

# THE WEIL EUROPEAN DISTRESS INDEX



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SEPTEMBER 2024

## Macro view

- The latest Weil European Distress Index (WEDI) indicated a marginal rise in the levels of corporate distress compared with the previous quarter but remained below the previous year.
- However, this masks a disparity in regional performance. Germany remained the most distressed market measured, with levels rising again on the previous quarter, now the highest in over four years (July 2020), during the early stages of the global pandemic.
- Distress among UK corporates also rose on the previous quarter to its highest level for 12 months, driven higher by weaker investment metrics, profitability and squeezed liquidity.
- Elsewhere, corporate distress in France rose on the previous quarter, primarily driven by pressure on liquidity. While Spain/Italy was the only market to show an easing in underlying distress.
- The European macroeconomic environment remains challenging. The latest data reported Germany's GDP contracting by 0.1% in the second quarter of 2024, notably weaker than that of other major economies and raising fears of another recession.
- The European Union (EU) as a whole grew by 0.3% during the same period, with Spain leading the way with 0.8% growth. France and Italy also posted modest gains of 0.3% and 0.2%, respectively.
- Meanwhile, the UK reported output rising by 0.6% as services grew by 0.8%, offset by falls of 0.1% in both the production and construction sectors. Concerningly, more recent estimates showed GDP in June and July flat lining.
- Forecasts for economic activity remain lacklustre. The latest IMF projections show growth in the Euro Area of just 0.9% in 2024, led by Spain which is expected to see a rise of 2.4%, and Germany expected to see the weakest growth in the Euro Area of 0.2%.
- An unusually high degree of uncertainty persists. Ongoing disruption in Russia and Ukraine, and rising tensions in the Middle East cast a shadow over recovery.
- Elsewhere, major elections across the globe, in particular the US presidential election due to take place on 5 November, create further investment anxieties.

## Weil European Distress Index Movements

Aug 2024	QoQ trend	YoY trend
+2.6	 +2.4 May 24	 +3.1 Aug 23

- Over the latest quarter, there has also been a coordinated easing of monetary policy across major markets. The European Central Bank (ECB) cut interest rates twice, once in June followed by another cut in September to 3.5% (deposit facility rate). The latest cut was accompanied by a lowering of its growth outlook for 2024.
- The Bank of England's Monetary Policy Committee (MPC) cut interest rates in July 2024 to 5%, while choosing to keep rates on hold in its September meeting. Meanwhile, the Federal Reserve has made its first rate cut in four years, reducing rates by 0.5%, with knock-on effects felt across European markets.
- However, the UK Government has also signalled a period of fiscal tightening, the detail of which will be clearer upon the Budget scheduled for 30 October.

## Sector view

- Key industries such as real estate, industrials, healthcare and retail/consumer remain above long-term distress levels.
- Retail Estate remained the most distressed sector according to the latest data, although levels eased on the previous quarter. On a rolling three-month basis, distress across the sector has fallen to the lowest level since January 2023.
- Stabilising property valuations, adjustments to refinancing costs and greater levels of certainty have helped settle market conditions.
- Industrials has experienced a marked increase in the levels of distress, rising from the fourth most distressed sector to the second. Considerably weaker investment metrics, squeezed liquidity, and a weaker appetite for risk all contributed.
- Healthcare companies remained above long-term distress levels, although easing on the previous quarter. A reduction in operating costs due to lower energy bills and slower wage growth, along with increased stability in the real estate market, have likely contributed to a decline in financial distress.

## How do we define ‘distress’?

The Weil European Distress Index (WEDI) provides a measure of the level of corporate distress by aggregating company fundamentals and financial market indicators across key European countries.

Corporate distress can be defined as uncertainty about the fundamental value of financial assets, volatility and increase in perceived risk. It also refers to the disruption of the normal functioning of company financial performance, including their ability to fulfil their debt requirements.

The definition is purposefully broad as corporate distress can manifest in different ways, and no two stress events are identical for each company.

Although stress events differ in composition, there are several common characteristics of corporate distress ranging from pressure on liquidity, reduced profitability, rising insolvency risk, falling valuations and reduced return on investment. These company indicators are also set against a backdrop of market conditions that can also indicate levels of distress (e.g. business confidence, rising volatility and rising levels of perceived market risk).

## Methodology

The WEDI is a univariate time series that distils information embedded in more than 16 indicators into a summary measure of corporate distress. It can then be decomposed into five markets (Total Europe\*, UK, Germany, Spain-Italy, and France), size of company (based on market cap) and 10 industry groups:

- Retail and Consumer Goods
- Travel, Leisure and Hospitality
- Industrials
- Healthcare
- Technology, Media and Telecoms
- Financial Services
- Oil and Gas
- Infrastructure, Utilities and Power
- Commodities and Natural Resources
- Real Estate

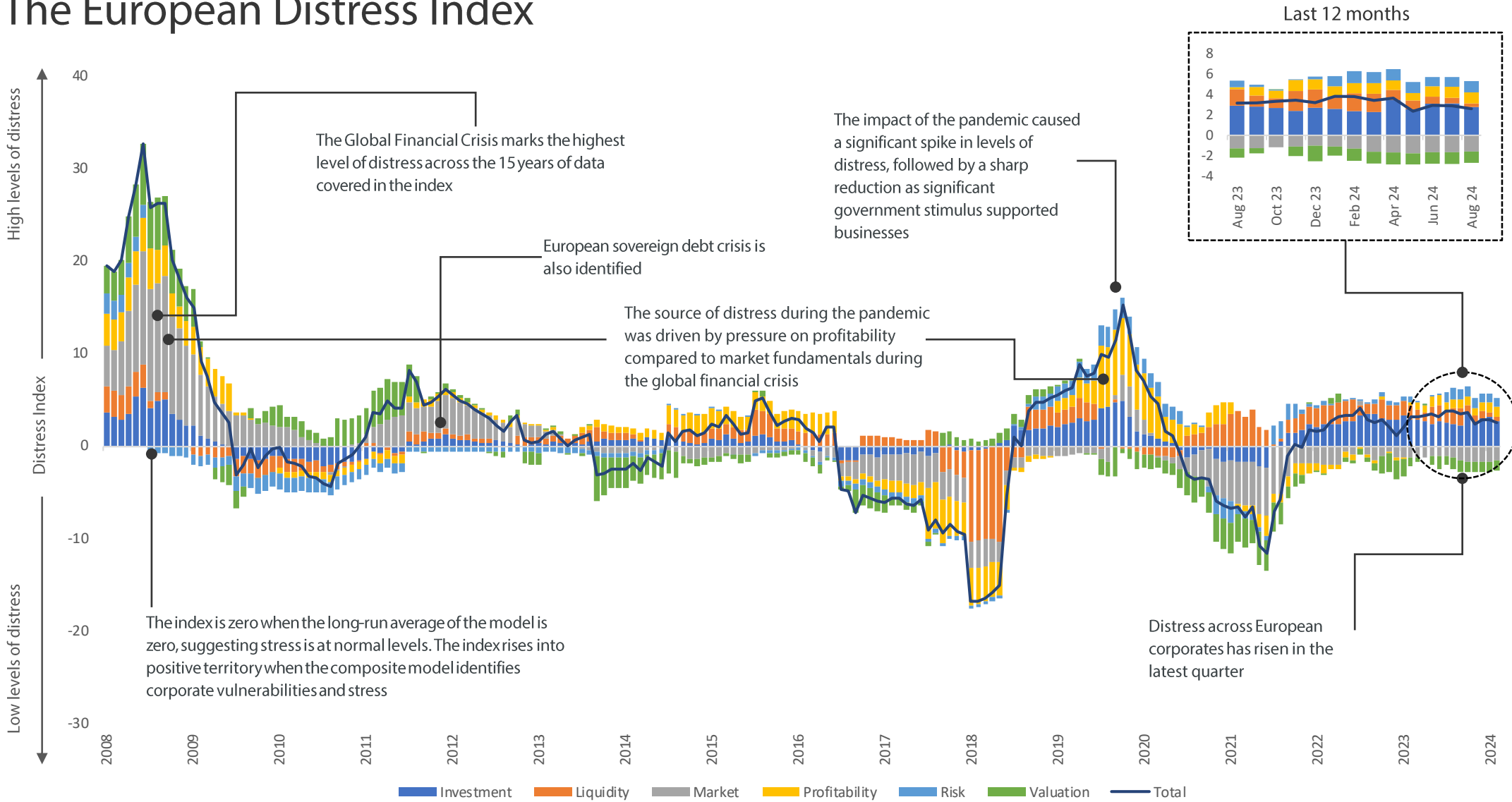
The WEDI is constructed using data from over 3,750 listed European companies and a range of financial market indicators. 16 indicators have been used to construct the WEDI which reflect one or more symptoms of corporate distress based on comprehensive academic and desk-based research.

The WEDI uses a Dynamic Factor Model – a statistical approach that captures the variability across the 16 indicators in a single composite index using key company fundamentals going back to 2005 and incorporates over five million data points. Overall expected to rise by 0.9% this year and 1.7% in 2025.

METRIC	DEFINITION
<b>Liquidity</b>	Contains measures of liquidity such as the current ratio, quick ratio and operating cashflow metrics which are used to determine a company's ability to pay off current debt obligations without needing to raise external capital.
<b>Profitability</b>	Contains measures such as return on equity, net profit margins and return on assets to assess the business's ability to generate earnings relative to its revenue, operating costs, balance sheet and shareholders' equity over time.
<b>Risk</b>	Contains measures such as debt to equity ratio and interest cover to assess a company's capital structure and current risk levels, often in terms of debt levels and risk of default or bankruptcy.
<b>Valuation</b>	Contains measures such as price to earnings, price to book value and enterprise value to EBITDA multiples, used to assess the relative valuation of a company over time.
<b>Investment</b>	Contains measures such as dividend per share and dividend yield used to assess the potential attractiveness of a business as an investment opportunity.
<b>Financial markets</b>	Contains measures such as index market capitalisation, market volatility, risk, credit default swaps and business confidence which are used to track levels of distress across broader financial markets in key European markets.

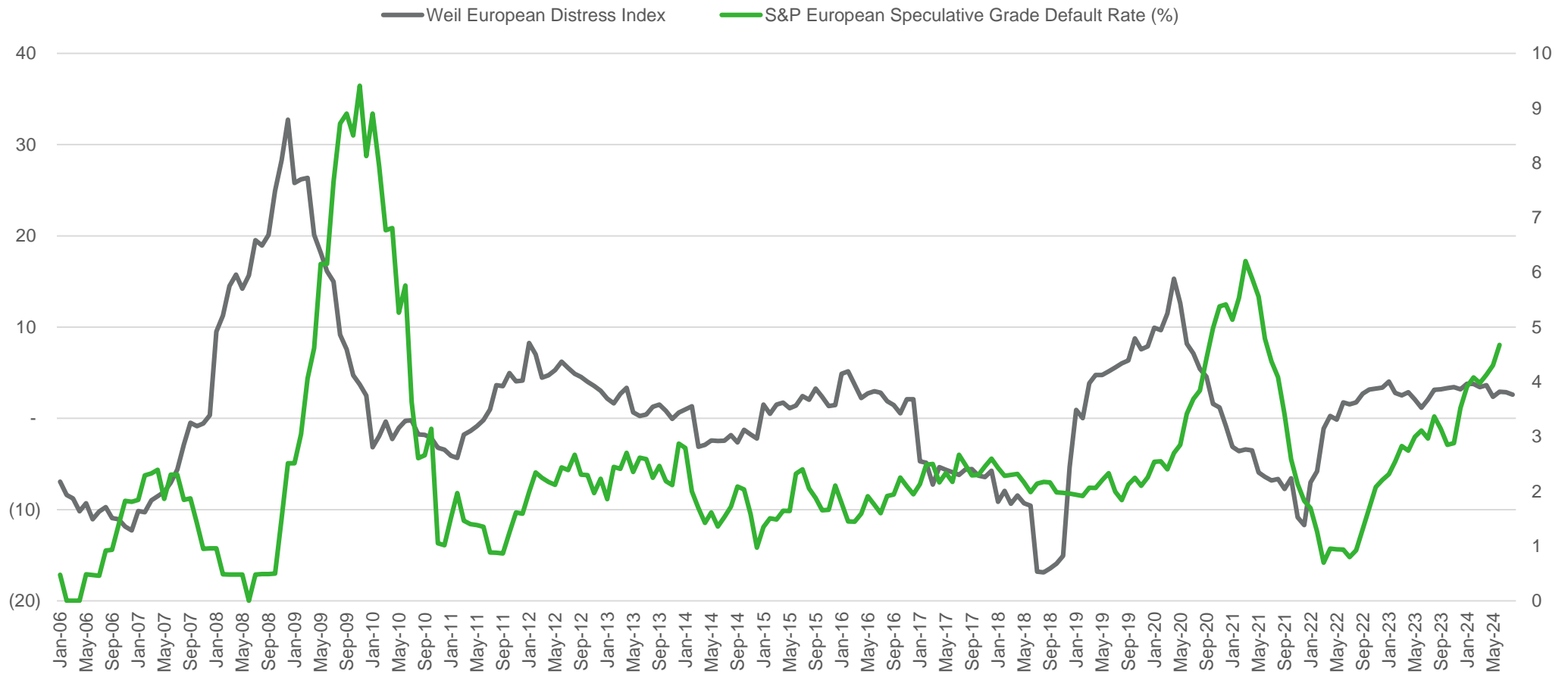
\*Total Europe includes UK, France, Germany, Spain, Italy, The Netherlands, Republic of Ireland, Belgium, Norway and Portugal

# The European Distress Index



# The Weil European Distress Index vs Default Rates

- In the two most major recent crises, the Global Financial Crisis and Covid pandemic, we have observed that the WEDI peaks in advance of the S&P European Speculative Grade Default Rate.
- The WEDI tracks the deterioration in financial markets conditions and company performance which occurs in advance of a default wave to provide an early warning indicator.



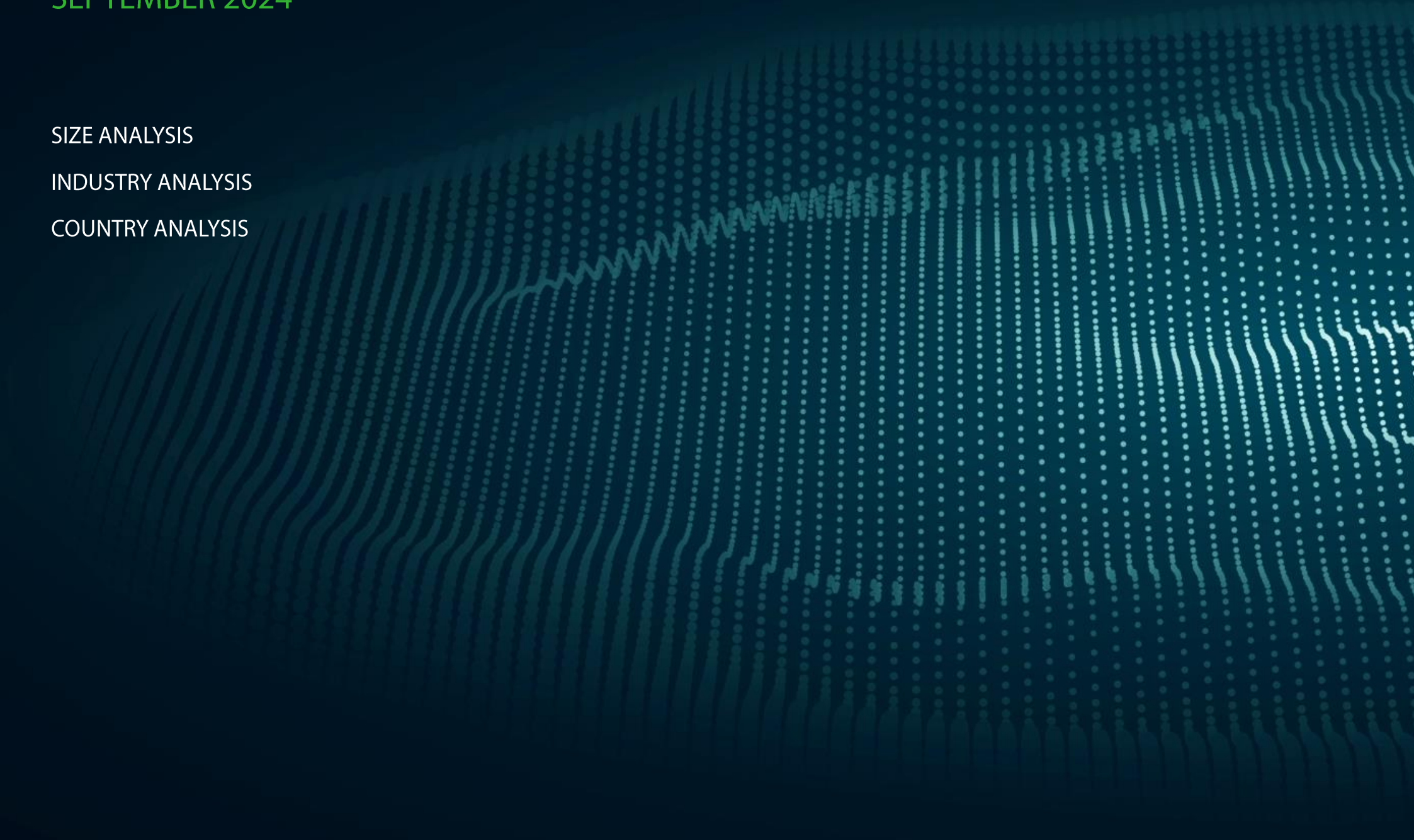
# THE WEIL EUROPEAN DISTRESS INDEX

SEPTEMBER 2024

SIZE ANALYSIS

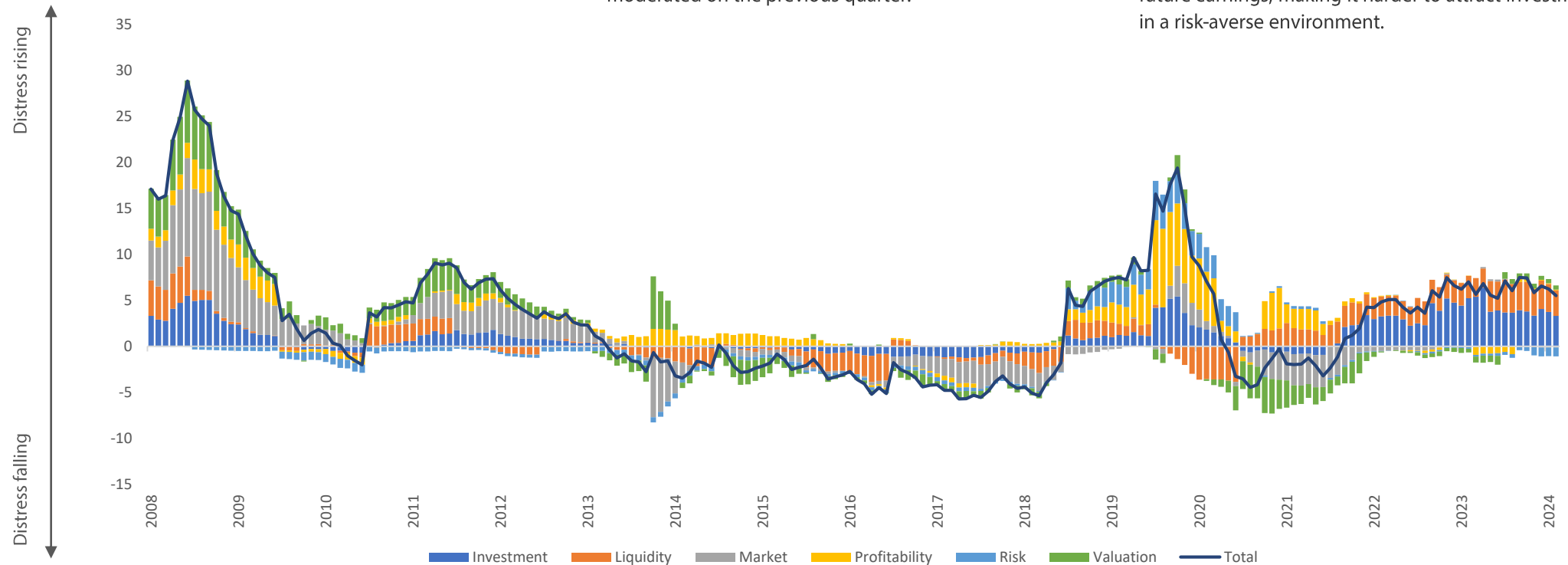
INDUSTRY ANALYSIS

COUNTRY ANALYSIS



# Small Corporates (market cap <€5bn)

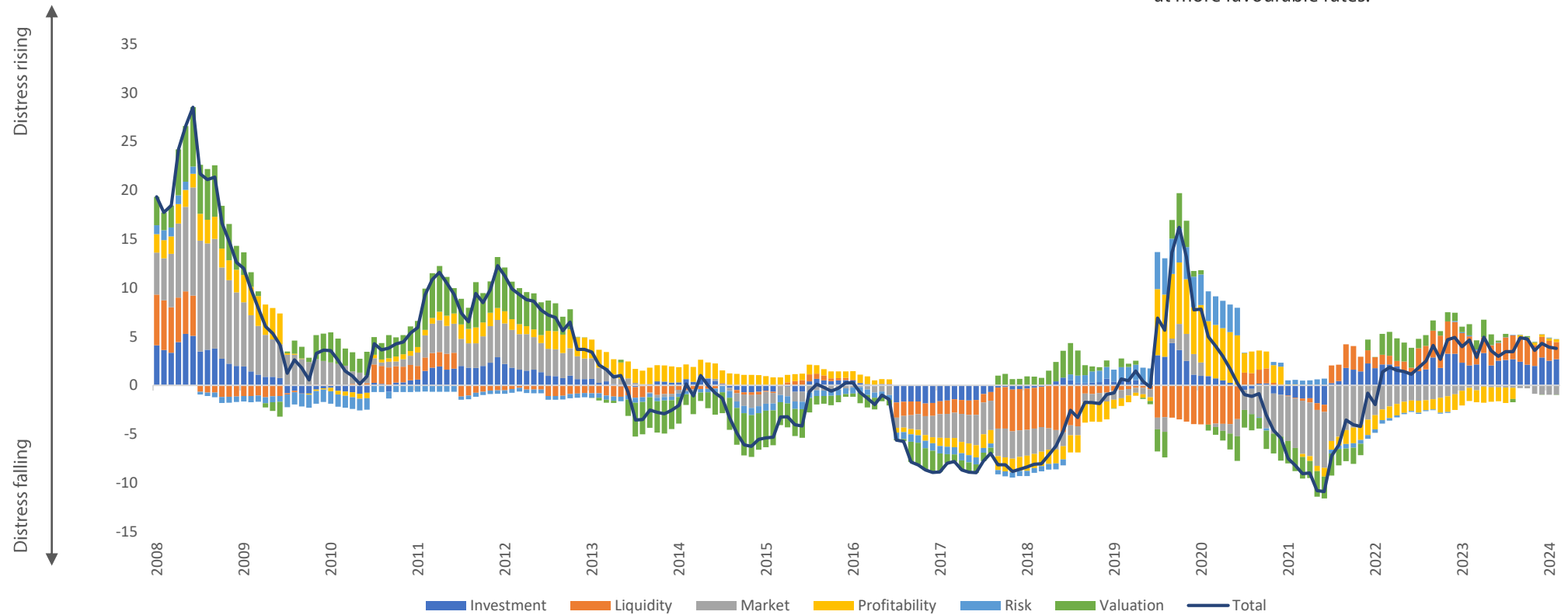
- In the landscape of European corporates, small companies (those with a market capitalisation under €5bn) continue to experience the highest levels of distress.
- Investment challenges and liquidity constraints remain the main contributors to distress, reflecting a persistent theme that has characterised recent quarters.
- While levels of distress have remained elevated compared with the long run average, overall levels have moderated on the previous quarter.
- Ongoing limited access to capital and higher borrowing costs make it more expensive for smaller firms to secure financing, restricting their ability to invest and manage operational costs.
- Meanwhile, weaker cash flow and lower liquidity leave small businesses vulnerable to economic shocks, with less ability to buffer against softening demand or slower sales.
- As such, investors apply greater discount rates to future earnings, making it harder to attract investment in a risk-averse environment.



# Medium Corporates

(market cap €5bn – €25bn)

- In the medium-sized corporate sector, those with market capitalisations ranging from €5bn to €25bn, levels of distress remain broadly similar to those experienced over the last 12 months.
- Corporate distress edged a little higher for medium sized corporates, but has remained largely stable, driven by continued pressures on investment and liquidity.
- Of concern, weaker investment, liquidity and profitability metrics have all contributed to levels of distress remaining elevated.
- At the same time, support from financial markets has strengthened over the last 12 months, offering some relief.
- Overall, distress levels remain above long-term averages and higher than those of larger corporates, which generally benefit from better access to capital at more favourable rates.

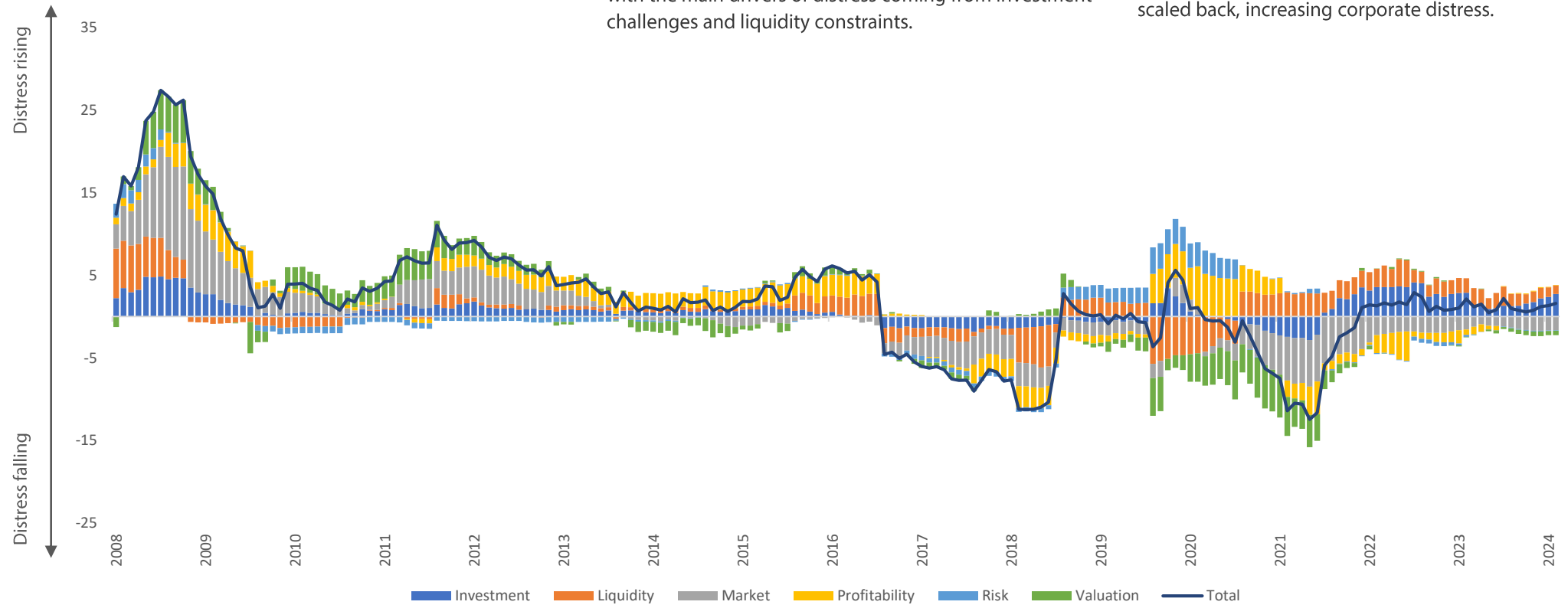




# Large Corporates

(market cap >€25bn)

- In the landscape of European corporates, large companies (those with a market capitalisation over €25bn) continue to experience the lowest levels of distress.
- While large businesses continue to show the least amount of distress, this group has seen distress rise by the most on the previous quarter.
- On a three-month rolling basis, distress among large businesses is now at the highest level since April 2023, with the main drivers of distress coming from investment challenges and liquidity constraints.
- In particular, investment metrics are driving higher levels of distress. Large firms often have significant capital expenditures for expansion, and when investment returns are lower than expected, or costs rise, the economics of these large projects can become challenging, increasing distress levels.
- Large firms are often more exposed to global economic trends and geopolitical risks. Uncertainty, such as trade disruptions, can delay investment decisions and cause projects to be postponed or scaled back, increasing corporate distress.



# Distress Index September 2024

Least distressed

Most distressed



## Real Estate



## Industrials



## Healthcare



## Retail and Consumer Goods



## Travel, Leisure and Hospitality

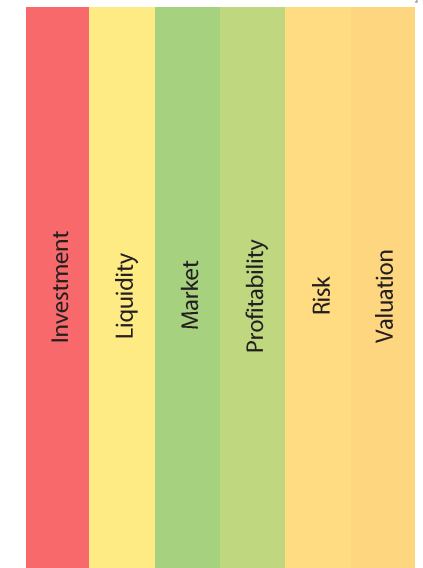
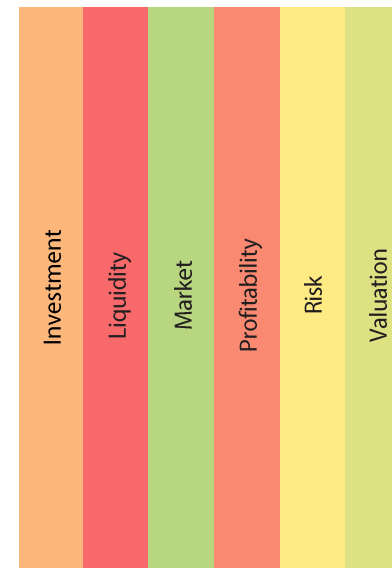
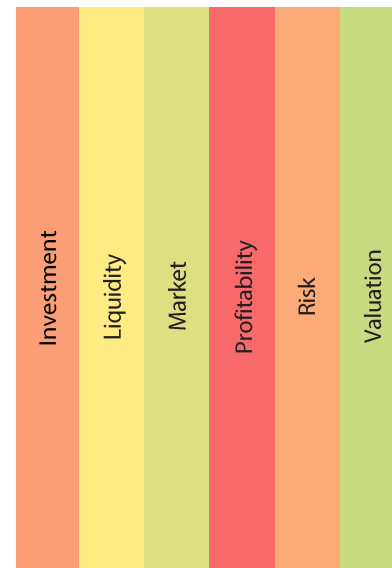
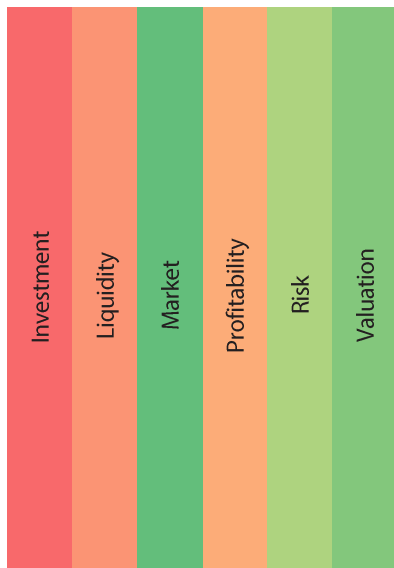
Distress ranking	Index value	YoY trend
1	+5.6	↓ +6.6 Aug 23

Distress ranking	Index value	YoY trend
2	+5.5	↑ +2.2 Aug 23

Distress ranking	Index value	YoY trend
3	+4.9	↓ +8.5 Aug 23

Distress ranking	Index value	YoY trend
4	+4.5	↑ +1.7 Aug 23

Distress ranking	Index value	YoY trend
5	-1.3	↑ -1.8 Aug 23



# Distress Index September 2024

Least distressed

Most distressed



## Financial Services



## Oil and Gas



## Infrastructure



## Technology, Media and Telecoms



## Commodities and Natural Resources

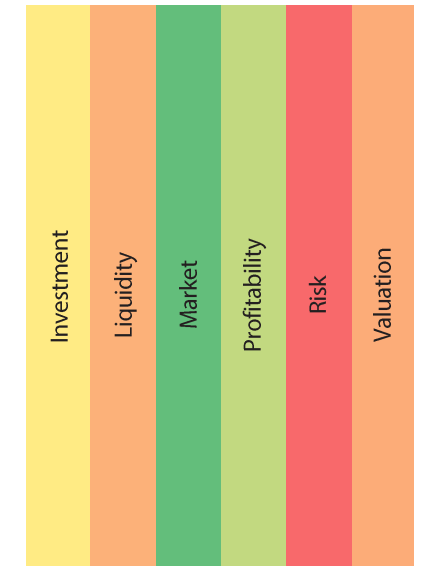
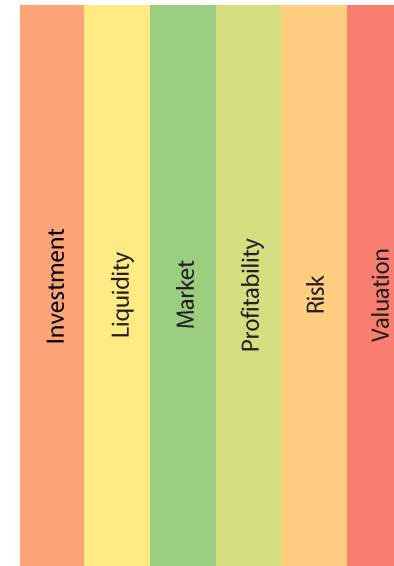
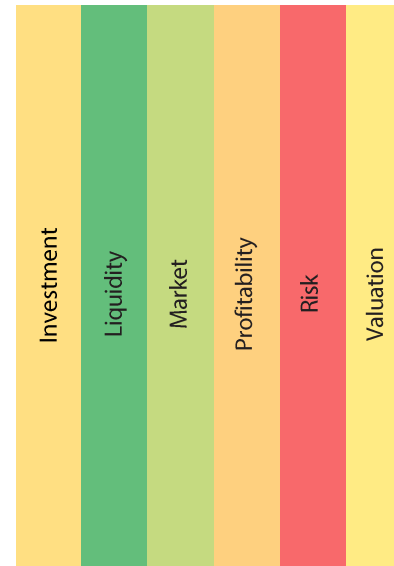
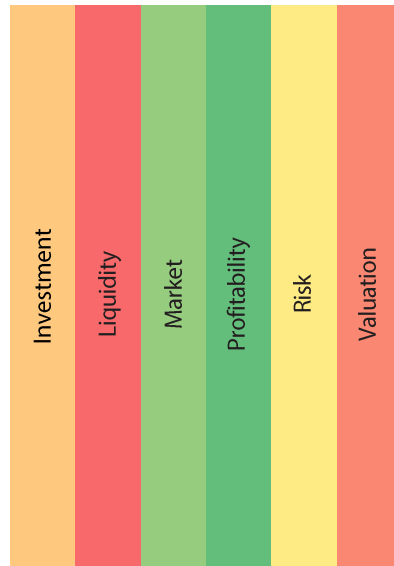
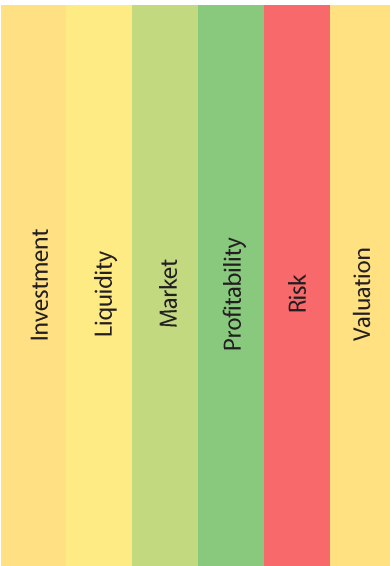
Distress ranking	Index value	YoY trend
6	-2.7	↓ -1.5 Aug 23

Distress ranking	Index value	YoY trend
7	-2.7	↓ -2.0 Aug 23

Distress ranking	Index value	YoY trend
8	-3.0	↑ -4.2 Aug 23

Distress ranking	Index value	YoY trend
9	-3.1	↑ -3.5 Aug 23

Distress ranking	Index value	YoY trend
10	-6.5	↓ -2.4 Aug 23



# INDUSTRY ANALYSIS

## Real Estate

Real estate remains the most distressed sector, but levels have eased compared to the previous quarter and are lower than the previous year. On a rolling 3-month basis, distress is at its lowest level since January 2023. A slight improvement across investment and profitability metrics has helped contribute to the overall improvement. However, highly leveraged companies struggling to refinance their debt in a high-interest-rate environment remains a cause for concern.



## Healthcare

The healthcare sector has dropped to the third most distressed sector, from the second in the previous quarter. While conditions eased across a range of drivers, the sector is dealing with ongoing challenges in managing cash flow, and while liquidity has improved on last year, weaker investment sentiment continues to weigh on overall performance.



## Industrials

The industrials sector has seen a sharp increase in distress, moving up from fourth to second in the ranking. Investment pressures are particularly severe, contributing significantly to the overall rise in distress. The sector's increase in distress reflects an environment of rising capital costs and a reduction in new project commitments, reflecting the broader slowdown in global demand.



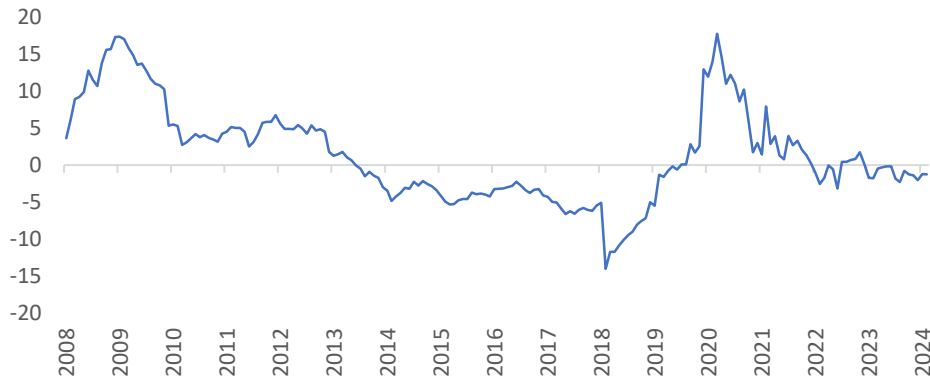
## Retail and Consumer Goods

Retail and consumer goods continues to see rising distress, as households struggle with higher interest rates, which are curbing consumer spending. Levels of distress have risen on the previous quarter and on the previous year. The sector is facing challenges from liquidity pressures, compounded by higher borrowing costs, while profitability remains low, and the overall outlook remains uncertain.



## ✈️ Travel, Leisure and Hospitality

Distress in the travel sector has risen moderately, with the sector ranked fifth in the latest period. Support from profitability and liquidity has helped ease some of the pressure. However, weaker investment metrics remains a concern, but strong demand for both business and leisure travel has kept distress below the long-term average.



## 🛢️ Oil and Gas

The oil and gas sector has seen a marginal fall in distress, maintaining its position as one of the least distressed industries. While global demand has slowed, oil prices continue to maintain robust and the sector is benefitting from a more positive global outlook compared with the previous year.



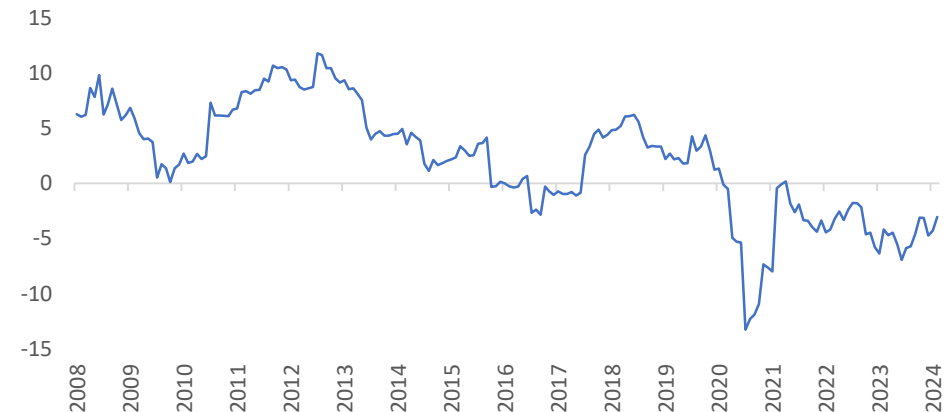
## 🏛️ Financial Services

While distress in the financial services sector remains below the long-run average, it has risen on the previous quarter to its highest level this year. Rising interest rates have helped the sector by boosting margins, while liquidity and balance sheets have remained strong.



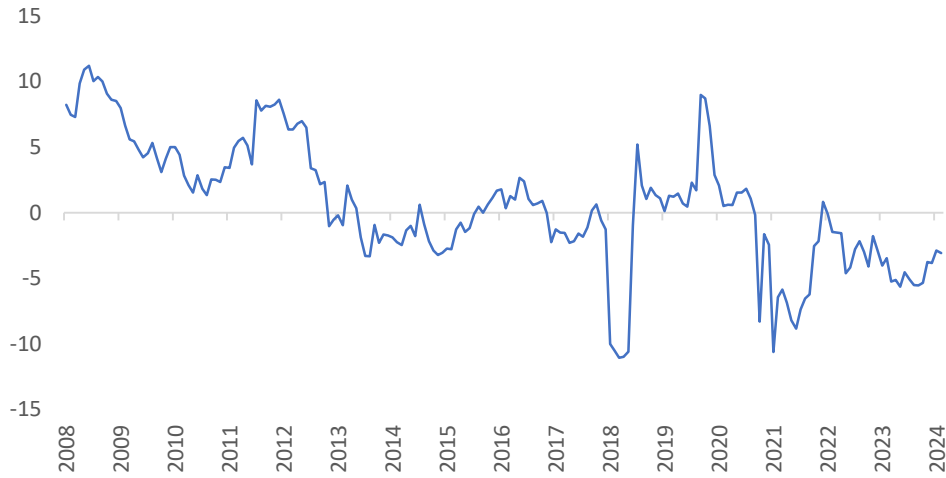
## 🏗️ Infrastructure, Utilities and Power

Infrastructure and utilities have experienced a moderate easing in distress, moving from eighth to seventh in the ranking. The sector remains under pressure from risk concerns, but investment, liquidity and market conditions appear robust. As a vital part of the economy, the sector has demonstrated resilience, supported by steady demand for essential services.



## Technology, Media and Telecoms

The technology sector continues to show resilience, with distress levels remaining below long-term averages. Market support and profitability metrics continue to support businesses operating in the industry, keeping distress levels below the long-run average. The sector remains an outperformer compared to more capital-intensive industries.



## Commodities and Natural Resources

Commodities remain the least distressed sector, although overall levels of distress deteriorated slightly from the previous quarter. Profitability, market conditions and strong liquidity positions have all helped the sector maintain its resilience. Despite ongoing risks in the global economy, the commodities sector has shown strength and stability.

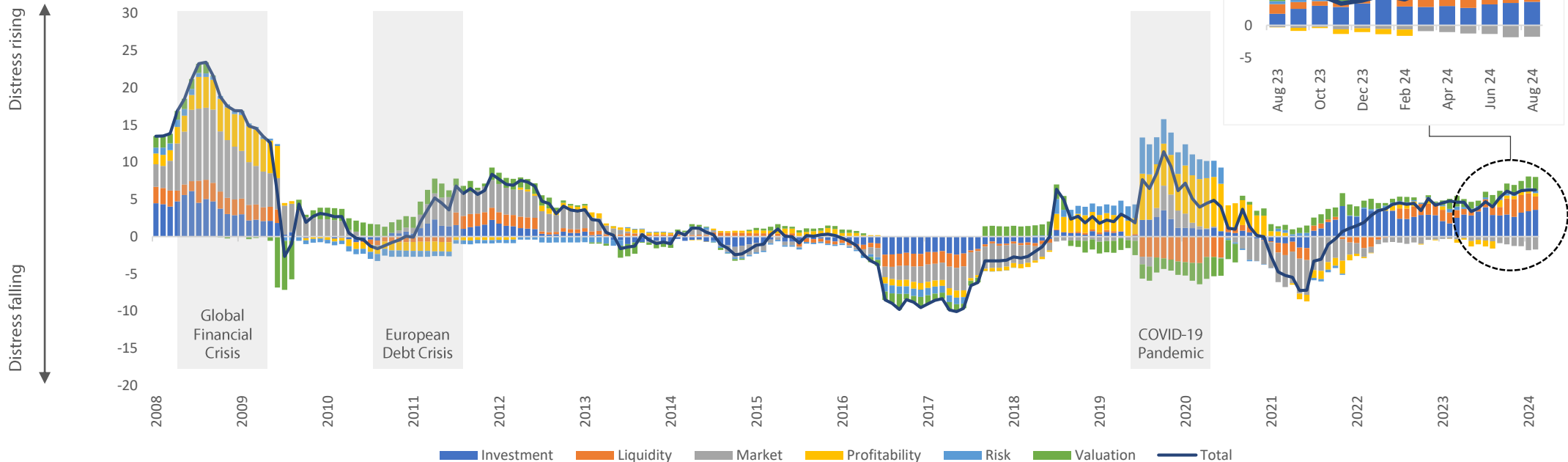


# Germany Distress Index

Distress Ranking	Aug 2024	QoQ Trend	YoY Trend
1	+6.3	↑ +5.7 May 24	↑ +4.8 Aug 23

- German corporates continue to face significant levels of distress, with conditions worsening over the last quarter and higher than the previous year. Levels of corporate distress are now at their highest level since July 2020.
- Key drivers of this rise include investment and liquidity, as companies remain hesitant to deploy capital and struggle with tighter financing conditions against a backdrop of weaker demand. Industrial output has been particularly weak, with a sharper-than-expected fall in July 2024 (-2.4%) according to government statistics. Analysts polled by Reuters had predicted a 0.3% fall. The fall was largely driven by a decline in global demand and the struggles of energy-intensive sectors like manufacturing and particularly automotive.
- Overall, the German economy contracted in the second quarter, sparking fears of another recession as it lagged other major European economies. While the European Union grew by 0.3% during the same period, Germany posted fall of 0.1% on the previous quarter.

- Profitability remains a major concern, particularly in manufacturing, where high energy costs and reduced export demand have eroded margins. Domestic demand remains subdued, falling 0.2% in the latest period, as declining consumer spending exacerbates the economic downturn.
- Despite some signs of relief—such as easing inflation and expected wage growth—the overall outlook remains challenging. While market conditions have shown slight improvement, this has done little to offset the challenges posed by weak investment and tightening liquidity.
- Germany remains the most distressed market across Europe. Persistent challenges in investment, liquidity, and profitability are unlikely to ease in the near term, with only a gradual recovery anticipated in 2025 as the broader economic environment stabilises.

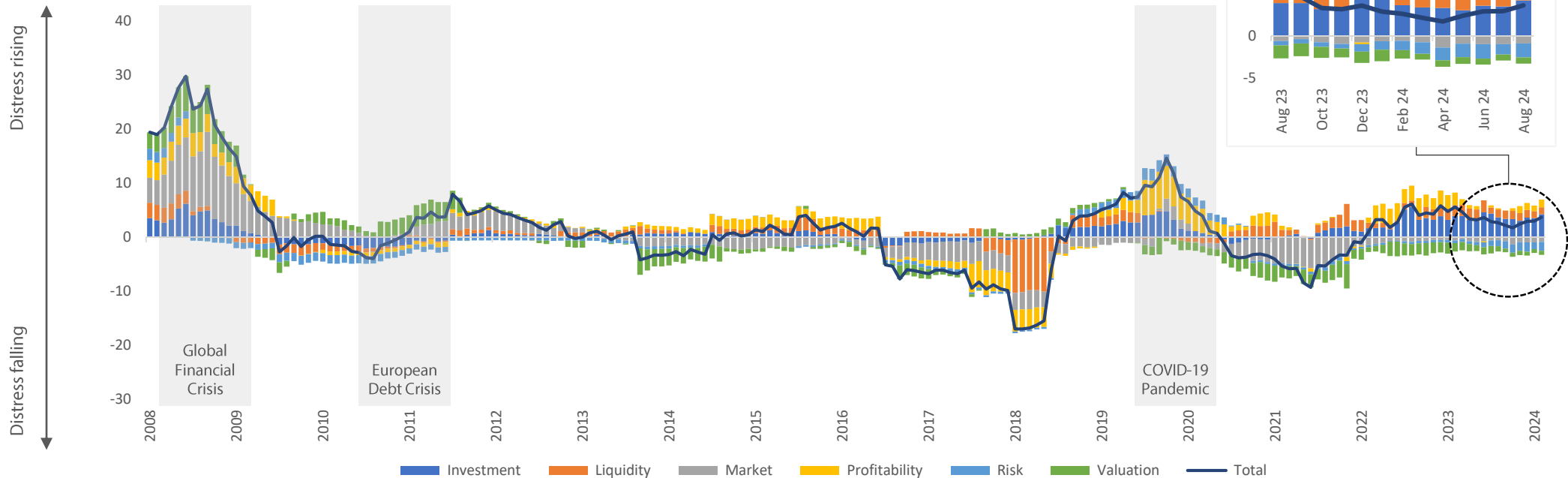


# United Kingdom Distress Index

Distress Ranking	Aug 2024	QoQ Trend	YoY Trend
2	+3.7	↑ +2.4 May 24	↓ +5.6 Aug 23

- In the UK, corporate distress has risen slightly over the last quarter, driven primarily by challenges in investment, liquidity and profitability. The UK remains the second most distressed market in the WEDI, and while distress remains lower than the previous year, it has risen on the previous quarter and resides at the highest level in 2024.
- Concerns around investment have driven distress higher since the beginning of the year, hindered by uncertainty around the general election, and now the potential impact caused by fiscal tightening.
- While GDP rose strongly in the second quarter (+0.6%), the latest monthly data for June and July reported that there was no growth in the economy, signalling a slow-down in the third quarter.
- The ongoing high interest rate environment continues to strain businesses, particularly in their ability to refinance debt or pursue new investments.

- The Bank of England held its interest rate at 5% in September, but signalled potential cuts in the coming months, which could restore some business confidence.
- However, consumer confidence has deteriorated significantly, falling back to levels last seen in January, driven by fears of a "painful" upcoming Budget and ongoing concerns about household finances.
- Overall, the UK's economic outlook remains mixed. While profitability pressures remain significant, easing inflation and potential rate cuts offer some hope of recovery in 2025. However, the upcoming Budget, combined with consumer caution, could pose risks to a more sustained improvement in corporate health in the short term.



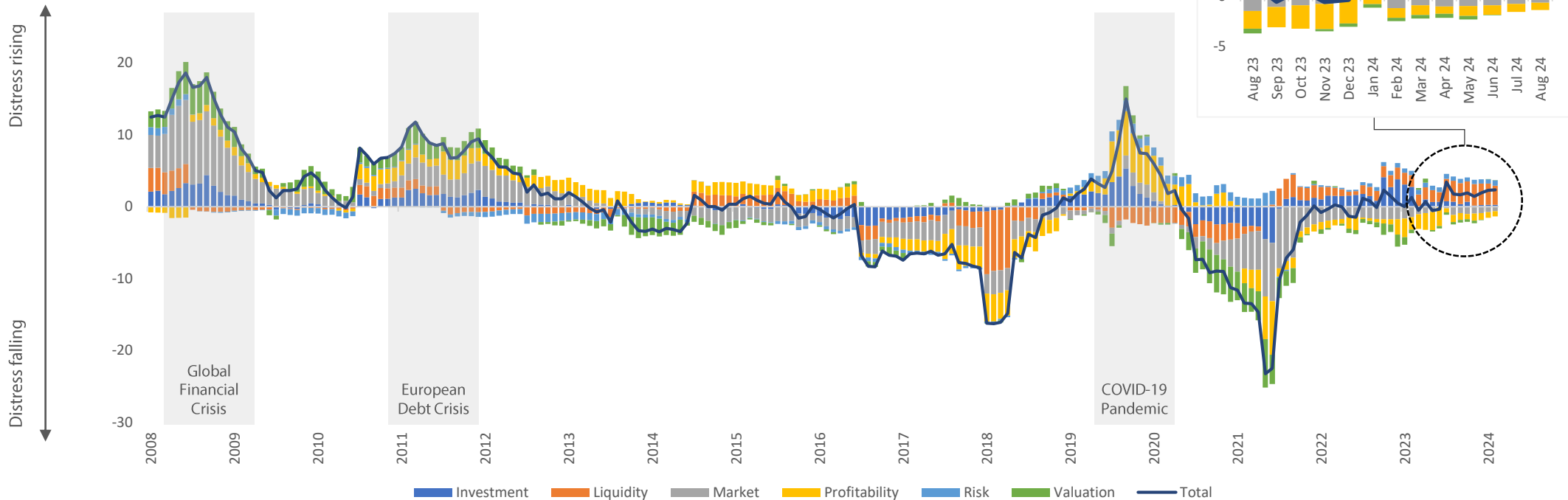


# France Distress Index

Distress Ranking	Aug 2024	QoQ Trend	YoY Trend
3	+2.4	↑ +1.4 May 24	↑ +1.3 Aug 23

- Distress levels in France remain above the long-run average, rising on the previous quarter and higher than the previous year. Distress levels are now the highest since January 2024.
- The main sources of distress in France continue to be liquidity pressures, a cautious risk appetite, and weaker investment metrics, which have shown some stability recently.
- Higher borrowing costs, fragile business confidence and lacklustre economic growth are all undermining business resilience against a backdrop of political turbulence.
- The French economy has shown modest improvement, with GDP rising by 0.2% in the most recent quarter. This slight growth was driven by increased government spending and positive contributions from net trade, with exports up 0.4% following a 0.6% rise in Q1 2024 (INSEE).

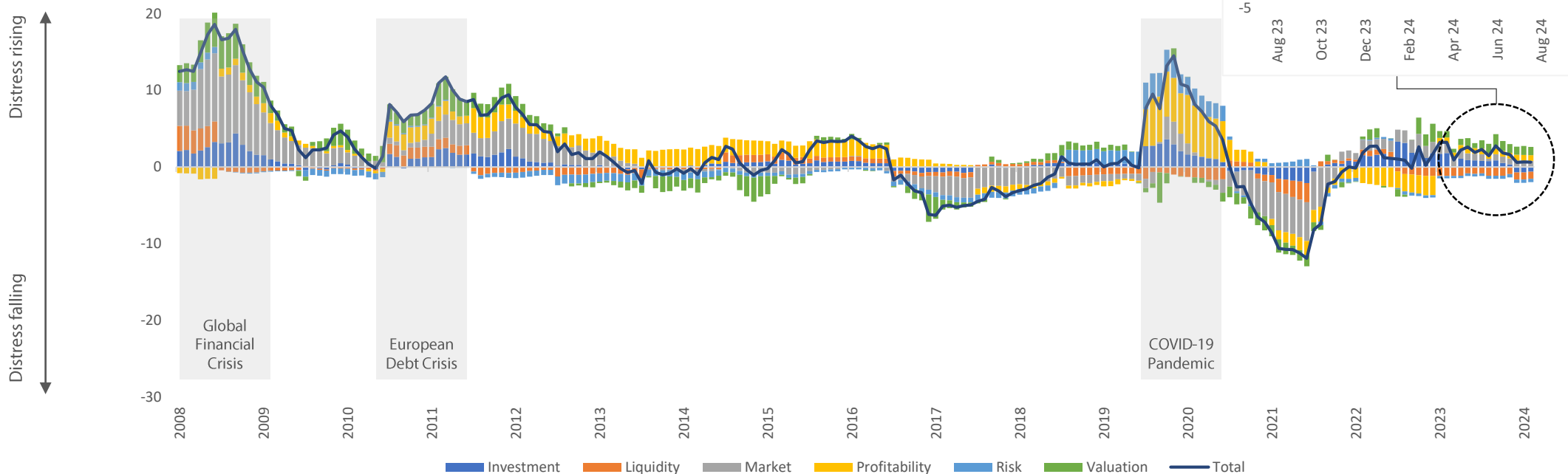
- However, challenges persist in manufacturing, as the sector remains in contraction according to the latest PMI. The data showed the sharpest contraction since January, as new orders decreased at the fastest pace since May 2020, while export orders sank to its fastest for three months.
- Looking ahead, France is expected to experience gradual economic recovery, with GDP projected to grow by 0.9% in 2024 and 1.3% in 2025, slightly behind the Eurozone average (IMF).



Distress Ranking	Aug 2024	QoQ Trend	YoY Trend
4	+0.6	↓ +1.6 May 24	↓ +3.2 Aug 23

# Spain and Italy Distress Index

- Corporates in Italy and Spain continue to experience levels of distress above the long-run average, though they remain the least distressed market in the WEDI. On a rolling 3-month basis, distress is at the lowest level in 16 months.
- Interestingly, Spain/Italy is the only market to report investment metrics supporting lower levels of distress, which is likely to reflect the ongoing strength in the underlying economy, particularly in Spain, and associated business confidence.
- However, areas such as profitability, valuation and markets have all contributed to overall levels of distress, keeping it above the long-run average.
- In Spain, GDP growth continues to exceed expectations, expanding by 0.8% in Q2 2024, bolstered by strong household consumption and a recovery in exports.
- Key sectors, including manufacturing, construction, and services, have all contributed to Spain's robust economic performance. Spain remains one of the Eurozone's strongest performers, with the IMF projecting growth of 2.4% for 2024, well above the Eurozone average.
- Italy's growth, while more subdued, remains stable. The latest quarter saw GDP rise by 0.2%, with easing energy prices and a gradual improvement in domestic demand helping mitigate some of the pressures facing Italian businesses. The IMF forecasts Italy's growth at 0.7% for 2024, positioning it ahead of the UK and Germany, but trailing behind Spain.



## KEY RESTRUCTURING CONTACTS

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### London



Andrew Wilkinson  
Partner  
+44 20 7903 1068  
andrew.wilkinson@weil.com



Neil Devaney  
Partner  
+44 20 7903 1199  
neil.devaney@weil.com



Matt Benson  
Partner  
+44 20 7903 1009  
matt.benson@weil.com



Jenny Davidson  
Partner  
+44 20 7903 1438  
jenny.davidson@weil.com



Lois Deasey  
Partner  
+44 20 7903 1702  
lois.deasey@weil.com



Mark Lawford  
Partner  
+44 20 7903 1050  
mark.lawford@weil.com



Gemma Sage  
Partner  
+44 20 7903 1419  
gemma.sage@weil.com

### Paris



Jean-Dominique  
Daudier de Cassini  
Partner  
+33 1 4421 9797  
jean-dominique.  
daudierdecassini@weil.com



Céline Domenget-  
Morin  
Partner  
+33 1 4421 9797  
celine.domenget-morin  
@weil.com



Gerhard Schmidt  
Partner  
+49 89 24243 101  
gerhard.schmidt@weil.com



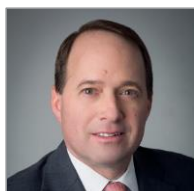
Britta Grauke  
Partner  
+49 69 21659 664  
britta.grauke@weil.com

### Germany

### U.S.



Matt Barr  
Partner  
+1 212 310 8010  
matt.barr@weil.com



Gary Holtzer  
Partner  
+1 212 310 8463  
gary.holtzer@weil.com



Ray Schrock  
Partner  
+1 212 310 8210  
ray.schrock@weil.com

### Asia



Kathleen Aka  
Partner  
+852 3476 9000  
kathleen.aka@weil.com