# Closing the gap between growth businesses and alternative lenders

By Gary Palmer

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As South Africa continues to drift in the doldrums of economic stagnation, the apparent disconnect between traditional lenders and entrepreneurs seems to be widening. This is especially highlighted when it comes to growth finance, with many business owners unaware of products such as mezzanine finance and, even if they know about it, are unaware how to access it.

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In contrast, trends in the US show non-traditional lenders investing more and closing bigger deals than the banks. And while there is no doubt that there is still money to be had in the local market, most business owners simply don't know where to find it.

## Why mezzanine is right for growth

Mezzanine debt is the middle layer of capital that falls between secured senior debt and equity. This type of capital is usually not secured by a first charge over assets, and is lent based on a company's ability to repay the debt purely from cash flow. So, the primary security holder would be the base finance secured against assets and personal securities – most often from the banks.

Mezzanine finance is particularly attractive to established and growing companies as business owners don't have to part with equity to secure the deal. Terms tend to be more flexible and the funders will often assign a dedicated person to work with companies who have borrowed money.

## Taking a new look at lending

While South Africa banks are among the finest in the world, our traditional institutions are by nature (and by regulatory requirement), fairly conservative in their lending practices. And, it's fair to assume that as the economy gets tougher, they will become more hawkish.

What’s more, our alternative lending sector is not as mature as that of Australia, the UK or the US where there are qualified intermediaries between the banks and the clients. The role of independent finance broker is common and respected in many international markets. This is sadly not the case in the local markets as banks have their own sales teams. An unfortunate consequence is that banks will often not think to refer on clients who may not have made their strict criteria, but who may be appealing to a non- traditional lender, impinging deal flow and stunting economic growth.

To put it into context, according to the Statista Digital Market Outlook, in 2018, the global alternative credit market had a transaction value of $197.6bn. Comparing the three major regions US, China and Europe, the size of the Chinese alternative lending market is described as ‘remarkable’ - with a volume of $178.9bn, with China accounting for 91% of the global market in 2018.

That said, there is a lot going for local businesses trying to access growth finance. With well over 100 alternative lenders available, working with an independent lender, business leaders are in a great position to find a lender who understands their business and can offer a deal to suit their growth strategy.

## The right deal with the right partner

Accessing suitable alternative/ mezzanine funding can significantly boost a company looking to grow, but which does not want to dilute shareholding through an equity deal. An additional benefit is that since mezzanine funding is often given to founder-run companies, some of whom may not have all the experience of running a growing company, working with a dedicated mezzanine partner can make the cat’s cradle of corporate governance and reporting a little less painful.

Working with an independent partner can also give a company the edge when they approach the lender. Understanding exactly what is required from the lender means an independent lending partner can help a business prepare all the correct documentation, and more importantly, present it in a way that ticks all the right boxes for the alternative lender.

While South Africa may still be in its infancy when it comes to alternative lending and our economy may be little lackluster at the moment, but there is every reason for established companies to seize opportunities when they see them – knowing that if the deal is right, the finance can be found.

## ABOUT THE AUTHOR

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