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FUND FINANCE FRIDAY

What About Me? Private Funds See Mostly Tangential Benefits from the Recent Round of Stimulus

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By Chris van Heerden
Associate | Fund Finance

The Federal Reserve has moved quickly since mid-March to expand the use of conventional monetary policy along with adding a slate of temporary programs to support specific capital markets and intermediaries. For once, fiscal policy has moved in step, with the $2.2 trillion Coronavirus Aid, Relief, and Economic Security (CARES) Act making a relatively expedited trip through the legislative process.

How have private funds fared so far? Here are the key takeaways:

- The CARES Act allocates $349 billion in cash-flow assistance through federally guaranteed loans to employers to pay their employees during the emergency through the Small Business Administration (SBA).
- Existing affiliation rules can lead to portfolio companies exceeding the size standards for qualifying for an SBA loan by aggregating a portfolio with all other controlled portfolio companies of the same sponsor for the purpose of determining its size. There are a few limited exceptions.
- These loans will be made available to businesses with 500 or fewer employees, and loan size is capped at the lesser of 2.5x monthly payroll or $10 million. In other words, the loans will primarily benefit businesses sized below the institutional private market strike zone.
- The Fed has launched a number of loan facilities that backstop the primary corporate credit market, the secondary corporate credit market, ABS, commercial paper, money markets and primary dealers.
- These facilities have helped to restore liquidity in targeted markets, but they're not an antidote to the uncertainty around fundamentals.
- The Fed programs primarily support highly rated securities, limiting their direct relevance to private market sponsors. Funds that rely, for example, on ABS, agency CMBS, or corporate market debt financing will be more directly affected than the industry as a whole.

- Tax changes in the CARES Act have the potential to be meaningful in specific cases. These include changes to net operating loss rules, limitations on business interest deductions, depreciation of qualified improvement property, corporate alternative minimum tax credit refunds, excess business loss deductions for individuals and new payroll tax credits.
- Future initiatives may be more directly relevant to the private market on a large scale. The CARES Act includes a $454 billion appropriation for “loans, loan guarantees, and investments in support of the Federal Reserve’s lending facilities to eligible businesses, states, and municipalities.” This appropriation may support future lending programs from the Fed and may be used on a leveraged basis to increase the impact. Future programs could address additional markets and may potentially reach further down the ratings spectrum.
- The Main Street Business Lending Program may be one such program. The program has been referenced as an anticipated future initiative from the Fed. While details have yet to be unveiled, the program may expand the Fed’s support to include medium-sized businesses.
- Finally, discussions of a Phase 4 legislative package has been percolating over the past two weeks and could include spending initiatives that may be directly relevant to the private market.