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International edition

June 2021

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Giovanni Marino
Director Grant Thornton FAS

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Partner Grant Thornton FAS

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Overview

Post Covid-19: effects and outlooks within and outside the EU

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The previous issue of Tophic concerned the financial restructuring of banks and companies in the post-Covid phase. This issue aims to give a less local perspective of this phenomenon and provide an overview of what is happening in other EU countries.

In particular, we focused our analysis on three countries, which, due to their characteristics, can in our opinion provide a good representation of the EU situation: UK, France, and Spain.

In order to provide such an overview, we involved some of our Grant Thornton network colleagues, specialized in financial restructuring of companies who, thanks to their experience in this area, provided us with an ”as is” and a “to be” situation in their respective countries, as well as with some useful cues on the role that financial advisors have and could have in the next future within financial restructuring plans, following the disapplication of support measures to businesses that are currently in force, since they will not continue being effective for long. Another analysed issue concerns the effects of the pandemic on the bank system in each of the countries under examination.

Lastly, our network colleagues were asked to briefly explain the main measures adopted by their Governments to support companies in the Covid phase, in order to identify the difference between these measures and those adopted by the Italian Government.

Expert's Opinion

What's happening outside the EU? The UK reaction to the pandemic

Giovanni Marino, *Director Grant Thornton FAS in collaboration with* ***Andy Charters****,*
Partner Restructuring Grant Thornton UK LLP

The quick spreading of the Covid-19 at the beginning of 2020 has shaken the world's economy and the subsequent lockdown during both the first and the second waves led to the worst economic downturn in history. During the crisis, many countries have reacted implementing fiscal stimulus measures to support distressed businesses, which led to a net increase in public debt.
However, in the light of the forecasted recovery of the global economy and of the reduced possibility of further total lockdowns, the economic outlook for 2021 should record a gradual growth with a steady improvement starting from 2022. Undoubtedly, during the recovery phase, the countries that succeeded in better managing the crisis and boost the transformation process (digitalisation, legislation, sustainable economic models) will attain an indisputable advantage.
Basing on the above, we started our discussion with **Andy Charters**, *Partner Restructuring Grant Thornton UK LLP*[1], in order to understand how the UK dealt with the emergency and how it is shaping its future.

The UK market: the management of the pandemic and future scenarios

The UK government sought to alleviate some of the financial strain imposed by Covid-19 pandemic on both private and public sectors with a suite of schemes such as furlough, business interruption loans and tax deferrals.

Giovanni Marino

In addition, new legislation came into effect with the introduction of the Restructuring Plan and Moratorium processes, both of which were intended to give companies sufficient breathing space to restructure their debts and implement turnaround plans. These are positive solutions that should help some underperforming businesses to navigate 2021 and beyond.

The Restructuring Plan introduces the 'cross-class cram-down' which enables companies to limit the influence of dissenting creditors when presented with a viable restructuring proposal, as long as considerable support from other creditors is provided.

The Moratorium gives companies breathing space to devise a turnaround plan, focusing on the rescue of the business rather than the realisation of assets. It protects companies from certain creditor action for an initial 20 business day period, which can be extended or terminated early.

Andy Charters

In addition, a temporary halt was imposed on the use of statutory demands and winding-up where a company is unable to pay its debts as a result of the Covid-19 pandemic.

For further information on the UK Government support can be found at[2].

Which are the consequences for banks?

The banks in the UK played a central role in assisting the UK government in delivering several of the support schemes and have sought to be pragmatic and responsible when approached by borrowers facing challenges meeting covenant tests or facing liquidity crises. This was carried out against the backdrop of the new working environment with a large number of bank staff having had to adapt almost overnight to remote working.

As we go through 2021, the economic impacts of Covid-19 as well as the recovery process for loans made under government-backed lending schemes will become clearer.

We are currently seeing very high levels of liquidity in the market and what is not clear is whether that will continue through 2021 or whether some of the reported liquidity positions are artificially inflated because of the continued government intervention (especially through the furlough scheme).

As is the case globally certain sectors such as retail, real estate, travel, tourism/leisure and hotels, have been more severely impacted by Covid-19 pandemic. Institutions with higher degrees of concentration to these sectors will need to monitor their positions carefully as we move through the next phase of the pandemic and economic recovery.

Whilst we have not yet seen a significant rise in insolvencies in the UK to date, we anticipate that there will be an increase in distressed situations and insolvency appointments starting in Q4 2021 and moving in to 2022. This will place increased pressure on internal systems, processes and management teams in the banks.

Further details on how we can assist banks and businesses can be found at[3].

Which are the consequences for businesses?

Restructuring and insolvency data for Q1 of 2021 shows a continuing low level of formal UK insolvency appointments, but we are seeing a busy corporate finance environment and transactions in the mid-market were very strong in the first quarter. Restructuring advisory projects continued at 2020 levels, particularly lender-led, with a leaning towards real estate, travel, tourism, hotels and leisure.

As expected, we are seeing the impact from the extension of government support, and the general prohibition on creditors petitioning for the winding-up of companies until, at least, 30 June 2021. This continues to act as something of a life-line for businesses that may otherwise have fallen into the distressed category.

It is anticipated that this will continue for the foreseeable future and mid-market insolvency appointment are not expected to start increasing substantially until Q4 (or perhaps H1 2022), at the earliest.

Further details about our view for 2021 can be found at[4].

How can financial advisors support banks and businesses?

Throughout 2020, our restructuring and insolvency team has been busy on a wide variety of assignments. Projects have not only focused on the well documented sectors of retail, travel, leisure and tourism and real estate, but also in financial services, oil and gas and healthcare. We have one of the largest restructuring and insolvency practices in the world, with a truly global reach.

Uncertainty and challenge inevitably lead to opportunities. It's likely that the number of carve-outs and businesses for sale will increase in 2021, as companies' cash flows unwind and new operating models become established. This will lead to opportunities for those with funding or able to access funding to fast track their growth.

Further details on how we can assist banks and businesses can be found at[5].

[1] *https://www.grantthornton.co.uk/people/andy-charters/*

[2] *https://www.grantthornton.co.uk/en/insights/navigating-government-funding-support/*

[3] *https://www.grantthornton.co.uk/en/insights/uk-banking-sector-top-ten-themes-for-2021-and-beyond/*

[4] *https://www.grantthornton.co.uk/en/insights/restructuring-review-q1-2021-what-does-the-future-hold/*

[5] *https://www.grantthornton.co.uk/en/insights/restructuring-credentials/*

~~Focus on~~

The Covid-19 impact on the economy: the response of Spain and France

***Enrico Cimpanelli,** Partner Grant Thornton FAS in collaboration with **Clotilde Delemazure**, Partner Grant Thornton France e **Carlos Asensio**, Partner Grant Thornton Spain*

The current pandemic, from which we are hopefully starting to see a way out, had a significant economic and financial impact on various international economies.

We tried to understand how two EC member States, more similar to Itay from a cultural point of view, reacted to the crisis generated by the pandemic and which are the possible future scenarios.

For this reason, we asked for insights form two colleagues of the Grant Thornton network: **Clotilde Delemazure**, *Partner in charge of the French Prévention et Restructuration practice at Grant Thornton France*[6] e **Carlos Asensio**, *Partner of the Spanish Debt Advisory & Financial Restructuring practice at Grant Thornton Spain*[7].

We asked them 4 questions in order to understand what the respective countries did in order to face the economic downturn caused by the pandemic, the consequences for banks and businesses and the role financial advisors can play to help companies out of the financial crisis.

Below are their replies, which in some respects are quite similar between them, as well as to the Italian situation, whereas they differ for other aspects, due to both the different approach adopted by each country and the subjectivity of the responses of the two professionals.

From the feedback it appears clear how France, compared to Spain and Italy, provided business with a wider range of tools to overcome the crisis, without assessing their status prior to the pandemic.

Which main measures have been taken by your government to manage the economic consequences of the pandemic?

FRANCE
by ***Clotilde Delemazure***
Partner Grant Thornton France

The French Government has provided a large number of measures to support all economic actors. Since March 2020, hundreds of billions of euros have been made available to ensure that companies have sufficient cash flows to get through this exceptional period.
The state-guaranteed loans ("PGE"), a specific and exceptional mechanism set up to provide short-term relief for companies suffering from health crisis, has been offered to more than 675,000 companies. This measure has been extended until December 2021 and a deferment of one more year to its repayment can be obtained for any company that wishes it. However, as the duration of PGE is 6 years maximum, the reimbursement will be spread over only 4 years in case of a second year of deferment. The stake is to know if companies will be able to repay the loan. Indeed, the "PGE debt wall" is currently a major concern for restructuring players.
Furthermore, the postponement of tax and social security deadlines is helping to alleviate the impact of the health crisis.
Finally, public aid, and in particular the introduction of furlough allowance at national level or targeted aid for the most affected sectors (catering, hotels, and events) at local levels are also working to keep companies alive.
Major injections of cash into the economy have saved many companies. However, when PGE and tax and social debts have to be repaid, Covid will undoubtedly have an effect on those businesses losing pace and where the pandemic has only accentuated the difficulties.

SPAIN
by ***Carlos Asensio***
Partner Grant Thornton Spain

The Spanish Government has implemented several economic measures to mitigate the effects of the COVID -19 outbreak amongst which we may find the Temporary Employment Regulation Record (ERTE) and its subsequent extensions as well as one hundred billion euro financing granted by means of guarantees securing the company's indebtedness provided by banks up to certain levels (60%~80%) (the "ICO Guarantees").

Which are the consequences for banks and what are the possible mid-term scenarios?

FRANCE

The state-guaranteed loans ("PGE") have enabled companies to secure their cash flows to offset the effects of lockdown by borrowing up to three months' sales. It is, therefore, logical to ask whether PGE are not artificially keeping non-viable companies alive, described as "zombies".
In the short-term, the French "whatever it takes" strategy of President E. Macron has been so effective, that comparing the 1st quarter of 2020, ante-covid, to the 1st quarter of 2021, the number of insolvency proceedings opened has decreased by 32.1%, from 7,609 openings to 5,743.
However, in the long-term, it is important to be vigilant about corporate over indebtedness. Indeed, the Government includes an estimated probability of default of 6.2% of the guaranteed outstanding amount.
A senatorial proposal has requested that the State guarantee be maintained, with the authorization of the European Commission, beyond the 6 years provided for in the PGE. No answer seems to have been given yet by the Government.

SPAIN

Mainly a surge in the nonperforming debt position resulting in a Tier 1 capital buffer downturn. Thus, the banks might find themselves in a situation where they will not be able to meet the applicable regulatory solvency requirements as the COVID 19 outbreak has caused a downgrading in the company ratings and consequently an increase in the bank's loan loss provisions and a credit contraction.
Having said the above, it should be noted that currently such an increase has been mitigated by the Government with the abovementioned ICO Guarantees yet, in the medium term, once the new company ratings are issued in accordance with the financial information for 2020, the companies will require from the banks the provision of additional cash, debt write-offs or an increase in their unsustainable indebtedness. It will be under this scenario where the banks will need more flexibility from the regulator so as not to demand the same loan loss provisions that would prevent the banks from helping companies without further damaging their balance sheets.

Which are the consequences for corporations and what are the possible mid-term scenarios?

FRANCE

The state aid measures extension has allowed, and will allow, the maintenance of the cash flow "perfusion" helping companies to mitigate the cyclical shock linked to the health crisis and thus ultimately to avoid insolvency. Nevertheless, these measures will be likely to postpone decision-making and encourage a wait-and-see attitude. This situation could be overcome for businesses that were not structurally in difficulty before the crisis, but particularly insolvent businesses may not be able to resist and may not have sufficient prospects for recovery. Indeed, measures such as state-guaranteed loans ("PGE") or other aid (as mentioned above) were necessary, but it now seems even more necessary to anticipate the treatment of this new accumulated debt.

It is therefore essential for companies to move quickly towards an in-depth restructuring strategy, whether operational (Transformation & Steering) and/or financial (Strengthening of equity / Consolidation), with the guiding principle being the sustainability of the company and the treatment of the accumulated "debt wall".

In line with this logic, the French government's recovery plan (100 billion euros deployed around 3 main strands: Ecology, Competitiveness and Cohesion) aims to support the recovery with equity loans and other aid. However, not all French companies will be eligible for this aid and will have to demonstrate their sustainability to benefit from it.

SPAIN

From a company's perspective, we may conclude that (i) the ERTES and their subsequent extensions have allowed companies to reduce their structural costs and be able to match the drop in revenues and profitability caused by the pandemic; as well as (ii) the granting of the ICO Guarantees have allowed companies to have enough liquidity to maintain their business activity and honour their payment commitments. However, in the medium term, we envisage that the companies will emerge from this pandemic with higher leverage ratios (due mainly to the new debt granted with ICO Guarantees and the lower profitability of the business) and greater uncertainty in terms of recovery as the COVID outbreak has changed consumers' preferences and consumption patterns. Consequently, companies will face a situation where either additional liquidity is needed or existing debt is refinanced (by extending its maturity or granting write-offs on the basis of the repayment capacity) as a condition to continue the business activity.

How do you repute financial advisors can support banks and businesses in the post-pandemic phase?

FRANCE

In order to meet the need for transformation mentioned above, the financial advisors will have to intervene in three distinct, but complementary, phases:

- firstly, an assessment of the situation with an operational and financial diagnosis;
- secondly, the Business Plan review: it is through this first phase that the hypothesis underlying the business plan can be reviewed and validated in order to ensure both the sustainability of the company and the conditions for transformations or reorganisation necessary to achieve the business plan;
- based on the second step, it would then be necessary to carry out cash flow forecasts to identify and quantify the financing needs necessary for the sustainability of the activities.

The interweaving of these three steps allows for the orientation towards a sharing of efforts between the shareholders, the public debt, and the private debt.

In the second half of 2020, the French State, through the Ministry of Economy and Finance, has issued a call for tender to select 5 financial advisory firms to assist it, through financial and operational diligences within independent business review, in the restructuring of companies. The Recovery & Reorganisation Team of Grant Thornton France has been selected among the five nominees. This recognition confirms the place of Grant Thornton's French Restructuring Team among the leading players of restructuring.

SPAIN

Financial advisors may help by identifying and structuring financing schemes to be used as an alternative to bank financing, acting as independent experts who verify the fulfilment and execution of the action plans included in the business plans. Our rigor and multidisciplinary expertise place us in a great position to monitor and improve the companies' productivity, as well as to adjust the nonperforming and recovery models on which the banks are based.

[6] *https://www.grantthornton.fr/fr/nos-experts/clotilde-delemazure/*

[7] *https://www.grantthornton.es/en/meet-our-people/carlos-asensio/*

More info:

FRANCE: https://www.grantthornton.fr/fr/service/conseil-financier/prevention-et-restructuration/

SPAIN: https://www.grantthornton.es/en/services/financial-advisory/debt-advisory-and--financial-restructuring/

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