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Op Assist Earnings Call
Conference Call
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Operator: Welcome to the Investcorp Credit Management BDC Incorporated Scheduled Earnings Release for Third Quarter Ended March 31st for today's call are Mike Mauer, Suhail Shaikh and Rocco DelGuercio. Operator assistance is available at any time during this conference by pressing 0, pound (#). A question-and-answer session will follow the presentation. I would like to now turn the call over to your speakers. Please begin.

Michael Mauer: Thank you operator, and thank you for joining us on our third quarter call today. I'm joined by Suhail Shaikh, my co-CIO, and Rocco DelGuercio, our CFO. Before we begin, Rocco will give our customary disclaimer regarding information and forward-looking statements. Rocco.

Rocco DelGuercio: Thanks, Mike. I would like to remind everyone that today's call is being recorded and that this call is the property of Investcorp Credit Management BDC. Any unauthorized broadcast of this call in any form is strictly prohibited. Audio replay of the call will be available by visiting our investor relations page on our website at icmbdc.com. I would also like to call your attention to the safe harbor disclosure in our press release regarding forward-looking information and remind everyone that today's call may include forward-looking statements and projections. Actual results may differ materially from these projections. We will not update forward-looking statements unless required by law. To obtain copies of our latest SEC filing, please visit our investor relations page on our website. At this time, I'd like to turn the call back over to our chairman and CEO, Michael Mauer.

Michael Mauer: Thank you, Rocco. March quarter marks the third quarter of our fiscal year. In the beginning of 2023, there continued to be limited, new issuance and refinancing opportunities driven by broader market uncertainty and high interest rates. In the second half of the March quarter, we saw the level of activity pick up slightly. The collapse of Silicon Valley Bank and Signature Bank led to a broadly accepted credit contraction for middle market banks which will further increase our opportunities.

We saw our deal flow pick up after a slow December quarter primarily driven by secondary opportunities across all industries. Especially during periods of market volatility, we actively focus on opportunities in both existing portfolio companies across our platform as well as investors we are familiar with.

During the quarter, we invested in one new portfolio company and three existing portfolio companies. We have typically found in a highly competitive market environment, our best opportunities come from companies we already lent to as these tend to have known performance and better structures. The investments we made during the quarter and after-quarter end were all sponsored-backed. Even in a competitive environment, we remain optimistic about our pipeline and believe our portfolio is well-positioned to benefit from any further increase in interest rates. The weighted average yield of our debt investments during the quarter increased approximately 25% to 13.4% from 10.7% at 12/31.

Although our pipeline is robust, we continue to very selective when investing in new credits. We remain focused on investing in high free cash flow and recession-resistant businesses. The credit quality of our current portfolio remains stable. Despite the challenging market environment, the weighted average EBITDA of our debt investments improved quarter over quarter. This is supported by the substantial amount of equity cushion in our portfolio companies provided by well-established middle market sponsors. Our weighted average loan-to-value ratio for all debt investments is approximately 50%. We're proud of the continued improvement in the credit quality of our portfolio. Suhail will now walk through our investment activities during the March quarter and after quarter-end. Rocco will go through the financial results. I'll finish with commentary on our non-accrual investments, our leverage, the dividend and our outlook for the rest of 2023. As always, we'll end with Q&A.

With that, I'll turn it over to Suhail.

Suhail Shaikh: Thank you, Mike. As Mike mentioned, we've been seeing a steady flow of new opportunities. These typically fall in two main categories. Add-on as secondary purchases of existing portfolio investment and opportunistic secondary purchases and refinancing of new companies. We're beginning to see some new responsive platform transactions, but the volume is significantly below our historical experience. We invested in our portfolio and one new portfolio company and three existing portfolio companies this quarter. We also fully realized the position in two portfolio companies. During the quarter, funding for commitments and new investments total approximately $11.1 million. In the same period, repayments total approximately the same amount of $11 million.

We invested in Sandvine, a portfolio company of Francisco Partners. We have been an investor in Sandvine and other funds for over four years. The company is a leading provider of Active Network Intelligence & Security Solutions for network operators and enterprises globally. We invested in the first lien term loan. Our yield at cost is approximately 11.8%. We opportunistically added to our position in two existing portfolio companies. First we invested in the first lien term loan of Laseraway. Laseraway is a leading chain of laser hair removal and noninvasive aesthetic dermatology centers. The yield at cost is 11.3%. Second, we invested in a priority term of loan of Bioplan. Bioplan provides packaging and sampling solutions to the beauty and fragrance industry. Our yielded cost is approximately 15.8%. We also participated in a small equity raise with Techniplas, one of our existing portfolio companies. Techniplas is a global manufacturer of plastic components for the automotive industry.

As mentioned above, we fully realized our position in Liberty Oil Field Services which was refinanced. Our fully realized IRR was approximately 11.3%. We also fully realized a position AgroFresh, which was repaid as part of a team private transaction by Paine Schwartz Partner. Our fully realized IRR was approximately 10%. After quarter-end, we invested in two new portfolio companies. First, we invested in the first lien term loan of PureStar, also known as AMCP Clean Acquisition Company. This is a good example of an opportunistic secondary purchase of a credit that we had been tracking. PureStar is a portfolio company of Cornell Capital. It’s one of the largest commercial laundry providers to the hospitality industry in the US. We invested in the first lien term loan and delayed draw term loan. Our yielded cost is about 15.7%.

We invested in the first lien term loan of American Auto Auction Group, formerly known as XLerate. This is another example of an investment that we own in other portfolios and we’re able to find an attractive opportunity to purchase in the secondary market. Our Brightstar Capital Portfolio company, XLerate or American Auto Auction Group is a fully service used vehicle auction services provider for B2B customers. Our yield at cost is 13.3%.

Using the GICS standard as of March 31st, our largest industry concentrations were: trading company and distributors at 15.9%, professional services at 14%, followed by IT services at 10.8%. Commercial services and supplies are at 6.5% and software remain at 6.2%. Our portfolio companies and 20 GICS industries as of quarter end, including our equity and warrant positions.

I'd now like to turn the call over to Rocco to discuss our financial results.

Rocco DelGuercio: Thanks, Suhail. For the quarter ended March 31, 2023, our net investment income was $2.5 million or $0.18 per share. The fair value of our portfolio was $221.3 million compared to $228.6 million on December 31. Our net assets were $88.2 million, a decrease of 3.6% from prior quarter. Our portfolio's net decrease from operations this quarter was approximately $1.1 million. Our debt investments made during the quarter had an average yield of 12.8%. Our realizations and repayments during the quarter had an average yield of 11.9% and our average IRR was 10.7%. As Mike mentioned, the weighted average yield on our debt portfolio increased 270 basis points to 13.4% as of December 31. As of March 31, our portfolio consisted of 35 portfolio companies; 90.6% of our investments were in first lien and the remaining 9.4% is invested in equity, warrants and other positions. 99.6% of our debt portfolio was invested in floating rate instruments and 0.4% in fixed rate investments.

The average floor of our debt investment was 1.1%. Our average portfolio company investment was approximately $6.3 million and our largest portfolio company investment is Fusion at $12.5 million. We had a gross leverage of 1.65% and a net leverage of 1.49% as of March 31 compared to 1.55 gross and 1.46 net, respectively, for the previous quarter. As of March 31, we had four investments on nonaccrual which included PGI revolver and three investments in 1888. This is a decrease of four investments from the previous quarter. With respect to our liquidity, as of March 31, we had approximately $14.1 million in cash, of which $11.2 million was restricted cash with $33.1 million of capacity under our revolving credit facility with Capital One. Additional information regarding the composition of our portfolio is included in our Form 10, which was filed yesterday. With that, I'd like to turn the call back over to Mike.

Michael Mauer: Thank you, Rocco. As mentioned last quarter, we acquired an SMA and had an initial close on our institutional fund. This doubled our platform AUM, expanding our level of investable assets and reducing average expenses across the funds. We also have an opportunity to grow the platform throughout the year. We believe that the scale and experience of our expanded team and platform positions us to be more meaningful to the market in terms of sourcing and origination.

I would like to also address that we have made significant headway in completing our portfolio rotation initiative. The number of portfolio companies on nonaccrual were reduced from eight in the previous quarter to four investments in the current quarter, those four investments across two companies. First, on Deluxe, we have recovered 8.9% of our principal and receive principal and interest representing 106% of our cost on that position to date. We believe future recoveries are likely to be minimal at this stage and have decided to write off the remaining position. For PDI, all remaining value is expected to be recovered in the priority revolver which remains on nonaccrual. We have written off our positions in the first lien and second lien loans and are not expected to realize any recovery on those, and as such, those were written off. Bioplan successfully completed a balance sheet restructuring during the quarter. We currently hold positions in the take-back term loan, priority term loan and the common equity. The two loan positions are on accrual, and we're excited about the company's prospects going forward. In summary, we expect significant progress on the remaining nonaccruals over the next 12 months.

Our NAV declined 3.6% this quarter. Equity positions represented a majority or $2.3 million of this decline. While this is disappointing, we believe that we will see a bounce back in the coming quarters. We had 3 portfolio companies which declined in value by half a million dollars or more. First, we marked down our investment in ArborWorks. ArborWorks is a vegetation management company providing services to utility companies. Their results have been challenged by weather patterns in California, their largest market. We reduced the mark in our equity position in Techniplas due to increased margin pressures and lower production volumes in the auto industry. We also marked down our equity position in Fusion due to changes in model inputs related to market conditions. Our gross leverage this quarter was 1.65 above our guidance of 1.25 to 1.5 times. Our net leverage was 1.49 times which is within the target range. As mentioned last quarter, we expect to see our gross and net leverage generally converge. As of May 15th, our gross and net leverage were 1.59 times and 1.56 times. As we have previously stated, the adviser will waive the portion of our management fee associated with base management fees over one turn of leverage.

We covered our March quarterly dividend with NII. The company is expected to earn its dividend through the next quarter ending June 30th. On May 4th, 2023, the board of directors declared a distribution for the quarter ended June 30th, 2023, of $0.13 per share payable on July 7th, 2023, to stockholders of record as of June 16th and a supplemental distribution of $0.05 per share, payable on July 7th, 2023, to stockholders of record as of June 16th, 2023. As we continue into the second half of 2023, we remain very optimistic about our team's ability to deploy capital in high-quality credits. Our growing platform will allow us to be more meaningful as club partners, gives us expanded reach into origination and brings new and valuable relationships with private equity sponsors. Our growth will provide you, our investors, an increasingly diversified portfolio as we have access to a larger set of opportunities in the market. Our goal has not wavered and has always focused on capital preservation and maintaining a stable dividend.

This concludes our prepared remarks. Operator, please open the line for Q&A.

Operator: Thank you. Ladies and gentlemen, at this time we will conduct the question-and-answer session. If you would like to state a question please press 7, pound (#) on your phone now and you will be placed into queue in the order received or press 7, pound (#) on your phone any time to remove yourself from the queue. Please listen for your name to be announced and be prepared to ask your question when prompted. We are now ready to begin.

Our first question is from Chris Nolan. I'm opening the line now. Go ahead please.

Christopher Nolan: Hey, guys, congratulations on improving the nonaccruals in the quarter. On Deluxe, did I hear you correctly that there was an 89% recovery?

Michael Mauer: I believe it's 80.9% recovery on costs, excluding the interest. Including the interest, it was 106% of our invested capital.

Christopher Nolan: Okay, great. In the comments that you guys participated in equity raised by one of your portfolio companies, would that be a rights offering?

Michael Mauer: It was a rights offering we participated so we were not diluted down. It was less than half a million dollars.

Christopher Nolan: Okay. I guess on that note, given that your focus on sponsored deals, has there been conversations from your sponsors where, if they have to raise equity for their portfolio companies, they want you to participate. What are your thoughts around that?

Suhail Shaikh: Chris, this is Suhail. The short answer is no. I mean, I think in a couple of situations, we're looking at sponsors come to us with a preferred equity investment opportunity so that they don't have to refinance the existing capital structures, but as an equity co-invest, if that's what you're looking for, no. We haven't asked to participate in any equity with outside sponsor.

Christopher Nolan: Great, thanks.

Michael Mauer: Now, just to clarify, in initial investment, we have looked at small equity co-invest and you'll see them in our portfolio, but that's rare, few and far between and that's our option.

Christopher Nolan: I guess, final question on leverage. Given the uncertain economic times, is the intent to maintain leverage in your target area which is the last I know 1.4 times to 1.5 times?

Michael Mauer: The answer is yes. As we continue to look at new opportunities, as we reinvest money coming back in, we're not looking to invest incremental capital, but reinvestments are all - never say 100%, but are principally lower risk, more equity, better covenants. So, we're improving the quality of the portfolio and maintaining a consistent leverage against that.

Christopher Nolan: Great. That's it for me. Thank you.

Michael Mauer: Thank you, Chris.

Operator: Thank you very much. Our next question is Mr. Robert Dodd. I'm opening the line now.

Robert Dodd: Okay. Thank you. I want to first follow-up on Chris's question. Obviously, you're 1.59 now in May on leverage, what kind of time frame do you expect to get back down in the target range of 1.41 times?

Michael Mauer: I'd expect at quarter end that we're back in that range. That's the expectation. If you look at 12/31, net leverage was 1.46. At 3/31, it was 1.49 million we'd expect to be somewhere around there on a net leverage at 6/30.

Robert Dodd: Got it. Thank you. Then on the credit – I mean, in your opening remarks when you talked about disruption in the bank granted Capital One isn't exactly a regional. But if you started having any conversations with them about amending the facility, I mean it does not mature until 2026, but the revolving period or an investment period ends next year. So, any preliminary discussions on the return on that front?

Michael Mauer: We've continued to have an active dialogue with Capital One, all positive. There's been no indication that they are starting to pull back on the credit that they want to commit to us or the sector. But yes, we have ongoing dialogue with them.

Robert Dodd: Got it. Thank you. Then one last one, if I can. I'll go ahead with this question again. Techniplas, I mean you said you participated in the rights issue, put in less than a half a million dollars, but then it got written down, obviously, during the quarter because of margin pressures, et cetera, that you talked about. I mean, yes, you didn't want to be diluted, but at the same time, you're putting more capital in one of your larger write-downs this quarter. So, could you give us any more thoughts on the capital purpose beyond non-dilution which may or may not be beneficial to shareholders?

Michael Mauer: Yes. I'd make a couple of observations. Number one is kind of from our cost basis of that equity, we're averaging down. That having been said, we don't want to keep putting more money in if we don't think this will recover. We think they are a critical supplier to Tier 1 OEMs to top platforms. I think we've all seen the inventory constrained, especially, from the foreign production, and they've been hurt by that. The forecast is that that's starting to normalize but I, personally and anecdotally, I have not seen that fully normalized. We expect this to recover over the next 12 to 24 months and did not want to see that over a small investment hurting our existing investment.

Robert Dodd: Got it. Thank you.

Michael Mauer: Thank you very much, Robert.

Operator: If you'd like to ask a question, please press 7, pound (#) on your phone. Again, that's 7, pound (#) if you'd like to ask a question. Our next question is from Paul Johnson.

Michael Mauer: Hi, Paul.

Paul Johnson: Good afternoon, guys. Thanks for taking my question. Yes, I only have one today, but I want to get a sense. I mean, it sounds like you guys have obviously made some investments in the platform since Investcorp came on, possibly raised some funds along the way. I was just hoping to maybe get a sense of like how many people, I guess, at Investcorp today, including yourselves are working directly on the BDC?

Michael Mauer: Well, the direct team on the BDC is about 12 people. Then indirectly, there's another 30 people in Investcorp Credit which expands to other liquid and separate accounts that we leverage off of research and flow and relationships, and then there is the middle market private equity team that we interact with constantly from a standpoint of, I'll call it, club origination, networking and other deal flow opportunities. So, it's a broad base that we work within at Investcorp.

Paul Johnson: Got it. Thanks for that. Then I guess just with the leverage, obviously, it sounds like it's kind of a focus to get that down further back in the line with the target range. But among all the other funds that you have access to with Investcorp. I mean, has the, I guess, maintenance of leverage then any kind of a constraining factor for you guys in terms of participating on deals?

Michael Mauer: No, it has not.

Paul Johnson: Okay. Thanks. That's all for me.

Michael Mauer: Thank you very much, Paul. We appreciate it.

Operator: There are no more questions at this time.

Michael Mauer: Thank you very much, operator, and thank you, everyone, for dialing in.

- End of Recording -