

Being resilient in these tough economic times is a necessity... practical steps for directors to consider in extra-ordinary times of financial distress!

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Prior to the World Health Organisation declaring COVID-19 a pandemic and the declaration by President Cyril Ramaphosa on Sunday 15 March 2020 of a national state of disaster in South Africa in terms of the Disaster Management Act 57 of 2002, South Africa's economy had already contracted in the last two quarters of 2019. As a result, not unexpectedly, on Friday 27 March 2020, the credit rating agency Moodys cut South Africa's sovereign credit rating to sub-investment grade, meaning that the country now has a "junk" rating status from all three major credit rating agencies. As a result of the downgrade, South Africa's government bonds will be excluded from the FTSE World Government Bond Index, and it will no doubt become more expensive to borrow money. In addition, within the first few months of this year, the International Monetary Fund (IMF) had reduced South Africa's growth forecast for 2020 to only 0.8% and for 2021 to 1.0%. There is no doubt that the ratings downgrade of South Africa will make trading conditions extremely challenging in the period ahead.

On 25 March 2020, final COVID-19 lockdown regulations were published restricting the movement of persons during the period of the lockdown and until 16 April 2020. The regulations restrict the movement of persons in South Africa and confines every person to his/her place of residence for the lockdown period, unless such person can demonstrate that they either provide or require an essential service as prescribed in the Regulations. Any person who contravenes the restriction regulations shall be guilty of a criminal offence.

There is no doubt that the effects of the lockdown on the South African economy and companies will be felt in the months ahead and probably for years to come. Save for designated essential service providers, the lockdown in particular shuts down all retail outlets, restaurants and fast food outlets, general service providers, and the travel, hospitality and airline industry. The inability to trade in this lockdown period leaves many companies and businesses unable to generate any revenue to meet their continued overhead costs, such as salaries and wages, rental obligations to landlords and the payment of public utilities (such as lights, water, electricity).

Tough economic times translate into hard decision making and where strong leadership at board level will become a necessity.

In these circumstances, directors need to be mindful of their responsibilities, duties and liabilities in terms of the Companies Act 71 of 2008 (the Act). Directors are required to take proactive steps in order to mitigate any losses that a company may face during these times, which may include implementing certain cost-cutting measures and taking legal advice where necessary. Failure by directors to take proactive steps may result in directors being held personally liable in terms of the Act (see Werksmans article on [COVID-19 Duties of Directors](#)).

Accordingly, directors, faced with the potential of financial distress, need to be resilient and must consider taking practical and effective steps to mitigate prejudice to the company caused by the impact of COVID-19. These include:

1. Consider implementing urgent measures which will have the effect of reducing costs. These may include, *inter alia*:
 - Reducing the size of your workforce/management through negotiated voluntary retrenchments;
 - Negotiating with suppliers of goods and services for extended credit terms and, if necessary, amendments to onerous terms and conditions;
 - Downsizing the size and scale of your business and its footprint. This might include negotiating a payment holiday with landlords or reducing the number of leased premises altogether;

- Negotiating with your bankers for increased limits on overdraft facilities and possible forbearance on outstanding loans (see further below);
 - Exploring Government Financial Aid programmes, in particular to SMEs such as the Solidarity Fund, employee relief schemes (UIF), corporate tax subsidies and employee tax incentives from SARS;
 - Establishing what relief is available from Credit Insurance policies;
 - Reducing spend on unnecessary expenses such as marketing and advertising;
 - Consideration of adjustments to monthly and annual budgets (revenue and expenses); and
 - Implementing cost saving policies across the board.
2. Consider discussing the financial position of the company with the company's bankers to assess how they may be of assistance. Most banks and financial institutions are well aware of and understand the tough economic circumstances that companies now find themselves in, especially given the economic impact that COVID-19 is having on businesses across the country. Banks generally are sympathetic to the difficult and challenging trading conditions that currently face companies and would usually, if taken into the company's confidence at the earliest possible opportunity, be willing to consider moratoriums on payment/service obligations of bank facilities.
3. Identify all of the company's major creditors and establish whether they would be open to discussing possible short-term payment "holidays" (or repayment plans that will take pressure off the cash flow constraints of the business). However, it is important to note that this option can potentially prejudice the company, as any admission of the company's inability to pay its debts will be grounds for a liquidation. Therefore, such discussions and communications must be handled with the utmost care and legal consideration.
4. If all else fails, speak to experienced turnaround specialists/attorneys who are skilled in restructuring and assisting companies during these difficult times. If an intervention is required as a last resort, the board will be advised, if it is appropriate, to file for [business rescue](#) (see the [Werksmans Business Rescue Toolkit](#)) or liquidation.

Difficult but informed decisions need to be made. The right decisions made by an informed board of directors may result in your business being able to survive these extraordinary times and further ensure that directors are not exposed to personal liability in terms of the Act.

South Africa and the world face unprecedented and very tough economic trading conditions. Many South African companies/businesses which appeared to be financially healthy a few months ago, now find themselves facing severe financial stress. How long these constraints will last is open for debate. Being pro-active, diligent and astutely aware of options available to struggling companies/businesses will become critical in the days and months ahead.



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