THE A&M DISTRESS ALERT

Pressures on performance and balance sheets deepen corporate distress across Europe

July 2024

ALVAREZ & MARSAL
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01 INTRODUCTION

The last year and recent months have not brought European companies the relief that many had hoped. With the expected rate-cutting cycle proceeding at a historically low pace and the “last mile” of inflation proving tricky to tame, the same operational and liquidity challenges that plagued businesses in the aftermath of the pandemic increasingly appear today.

A&M’s latest Distress Alert reveals how this weakened momentum is spelling trouble for firms in Europe and the Middle East. It shows that balance sheet issues are now affecting nearly a third of businesses in the region and that the share of those struggling with performance has increased over the past year. Overall, distress levels have risen to the highest since the peak of the pandemic, with 9.2% of firms in our analysis, equivalent to nearly 800 companies, facing financial distress.

Chart 1

	FY20	FY21	FY22	FY23
Distressed companies	11%	9.1%	8.3%	9.2%
Companies lacking robustness	29%	28.7%	29.1%	31.2%
Companies lacking performace	17.4%	14.4%	12.4%	13.5%

The dismal economic outlook has been especially problematic for corporates with overleveraged capital structures. Those firms have been fighting simultaneous headwinds – slowing revenues, inflation and higher cost bases, secular shifts in consumer behaviour, net-zero regulation, and geopolitical risks and uncertainties – all while managing excessive debt burdens amid reduced investor appetite for risk. Deleveraging has been difficult because credit conditions remain tight, meaning cash levels are dropping as businesses dip into their savings to cover their interest payments.

Business models are vulnerable

In this tough environment, firms with business models that are no longer competitive or future-proof are particularly vulnerable to distress. Take the case of consumer businesses, which need to urgently realign their strategy and transform operating models to deal with the shift to e-commerce and rising demand for cheaper and sustainable products.

Similarly, the energy transition is pushing chemical firms to rethink the way they operate, from the sourcing of raw materials to the diversification of product portfolios. The most recent ADA highlights the scale of the challenge facing these sectors, with firms in the Fashion sector and Chemical sub-sectors among the most distressed.

The great unwinding of corporate leverage is currently underway, with defaults in Europe at their highest year-to-date levels since 2008, according to S&P Global Ratings[1]. Notably, there has been an uptick in the number of distressed exchanges in the region, with over a quarter involving repeat defaulters (issuers with at least one previous default). The rise in repeat defaults shows that corporates have become accustomed to operating with high levels of leverage in their capital structures.

We anticipate that the surge in distress and restructuring activity, including waiver requests and “amend and extend” transactions, is set to continue in the coming months, particularly as refinancing dates come closer. According to S&P Global Ratings data, $763.2 billion in corporate debt across Europe is expected to mature until end of 2024, with the figure rising to over $961 billion in 2025[2].

At the same time, we view this turbulent period as an opportunity for companies to pursue simultaneous enhancements in balance sheets and operational efficiency, to strengthen themselves for the long-term.

In this report, we explore the key findings of our latest analysis and discuss how the current economic outlook is likely to shape corporates’ financial health in 2024 and beyond.

1 https://www.spglobal.com/ratings/en/research/articles/240612-default-transition-and-recovery-an-increase-in-distressed-exchanges-drives-defaults-in-europe-13145301
2 https://www.spglobal.com/ratings/en/research/articles/240205-credit-trends-global-refinancing-maturity-wall-looms-higher-for-speculative-grade-debt-12991317

02 EXECUTIVE SUMMARY

The key findings of our most recent analysis include:

Distress is growing in most countries and sectors

Levels of financial distress have risen to the highest since the pandemic, with 9.2% of companies in the ADA dataset (which includes over 8,200 firms) facing distress by lacking both operating performance and balance sheet robustness. This equates to nearly 800 businesses, representing a 10% increase compared to the previous year. Notably, the deterioration of corporate financial health has been felt across the board as 10 out of 16 sectors, and five out of nine key countries/regions, saw distress levels increase in the past year.

Balance sheets fragile as companies struggle to deleverage

Since 2020, the share of businesses lacking balance sheet robustness has steadily increased, reaching a record 31.2%, which represents over 2,500 corporates. This trend highlights how companies' ability to generate cash and profits to service their debt is being eroded due to lower revenue generation and increased expenses in the new norm of higher rates and slower growth. With interest rates expected to come down slowly, we anticipate a further increase in distress as cash flow pressures continue and maturities come due in the coming quarters and years.

U.K., Germany and the Benelux are the most distressed markets

Benelux is the most distressed market covered in the ADA, with 10.2% of companies in distress in 2023. This is followed closely by the U.K., where corporate distress has increased significantly to 9.9% of companies from 8.4% a year earlier, the biggest year-on-year rise among all countries. Distress in Germany has reached 9.4%, the highest share since the pandemic and is also affecting more companies in France than the prior year, reaching 8.5%.

Fashion and Media & Entertainment are the most distressed sectors

Fashion Retail emerged as the most distressed sector, with the highest year-on-year increase in distress levels among all sectors. The corporate health of Media & Entertainment companies has worsened further from the previous ADA, making it the second worst industry, followed by Chemical & Others[3]. In addition, Construction has also seen a significant rise in distress levels compared to the previous comparable period.

Higher-for-longer and elections complicate outlook for borrowers

A slower pace of interest-rate reductions, heightened uncertainty with several major upcoming elections and stubbornly high inflation suggest that financing conditions will remain tight for corporates through the second half of the year and into 2025. The pressure will be higher for lower-rated companies with debt maturing in the next six to 12 months, as they struggle to access the credit market to meaningfully push out their maturity walls. We anticipate this will result in increased restructuring activity in the latter part of the year.

3 Chemical & Others include the following sub-sectors: Chemicals and Chemical Preparations, Diversified Chemicals, Fertilizers and Agricultural Chemicals, Industrial Gases, Specialty Chemicals, Commercial Printing, Paper Products, Metal and Glass Containers and Paper Packaging.

*The dataset for Spain is considered to be too small to be a true representation.

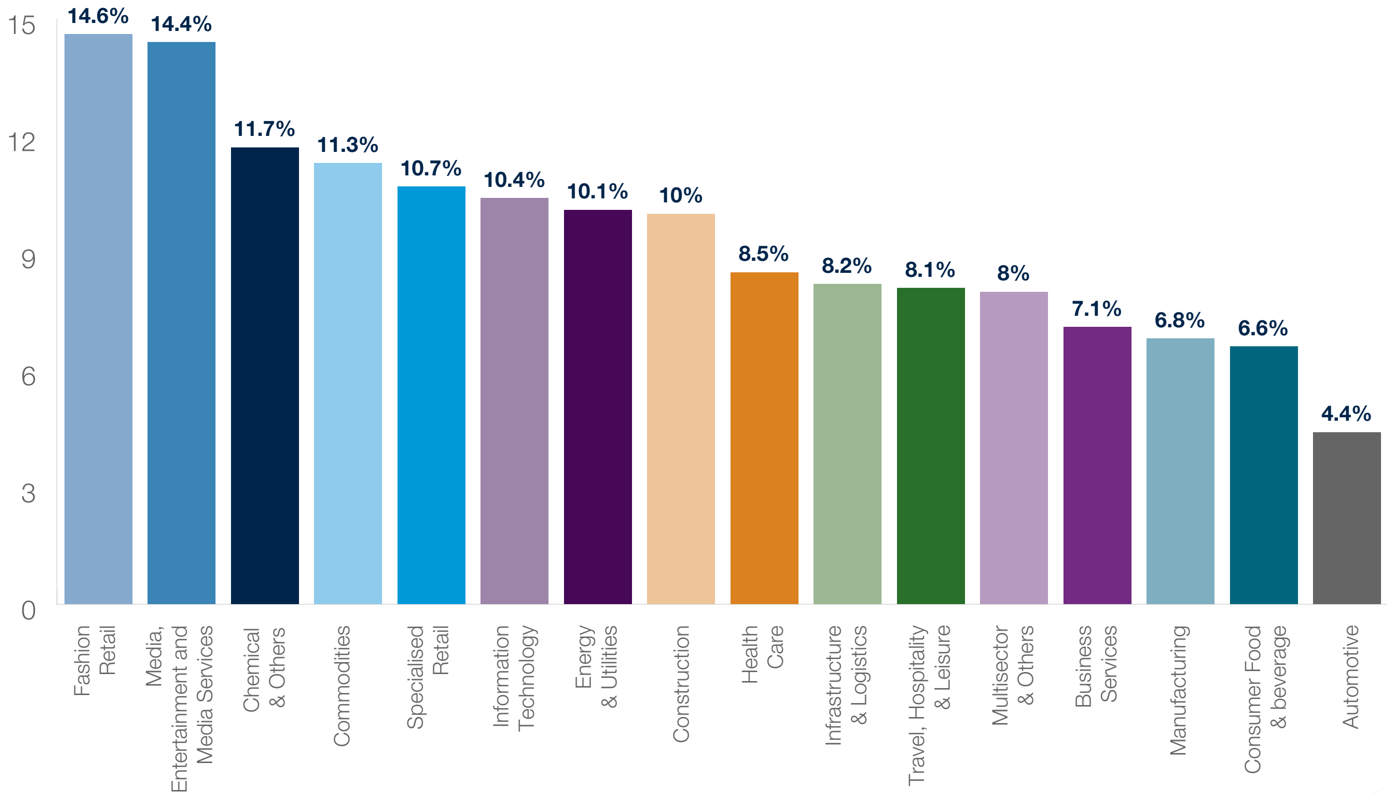
03 SECTOR TRENDS

Corporate distress has increased in 10 out of 16 industry groups covered in the ADA. Two sectors showed stable, albeit elevated, levels of distress compared to the year 2022, while four industries saw a decrease.

In the latest data, Fashion Retail emerged as the most distressed sector, followed by Media & Entertainment Services, Chemical & Others, Commodities and Specialised Retail[4].

Companies in Construction and Business Services in 2023 have experienced a significant rise in levels of distress versus 2022. We discuss the main sector findings in more detail in the following pages.

Chart 3



4 Specialised Retail includes Computer and Electronics Retail, Consumer Electronics, Drug Retail, Home Furnishings, Home Improvement Retail, Household Appliances, among other sub-sectors.

FASHION RETAIL

- Nearly 15% of Fashion Retail companies in our dataset are in distress, compared to 9.6% a year earlier. This is by far the biggest year-on-year rise across all sectors measured by the ADA.
- Fashion businesses have experienced a significant deterioration in both performance and balance sheets, with nearly 20% of them lacking performance and 31.3% lacking robustness.
- Firms' top-line growth has been under pressure due to restrained consumer spending and changing buying behaviour, including the persistent shift to online shopping and the preference for more affordable and/or sustainable products.
- Additionally, the sector struggles with a relatively high-cost base (e.g., personnel, marketing, rents) and the need to make significant investments to operate more efficiently (e.g., renewal of IT systems) in a fiercely competitive environment. These challenges are exacerbated by the lingering effects of recent supply chain crises.
- In the U.K., several retailers have buckled under these market pressures, with insolvencies surging among both brick-and-mortar and e-commerce players in the past two years.

Key findings

	Apparel Retail	Apparel, Accessories and Luxury Goods	Textiles
Worst sectors	19.3%	12.4%	3.1%

	Apparel, Accessories and Luxury Goods	Apparel Retail	Textiles
Worst trend sectors	6.7pp	4.2pp	3.1pp

	FY20	FY21	FY22	FY23
Distress in %	15.8%	17.5%	9.6%	14.6%

	FY20	FY21	FY22	FY23
Lacking performance in %	23.8%	25.4%	13.8%	18.8%

	FY20	FY21	FY22	FY23
Lacking robustness in %	28.8%	30.4%	26.3%	31.3%

MEDIA & ENTERTAINMENT SERVICES

- Distress levels for Media & Entertainment Services firms, which were already high in our previous ADA, have worsened further in the most recent data, reaching 14.4% of all companies in our dataset.
- Firms in the sector continue to struggle with the reduction in consumer spending on discretionary media. The multi-month writers' strike in the U.S. has disrupted film and TV production, putting additional strain on businesses.
- In addition, companies in adjacent sub-sectors including Marketing & Advertising face intensifying secular pressures such as the softening of advertising spending on legacy media. This has been worsened as corporates cut off on advertising spend in a less favourable economic environment.
- Around 38% of companies in the industry lack balance sheet robustness, one of the highest levels among sectors in the ADA, reflecting higher interest burdens faced by leveraged corporates. Such strains are likely to lead to more distress and stress going forward given the likely higher-for-longer interest rates scenario.
- The sector leads European defaults in the first five months of 2024, according to S&P Global Ratings, with 19 defaults versus 13 in the same period last year, including several distressed exchanges[5].

Key findings

	Movies and Entertainment	**Alternative Carriers**	**Broadcasting**	
Worst sectors	24.4%	22.2%	20.8%	
	Broadcasting	**Interactive Home Entertainment**	**Alternative Carriers**	
Worst trend sectors	16.7pp	12.9 pp	7.4 pp	
	FY20	**FY21**	**FY22**	**FY23**
Distress in %	14.6%	11.6%	12.1%	14.4%
	FY20	**FY21**	**FY22**	**FY23**
Lacking performance in %	24.7%	15.2%	17.9%	20.5%
	FY20	**FY21**	**FY22**	**FY23**
Lacking robustness in %	33.3%	34.8%	35.1%	38.1%

5 https://www.spglobal.com/ratings/en/research/articles/240612-default-transition-and-recovery-an-increase-in-distressed-exchanges-drives-defaults-in-europe-13145301

CHEMICAL & OTHERS

- With 11.7% of companies now in distress, the segment comprised mainly of Chemical firms has seen distress levels increase more than 40% between 2021 and 2023.
- Our analysis shows that a quarter of companies in this group are lacking performance, and around 40% lack balance sheet robustness.
- The European chemical industry is experiencing a particularly tough period, with a perfect storm of challenges including sagging demand, sustainability pressures, a sharp rise in energy costs and the lack of competitiveness against other regions (China in particular).
- Faced with depressed earnings and burdened by increasingly expensive debt incurred during the era of ultra-low interest rates, companies are struggling to see through the crisis. Many are turning to shareholders for fresh capital or asking lenders to agree to amend and extend loans to avoid restructurings.

Key findings

	Fertilizers and Agricultural Chemicals	Diversified Chemicals	Commercial Printing
Worst sectors	35.3%	16.7%	11.8%

	Fertilizers and Agricultural Chemicals	Diversified Chemicals	Specialty Chemicals
Worst trend sectors	23.5pp	8.3pp	1.5pp

	FY20	FY21	FY22	FY23
Distress in %	6.8%	8.3%	11.2%	11.7%

	FY20	FY21	FY22	FY23
Lacking performance in %	13.7%	12.7%	13.2%	16.6%

	FY20	FY21	FY22	FY23
Lacking robustness in %	22%	21.5%	24.4%	27.3%

CONSTRUCTION

- Distress levels among Construction businesses rose from 6.7% in 2022 to 10%, the second biggest year-on-year increase among sectors (after Fashion Retail).
- The sector, which includes firms in Building Products, Construction and Engineering, Construction Materials and Homebuilding, has suffered from a severe hit to demand due to higher interest rates, alongside rising input costs and labour disruptions. These woes have made it difficult for corporates to service or refinance debt, tipping many into distressed territory.
- The proportion of Construction companies in distress has risen markedly in the Benelux countries, Germany, Switzerland and the U.K., driving the overall increase in distress.

Key findings

	Construction and Engineering	Building Products	Homebuilding	
Worst sectors	11.2%	10%	8.5%	
	Building Products	**Construction and Engineering**	**Construction Materials**	
Worst trend sectors	6.7pp	4.3pp	0pp	
	FY20	**FY21**	**FY22**	**FY23**
Distress in %	8.7%	6.3%	6.7%	10%
	FY20	**FY21**	**FY22**	**FY23**
Lacking performance in %	19.1%	13.4%	12.1%	14.3%
	FY20	**FY21**	**FY22**	**FY23**
Lacking robustness in %	19.6%	19.3%	21.8%	24.2%

04 COUNTRY TRENDS

Benelux, the U.K. and Germany are the most distressed markets covered in the ADA, in descending order. The U.K. has seen the biggest increase in corporate distress, with nearly one in ten U.K. companies in our dataset showing signs of distress, compared to 8.4% a year earlier.

BENELUX

- With one in then corporates now in distress, the Benelux region is the most distressed market covered in the ADA. Benelux also has the highest proportion of firms lacking balance sheet robustness across the countries measured, of nearly 35%, from around 32% a year before.
- Balance sheets of Benelux corporates were adversely impacted by the lingering effects of high inflation and supply chain disruptions of 2022, as companies sold their expensive inventories at lower prices last year. Additionally, firms' finances were strained by rising debt servicing costs and the first repayments of Covid-related tax referrals.
- Our analysis shows that 38.5% of the Fashion Retail companies in Benelux are in distress, the highest percentage across the sectors measured. The industry is grappling with several challenges, including thinning margins due to higher operating costs, lower discretionary spend and changing consumer habits (e.g. shift to online channels and preference for affordable and sustainable products). Many businesses are also burdened by a high-cost base and require significant investments to operate more efficiency and remain competitive.
- Other sectors of elevated distress include Automotive, driven by difficulties faced by car dealerships due to lower consumer confidence and limited supply, and the IT sector.

Key findings

	Fashion Retail	Automotive	Information Technology	
Worst sectors*	38.5%	18.2%	15.8%	

	Fashion Retail	Construction	Automotive	
Worst trend sectors**	23.1pp	14.3pp	9.1pp	

	FY20	FY21	FY22	FY23
Distress in %	6.2%	10.4%	9.6%	10.2%
Lacking performance in %	16.6%	18.5%	13.8%	13.4%
Lacking robustness in %	18.1%	29.6%	32.6%	34.7%

* Sectors with the highest share of companies in distress.
** Sectors with the biggest increase in share of companies in distress.

FRANCE

- Distress levels increased for French companies this year, at 8.5% from 7.7% in the year earlier period. France also had among the highest proportion of companies lacking robustness, at 31%.
- Sector-wise, healthcare companies were the worst hit in France, with 15.3% in distress. Significant increases in the cost base (salaries, rent and energy) and a decrease in coverage by public health insurance have left their mark on the sector. Moreover, highly leveraged care-home and testing businesses – some of them with LBOs structured before interest-rate increases – have seen adverse conditions.
- Our data shows the biggest increase in distress was in Business Services (8.1%), followed by Commodities and Media & Entertainment Services.
- We also observe that higher interest rates and inflation are having a deep impact on Construction and Real Estate sectors.

Key findings

	Health Care	**Commodities**	**Media & Entertainment Services**	
Worst sectors	15.3%	12.5%	12.2%	
	Business Services	**Commodities**	**Media & Entertainment Services**	
Worst trend sectors	8.1pp	7.5pp	7.3pp	
	FY20	**FY21**	**FY22**	**FY23**
Distress in %	12.9%	11.6%	7.7%	8.5%
	FY20	**FY21**	**FY22**	**FY23**
Lacking performance in %	17.3%	16%	10.3%	10.2%
	FY20	**FY21**	**FY22**	**FY23**
Lacking robustness in %	33.2%	29.9%	29.5%	31%

GERMANY

- Corporate distress has increased steadily in Germany and reached the highest level since the start of the pandemic. Companies facing distress currently account for 9.4% of the German firms in our dataset.
- The number of firms lacking performance and balance sheet robustness has also grown in recent years, now accounting to 15.7% and 27.8% of total businesses, respectively.
- German companies in the Infrastructure & Logistics and the Energy & Utilities industries show the highest distress levels among sectors covered in the ADA. Both markets are undergoing structural changes driven by the energy transition, including the need to decarbonise supply chains and invest in renewable energy sources.
- The Logistics industry in particular has long suffered from a shortage of skilled workers, a challenge that has been exacerbated more recently due to a persistently tight labour market in Europe.
- Alongside strong increases in construction costs and skilled labour shortages, Construction companies have been hit particularly hard by higher interest rates, which resulted in a steep slump in buyer demand. The downturn meant many highly levered firms have struggle to refinance or access bank financing at all, further compounding their financial woes.
- Anecdotally, we observe the Automotive, Retail and Chemical sectors as facing several major challenges that can lead to more distress activity.

Key findings

	Infrastructure & Logistics	**Energy & Utilities**	**Consumer - Food and Beverage**	
Worst sectors	22.2%	18.8%	15.8%	
	Consumer - Food and Beverage	**Construction**	**Energy & Utilities**	
Worst trend sectors	15.8pp	8.3pp	6.3pp	
	FY21	**FY21**	**FY22**	**FY23**
Distress in %	12.9%	8.6%	8.6%	9.4%
	FY21	**FY21**	**FY22**	**FY23**
Lacking performance in %	21.8%	16.2%	14.2%	15.7%
	FY21	**FY21**	**FY22**	**FY23**
Lacking robustness in %	28.4%	26.1%	26.3%	27.8%

ITALY

- Overall, Italian companies showed a small improvement – 6.6% were in distress in our current analysis, down from 7.1% a year earlier. While a smaller proportion of companies were lacking in performance from a year earlier, lack of robustness increased to 30.6%.
- Companies are seeing the impact from the end of Covid-era state financial support to individuals, which is hitting consumer-facing sectors particularly hard. Simultaneously, businesses are now facing the repayment of their own Covid loans and the withdrawal of state financial aid such as SACE and Medio CreditoCentrale.
- Commodities was the most distressed sector in the latest data, at 15.9%, followed by Media & Entertainment at 14.3%. Business Services and Fashion Retail were among areas with worsening trends.
- In addition, we have observed growing signals of distress in the Automotive sector in Italy, with several original equipment manufacturers (OEM) in a stressed or distressed situation due to the turmoil in OEM strategies that is affecting suppliers' business models.

Key findings

	Commodities	Media & Entertainment	Services	Multisector and Others
Worst sectors	15.9%	14.3%		10.2%

	Multisector and Others	Business Services	Fashion Retail
Worst trend sectors	8.5pp	3.3pp	2.6pp

	FY20	FY21	FY22	FY23
Distress in %	8.8%	7.1%	7.1%	6.6%
Lacking performance in %	17.2%	11.7%	11.8%	11.4%
Lacking robustness in %	28.1%	29.6%	28.9%	30.6%

MIDDLE EAST

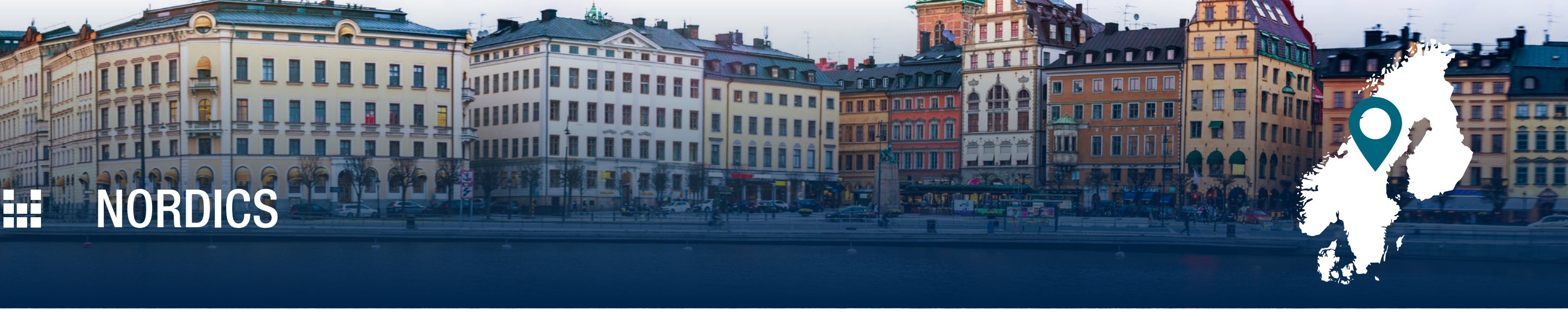
- Although corporate distress has stabilised in the two Middle East countries included in our analysis (Saudi Arabia and United Arab Emirates), the latest data indicates an increase in the number of companies lacking performance in those markets.
- This reflects an environment of weakened consumer demand both regionally and in the region's key export markets, coupled with persistent inflation and supply chain disruptions that are increasing input costs and compressing margins.
- Not only has Ebitda generation significantly deteriorated, but businesses are also being challenged by highly leveraged balance sheets that were built during a period of zero interest rates and strong market performance. The ADA shows that more than a quarter of companies lack balance sheet robustness. As a result, many are squeezing working capital balances to manage cash flows and meet large debt burdens.
- The impact of higher inflation on asset collateral's valuations has largely delayed the need for restructurings. However, as inflationary pressure eases and interest rates decline at a slow pace, more restructuring activity is expected across the region.

Key findings

	Chemical & Others	Commodities	Specialised Retail
Worst sectors	30%	20%	14.3%

	Chemical & Others	Consumer - Food and Beverage	Specialised Retail
Worst trend sectors	20pp	11.8pp	7.1pp

	FY20	FY21	FY22	FY23
Distress in %	15.8%	9.9%	8.9%	8.9%
Lacking performance in %	21.2%	15.3%	11.3%	11.8%
Lacking robustness in %	36%	26.6%	26.6%	26.1%



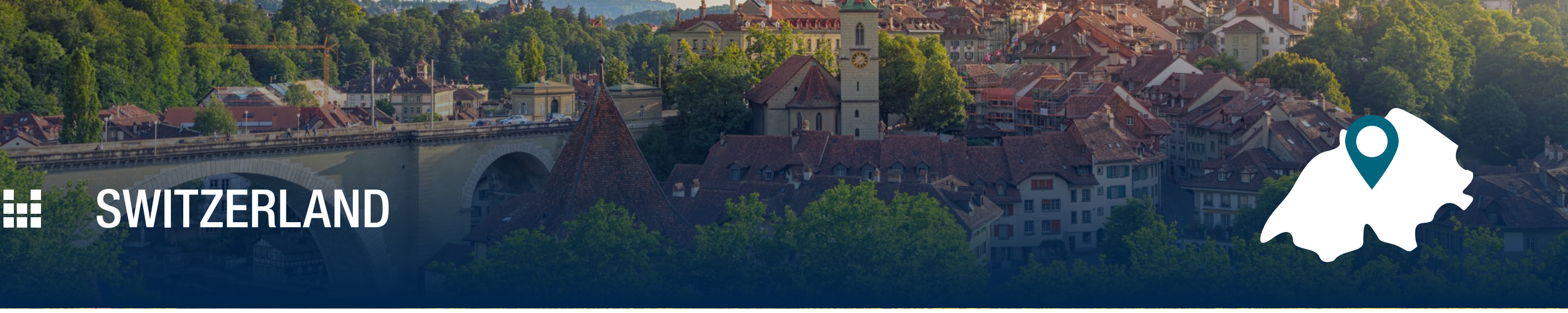
NORDICS

- In the Nordics, 9.2% of companies were in distress, down from 9.8% the year before. However, nearly one in three companies were lacking robustness, indicating a challenging environment overall.
- Outside the hard-hit real estate industry (not included in our analysis[6]), our data showed the highest levels of distress in Infrastructure and Logistics, Multisector and Consumer Fashion industries. The Automotive and IT sectors showed the biggest increase in distress year-on-year.
- The spread of distress across multiple industries with no clear trend is consistent with our experience on the ground, reflecting the broader challenges of persistent inflationary pressures and higher interest rates. In the first months of 2024, this has translated into weakened consumer demand, reduced Capex spending and investment appetite.
- Whilst there are no signs yet of a sharp increase in the volume of distressed transactions, restructuring activity levels across the Nordics have intensified and large corporates have defaulted.

Key findings

	Infrastructure & Logistics	Multisector and Others	Fashion Retail	
Worst sectors	12.5%	12.3%	12%	
	Automotive	**Information Technology**	**Multisector and Others**	
Worst trend sectors	5.3pp	4.8pp	4.6pp	
	FY20	**FY21**	**FY22**	**FY23**
Distress in %	8.8%	7.5%	9.8%	9.2%
	FY20	**FY21**	**FY22**	**FY23**
Lacking performance in %	13.3%	10.3%	13.6%	14.6%
	FY20	**FY21**	**FY22**	**FY23**
Lacking robustness in %	24.4%	26.4%	29.7%	31.5%

6 The Real Estate sector, comprised of REITs, Real Estate Development and Real Estate Services companies, among others, has not been included in our analysis because most of its KPIs are not comparable with those of the industries covered in the report.



SWITZERLAND

- Overall, corporate distress levels in Switzerland improved to 5.2% in 2023, from 6.1% a year earlier, reflecting the country's moderate economic recovery.
- Yet, roughly one in ten Swiss companies were lacking in performance, and balance sheets have weakened year-on-year, with 24.1% of firms lacking robustness.
- The underperformance of hospitals and challenges related to their financing have weighed on Healthcare. In 2023, 10.3% of such businesses were in distress, the highest percentage across sectors. High inflation and energy costs have had a strong adverse impact on hospitals, with increased costs of personnel and goods contributing to performance issues, alongside increasing health insurance premia.
- Our data also showed a worsening trend for Construction companies, where demand has been hit by the impact of higher rates. Highly leveraged companies in the sector are being increasingly pushed into distressed situations as they struggle to manage their debt in a higher-for-longer rates environment.
- Another industry showing elevated levels of distress is Chemical & Others, at 6.3%, underscoring structural challenges such as higher energy prices, the growing Chinese competition and the need to decarbonise operations.
- Throughout 2024, we observe that the deferred adverse effects of the pandemic, compounded with the rise in interest rates since 2022, are finally hitting businesses' earnings and balance sheets, leading to increased levels of restructuring activity.
- The recent decline in interest rates and the stabilisation of inflation (though still at historically high levels) is creating favourable conditions for high refinancing volumes going forward.

Key findings

	Health Care	Construction	Chemical & Others	
Worst sectors	10.3%	8.3%	6.3%	
	Construction	**Health Care**		
Worst trend sectors	8.3pp	6.9pp		
	FY20	**FY21**	**FY22**	**FY23**
Distress in %	13.2%	5.7%	6.1%	5.2%
	FY20	**FY21**	**FY22**	**FY23**
Lacking performance in %	24.1%	9%	11.3%	9.9%
	FY20	**FY21**	**FY22**	**FY23**
Lacking robustness in %	26.4%	25%	23.6%	24.1%

U.K.

- The U.K. has seen corporate distress increase significantly year-on-year, with 9.9% of total companies in our dataset now in distress, compared to 8.4% a year earlier. This is the biggest year-on-year increase across countries in the ADA.
- The uptick aligns with the stagnant economic conditions of recent years. After a technical recession in 2023, growth has so far remained sluggish. The OECD expects the U.K. to experience GDP growth below that of other G7 nations this year.
- The most distressed sector in the U.K., Media & Entertainment Services, continues to struggle with the reduction in disposable income that is forcing consumers to reassess subscriptions like streaming services. The multi-month writers' strike in the U.S. has disrupted film and TV production, putting additional strain on these businesses.
- Additionally, the adjacent media marketing & advertising sector is experiencing stress as corporates, much like consumers, reduce discretionary spend to mitigate top-line deterioration.
- Pressures on disposable income are also driving the continuing downward trend in the clothing retail market. According to the latest data, Fashion Retail businesses are the second most distressed in the U.K. With a 14.4 percentage points increase year-on-year, 21% of firms in this industry are now in distress. Corporate failures continue to mount across the sector, including of online-only retailers.
- The Construction sector has seen the third biggest increase in distress levels, as it struggles with a depressed housing market and increased input costs that companies are unable to pass through.

Key findings

	Media & Entertainment Services	Fashion Retail	Energy & Utilities
Worst sectors	21.6%	21.1%	13.6%

	Fashion Retail	Media & Entertainment Services	Construction
Worst trend sectors	14.4pp	7.9pp	4.2pp

	FY20	FY21	FY22	FY23
Distress in %	11.2%	10.1%	8.4%	9.9%

	FY20	FY21	FY22	FY23
Lacking performance in %	17.9%	16.8%	13.1%	15.1%

	FY20	FY21	FY22	FY23
Lacking robustness in %	27%	27.9%	27.7%	30.2%

05 CONCLUSION

A&M's latest ADA indicates that economic pressures and the prolonged higher-interest-rate environment are pushing a rising number of companies across Europe into distress.

This is evident in the uptick in restructuring activity observed in the market this year, that includes both formal insolvency processes and other transactions designed to give borrowers breathing room such as "amend and extend" and waiver consents.

Companies looking to protect earnings and balance sheets against these market challenges must act proactively. Some of the key preventive measures for management, boards and financial stakeholders include:

For companies facing imminent distress, their chances of a successful restructuring can significantly increase by focusing on the following areas:

Business model review

Transparency regarding profitable and cash burning areas, clients and products, along with robust business planning grounded in realistic analyses will help business leaders understand the impact of market conditions and changes in customer behaviour so they can implement the necessary counter measures early enough.

Liquidity assessment

Critical review of short-term cash flow forecasting and cash management tools to obtain a robust platform for restructuring remain top priorities when situations become challenging or resolution uncertainty rises.

Plan for volatility

Permanent screening of macroeconomic drivers, peer behaviour analysis and scenario planning should be conducted in a three-way financial planning model. Relying on business-as-usual practices is no longer enough given the several operational and financial headwinds facing companies.

Robust three-way financial planning

The development of a robust, integrated financial plan which combines the business plan and the impact from restructuring measures is vital to evaluate the feasibility of a restructuring against different scenarios.

06 HOW A&M CAN HELP

A&M has the most comprehensive suite of services to help companies and their stakeholders through challenging times.

Our multi-function, European-wide Restructuring team brings decades of experience of working on the world's largest and most complex transactions and gaining consensus amongst multifaceted stakeholder groups to deliver outstanding outcomes against difficult backdrops.

These core restructuring services are supported by complementary skills that can address every aspect of complex transactions from within one team. Our deep strategic, operational and financial expertise, valuations and tax advice combined with cutting-edge contingency planning and bias-to-action culture ensure we can get a transaction done in any circumstances.

07 METHODOLOGY

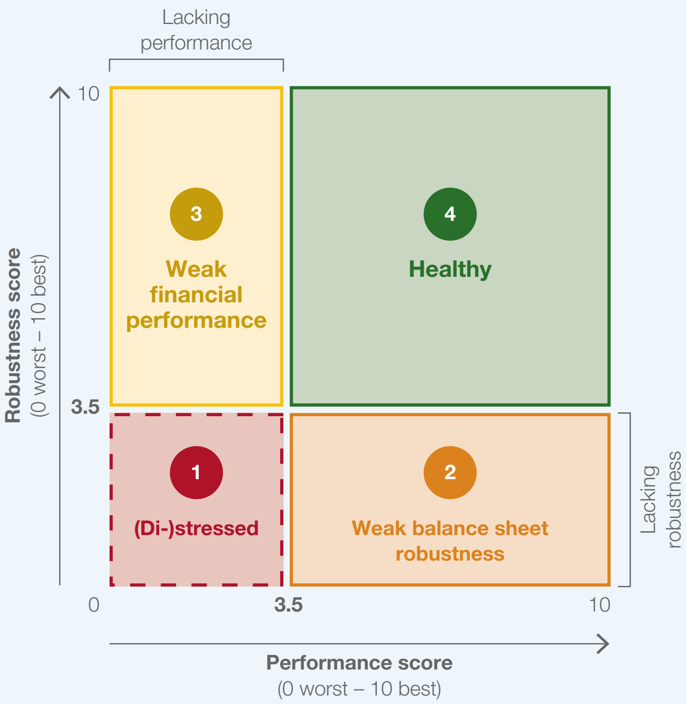
A&M's Financial Restructuring Advisory team has developed a methodology to assess performance and balance sheet robustness of European businesses, aiming to identify those that are in financial distress or may soon be heading in that direction.

The study includes more than 8,200 listed and private companies, each with annual revenues exceeding €20 million, across 33 countries in Europe and the Middle East. These companies consistently provided data for all years from 2019 to 2023.

The ADA index analyses 18 KPIs to create two sub-scores: the performance score, which is based on the company's own income statement as well as related KPIs measured against its industry peers, and the robustness score, based on detailed balance sheet data.

The scores are applied on a scale from zero (heavily impacted) to 10 (very solid situation). Based on the scoring, companies are clustered into four groups: businesses that are in or on the verge of financial distress because they have significant deficits in both their financial and earnings situations (cluster 1), those with weak balance sheets (cluster 2), those with weak performance (cluster 3) and finally, firms considered to be in a healthy financial position (cluster 4).

Index-based clustering



Explanation ADA and recommended actions

Cluster 1/ (Di)stressed: companies have (significant) deficits in terms of both their financial and earnings situation. These therefore have ***insufficient liquidity and/ or inadequate and unsustainable capital structures*** and, at the same time, ***weak/insufficient profitability***. Some of these companies are therefore likely to be in "financial (di)stress".

Cluster 2/ Weak balance sheet robustness: companies with a robust earnings/profit performance but insufficient liquidity and/or inadequate and unsustainable capital structures. These companies are in a potential ***need of a financial restructuring***.

Cluster 3/ Weak financial performance: companies have a fundamentally solid balance sheet but show weaknesses in their earnings or profitability. These companies are in a potential ***need of performance improvement measures***.

Cluster 4/ Healthy: includes companies that have a solid balance sheet and robust earnings.

The ADA series focuses on the percentage of companies in the distress cluster (cluster 1) within a sector/ country

08 CONTACTS

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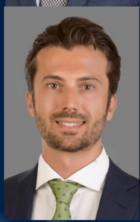

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Companies, investors and government entities around the world turn to Alvarez & Marsal (A&M) for leadership, action and results. Privately held since its founding in 1983, A&M is a leading global professional services firm that provides advisory, business performance improvement and turnaround management services. When conventional approaches are not enough to create transformation and drive change, clients seek our deep expertise and ability to deliver practical solutions to their unique problems.

With over 10,000 people providing services across six continents, we deliver tangible results for corporates, boards, private equity firms, law firms and government agencies facing complex challenges. Our senior leaders, and their teams, leverage A&M's restructuring heritage to help companies act decisively, catapult growth and accelerate results. We are experienced operators, world-class consultants, former regulators and industry authorities with a shared commitment to telling clients what's really needed for turning change into a strategic business asset, managing risk and unlocking value at every stage of growth.

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