# Business Development Companies – New Frontier For Income Investing

23 October 2013
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## BDC Overview

Business Development Companies (BDCs) focus on investing in private companies rather than publicly traded companies. They largely invest in Equity Investment as well as various debt instruments. Thus, by investing in a BDC, shareholders enjoy the liquidity of a publicly traded stock while participating in the private equity industry. Most BDCs are registered as regulated investment companies (RICs), which requires them to pay out at least 90% of their profits in dividends. While these businesses might not be familiar to all investors, they have qualities that should be appealing to nearly everybody. Specifically, many BDCs trade for attractive multiples of their earnings and pay huge dividends to shareholders.

Here are 4 reasons to consider owning a BDC.

## 1. True Growth Stocks are Hard to find

The truly great growth stocks are hard to find. Sure, we have high fliers like LinkedIn or Facebook, but these examples are few and far between as smaller companies stay private. Over time, a combination of regulation and takeovers have kept good companies off the market. Smaller firms are waiting longer to come out with an IPO -- Facebook waited until it earned a $100 billion valuation to list publicly -- which keeps many growth stocks out of investors' portfolios. Investing in BDCs indirectly positions an investor to take advantage of companies experiencing exponential growth.

### 2. Smaller companies outperform

History provides evidence that the smaller companies outperform larger companies. That outperformance boils down to the reality that small companies have much more room to grow, and such companies are generally under owned and under covered by Wall Street's best and brightest. Several BDCs offer exposure to smaller companies. These smaller middle-market companies offer tremendous growth opportunity as well as income potential.

### 3. Superb yields

BDCs have to distribute at least 90% of their annual income to shareholders, which often means dividend yields of 10% or more. BDC Prospect Capital (NASDAQ: PSEC ) paid out 86.4% of investment income in monthly dividends during its most recent quarter, with plans to step up its dividends in every month through March 2014, as it has since 2009.

### 4. Active managers

Business development companies are active debt and equity investors that make deals with businesses that are too small to get attention

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from big investors. That's a corner where it makes sense to have an active manager making decisions on your behalf. Investing in BDCs is a sure-fire way to get access to leading companies that may be Wall Street's next hot IPO-companies.

### Prospect Capital (NASDAQ: PSEC)

Prospect Capital is a BDC that provides capital to middle-market companies and private-equity firms for refinancing, leveraged buyouts, acquisitions, recapitalizations, later-stage growth investments, and capital expenditures. PSEC is a BDC that had investments in 124 portfolio companies as of the last quarter. PSEC ranks high on the list of quality BDCs, thanks largely to its balance-sheet makeup. Due to the fact PSEC has produced an annual dividend yield between 10% - 13% over the past several years; many investors have chosen this stock for income-producing equity investments.

### Consistent Dividend

PSEC has been named as a Top 10 dividend-paying financial stock, according to Dividend Channel, which published its most recent "Dividend Rank" report. The report noted that among shares of financial companies, PSEC displayed both attractive valuation metrics and strong profitability metrics. Prospect's common stock trades at a price roughly equal to book value, giving it a yield of 12%. Since the financial crisis, it has regularly increased its monthly dividend while reporting solid performance for its underlying portfolio. The company hasn't had a single non-performing loan in nearly six years.

Strong Management Team

PCM, the managing LLC of PSEC, has a 25-year history and track record of investing in middle-market companies and managing private, high-yielding debt and equity investments. The team at PSEC has worked together for over a decade, and John F. Barry III has a history of excellence. This is a management team that has excelled in picking real equity investments. Management stakes a significant amount of its own money on its investment selection. Managers have never sold a single share of stock, and currently own more than $35 million of the company's shares.

Conclusion

The economic expansion will particularly fuel the growth of the bulk of midmarket companies, and as this BDC's goal is to invest in these companies, it will benefit them indirectly. PSEC holds favorable long-term multi-year growth rates in key fundamental data points which makes it a very desirable investment option. ■