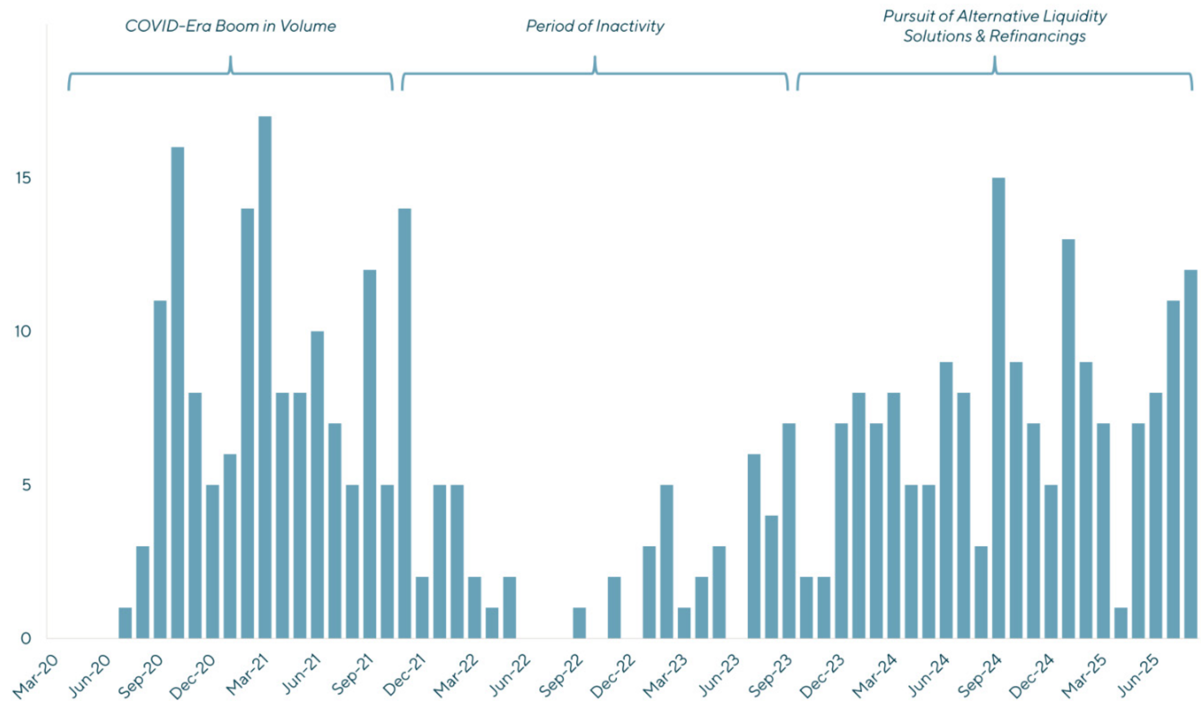
Dividend Recapitalization Activity Remains Robust

Driven by an availability of capital and a desire to return capital to their investors, private equity sponsors continue to pursue alternative exit strategies, including dividend recapitalizations. Despite persistently higher base rates, tariff uncertainty and stubborn inflation, the availability of capital and competition within private credit and broadly syndicated loan markets has put downward pressure on credit spreads and has made it more attractive for sponsors to refinance or recapitalize performing portfolio companies. Additionally, floating rates have decreased following recent federal funds rate cuts, which has further reduced all-in borrowing costs. Given current market dynamics, sponsors have increasingly utilized dividend recaps as a capital cost-effective way to enhance fund Distributions to Paid-In Capital (DPI).

In our latest perspective, Lincoln International explores the current market environment, provides an overview of dividend recaps and why many sponsors continue to pursue them and discusses how solvency opinions can mitigate risks faced by directors and the sponsor in these transactions.

Dividend Recap Market Environment

Number of Dividend Recapitalizations[1]



Following the slowdown post-pandemic, the dividend recapitalization activity has increased as sponsors pursue alternative liquidity solutions and refinancings.

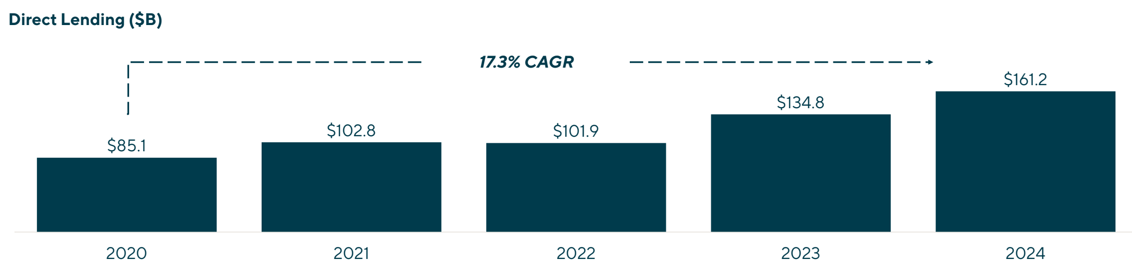
What Does the Current Environment for Dividend Recaps Look Like Compared to the last several years?[2]

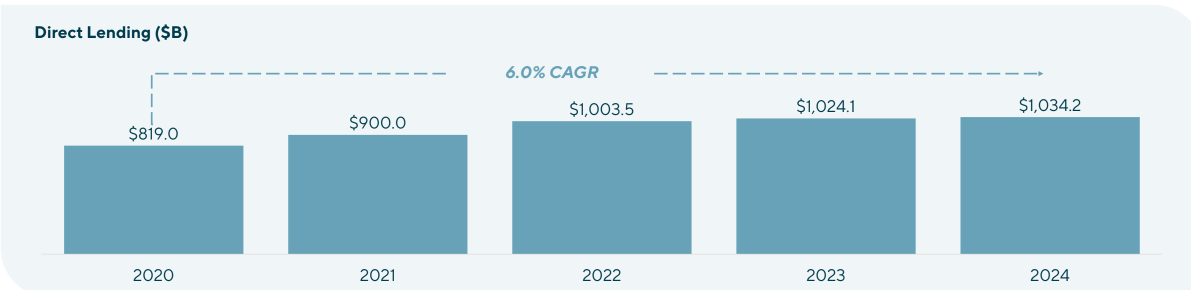
	July 2020 – November 2021	December 2021 – October 2023	November 2023 – August 2025
Market Activity (# of deals)	**150 (Monthly Average: ~8.8)**	**48 (Monthly Average: ~2.3)**	**166 (Monthly Average: ~7.5)**
Spreads (1)	**1st Lien: S + 400 (350 – 450) 2nd Lien: S + 725 (675 – 775)**	**1st Lien: S + 425 (375 – 475) 2nd Lien: S + 725 (675 – 775)**	**1st Lien: S + 350 (300 – 400) 2nd Lien: S + 550 (500 – 600)**
Illustrative FCCR (2)	**~2.00**	**~1.25**	**~1.25**
All-In Yields	**SOFR: 0% (0.75% Floor) All in 1st Lien: 4.50% - 5.50% All in 2nd Lien: 7.75% - 8.75%**	**SOFR: 3.75% All in 1st Lien: 7.75% - 8.75% All in 2nd Lien: 11.0% - 12.00%**	**SOFR: 4.75% All in 1st Lien: 8.00% - 9.00% All in 2nd Lien: 10.25% - 11.25%**

Although all-in yields remain elevated, lower spreads have made refinancing an attractive option for some borrowers.

U.S. Private Capital Markets Dry Powder Continues to Grow[3]

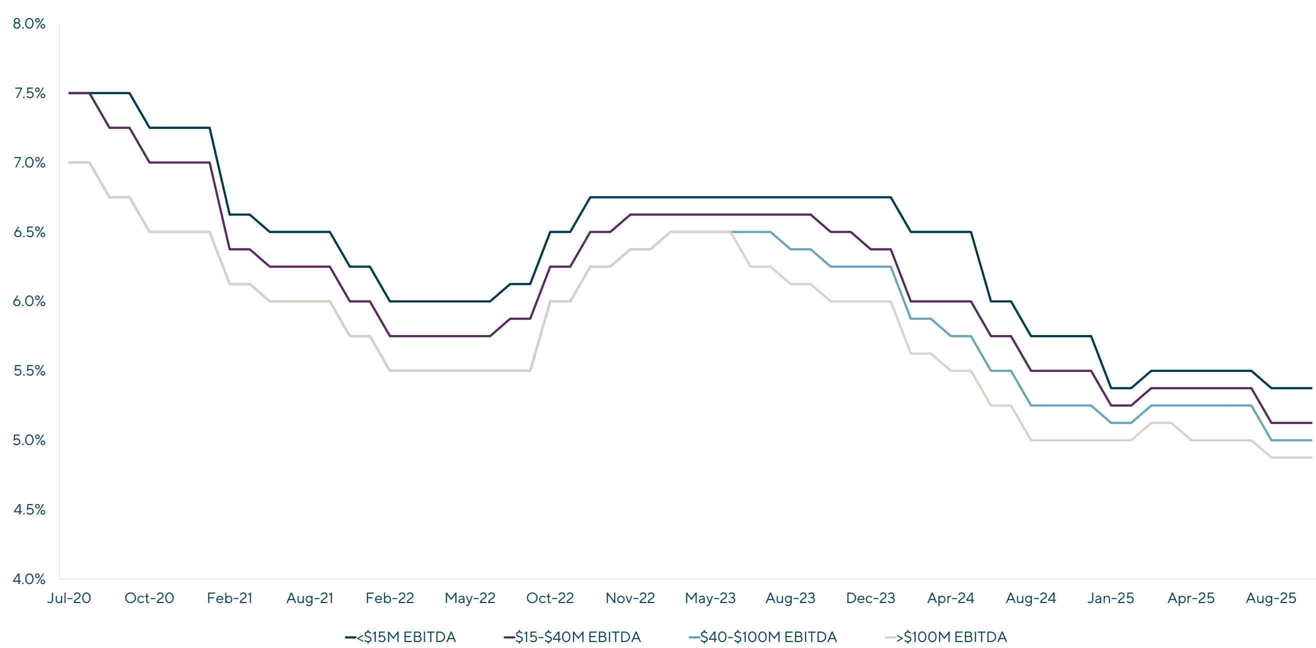
Direct Lending ($B)





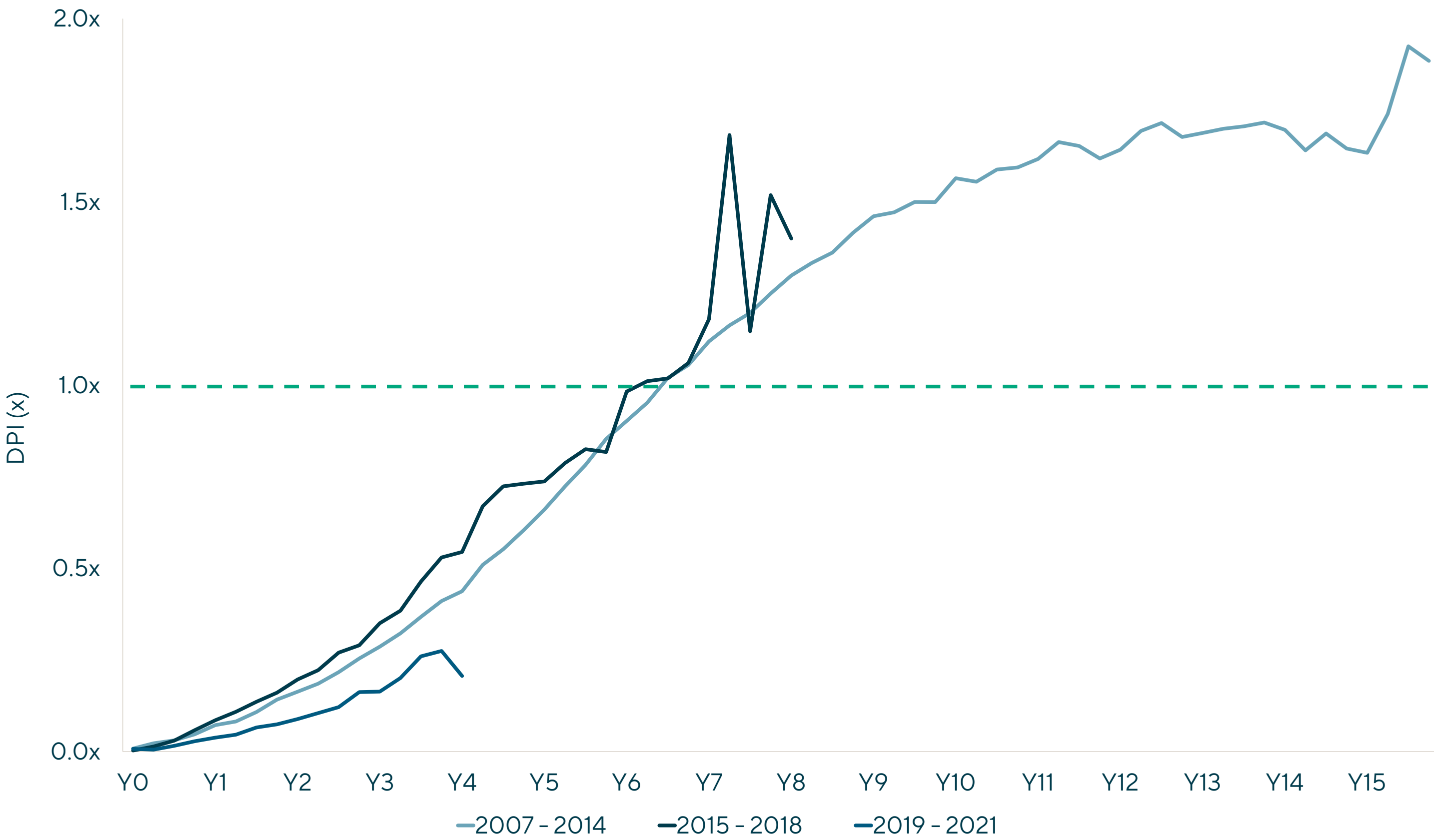
In addition to improved pricing, availability of capital in the private credit markets has increased competition among lenders and put downward pressure on spreads.

Unitranche Spreads by Size[4]



Pricing spreads have generally trended downward across all borrower sizes, as illustrated by Lincoln's reported unitranche loan pricing.

North American Private Equity DPI by Fund Vintage[5]



DPI for 2019 – 2021 vintage funds has lagged earlier vintages, which has increased demand for partial exits and alternative liquidity solutions.

Dividend Recaps Overview

Why should a sponsor or board consider a dividend recap?

- If current leverage level is below "market," including situations where a sponsor over-equitized the initial purchase due to lower leverage availability
- If a company is generating strong free cash flow and has the ability to service a higher level of debt while maintaining appropriate fixed-charge coverage

What borrower characteristics do lenders look for?

- Steady historical revenue and EBITDA with good visibility, ideally demonstrated by some combination of multi-year contracts, sole-source relationships, recurring "sticky" customers and / or high barriers to entry / competition
- Non-cyclical with favorable industry dynamics; underlying market growth

- As an avenue to provide liquidity to shareholders in an M&A environment where a full sale is not optimal
- For a simultaneous balance sheet recapitalization and continuation vehicle transaction
- To allow owners to take "chips off the table" and de-risk fund returns today while preserving upside returns through a future M&A exit
- As a potential alternative to a full sale or initial public offering (IPO) in the event the board / management believes appropriate value has not been achieved through the sale / IPO process
- Stability in cost structure and asset base; borrower not undergoing major operational changes or embarking on large capex projects
- Minimal adjustments to underwritten EBITDA
- Clear understanding of underlying business enterprise value and equity cushion
- Private equity-backed or other institutional ownership is preferred. Non-sponsored companies will likely have access to lower levels of leverage, all else being equal

Risks

In the event the borrower becomes distressed or insolvent in the future, creditors may allege the dividend was a fraudulent conveyance.

- Directors: Could face significant personal liability
- Shareholders: Could be forced to return dividend proceeds and / or incur costly litigation
- Secured Lenders: Secured claims may need to settle for significant discounts, despite previously negotiated collateral

Mitigating Risk in Recapitalization Transactions

- Investigate financial flexibility of borrower and its ability to achieve strategic goals with the increased leverage
- Understand the legal requirements to pay a dividend (e.g., surplus under DGCL 154)
- Obtain a solvency opinion from a qualified investment bank, such as Lincoln International
    - Directors can rely on the opinions of experts in discharging duty of care
    - Line of defense for shareholders and directors in a fraudulent conveyance claim
    - Reduces risk and potential liability in a bankruptcy

> Our clients obtain solvency opinions for many reasons, but the personal liability that members of the board of directors could face is often the leading one.

Chris Gregory
Managing Director in Lincoln's Valuations & Opinions Group who leads fairness and solvency opinions

The Lincoln Difference

Lincoln's dedicated Transaction Opinion & Board Advisory practice specializes in providing highly defensible fairness and solvency opinions and strategic financial advice to boards, special committees and other decision makers. Being housed in a global investment bank with highly active Mergers & Acquisitions and Capital Advisory Groups, we bring deep product and industry expertise and real-world experience to each of our transaction opinion engagements. Please let us know if we can help you navigate a dividend recapitalization transaction.

Sources:

1. PitchBook | LCD Comps based on reported Recap/Dividend transactions
2. PitchBook | LCD Comps, Lincoln International
    1. in chart: Reflects syndicated market pricing
    2. in chart: Illustrative example based on 50% LTV
3. PitchBook
4. Lincoln VOG Proprietary Private Market Database and Private Credit Snapshot; represents midpoint
5. Preqin as of 9/30/2025; Year 0 (Y0) represents the first non-zero DPI; changes in cumulative DPI also reflects differences in the availability of data across reporting periods

Ready to discuss the opportunities ahead for you?
Connect with a senior professional at connect@lincolninternational.com