

Business Development Company Terms Explained

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Demystifying the fees and terms used by Business Development Companies (BDCs)

BDC investing comes with several investment terms and fees that can be difficult to decipher. Understanding the terms, what they mean, and how they are applied can help investors determine if an investment is suitable for them. When deciding to commit to a fund, ensuring alignment of interest between the investment manager and the investor is crucial.

Below, we explain many terms one would see when evaluating an investment in a BDC.

Management Fee: A Management Fee, also known as an "Advisory Fee," is charged to cover the costs of managing and overseeing a fund. It covers employee compensation, overhead costs, and related fund expenses. For BDCs, it is essential to note whether the fund charges fees on the Net Asset Value (NAV) or its Gross Asset Value (GAV). The difference depends on the leverage applied to the fund. When a fund charges fees on the GAV, they are charging fees on a larger capital base, which will increase the fees paid.

Incentive Fee: The investment manager earns the Incentive Fee based on the fund's performance. This fee is designed to align the interests of the investors and the investment manager because investment managers only receive the Incentive Fee when the fund achieves a certain return threshold called a Hurdle Rate (defined below).

Hurdle Rate: The Hurdle Rate is the rate of return the investment manager must pay investors before the manager can earn an Incentive Fee.

Catch-Up: A catch-up provision allows an investment manager to realize a portion of their Incentive Fee above the Hurdle Rate. For BDCs that make regular cash distributions, the Catch-Up applies to quarterly net income distributions. Once the BDC pays investors the quarterly Hurdle Rate, the remaining funds are distributed based on the contractual split.

At PennantPark we are thoughtful about the fees that we charge on our funds, with a special focus on ensuring alignment of interest between us and our investors. We welcome a conversation; please contact invest@pennantpark.com or the professionals listed below.

Contact Us

About PennantPark:

PennantPark is an independent middle market credit platform founded in 2007 by private credit industry veteran Art Penn (most recently Managing Partner at Apollo Credit). As of March 2024, PennantPark has invested \$18.5B in over 700 private credit transactions since its inception. We have \$7.0B in AUM today from some of the world's largest and most sophisticated institutional investors. The Firm is headquartered in Miami with additional offices in New York, Chicago, Houston, Los Angeles, and Amsterdam. PennantPark primarily invests in the core middle market, defined as companies with earnings of \$10 million to \$50 million. Our industries of focus include business services, government services, healthcare, consumer, and software/technology. In addition to middle market CLOs, the firm offers its investment strategies through a range of public and private fund structures.

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