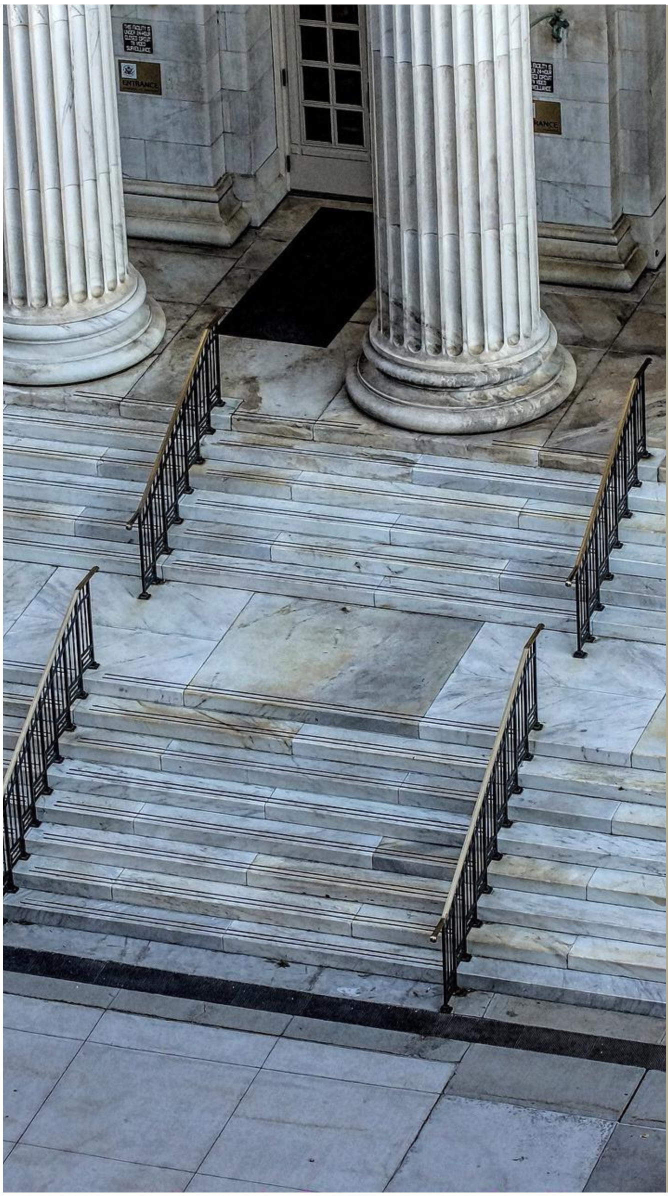
NEW CRISIS INDICATORS

Quick read by the Restructuring and Litigation Departments



SUMMARY

New crisis indicators developed by CNDCEC: 7 indexes enabling entrepreneurs to detect crisis early warnings quickly to prevent and timely address a company's insolvency.

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Legislative Decree No. 14 dated 12 January 2019 sets forth the new Italian Insolvency Code ('**IC**'), which enters into force on 14 August 2020 (except for some provisions which are already effective). Through the IC a set of early warning signals and prevention procedures are adopted, which aim to provide suitable tools to both foresee and forestall a company's financial distress.

In most cases, business crises can be avoided, but companies (and their management) are often unable to detect them in due time, as they flow from the economic and financial performances of the company. To prevent situations where a company crisis has to be addressed too late, Art. 13 of the IC provides the so-called "Crisis Early Warnings", a set of predictive parameters showing that a financial distress situation is foreseeable, so that it can be addressed by the management of the company in a timely fashion.

Consiglio Nazionale dei Dottori Commercialisti ed Esperti Contabili ('**CNDCEC**'), the Italian National Council of Certified Accountants, was appointed to develop these indexes, "in light of domestic and international best practices and based on each type of business according to the ISTAT classification" and is charged with the task of reviewing them on a three-year basis.

CNDCEC recently submitted a first draft with a hierarchical sequence of **7 parameters**. The first two indexes apply to all types of businesses, regardless of the business sector of the company. These are "Net Equity Value" and "Debt Service Coverage Ratio".

"Crises can be avoided; early warning signals need to be detected."

The First Two Indexes

1. NET EQUITY VALUE

According to the first early warning index, a financial crisis exists **when the net equity value is negative as a result of operating losses.** This condition may be superseded through a company's recapitalization and, therefore, the company may adopt measures which evidence a reconstitution of positive net equity value.

2. DEBT SERVICE COVERAGE RATIO ("DSCR")

The second early warning index by CNDCEC is a **6-month Debt Service Coverage Ratio lower than 1.** DSCR requires that there is evidence of debt sustainability over a period of at least 6 months. Specifically, DSCR is calculated as the ratio of free cash flows available to settle debts expiring in the following 6 months. Thus, if the value of DSCR is higher than 1, the company is in a position to face debts that will become due in the following 6 months. Otherwise, if the value of DSCR is lower than 1, a financial crisis situation may occur in the short term.

The CNDCEC developed **5 additional early warning** indexes in the event that the first two above are not appropriate to disclose the crisis of the company: for instance, where the net asset value is positive or the DSCR is not useful because the company generates unreliable data. Currently, not all companies, especially SMEs, are in fact able to provide a 6-month cash flow forecast.

These additional indexes have a subsidiary role compared with the "net equity value" and the "debt service coverage ratio" parameters and, unlike these two, they were developed by setting different thresholds based on the economic sector in which the company operates, as stated in the following table.

SECTOR	Financial debts / Sales	Net Equity / Total debts	Short-term assets / Short-term liabilities	Cash flow / assets	Tax and Soc. Sec. Debt/ Assets
Agriculture, forestry and fishing	2,8%	9,4%	92,1%	0,3%	5,6%
Mining, manufacturing, gas/energy production	3,0%	7,6%	93,7%	0,5%	4,9%
Water supply, sewerage systems, waste; gas/energy transmission	2,6%	6,7%	84,2%	1,9%	6,5%
Building construction	3,8%	4,9%	108,0%	0,4%	3,8%
Civil engineering, specialized construction	2,8%	5,3%	101,1%	1,4%	5,3%
Sale of motor vehicles, wholesale, gas/energy distribution	2,1%	6,3%	101,4%	0,6%	2,9%
Retail sales, restaurants and bars	1,5%	4,2%	89,8%	1,0%	7,8%
Transport and storage, hotels	1,5%	4,2%	86,0%	1,4%	10,2%
Services to business	1,8%	5,2%	95,4%	1,7%	11,9%
Services to individuals	2,7%	2,3%	69,8%	0,5%	14,6%

To ensure a more accurate forecast of a financial distress situation, all five indicators above should be exceeded at a given time, and not one or more of them only.

Additional Early Warning Indexes

3. FINANCIAL DEBTS TO SALES INDEX

This parameter measures the ratio of financial debts to sales of a company and, according to CNDCEC, it must not exceed values ranging from 1.5% to 3.8%, depending on the business sector of the company. It gives a generic analysis on the sustainability of the company's financial debts.

4. NET EQUITY TO TOTAL DEBT INDEX

This indicator measures the ratio of net equity value to total debt of the company and it must not be lower than certain threshold values ranging from 2.3% to 9.4%, based on the sector of the company. The more the company is capitalized with its own equity, the less it is considered as facing insolvency risks.

5. CURRENT RATIO INDEX

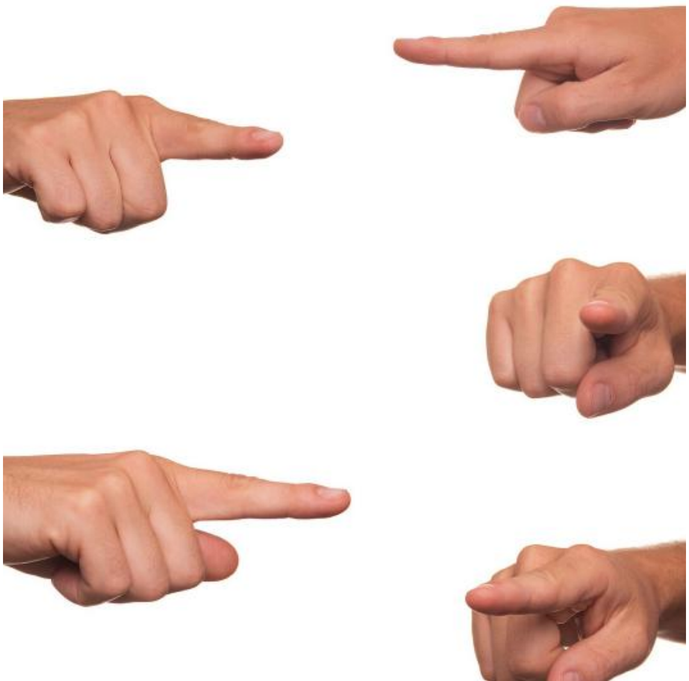
This index measures the ratio of short-term assets to short-term liabilities and, thus, the imbalance of the company's working capital. It must not be lower than threshold values ranging from 69.8% to 108%. The lower the percentage, the lower the amount of outstanding short-term receivables that can cover suppliers and other short-term liabilities.

6. CASH FLOW TO TOTAL ASSETS INDEX

This index is based on the ratio of cash flow to total assets of the company. It reflects the value of the return of the company in connection with capital resources invested in assets for its benefit. According to the CNDCEC, it must not be lower than threshold values ranging from a minimum of 0.3% to a maximum of 1.9%, based on the reference sector.

7. INDEX OF SOCIAL SECURITY AND TAX DEBTS

This indicator measures the ratio of social security and tax debts to the company's assets. This parameter must be lower than the threshold values set by CNDCEC which range from 2.9% to 14.6% based on the business sector to which the company belongs.



Mandatory Internal Controls and Early Warning Analysis

A new duty on the entrepreneur (and on the management and controlling bodies of the company) is specified by the IC: to implement internal procedures aimed at timely and rapidly detecting financial distress and the threat of the loss of the company as a going concern, which applies irrespective of its actual financial and economic situation.

Therefore, all corporate bodies must adopt such new internal procedures and checks to ensure that the early warning indexes are constantly monitored and that a financial crisis does not overtake a company.

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