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# Addressing the financial and operational challenges caused by COVID-19

FW discusses how to address the financial and operational challenges caused by COVID-19 with Alan Tilley, David Bryan and Matthew Quade at BM&T European Restructuring Solutions.

## THE PANELLISTS

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Alan Tilley is a founding principal of BM&T European Restructuring Solutions. He has significant expertise in turnaround and restructuring, managing the complex issues in preserving enterprise value while operating in the zone of insolvency. He is a frequent speaker on cross-border European restructuring and has written several articles on the subject, as well as a recent book. He is the 2008 and 2014 recipient of the TMA International Chairman's awards for outstanding service to the international turnaround and restructuring profession.

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David Bryan is a founding principal of BM&T and has extensive experience working with international and UK companies in restructuring and improvement. He has operated at chief financial officer (CFO) level in large and SME companies in the UK, US and Europe, and worked for many years in a Plc acquisition and integration team. He was the 2018 recipient of the TMA International Chairman's awards for outstanding service to the international turnaround and restructuring profession.

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Matthew Quade has 19 years of turnaround and restructuring experience working for a wide range of stakeholders across a variety of industries during a career which has taken him from a 'Big 4' accountancy firm to a major international bank, a global consultancy practice and to building his own successful business before joining BM&T in 2018.

**FW: Although we are still in the midst of the COVID-19 crisis, how would you characterise its impact on business and financial markets to date?**

**Tilley:** With a few exceptions, the impact of COVID-19 on business has been catastrophic. Businesses have seen their revenues drop dramatically almost overnight and in many cases to zero. Financial markets have been badly hit worldwide with about a 30 percent drop in global wealth. It is an incredibly volatile situation with markets reacting to every bit of news. Businesses are understandably very uncertain and frightened as they try to navigate these uncharted waters.

**Quade:** The government is trying hard to prop things up and offer help to businesses, as well as to keep as much running as possible while operating within the hygiene and distancing requirements, but there are real issues with the way many statements and policies get communicated by mainstream and social media. You can only trust the source to give you the full, accurate picture, but the amount of noise out there is creating a great deal of confusion and misunderstanding, resulting in poorly informed and rushed decisions which are often unnecessarily detrimental.

**FW: To what extent is the pandemic already placing unprecedented stress on companies? What sectors appear most at risk?**

**Bryan:** The stress is widespread and very real. In normal times, businesses slide into distress, sometimes quickly, and there are warning signs, but this is a new phenomenon with good businesses having to close down overnight. In many ways the stress is bifurcated with businesses either having to close or finding themselves under extreme pressure to ramp up essential supplies. Healthcare-related businesses, food manufacturing and distribution are all struggling to cope. Some are looking to hire thousands of people. On the other hand, most non-essential retail businesses have closed, the hospitality industry has shut down and the car industry and much manufacturing has shut down as supply chain issues, workforce sickness and a dramatic drop in demand have made it impossible to continue production.

**Quade:** Some pockets seem to be managing well, but even then, there remains unprecedented stress on both their management and workforce from sudden changes to working arrangements and the social pressures and confused messaging in the media. For businesses not told to close their doors, but needing to attend site, those that survive will be the ones able to best adjust to the hygiene and social distancing requirements, with robust supply chain contingency plans and working in industries that will keep going – a broader range than people might think if you take the US Federal Critical Industry list as a guide. Many service businesses have been able to adapt to remote working quickly, but it remains to be seen whether there will be sufficient demand to remain at or near normal capacity.

**FW: As businesses find themselves in uncharted waters, to what extent does the prevailing uncertainty and volatility present its own problem? With little basis for comparison, how can business leaders make key decisions and develop reliable strategies?**

**Bryan:** Even under normal circumstances, few people in senior management teams have had any experience of running a business in distress. Ordinarily they would have to learn as things unfold and be guided by external professionals. This situation is far worse than normal and will test everybody, including those of us who normally work in the zone of near insolvency. There are no comparisons and huge unknowns remain. Every day seems to bring something new and government announcements are coming thick and fast. Perhaps the greatest unknown is how long this will last and even when life starts to return to normal, how quickly will the economy pick up again?

**Tilley:** The worst thing that management can do is panic and just thrash around looking for quick solutions. It is highly unlikely there will be any. This needs a calm, careful analysis of the business situation and the development of a survival plan. The plan needs to be as flexible as possible because circumstances will change as the COVID-19 crisis unfolds and both governments, businesses and people react. For a good viable business there should be a way through all this. For those businesses that have been forced to close down by government restrictions or lack of demand due to the lockdown, it may mean a form of business hibernation. However, we must recognise that some businesses that were only marginally viable and close to insolvency before COVID-19 may not survive.

**FW: Given that the measures taken in response to COVID-19 will very likely lead to an increase in restructuring and insolvency cases, what practical steps should business leaders be taking now? What considerations may be critical to survival?**

**Quade:** Any future growth in restructuring and insolvency cases will be very dependent on individual business circumstances and the ever-changing legal and political frameworks. The first thing to take a view on is business viability. There is little point in trying to rescue a business that was already on its knees before COVID-19 arrived if it really has no hope of long-term survival. This can be a hard decision for owners and managers to make as they will always want to see their business continue, so it often helps to have somebody impartial give objective advice. Businesses with high levels of pre-existing debt will clearly find it harder to get through this than those with significant cash reserves or lending headroom. The issues are not just financial, however. Assessing viability requires a robust look at what the company does, its markets, its competitors and many external factors to make a reasoned decision on the prospects of the business. If it is not viable then the directors should be consulting an insolvency practitioner with a view to putting the company into a formal insolvency process.

**Bryan:** If the business is viable then a model needs to be prepared quickly to gain an understanding of what the business will look like in the coming few months. It will be necessary to look at it week-by-week with such a fluid situation. Existing budget models are rarely suitable for this type of exercise. Cash is king and modelling needs to be highly focused on cash and much less on detailed profit and loss (P&L) analysis. It also needs to be highly flexible so that all key assumptions can easily be altered and the model recast. External support from those who have done this many times can help to get this in place much more quickly with the requisite level of detail and flexibility. One key factor will be the ability to add government initiatives into the modelling. Only once you have this can you start to see where the critical problems are and what needs to happen to survive the next few months. In turn, this will guide the negotiations that have to take place with creditors, lenders, the workforce, HMRC and so on, for the survival plan to be implemented.

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**Tilley:** In the UK, government help with 80 percent of salaries and wages will be a great help but is subject to a cap and there will likely be a timing delay. It may not cover agency and all self-employed workers. Government help has also been offered by way of business rates relief, grants to small and medium-sized enterprises (SMEs), delays in VAT and self-assessment tax payments. There is also the government backed loan scheme through the banking system but quite how this will work out remains to be seen. In any case, the question must also be asked as to whether more debt is the answer for already indebted businesses. There will likely be further reliefs announced as things progress. The issue of directors' duties and insolvency triggers is also important. These are a grey area at the best of times, but even more so in the current environment. The government has recently announced it will suspend the wrongful trading rules and accelerate the introduction of planned legislation for a moratorium from creditor action. Exactly what this will entail remains to be seen. However, it is unlikely to be a carte-blanche to just continue trading regardless. A good plan that demonstrates how the business will survive and justifies the actions the directors are taking will always be essential.

**FW: What advice can you offer to those companies that are facing bleak prospects? What is their hope for rescue and recovery versus insolvency?**

**Quade:** The speed with which many businesses have fallen into crisis is unprecedented and is causing huge uncertainty and concern. There is no doubt that some companies will go under.

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We may see more liquidations rather than administrations where the business goodwill and assets are normally sold out of the administration process. Who will the buyers be for businesses that did not have a strong business model and were propped up by cheap debt pre-COVID-19? Without them, liquidation may be the only alternative with the business perhaps not surviving at all, but an element of this is required for a healthy economic recovery led by businesses with viable strategies and without over-leveraged balance sheets.

**Tilley:** Those with a sound business model that can clearly recover at the end of this will be in the best position. Of those, the businesses with the lowest levels of debt will find it easier to ride out the storm. Good businesses should have hope. The key is to be able to negotiate consensual arrangements with the various stakeholders and stay out of any formal insolvency process. This preserves the goodwill in the business, often represented by the collective skills and knowledge of the management team. It will not be easy, but nobody wants to see good businesses going into insolvency processes.

**Bryan:** In the past, we have often seen distress manifest itself in certain sectors. This crisis will have a much broader impact and will require some innovative thinking. One thing we will undoubtedly see is businesses being put into what can only be termed 'hibernation'. It will effectively cease trading and look to achieve the lowest possible cash outlay to keep the business alive and no more, but be ready to start again once we are past the crisis. With government initiatives on certain costs and a strong focus on lowering others, this should be possible. It has not really been done before so it will be interesting.

**FW: In times of distress, what benefits can companies gain from turning to external experts – especially those who have navigated similar, if not identical, situations, in the past?**

**Bryan:** Even those with experience in turnarounds and working with near insolvent businesses will not have experienced anything quite like this in terms of the speed and severity of the crisis. But having worked in the zone of insolvency is invaluable experience. Bringing a calm, orderly approach to a chaotic situation, prioritising what is important, being able to rapidly marshal the available data and having the skills to manage expectations and negotiate with stakeholders can be a great help to management teams who have never experienced such circumstances.

**Tilley:** Experts with this sort of experience understand the pitfalls and what can go wrong. They also understand the art of what is possible. This is often much more than management might believe at the outset. They are always on the lookout for anything that can be used to leverage the situation and achieve a result for the client. Years of experience also mean they know the likely stance of the various stakeholders, what is important to them, and how to sell a turnaround plan to them.

**Quade:** The nature of turnaround work means those involved are experienced negotiators who understand the need to achieve rapid agreement between parties with often competing agendas. They are also especially helpful, if not essential, when dealing with complex group situations and multinational businesses where different jurisdictions have different approaches to restructuring and insolvency. The chances of avoiding an insolvency process will be much higher with external help that can demonstrate it has succeeded in avoiding insolvency for clients many times in the past.

**FW: Do the conditions created by COVID-19 give rise to new market opportunities, where strong, adaptable organisations can take advantage?**

**Quade:** We are already seeing innovative organisations finding new ways to apply their skills to help in the current situation. Automotive and motor sport companies are using their highly skilled engineers and rapid product development processes to produce much needed ventilators and other healthcare equipment. An artisan gin distillery has used its stocks of alcohol to produce hand sanitiser. Opportunities are opening up in distribution and healthcare-related activities and smart companies will move in. However, there is still an artificial barrier being created by social pressures around staying at home that result from a misunderstanding of the key advice and the government guidelines that could yet derail some of this vital activity to keep the economy running in a state from which it can recover.

**Tilley:** There is still a lot of dry powder available in private equity (PE) and distressed investing funds. We have already been contacted by distressed funds telling us they are looking for new situations where they can deploy capital. There are bound to be M&A opportunities as a result of the current disruption. Good viable businesses that have been damaged by the COVID-19 crisis may be well advised to consider an equity injection, both to ensure survival and to bounce back more quickly when the crisis is over. That bounce back could include buying up competitors or investing to scale up or expand into new business areas.

**Bryan:** Many of the things we have taken for granted in the past have been severely disrupted by this crisis and that is forcing innovation to compensate. It is amazing what is being achieved by resourceful and imaginative individuals and businesses. Some just address the immediate problems and may not continue beyond the crisis, but others may well continue as we all adapt to new ways of working and living. There will be many opportunities as both consumers and businesses look at things in a different light. Some hard-hit sectors will see M&A activity as they consolidate to gain efficiencies post-crisis.

**FW: It may be too early to make any short-, medium- or long-term predictions about COVID-19's impact on the corporate world, but based on your experience, what trends do you expect to see?**

**Tilley:** It is difficult to know how it will all work out. Governments around the world are having to react as things evolve and time will tell who did well and who did not. Government spending around the world will have increased dramatically and that bill must be paid. Taxes may have to rise. One interesting corporate trend may be toward more dispersed working with teams in different places and many more working from home. This will be very good news for the suppliers of online meeting services and other tools for remote teams to work together. It would also have a knock-on effect on office space requirements and commuting. It could also mean less business travel. This would not be so good for the railways and airlines, but it would aid climate change challenges.

**Quade:** Of course, the future depends on how and when we come out of the crisis and how quickly confidence returns. On the one hand you can look at China where factories have reopened and people are starting to be allowed out, but even then, there is nervousness about a second wave of the virus and reports suggest consumer demand is very weak. People will likely save more and spend less to build a buffer against any future crisis. Maybe they will change other behaviours with more focus on locally produced goods and less travel. Business confidence and investment may also lag as they wait for consumer confidence to recover. Another indication of the likely impact is that US distressed debt has quadrupled to the $1 trillion mark in just a week. If this impacts market liquidity as in 2008 then we will have a second wave of dire economic impact and funding issues for the corporate world to contend with.

**Bryan:** The corporate world will take a long hard look at resilience. Often thought of as plans to deal with one-off events, such as weather-related crises, COVID-19 has shown up much greater issues. Supply chain resilience will come under much greater scrutiny and long-distance chains will start to look a lot less attractive. On-shoring from China and the Far East was already happening as cost advantages were eroded; I expect to see that trend accelerate. Single sourcing and just-in-time may also be looked at in a different light. The competition for scarce resources, such as ventilators and personal protective equipment, during the COVID-19 crisis may also lead governments to look at redefining critical industries and better protecting them. ■

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