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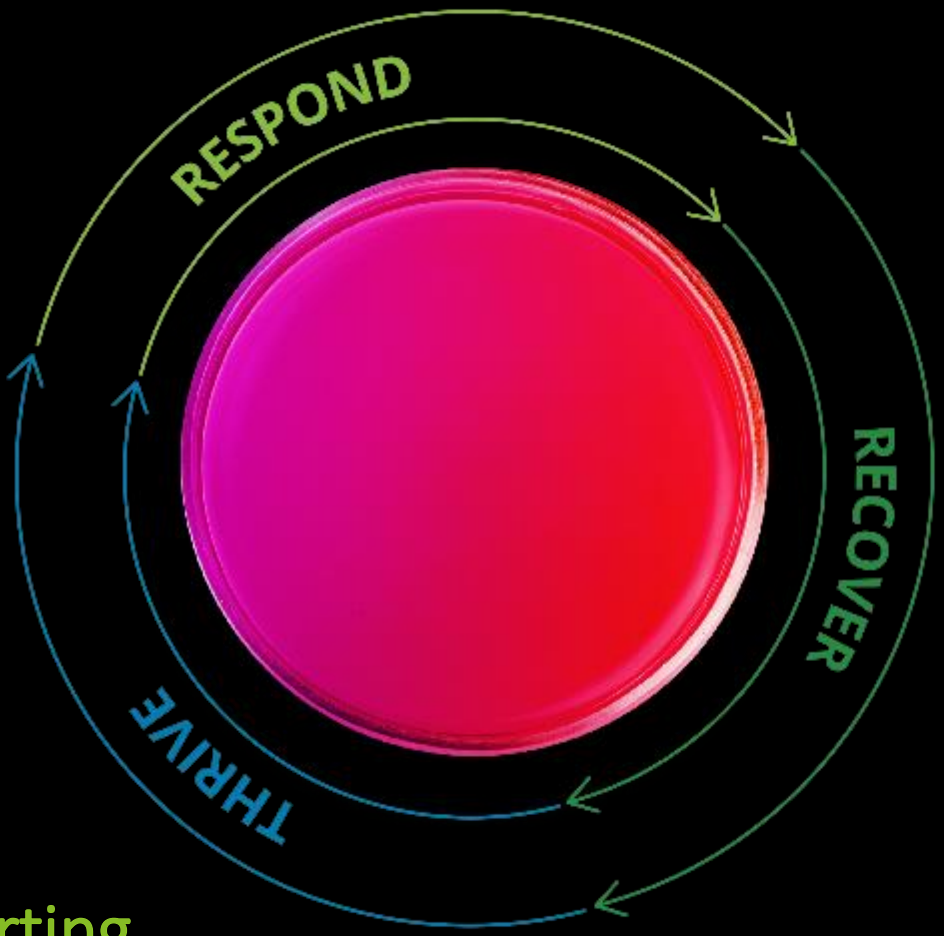

Recover: Financial Reporting and Business Recovery

Responding to the challenges, 17 July 2020

MAKING AN IMPACT THAT MATTERS since 1845

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Introductions

Deloitte Presenters

Daryl Walcott-Grappie

Partner
Audit & Assurance
Risk Advisory

Career Summary

Daryl is a Partner in the Audit & Assurance and Risk Advisory departments at Deloitte, serving clients within the financial, manufacturing, and other sectors in Trinidad and Tobago, Barbados and the EC.

Daryl has served on the firm's Professional Practices Group, providing consultations and guidance on IFRS, accounting and auditing matters; and, he facilitates internal and client training and workshops on a range of accounting topics.

Daryl also previously led the finance team of a five branch consumer goods firm and the project accounting team of a leading real estate developer.

He is a member the Institutes of Chartered Accountants of Trinidad and Tobago and of Barbados where he served on the Accounting and Auditing Standards Committee.

Paul Leggett

Partner
Financial Advisory

Career Summary

Paul is a financial advisory leader who spent the last 20 years successfully advising corporate entities and their various stakeholders in a range of industries including, financial services. Paul specialises in business reviews, turnaround and contingency planning.

During his time in Deloitte he has spent nine months working for one of the UK's leading banks in their special situations team dealing with borrowers requiring turnaround advice.

As well as providing advice to stakeholders, Paul has also been involved in the trading and sale of a number of businesses, including advising the relevant stakeholders.

Raymond Haynes

Director
Financial Advisory

Career Summary

Raymond's brings over 15 years' experience serving government, corporate and private equity clients on complex financial advisory engagements across the region.

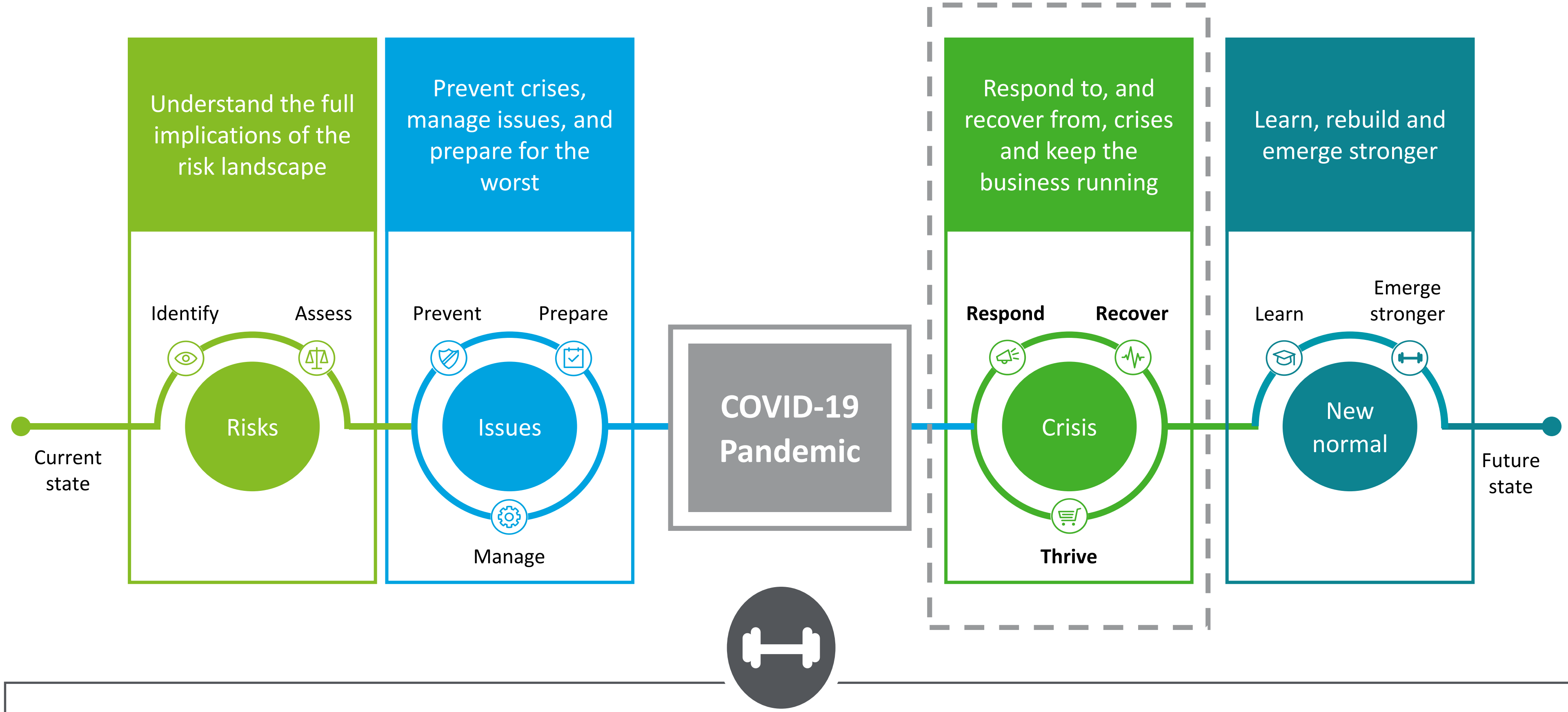
Raymond has advised key stakeholders on M&A advisory, valuation analyses, corporate restructuring, due diligence, financial analyses and modelling, and debt/equity advisory across a number of business sectors.

He has led financial reporting valuation reviews for assets impairments, business combinations and financial instruments.

Raymond is a member of the CBV Institute, the Chartered Professional Accountants of Canada, and the Institute of Chartered Accountants of Barbados.

Crisis and resilience framework

A holistic approach enables a business to prepare, respond, recover and emerge stronger



Truly effective crisis management goes beyond being reactive and simply protecting existing value.

It also enables **resilience** and powers **future performance**, thereby **enabling an organisation to emerge stronger**.

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Key financial reporting considerations

Judgements and estimates – COVID-19

IAS 1 disclosure requirement for significant accounting judgements (excluding estimates) and key sources of estimation uncertainty

Extremely wide range of possible outcomes of the Covid-19 Pandemic resulting in a high degree of uncertainty about the path it will take and the time needed to return to a "Normal" state.

Entities will still need to do their best to make reasonable estimates, prepare comprehensive documentation to support the basis of those estimates and provide robust disclosure of the significant judgements exercised, the key assumptions used and their sensitivity to change.

Consistent assumptions should be used for all relevant assessments.

IAS 1 disclosure requirement if source of estimation uncertainty results in a significant risk of material adjustment within the next financial year.

Covid-19 Pandemic may require a more broad consideration of what is a significant source of estimation uncertainty.

- Government support measures
- Cash and banking covenants
- Social distancing measures and their impact

Judgements and estimates – COVID-19

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Uncertainty around COVID-19

There is no single view on how COVID-19 Pandemic will evolve and its impact on the economy.

This lack of consensus increases the need for, and importance of, full disclosure of judgements, assumptions and sensitive estimates

- Going concern
- Impairment of non-financial and financial assets
- Measurement of financial instruments
- Events after the reporting period

Judgements

- Why was the judgement made?
- Why it is significant?
- How did you reach that conclusion?
- Most useful when it is specific, tailored and informative. Therefore avoid generic statements.

Estimates

- Nature of the uncertainty
- Carrying amount of the affected assets / liabilities
- Sensitivity analyses / ranges of possible outcomes
- Expectation of these disclosures for all items identified as sources of estimation uncertainty

Expected credit losses on financial assets

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COVID-19 can affect the ability of borrowers, whether businesses or individuals, to pay amounts owed

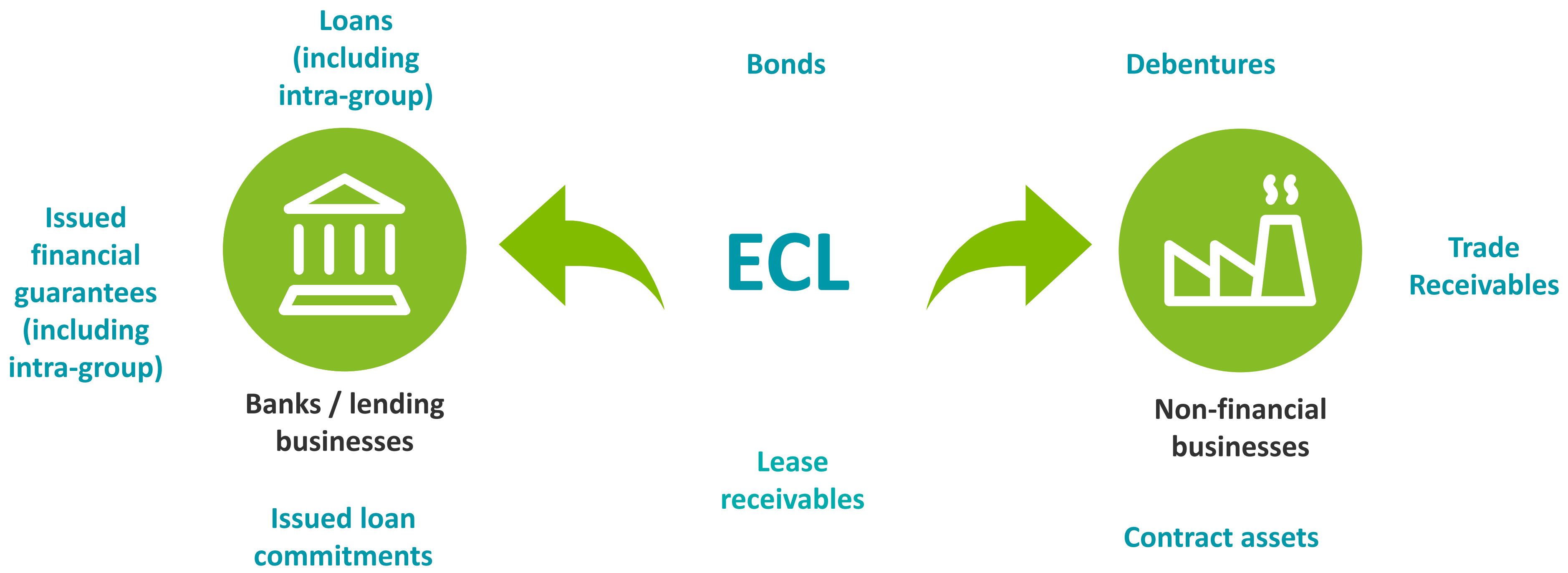
Both individuals or businesses, may have a particular exposure to the economic impacts depending on their geography and industry sector

Reductions in forecasts of economic growth increase the probability of default across many borrowers.

More broadly, falls in prices of assets mean a fall in value of collateral, which then may lead to increased loss rates.

Unsecured facilities are more susceptible to increased loss rates.

Expected credit losses on financial assets



- Estimate of lifetime probability of default at initial recognition and each reporting date
- Assessment of forward-looking information

"Staging" analysis

- Based on reasonable and supportable information that is available without undue cost and effort at the reporting date
- Sources can include:
  - Information used in your ongoing credit evaluation process
  - Financial forecasts for economies or industries that are becoming available over time

Expected credit losses on financial assets

Trade receivables / contract assets

- Simplified approach
- No requirement for a complex staging analysis
- Lifetime ECL is recognised from the date of initial recognition
- Measurement of lifetime ECL follows the same principles as under the general model
- Reasonable estimate for portfolios of trade receivables: historical credit losses on a large group of trade receivables with shared credit characteristics
- Common example is a provision matrix developed using historical credit loss experience

Provision matrix

- IFRS 9 requires historical loss rates to be adjusted to reflect current conditions and estimates of future economic conditions.
- COVID-19 will require you to revisit the provision matrix approach and consider the following…

Amount/timing of ECL

- Amount and timing of ECL and probability of alternative scenarios given economic uncertainty
- Reconsider previous ECL expectations
- May require significant judgement

Potential lack of historical data

- Lack of relevant historical data on sufficiently adverse economic conditions on which to base the estimate

Operational disruption

- Operational disruption / moratoriums on debt repayments
- Delays in processing and settling of transactions
- If delay is temporary, "days past due" analysis may not be reflective of expected losses

Greater incidence of individual receivables in default

- Loss rates to be applied to individual receivables or sub-portfolios rather than on a whole portfolio basis
- Individual ECL should reflects probability-weighted outcome
- Collective basis ECL is appropriately reflective of changed circumstance

Expected credit losses on financial assets

Other receivables

General ECL model

- Intercompany receivables
- Loans to associates and joint ventures
- Other long-term receivables e.g. from business disposals

ECLs may not have been material in the past but may now be potentially material due to COVID-19

- Increased weighting to negative economic scenarios.
- Exposure to specific industry sectors or geographical areas that are most significantly affected by COVID-19
- Reconsider appropriateness of past methods for assessing ECL with up-to-date inputs

Disclosure of key assumptions

Describe the approach to determining the value of each assumption. Include assumptions on:

1. Duration
2. Intensity

of any effects from suspension of activities and recovery phase

If estimation uncertainty, give information required by IAS 1 (e.g. sensitivity analysis)

Impairment of non-financial assets within scope of IAS 36 – COVID-19

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Identify impairment indicator

IAS 36 requires that the asset be carried at not more than their recoverable amount

Higher of:

Fair value less costs of disposal (FVLCD)

and

Value in use (VIU)

Factors resulting from COVID-19 which indicate that the carrying amount of an asset or CGU ***may not be recoverable***:

- Decreased demand for your products or services
- Increased costs/business interruptions due to supply chain issues
- Cancellations or postponements of orders by customers
- Needing to provide significant concessions to customers
- Significant customers experiencing financial/ cash flow difficulties
- Carrying amount of net assets are more than its market capitalisation

Impairment of non-financial assets within scope of IAS 36 – COVID-19

Key inputs to discounted cash flow calculations

Cash flow projections

Projection based on the conditions that existed on the reporting date (including everything that could have reasonably been known at that date)

Excludes effects of restructuring plans that are not committed at the reporting date

Growth rate(s)

Discount rate(s)

Estimate of the rate that the market would expect on an equally risky investment

Includes uncertainties about the future

Uncertainties reflected either in the cash flows (e.g. expected cash flows method) or discount rate

Assigning probabilities to estimates of future cash flows more transparent / tied to underlying commercial expectations than addition of a "COVID-19" risk premium

Disclosure of key assumptions

Describe the approach to determining the value of each assumption. Include assumptions on:

1. Duration
2. Intensity

of any effects from suspension of activities and recovery phase

If estimation uncertainty, give information required by IAS 1 (e.g. sensitivity analysis)

Other COVID-19 considerations: Breach of covenants and Going concern

Breach of a loan covenant may affect the **timing of repayment** of the facility

- It may become repayable on demand - which affect the classification in the financial statements.

- **IF the breach occurred on or before the reporting date** and it provides the lender with the option to demand payment within 12 months of the reporting date it should be classified as a current liability
- However, if the lender agrees, on or before the reporting date, to not seek repayment within 12 months after the reporting date, it is classified as non-current

- **IF the breach occurred after the reporting date**, it is a non-adjusting event and should be disclosed.
- Consider whether a breach after the reporting date **raises considerable uncertainty about the entity's ability to continue as a going concern**.

The **going concern basis should be used** unless management intends to:

- Liquidate the entity
- Cease trading
- No realistic alternative but to do so

You need to consider whether disruptions will:

- Be prolonged and result in diminished demand
- Result in significant liquidity shortfalls
  - Management to assess going concern for at least 12 months from the reporting date
  - If material uncertainty – Disclose the uncertainties

COVID-19 makes such an assessment more difficult due to impact on economic conditions. However need to consider:

- Impact on the entity's **specific** circumstances
- Current and potential cash resources
- Access to existing and new financing facilities

The assessment takes into consideration **conditions and information before and after the reporting date** up to the date of authorisation of the financial statements.

For interim financial statements consider for 12 months after the interim reporting date.

Presentation of COVID-19 items in the statement of profit or loss

COVID-19 may give rise to material items of income or expense

e.g. restructuring provisions and impairment losses

If practicable to identify and quantify discrete items, disclose separately in:

- ✓ statement of profit or loss and other comprehensive income
- ✓ notes to the financial statements

Disclosure and presentation

Consider additional line items, headings or subtotals

✗ 'extraordinary' is prohibited

Considerations

- Nature and magnitude of the costs
- Rationale for creating a new heading or subtotal and its usefulness

Caution should be used when *excluding* certain items from "operating profit or loss"

Impacts of COVID-19 on performance

Difficult to identify without using arbitrary assumptions

Not appropriate to present results as though the impacts of COVID-19 had not happened (on the grounds that it was not present in the comparative period)

Not appropriate to consider that the function of costs has changed (when presentation is on a functional basis)

Any additional information should be included in the notes

Business recovery considerations

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Navigating through uncertainty and disruption will require an iterative process of scenario-based forecasting to assess different alternatives

Market influences

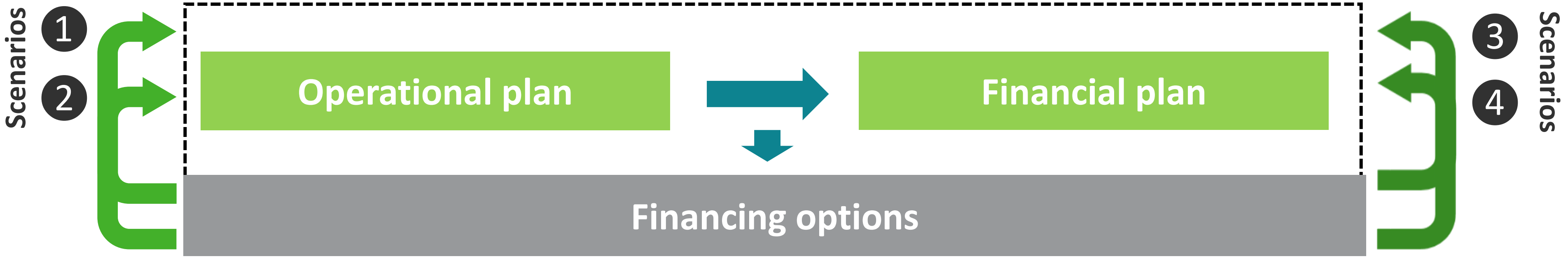
- Length of COVID impact?
- Supply chain disruption
- New competitive dynamics
- Potential investors?
- Product/service demand changes?

Historical performance

- Significant changes in historical relationships?
- Is data set consistent?
- Benchmarking?
- Current financial health?

Proposed initiatives

- What are post-COVID plans?
- New target areas?
- Can the people responsible deliver?
- Is investment required?
- Cost-benefit analysis?



Multiple scenarios will reveal **multiple** financing requirements and the consideration of **multiple** alternatives

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Five step process to scenario planning

Step 1: Understanding the driving forces of performance
- Current position
- Current strategy
- Driving forces

Step 2: Assess impact and relevance
- Key drivers
- Critical uncertainties

Step 3: Develop scenarios
- Scenario framework
- Scenario narratives

Step 4: Identify opportunities and mitigate risks
- Implications and options
- Strategic choices

Step 5: Agree actions and execute the plan
- Plan and execute

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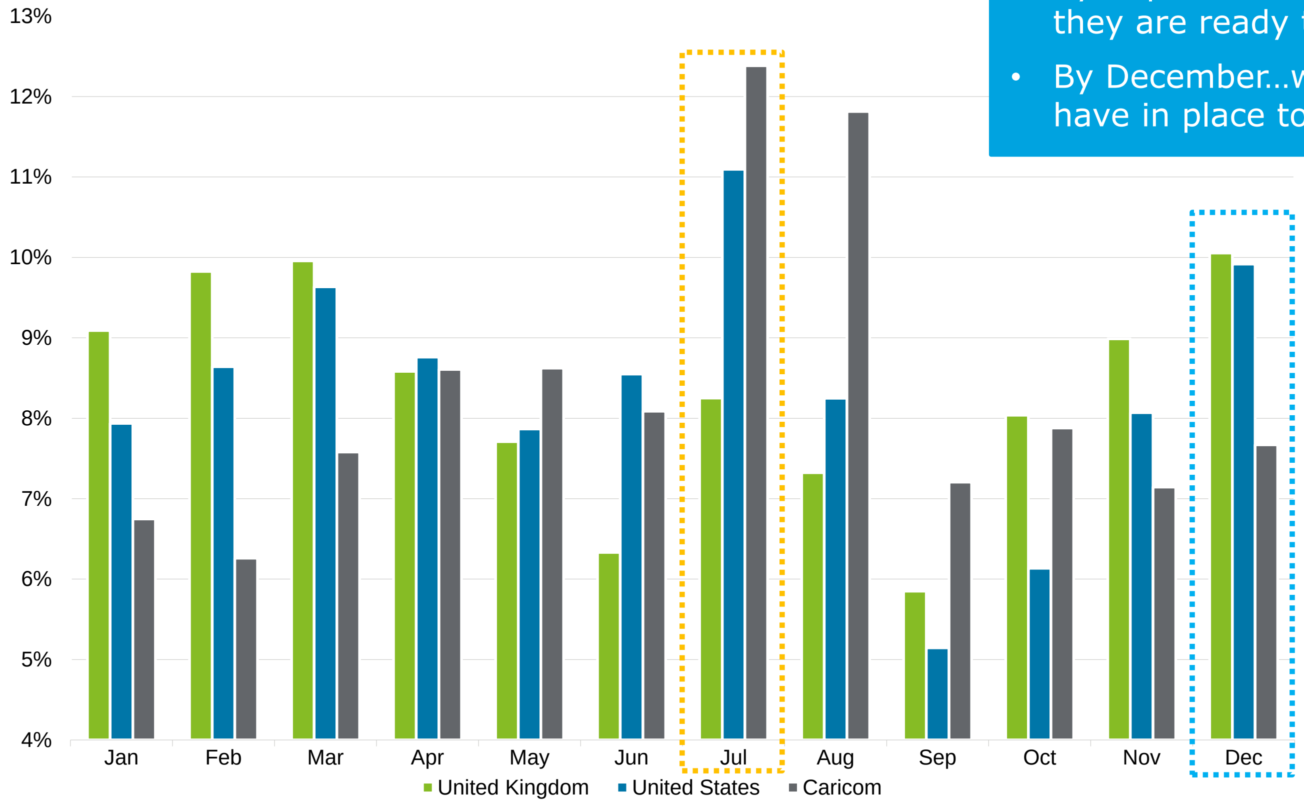
Discussion: next steps for the hospitality sector?

Percentage by month of total long-stay arrivals over last 20 years



Source: Central Bank of Barbados,

Let’s say, albeit optimistically, that we are rid of COVID-19

- By September… are accommodations considering scenarios where they are ready to capitalize on everything October has to offer, or
- By December…what plans will hotels and other accommodations have in place to finish the winter season stronger than it started?

Hospitality industry

- Create and analyze multiple scenarios of your cash flows forecasts;
- Develop pricing models that demonstrate innovation and quick response to rapidly changing market developments;
- Maintain engagement and morale amongst staff;
- Introduce and vary new options for guests; and
- Engage openly and honestly with suppliers, bankers and other stakeholders

Actions that seemed aggressive just months ago may now be a fundamental part of the cash management toolkit

13 week cash flow forecast

- Weekly outlook on rolling basis
- Daily reconciliation to bank account
- Rapid allocation of cash receipts is key

Real-time updating of forecast

- Daily update required to keep forecast relevant
- Incorporate impact of government updates
- Reflect latest discussion with customers/suppliers
- May require re-directed resources (e.g. Finance / IT)
- Ransom suppliers payments / likelihood of receipts

Real-time scenario planning

- Requires flexibility (supply chain losses, Lockdown extension etc.)
- Consider solvency scenarios and risk mitigation plan
- Build and refresh Base, Upside and Downside scenarios with mitigating strategies

Governance

- Centralise cash flow management in particular payments
- Priority payment sign off and DoA reduction - Cash Czar /CFO to authorise payments
- Tighten update and version control – one owner
- Log changes with brief narrative

Communication

- Increased focus on funder and external stakeholder communications, linking into Central Command Centre
- Clear internal understanding of new cash management controls

Establish effective new ways of working

- Where teams split or virtual working environment key team members to look to create as close to ‘normal’ work environment as possible
- Ensure updates and decisions can be made quickly and effectively

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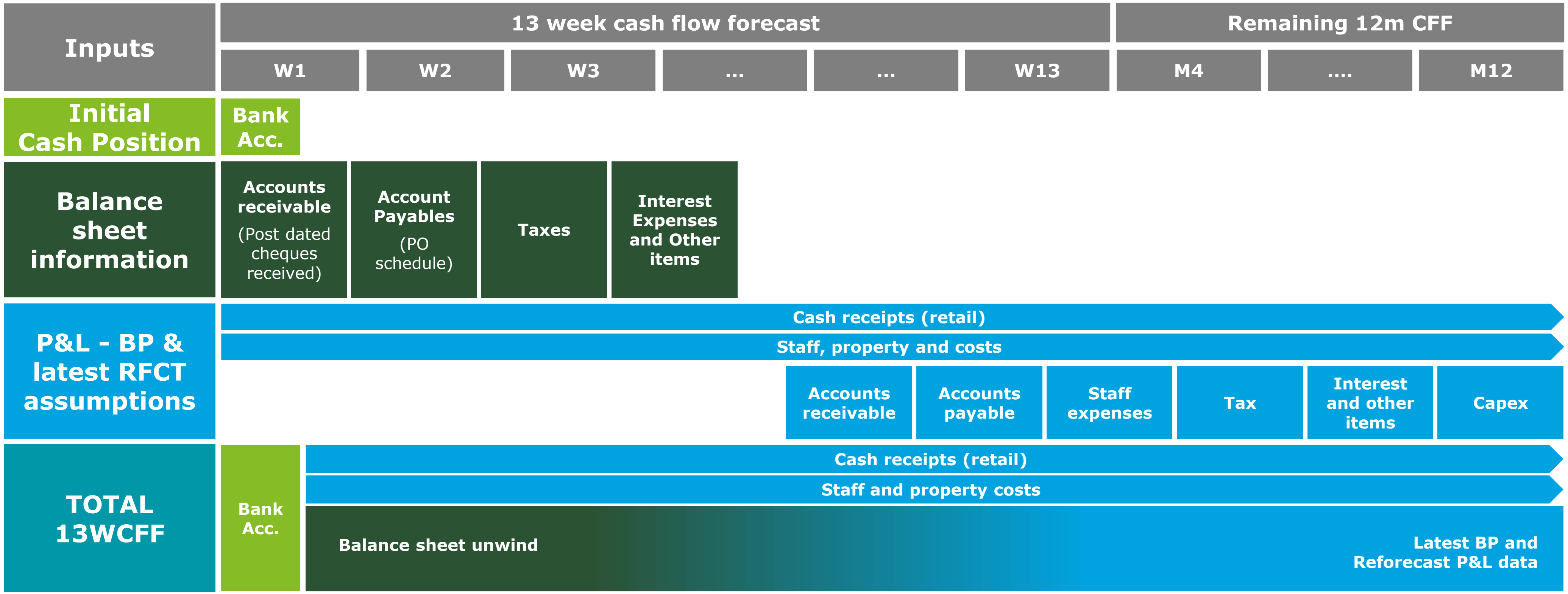
13 week cash flow forecasting - should be anchored in the latest cash position and balance sheet and transition into BP assumptions as it runs further out



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Example of 13 week cash flow

	Projection Period													
Days	**0**	**7**	**14**	**21**	**28**	**35**	**42**	**49**	**56**	**63**	**70**	**77**	**84**	
Week Ending	**18-Jan**	**25-Jan**	**1-Feb**	**8-Feb**	**15-Feb**	**22-Feb**	**1-Mar**	**8-Mar**	**15-Mar**	**22-Mar**	**29-Mar**	**5-Apr**	**12-Apr**	**Total**
Total Sales	**2,000**	**6,500**	**-**	**2,950**	**1,500**	**4,250**	**-**	**3,250**	**-**	**6,750**	**1,500**	**1,750**	**-**	**30,450**
Cash Receipt														
Operating Receipt	3,500	5,000	500	5,000	1,500	3,000	1,200	5,000	2,500	-	3,250	4,000	1,750	36,200
Excess Inventory Receipt					-			1,500						1,500
Total Receipt	3,500	5,000	500	5,000	1,500	3,000	1,200	6,500	2,500	-	3,250	4,000	1,750	37,700
Disbursement														
Vendor Payment	2,000	3,750	-	1,000	5,180	600	1,700	-	2,050	1,350	1,350	600	2,950	22,530
Gross Payroll	863	288	963	288	863	288	963	288	863	288	863	388	863	8,063
Rent and Utilities	25	25	225	25	25	25	225	25	25	25	25	225	25	925
Equipment Leases	-	-	500	-	-	-	500	-	-	-	-	500	-	1,500
Property Tax	-	-	-	-	4,000	-	-	-	-	-	-	-	-	4,000
General Insurance	-	-	38	-	-	-	38	-	-	-	300	-	-	375
Other	50	50	50	50	50	50	50	50	50	50	50	50	50	650
Total Op. Disbursements	2,938	4,113	1,775	1,363	10,118	963	3,475	363	2,988	1,713	2,588	1,763	3,888	38,043
Net Operating Cash Flow	563	888	(1,275)	3,638	(8,618)	2,038	(2,275)	6,138	(488)	(1,713)	663	2,238	(2,138)	(343)
Non-operating Disbursement														
Interest Payment	-	-	376	-	-	-	387	-	-	-	-	585	-	1,349
Capital Expenditure	125	125	125	125	125	125	125	3,000	125	125	125	125	125	4,500
Professional Fee			100				100					100		300
Total Non-op. Disbursements	125	125	601	125	125	125	612	3,000	125	125	125	810	125	6,149
Net Cash Flow	438	763	(1,876)	3,513	(8,743)	1,913	(2,887)	3,138	(613)	(1,838)	538	1,427	(2,263)	(6,491)
Revolver roll-forward														
Beginning revolver	20,500	20,063	19,300	21,176	17,663	26,406	24,493	27,381	24,243	24,856	26,693	26,156	24,729	20,500
Add: draw	-	-	1,876	-	8,743	-	2,887	-	613	1,838	-	-	2,263	18,218
Minus: Paydown	(438)	(763)	-	(3,513)	-	(1,913)	-	(3,138)	-	-	(538)	(1,427)	-	(11,727)
Ending revolver	20,063	19,300	21,176	17,663	26,406	24,493	27,381	24,243	24,856	26,693	26,156	24,729	26,991	26,991

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Every situation is unique, and whilst the general principles apply, specific application is key to success

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Example 1: International retail business (store based)

- Company faced declining cash performance due to increasing pressure from on-line and tech
- Cash flow forecast income focused on P&L and limited B/S
- Modelling various scenarios (e.g. launch dates, weather patterns (footfall)) = permanent or timing
- Drives discussions with landlords, suppliers etc

Example 2: Contractor (Hotels & malls)

- Global restrictive covenants on head office debt leading to evaporation of liquidity at regional level
- Cash flow forecast income focused on B/S and limited P&L
- Timing of receipts had massive impact on ability to stay within forecast – headroom provisions critical
- Project level control vs company wide position dynamics

Example 3: Conglomerate

- Underperformance in certain sectors causing critical drag on crown jewels
- Bad cash control by central treasury resulted in cash being sub optimally deployed
- Negative feedback loop created increasing management distraction and pressure
- Required divisional reporting overhaul and central treasury overlays

Questions & Answers

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