# Jefferies Insights
APRIL 2020

## Even With Heartbreaking Loss, Springtime Can Bring Green Shoots of Optimism

## Dear Jefferies Clients and Friends,

We hope you, your family and your colleagues are healthy and managing through this crisis as safely and effectively as possible. As you know, this week the coronavirus caused us to lose our friend and partner, Peg Broadbent, who served as CFO of Jefferies Group since 2007. We mourn his passing and will carry his memory forever into the future. We owe it to Peg's legacy and to each other to stay strong and to persevere through this difficult time.

Peg loved Jefferies and was incredibly proud of how our firm always rallied together in times of adversity to fight for the collective benefit of our clients and each other. With Peg in mind, we wrote the note below to our almost 4,000 Jefferies employee-partners to allow all of us to begin to find the positives that can come from this awful tragedy. We are a long way from healing and there are many challenges ahead for all of us, but hopefully these thoughts will help your team and ours put perspective to our challenges and provide some further motivation for us all to get to the other side together.

Please stay healthy and safe,

Rich and Brian

### IN THIS ISSUE

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## Dear Jefferies Partners,

The tragedy of what happened to our friend, Peg Broadbent, puts in perspective the daily upheaval and personal challenges that each of us now face. Peg will be sorely missed and we will celebrate his life as soon as the world steadies and we can all be together again. For the sake of his memory and the passion he had for Jefferies and all of us, together we will push forward to serve our clients and continue to build our firm.

For each of us, the days are turning into weeks which will eventually turn into months and hopefully no more than a quarter or perhaps two. Today is April 1st and we are in the early days of one of our nicest seasons, spring. With the blessing of Peg's memory and a will for all of us to find the path forward, we would like to share with you a few positive observations of what will hopefully emerge from the pain and misfortune we and the world are experiencing. It is most important in times of great distress to appreciate what we all have and realize that the seasons will keep turning and together we will continue to grow and evolve. Here is the beginning of a list of positive thoughts stemming from this virus that hopefully we can all build upon:

1. **Priorities**: How many times have people paid lip service to the trite phrase, "if you have your health, you have everything?" Well, because of the scope, severity, contagiousness and swiftness of this illness, we now know the true meaning of these words. The Coronavirus is reshaping the way we think about our health, the health of our families, including our extended Jefferies family, and the health of the communities in which we live and work. The Coronavirus disaster is not fully reflected in stock indices. It is reflected in the ever-growing list of souls who are contracting the virus and the effect it has on their loved ones. Material wealth is meaningless without sound physical health. The coronavirus is sweeping throughout the world and reminding us that if you or your loved ones are not healthy, there is no happiness.

2. **Clarity**: Relationships are only proven and truly appreciated in bad times. Success, fame and wealth attract a bevy of admirers eager to squeeze into the bright spotlight so they can share the good times. Uncertainty, hardship and duress attract a different type of person who helps ease the pain, not because they have to, but because they want to. True friends show their heart at these difficult times and are there to provide direct assistance, empathy, moral support or whatever is needed. It's amazing how many enjoy the happy-time spotlight, and how few will be with you to help you through the lonely darkness. Today is a perfect day to begin prioritizing the people most important to you and those to whom you truly matter. It's also no coincidence that the people who are always there for many in tough times are the ones blessed with an army of their own true supporters when the chips are down. We count all of you as important to us and as the folks who have been there for us and each other from well before the beginning of this pandemic. That is why it is so easy and important for us to be there for each of you now.

3. **Fragility**: In the course of mere weeks, healthy people have become seriously ill, fearless people have become incredibly frightened, wealthy people have become less wealthy, strong businesses have been brought to their knees and invincible societies have become hugely vulnerable. Facing fragility and mortality causes us to value, respect and enjoy everything we have ever had and the preciousness of life. Envy, greed and other similar byproducts of a long bull market can now be replaced with a great appreciation of how fortunate so many of us are already with all that we currently possess.

4. **Hygiene**: We have truly taken this one for granted in the developed world and this experience had better serve as a reminder that we need to improve conditions globally, if not because it is the right thing to do for all people, which we believe firmly, but also because health-wise we now know we are truly one. There is no doubt that people will remember this experience for a very long time, and the phrase "cleanliness is next to godliness" will never again have to be explained.

5. **Oneness**: This is the most difficult one and our perspective may raise some controversy. Coronavirus brings to the fore the question of whether the world is going to work together or continue to retreat from connection. In the age of pandemic, global coordination, communication and trust are the best path to assuring our world survives. Each country and continent is currently fighting their own fights independently, as people tend to do in the heat of the moment and when life or death decisions are happening in real time. However, to avoid or minimize the risks in the future, global policies and means of coordination must be implemented for the benefit of the collective world. Accurate Information must be transparently shared on a real-time basis. Therapy and vaccine development will require the collective brainpower and large data capabilities of the world. Positive breakthroughs must be quickly shared globally, as we know that if one region is sick and the rest of the world is healthy, it will not remain that way for long. Countries will need to be able to act to protect their own people, but if the world doesn't come together as well, nobody will be truly safe. Sometimes it takes a pandemic to realize that the world united will stand and a world divided could fall.

We have suffered a tremendous loss and nothing will make this better. It is highly possible that there will be even more pain to be felt by the Jefferies family, as we are large, global and heavily engaged with society. Our grieving period has just started and it is complicated by the fact that we are all working continuously in a manner different than ever before. None of this seems to make sense. All we are asking is that while we grieve, let's allow ourselves the opportunity to embrace Spring and enjoy a small taste of the renewed freshness and optimism it always brings. We can do this while we prioritize our families, friends, clients and each other at Jefferies. Also, let's make sure we go the extra mile for all of those who have been the most harmed by this disease, as well as the amazing people in the medical and related professions who are truly risking it all on our behalf every single day.

With sadness today and optimism for the future,

Rich and Brian

# Economics and Strategy

**Global Pandemic Fears Have Dampened Risk Assets, But Coordinated Policy Action Should Save the Day**

Jefferies' U.S. and European economists recently cut forecasts, highlighting that the economic impact of a pandemic is very different from anything else they have ever seen. Typically in a downturn, an economy loses momentum and a recession builds, instead of being actively slowed while the damage reverberates. We do not appear to be heading for a normal recession, and the U.S. Economics team does not currently forecast a recession this year. While the total effects of COVID-19 are not yet fully realized and may very well have much bigger implications for the rest of the year, Jefferies' economists also believe that the economy will remain intact and functioning. They also are in broad agreement that what is important now is for both fiscal and monetary policy responses to be measured and prompt. David Owen, Chief European Economist, points out that while we have already seen this in the UK, the ECB needs to demonstrate its complete commitment and unlimited firepower to support the European markets through its new Pandemic Emergency Purchase Programme, as it does not have the luxury of sitting back and letting the politicians deal with this emergency. The policy response in the euro area has so far been lacking.

Christopher Wood, Head of Global Equity Strategy, suggests that the most practical thing governments can do is provide support to small businesses hit by a sudden loss of cash flow. In addition, aside from renewed QE, he believes the Fed's recent crossing of the Rubicon in terms of explicitly entering the fiscal area will be significant, as it enables the purchase of corporate bonds and loans to businesses. Chris also believes the Federal Reserve does not want to venture into negative rates. However, this calls into question how it is possible to stop bond yields from being driven into negative territory by investors, as has happened in Europe and Japan. To him, the most obvious way to counter this is by a more elaborate version of the Bank of Japan's yield curve control, where the central bank targets yields at longer-term maturities. He points out that this also means the long-term risk-reward ratio of owning Treasury bonds IS in no longer interesting, hampering the risk-parity trade.

David Zervos, Chief Market Strategist, believes that the Fed's monetary policy moves have been extremely helpful in provoking aggregate demand and easing short-term funding stress. Recently announced policy sends the Fed firmly into the fiscal arena with the Treasury's backing. Looking ahead, however, David highlights that the only real policy that can save the day against the virus is something that makes it safe for people to return to work. He points out that one driving force of the unprecedented price action has been risk parity unwinds. The key trigger here was when the 10-year and 30-year gapped to their respective low yields. He believes the combination of QE and risk parity unwinds has been, and will likely continue to be, quite lethal for the long end of the yield curve. As a result, he moved to the sidelines with his preferred risk parity trade structure. Global Equity Strategist Sean Darby points out while fears over the global economy keep credit spreads wide, the dollar has come back in line. He highlights that following the shock and awe of the Fed policy toolkit deployment and the U.S. government's fiscal stimulus package, his indicators are moving away from deep risk aversion. He recently upgraded the S&P 500 to Bullish within his asset allocation framework.

# Actionable Ideas for Companies and Sponsors

## MERGERS AND ACQUISITIONS

### M&A Approaches In A Volatile Deal Making Environment

As a result of the financial impact of COVID-19, regular-way M&A activity will experience historically low volumes until the economic environment normalizes. During this period, we expect M&A activity will rapidly evolve to a range of transactions that will include the following broad themes:

- Stock for stock mergers within industry verticals where relative ownership is the main driver, not absolute valuation of the acquiror or target. These transactions will be driven by the even greater need for scale in this new economic environment.
- Equity investments by companies and private equity firms to establish toe-hold positions in quality companies that need bridge equity capital but are not willing to sell at depressed values, and potentially providing a natural path to acquisition when valuations recover.
- Sponsor-led acquisitions that are funded entirely with cash equity to eliminate the need for external financing and to capitalize companies with less leverage. Acquirors pursuing cash acquisitions may also need to employ structuring tools to bridge valuation gaps, including earn-out structures in private transactions and contingent value rights in public deals.

### While Activism Will Decline In The Near-Term, Companies Should Prepare For The Next Wave

We expect the number of activism campaigns to decline in the near term, given record level market volatility historically has served as a deterrent to new activist campaigns. However, given the large amount of capital allocated to activist funds, we believe that once market volatility levels decline, we will see a robust return to historical activity levels and to a large universe of activist targets, given some companies will rebound slower than others.

While the critical near-term priority for all companies is to get their businesses returning to normal operating levels, advanced preparation for activism should also be a priority in order to mitigate the tactical advantages activists possess in this market environment. While there are many components to defense preparedness, some near-term key action steps should include (i) achieving alignment among Board members regarding a collective view on the company's intrinsic value, and (ii) the adoption of an ISS-friendly short duration poison pill, or putting such a pill "on the shelf" for rapid adoption if a threat is perceived. Several companies have adopted such pills over the past several weeks in response to their share price declines.

## DEBT CAPITAL MARKETS

### Tapping Incremental Debt Facilities To Increase Liquidity

Issuers adversely impacted by the effects of COVID-19 can shore up balance sheets and increase liquidity by utilizing the incremental debt capacity available through various baskets and carve outs in their loan agreements to issue additional debt. For some issuers, this can often be done without triggering MFN provisions by utilizing carveouts such as issuing secured bonds or varying maturity profiles.

We are currently working with several companies to enhance their liquidity through senior secured notes transactions. These companies have incremental debt baskets that permit them to raise pari passu secured notes without triggering the MFN yield provisions in their existing credit agreement. This solution provides these companies with an immediate liquidity boost while preserving the low interest rate pricing under their existing debt facilities.

**Transferring Assets to Raise Debt Capital Outside Existing Credit Agreement**

Companies seeking near-term liquidity can explore using restricted payment and investment baskets in existing loan agreements to transfer assets into unrestricted subsidiaries to raise capital. The unrestricted subsidiary will have exclusive or priority liens on the transferred assets and the transferred assets should be assets that can be valued by the market, and can include intellectual property or unique business units. The money raised at the unrestricted subsidiary is then reinvested in the parent company via an inter-company loan.

This structure allows the new debt investor to benefit from liens on the existing asset base in addition to the specific collateral transferred into the unrestricted subsidiary. In addition to providing much needed liquidity to the existing company, this structure also avoids MFN provisions, enabling companies to preserve borrowing rates on their existing credit facility. Jefferies is currently discussing this structure with several companies across a wide range of industries and notably, we used this structure on the firm's recent $850 million committed financing for Revlon.

## EQUITY CAPITAL MARKETS

**Using ATMs To Provide Immediate Access To Equity Capital**

In the volatile markets we are currently experiencing, the ATM (At-The-Market) equity product provides immediate access to equity capital to strengthen balance sheets and improve liquidity when traditional equity capital raising alternatives may not be available. An ATM allows a company to discretely sell primary stock into the market with complete control over timing, price and volume of shares sold. The only upfront disclosure for an ATM is the filing of a sales agency agreement that includes the maximum dollar amount to be sold under the program. Public disclosure of the primary stock sales occurs in the company's subsequent quarterly filings.

Since volatility started to move higher around February 20th, 55 ATMs have been filed with the potential to raise over $10 billion in primary equity proceeds. These ATM filings have occurred across most sectors including, real estate, healthcare, technology, energy, utilities, industrials, and financial services. Jefferies has filed 33% of these ATM programs and remains the industry leader in the ATM product.

**SPAC IPOs Can Get Done In Volatile Markets**

In the current equity environment, the window for most traditional IPOs is largely closed. However, as noted below, investor receptivity to SPAC IPOs has proven to be far greater in higher volatility equity markets. In addition, for the SPAC IPO sponsor, raising a SPAC IPO over the next few quarters should be very timely, as there should be numerous attractive acquisition opportunities that emerge from this economic environment.

Three of the five U.S. IPOs priced in March 2020 have been SPACs and 8 of the 13 IPOs publicly filed in March have also been SPACs. Because SPAC share prices are supported by their cash-in-trust value, the existing SPAC IPOs have seen limited downside in the aftermarket despite the sell-off in the equity markets. Since the market hit an all-time high on February 19th, the S&P is down over 30% while SPACs are down 5% on average. Another example of SPAC IPO activity in challenging equity markets was Q1 2019 (after the market sell off in December 2018) when 15 SPAC IPOs were completed for $3.3 billion in proceeds, and SPAC IPOs represented 50% of the U.S. IPO market in that quarter.

## DEBT ADVISORY & RESTRUCTURING

**Using Up-Tier Exchanges To Address Near Term Maturities**

An up-tier exchange can provide several potential benefits to the issuer, including addressing near term maturities, improving leverage, reducing cash interest expense, and relaxing covenants. It can also provide more runway and potentially enhance liquidity by requiring exchange participants to also provide new money. The most common type of up-tier exchange is when a company offers to exchange unsecured bonds for a lower principal amount of secured bonds that are either pari-passu with, or subordinated to, the company's existing secured debt. Therefore companies should examine if they can take advantage of flexibility in their credit agreements and indentures to structure up-tier exchanges accompanied with a new money investment. The up-tier exchange can be executed on an expedited basis and can be exempt from registration requirements.

# Best Research Ideas

**U.S. Insights – Practically Stealing: 47 Stocks with Strong Fundamentals and Attractive Valuations**

Jefferies recently identified the stocks the firm's Equity Research Department found the most compelling given the current market turbulence. Jefferies' analysts selected high-quality names investors would want to own across a cycle – great companies that have strong business models, healthy cash-flow and very robust balance sheets. Many of those selected held up well in the last downturn and include businesses that are well differentiated vs. peers and stocks that have both yield and the cash-flow to support dividends. The 47 selected stocks span all sectors under coverage by Jefferies.

— *Jefferies U.S. Equity Research*

**Global – Covid's Impact: How Will We Live, Work and Play?**

In a very atypical research report, Jefferies explored the impact of COVID-19 on the global population. The firm presented 20 thought experiments regarding potential changes to life in the weeks, months and years ahead. For each, Jefferies worked with 120+ analyst teams around the world to identify sectors and stocks that may benefit, as well as some that may lose out. Jefferies does not think securities prices today reflect these potential outcomes – and the firm remains bullish for humanity and its prospects.

— *Jefferies Global Equity Research*

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NOTABLE RECENT TRANSACTIONS

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|---|---|---|---|
| Healthcare February 2020<br>PPD<br>**$1,863,000,000**<br>Initial Public Offering<br>Joint Bookrunner | Automotive Aftermarket March 2020<br>IXS Mark of Innovation<br>**$695,000,000**<br>Credit Facility to Finance Acquisition by<br>**Clearlake Capital Partners**<br>Joint Lead Arranger | Technology January 2020<br>Decawave<br>**$400,000,000**<br>Sale to<br>**Qorvo, Inc.**<br>Sole Financial Advisor | Energy January 2020<br>CVR Energy<br>**$1,000,000,000**<br>Senior Unsecured Notes Offering<br>Sole Bookrunner |
| Telecom January 2020<br>Gilat<br>**$533,000,000**<br>Sale to<br>**Comtech Telecommunications Corp.**<br>Joint Financial Advisor | Healthcare January 2020<br>Black Diamond Therapeutics<br>**$231,000,000**<br>Initial Public Offering<br>Joint Bookrunner | Finance March 2020<br>AmeriLife<br>**$540,000,000**<br>Credit Facility to Finance Acquisition by<br>**Thomas H. Lee Partners**<br>Joint Lead Arranger | Technology February 2020<br>Clover Technologies Group<br>**$644,000,000**<br>Restructuring<br>Financial Advisor to the Company |
| Healthcare February 2020<br>Alvogen<br>**$800,000,000**<br>Term Loan Amendment and Extension<br>Financial Advisor & Sole Lead Arranger | Finance February 2020 Pending<br>INTL FCStone<br>**$328,000,000**<br>Acquisition of<br>**GAIN Capital Holdings, Inc.**<br>Sole Financial Advisor | Healthcare February 2020<br>Beam Therapeutics<br>**$207,000,000**<br>Initial Public Offering<br>Joint Bookrunner | AeroDefense January 2020<br>Wesco Aircraft<br>**$2,550,000,000**<br>Credit Facility<br>Joint Lead Arranger |
| Automotive Aftermarket February 2020<br>DealerTire<br>**$415,000,000**<br>Credit Facility to Finance Acquisition of<br>**Dent Wizard**<br>Joint Lead Arranger<br>**$350,000,000**<br>Senior Unsecured Notes Offering<br>Sole Bookrunner | Healthcare February 2020<br>Schrödinger<br>**$232,000,000**<br>Initial Public Offering<br>Joint Bookrunner | Consumer January 2020<br>Grocery Outlet bargain market<br>**$528,000,000**<br>Common Stock Offering<br>Joint Bookrunner | Municipals February 2020<br>Buckeye Tobacco Settlement Financing Authority<br>**$5,352,000,000**<br>Tobacco Settlement<br>Asset-Backed Refunding Bonds<br>Joint Bookrunner |
| Consumer February 2020<br>unitedpf<br>**$746,000,000**<br>Credit Facility to Finance Acquisition by<br>**American Securities LLC**<br>Joint Lead Arranger | Municipals February 2020<br>NYC HDC<br>**$375,000,000**<br>Housing Impact Bonds<br>Sole Bookrunner | Industrials January 2020<br>Hermes<br>**$400,000,000**<br>Sale to<br>**CVC Capital Partners**<br>Sole Financial Advisor | Gaming February 2020<br>Landry's / Golden Nugget Casinos<br>**$2,593,000,000**<br>Credit Facility<br>Joint Lead Arranger |

## JEFFERIES KEY FACTS & STATISTICS

(February 29, 2020)

Founded: 1962

Total Long-Term Capital: $12.7 billion

Number of Employees: 3,822

Companies under Global Equity Research Coverage: 2,300

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