Bloomberg Law

Bankruptcy Law

Corporate Bankruptcy Wave Turns to Dust, Defying Expectations

By Alex Wolf

Jan. 5, 2022, 5:00 AM

- Government stimulus, easy borrowing staved off defaults
- Distress looms, but bankruptcies again could remain low

An anticipated surge of pandemic-induced Chapter 11 cases failed to materialize in 2021, thwarting corporate restructuring professionals' predictions.

Government stimulus programs, combined with low borrowing rates and greater debt forbearance, disrupted early forecasts that a wave of corporate bankruptcies would wash over at some point during the year.

Instead, 2021 saw the fewest annual bankruptcy filings in nearly four decades, falling 24% from 2020, which had recorded the fewest bankruptcies since 1986. A total of 3,596 Chapter 11 cases were filed in 2021, about 3,000 fewer than the year before.

Some sectors, such as retail and health care remain vulnerable as the pandemic continues to take its toll, supply chain issues persist, and inflation rises, bankruptcy and turnaround practitioners say.

But expectations of when the bottom will drop out are tempered following a year of relatively low bankruptcies that threw the restructuring world for a loop.

"I was as surprised as everyone else that the numbers went down as much as they did," said Michael Sweet, chair of Fox Rothschild LLP's financial restructuring and bankruptcy practice. We may look back and consider that "the shortest recession in history," he said.

The steep bankruptcy hike in 2020 also helps to explain the tame 2021 numbers in comparison. The economic shock caused by the pandemic tipped nearly 250 large companies into Chapter 11 bankruptcy in 2020, the most since the 2008-2009 financial crisis.

But Covid-19 largely accelerated restructuring proceedings that already were in motion. Many of the major retailers, commercial landlords, and energy companies that filed for bankruptcy in 2020 already were reeling from industrywide distress.

"It's interesting to me that we don't seem to really have seen a rush of pandemic-caused or purely pandemic-caused filings yet," said McKool Smith bankruptcy attorney John Sparacino.

Saved by Stimulus

Earlier in 2021, restructuring professionals understood that stimulus funds and debt forbearance would help avoid a wave of bankruptcies in the near term. But many didn't expect the relative calm would last this long, or that filings would fall to historic lows.

Beginning in March 2020, the federal government appropriated about $4.5 trillion for stimulus payments and other relief programs in response to the pandemic.

Those programs included a $16.2 billion relief fund for shuttered entertainment venues, $28.6 billion to aid struggling restaurants, and a low-interest Economic Injury Disaster Loan.

The Paycheck Protection Program, one of the most popular pandemic relief efforts, provided $800 billion worth of forgivable loans to mostly small companies. A 2021 survey by the Federal Reserve found that 82% of small employers applied for the PPP.

As of the end of September 2021, $3.5 trillion of Covid-related appropriations were spent, and another $500 billion had been committed for future expenses, according to federal reports.

Meanwhile, interest rates remained at historic lows.

Flowing Capital

The easy access to liquidity, combined with negotiated debt forbearance, also boosted the economy and kept vulnerable companies from going under in a variety of industries.

Consumer-facing companies like airlines and cruise operators, which experienced stark revenue plummets in 2020, were able to raise "a mind-bending amount of capital" the following year, said Paul, Weiss, Rifkind, Wharton & Garrison LLP restructuring lawyer Kelley Cornish.

Debt from the airline industry alone grew more than 20% to $340 billion between 2020 and 2021. Yet airlines also were handed $54 billion in government aid to cover payrolls.

Even the auto industry, which was hammered by pandemic-caused supply chain disruptions, isn't likely to see any immediate bankruptcies, said Ann Marie Uetz, vice chair of Foley & Lardner LLP's national litigation department.

There are a lot of out-of-court restructurings taking place, as some larger auto parts makers take over smaller suppliers, Uetz said. But those smaller suppliers increasingly are seeking help from their manufacturer customers rather than the bankruptcy courts, she said.

Economic factors aren't consistently indicating to a sanguine outlook for struggling companies. Inflation remains a concern, as are lingering supply chain disruptions and new waves of Covid-19 cases.

Should interest rates and inflation continue to rise, 2022 could spell disaster for some companies that have been limping along.

"It seems like everyone is on edge waiting for the dam to burst," Sparacino said. "I've got to believe that the day of reckoning has just been deferred for a lot of people."

Oil prices also are rising, and business stimulus subsidies are drying up, said Mark Duedall, a corporate restructuring attorney at Bryan Cave Leighton Paisner LLP. "So I do think we'll have distress next year."

"But I've given up trying to predict," he said.

To contact the reporter on this story: Alex Wolf in New York at awolf@bloomberglaw.com

To contact the editors responsible for this story: Laura D. Francis at lfrancis@bloomberglaw.com; Roger Yu at ryu@bloomberglaw.com