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RESTRUCTURING & INSOLVENCY 2022

Contributing editors**Catherine Balmond and Katharina Crinson**Freshfields Bruckhaus Deringer

Lexology Getting The Deal Through is delighted to publish the 15th edition of *Restructuring & Insolvency*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on the British Virgin Islands, the Cayman Islands, Guernsey and Jersey.

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Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Catherine Balmond and Katharina Crinson of Freshfields Bruckhaus Deringer for their continued assistance with this volume.

 LEXOLOGY**Getting the Deal Through**

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Global overview

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At the time of writing in September 2021, while improving, covid-19 is still having a significant adverse impact on the global economy. Many developed countries have vaccinated most of their adult population, resulting in an easing or removal of restrictions. This has allowed their economies to move into a recovery phase, often leading to impressive economic growth. However, the Delta variant is causing a spike in cases that has forced reopenings in other countries – particularly those with slower vaccine roll-outs – to go into reverse. The emergence of other covid-19 strains further clouds the picture.

Still, the economic outlook is far better than at this point last year, and the expected wave of restructurings has not, in the main, materialised – at least not yet. Indeed, restructuring markets around the world are remarkably benign. This is largely due to continued government support measures and super-low interest rates, running alongside strong economic bounce backs in many countries, as well as abundant liquidity in the market (particularly among private sponsors and lenders). In June 2021, Standard & Poor noted that corporate defaults year to date were nearly 60 per cent lower than they were in 2020, with such defaults as there were focused on the oil and gas, consumer products and media and entertainment sectors.

Consumers to the rescue

For businesses in a precarious position, a rapid rebound in consumer spending (as seen in some countries) may offer a lifeline. Households around the world cut discretionary spending during the first year of the pandemic, resulting in them accumulating an extra US\$5.4 trillion of savings by the end of the first quarter of 2021, according to Moody's. Even if they were to spend only a third of that, it would boost global output by just over 2 percentage points both this year and next.

At a national level, the UK business organisation the Confederation of British Industry predicts that consumer spending will be the driver of 70 per cent of UK growth in 2022, with the UK economy returning to pre-pandemic levels by the end of 2021.

US rebound

The economic outlook in the US looks even rosier. President Biden's US\$1.9 trillion March 2021 stimulus package included financial support for lower-income households, families and the unemployed, along with aid for small businesses and key sectors, such as aviation and surface transport.

Since then, organisations such as the non-partisan US Congressional Budget Office and the International Monetary Fund have revised their earlier 2021 US growth forecasts upwards to 7 per cent or more. If their predictions are accurate, it will not be long until the US economy gets back to its pre-pandemic position. In turn, this has generated some fears of inflation and whether the historically low interest rates will need to be raised sooner than expected. Although those worries and related disagreements surface regularly, thus far they do not seem to be troubling the majority. Is this justifiable comfort or casual complacency? Who knows? Notably, the Delta variant has taken

a foothold in regions of the US with large, unvaccinated populations, posing a growing threat of spread to vaccinated regions. This has caused some states to roll back the relaxation of pandemic-related restrictions. Whether the Delta and breakthrough cases to vaccinated populations will slow the US economic rebound is unknown. At least in so far as the US central bank is concerned, one thing is clear. As stated by Federal Reserve Chairman Jerome Powell, covid-19 has fundamentally changed the US economy and it will not return to the way it was pre-pandemic. What those changes mean in actual effect remains to be seen.

The big thaw

Assuming no vaccine-proof coronavirus variant materialises, governments around the world will continue phasing out their business-support measures. So what will happen once they end?

Again, no one knows for sure, but an Alix Partners survey found that almost a third of global restructuring experts believed more than half of their clients that needed financing during the pandemic in 2020 would find themselves in financial distress again.

That distress will be particularly acute in those sectors that went into a deep freeze during the pandemic and are only slowly thawing out, such as aviation, hospitality and physical retail.

Infrequent fliers

The year 2020 saw a huge slump in international air travel, which resulted in net debt of the global airline industry soaring to US\$220 billion by year's end, according to International Air Transport Association figures.

Since then, European countries have imposed various ever-changing restrictions on inbound and outbound travellers. With these continuing into the summer, airlines are bracing for another sub-peak season.

Corporate travellers are proving even slower to return to the air, with the US Travel Association saying that business travel in the United States will not recover until 2024 at the earliest. In the longer term, even once the pandemic subsides, environmental considerations and the popularity of videoconferencing may continue to leave business-class seats unfilled. So for carriers reliant on cross-border and business travellers, any rebound may not be big or quick enough to prevent debt defaults and – in some cases – failures.

This has all had an impact on airports too. For example, UK airports stood to lose £2.6 billion between April and September 2021 without another summer of mass international travel. The Airports Council International has also warned of a 'severe airport investment crunch' in Europe after the industry was forced to take on more than €20 billion of additional debt last year. Some of the large international airports may be 'too big to fail'. But regional airports might be unable to find the necessary travellers or financial support.

High street blues

Two other sectors with interdependent fortunes are high street retail and commercial real estate.

With tough lockdowns continuing into 2021 and closing most shops, people once more turned online to make purchases. Several physical retailers that were already struggling against online competition ended up as either an online-only brand or consigned to corporate history. As a result, owners of commercial real estate have a growing number of city-centre vacancies.

In the United Kingdom, for shops that continue to trade, the ban on evictions has been extended to March 2022 (for England at least). Meanwhile, retailers and others in the leisure sector have used restructuring mechanisms to adjust commercial leases they believe are no longer sustainable (eg, fitness chain Virgin Active's restructuring using a UK restructuring plan in May 2021).

Some of these mechanisms have been challenged by landlords who, with around £6 billion in unpaid UK rent due, are facing a financial crisis of their own. For example, landlords challenged the company voluntary arrangements of fashion retailer New Look, personal-care business Regis and coffee-shop chain Caffè Nero, and the restructuring plan of Virgin Active. The challenges were, however, in the main, unsuccessful.

Carbon upset

The oil and gas sector is no stranger to restructurings. The record slump in the price of crude in April 2020 prompted several US oil services companies to file for Chapter 11 protection. While some will emerge from the process in a healthier financial position, with environmental, social and governance (ESG) threats hanging over the sector, the market conditions are still not especially good. Even though the oil price has recovered significantly over the last year or so, disagreements at the July 2021 OPEC+ meeting suggest that a continued resurgence is not guaranteed.

The sector is also suffering from an oversupply of rigs and a drop in new drilling activity. And that's all before the growing pressure on lenders to apply stricter ESG criteria and the challenge of achieving the Paris agreement's target of net-zero carbon emissions by 2050.

In the United Kingdom, we saw alternative investment market-listed Hurricane Energy try to address its financial difficulties early by proposing a restructuring of its issued notes – over a year out from maturity. The company proposed to implement a debt-for-equity swap that would have seen existing equity holders retain only 5 per cent of the restructured company. To some commentators' surprise, the English courts declined to sanction this restructuring plan as there was no immediate threat of insolvency and the business was, in the short term, trading profitably. Hurricane Energy is now instead pursuing a tender offer for its bonds.

Brexit friction

The effects of Brexit rumble on, but with covid-19 dominating the headlines, have not received the attention they might have done otherwise.

Businesses in England, Scotland and Wales are still getting to grips with new trading rules agreed with the European Union in December 2021. Businesses in Northern Ireland, meanwhile, can trade more freely with Ireland and the rest of the European Union. However, the movement of goods across the Irish Sea is proving less straightforward, causing friction between the British government and the EU Commission.

There is no sense yet that the additional costs of compliance (or the loss of revenue if EU sales are abandoned) are leading to financial distress. However, it may be that the UK government's pandemic-induced support measures are masking the worst effects.

The UK restructuring plan, Dutch WHOA scheme and German StaRUG

Introduced in June 2020, the UK's restructuring plan, which introduces cross-class cram down, is one of the biggest changes to the English



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insolvency and restructuring landscape in recent decades. Understanding of the legislation is developing as cases are heard (approaching 10 at the time of writing), but its impact is being felt across the UK restructuring market as it shapes negotiations. There are still several untested elements and the full reach of the plan is yet to be established.

The UK has, for the past decade, dominated Europe's restructuring and insolvency market. However, that may be changing as other European countries – notably Germany and The Netherlands – introduce their own mechanisms to comply with Directive (EU) 2019/1023 (preventive restructuring frameworks) and, to a degree at least, the impact of Brexit is felt.

The Dutch equivalent of the English scheme of arrangement (court confirmation of extrajudicial restructuring plans (WHOA)) is designed to attract both domestic and big cross-border restructurings, and provides a great degree of flexibility in the choices the debtor can make. The regime can be implemented on a confidential or public basis. To date, most of the restructurings have used the private route, making it difficult to assess WHOA's success. And while it is still early days, most companies using it have been in the small to medium-sized (SME) enterprise space.

The Stabilisation and Restructuring Framework for Businesses (StaRUG) regime, which was powered through Germany's legislative

process and came onstream in January 2021, also seeks to provide a real alternative in many ways to the English scheme – at least for companies with their centre of main interest in Germany. The StaRUG has, to date, been used by relatively few companies and, like in The Netherlands, only in the SME sector. At this stage, it seems unlikely to become a tool of choice for non-German companies.

Elsewhere in Europe, further reforms are expected in France and Italy before the end of 2021. However, it is too early to say whether any of these new tools will help pull European restructuring's centre of gravity away from London.

Risky ESG

As seen with the oil and gas, and travel industries, the emergence of ESG considerations could make it harder for companies to obtain financing. When assessing potential investments, more lenders and sponsors are requiring borrowers to disclose more details about their ESG credentials, and lenders and sponsors themselves are conducting ESG audits of their investment portfolios. They might also add ESG-related covenants to credit agreements and be less keen to waive covenants for companies with a riskier ESG profile.

Market commentators have also been considering whether ESG issues will influence credit positions in distressed scenarios, particularly if lenders are looking to do less investment in high-risk companies (although conversely, this may increase opportunities for distressed investors).

US opioid bankruptcies

The effects of the opioid crisis continue to reverberate throughout the United States, including in the restructuring sphere. Opioid manufacturers and distributors face substantial liability from opioid-related lawsuits, many of which have been filed by federal and state agencies. Lawsuits by individuals also exist in large numbers, but the extensive

public impact of the opioid crisis distinguishes it from other mass tort situations that have historically been dominated by private plaintiffs (eg, asbestos and product liability). In any event, several large pharmaceutical companies have filed for bankruptcy to address their opioid-based liabilities, including most prominently, Purdue Pharma, and more filings in the sector are predicted.

Conclusion

A year ago, the world had no covid-19 vaccines. Now it has many, with doses finding their way into billions of arms. Distribution is not uniform but developed economies are making great strides, despite vaccine hesitancy in some quarters. What this means for the restructuring landscape is still unclear and commentators differ – both as to impact and timing.

The quicker vaccines are administered, the sooner government support measures will fall away. In some economies, this could prompt a major increase in insolvencies rather than the gentle wave seen so far. However, with economic activity picking up strongly in many sectors, the wave may still be far off and smaller than many had feared. Moreover, given the regional concentration of vaccine hesitancy in some countries, and the resurgence of covid-19 in those areas, the economic rebound may well impact national economies disparately, and may further stress existing income inequality within and among countries.

Which scenarios prove to be more accurate, only time will tell. However, there is a strong sense that – even if the economies are rebounding on a macro level – not all businesses and sectors will flourish in the post-pandemic world as they seek to grapple with much larger debt burdens and the 'new normal'. There are certainly interesting times ahead.

This guide, as a way of keeping track of global legal developments, will continue to be an important reference tool. As ever, we hope that you enjoy reading and using it.



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