the company is relying heavily on borrowed money which would increase financial risk for the business. After the new loan, Atkinson Widget's liabilities would rise which would cause them to be more vulnerable to cash flow issues. The company must generate enough cash to cover operating expenses and debt payments, which could be difficult if the business takes a hit. With high leverage, the company would have less room to take on additional debt or invest in growth. Lenders may see this as risky due to potential default which would affect the company's credit score and their ability to be trusted to receive loans/pay back loans. If the company won't be able to back its loan, lenders could also take steps to mitigate their risk through seeking collateral, increase interest rates, impose stricter repayment terms, or pursue legal action.

Question 3: Can Atkinson Widget repay the loan?

Atkinson widget through the years of 2020-2023 has grown their revenue from 3.756.124 dollars to 8.175.123 dollars. Although impressive, this company has high costs and consistently only pulls in around 40.000 dollars in net profit despite their exponential growth in profits. If they can keep growing their revenue exponentially it is possible to pay back the 600.000 dollar loan from Evans bank. However, in reality this is not likely to happen as the oil and gas market is subject to volatile prices and there are other companies competing for market share which drives prices for oil back down. Even if in 2024 Atkinson Widget's assumed revenue was over 8 million, the company's total net profit would have similar results to previous years (~40.000 dollars). Thus, they will not be able to repay the loan over 10 years.

Question 4: Collateral – Is there enough to cover the debt?

Atkinson Widget is looking for a $2 million loan to buy new machinery and pay off existing debts. The main assets the company can offer as collateral are their machinery and equipment worth $1,800,000 dollars. However, these machines are subject to depreciation and have accumulated up to $1,765,950 dollars leaving them to be worth $184,050 dollars. The company could also offer up their short term assets. However, according to the balance sheet they only have $979,467 dollars worth of short term assets. This means that in total they can offer up $1,163,517 dollars worth of assets as collateral. The loan is for $2,000,000 dollars so the collateral can only cover around half of the loan. Additionally, the bank requested a personal guarantee from Dean Atkinson, but he declined, further increasing the risk since the bank can only rely on the company's assets which covers only half of the total value of the loan. Overall, the available collateral seems insufficient to cover the loan amount of $2 million dollars. However, if the company chooses to liquidate they will have enough to pay off their existing debt of $911,760 dollars.

Question 5: Management – Evaluate from a succession standpoint and depth.

From a succession standpoint, the company does not project to fair well. Dean Atkinson has the necessary experience to run the company however at 62 years old he is nearing retirement. His daughter Megan is 27, and has an MBA in finance and is already involved with the company. However, with her credentials it may be more straightforward to have her succeed the CFO role as Andrew Jewett is 65 and also nearing retirement. The company has hired Patrick Burns but he is a recent graduate and inexperienced. Depthwise however, because Atkinson took a pay cut to retain all 25 employees, the company needs to make no plans immediately. The only issue is hiring someone to fill in the position as machinist for the CNC machines.

Question 6: Would your Loan Committee ask for a personal guarantee?

If we were the loan committee, we would ask for a personal guarantee from Dean Atkinson. The company is currently facing significant debt including a 400.000 dollar officer loan and a 2.000.000 dollar loan to replace their existing equipment and pay off liabilities. Although the business has survived past economic struggles, it operates in the oil and gas sector which is highly volatile and thus, leaves any loans subject to a high risk of default. Furthermore, the company's existing collateral is insufficient to cover the loan amount which means that if they default, we as the loan issuers get less than what we loaned. Essentially, this loan is one with a high risk of default, and no guarantee of repayment of the principal amount in the case of a default. Therefore, for this loan to go through it is basically required for Dean Atkinson to provide a personal guarantee, otherwise the risk is too high.

Question 7: Would your Loan Committee require covenants?

Our loan committee would definitely enforce covenants if they approve the loan for Atkinson Widget. Our committee would include financial covenants. The covenant we would enforce would be a limit on the company's debt-to-equity ratio. This would not allow Atkinson widget company to take on too much debt which would make them more stable. We would also enforce a minimum cash flow coverage ratio which would ensure that the company generates enough cash to meet its loan obligations. We would also require the company to maintain a certain level of net worth which would protect our loan committee in case of financial difficulties. Our committee would also include operational covenants. Atkinson Widget would also face restrictions on taking on additional debt or making large capital investments, like further equipment purchases, without our committee's approval. This would prevent the Atkinson widget company from becoming too leveraged or risking its liquidity during the loan term.We would also enforce reporting covenants, which would require the company to provide regular financial updates, such as quarterly or annual financial statements. This would allow our committee to monitor Atkinson Widget's financial condition.

Our Recommendation:

Our loan committee would counter the loan offer by only accepting it under the conditions of the covenants listed or a personal guarantee from Dean Atkinson. We would enforce covenants so we can personally monitor what our money is being used on and prevent moral hazards. Or we would enforce a personal guarantee in which Dean

Atkinson has to personally guarantee to pay the rest of the 2 million that the collateral cannot cover so that we at least get our initial payment of 2 million back.