CNL Securities

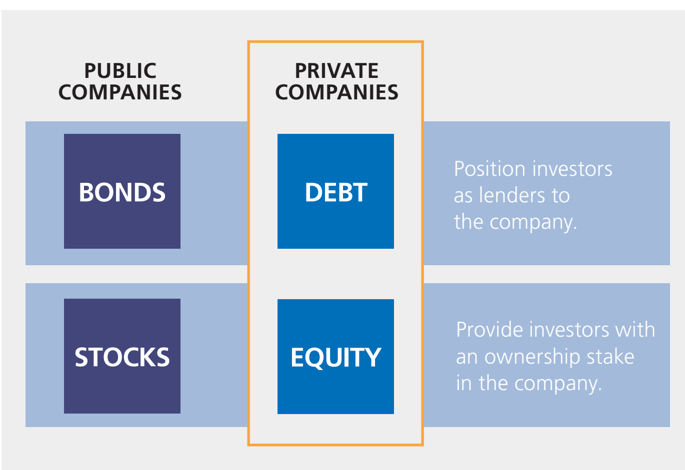
EDUCATIONAL FLYER

What Is Private Debt?

PRIVATE COMPANIES AND DEBT

From jobs to the gross domestic product, privately owned companies help drive the American economy. In the United States, nearly 200,000 businesses comprise the middle market, which employs 47.9 million people as of March 2016.[1]

However, when these private companies need funds to expand or manage their operations, they may not have access to funding through a public offering, such as the sale of stocks and bonds. In this situation, private companies raise funds by selling equity (ownership) shares in the company or through debt financing in the form of loans and lines of credit.



HOW PRIVATE DEBT FINANCING WORKS

When a private company identifies an opportunity to grow its business, the company may not have the cash or assets on hand to pursue the necessary expansion. In this situation, debt may be the preferred financing option.

To fund the growth opportunity, the company borrows the needed funds by asking a lender for a loan. In exchange for making the loan, the lending institution receives interest payments in addition to the repayment of the contractual loan amount. Both parties have the potential to benefit. If all goes as intended, the company grows its business, while the lending institution receives a contractual return on its investment.

SOURCES OF PRIVATE DEBT FINANCING

Private companies can seek debt financing in the form of loans from:

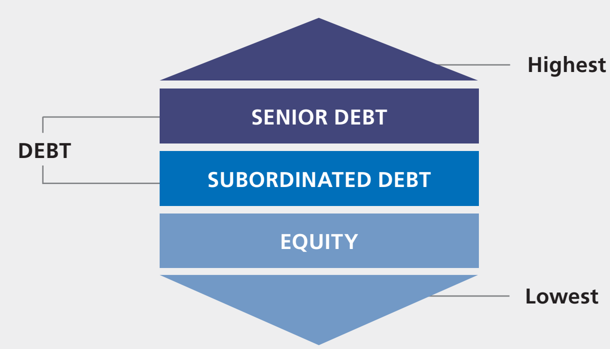
- BANKS
- BUSINESS DEVELOPMENT COMPANIES
- SPECIALTY FINANCE COMPANIES
- INSURANCE COMPANIES
- HEDGE FUNDS
- CREDIT PLATFORM OF PRIVATE EQUITY

THE CAPITAL STRUCTURE AND DEBT

The combination of equity and debt forms a company's capital structure. The balance of debt versus equity is unique to each company and is determined by the management team's evaluation of various loan terms and other business factors.

Debt has a priority claim on cash flows and assets. In addition, there are different levels of debt. Senior debt ranks first in repayment priority, while subordinated debt ranks second. Equity comes with the highest return expectations to reflect the higher risk of loss, based on its lower claim priority.

Cash Flow Repayment Priorities



[1] *1Q 2016 Middle Market Indicator*, National Center for the Middle Market, 2016.

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