Roller Coaster Ride

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By **Wes Misson**
Partner | Fund Finance

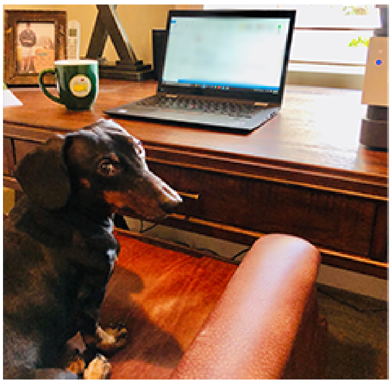
Another wild week: we saw massive swings on the stock market, political drama over aid packages, and many settling into a work-from-home routine that includes challenges such as home schooling and the need for at least one-third of the world's population to comply with government-mandated stay-at-home orders. All of this in the midst of the greatest public health crisis the world has seen since 1918. Just two weeks ago, many of us were going about our daily lives – traveling, going to shows and sporting events, eating and drinking at our favorite restaurants and bars, and routinely convening face-to-face with colleagues and clients. This seems like two decades ago. Now we can't even find eggs or milk in the grocery store. We have traded suits for sweatpants. Every day is Groundhog Day. My kids ask me each morning if they can go back to school. While I love the enthusiasm (and would certainly welcome the break!), it's difficult to tell them that they will not be seeing their friends or teachers for the foreseeable future (and, in some cases, maybe never again). My daughter's kindergarten teacher made the decision to retire this week. Today, we are doing a Zoom meeting so Parker can say goodbye.

As saddening as this is, our world is overflowing with hope. Kindness and generosity are once again at the forefront. We have banded together to beat our newest challenge as a society and to come out the other end stronger. The light at the end of the tunnel is growing brighter. There are now 2.2 trillion reasons for hope in the U.S. economy. And there is plenty of opportunity in fund finance.

What has this week's hiatus meant for fund finance? A few updates and my observations below:

- The Fund Finance Association has rescheduled the 6th Annual European Fund Finance Symposium from July 8, 2020 to October 22, 2020. For more details, see **here**.
- The Executive Order issued this week by New York Governor Andrew Cuomo does not apply the 90-day forbearance for "any person or business who has a financial hardship as a result of the COVID-19 pandemic" to subscription line borrowers. See our Clients & Friends memo authored by my partners Scott Cammarn and Mark Chorazak **here** that discusses the order and guidance from the New York State Department of Financial Services in greater detail.
- The Fed window is open but, given its short-term nature, is it a viable solution for subscription finance lenders? We think certain domestic subscription loans would qualify as eligible collateral to be pledged. See full criteria **here**.
- E-signatures are becoming the norm (at least for now). Parties are increasingly relying upon relevant state and national e-signature laws to accept non "wet-ink" signatures during this crisis as a necessity to move transactions forward. Language is also routinely being included in operative agreements regarding the acceptance and validity of such signatures for purposes of binding the parties to the agreement. Some lenders have a preference over certain e-signature formats or platforms. Others are requiring the ability to request verification either via a callback or email if elected. On the whole, however, the market has been extremely receptive and flexible in accommodating signatories during this time of need. My colleague Joe Zeidner touched on e-signature law last week and how this is being papered. You can read it **here**.
- Many state filing offices are closed for business. This has obviously raised a number of challenges in terms of how and when we can file things such as UCCs. In many cases, e-filing is an option but has required some nimble pivots by parties on the date of closing to adjust to the new system. For instance, many e-filing systems only permit one-page filings. As a result, collateral descriptions are being reduced (without losing substance) to fit within the tiny block on the cover sheet of a UCC filing. Fortunately, everyone has been accommodating, and this has led to no disruption in terms of closings and opinion coverage.
- Some funds are calling capital to have cash on hand and/or be prepared to move quickly on investments as valuations become more attractive, with the intent of redistributing to investors as recallable capital later when things settle. In a few cases, this is triggering potential borrowing base paydowns or significant reductions on borrowing availability in the interim. Other funds, instead of calling capital, are drawing down on their subscription lines for the same purpose or are requesting immediate temporary or long-term line increases in the line size. We are also seeing the exercise or request of a great number of early facility extensions.

- Parties are more focused on execution as market dislocation has led to pricing increases, LIBOR and prime rate floors well above zero and other terms that would have seemed unthinkable just a few weeks ago. Many borrowers have received the memo and are pushing deals forward at lightning speed. In the last two weeks alone, we have closed 9 deals. Nearly 4x that number of deals are extending or increasing during the same period.
- Many borrowers with uncommitted lines are seeking to convert to committed facilities to ensure that liquidity will be there when they need it. These amendments are becoming frequent.
- Many sponsors are adding Qualified Borrowers, with guarantees from the primary funds, to new or existing facilities as a way to provide additional liquidity to underlying portfolio companies. This is likely to be a continuing trend for the foreseeable future.
- Deposit account control agreements, already a rigid and often delay-filled process, are seeing enhanced execution delays, given WFH and related disruptions that are lengthening onboarding, account opening and agreement processing times. Many deals are pushing through and finding workarounds in the event that the account bank is unable to get there by closing.
- Much like the rush to get in-progress deals closed, fundraising is pushing forward with lightning speed to close in new capital for near-term opportunities during the crisis period and to provide additional collateral to support facility increases. It remains to be seen if new (not already in-progress funds) will see a dramatic drop-off in fundraising over the next quarter. New facility origination will likely start to slow some once the current pipeline of deals close, and that will especially be likely if fundraising slows in parallel. That said, we have opened 11 new matters in the last week and are still receiving a modestly healthy level of LPA reviews for new funds.
- There are potentially massive opportunities on the horizon for distressed and “vulture” funds. This may help offset some reduction in new origination.
- The volume of portfolio work is exponentially picking up – facility amendments, waiver, joinders and maintenance are peaking and may soon reach an all-time high for us in the coming weeks. This activity will help offset some lower origination numbers for many and will likely start new trends on deal terms as players adjust to new dynamics in the market.
- Please forgive my typos: now more than ever, I am seeing duplicate language or minor typos being inserted into drafts. I think that this is a side effect of so many of us working from home and editing/reviewing documents on-screen. The ability to print thousands of pages of documents are no longer a luxury for many. We should, of course, catch these, but be forgiving to our colleagues during this time. None are fatal.
- If there is a plus to WFH, it has definitely been getting to know my colleagues on a more personal level. We now see or hear each other’s kids playing in the background, dogs barking, and, oh, the outfits! Before last week, I had never done a Webex or Zoom meeting. My count is now approaching 30.
- We are all extremely fortunate to have the careers that we have, and current events should be a reminder of the role we need to play to helping out the less fortunate. Many are struggling to have even basic needs met. Please consider giving to a local charity that will help those most in need get through this time.
- This is now just an average Friday in the Misson household. I have a new-found appreciation for teachers. I have never been happier that I am marrying one later this year.



Stay blessed, healthy and safe, my friends.

'Fund Finance Friday: Industry Conversations' — Podcast with Jocelyn Hirsch of Kirkland & Ellis (15 minutes)

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Industry Conversations

Starting this week, *FFF* is going to include short podcasts with third-party industry leaders in an effort to get real-time information to our readership. The podcasts will be accessible from *FFF*, on fundfinancefriday.com and on Spotify. In our premiere "Fund Finance Friday: Industry Conversations" podcast, Cadwalader's Mike Mascia interviews Jocelyn Hirsch of Kirkland & Ellis on what she is seeing in the leveraged finance and fund finance markets along with what she is hearing from her fund sponsor clients.

FUND FINANCE FRIDAY | INDUSTRY CONVERSATIONS

Analyzing the Impact of COVID-19 with Jocelyn Hirsch

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Maples Group Shares Market Views

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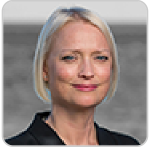

By **Tina Meigh**
Partner | Maples Group

Amid the global COVID-19 pandemic, opportunities continue to arise in the fund finance space for both banks and borrowers alike. The markets are showing some signs of calm this week, and all parties are looking for new opportunities to continue and grow business. Private equity firms, in particular, are looking more closely at distressed asset investments that are now available at discounted prices, and general partners are already identifying new business investments across the more suddenly successful technological, pharmaceutical and biotech markets. Many managers with dry powder are investing with a view to medium-term investments and a hopeful eye on a Q3 or Q4 return, while general partners are looking to defend the value of existing portfolios. Those general partners are looking to refinance and restructure certain holdings and create portfolio-level debt financing, with the aim of avoiding any breach or calls under existing financing structures.

The Maples Group is helping lenders and general partners to successfully structure this while protecting solvency by using Cayman Islands' bankruptcy remote structuring and ring-fenced investment vehicles. We are noticing that lenders are also being reactive and versatile, offering financing in true hybrid form and relying on typical subscription lines of credit collateral as well as downstream assets, co-mingling the subscription and NAV products. We are also seeing some managers swap debt for equity by using Cayman Islands preferred share structures, as well as an increase in hedge and derivatives products across the market. Some leveraged funds are dusting off their 2008 experience by investing in U.S. CLO AAA notes, as valuations dip below 2008 pricing, to target returns in the low teens from what are viewed as future par assets.

Conditions are changing daily, but as everyone is settling into new ways of working, the home office seems to be inspiring nimble action and encouraging the identification of new products and structures. We are certainly looking forward to what the next few weeks will bring to the table.

FFA European Symposium Rescheduled for October 2020 in London

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The Fund Finance Association is postponing its European Symposium in response to the coronavirus pandemic. Originally scheduled for July 8, 2020, the conference is now scheduled to take place on October 22, 2020 at The Landmark in London. According to the FFA, the planning of the conference was well underway, with more than 600 registered participants and 11 confirmed sessions scheduled to take place over the course of the day.

PE and Fund Finance Face Defining Moment — Investec

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The spread of COVID-19 and its impact on markets across the world present the largest test of private equity and fund finance in more than a decade, according to a **report** by *Investec*. According to the authors, the current difficulty in valuing assets may delay first quarter and December reports, but portfolio valuations are expected to decrease by 20-50%. *Investec* further outlines what they are seeing in the market. GPs have increased hedging transactions and are looking into NAV facilities as their focus shifts to defending assets and managing liquidity. Banks appear to have sufficient liquidity, but most are focusing on existing relationships and becoming more selective of new business.

Hamilton Lane Enters into Term Loan Agreement with First Republic Bank — Private Equity Wire

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According to *Private Equity Wire*, this week Hamilton Lane entered into a $75 million credit facility with First Republic Bank for working capital and general corporate purposes. Click **here** for the full article.

Maintaining Revolving Line Availability — Law360

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A *Law360* contributed article reports on some key considerations for maintaining availability of revolving credit facilities and the continued compliance by companies faced with the wide-ranging effects of COVID-19. Under certain circumstances, companies may consider preemptively seeking an amendment or waiver to avoid an anticipated default, or to create borrowing capacity, bearing in mind the ongoing obligations with respect to the representations and warranties under the credit agreement. Investment funds are similarly faced with reduced availability as a result of various exclusion events at the investor level, triggering a decrease in the borrowing base. Funds are encouraged to review their credit agreements to ensure ongoing access to their facilities. The article is available **here**.

LPs Assess Risk of Capital Call Credit Lines — Buyouts

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According to *Buyouts*, with the recent market downturn, funds are reportedly concerned about the risk that banks may suddenly call in the credit facilities, which would lead to massive amounts of capital being called by general partners and likely a tidal wave of limited partner defaults as limited partners struggle right now to pay normal capital calls. Nevertheless, at the moment, banks are still holding strong, and there is not a substantial threat of the banks suddenly calling in the credit facility lines. The article is available **here**.

Private Equity News Article Addresses Subscription Facilities

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In “Capital calls look set to increase as firms try to weather coronavirus crisis,” *Private Equity News* examines how private equity managers are moving towards calling capital earlier and more frequently to pay down debt. While the funds are paying down their subscription credit lines with a view towards using them at a future date, investors may prefer that the funds rely on the credit lines to extend the time before a capital call is made. Meanwhile, some analysts expect an increase in short-term financing as funds preemptively use their capital call facilities due to concerns that investors may not be able to pay when the funds issue their capital calls. The article is available **here**.

Public Market Declines Have LPs Preparing — Institutional Investor

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Institutional Investor reports that LPs are gearing up to sell some of their private equity assets in preparation for the continuation of the coronavirus-triggered market rout. The reasons for the potential liquidations vary from the need for cash to portfolio rebalancing. The **report** notes that LPs are not panicked, but they are concerned and want to be prepared.

Partner Michael Newell Joins Cadwalader in London

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Michael Newell, a leading fund formation partner, recently joined our firm in London. Mike's arrival strengthens our growing transatlantic funds group, which includes fund formation partners supported by and supporting our market-leading U.S. and UK fund finance, regulatory and tax teams.

Mike, who joined us with his team from Norton Rose Fulbright, where he was a partner, focuses primarily on the formation of real asset funds (including listed and mutual funds), credit funds and hedge funds and technology and emerging market-focused private equity funds. He has extensive experience advising the asset management industry on corporate, regulatory and investment fund-related matters and helps both household names and innovative start-ups set up new businesses and products in both the mainstream and alternative sectors. Mike is a member of INREV's Public Affairs Committee and was a member of the FSA's legal expert group and the technical committees of a number of industry bodies dealing with the implementation of the AIFM Directive.

Recommended Reading

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- Private funds are taking steps to manage available liquidity, in-process credit facilities continue to move forward, and a number of players are poised to take advantage of investment opportunities, according to the **latest update** from Fund Finance Partners.

- Scott Aleali of First Republic Bank published the second of a two-part series on LinkedIn titled "NAV Facilities: A Portfolio Management Solution for a PE Fund's Sunset Years." Our write-up and link to Part One can be found **here**. Part Two continues to use input from Dave Philipp and Amit Mahajan of Crestline Investors' Fund Liquidity Solution Group and focuses on how NAV lenders underwrite their facilities, considerations for funds when determining whether to draw on a NAV facility and some real-world examples where NAV facilities have been good solutions for funds. The article is available **here**.