

ANALYSIS

‘A new era of stress’: Perspectives from City restructuring partners and what to expect from 2024

How did the restructuring scene navigate the challenges of 2023 and what's on the horizon for the coming year?

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Restructuring

Casting a glance back at the year nearly at its end, industries faced challenges from inflationary pressures, soaring interest rates, geopolitical uncertainties, and an energy crisis, putting even the more robust sectors to the test.

In the midst of these conditions, company insolvencies during Q2 and Q3 2023 reached their highest point since Q2 2009, according to data provided by the Insolvency Service.

Mark Fennessy, who co-heads the finance, restructuring and special situations group at McDermott Will & Emery in London, sets out the state of play: 'In the UK, we have recently had a combination of some of the worse economic factors possible – exiting the Covid-19 pandemic, weak economic growth and energy price escalation. It has taken some time for the UK economy to adjust to Brexit and energy prices have

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spiked. Combined with high interest rates and high levels of inflation we have a perfect storm leading to year-on-year increases in the level of insolvencies.'

LB took to the scene to speak with restructuring heads and partners at City firms to review the landscape of 2023 and glean perspectives on how the market is shaping up as we move into 2024.

The backdrop

Although certain industries inevitably face more challenges than others, no sector is completely immune to economic reversals. Partners point to the difficulties in forecasting asset valuations and the increased pressure on companies to refinance.

Dechert London practice head Adam Plainer comments: 'There has been an uptick in insolvencies in the SME market, but we have yet to see a volume of insolvencies affecting large corporations. There is a fair amount of debt that needs refinancing and, given the cost of capital, some businesses may not survive.'

He adds: 'Another challenge is the valuation of assets in a market which is increasingly uncertain, but it has been busy towards the end of 2023 with a real uptick in the distressed investing market.'

Mark Knight, co-head of restructuring at Sidley in London, notes other issues as we look ahead to the prospects of the coming year. 'Employment remains high for now, but pressure on the consumer is building. We expect a further uptick in restructuring activity through 2024.'

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Nick Moser, head of the UK restructuring and insolvency practice at Taylor Wessing, agrees: 'Every January since 2009, there have been insolvency lawyers saying, "This is the year for the tsunami of restructurings", but it has not yet transpired like that. I believe next year will continue with a steady uptick and there will be more and more restructurings but I don't expect a deluge in the short term.'

Strong US firms remain confident in navigating through these market conditions using existing tools.

Kon Asimacopoulos, partner in Kirkland & Ellis' restructuring group in London, comments: 'We are clearly entering a new era of stress; the convergence of high borrowing costs, subdued growth, and stubborn

inflation continue to have a material impact on certain companies which have so far been able to survive without coming back to market.'

He adds: 'Thankfully, the cross-border legislative and documentary web has not impeded the ability of the profession to find ways through even the most challenging situations.'

Lawyers remain less certain on the role of amend and extend (A&E), in which lenders opt to extend a loan's maturity instead of securing new loans, particularly when faced with high interest rates.

Liz Osborne, partner in Akin's restructuring team based in London, asserts: 'We have seen a number of amend and extend restructurings, which will probably continue to an extent for some time. However, the interest rate environment, when coupled with over-leveraged balance sheets, means there will be some situations where an A&E is not feasible and a more holistic solution is needed.'

Knight adds: 'There is a maturity wall looming large in 2024 and 2025. The era of cheap money is over, and efforts to refinance or amend and extend will inevitably be more challenging than we have witnessed for some time now. Private credit funds have plenty of capital to deploy, but they will be selective.'

On a global scale

City restructuring teams have continued to advise on some of the world's biggest mandates. Notably, German property developer Adler and oil and gas group McDermott, both of which engaged in the English Part 26A Restructuring Plan, alongside multiple procedural and parallel proceedings in various jurisdictions.

Enacted in 2020, the UK Restructuring Plan provides companies with an alternative to a Scheme of Arrangement, aiming to safeguard businesses from collapse by facilitating restructuring. It empowers courts to approve the restructuring order, even if certain creditors oppose it, using the 'cross-class cram down' mechanism.

Jifree Cader, co-head of restructuring at Sidley alongside Knight, comments: 'The UK Restructuring Plan has proven to be an effective tool in helping debtors find creative solutions to deal with their balance sheets. Use of the Restructuring Plan continues to evolve and it is likely that cases will break new ground in the coming years.'

Partners note a rise in the challenges to restructurings as a prevailing theme, noting high-profile recent cases. Adler was the first UK Restructuring Plan to go to the English Court of Appeal, and McDermott has been challenged by different groups in UK, US and Dutch proceedings.

Howard Morris, who heads the London business restructuring and insolvency team at Morrison Foerster, comments: '2024 will be interesting as the courts wrestle with Adler and other cases. This is important for restructuring plans and schemes of arrangement as it means judges are not simply rubber stamping. The UK courts will be looking at this concept of fairness, and this will be at the heart of a number of issues into next year.'

Osborne adds: 'We are still waiting to see what the Court of Appeal is going to say [on Adler]. We expect some judicial guidance will be given around what a robust plan process should look like.'

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She adds: 'That kind of more litigious environment is inevitable with the introduction of the Restructuring Plan and cross-class cramdown. To date, European restructurings have been largely consensual – in the past 20 years there have been relatively few significant challenges, largely because schemes of arrangement implied a high degree of consensus throughout the classes with the alternative being an insolvency process.'

Elsewhere in Europe, lawyers highlight that the road testing of EU preventative restructuring processes, which have been implemented in recent years, will extend into 2024.

In June, international auto parts manufacturer Leoni received court approval for a plan under Germany's Corporate Stabilisation and Restructuring Act (StaRUG), marking the first major restructuring using this 2021 tool. Likewise, around a similar time, South African retail conglomerate Steinhoff secured court sanction of its WHOA restructuring plan in the Netherlands, as the first major international Dutch case.

'Notwithstanding Brexit and European reforms, the introduction of the Dutch WHOA and German StaRUG means we are becoming more adept at getting parallel schemes and using multiple jurisdictions,' says Morris.

Asimacopoulos agrees: 'We also now have a range of flexible processes in Europe which have enhanced the ability of stakeholders to implement restructurings – restructuring plans in the UK and Spain, WHOA in the Netherlands, StaRUG in Germany and others.'

The pressure continues

Looking ahead to next year, lawyers have pointed out key sectors that are predicted to face greater challenges compared with others, given the cost of living crisis putting pressure on expenditure.

Fennessy notes that a downturn in consumer spending and ongoing inflationary pressures will impact businesses across a variety of sectors. 'Any business linked to consumer spending, such as retail estate, travel and tourism, has been badly affected in 2023 and that is set to continue into 2024,' he says.

Plainer adds: 'There are more inquiries coming through in certain industries including healthcare, transportation, and construction – these are industries which have had some serious issues post-Covid. Retail will be affected too, but we'll see what happens after Christmas.'

Despite the clear reversals, partners remain confident in the robustness of London as an enduring centre for cross-border restructurings. LB