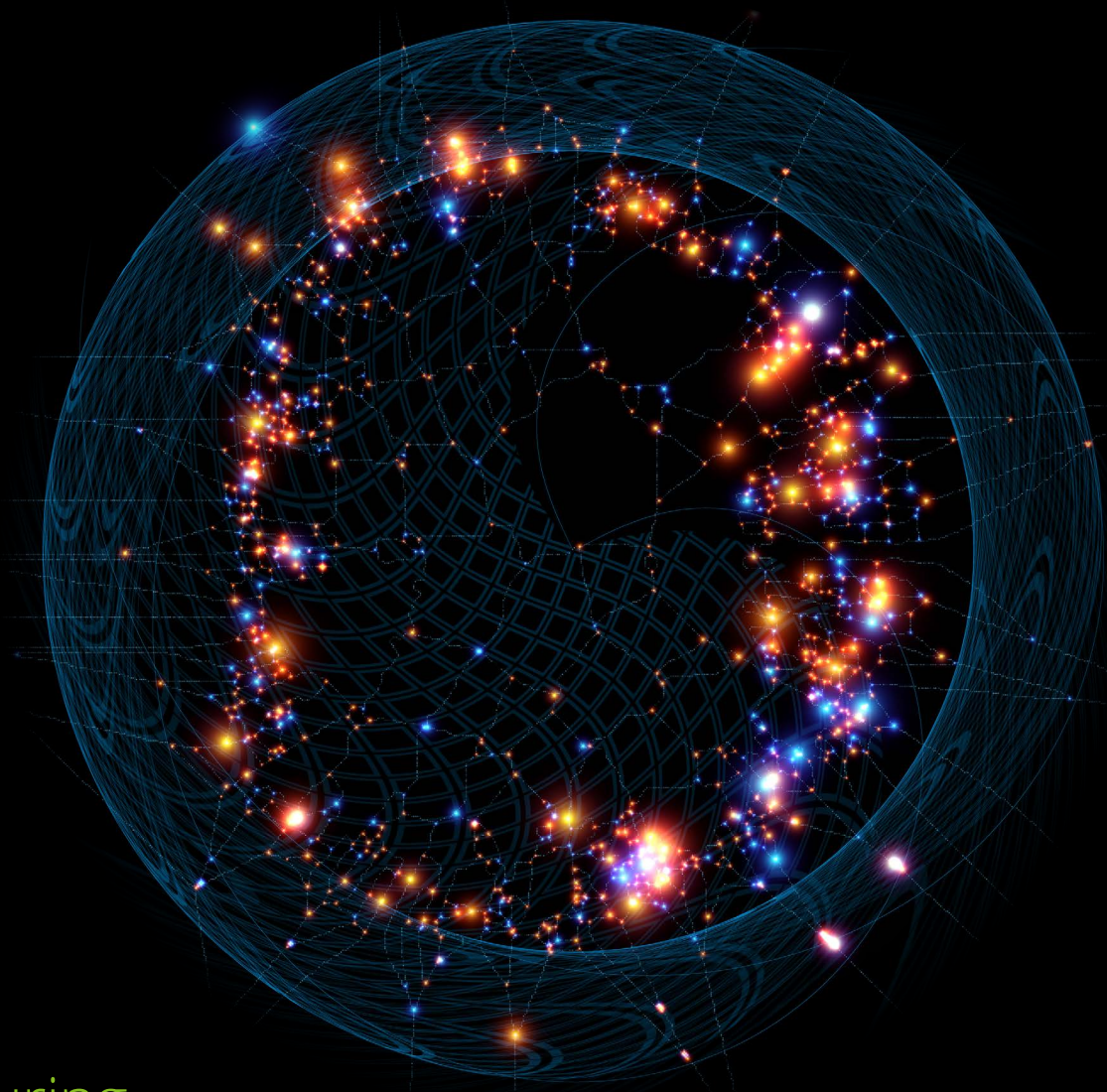
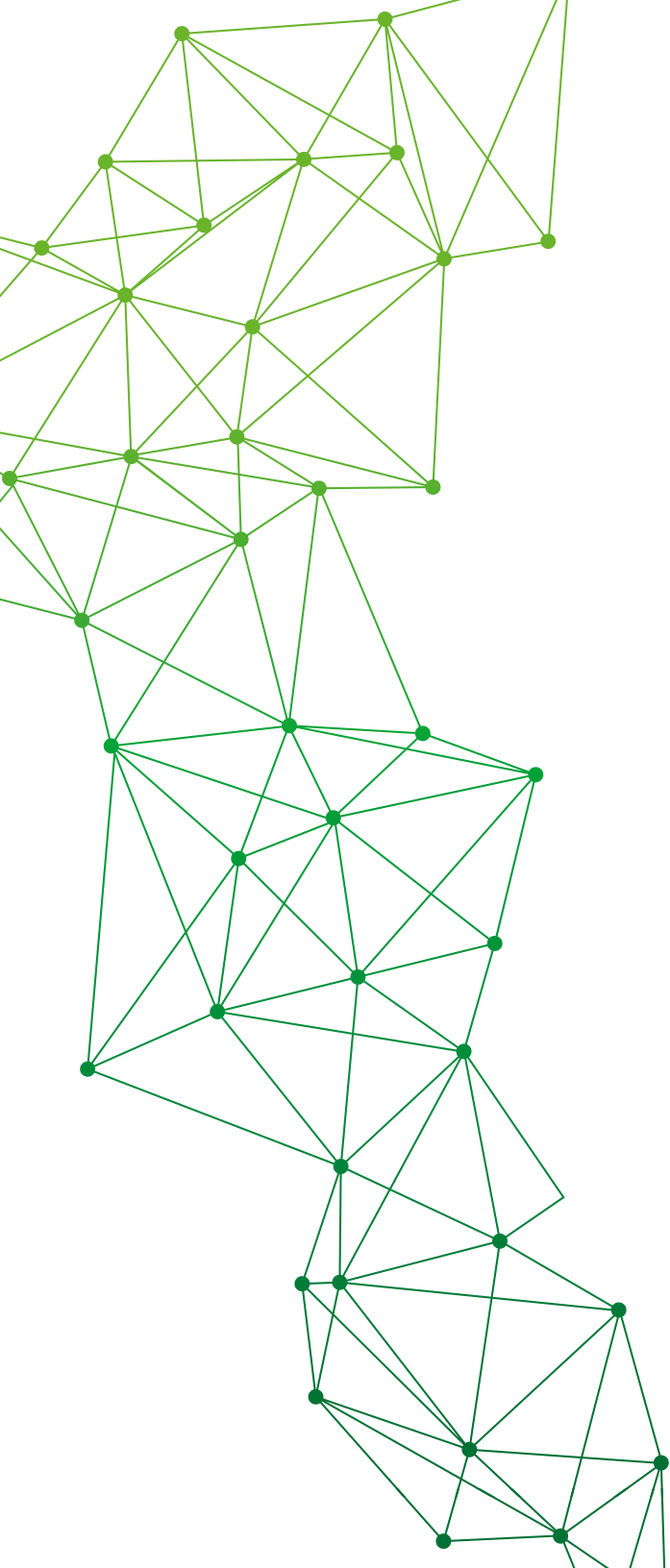


Deloitte.



Seeing restructuring
through a wider lens—and
embracing the opportunities

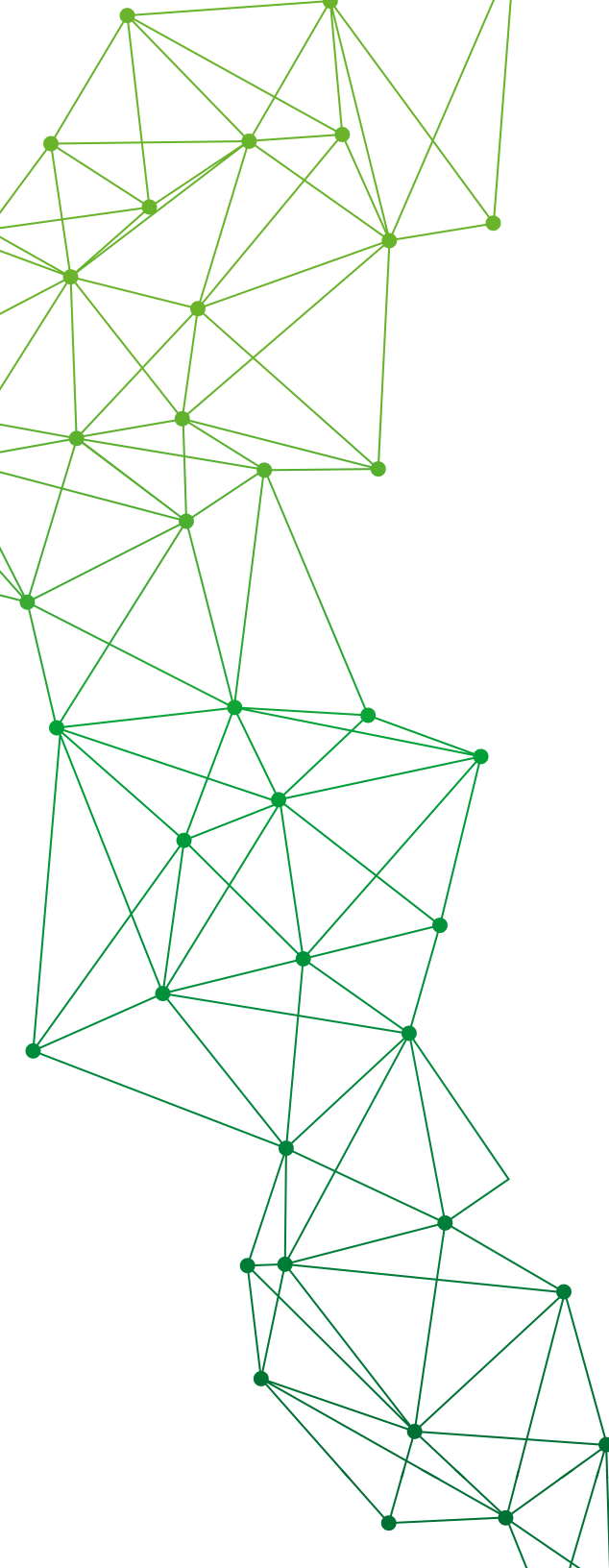


Restructuring is commonly employed to turn around troubled enterprises, but this narrow lens misses a broader opportunity to improve business performance. A holistic restructuring approach deploys levers and tools that have been effectively applied across a spectrum of circumstances to help companies achieve greater profitability and competitive advantage. An organization that's been **disrupted** may still want to refresh, rethink, or redesign itself. A company that finds itself **disadvantaged** in the marketplace might reset, rebalance, or reconfigure its operating model or capital structure. A business that's significantly **distressed** may need to reconnect, reconstruct, or restore its strategy or structure.

Introduction

Businesses now operate in a set of circumstances that has been reshaped by a pandemic. The longest economic expansion in US history ended abruptly in February 2020. Gross domestic product plunged in first part of the year and then rebounded, but the economy remains about 3.5% smaller than it was in 2019. Large US companies are filing for bankruptcy protection at the fastest pace since the end of the Great Recession, and some 60,000 local, small businesses had shuttered permanently as of late July, according to Yelp data.¹ Amid all this economic turmoil, organizations should be prepared to embrace change. Doing nothing is not an option when the business environment, customer behaviors, regulatory factors, and capital markets have all shifted abruptly and dramatically.

For some businesses, the need for change may be painfully obvious. A company's operating model may be deeply damaged or its finances strained; think of an international airline, or a small operator of local gyms, or any number of businesses in between. Such companies may be facing balance-sheet concerns or new liquidity management requirements, or they may be waiting to see how long government pandemic relief measures might last. They may be divesting assets to cut losses from a crippled business line, or they may be raising funds to invest in a new strategy. Some may be in bad enough shape that they must work with creditors or seek court protection to reorganize and shed liabilities. These enterprises are restructuring in the more narrow, traditional sense.



For companies experiencing a milder impact from the pandemic, there still may be a benefit in seeing their future through a restructuring lens. The enterprises most likely to thrive in the next normal that will eventually supplant the coronavirus disruption are those that take deliberate steps to reposition themselves based on their new or shifting circumstances.

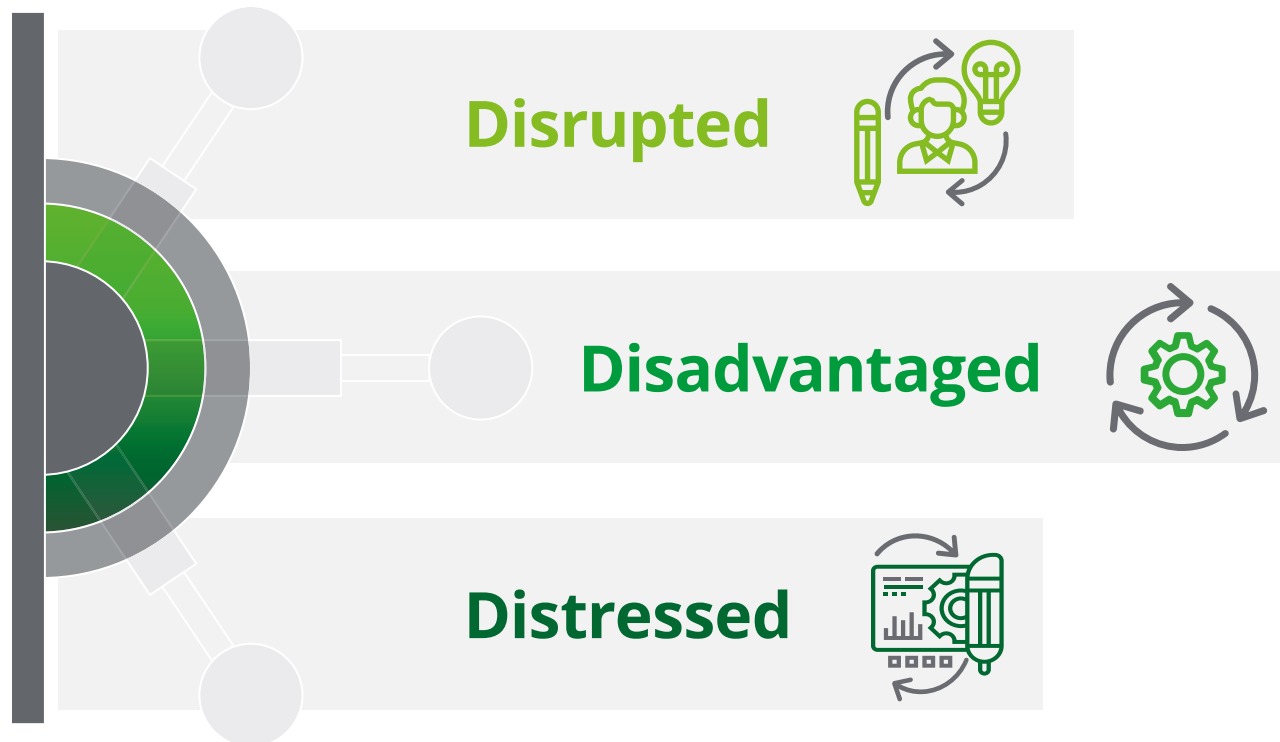
Studies of how companies came out of the last recession support this idea. Businesses that acted to foster brand loyalty, for example, or develop new methods to keep customers engaged as the financial recession ran its course were successful in the next cycle.² Key attributes of the most resilient companies were that they moved quickly to cut expenses and boost cash flow, and they built flexibility into their investment planning and operations.

Restructuring, in the broadest sense of the term, should be on the table for every business to help them pursue the actions that have been shown to be effective in previous cycles. The underlying purpose of restructuring is to ensure that the assets and resources a company deploys are performing to their highest potential—and fully meet return expectations. That’s the goal when a company seeks bankruptcy protection, which can be a valuable tool for making changes that can’t happen otherwise. But it can also be the objective in less distressed situations. Enhancing the performance of assets and resources can be addressed across a spectrum of circumstances.

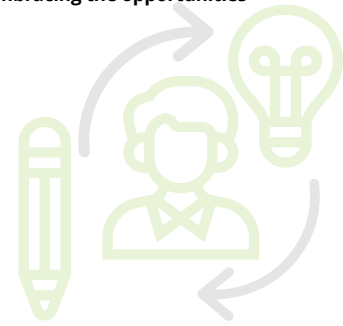
When business leaders bring an expanded focus to the restructuring process, they have a way to organize their thoughts to envision and execute the turnaround or transformation that can most benefit their organization.

Restructuring reconsidered

Deloitte sees restructuring activities grouped into three segments along a continuum. At one end are simpler measures that may be entertained by a company that has been **disrupted**, as indeed most companies are today due to the pandemic. In the middle are more aggressive steps appropriate for a business that has been more deeply **disadvantaged** by its current circumstances. At the far end of the spectrum are measures for a company that's clearly **distressed**, including those in need of the reorganization tools that fit within any narrow definition of restructuring.



In this paper, we will explore each of these three categories in turn. Our goal here is to create a broad, holistic view of the restructuring efforts a business might consider—and to sketch the benefits that may accrue in the form of enhanced returns.



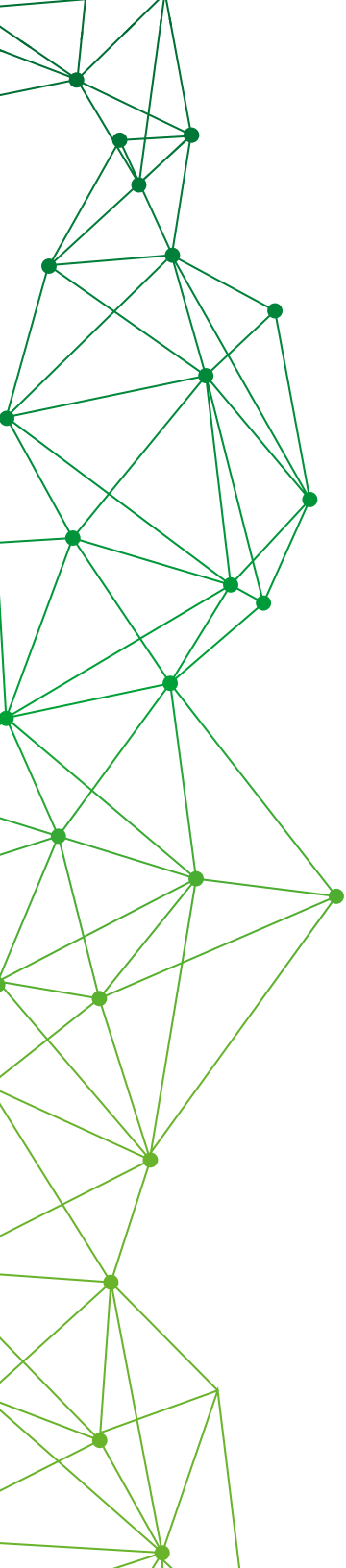
1. Disrupted

Refresh, rethink, redesign



The dramatic changes the pandemic has brought to the business environment should prompt most companies to explore ways to improve their customer strategy and their operational and tax models to get the most effective returns from their resources, assets, and capital in a new environment.

For an organization that's been **disrupted**, whether its due to the pandemic or some other business trend, the impact may be relatively fleeting, and revenue might be starting to recover. In such a situation, a company may want to **refresh** its go-to-market model, brand positioning, or other parts of its strategy. By being willing to **rethink** the business, leadership may find new ways to thrive amid shifts in customer behaviors, supply chain interruptions, or changes in capital requirements or availability. Where impacts are lasting, there may be reasons to **redesign** specific business processes.

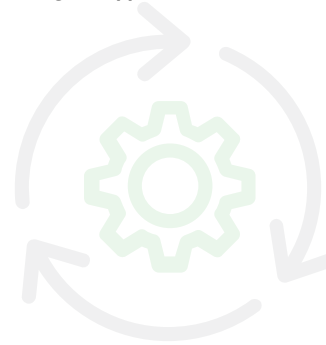


The potential changes a company looks at when facing a disruption may be around optimization of its business portfolio. Consider, for example, a retailer that has primarily been identified as a brick-and-mortar operator but has now seen a shift in the willingness of its customers to order online for delivery or curbside pickup. Embracing the possibility that this shift might be lasting, the retailer may need to **rethink** its supply chain practices, its real estate footprint, or its staffing. It may need to **refresh** its marketing around delivery options or its contracts with delivery services. Those changes, in turn, may create the need for a **redesign** of its organizational structure.

The disruption of the economy has also had a significant effect on working capital requirements for many businesses. If your sales are down, it may be time to **rethink** the variety of merchandise that you stock to avoid having too much cash locked up in inventory that is turning over more slowly. There may also be questions that need to be asked about whether your receivables financing is optimal, for example.

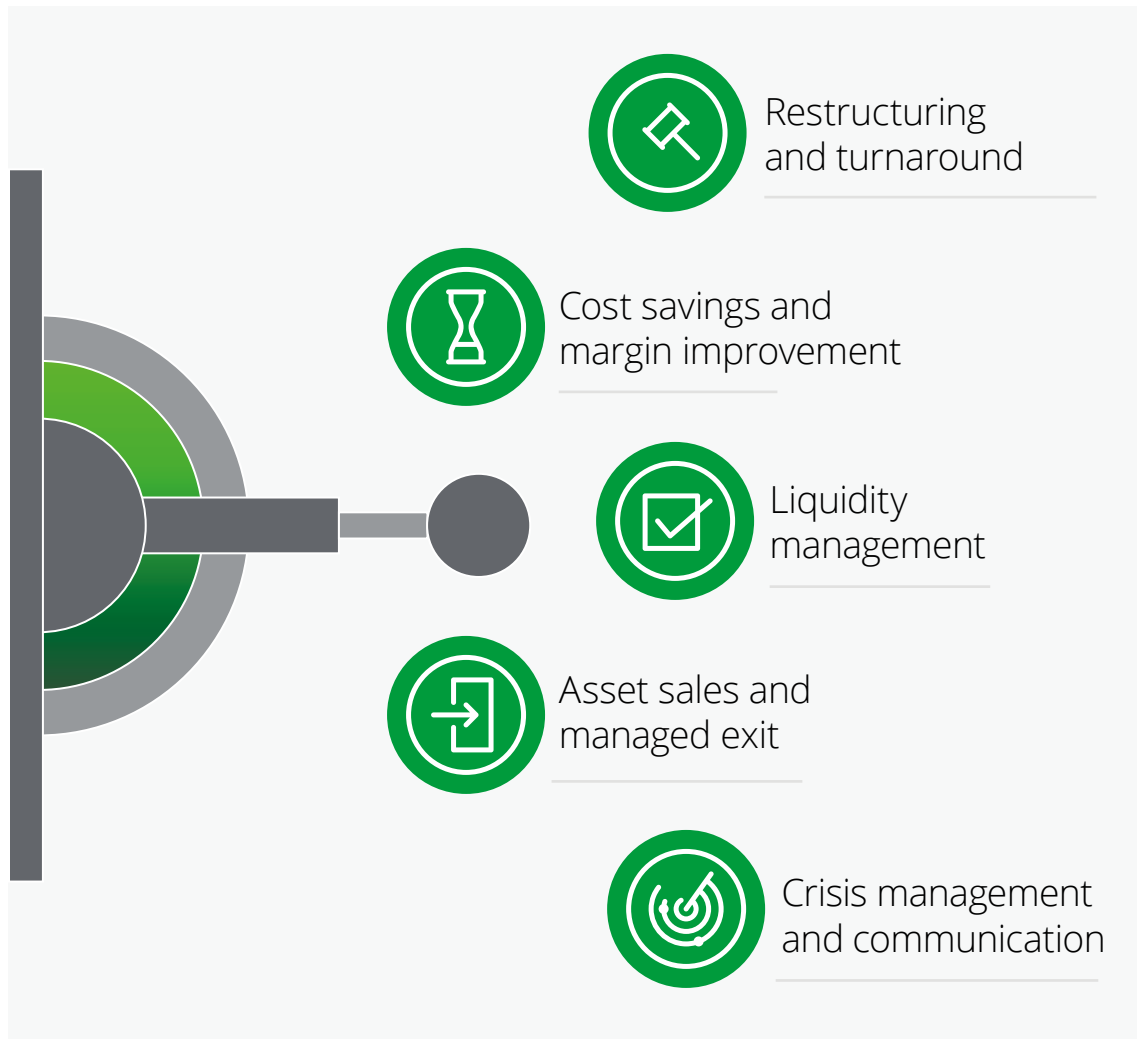
Many businesses have seen changes in how or where their employees do their work, and these changes may require a **rethink**. Here, the example might be a medical practice that has finally seen significant adoption of telemedicine appointments in place of in-office visits. Now it's time to **rethink** what the right mix will be for doctors, nurses, and support staff to allocate their time between working in the office and working from home. It may be time to **redesign** workplace rules and **refresh** recruiting efforts or HR practices.

A number of trends affecting the future of work have clearly been accelerated in the pandemic, and resilient companies should consider using the current disruption to **rethink** and **refresh** their workforce strategies.³ An organization **redesign** may help to seize the opportunity to ensure that there are clear connections across individual jobs, team objectives, and the organization's mission (for example) to strengthen links between belonging and organizational performance.



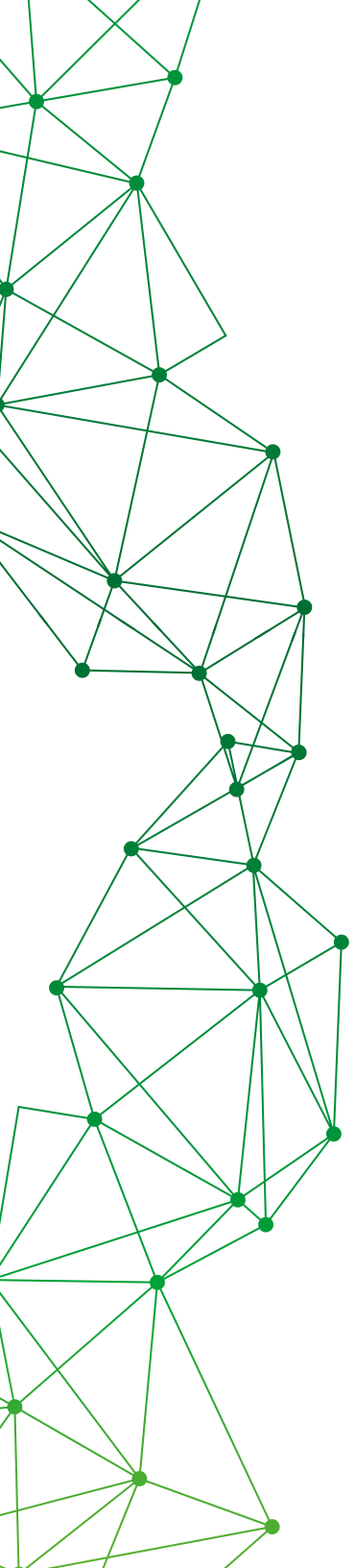
2. Disadvantaged

Reset, rebalance, reconfigure



Where the disruption of a business or an industry has been more lasting or severe, a company may need to embark on more ambitious initiatives or a deeper transformation. The enterprise may not be responding yet to a distress situation, but it may be taking steps to avoid one.

Some businesses may find they have been **disadvantaged** by changes in the operating environment, with their ability to bring products or services to market threatened or interrupted by the pandemic. There may be a need to **reset** relationships, making big changes in the supply chain, for example, or developing new customer marketing efforts. There may be a need to **rebalance** the company's financial and tax condition, strengthening the balance sheet, or making better use of available capital. A company may need to **reconfigure** its workforce, reducing the number of employees or dramatically changing the mix of job titles.



In our disadvantaged grouping, the actions a company might consider include those meant to put the enterprise on a more solid financial footing. If the balance sheet carries debt that could ultimately be difficult to service, the sooner the business takes steps to **reset** or **reconfigure** those obligations, the better. For a hotel operator that is trying to weather the dramatic downturn in travel, for example, it may be time for an equity offering to **reconfigure** the balance sheet. This may be particularly attractive given the strength that's been seen in the stock market relative to the economy overall. The effort to **reset** or **rebalance** the business may even involve the necessity of opening negotiations with creditors.

Another option for a company that needs to shore up its finances is to **reconfigure** the business through a divestiture or, in some cases, a managed exit. By identifying and shedding noncore assets, including units that have been made less competitive or profitable by the pandemic, a company can raise capital to support the heart of its business—or at least to stem the drain on its resources. To return to the retailer example, the effort to **rebalance** and **reconfigure** might involve selling or even winding down a severely impaired unit that has little prospect of returning to profitability to help strengthen other operations.

There may also be opportunities for a company to monetize tax assets that may not have been addressed in the past. When that change buffeting a company is significant enough to prompt divestitures or similar steps, it may also serve as a catalyst that boosts efforts to optimize tax assets or **reconfigure** for greater tax efficiency.

Sometimes, there may be M&A solutions to address supply chain issues that have been created by the pandemic, such as an acquisition of a supplier or a partnership to create better vertical integration. There may also be scenarios in which the effort to **reconfigure** the company involves acquisitions meant to support a **reset** in strategy or an initiative to **rebalance** operations.

The workforce challenges a disadvantaged company may face are bigger than the adjustments highlighted under our first category. If you're an airline or a hotel operator, the size of your workforce may need to be **reset** or **reconfigured** to a sustainable level for a future in which fewer people travel. Here, the organization that **rebalances** quickly and decisively, communicating its actions transparently to all stakeholders, is likely to come out of the current circumstances with improved employee morale and perhaps greater flexibility to thrive in the new business environment.



3. Distressed

Reconnect, reconstruct, restore



Some companies may reach a level of strain that requires difficult issues to be addressed urgently, using the tools and proceedings that fit the narrow, textbook definition of restructuring. Even at this point, though, the focus should remain consistent: This is about finding, preserving, and enhancing the value of the resources and assets of the organization.

Should a company find itself significantly **distressed**, in need of a turnaround, it becomes vital to reconnect with shareholders and debt holders, along with other stakeholders such as employees and, certainly, customers. A company placed in distress due to the pandemic, or because of longer-term trends or missteps, may now have to **reconstruct** itself, and that includes making changes in capital structure. If successful, these steps should lead directly to a longer-term mandate to **restore** faith in the company and its purpose, with customers first and foremost, but ultimately with all stakeholders.



The level of distress that creates an imperative for a company to embrace a full reorganization will likely involve a pressing need to **reconstruct** the capital structure by renegotiating terms with existing debt holders and other creditors. To do this requires a viable plan to **restore** the company to health or viability. The plan has to take into account changes in the current business environment and the capital markets, along with the increased uncertainty the pandemic has created. Any such plan or strategy needs to **reconnect** with the business's customers, or it will not appear to be credible to anyone else, including potential new investors. Selling assets may well be part of the effort to raise capital and **restore** the parts of the business that have the greatest value as a going concern.

In any comprehensive restructuring, there has to be considerable attention given to the identification and preservation of certain valuable tax assets, including net operating taxes. Typically, the transaction structure for an entity emerging from bankruptcy is guided, in part, by the potential tax consequences to the entity

and the various stakeholders. In a court proceeding, there are complex tax rules that need to be considered by the entity to ensure it is restructured to maximize the value of tax assets.

Court protection can help a company to shed obligations that it would be unable to get out of through other methods. A retailer, may be able to reconstruct itself by breaking leases that suddenly are underwater because the pandemic is keeping shoppers out of stores. Bankruptcy proceedings may also help companies to restore themselves to health by getting out of other untenable contracts.

For all of these reasons, bankruptcy protection should not be seen as the endpoint, but rather as an available tool that makes possible to **restore** things in ways that wouldn't be possible any other way. It comes about when a company hasn't been able to achieve what it thought it could and when its options have deteriorated, demanding it **reconstruct** itself and **reconnect** to its purpose.

Conclusion

The tools in the restructuring toolkit can be relevant to an organization that finds itself anywhere along a broad spectrum of circumstances. Common concerns arise: Addressing portfolio imbalances may be key to position a company for the current environment; making certain that the capital structure is fit for the present circumstances can be vital; a careful profitability analysis may be more urgent than ever; taking tax efficiency into account may be necessary; and designing for workforce flexibility may benefit any number of companies, especially given the uncertainty that persists today.

The three categories of restructuring activities presented in this paper are designed to highlight the available tools (and potential benefits) a restructuring mindset can bring. They are intended to show how a disrupted organization may need to rethink or redesign the business model or processes, for example. They are meant to help a company that's disadvantaged in the current environment understand when it might benefit by resetting supply chain or customer relationships.

Understanding the levers that can be applied across the spectrum of situations that may be faced today can help organizations embrace change and find opportunities, whether the disruption is mild or the distress is severe. Seeing circumstances clearly and weighing the available restructuring tools may even help a company to better understand where it lies on this spectrum—and anticipate what comes next.

Endnotes

1. Tayyeba Irum and Chris Hudgins, “U.S. Bankruptcies on Track to Hit 10-Year High as Pandemic Rages On,” S&P Global, August 10, 2020; Madeleine Ngo, “Small Businesses Are Dying by the Thousands—and No One Is Tracking the Carnage,” Bloomberg News, August 11, 2020.
2. Kevin Laczowski and Mihir Mysore, “What Companies Should Do to Prepare for a Recession,” Harvard Business Review, May 2019.
3. Deloitte, “Returning to work in the future of work,” May 2020.

Restructuring Contacts

Kuttayan Annamalai
Deloitte Consulting LLP
kannamalaiei@deloitte.com

Kirk Blair
Deloitte Financial Advisory Services
kiblair@deloitte.com

Elias Tzavelis
Deloitte Tax LLP
etzavelis@deloitte.com



About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee (“DTTL”), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as “Deloitte Global”) does not provide services to clients. In the United States, Deloitte refers to one or more of the US member firms of DTTL, their related entities that operate using the “Deloitte” name in the United States, and their respective affiliates. Certain services may not be available to attest clients under the rules and regulations of public accounting. Please see www.deloitte.com/about to learn more about our global network of member firms.

This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional adviser. Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.