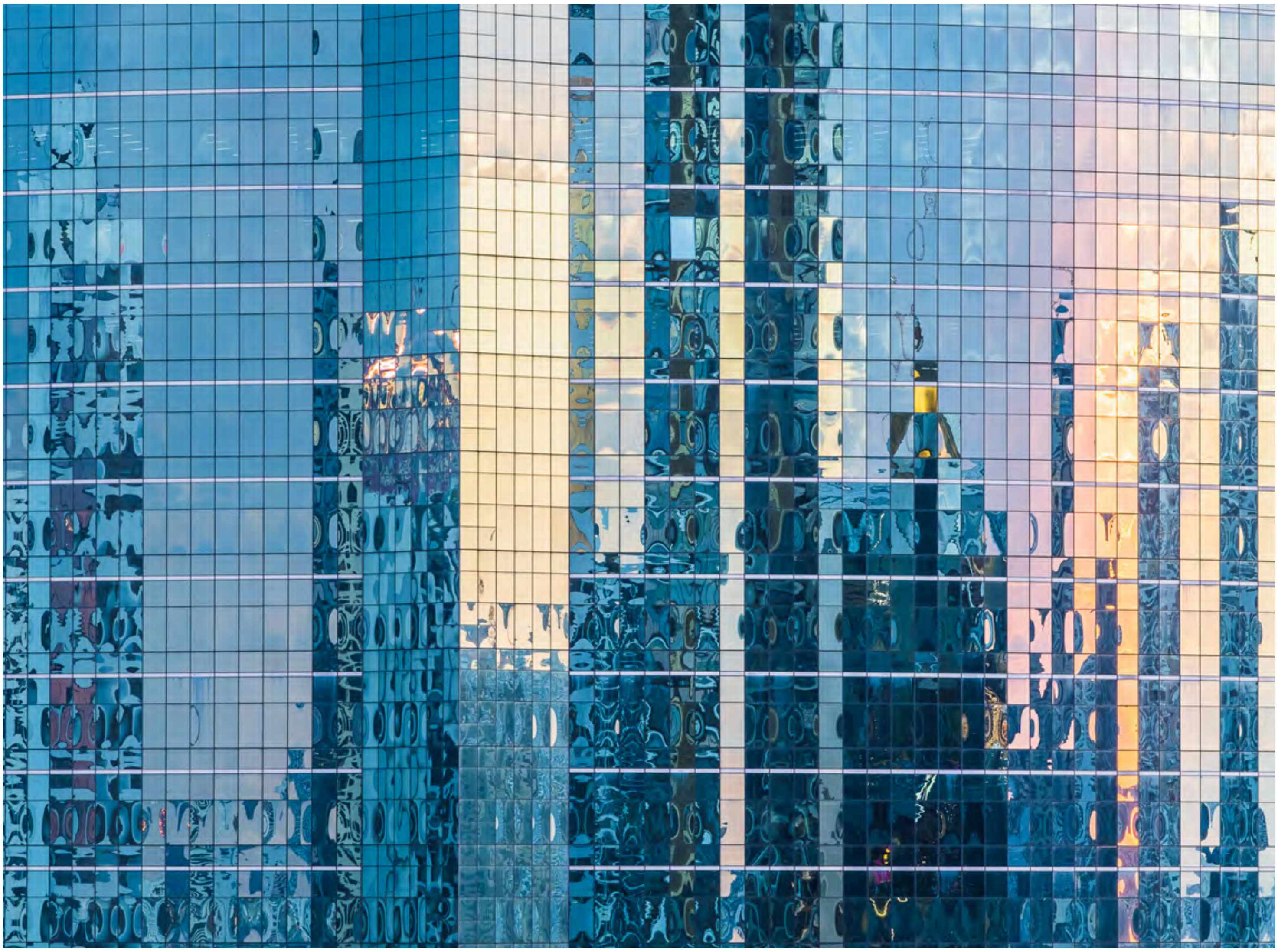
AN FTI CONSULTING REPORT – PUBLISHED MARCH 2025

Special Situations M&A Market Snapshot

Reflections on 2024 and Outlook for 2025



EXPERTS WITH IMPACT™

FTI CONSULTING™

Introduction

With geopolitical turbulence and economic slowdown, 2024 saw an increase in special situations activity, but still below the expectations for distressed M&A opportunities from investors. Whilst 2025 is likely to bring some degree of geopolitical certainty, sentiment has not yet tipped into optimism. In our latest Special Situations M&A Market Snapshot, we share the views of UK-based investors primarily focussed on alternative investments in the mid-market, alongside market analysis from FTI Consulting's expert M&A advisors on UK distressed deal activity for the year ahead.

Key Themes

— The majority of investors we spoke to saw an increase in special situations opportunities in 2024, with a slight lift in the second half of the year. This trend correlates with the wider economic slowdown in H2, despite better-than-expected growth in H1.

— Whilst there was an increase, the volume of distressed M&A opportunities failed to meet investors' expectations, given the economic and political turbulence experienced in 2024. Some investors also noted that many of the opportunities were simply just too distressed, without viable turnaround plans.

— Sectors heavily exposed to discretionary spend offered the most opportunities in 2024, with investors highlighting higher levels of opportunity in automotives, retail and consumer goods. The cost-of-living crisis continues to squeeze many customers, despite the stabilisation of inflation.

— Looking into 2025, most respondents are not optimistic about the outlook for the UK economy, and many expect to increase capital deployed across special situations opportunities.

In 2024, we have been involved in a diverse range of situations and sectors, including pharmaceuticals, hospitality, retail, energy, transport infrastructure and telecommunications. Triggers across these situations have been equally diverse — ranging from withdrawals of shareholder support, lenders seeking to reduce exposure to higher risk sectors and shifts in demand driven by external factors. Around four years after the Covid-19 lockdowns and three years after the onset of the Russia-Ukraine war, the impact on consumer behaviour and input costs remains a significant issue for many companies.

2024 in Review

Insights from investors indicated elevated levels of distressed M&A in 2024, particularly driven by unsustainable debt levels and failed refinancings. Echoing the themes of previous years, there is an indication that the levels of distressed deal activity remained far below special situations investors' expectations in 2024.

In our survey conducted in December 2023, mid-market special situations investors had anticipated increased levels of distressed deal activity in 2024, expected as a result of the UK's economic contraction in the second half of 2023. Defying these predictions, the UK exceeded economic growth targets in the first half of 2024, though growth had stagnated by the end of the year — a tale of two halves. Overall, 2024 was split in terms of meeting and challenging investor expectations.

Our discussions with investors indicated that on balance they saw an increase in distressed M&A opportunities in 2024, particularly in the second half of the year. However, the volume and quality of distressed deal activity remained below expectations yet again. One reason for this that investors highlighted was because many of the deals available were of low quality or brought to market too late to represent a feasible investment for financial investors, in contrast to opportunistic trade buyers.

Distressed Deal Drivers

Insights from investors illustrated expectations of an increase in distressed deal activity to be driven by cost inflation and changes in customer demand, alongside unsustainable debt levels and failed refinancing. These factors were apparent in the high-profile sales in the retail sector, including The Body Shop and Carpetright.

The Body Shop was bought out of administration in September 2024 by Auréa Group. Working capital challenges, unsustainable lease liabilities and debt levels drove the distress and finally insolvency.[1]

Carpetright was bought by trade-buyer, Tapi in July 2024 in a prepack transaction, following a reduction in customer demand and increased competition, as well as supply chain and input cost challenges. Ultimately, insufficient working capital and challenges in negotiating with key creditors including HMRC, triggered the need for a sale.[2]

Despite financing factors, we noted several instances of sector-specific distress, triggered typically by high and rising capex or input costs.

- In 2024, FTI Consulting supported as joint administrators the $295 million sale of LumiraDx Group's Point of Care Technology Business. The business was sold via prepack to Roche Diagnostics following regulatory clearances. The reduction in demand for LumiraDx's products post-Covid-19 resulted in significant excess capacity and a drop in revenue, making it difficult to service the high cost base.[3]
- TriRx Speke Ltd, one of the UK's leading sites for fermentation-derived products, faced immediate closure, challenges were driven by energy price increases and surplus capacity at the plant. These factors made profitability difficult to achieve and eventually caused the business to fail. Once Administrators from FTI Consulting were appointed, the business was traded for approximately three months, after which, Elanco Animal Health purchased the business, acquiring the facility and related assets, allowing the business to continue to trade, preserving jobs and ensuring the continued supply of its important pharmaceutical products.[4]

— Spring Fibre was sold via prepack to Harmony Networks in November 2024. Given the rising build costs and pre-revenue nature of the business, key investors withdrew support from the company.[5]

Macroeconomy: Impact on Distress

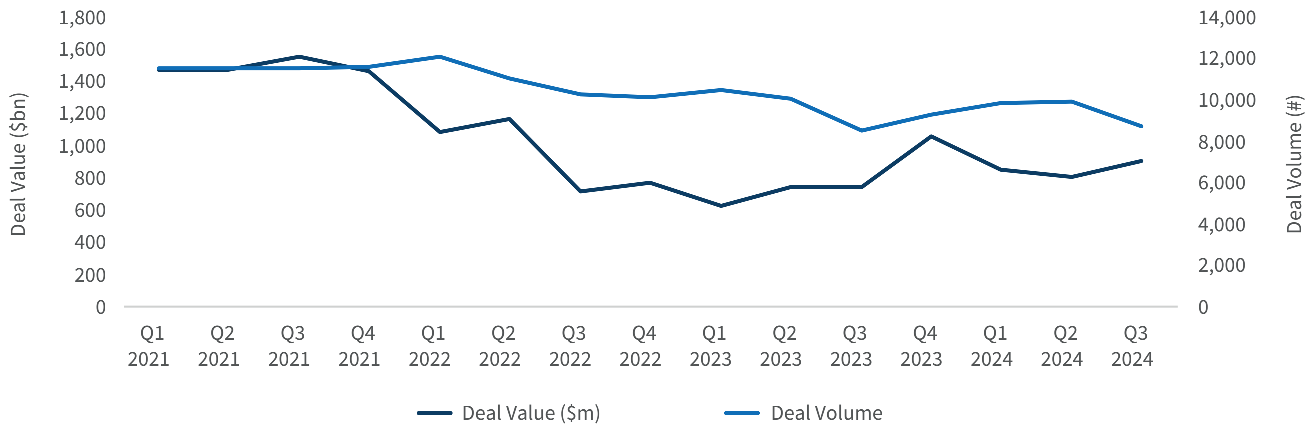
Over 2024, the UK economy began to stabilise, albeit at lower growth rates and with political shifts due to a change in government. Following a significant period of elevated inflation and interest rates, which were at their highest since 2008, inflation fell back to the Bank of England's target 2% in May 2024. Consequently, interest rates were reduced to 5% in August and then 4.75% in November. Whilst slightly lower rates will provide an easing of the interest burden on leveraged companies, rates are still materially higher than during the 2010-2019 period when large amounts of private capital across debt and equity were invested.

With an early election called in May for July 2024, political uncertainty was mitigated to some extent with all polls leaning towards a Labour government and no indications of a hung parliament. However, the Labour Autumn Budget changed the landscape for many UK businesses, which may now face higher staff costs due to increased National Insurance contributions.

For further reading, take a look at our detailed analysis of the **Autumn Budget 2024**.

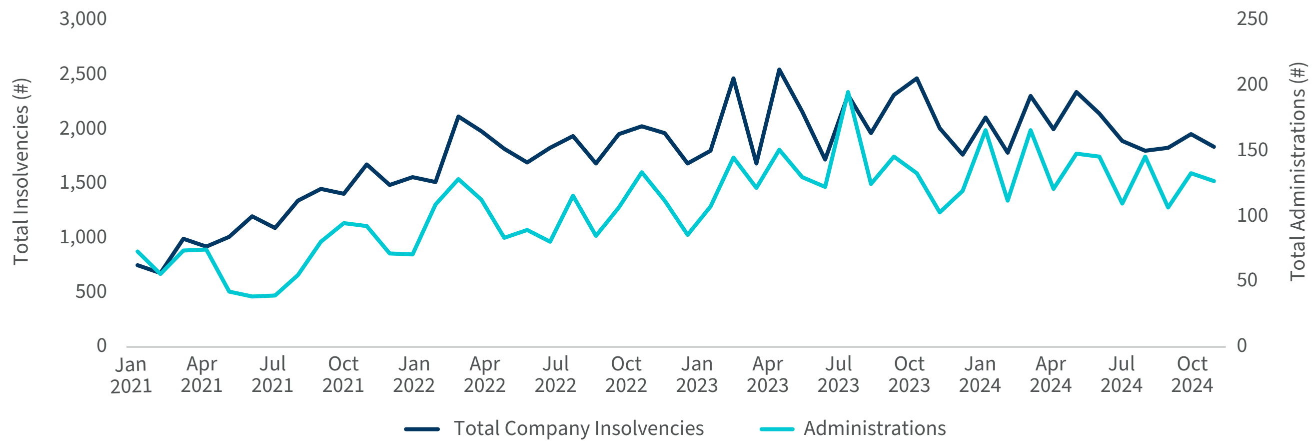
Despite these domestic headwinds, the UK appeared to buck global trends in overall deal activity. While global deal volumes decreased by around 3% in the 12 months to September 2024, compared to the same period in 2023, UK deal volumes increased by 11%. Furthermore, increases in UK deal volumes far exceeded the global rate — at 68% and 26% respectively.[6]

Figure 1: Decline in Overall Deal Volume, Despite Recovery in Deal Value



Data sourced from White & Case, "M&A Explorer", February 2025, https://mergers.whitecase.com/

Figure 2: Steady Rise in UK Insolvencies and Administrations



Data sourced from GOV.UK, "Company insolvency statistics releases", January 2025, https://www.gov.uk/government/collections/company-insolvency-statistics-releases

At the far end of the distressed spectrum, insolvencies in the UK have risen steadily since January 2021. Although total insolvencies in 2024 were 5% lower than 2023 levels, 2023 had the highest levels of total company insolvencies since 1993 — so this 5% drop is still a significant number in comparison to previous decades. It is worth noting that a significant overall increase in the number of registered companies is likely also a contributing factor.

Despite the increase in insolvencies, the number of administrations remained broadly in line with previous year's total.[7] More commonly associated with delivering distressed prepack deals to connected or third parties, administrations tend to correlate to deal activity. The increase in alternate insolvency procedures, such as compulsory liquidations, also suggests higher levels of activity among smaller companies which lack either the turnaround prospects or the funding of larger businesses. However, as noted by investors, many companies are going past the point of a viable rescue before decisive actions are taken. In our experience, many companies are struggling to reach agreements for prepack deals, largely as a result of inflexibility of investment in the required time frame, driven by impending liquidity crises.

Sector Specific Situations

As our analysis identified, the automotive and retail sectors, as well as the wider consumer goods and construction sectors, are the key areas for distressed deal activity in 2025. As the sectors most exposed to discretionary spend, it is no surprise that they have been most severely impacted by the continued cost of living crisis, particularly those operating on low margins which face the further threat of rising input costs.

Automotive: In the automotive sector a number of opportunities have been driven in part by the 'motor finance crisis', with many lenders considering exiting the industry as a result of the FCA investigations into car dealership interest payments announced in January 2024.[8] The resulting increased cost of motor finance squeezes many car dealerships that do not wholly pass these increased costs to customers. Alongside heightened supply chain costs as a result of increased oil prices, shipping and labour costs, and cost of living pressures, this has created a cocktail of distress in the sector and we expect to see further challenges throughout 2025.

Retail and Consumer Goods: The well-documented decline of the UK high street has been further exacerbated by the reduction in disposable income of consumers and increasing competition, particularly from online-only fast fashion businesses gaining access to the market as a result of innovations within the sector reducing barriers to entry. In 2024, we have seen consumers changing the way they shop, with the growth of online marketplaces and pop-up digital-first stores harnessing social media, as well as the rise of rental fashion. With many traditional retail businesses relying on cheap, covenant-lite financing to tide them over since Covid-19, the maturities and refinancing requirements coming in 2025 and 2026 pose an existential threat to many businesses, with stakeholders making difficult decisions regarding the future viability of their company.

For further reading, see our detailed summary of challenges across Europe: The Perfect Storm on the High Street.

We expect further challenges in these sectors in particular, with many companies seeming to delay taking decisive action until there is an imminent liquidity requirement.

The economic challenges impacting private equity's ability to raise funds have also persisted, with the many investors who attempted to raise funds in 2024 noting that it was just as difficult in 2024 as in previous years. Many special situations investors, particularly in the mid-market space, noted a lack of quality opportunities inhibiting the ability to balance other, more risky investments.

2025 Outlook

Special situations investors continue to hold their breath, despite the persistent economic turbulence. Nonetheless we continue to expect an increase in special situations opportunities – as with previous years – due to economic and financial market conditions.

With many noting a lack of optimism for the UK economy in 2025, the majority of investors we spoke to expect to deploy more capital than in 2024. While the UK economy seems to be stabilising following a period of uncertainty, indicated by lower inflation and interest rates, this appears to be precarious given the lack of demonstrable economic growth through 2024.

Economic Expectations

— Despite inflation rates realigning with the Bank of England's 2% target in May 2024, a slight increase is expected before stabilising at 2% again in late 2025 — this fluctuation is driven predominantly by global uncertainty, rising energy costs and wage increases.

— While the Bank of England has stated a gradual reduction in interest rates, the risk of hikes in relation to external economic shocks, such as ongoing global conflicts, remains.[9]

— With stagnant 0% GDP growth in the final quarter of 2024, the OECD forecasts 1.7% real GDP growth for the UK over 2025, exceeding the estimate for the Eurozone of 1.3% but significantly lagging the US forecasted economic growth of 2.4%.[10] The lower growth rates expose the continued fragility of the UK economy in comparison to the United States.

— Unemployment is forecast to reduce to 4.1% in 2025, remaining roughly at that level for the next five years. Higher levels of employment are expected to continue to drive up wages, applying further pressure on companies and their ability to retain staff, as job vacancies remain high — particularly in key sectors such as retail and industrials.[11]

— The new Labour government committed to maintaining the current levels and fundamental of corporation tax. While this provides an element of certainty, the incoming tax changes elsewhere, such as increases in employers' National Insurance Contributions, may significantly change many businesses' cost base from April 2025 — particularly for those in the mid-market space. Anecdotally, investors are already suggesting many of the urgent opportunities seen at the end of 2024 were predominantly among the businesses most impacted by the Autumn Budget.

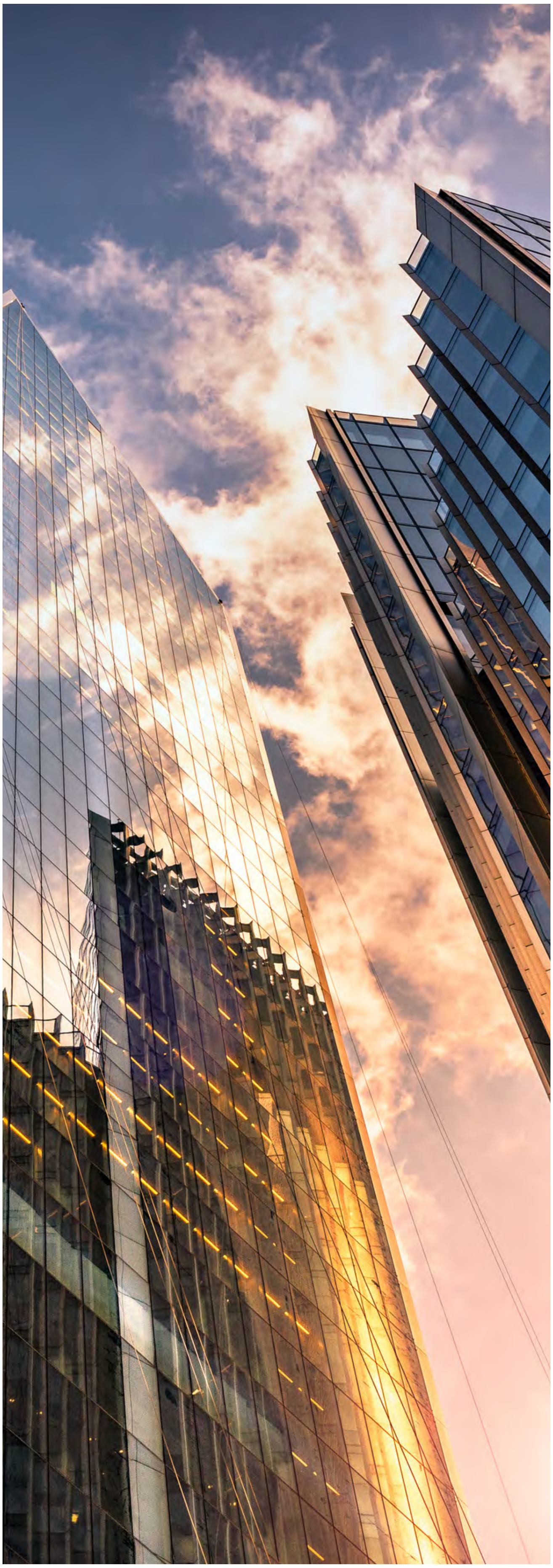
Anticipated Areas of Distress

Input from investors indicated continued interest in automotives and retail opportunities in particular but also highlighted industrial and construction as key sectors to watch. Construction continues to face significant headwinds, heavily reliant on low-cost labour and government policies, while facing significant exposures to supply chain fragility and input costs with sizeable lead times.

Opportunities are expected to be driven by the same key factors as in 2024: inability to raise funds or refinance existing debt and unsustainable debt servicing costs. However, investors also highlighted continued inflationary pressures impacting input costs despite inflation easing, noting that price rises are not evenly spread and observing a particular volatility in energy prices.

It would be challenging to look to the future without considering the impact of artificial intelligence ("AI"), which we expect to become even more ubiquitous in 2025. The frenzy surrounding AI has boosted interest, investment and valuations as its usage in our everyday life grows – though the risks from inflated expectations remain As noted in FTI Consulting's Survey, AI Radar for Private Equity, investors have highlighted the anticipated impact of AI on top line growth as a key lever, with many seeking to utilize AI for value creation in their portfolio companies. We have also seen the increased application of AI among both investors and advisors in establishing investment opportunities – but the level of human judgement required to navigate distressed companies' complex issues may, for now, exceed the capabilities of AI.

Overall, we expect a gradual increase in distressed deal activity, concentrated in certain sectors and in particular driven by upcoming maturities and limited lender appetite to continue to support struggling companies.



FTI Consulting's Special Situations M&A Offering

We offer specialist M&A expertise at the pivotal moment to guide clients through challenging, complex and business-critical issues to deliver the optimal outcome.

Complex sell side M&A

Creating bespoke M&A processes designed to maximise shareholder value in situations which have some areas of complexity (e.g. public company M&A).

Accelerated M&A

Sale process with truncated timetable due to a pending liquidity event or other precipitative factors such as unresolvable stakeholder conflict.

Accelerated funding solutions

Securing flexible capital for stressed or distressed corporates where the funding requirement is more suited to special situation financiers.

Non-core exits

Sale process involving the exit of non-core divisions of large corporates or non-core investments sitting within private equity portfolios.

Strategic M&A support

Broad range of M&A support, including market mapping, sales process monitoring, retrospective sales process reviews, strategic options reviews and exit planning.

IAIN REILLY
Managing Director
Head of UK M&A
iain.reilly@fticonsulting.com

ANNA CUNNINGHAM
Consultant
UK M&A, Corporate Finance & Restructuring
anna.cunningham@fticonsulting.com

MATT CALLAGHAN
Senior Managing Director
Mid-Market Restructuring and Insolvency Leader
matthew.callaghan@fticonsulting.com

Endnotes

1 Retail Dive, "The Body Shop acquired out of UK administration", July 2024
https://www.retaildive.com/news/consortium-aurea-acquires-the-body-shop/721566/

2 Retail Gazette, "Carpetright rival Tapi to snap up chain in pre-pack deal today", July 2024
https://www.retailgazette.co.uk/blog/2024/07/carpetright-tapi-pre-pack/

3 LumiraDX, "LumiraDx Announces Agreement to Sell its Cutting Edge Point of Care Technology Platform to Roche", December 2023
https://www.lumiradx.com/en-uk/publications/lumiradx-announces-agreement-to-sell-its-cutting-edge-point-of-care-technology-platform-to-roche

4 FTI Consulting, "Sale Completed: Over 300 Jobs Safeguarded and £100 Million in Economic Impact in Liverpool Secured", January 2025
https://www.fticonsulting.com/insights/case-studies/sale-completed-over-300-jobs-safeguarded-100-million-economic-impact-liverpool-secured

5 Total telecom, "Struggling altnet Spring Fibre sold to Harmony Networks", November 2024
https://totaltele.com/struggling-altnet-spring-fibre-sold-to-harmony-networks/

6 White & Case, "M&A Explorer", data correct as of February 2025
https://mergers.whitecase.com/

7 GOV.UK, "Company insolvency statistics releases", January 2025
https://www.gov.uk/government/collections/company-insolvency-statistics-releases

8 FCA, "FCA to undertake work in the motor finance market", January 2025
https://www.fca.org.uk/news/statements/fca-undertake-work-motor-finance-market

9 Bank of England, "Monetary Policy Report", November 2024
https://www.bankofengland.co.uk/monetary-policy-report/2024/november-2024

10 House of Commons Library, "GDP international comparisons: Economic indicators", January 2025
https://commonslibrary.parliament.uk/research-briefings/sn02784/

11 Statista, "Annual unemployment rate in the United Kingdom from 2000 to 2029", November 2024,
https://www.statista.com/statistics/374800/unemployment-rate-forecast