SALE LEASEBACKS

Efficient and Flexible Capital for Middle-Market Companies

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Executive Summary

Middle-market companies today face increased borrowing costs, tighter covenants, and reduced flexibility from traditional lenders. Sponsors and operators need capital solutions that offer stability and zero dilution. Sale-leasebacks (SLBs) deliver these benefits by converting owned real estate into long-term, covenant-free capital.

I. Why Middle-Market Companies Are Turning to Sale-Leasebacks

SLBs unlock equity trapped in critical facilities—often reflected on the balance sheet at well below market value.

- **Utility:** SLBs unlock capital for acquisitions, deleveraging, refinancing maturing loans, strategic investments, or growth initiatives.
- **Result:** Operators gain strategic flexibility to execute business plans without adding near-term covenant compliance pressure or refinancing risk.

II. SLBs vs. Corporate Debt: Cost & Flexibility Advantages

1. The Cheapest Incremental Dollar

- At a ~7% to 8% implied annual rent, SLB proceeds are significantly cheaper than raising incremental capital through mezzanine debt (13–17%) or preferred equity (15–25%+)

2. Breaking the Refinancing Cycle

Traditional loans force CFOs to plan in 3-to-5-year increments, creating constant "refinancing cliffs."

- **Long-Term Planning:** SLBs provide 15–25 years of predictable occupancy costs.
- **Operational Security:** SLBs allow management to focus on long-term capital planning rather than worrying about near-term maturity dates.

3. True, Covenant-Free Capital

Unlike bank loans or private credit, SLBs do not impose onerous covenants:

- No leverage tests
- No DSCR (Debt Service Coverage Ratio) requirements
- No amortization or sweep provisions
- No balloon payment at maturity

4. Balance Sheet & Credit Enhancement

When SLB proceeds are used to retire existing debt, the impact is transformative:

- **Leverage Reduction:** Swapping debt for lease obligations lowers total funded debt.
- **Interest Coverage:** Replacing high-interest floating rate debt with fixed rent payments improves coverage ratios.
- **Strengthened Borrowing Capacity:** A cleaner balance sheet positions the company for more favorable terms on future working capital facilities and other borrowings.

III. Strategic Advantages of Sale-Leasebacks for Operators & Sponsors

- **Operational Autonomy:** No lender interference in business operations.
  - *The sale-leaseback removes the lender from the boardroom and prevents technical defaults during temporary operational dips.*
- **ROI Enhancement:** Enhances sponsor IRRs by reducing the equity investment required at acquisition.
- **Asset-Lite Transformation:** Converting owned real estate to a lease structure creates an asset-lite balance sheet, further enhancing returns on invested capital.
- **Non-Dilutive Growth:** Provides growth capital (M&A, Strategic Investment, or CapEx) without issuing equity.
- **Asset Security:** Ensures long-term control of mission-critical facilities, with extension options providing continued operational certainty.

IV. Why Sale-Leasebacks Are Attractive Now

- **The "Rate Shock" Gap:** Borrowing costs from traditional sources are elevated significantly compared to expiring facilities from the 2020–2022 era.
- **Lender Retrenchment:** Banks are pulling back from cash-flow lending, while private credit is tightening loan sizing metrics.
- **Institutional Demand:** There is robust appetite for SLB investments, ensuring liquidity is available even when debt markets freeze.
- **Faster, More Certain Execution:** SLBs offer streamlined closing processes compared to syndicated debt transactions.

V. The Execution Advantage: Partnership Matters

Not all capital partners are created equal. In a complex market, who you transact with matters!

- **Certainty of Execution:** A partner with a track record across tenant profiles—from middle-market operators to publicly traded companies—significantly reduces execution risk and ensures speed to closing.
- **A Growth Partner:** The right partner views the landlord/tenant relationship as a platform. Just as a commercial lender grows with a company, a creative and financially strong landlord can provide follow-on capital for future expansion, renovations, or acquisitions.
- **Relationship Continuity:** Unlike fee-driven lenders paid by the transaction, a long-term landlord becomes a capital partner invested in the tenant's operational success.

Conclusion

Sale-leasebacks have become one of the most powerful financing tools available to middle-market companies and private equity sponsors. By providing long-duration, non-dilutive, covenant-free capital, Sale Leasebacks offer significant capital structure and operational advantages:

- **Enhance credit profiles**
- **Support growth initiatives**
- **Drive long-term strategic flexibility**
- **Lower cost than alternative capital sources**

For operators and sponsors seeking improved capital efficiency with enhanced operational flexibility and capital partner alignment, long-term sale-leasebacks with experienced partners may prove to be a superior capitalization strategy.

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