BDC Financial Instruments

BDC can structure its funding as follows:

<u>Debt Capital:</u>

Senior Secured:
These are debt instruments that gets priority repayment in case of bankruptcy. They are typically floating rate instruments with maturities between five to eight years. Assets or stock in subsidiary companies of the borrower are normally pledged as security, which gives BDC seniority and priority in the capital structure of the investee company. The instruments are normally amortised on a straight line basis and have a negative pledge covenant attached to them.

Senior Unsecured:
Unlike senior secured, these are not collateralised and normally attract higher interest rates to compensate for the risk. They normally rank below secured facilities but above other unsecured or subordinated debt for payment in the event of bankruptcy.

Subordinated:
These rank below other debts with regard to claims on company resources. Because these are repayable after other debts have been paid, they are riskier and attract higher interest rates.

<u>Mezzanine Capital</u>
This refers to a tier between debt and equity in a company's capital structure. It can come in the form of a standalone equity investment, typically preferred stock, or a debt investment. Most often, mezzanine financing takes the form of subordinated, unsecured debt. Due to its capital structure raking and because mezzanine investments are often not as liquid as debt instruments, the capital is normally expensive with required returns of 12% - 24%. This form of funding is ideal for growth companies, LBO transactions, real estate projects and restructurings.
This form of capital promotes flexibility in the financing structure as it takes into consideration the cash flow needs of the business from time to time and negotiations are normally open in terms of type of instrument, maturity, interest rate and fees, ranking, security and covenants.

<u>Equity Capital</u>
BDC can buy ownership interest by way of ordinary shares from a business that is looking to raise capital for business purposes. A significant minority holding is required (26% - 49%) coupled with board representation. A defined dividend policy is necessary to allow BDC to assess the commercial viability of the investment opportunity. This form of financing ranks below other instruments in the event of bankruptcy.

Considerations in determining which instrument to extend to a prospective investee company

Cash flow position:
The availability and variability of future cash flows need to be considered when determining one's capital structure. i.e. Debt capital should only be used in companies that have periodic and good cash flows to allow for debt service while equity should be used for companies that have tight cash flows but have growth potential. Mezzanine type structures may be used to match the complexity and variability of cash flows.

Leverage:
This is the extent to which debt capital is used to finance a company. In order to increase company's profits, Debt capital may be used only if assets that are purchased with the debt capital earn more than the cost of the debt that was used to finance them. Debt capital may also be preferable due to the interest tax shield that is afforded by the corporate income tax law. BDC will assess the level of existing debt in the company's capital structure while taking into consideration the norms in the industry or business sector and decide on the ideal instrument that is optimal for the investee company.

Risk profile:
BDC assess the risk profile of the investee company in terms of corporate governance, operational and market risk and from the analysis, determine which structure yield acceptable returns considering the mitigations.

Promoter sponsorship:
BDC will assess the level of commitment that the promoters have dedicated to the investee company by reviewing the capital already injected from the promoters. The promoters need to have enough commitment ("skin in the game") for BDC to consider partnership. The ideal position is for the promoters to have at least 40% of the required capital.

Development impact:
The business needs to have a positive and sustainable effect on the general community either by way of creating jobs, protecting the environment, paying government taxes etc.

Scalability:
The business needs to have the capability to handle growth within and beyond boarders or it needs to have potential to be improved in order to accommodate that growth.