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Preparing for the End of Stimulus

Restructuring Services Insights

Q4-2020

Introduction

As the Covid-19 pandemic spread, governments around Southeast Asia initially focussed on emergency health measures. Financial support for economies, business and employment quickly followed. The financial hangover together with the winding-down of stimulus schemes presents clear challenges. In this edition of Deloitte Restructuring Services Insights we examine the economic impact of Covid-19, government fiscal and legislative responses and the risks to business associated with the end of stimulus.

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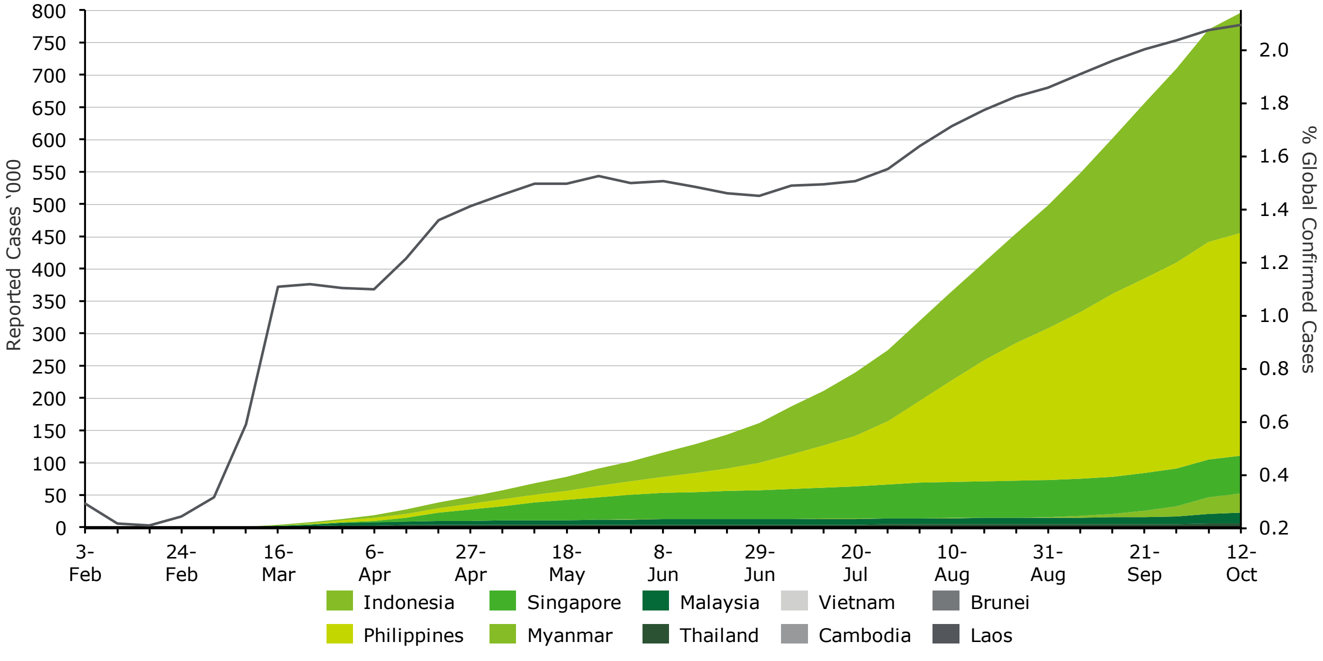
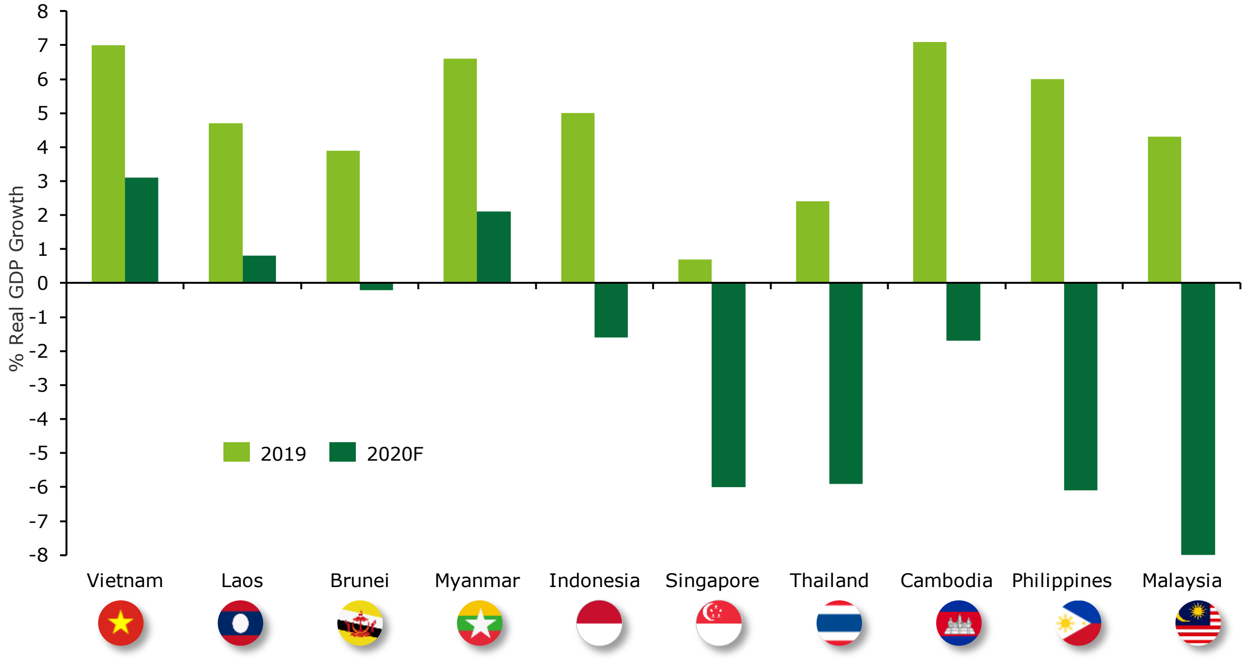
Economic Impact in Southeast Asia

Since June, the Philippines and Indonesia have seen a significant increase in reported Covid-19 cases and now account for ~90% of the reported numbers in Southeast Asia. Unsurprisingly, following the implementation of various control measures across the region, GDP growth is forecast to slow or contract in all countries in Southeast Asia with Malaysia, Singapore, Thailand and the Philippines among the hardest hit.

Cumulative reported COVID-19 Cases in Southeast Asia (as at 12 October 2020)



Southeast Asia GDP Projections



Sources: World Health Organization, EIU, Deloitte Research and Analysis

Industries Under Pressure

Covid-19 is clearly impacting some industries harder than others. The aviation industry has seen unprecedented structural changes to demand, which will persist in the medium term, and the disruption requires businesses in that sector to take rapid steps to reconfigure their operations and balance sheets in order to survive. Others, including many in the hospitality, leisure and retail sectors have taken up support schemes to put-off difficult decisions as long as they can. However, the tapering of these support schemes means businesses will need to act soon.

Sector Impacts + Responses

Automotive

- Automotive dealers are under significant cash flow pressure due to the sharp decline in sales; dealer capacity is too high and **consolidation of dealerships is expected**
- OEMs are hard hit and need to shift to **"resilient supply chains"** (i.e. regional focus on flexibility rather than global supply chain cost optimisation); expect a rise in domestic and near-shore supplier network
- **OEM and supplier concentration expected to shift to the East** with US and EMEA on sell-side

Aviation

- Airlines are expected to **reduce the size of their fleets** as a result of demand sharply declining; reduction in capital expenditure on new aircrafts and renegotiation of leases
- Many national carries have access to cash reserves or will be nationalised; **discount airlines and mid size / regional carriers are hardest hit**
- Privatised airport operations and **ground handling services are facing radical capacity reduction** and financial restructuring and potential wind down

Hospitality

- Halted consumer demand has **forced closure of many hospitality venues** (live sports and large-scale venues hardest hit)
- **Business model changes have been accelerated** in particular for big restaurants chains to address profitability in a social distancing era
- **Digital channels and home delivery** are expected to grow fast
- Many hotel chains are facing liquidity issues due to very low occupancy rates and **further consolidation is expected**

Oil and Gas

- At US$40 per barrel most upstream operators cannot make a profit; national oil companies (including SOEs) have cash reserves but **services / maintenance companies are being hit hard**
- **Downstream companies and related chemical companies** are facing liquidity issues and undertaking financial restructure
- **Workforce instability is a significant issue** as the ability to work remotely is limited on many sites and travel restrictions have greatly impacted the FIFO workforce

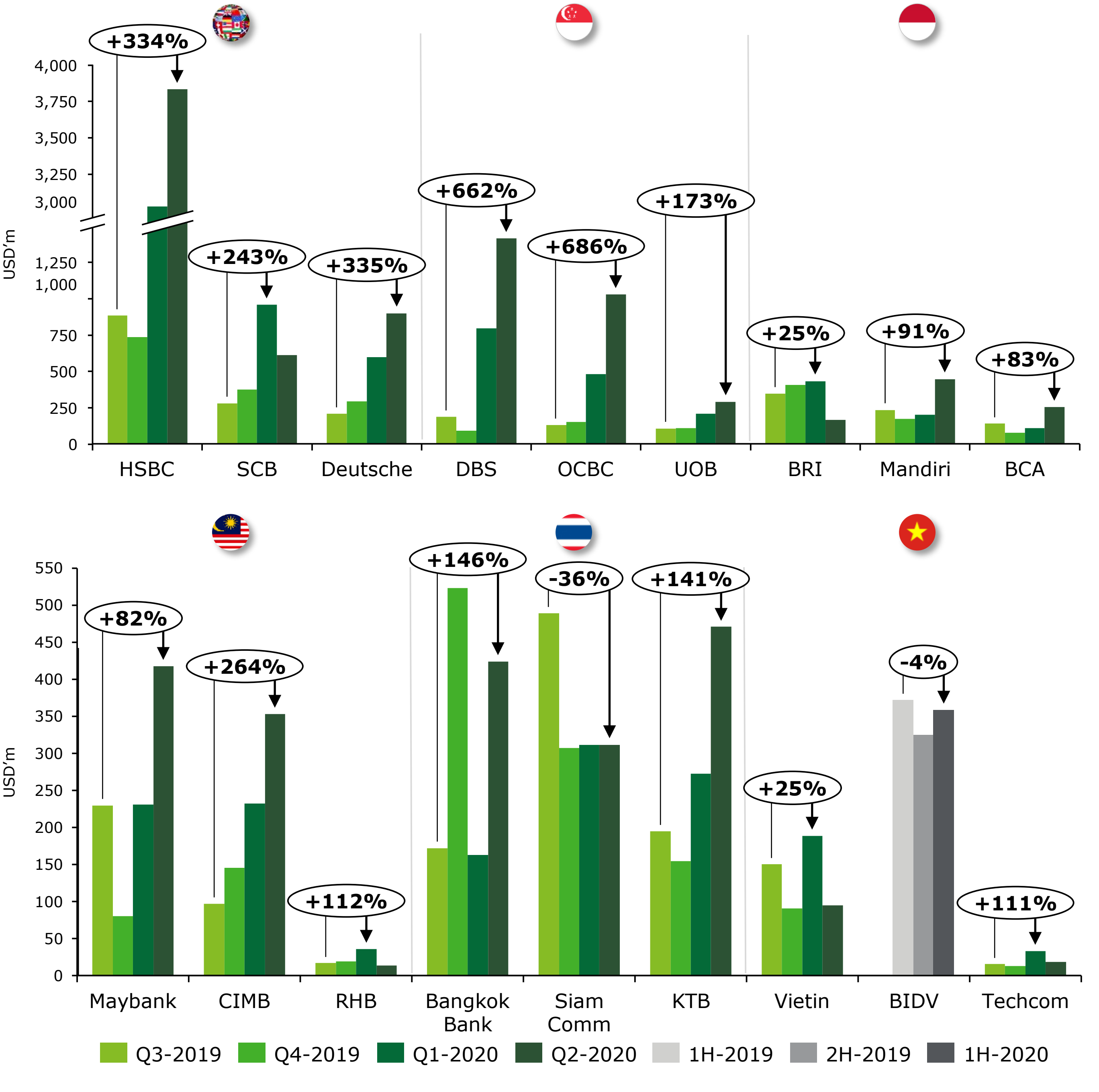
Retail and Wholesale (non-food)

- Physical locations will face a prolonged reduction in footfall, posing **viability issues for companies that can not move to digital channels**
- There has been a significant **acceleration in consumer online sales** with companies rushing to move their offering to digital channels to maintain demand
- More than ever before, customers will expect a **seamless omni-channel experience** with new shopping and delivery options that affect margins

Credit Risk Trajectories

Increasing credit risk and corporate failures in the region have led to a surge in credit loss allowances and impairment provisioning by the major banks. Concentration risk is coming into sharp focus as banks seek to re-balance their portfolios, re-evaluate facility headroom and adjust credit risk tolerances for new lending. International Financial Reporting Standard 9 (IFRS 9) requires a facility level and forward looking view on impairment losses and this is becoming more challenging due to the uncertainty created by the pandemic.

Reported Allowance for Expected Credit Losses

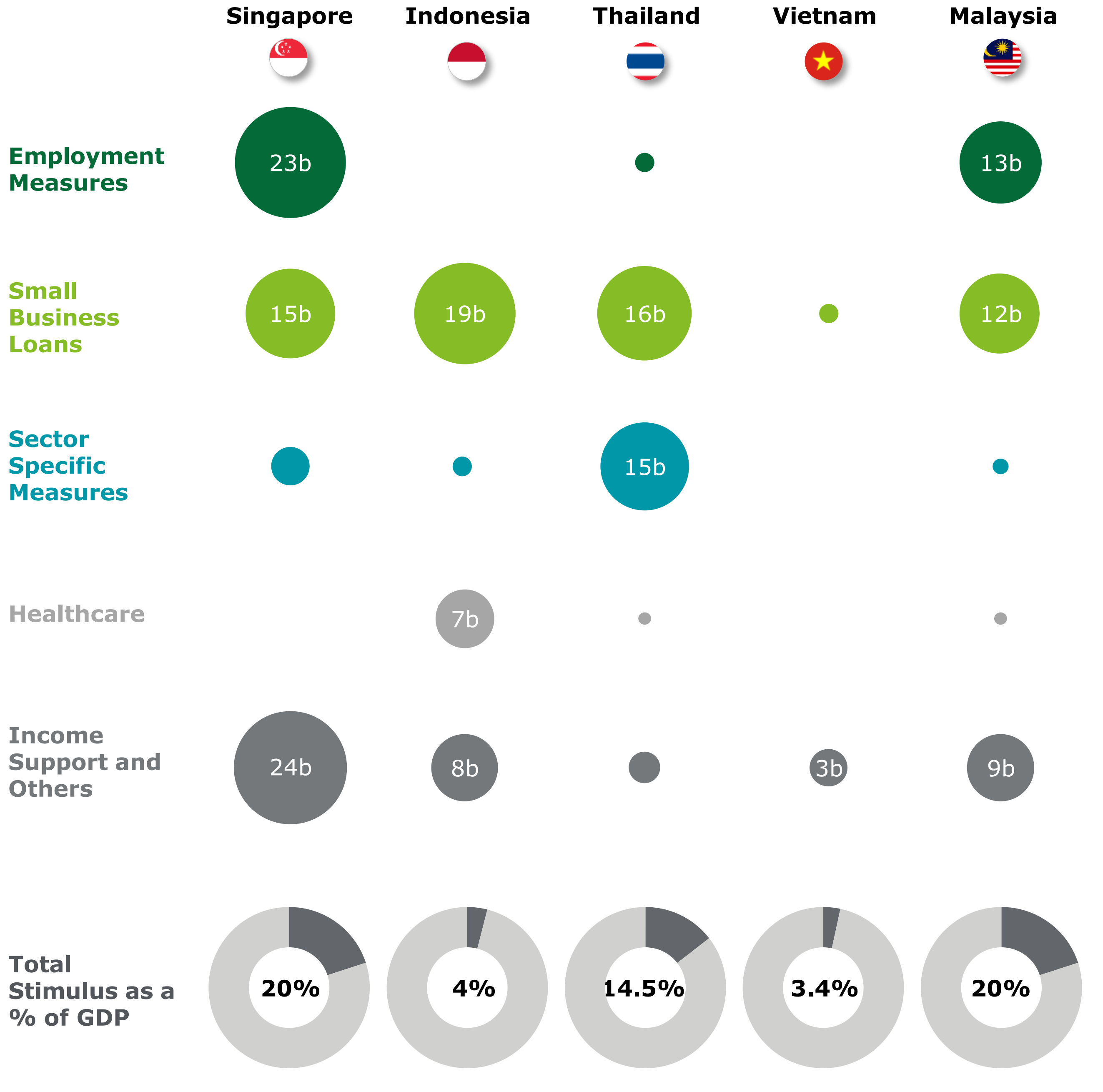


Sources: Bank Financial Statements and Quarterly Reports

Government Fiscal Responses

To mitigate the financial and economic impact of Covid-19, governments across Southeast Asia introduced stimulus packages in the form of employment, business loan, and tax support schemes. A positive fiscal response is certain to cushion the short term economic impact of Covid-19. However interventions that require drawing down on state reserves and / or taking on sovereign debt are not sustainable in the long term and overleveraging by the state in a low cost credit environment may create a drag on future growth.

Reported Budget for Fiscal Stimulus Packages across Southeast Asia



Sources: Singapore Budget 2020, Ministry of Finance Malaysia, Organisation for Economic Co-operation and Development

Approaching the End of Stimulus

Singapore businesses have benefited from various government support schemes rolled out since the pandemic began. However there are serious concerns about the ongoing financial sustainability of many businesses when these programs come to end in December and Q1-2021 (if those measures are not extended). Businesses need to prepare for the end of stimulus by implementing cost and liquidity measures now to position themselves to survive and thrive in a post stimulus, post Covid-19 "new normal".

Current End Dates for Singapore Covid-19 Support Measures

Jul | Aug | Sep | Oct | Nov | Dec | Q1 2021 | Q2 2021

We are here

Employment Measures

Dec:
- End of Foreign Worker Levy (FWL) waiver
- End of Wage Credit Scheme
- End of Job Support Scheme (JSS) for sectors that are managing well

Q1 2021:
- End of JSS

Economic Stimulus

Dec:
- End of deferment of principal payments on secured term loans for SMEs

Q1 2021:
- End of Loan Insurance Scheme
- End of SME Working Capital Loan
- End of Extended Support Scheme – Standardised (ESS-S) for Tier 3A and 3B
- End of SG Together Enhancing Enterprise Resilience (STEER) Programme
- Extension of Temporary Bridging Loan programme to Sep 2021

Q2 2021:
- End of ESS-S for Tier 1 and 2

Sector Specific Measures

Q1 2021:
- End of Enhanced Aviation Support Package
- End of Point-Point Special Relief Fund for Private Hires and Taxis

Jul:
- End of rental waivers for commercial tenants

Aug:
- End of rental waivers for hawkers and markets managed by NEA

Dec:
- End of Additional Deferment of rent under Rental relief framework
- End of Maritime port due concessions for cruise ships and regional ferries
- Extension of 12 months from end of FY2020 to distribute taxable income derived in FY2020 for S-REITS

Tax Support Schemes

Oct:
- End of deferment of corporate income tax payment for 3 months.

Dec:
- Enhanced corporate Income Tax Rebate of 25% of tax payable, capped at S$15,000 for YA 2020
- Option to accelerate capital allowance on plant and machinery in basis period YA2021 over 2 years: 75 % in YA2021 ; 25% in YA 2022

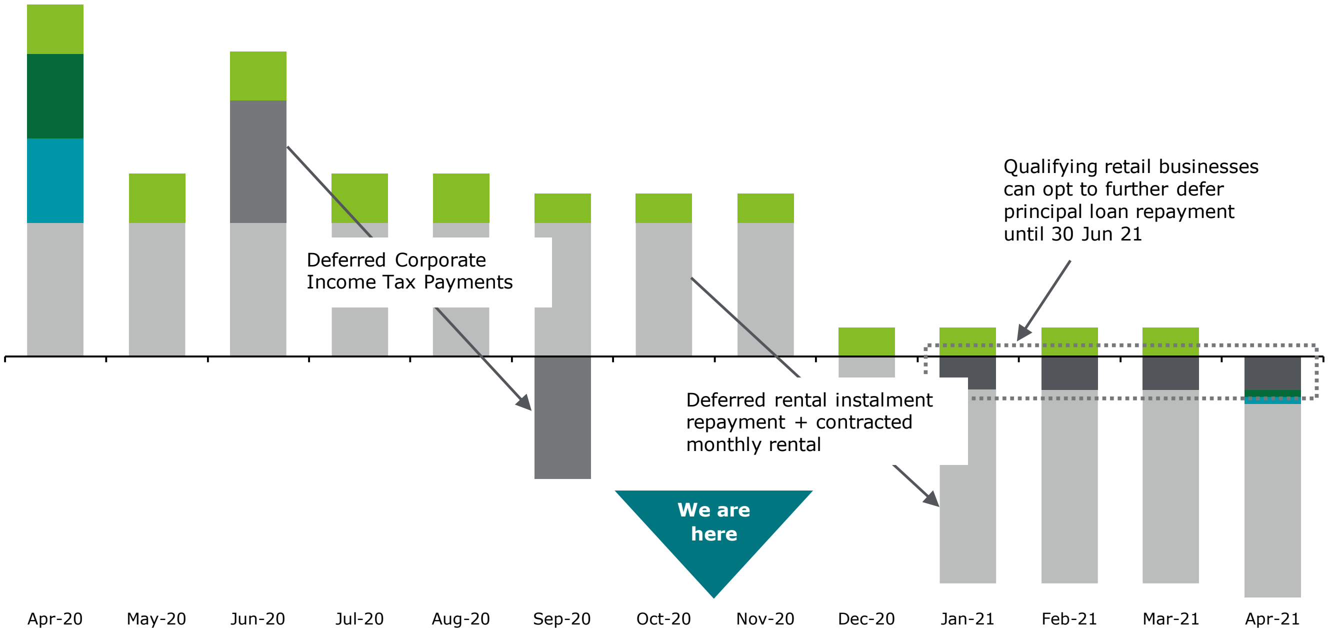
  Option to accelerate capital allowance on renovation and refurbishment in basis period YA2021 in one YA
- Enhanced carry-back relief scheme to carry back qualifying deductions (capped at S$100,000) for up to 3 immediate preceding YAs

Sources: Singapore Budget 2020, Parliament of Singapore, Monetary Authority of Singapore

Illustrative Cash Flow Impact

As fiscal stimulus schemes wind down and deferrals of taxes, rental payments and debt repayments become due, increasing financial stress rates may be expected; particularly businesses facing existing liquidity and leverage pressures. We expect that this will lead to increasing distressed M&A opportunities, debt restructuring as well as cost, headcount and portfolio re-alignment. We examine the illustrative cash flow impact of the support measures on a typical Singapore retail business below.

Illustrative Cash Flow Impact of Covid-19 Assistance for a Singapore Retail Business



Key	Measure	Assumptions
	Job Support Scheme ("JSS")	JSS supplement under the Singapore Budget Stabilisation and Support Package Assumes salary cost ~10.2% of revenue, fully borne by businesses in Apr 21 when JSS ends JSS cash grant up to the first $4,600 gross monthly salary per local employee (retail industry): • 50% cash grant from Apr to Aug 20 • 30% cash grant from Sep 20 to Mar 21 • Monthly payment is illustrative; actual cash reimbursement may differ
	Temporary Bridging Loan Scheme	Assumes Temporary Bridging Loan from Enterprise Singapore taken up in Apr 20: • Assumed loan of 0.5% of annual revenue • Deferment of principal loan for a year, repayment of principal to commence Mar 21 • Interest rate cap at 5% p.a.
	SME Working Capital Loan Scheme	Assumes SME Working Capital Loan from Enterprise Singapore taken up in Apr 20: • Assumed loan of 0.5% of annual revenue • Deferment of principal loan for a year, repayment of principal to commence Mar 21 • Interest rate assessed by Participating Financial Institutions
	Deferment of Corporate Income Tax	Resilience Budget IRAS prescribed tax deferral Assumes final assessment due in June 20: • Deferment of principal loan for 3 months, payable in Sep 20
	Rental Deferral Scheme	Rental relief available for commercial tenants under the Covid-19 Temporary Measures Act Assumes annual rental cost 9.5% of revenue: • Eligible tenants in retail granted a total of four months' rental waiver from Apr to Jul 20 • Additional 4 months deferral of rent under the repayment scheme for rental arrears under the rental relief framework (9 months repayment period, interest at 3% p.a.)
	Deferment of Principal Payments on Secured Term Loans	Assumes business opt to defer principal payments on their secured term loans with bank lenders until end Dec 20. Repayments resume in January 2021.

Sources: Enterprise Singapore, Singapore Budget 2020, Parliament of Singapore, Inland Revenue Authority of Singapore, Monetary Authority of Singapore

Government Legislative Responses

Recognising the risk of a potential increase in corporate stress, governments around the world have responded by reforming and modernising their corporate restructuring and insolvency laws. Singapore, the United Kingdom, Australia and the Netherlands have led the way. The trend for reform globally represents a shift in the balance away from creditors who might typically seek to recover assets against defaulted loans towards favouring debtors typically seeking to restructure and salvage their businesses as going concerns.

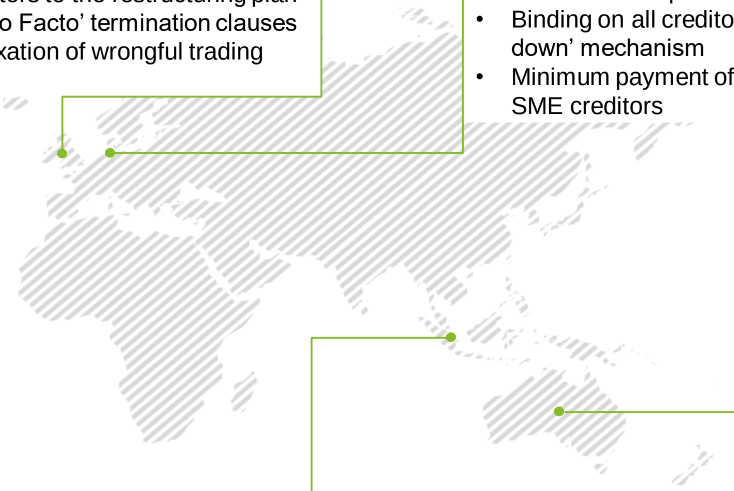
Illustrative Legislative Reforms in 2020

Changes to UK Insolvency Regime

- Go live date: **25 June 2020**
- Introduction of 'debtor-in-possession' corporate moratorium
- Cross-class 'cram-down' concept to bind dissenting creditors to the restructuring plan
- Restraint of 'Ipso Facto' termination clauses
- Temporary relaxation of wrongful trading provisions

Reforms to Dutch Bankruptcy Act

- Go live date: **1 January 2021**
- Dutch Act on Court Confirmation of Extrajudicial Restructuring Plans ("WHOA")
- Seeks to prevent bankruptcies of viable businesses through a debt restructuring plan outside formal proceedings
- Binding on all creditors via cross-class 'cram-down' mechanism
- Minimum payment of 20% for required for SME creditors



Singapore's Insolvency, Restructuring and Dissolution Act (IRDA)

- Go live date: **30 July 2020**
- Restriction on Ipso Facto clauses
- Out of court voluntary appointment of judicial managers
- Assignment of claims by judicial managers to third party funders
- New summary procedure for dissolution of a company to avoid costs incurred for appointing liquidators or court processes

Reforms to Australian Insolvency Law

- Go live date: **1 January 2021**
- Significant shift from current 'Creditor-in-possession' regime to 'Debtor-in-possession' system
- Business owners will retain control and work with a Small Business Restructuring Practitioner (SBRP) to develop restructuring plan to be accepted by creditors.
- Establishing the SBRP category for professionals

Sources: Legal analysis by Simmons & Simmons, Herbert Smith Freehills, Squire Patton Boggs and Holding Redlich

Deloitte Restructuring Services

We work with clients to improve outcomes across the stress spectrum ranging from companies seeking to turnaround short term underperformance to those in deep financial distress requiring crisis management. We are actively helping businesses in Singapore and Southeast Asia to turnaround, transform and grow their businesses and to successfully navigate the financial impact of Covid-19.

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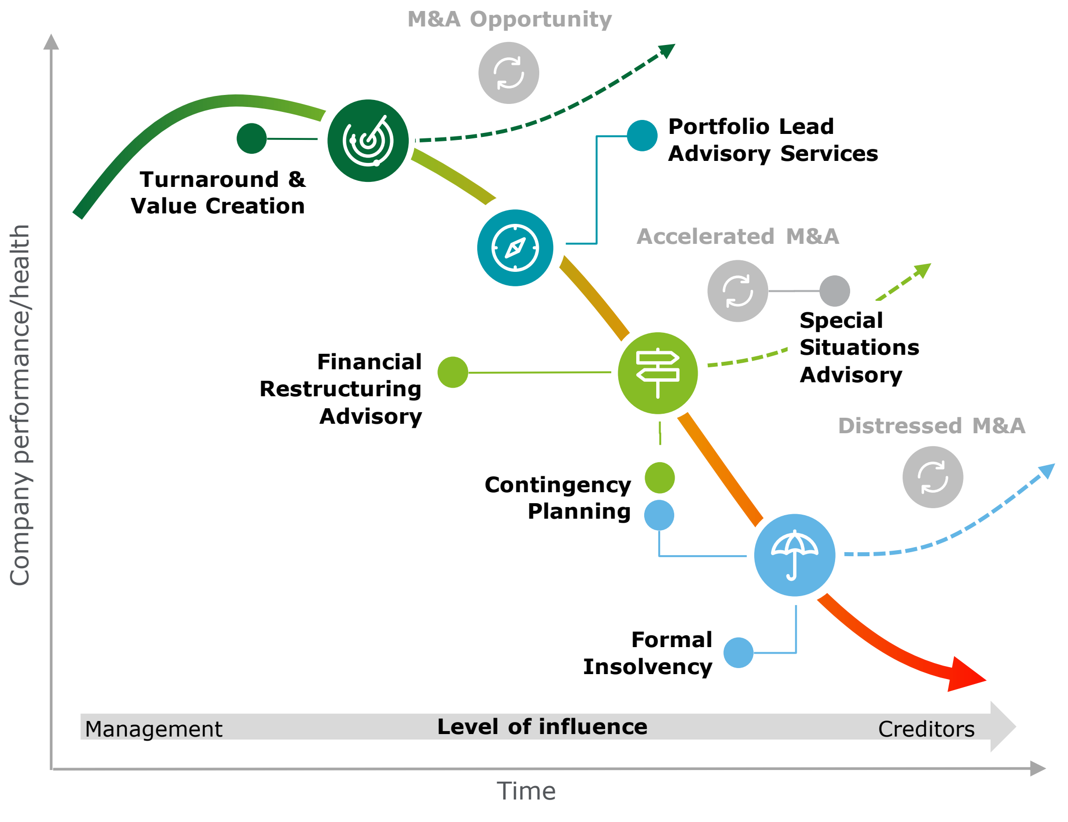

- **Turnaround & Value Creation Services** for underperforming businesses using M&A, restructuring and private equity techniques to deliver performance improvement …fast
- **Portfolio Lead Advisory Services** deleveraging and loan portfolio sale transactions acting sell-side / buy-side and providing strategic advisory to maximize value from non-core assets
- **Financial Restructuring** business reviews and options assessment to establish a foundation to assist stakeholder negotiations in corporate refinancing, restructuring and M&A situations
- **Special Situations Advisory** accelerated capital raising, M&A, debt advisory and structuring assistance in complex cross border multi-stakeholder special situations
- **Contingency Planning** before and during complex restructurings, supporting with options analysis and "plan B" scenarios to drive a consensual deal or provide a bridge into insolvency
- **Formal Insolvency** where a consensual restructuring is not possible; we can provide assistance to debtors and creditors through formal corporate insolvency processes

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