

COVID-19 and the impact on financial covenants



INTRODUCTION

Since the escalation of the COVID 19 outbreak in the UK during March and April 2020, businesses across all sectors have been affected by issues flowing from customers and the workforce self-isolating and from staff having to work from home and adjust their usual working patterns. Many businesses have experienced severe interruptions in their supply chains and the financial sector has experienced market volatility not seen for over a decade. These

is still common to see club deals and bilateral facilities with at least one form of financial covenant. Even on larger deals, lower revenues resulting from COVID 19 could result in a breach of financial ratios which may impact on pricing or on a borrower's flexibility to undertake other activities (for example incurring new debt, paying dividends or making acquisitions).

IMPACT OF DRAWING DOWN EXISTING FACILITIES

Many borrowers have reacted to COVID 19 by drawing down liquidity facilities which, in times of normal trading, may have remained untouched. Some have elected to draw down their revolving credit facility (RCF) in full, despite the interest cost of doing so. This maximises liquidity and may be necessary to cover working capital

this ambiguity to increase its flexibility in interpreting EBITDA.

but explicitly non-exhaustive, list of items which are to be treated as "exceptional" and thus ignored when calculating EBITDA.

Financial covenant definitions may also include business disruption event provisions. Such clauses are triggered by exceptional events, such as an act of god, terrorism or (possibly) a pandemic, which negatively affect the performance of the business during the relevant covenant testing period. The impact on the covenant calculations will be that,

