Business Development Companies (BDC): Update

OLLI Investment Forum

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Disclaimer: I am not a certified financial analyst. Any trading decisions you make are your responsibility

Agenda

- What is a Business Development Company (BDC)?
 - How to evaluate a BDC
 - Compare BDC performance with S&P500
 - Deep dive into Gladstone Capital (GLAD)

What is a BDC?

Wikipedia Definition:

- Established by Congress with the Investment Company Act of 1980; Amended in March 2018
- A company that makes loans to small and mid-size businesses
- Companies use loans to finance expansion, acquisition, LBO, etc
- Regulated by the SEC as Registered Investment Companies (RIC)
- PAY NO TAXES as long as they distribute 90% of earnings
- Similar to a REIT, but assets are loans to small and medium size companies
- Private Equity or Venture Capital for retail investors
- Most BDCs are publicly traded some are not

Primary reason for investing:

- Long term, alternative investment, high dividends with diversification
- Can result in good returns in a buy and hold portfolio, with a Dividend Reinvestment Program (DRIP)
- Investing is primarily for dividends, not capital gains
- Most BDCs issue a fixed dividend with a variable supplemental dividend
- Most pay quarterly, a few monthly

BDCs are filling a gap

Large Commercial Banks Are Biased Against Small/Medium Companies



FDIC Chartered Banks

• Source: FDIC

Typical BDC Capitalization

Assets

- First Lien secured loans
 - 75% of portfolio is very good
- Second Lien secured loans
- Senior secured loans
- Mezzanine Loans
- Warrants
- Equity Stakes
- Board seats
- Partnerships and JVs
- Venture Debt
- SBA Facilities
 - Government guarantees



- Loans from money center banks
 - Revolving credit facilities
- Preferred stocks and dividends
- Common Stocks and dividends
- Notes
- Convertible Notes
- Baby Bonds
- Hedges

BDCs borrow at fixed rates; Lend out at floating rates Rising interest rates are good for BDCs! Usually.

How to Evaluate a BDC

- Is the BDC externally managed? Or internally?
 - External: A company owns the BDC
- Is the stock selling at a premium to NAV?
- What is the NAV record?
- What percentage loans are first lien?
- What is the quality of the loan portfolio?
 - Quarterly reports to investors
 - Read SEC reports for quality assessments
 - Non-accrual rate < 1% is good
- Is the dividend sustainable?
 - What is the dividend history?
 - Is Net Investment Income increasing?

How to Evaluate a BDC, cont'd

- S&P Investment grade rating? BBB or better
- What are the qualifications of the managers?
- Analyst opinions?
- Short interest?
- Do they have a Small Business Administration guarantee / license?
- Check SEC 10Q/10K quarterly reports very insightful
 - Quarterly transcripts of shareholder meetings
- Read the Blogs on Seeking Alpha
 - Scott Kennedy, High Yield Investor (HYI), Brad Thomas
- Check Simply Safe Dividends provides excellent, indepth analyses
- Check BDCInvestor.com

BDC Market Landscape

There are approximately 60 BDCs registered with the SEC

Price to NAV: Guide To Quality

BDC Investor.com

Provides a Rank-order of BDCs by

Highest Price / NAV Ratio



Review BDC's Dividend History and Policy

For example: Main Street Capitol Corp (MAIN)

provides recurring monthly dividends and also irregular supplemental dividends

Yield Comparison: BDCs vs SP500

- Hercules Capital 10.55%
- Main St Capital 8.03%
- Capital Southwest 12.26%
- Blackstone Secured* 10.37%
- Gladstone Capital* 7.65%
- SPY (S&P500 ETF) 1.29%
- * Denotes externally managed BDC

5-Year Total Return Comparison: BDCs vs S&P500



Deep Dive: Gladstone Capital

Review BDC's price history and statistics

Deep Dive: Gladstone Capital Corp (GLAD)

- Headquartered in McLean, Va
- Externally managed
- Current price: \$25.13
- Net Asset Value: \$22.0 / share
- NAV trend: Rising 6.6% on average over 10 years
- Morningstar rating: 3 stars; undervalued by 8%
- Debt / Equity: 0.58
- #loans: 55
- Non-accrual rate: 4% (too high)

Compare Nonaccrual rates

GLAD: 4.1%

CSWC: 3.5%

HTGC: 1.8%

BXSL: 0.3%

MAIN: 1.7%

Gladstone Investment Portfolio, Q1, 2024

Review Annual Report for

BDC's Portfolio Diversification

of investments

Conclusion

- BDCs are not for everyone
- For long term buy and hold portfolios
- Especially good in IRAs / 401ks with DRIP
- Prices are volatile, but total return is enviable
- Now is a good time to invest, but the window is closing

Will Rogers: "Invest in inflation. It's the only thing going up." GLTA!

Sources:

Seeking Alpha Blogs

- Scott Kennedy
- Colorado Wealth Management
- High Yield Investor
- Brad Thomas

Fidelity, Schwab, Vanguard

Morningstar

Simply Safe Dividends

BDCInvestor.com

SEC 10Q reports