



Annual Spring Conference  
May 16-17, 2024  
Madrid, Spain

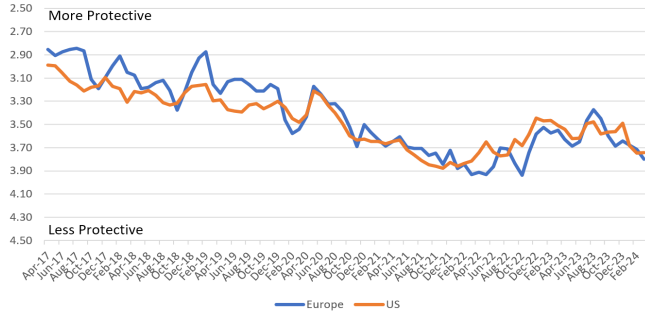
European Leveraged Loan Covenants – Trends

**Ricky Sharma**  
*Covenant Review*  
*Senior Director, Senior Covenant Analyst*

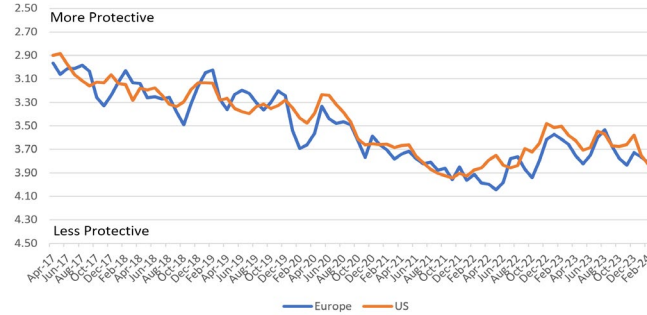
[www.iacpm.org](http://www.iacpm.org)

# Trends| Documentation Scores

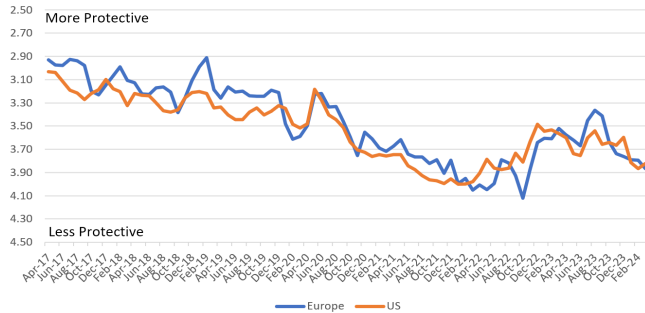
European vs US Loans: Composite Documentation Score  
Three-Month Rolling Average



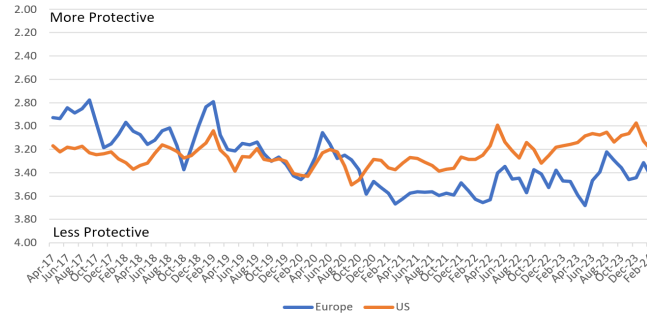
European vs US Loans: Collateral Protection Score  
Three-Month Rolling Average



European vs US Loans: Default Protection Score  
Three-Month Rolling Average



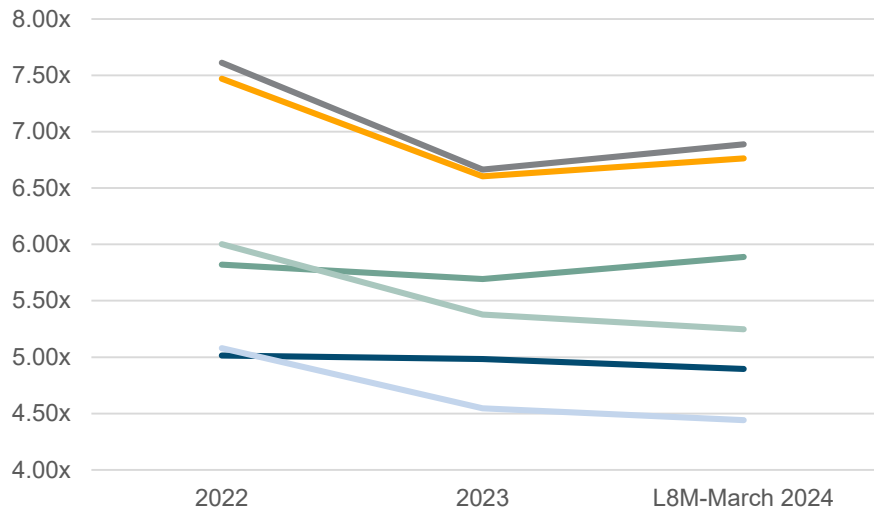
European vs US Loans: Lenders' Repricing Optionality Score  
Three-Month Rolling Average



Source: Covenant Review, a Fitch Solutions service

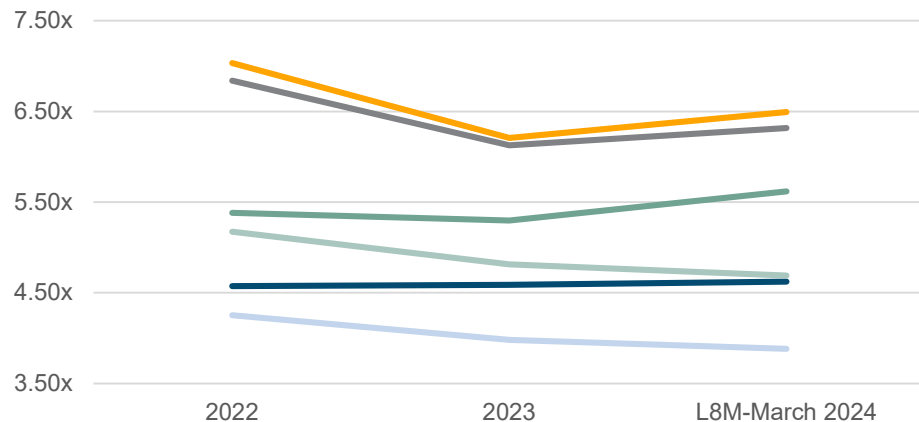
# Trends| Day-One Credit Stats at Opening

## Europe vs. US Total Leverage



- Europe Avg. Gross PF Adjusted Total Leverage
- US Avg. Gross PF Adjusted Total Leverage
- Europe Avg. Gross PF Adjusted Total Leverage incl. Free-and-Clear Tranche Only
- US Avg. Gross PF Adjusted Total Leverage incl. Free-and-Clear Tranche Only
- Europe Avg. Gross PF Adjusted Total Leverage incl. General Purpose Debt Capacity
- US Avg. Gross PF Adjusted Total Leverage incl. General Purpose Debt Capacity

## Europe vs. US First Lien Leverage



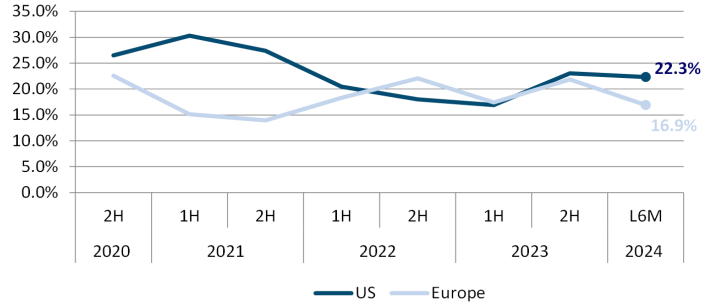
- Europe Avg. Gross PF Adjusted First Lien Leverage
- US Avg. Gross PF Adjusted First Lien Leverage
- Europe Avg. Gross PF Adjusted First Lien Leverage incl. Free-and-Clear Tranche Only
- US Avg. Gross PF Adjusted First Lien Leverage incl. Free-and-Clear Tranche Only
- Europe Avg. Gross PF Adjusted First Lien Leverage incl. General Purpose Debt Capacity
- US Avg. Gross PF Adjusted First Lien Leverage incl. General Purpose Debt Capacity

Source: Covenant Review, a Fitch Solutions service

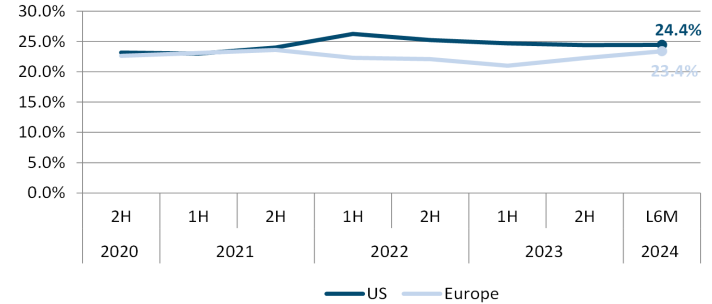


# Trends| EBITDA Adjustments Inflate Covenant Capacity

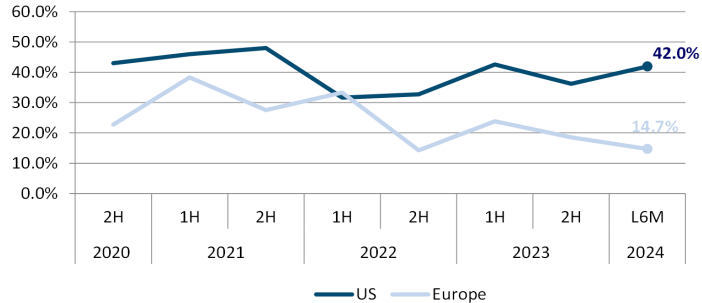
Total EBITDA Adjustments as % of PF Adjusted EBITDA



Synergies & Cost Savings Addbacks Provision Cap



Percentage of Loans with Uncapped Pro Forma Adjustment Provision



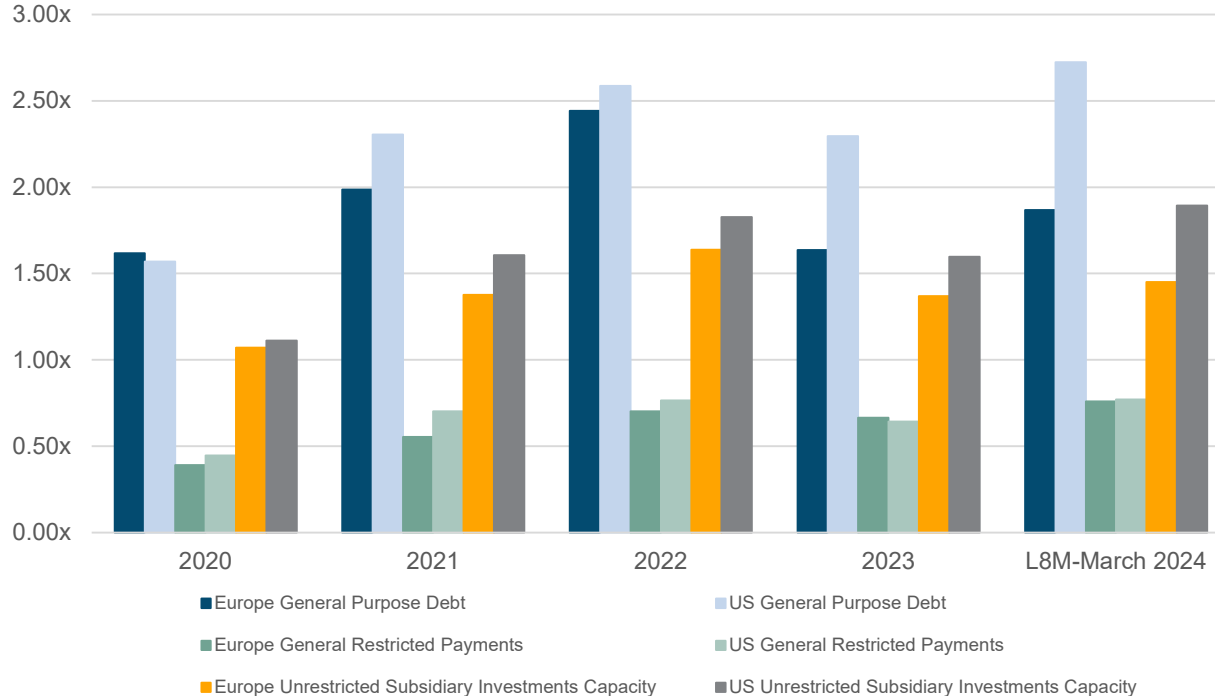
Source: Covenant Review, a Fitch Solutions service

# Trends and Traps| Calculation Flexibility

- **Misleading leverage ratios mask true position**
  - Overly narrow leverage ratios
    - Limited to certain debt yet takes full advantage of cash and EBITDA across the Group
  - Carveouts for debt incurred on the calculation date
    - Including for restricted payments
  - Exclusion of potentially material debt
    - All outstanding carveout debt all revolving debt / debt incurred (“for working capital purposes”)
  
- **Test date flexibility**
  - LTM based on last reported period, or any period where sufficient **internal** information available
  - Commitment date, notice date, definitive agreement date, “any other date relevant”
  
- **Other**
  - “Any other adjustments [...] pursuant to the terms of any financial definition or component thereof (including Consolidated EBITDA [...]) shall be available and be determined by the Board of Directors of the Company acting in good faith [...]
  - Automatic resets / “Highest Watermark” provisions – fixed baskets increase, but never reduce

# Trends and Traps| Day-One Fixed Basket Capacity

Europe vs. US Minimum Day-One Capped Basket Capacity



- Uncapped “consistent with past practice” / “ordinary course of business” baskets
- Additional facility capacity – “freebie baskets” replaced by “capacity under the Debt covenant”. Specific purpose debt capacity becomes additional general purpose debt capacity
- “Available RP Capacity” flexibility
  - Conversion of Restricted Payments capacity into unsecured or secured debt capacity
- 200% equity credit debt baskets
- Asset Sale leveraged based step-downs facilitate dividend capacity
  - Lack of “pro forma” calculation mechanics may skew prepayments leverage threshold
- General purpose Restricted Payments baskets often lack *any* conditionality

Source: Covenant Review, a Fitch Solutions service

# Trends and Traps| Transfers

- Transfer restrictions extending to voting and non-voting sub-participations
- Widening restrictions via extended definition of “Loan to Own” definition
  - Carveouts for bona fide debt funds
- Loan to own restrictions extending to affiliates
- Cap (10% / 20%) on holding amount
- No deemed consent provision
  - 2022 and 2023, 37.5% and 31.91% of deals, respectively, had no deemed consent mechanism
- By way of comparison, the equivalent figure for 2021 as a whole was 22.1%
- Deletion of the requirement for the borrower not to unreasonably withhold consent
- Cumbersome requirement for lenders to give pre-notification on transfers
- Consequences of non-conformity – transfers made void / disenfranchisement

# Trends and Traps| Liability Management Transactions

## Liability Management spectrum

- Asset Sales
- Dropdown transactions
- Uptiering transactions
- Double-Dip transactions
- Envision/Amsurg-type (KKR)
- Distressed exchanges / exit consents

## Enabled by weakening documentation

- Excessive capacity for non-guarantor and effectively senior debt
- Excessive investments capacity
- Missing/ineffective J.Crew Blocker
- Missing anti-subordination protection
- Weak sacred rights provisions
- Missing payments for consent covenant
- Weak Unrestricted Subsidiary conditions

## Out of court LMTs relatively uncommon in Europe

- Directors' duties (personal liability)
- Availability of English Scheme of Arrangement / Restructuring Plan
- English case law (Assenagon) reduces viability of coercive exit consent
- Relatively tightly knit investor community

## Market factors may see increase in European LMTs

- Higher for longer interest rates
- Approaching 2025 and 2026 maturities
- Accommodating European documentation backdrop
- U.S. market precedent



# Loans | Common Market Flex

- **Margin**
  - Fewer step-downs on Facility B
  - Deleveraging increments between steps increased
  - Improved initial guaranteed fee period
- **EBITDA adjustments**
  - Caps added
  - Revenue synergies removed
- **Transfers**
  - Deemed consent added
  - Restrictions on holding amounts removed
- **Incremental debt**
  - Freebie basket reduced
  - Inside maturity basket removed
- **Debt**
  - “Available RP Capacity” flexibility removed
  - 200% equity credit removed
  - “No worse” leverage for any transaction removed
- **Restricted Payments**
  - CNI starter amount removed / reduced
  - Restricted payments ratio carveout tightened
  - General restricted payment basket reduced
- **Change of Control**
  - Portability removed
- **Asset Sales**
  - Leverage step-down removed / tightened
- **Information Undertakings**
  - Obligation for annual lender presentation
  - Quarterly lender updates added
  - Improved timing for delivery of financial statements
- **Enhanced investor protection**
  - “J. Crew” / “Chewy” / “Serta” blockers added

# Contacts |

For general information and queries, email [research@covenantreview.com](mailto:research@covenantreview.com)

## European Research Contacts

### Jane Gray

Head of Covenant Review Europe  
[jgray@covenantreview.com](mailto:jgray@covenantreview.com)

### Ricky Sharma

Senior Director, Senior Covenant Analyst  
[rsharma@covenantreview.com](mailto:rsharma@covenantreview.com)

### Shane Burke

Director, Senior Covenant Analyst  
[sburke@covenantreview.com](mailto:sburke@covenantreview.com)

### Shoshanna Harrow

Senior Director, Senior Covenant Analyst  
[sharrow@covenantreview.com](mailto:sharrow@covenantreview.com)

### Alastair Gillespie

Senior Director, Senior Covenant Analyst  
[agillespie@covenantreview.com](mailto:agillespie@covenantreview.com)

### Kirsten Heenan

Senior Director, Covenant Analyst  
[kheenan@covenantreview.com](mailto:kheenan@covenantreview.com)

Covenant Review is a Fitch Solutions company.  
See [www.fitchsolutions.com](http://www.fitchsolutions.com) for more corporate information.

London

T +44 (0)20 3530 2400

[emeaclientservices@fitchsolutions.com](mailto:emeaclientservices@fitchsolutions.com)

New York

T +1 212 908 0800

[usaclientservices@fitchsolutions.com](mailto:usaclientservices@fitchsolutions.com)

Tokyo

T +81 3 3288 2715

[asiaclient.services@fitchsolutions.com](mailto:asiaclient.services@fitchsolutions.com)

Hong Kong

T +852 2263 9999

[asiaclient.services@fitchsolutions.com](mailto:asiaclient.services@fitchsolutions.com)

Singapore

T +65 6796 7231

[asiaclient.services@fitchsolutions.com](mailto:asiaclient.services@fitchsolutions.com)

