TAMULawAnswers.info Webinar Series

Panelists:

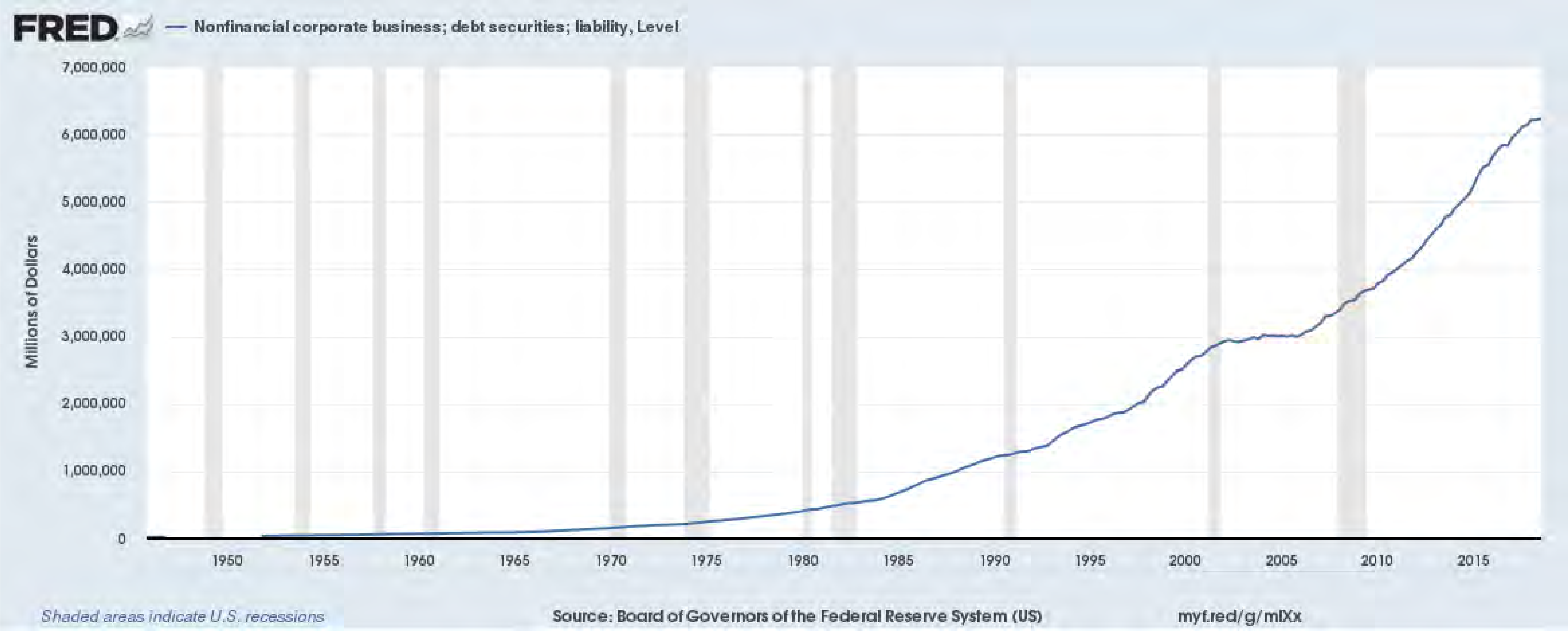
Wayne Barnes, Professor of Law, Texas A&M University School of Law

Steve Montgomery, President, MontgomeryGR

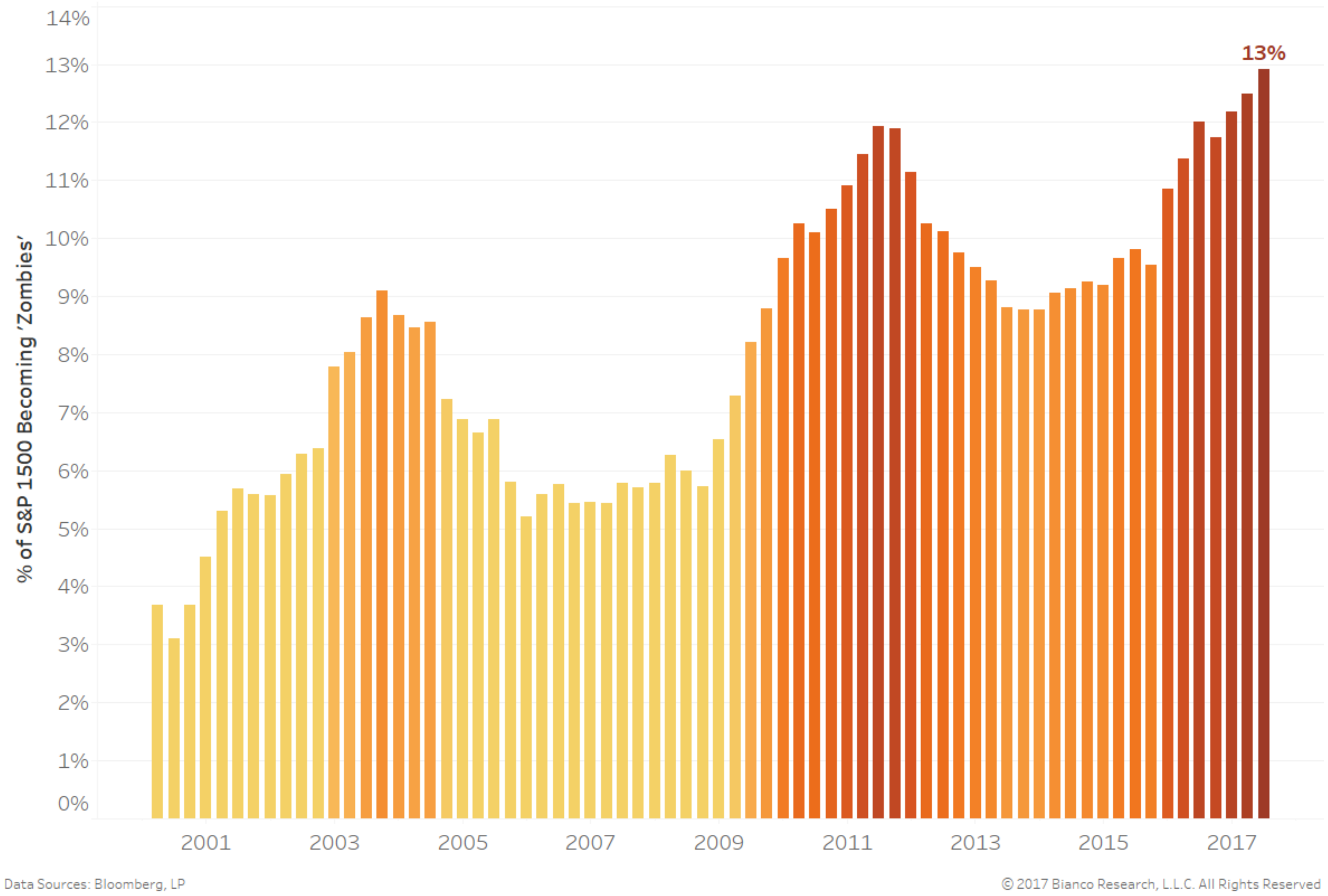
J. Machir Stull, Partner, Cantey Hanger L.L.P.

William Magnuson (moderator), Professor of Law, Texas A&M University School of Law

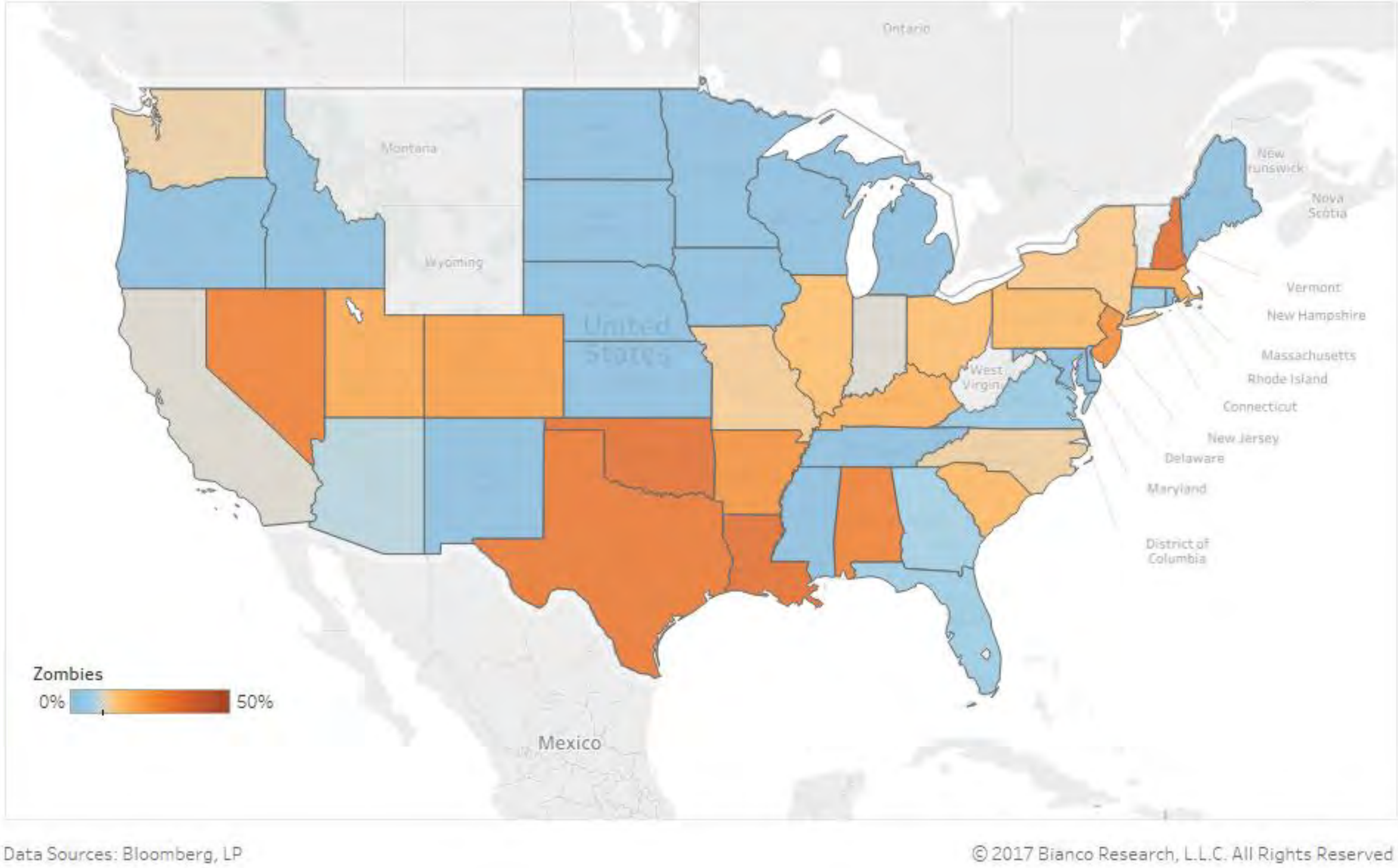
U.S. Corporate Debt = $6.3 trillion



Source: Federal Reserve Bank of St. Louis



Source: Bianco Research, available at: https://www.biancoresearch.com/?p=156962



Source: Bianco Research, available at: https://www.biancoresearch.com/?p=156962

Source: Raul Elizalde, “Investors are the main lenders to U.S. businesses, and they may not understand the risks”, Forbes, June 29, 2018.

"In the US, **22% of nonfinancial corporate debt outstanding comprises 'junk' bonds** from speculative-grade issuers, and **another 40% are rated BBB, just one notch above junk**."

"**Covenant-lite loans**, an issuer-friendly feature that offers less protection for lenders and investors than traditionally structured credits, now account for a record 75% of the roughly $970 billion in outstanding U.S leveraged loans[.]"

"And some of these **loans are packaged and resold as bonds** or as other complicated investments."

Source 1: Susan Lund, "Are we in a corporate debt bubble?", McKinsey Global Institute, June 21 2018.
Source 2: Tim Cross, "Covenant-lite credits continue to dominate U.S. leveraged loan market", Forbes, February 2018.
Source 3: William D. Cohan, "The big, dangerous bubble in corporate debt", The New York Times, August 9, 2018

"To put it simply, the root cause of the **U.S. corporate bond and stock market bubble** is **ultra-low interest rates**. Though interest rates of practically all types have been falling since the early-1980s, the trend has been amplified by the actions of central banks like the Federal Reserve since the Great Recession of 2008 and 2009."

Source: Jesse Colombo, "The U.S. is experiencing a dangerous corporate debt bubble", Forbes, Aug. 29, 2018

Robert Kaplan
President of the Federal Reserve Bank of Dallas
August 2018

“At this juncture, the challenge for the Fed is to **raise the federal funds rate** in a gradual manner calibrated to extend this expansion, but not so gradually as to get behind the curve so that we have to play catch-up and raise rates quickly. Having to raise rates quickly would likely increase the risk of recession.”

Source: Essay by Robert S. Kaplan, “Where we stand: Assessment of economic conditions and implications of monetary policy”, Federal Reserve Bank of Dallas, 2018.

Robert Kaplan (cont.)

"Further, high and rising levels of government debt as well as elevated levels of corporate debt mean that **the U.S. economy is becoming much more interest rate sensitive**. That is, increases in interest rates would likely require a higher proportion of cash flow in order to service corporate and government debt obligations."

Source: Essay by Robert S. Kaplan, "Where we stand: Assessment of economic conditions and implications of monetary policy", Federal Reserve Bank of Dallas, 2018.

Is it a good thing to get rid of zombie firms?

"Zombies are **less productive** and may **crowd out growth** of more productive firms by locking resources (so-called 'congestion effects'). Specifically, they depress the prices of those firms' products, and raise their wages and their funding costs, by competing for resources."

"Too much capital stayed in **bloated and inefficient companies** leaving too little to support the growth of smaller, more dynamic, enterprises. It was, perhaps, a western version of the Japanese 'zombie company' problem."

Source 1: BIS Quarterly Review, "The rise of zombie firms: Causes and consequences", September 2018.
Source 2: Stephen King, Senior Economic Advisor for HSBC, per Bob Bryan, "HSBC: 'Zombie companies' are killing the economy, so we should just let them collapse", Business Insider, March 16, 2016.

Overview of Bankruptcy Relief and Tools Available for Business Debtors

Professor Wayne Barnes

Types of Bankruptcy Cases

- Chapter 7 (straight liquidation)
  - (give up (non-exempt) assets, keep future income (if any))
  - Means test (for individuals) determines if allowed to file Ch. 7 vs. Ch. 13

- Chapter 13 (individual repayment plan)
  - (give up 3 to 5 years of income, keep assets)
  - Individuals/sole proprietorships only (not corporations, LLCs)
  - Regular income required
  - Debt limits (if over, required to file Ch. 11 or Ch. 7):
    - Unsecured - $419,275
    - Secured – $1,257,850

- Chapter 11 (Business Reorganization)
  - “normal” case (expensive, complex, many players have say, time-consuming)
  - Allows many different plans (e.g., selling certain assets/downsizing, debt-to-equity conversion, new investment, orderly liquidation)
  - new “Small Business Debtor Reorganization” subchapter

Overview of Bankruptcy Benefits

- Automatic Stay
  - Temporarily prevents creditors and other parties from taking collection actions once bankruptcy is filed
- Continuation of Ordinary Business Operations
- Debtor-in-Possession Financing
- Assume or Reject Executory Contracts and Leases (reduce footprint)
- Selling assets “free and clear”
- Stripdown of business secured loans (if underwater)
  - And reduced payoff/discharge of underwater “unsecured” portion over time in plan
- Avoidance recoveries to help pay creditors (fraudulent transfers, preferences)
- Collective Remedy
- Discharge of Pre-Bankruptcy Plan Unsecured Debts
  - Except for corporations filing Chapter 7

TEXAS A&M UNIVERSITY
SCHOOL OF LAW

Questions?

Please also see

Tamulawanswers.info

for more info

TEXAS A&M
UNIVERSITY

Strategic Communications

For Distressed Companies

Chapter 11 Filings On the Rise

Monthly Filings[1]

+ 52%

YTD Filings[2]

+27%

[1] *July 2020 over July 2019. Source: American Bankruptcy Institute website*
[2] *First half of 2020 over first half of 2019. Source: Ibid*

Distressed Business Communications Plan

What and Why?

- Complexity, Clarity
- Combating Misinformation
- No Panic Zone
- Minimize, Maximize

Distressed Business Communications Plan

How?

- Tailored, Personal
- Specific
- Clear
- Multi-Channel
- Collaborative
- Timely, Staged

Distressed Business Communications Plan

Who?

- Employees
- Customers
- Vendors/Suppliers
- Investors
- Media
- Others
- Disclaimers

Distressed Business Communications Plan

What Else?

Not Crisis Communications

Rebuild

Steve Montgomery, President
steve@montgomeryGR.com
214.212.0304