Berenson Advisory

Berenson's **Restructuring & Recapitalization Practice** advises companies, sponsors and creditors in leveraged and financially distressed situations, with a focus on minimizing and managing financial crises, preserving stakeholder interests and reviving businesses; the practice provides high level, bespoke advice with the firm's senior partners leading the advisory teams.

COVID-19 UPDATE

Since our last letter, we have observed global markets reacting to the immediate and projected economic impacts of the COVID-19 health crisis. Current economic upheaval is expected to continue in the near-term, driven by substantial and continuing shocks to supply and demand dynamics and associated operational challenges across nearly all sectors.

COVID-19, unlike any prior crisis, has forced operators to take immediate proactive measures to offset the revenue impact that is being experienced by many businesses. Continued near- to intermediate-term revenue disruption will lead to a liquidity crisis for many businesses, irrespective of size, ownership or capital structure. In the face of these gale force economic headwinds, we continue to encourage our clients to: 1) marshal liquidity and manage operations to allow for a protracted period of moribund economic activity, 2) engage in active liability management and stakeholder dialogue, 3) take advantage of massive COVID-19 related government programs and bailouts and 4) (for our PE clients) never inject additional liquidity into portfolio companies outside of meaningful lender accommodations.

A COMMENT ON THE CREDIT MARKETS

The primary loan market remains closed for businesses as borrowers continue to hunker down and play defense against the unprecedented economic slowdown, including drawing remaining revolver capacity, amending existing credit agreements to stave off default and (in the case of PE sponsored businesses) injecting equity capital to bolster liquidity.

The secondary loan market has begun to show signs of life as it emerges from a historic collapse in March. With new deals on hold, focus has turned toward existing portfolios and secondary market opportunities. The percentage of loans trading under 80% of par has dropped to 22% as of April 8 from a high of 57% in late March as traders have begun to take advantage of arbitrage opportunities created by the collapse. We have also seen signs of original issuers (corporate and PE sponsors) of distressed loans buying back their debt.

Default rates continue to ramp up as 7 issuers defaulted in the first week of April. We expect the pace of rating agency downgrades and defaults to accelerate as the impact of the economic collapse wreaks havoc on balance sheets and triggers covenant/payment defaults in the coming weeks/months.

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THE GOVERNMENT STEPS IN

The CARES Act Paycheck Protection Program ("PPP") is a $349 billion new forgivable business loan program under the Small Business Administration's ("SBA") existing Section 7(a) loan framework. It is meant to provide liquidity support for franchises and small businesses, but private equity has joined the party subject to their portfolio companies meeting PPP requirements. The program is off to a rocky start and has been marred by confusion and overwhelmed lenders dealing with an avalanche of applications. Although the SBA issued guidance on April 3rd regarding PPP loan eligibility, processes and terms, this guidance was incomplete. Despite the issues (and assuming the program remains solvent in the intermediate- to long-term), the PPP could provide a lifeline to PE sponsored business that have seen precipitous drops in their top line as a result of COVID-19. PPP allows flexible use of the loan to sustain business payroll, utilities, mortgage, rent and other expenses, with most of the loan subject to forgiveness under certain parameters. We have encouraged our clients to determine if they are eligible for PPP or other government programs available to help offset the COVID-19 economic shock.

NAVIGATING THE COVID-19 MINEFIELD

While it is difficult to lay out specific prescriptive measures given the variability of the COVID-19 impact on specific businesses/sectors, it is useful to outline universal maxims that apply across the board:

- Model out various scenarios with stress testing that includes a prolonged economic shutdown morphing into a deep recessionary environment. While one should not manage to a doomsday scenario, it is useful to understand the resiliency or weaknesses in the business to reinforce holes in the city walls. Include specific detail around customer performance and potential payment delays, long-term impact of employee furloughs and creditor accommodations (stretching of vendors, deferral of debt service, etc.).

- Communicate with lenders and other stakeholders frequently. Although your lender knows your business, the transparency and frequency of discussions with them can have a meaningful impact on your liquidity in the months ahead.

- Cash is king and understanding the company's cash and working capital requirements is critical, especially as it pertains to understanding your borrowing base and any potential covenant breaches that could incur for debt and liabilities.

- Approach lenders and other creditors proactively to add stability around some of the more volatile and challenging aspects of your cost structure.

- Navigate covenants and work with lenders to secure amendments to existing credit agreements and opportunistically manage the securities in your current capital structure: repurchases, tenders, debt-for-debt exchanges, and/or debt-for-equity exchanges.

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