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Paris, July 10, 2020

United States: Two-speed business bankruptcies

As the COVID-19 epidemic hits the United States very hard, Coface forecasts in its baseline scenario that the country's GDP will contract by 5.6% in 2020, before rebounding by 3.3% in 2021. Nevertheless, this forecast is threatened by the resurgence of the outbreak in several states, which are already pausing or even reversing the resumption of activity after the extensive lockdown of April.

On the bankruptcy front, the sharpest drop in GDP should be followed by a massive increase in business bankruptcy filings. Nonetheless, since the beginning of the crisis, the latter has fallen since February, driven by a significant drop of bankruptcy filings under Chapter 7 of the US bankruptcy law¹ (liquidation). At the same time the number of companies seeking Chapter 11 protection (reorganization) is up sharply (+48% year-on-year in May), indicating that bankruptcies related to COVID-19 are already brewing. Coface forecasts bankruptcy to rebound in the second half of 2020, with an expected increase of 43% between the end of 2019 and the end of 2021.

Furthermore, Coface's estimates show that the "zombie" companies, which have grown over the last decade to represent more than 6% of companies in 2019, could also be pushed into bankruptcy in the coming months. The number of companies in difficulty is also likely to multiply as a result of the accumulation of debt.

Falling bankruptcies in recent months: a sham situation

2019 saw the first annual increase in bankruptcies since 2009 with an increase in proceedings initiated in 2019 by 2.5% compared to 2018². Data released³ after the first quarter of 2020 shows that after a jump of 21% in January, corporate bankruptcy proceedings began to decline starting in February.

As in Europe, measures to support corporate liquidity, a wait-and-see attitude of debtor companies and the closure of bankruptcy courts might explain this trend.

However, given the magnitude of the shock and while the support measures should gradually expire, business failures in the United States are expected to accelerate.

The health of aggregate company balance sheets highlights that the aerospace, retail, automotive and energy sectors are the most vulnerable to this situation.

Bankruptcies and "zombification" threaten debt-laden companies

The "zombie" companies, which continue to operate despite precarious solvency and profitability, could also be pushed into bankruptcy in the coming months. More importantly, with more companies

¹ Chapter 7 – Liquidation: Accounting for nearly 64% of business bankruptcy proceedings in 2019, this court-supervised process involves the sale of assets and the disbursement of sales revenue to creditors by a judicial representative, in accordance with the priorities established by the Bankruptcy Code.

Chapter 11 – Reorganization: This process, which accounts for over 25% of proceedings in 2019, enables a company to continue its activity while implementing a reorganization.

² Data published by the Administrative Office of the US Courts

³ Data published by the Administrative Office of the US Courts for the first quarter and advance publications for the months of April and May by the American Bankruptcy Institute (ABI)



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forced to leverage debt to cope with revenue losses, the threat of a multiplication of distressed companies is added to the risk of bankruptcy.

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ISIN Code: FR0010667147 / Mnemonic: COFA

