



Mezzanine Debt: A Flexible Financing Solution

**Presentation by:
BDC Capital**

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What is Mezzanine Debt

- Mezzanine debt bridges the gap between senior debt and equity
- It's a hybrid financing option offering flexibility
- Provides capital above that available from senior lender to finance strategic initiatives (growth, acquisition, recapitalization, refinance, etc.)
- Typically structured as a subordinated note



Mezzanine vs. Senior Debt

Aspect	Mezzanine Debt	Senior Debt
Position in Hierarchy	Subordinate	Senior
Risk-Reward Balance	Higher Risk, Higher Return	Lower Risk, Lower Return
Interest Rate	10 - 12% current pay plus kicker	7.5 - 9% current pay
Personal Guarantees	None	Yes
Amortization	Significant interest only period	Typically amortizing from close date



Features of Mezzanine Debt

- Subordinate to senior debt, but senior to equity
- Typically unsecured or subordinate lien position, relying on company's cash flow
- Higher interest rates and potential equity participation (for example, warrants, conversion or equity participation in transaction financed)
- Interest-only period eases cash flow required for debt service



Mezzanine Structure

- 5 to 7 year term note
- 10-12% current pay fixed interest
- Significant interest-only period with flexible amortization thereafter
- Subordinated in lien priority to senior lender
- Target mid-teens total return on capital – Achieved through current pay plus one or combination of the following:
 - Warrants
 - Equity Participation
 - PIK (Payment in kind interest)
 - Royalty



Benefits for Senior Lenders

- Enhances senior lender security due to the junior position
- Expands the borrower's funding capacity without diluting ownership
- Standstill on subordinated debt provides relief for senior lender value if borrower stumbles
- Allows more favorable terms for senior debt due to lower LTV ratios



Benefits for Borrowers

- Offers more flexibility compared to traditional senior loans
- Enables funding of growth/strategic initiatives, acquisitions, buyout of partner, generational transfer and capital projects
- Ability to extend term and improve cash flow through significant interest-only periods
- Reduces the need for a significant equity contribution
- Avoid potential control issues inherent in equity financing
- Less dilutive than equity financing



Risk Considerations

- Subordination means higher risk of loss in case of default
- Dependency on company performance for interest payments
- Due diligence critical to assess borrower's ability to meet obligations



Uses for Mezzanine Debt

- Mergers & Acquisitions:
 - Facilitates Acquisitions
- Expansion & Growth:
 - Funds Expansion Initiatives
- Recapitalization/Refinancing
 - Facilitate Recapitalization/Refinancing by bridging the gap



Mezzanine Example

Refinancing

Challenge:

- A company engaged in on-line ticket distribution was experiencing a strong rebound as it emerged from the pandemic.
- The company needed to refinance a federal government Main Street loan plus other debt and required additional working capital.

Solution:

- Bank provided a \$20 million line of credit
- BDC Capital provided a \$5 million non-dilutive mezzanine investment in a subordinated position to the bank to provide the working capital necessary to support continued growth



Mezzanine Example

Acquisition

Challenge:

- Investor group wanted to acquire small manufacture from founders
- The company needed sufficient capital to fund acquisition and provide necessary working capital post close

Solution:

- Senior lender provided a \$1.5 million 7 year term loan and a \$500k LOC undrawn at close
- BDC Capital provided a \$1.5 million mezzanine investment in a subordinated position to the bank to fill the gap and fund the acquisition



Conclusion

- Mezzanine debt: A strategic tool
- Offers benefits for both senior lenders and borrowers
- Increased capital access fosters growth and facilitates strategic transactions



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MB Capital Fund V

- \$50 Million in Capital
- Mezzanine Investments - \$1 – 7 Million Commitments
 - Established businesses
 - Fund growth, acquisitions, recapitalizations and refinancing
- Focused on Northeast



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