

**C**HAPTER 11 BANKRUPTCIES HAVE BEEN AT their lowest levels in more than two decades. But even before the economic jolt caused by the Covid-19 global pandemic, experts saw dark clouds on the horizon.

Edward Altman, creator of the “z-score” indicator of financial distress, is warning of a potential default level reminiscent of the 2008 financial crisis. What S&P calls the “weakest links”—issuers with at-risk credit—had already hit a record in the fourth quarter of 2019. At that point, the Professor Emeritus at NYU Stern School of Business estimated 5 percent of high-yield corporations were at risk of default in the coming year.

In March 2020, Prof. Altman estimated that the number had doubled in just a few weeks, and that the high-yield bond market could now see around \$150 billion in corporate defaults, with even more in the loan market.

“Today, our numbers are showing a likely default [rate] over the next 12 months of just under 10 percent—that is a huge, unprecedented increase in such a short period of time. It does signal a crisis in the credit market whenever you get to that 10 percent level,” Prof. Altman told Yahoo Finance in late March.

The US government’s massive \$2 trillion stimulus package may mitigate that estimate somewhat, while bringing its own set of unusual concerns. No matter what, the coming wave is likely to bring huge challenges for businesses.

First, the scope, severity and suddenness of the downturn are all unprecedented. Former Fed Chair Janet Yellen told CNBC that second quarter GDP could plunge by 30 percent in a “devastating hit” that would be the worst fall since the GDP metric was introduced in the 1940s. Industries such as travel and hospitality are likely to be hardest hit, but few areas of the economy or regions of the world will emerge unscathed.

Second, companies undergoing restructurings will face significant uncertainty regarding the length of time large parts of the economy will remain shut down and how far consumer spending will drop. Under these circumstances, it could be much more difficult to reach agreement on a plan of reorganization and avoid litigation in bankruptcy court.

Communications during both out-of-court restructurings and formal bankruptcy processes will be critical to a corporation’s success in navigating this terrain. Four key points to consider will help shape such a communications strategy in the event it becomes necessary.

# WHEN YOUR CRISIS STORY HITS CHAPTER 11

The current rough passage may not end with Covid-19. Brunswick’s **JONATHAN DOORLEY** and **WILL RASMUSSEN** lay out steps to take now.

**1 Trust and goodwill now are essential.** Restructuring resembles a battle between warring tribes, where factions within tribes often have strongly differing interests. Companies will have an easier time—whether negotiating with stakeholders to stave off bankruptcy or building consensus around a reorganization plan—if they have already established goodwill during the darkest days of the Covid-19 crisis.

Many companies have taken steps to help employees and communities deal with the harsh realities affecting them, displaying compassion and shared sacrifice in a time of need. Examples include Marriott’s and Air France-KLM’s announcement of executive salary reductions; Carnival Cruise Lines donation of its ships as makeshift hospitals; and BP offering free fuel at retail sites for emergency workers. In the heat of the crisis, such actions help to keep vital channels open for the future by demonstrating that the concerns of stakeholders and their communities are important to the business’s leaders.

Employees and customers will often feel overlooked in a restructuring process yet are essential to



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the success of the restructuring plan. Politicians may also raise their voices on bankruptcy and restructuring proceedings. Companies that have a history of doing their part for their community are far more likely to get favorable consideration.

**2 The government will take a big role.** Compared to previous bankruptcy waves, we will likely see a greater level of political involvement given the magnitude of the health crisis. In particular, companies taking CARES Act loans will face greater scrutiny over the treatment of workers and executive pay, and taxpayers may become a direct shareholder in the most distressed industries, such as airlines. This could cause controversy even greater than that which surrounded the Troubled Asset Relief Program (TARP) in the last financial crisis.

The government is also pushing stakeholders to work more collaboratively: Regulators including the Fed, FDIC and OCC for example have eased reporting requirements around troubled loans and encouraged banks to work together with borrowers. This evolving and more complex stakeholder

landscape will require new considerations, including the ability to understand a wider range of concerns and deploy effective messaging far more broadly.

**3 Prepare for a tough fight and focus on winning key victories:** A bankruptcy process will provide multiple opportunities for the involved parties and others to set the narrative. Establish a game plan in advance, deploy communications that will build momentum through a potentially aggressive battle, and mete out new information judiciously to keep the upper hand. Despite the possibility for a more collaborative spirit, it’s wisest to brace for an aggressive fight likely to include leaks and misleading information.

Take full advantage of the milestones, which may include a forbearance agreement, disclosure statement hearing and approval, or the start or outcome of a confirmation hearing. Companies must prepare to seize these moments to reach the critical stakeholders with messages that will resonate. Supportive third-party influencers should be cultivated in advance as they can help spread that message.

A key element in winning the battle in traditional media is educating critical reporters. Usually only top-tier financial outlets will have dedicated reporters on this beat, so education will play a major role.

Digital media must also not be overlooked. Infographics, messaging and videos should all be considered in order to tell the most compelling story, in multiple ways. Tools such as pixel tracking, issues and keyword targeting, and digital advertising will help identify and reach key targets.

**4 Prepare a strong turnaround narrative with a compelling vision for the future:** In a bankruptcy, winning court and stakeholder support for a turnaround plan is a requirement for emerging from Chapter 11. Those who can articulate a plan best despite the uncertainty will have an upper hand.

The highest cash bid may not win approval. The bankruptcy court approves the rules for the auction of assets, and the debtor can exercise its business judgment to determine the best bid, subject to court approval. In some cases, the debtor and the bankruptcy judge might accept a lower bid if it is more likely to allow the business of the debtor to continue in some form, thereby better protecting all the involved parties, including suppliers, employees, and the communities where the assets are located.

For all stakeholders, delivering a clear narrative that addresses public interests will be more important now than ever. ♦

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