

## STRATEGIC CONSIDERATIONS FOR BRAZILIAN COMPANIES DURING CHALLENGING MARKET CONDITIONS

The economic challenges and market volatility resulting from the Coronavirus outbreak has led to heightened risk for companies across a broad range of sectors. In this bulletin, we set out some practical considerations that Brazilian companies may wish to consider at this time, particularly if a potential restructuring is under consideration.

### **Analysis of Key Contracts Including Financing Agreements and Derivatives**

Companies should conduct an analysis of financial covenants in their financing agreements, prepare in advance for upcoming covenant compliance measurement dates and update cashflow projections based on alternative models for revenue and expenses. Advance preparation will be key in identifying issues and displaying a proactive approach to lenders and/or bondholders.

We also recommend that counterparty risk be assessed across all applicable contracts (including supply agreements, purchase agreements and derivatives). The material depreciation of the Brazilian *real* in relation to the U.S. dollar presents significant challenges to companies with revenues predominantly in *reals* with outstanding U.S. dollar-denominated debt obligations. Analysis of counterparty risk should include review of any credit events specified in ISDA agreements.

#### *Analysis of Borrower Covenants*

We understand that certain lenders, notably BNDES, may be pausing interest payment requirements during this period. We recommend that any borrower considering taking advantage of such developments first undertake an analysis of its covenants in other agreements in order to ensure that any non-payment of interest does not inadvertently trigger breaches or defaults.

### **Devise Strategy for Messaging to Lenders and/or Bondholders**

Lenders (both in Brazil and internationally) and potentially bondholders may contact companies to discuss concerns around repayments. It is critical to be prepared for requests that may include updated projections (including the value of collateral, if applicable), information on strategic decisions around cost reductions and, if default is a possibility, demands for default interest. The decision making process of certain lenders may be more bureaucratic, complex and/or time consuming than others and

the dialogue dynamic with each lender must be considered in order to establish a realistic timetable for negotiations. All such communications should be vetted by counsel. Early and proactive engagement with lenders and bondholders typically yields the most favorable outcomes.

## **Preservation of Cash and Exploration of Potential Sources of Liquidity**

In addition to broad internal reviews of costs to analyze which items may be suspended, deferred or eliminated in full, we recommend that companies confer with external counsel to review agreements to examine *force majeure* or other provisions that may excuse payment obligations, as well as recent legislation and court decisions including granting a moratorium of payments, if applicable.

Consideration of all potential sources of liquidity is key during times of market turbulence. Available options may include working capital facilities, funding from existing shareholders and asset sales (including non-ordinary course dispositions, factoring transactions, and sale-leasebacks). However, it is important to be aware that New York law financing agreements often impose restrictive conditions on these types of transactions that may frustrate their usefulness in this environment, including the absence of defaults, solvency representations, the receipt of a certain amount of cash consideration, fair market value determinations, and the requirement that the proceeds be swept to repay the existing loan – therefore, companies should discuss with counsel prior to structuring any transaction. Finally, companies should review their existing insurance agreements in order to analyze business interruption coverage, which may provide valuable liquidity during this period.

## **Preparation for Potential Restructuring**

As previously discussed, dialogue with lenders (and bondholders, if applicable) is critical. If restructuring is the only option, a fundamental issue will be convincing lenders that the restructuring will lead to a more favorable outcome than if no restructuring takes place. It is important to understand the motivation of each lender in order to determine an effective negotiation strategy. Among the items that may be attractive to lenders and warrant consideration in advance are: collateral enhancement; more frequent and/or detailed reporting; and strengthening certain covenants in return for waivers or weakening of others. With respect to syndicated loans and capital markets transactions, companies should determine whether there is a minimum quorum of lenders required in order to approve waivers or changes to the payment schedule.

The interplay between local Brazilian *real* debt and U.S. dollar debt is critical in connection with any potential restructuring. Thresholds for waiving defaults and/or the presence of collective action provisions may differ between local law and foreign law agreements. An attractive solution for Brazilian companies with U.S. assets and/or debtholders may be Chapter 15, an ancillary bankruptcy proceeding with the main proceeding taking place in the home country of the relevant company. It allows a debtor outside the U.S. to file an ancillary case in the U.S. to obtain recognition of the main bankruptcy proceeding in its home country and protection from creditor action in the U.S. against the debtor or its assets. The interplay between local Brazilian real debt and U.S. dollar debt is critical in

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Together with Brazilian counsel, companies should evaluate their corporate governance structure for issues relating to a potential distressed situation, including conducting an intercompany analysis and reviewing whether subsidiaries and affiliates share common governing bodies that may give rise to conflicts of interest in a reorganization transaction.

### **Contact Brazilian Law Counsel to Discuss Potential Relief Measures Available in Brazil**

We suggest that all companies actively discuss potential relief measures available in Brazil with their Brazilian law counsel. Such measures may include a 60-day moratorium on payment of debt during which companies, without the threat of remedies being undertaken, and their creditors could negotiate adjusted contractual terms, among others.

For further insights, our briefing on Coronavirus considerations in Brazil can be found [here](#) and other Coronavirus materials can be found [here](#).

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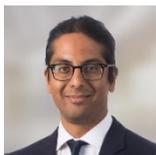
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