

A large, semi-transparent globe graphic is positioned in the upper right corner of the slide. It shows the outlines of continents and is overlaid with a grid of latitude and longitude lines. The globe is partially obscured by a solid blue horizontal band that spans the width of the slide, which serves as a background for the title.

# The Opaque Lending Market

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**Synopsis:** Because lending proposals vary dramatically between lenders, running a competitive financing process is the only way to surface the outlier proposal that optimizes your risk of default, available liquidity, and cost of capital. Failing to exploit this process imposes unacceptable opportunity costs on your shareholders.

Read on for our views...

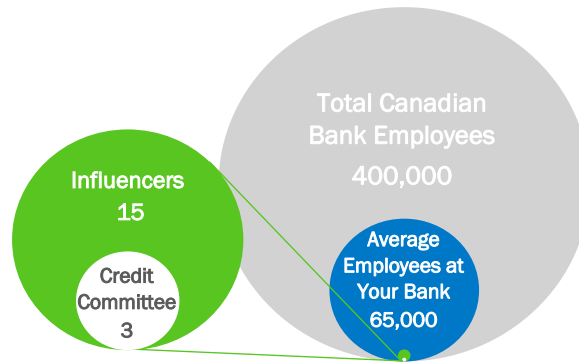


## The Opaque Lending Market

Our experience has shown that the credit markets for private companies in the US, Canada and the UK are opaque. Many of our fast-growing clients have experienced frustration with accessing capital from their existing lenders. This white paper discusses navigating and exploiting inefficiencies in the lending market to secure optimal lending terms.

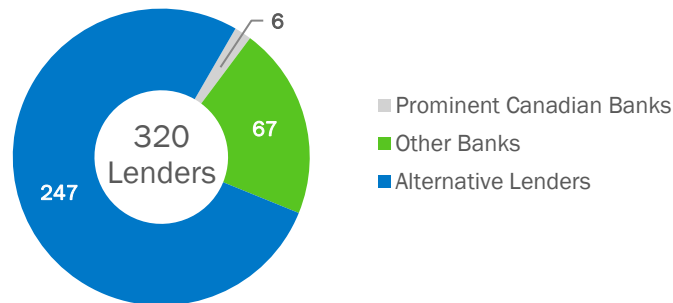
Domestic banks are the most active lenders to private companies. For businesses with complex credit needs, securing optimal financing often requires the right connections within the bank; most business owners lack these relationships. Scotiabank, the largest of Canada's "Big 5," has 89,755 employees, while the smallest, CIBC, has 44,516 employees. Even if you know which banks would lead in a competitive process, do you have *the right people* in those banks advocating for you?

**Figure 1: Key Players in Bank Lending Decisions**



Most business owners are unaware that there are alternatives to traditional banks. We maintain contact with more than 320 private lenders who actively lend to private companies. We say the lending market is opaque because there is minimal publicly available data regarding key lending metrics for private market lending.

**Figure 2: North American Lending Market**



## Exploiting Market Inefficiencies

A market is efficient when the players have access to all relevant information. The lack of comprehensive lending market research and secrecy between lenders has created inefficiencies.



These inefficiencies, however, present opportunities for strategic borrowers who understand how to navigate the system.

*“We exploit market inefficiencies by surfacing outliers and creating competitive tension between shortlisted lenders”*

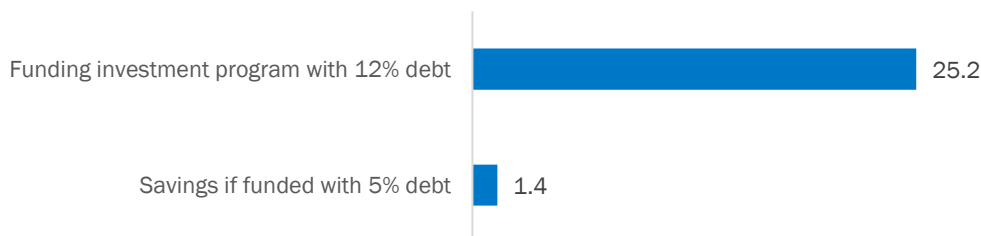
To exploit market inefficiencies, it is essential to optimize three dimensions of borrowing:

1. Cost
2. Availability
3. Flexibility

### *The First Dimension: Cost*

While many business owners focus on minimizing borrowing costs, cost should only be considered after ensuring sufficient availability and flexibility. As demonstrated in our white paper, [\*Unleashing Shareholder Value with Debt\*](#), the shareholder value impact of interest rates is a fraction of the [\*opportunity cost\*](#) of not pursuing high-return projects. In our example, financing an annual \$3.0 million investment with 12% debt versus 5% debt resulted in a \$1.4 million difference in year five shareholder value. While there is a difference, it is small compared to the \$25.2 million opportunity cost of not funding this investment program if, for example, the CEO declines to borrow to fund the program because 12% interest is “too expensive”.

**Figure 3: Year 5 Shareholder Value Impact (\$ millions)**



While we do optimize for borrowing costs in our process, we never do so at the expense of a more restrictive credit structure that compromises availability and flexibility.

*“Interest is cheap, opportunity costs, trying to operate while in the bank’s special loans group, and bankruptcy are expensive.”*

### *The Second Dimension: Availability*

When we talk about availability, we refer to the capital that lenders are willing to make available to you. Many of our clients express frustration with having to turn down high-return projects due to a lack of funding. That is why our process optimizes for availability. Like a credit card limit, a higher limit does not need to be spent; it offers the flexibility to access capital when the right opportunity arises. Greater availability ensures quick access to capital to fund your opportunities.

In our experience, securing incremental leverage on a credit facility allows you to:

1. Reduce the opportunity cost of using more expensive funding sources, such as mezzanine debt or equity, to meet the financing needs of future projects



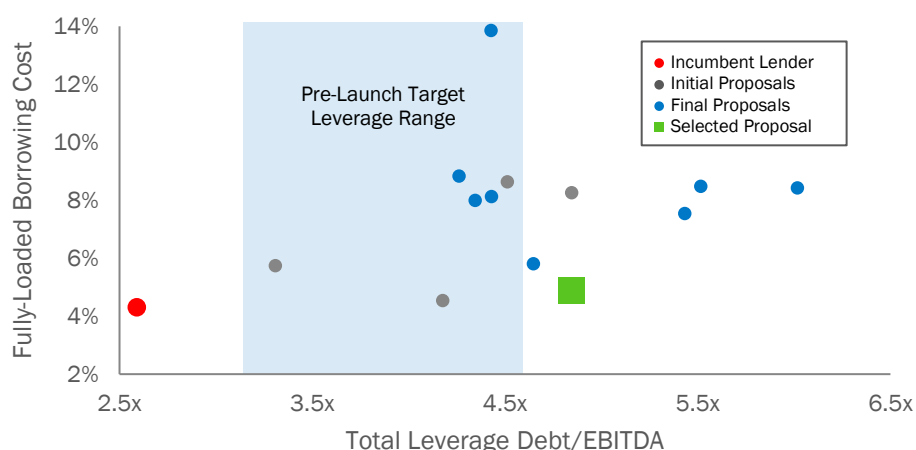
## 2. Proceed with high-return projects that otherwise would not be available to you

The economic benefits of additional availability far outweigh the borrowing costs.

Figure 4 below summarizes the differences between lending proposals one of our financing processes yielded for a client. The vertical axis plots the fully-loaded borrowing cost, while the horizontal axis plots the leverage the lenders were prepared to offer. The borrowing cost includes interest, speed of principal repayment, fees charged by the lender, and fees charged by Valitas. Even when factoring in our fees, the cost of funds for the winning proposal was comparable to the incumbent facility, yet it provided nearly double the committed funding.

This graph reveals striking differences, even though each lender received identical information. One would expect lenders to assess the same risks using the same parameters, yet their lending proposals vary dramatically.

**Figure 4: Fully Loaded Borrowing Cost versus Leverage**



Another surprising finding is that the graph shows a low correlation between:

Borrowing cost; and,

Leverage – a rough proxy for the risk assumed.

One would expect that as leverage increases, borrowing costs will rise accordingly. However, this is not the case. The old saying *you get what you pay for* clearly does not apply in this market.

If you were the borrower above looking for senior debt, you would have a poor result if you only contacted lenders to the left of the chart, as the proposal that was ultimately selected offered nearly double the leverage. For a combination of senior and mezzanine debt, some of the proposals were far superior to others on both borrowing cost and leverage.



Simply renewing your credit facility as its term ends, assuming it's the best you can get, imposes unacceptable opportunity costs on your company. Exploiting market inefficiencies through a competitive process is crucial to securing the best outcome.

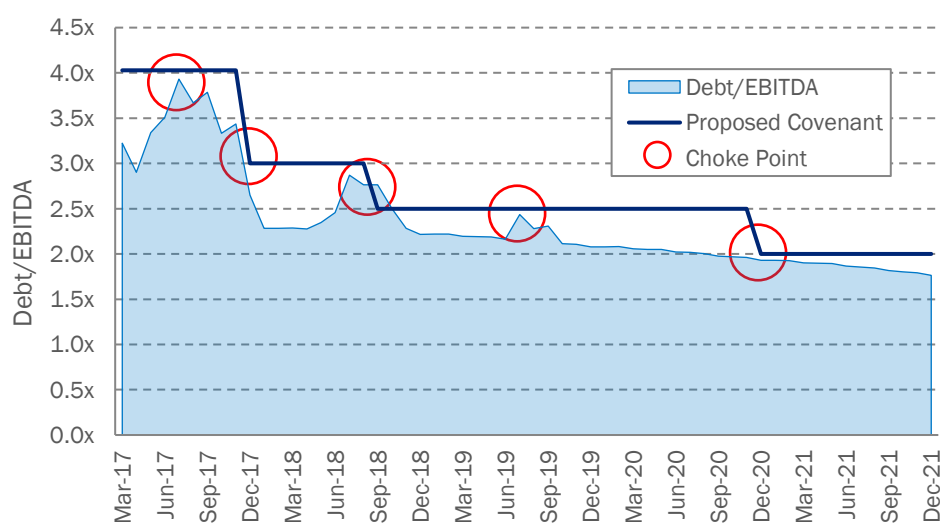
### *The Third Dimension: Flexibility*

More important than borrowing cost and the amount of financing is ensuring that the covenants on the credit facility are flexible enough that you will not breach them because of normal variability in your operating results. The last thing you want to do is manage your business to meet your covenants or worse, deal with the special loans group after breaching them instead of unleashing shareholder value.

While a proposal may look good at first glance due to low pricing or a large amount of committed capital, the covenant package is especially important. The challenge is that it is also less transparent. Breaching covenants will result in problems with your lender that will cost you both money and time to resolve. Worse, these costs are small compared to the opportunity costs imposed by [freezing] your lending and distracting you from your mission. To identify potential choke points or breaches, a credit model must be developed for the life of the credit facility. The credit model monitors the headroom under a range of operating scenarios to ensure ample convent room so that negative surprises (or a recession) will not cause breaches.

The example below reflects an acquisition financing we closed recently. We developed a five-year forecast for the client, including debt schedules and covenant tracking. By adjusting the model to reflect the terms of each proposal, we identified points over the course of the loan where breaches were most likely to occur. From there, we negotiated changes to the covenant package to increase the proposal's flexibility. In this case, we pushed the step-downs out by a quarter.

**Figure 5: Covenant Forecasting to Prevent Future Breaches**



### *Comprehensive Assessment of Your Lending Proposals*

In addition to exploiting market inefficiencies by surfacing outlier proposals, applying competitive tension between lenders to improve their initial lending proposals is crucial. One of the key tools we



use is our lender grid. Earlier, we examined a graph that compared proposals based on funding costs and leverage amounts. These are just two of over 10 factors that we assess using the lender grid. This tool informs the selection of our lender shortlist and negotiation strategy with that shortlist.

The lender grid below outlines three (of several) proposals we assessed for one of our clients, including key factors such as operating line utilization, minimum headroom on the financial covenants, terms, and amortization schedules. We leverage this information to encourage lenders to refine their terms to enhance their competitiveness. This holistic perspective enables our clients to make informed decisions about their optimal funding solution.



**Table 1: Sample Lender Grid**

	Lender A	Lender B	Lender C
<b>Leverage</b>			
At Close	0.59x	0.59x	0.62x
<b>Committed Amount:</b>			
1) Operating Line Facility	\$6 million	\$6 million	\$5 million
2) Term Loan Facility	\$5 million; single-draw	\$3.68 million; single-draw	\$5 million; single-draw
3) Acquisition Facility	\$10 million DDTL; Sub limit for equipment leases subject to S/H buyout valuation	\$10 million DDTL; Sub limit for equipment leases subject to S/H buyout valuation	\$10 million DDTL
4) Equipment Facility	See above; non-revolving	See above; non-revolving	\$7.5 million; revolving; the total drawn on Equipment Facility and Operating Line not to exceed \$10 million
<b>Term and Amortization</b>			
<b>Term Loan Facility</b>			
Term	5 years	5 years	3 years
Amortization	Straight-line over 10 years	Straight-line over 5 years	Straight-line over 5 years
<b>Acquisition Facility</b>			
Term	5 years	5 years	3 years
Amortization	Straight-line over 10 years	Straight-line over 5-7 years	Straight-line over 7 years
<b>Equipment Facility</b>			
Term	5 years	5 years	3 years
Amortization	Straight-line over 10 years	Straight-line over 5-7 years	Straight-line over 7 years
<b>Covenants and Headroom</b>			
Total Debt to EBITDA	3.50x; Senior Funded Debt; minus up to a maximum of \$1 million cash	2.50x - 2.75x with step-downs TBD; Senior Funded Debt	N/A
Minimum Headroom	37.3%	17.1%	N/A
Date	01/31/25	01/31/25	N/A
Total Debt to EBITDAR	N/A	N/A	3.00x; Senior Funded Debt
Minimum Headroom	N/A	N/A	22.0%
Date	N/A	N/A	01/31/25
FCCR	1.20x	1.15x	1.10x
Minimum Headroom	(49.1%)	(41.8%)	18.6%
Date	07/31/25	07/31/25	09/30/25
Corporate Distributions	TBC	TBC	Permitted if: Funded Debt/EBITDAR is <2.25x & FCCR compliance before/after distributions
<b>Incurrence Tests</b>			
	Total Debt/EBITDA <3.25x on Acquisition and Equipment Facility	Total Debt/EBITDA <2.50x-2.75x on Acquisition and Equipment Facility	Total Debt/EBITDAR <2.50x on Equipment Facility
<b>Cost of Funds</b>			
Fully-Loaded Cost (IRR)	10.5%	10.8%	11.7%
WACC 25% 7.0x TEV	24.4%	24.7%	23.9%
WACC 45% 7.0x TEV	43.8%	44.3%	42.5%
Commitment Fee	0.5%	0.2%	TBD
Standby Fee	0.5%	TBC	0.25%
<b>Liquidity (in \$000s)</b>			
Operating Line Limit	\$6 million	\$6 million	\$5 million
Max Operating Line Utilization	36.4%	45.1%	10.5%
Date	07/31/25	07/31/25	04/30/24
Minimum Available Liquidity	8,108	2,585	4,771
Date	01/31/25	05/31/24	01/31/25



Given the staggering opportunity costs of accepting sub-optimal funding, the executive team that declines the opportunity to exploit the inefficiency of the private lending market is indifferent to, if not in contempt of, their shareholders' interests. If you are interested in assessing how much additional funding may be available to your company and how much more flexible your covenant package could be, don't hesitate to get in touch with me at [paris.aden@valitascapital.com](mailto:paris.aden@valitascapital.com).



## About Valitas

Valitas Capital Partners is a premier transaction advisory firm known for its innovative shareholder value engineering system. This unique approach helps clients unlock at least \$25 million in previously inaccessible shareholder value.

Our clients rely on us when they:

- Aim to triple their company's value in five years or less, valuing our proven advisory experience.
- Want to sell their company and ensure they achieve the best possible outcome.
- Seek liquidity for specific shareholders through buyouts and recapitalizations.
- Are frustrated by missed growth opportunities due to their bank's limitations.

How we drive success for our clients:

- We unleash remarkable shareholder value with our shareholder value engineering system.
- We bring extensive experience navigating mission-critical projects.
- We are committed to deep, long-term client relationships

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## About the Author



### Paris Aden, Partner

Paris Aden is the founding Partner of Valitas Capital Partners. Since 1994, he has been involved with more than 100 M&A transactions with an aggregate value exceeding \$80 billion. He has advised clients at Morgan Stanley, Credit Suisse First Boston and RBC Capital Markets and has acted as a private equity investor at Clairvest Group where he served on portfolio company boards. Paris was also a co-founder of Alluence Capital Advisors, a mid-market M&A advisory boutique that focuses on cross-border transactions.

Paris is recognized as an expert in business strategy, M&A and corporate finance. Previous roles and speaking engagements include:

- Lecturer at the Stephen J.R. Smith School of Business at Queen's University in their Master of Finance (MFIN) program
- M&A subject matter expert for Moody's Analytics' Advanced Capital Markets Program for capital markets professionals
- Three-time expert panel moderator for the Toronto Business Transitions Forum
- TEC Canada "2018 Speaker of the Year" recipient
- Guest speaker for various industry and business leadership organizations

Paris formed Valitas to meet the unanswered needs of ambitious business owners seeking to:

- At least triple their business value in five years or less; or
- Are seeking an elite advisory boutique as their trusted advisor for their complex, mission-critical transactions.