RECOGNIZING + ADDRESSING ISSUES IN CORPORATE RESTRUCTURINGS

01 Causes of Financial Distress

- Companies face financial distress due to various reasons, often concurrently.
- Causes include poor management, industry challenges, macroeconomic factors, political issues, unprofitable contracts, and excessive real estate costs.
- Primarily, restructurings arise from cash crunches, often due to excessive debt or failed business strategies.
- Signs to watch for include declining revenue, increased costs, reduced profits, declining market share, higher borrowing costs, product failures, competition, and changes by vendors and customers.
- Companies facing liquidity problems may struggle to obtain cash infusion, with equity owners reluctant to invest further and lenders demanding significant concessions.
- Liquidity issues can trigger restructuring events, such as defaults on loan documents or indentures.
- Distressed companies may resort to debt exchanges, asset sales, or bankruptcy filings, or all three.
- Psychological factors, such as denial, can impede successful restructurings.
- Successful restructurings require objective identification of issues and formulation of a strategy by all stakeholders.

02 Getting Ahead of the Problem and Assembling a Team

- Understanding the company's cash profile is crucial to determine if it can operate long enough to implement a solution.
- Cash generation and conservation are key to a successful restructuring.
- A reliable and detailed cash flow forecast helps demonstrate the liquidity runway for negotiation and identifies where cost-cutting can be implemented.
- Measures like delaying vendor payments, deferring capital expenditures, exploring layoffs and real estate consolidation, and minimizing dividends can help build cash.
- Understanding enterprise and asset values is crucial, especially if the company is insolvent.
- Creditors or new investors may need to provide future liquidity for the company to survive.
- Determining enterprise value identifies the "fulcrum creditor," which may end up with a significant portion of ownership interests in the reorganized company.

- Understanding legal rights requires knowledge of primary loan documents, including covenant breach conditions, default notice and cure periods, and consent thresholds.
- Lien searches and title reports identify secured creditors and their security interests.
- A team of internal restructuring specialists and outside advisors, including counsel, accountants, investment bankers, brokers, and a communications team, is essential.
- Hiring a Chief Restructuring Officer or similar professional may be necessary to focus on restructuring issues while management runs the business.

03 Identifying Viable Restructuring Options

- Companies and creditors often seek out-of-court options first due to cost and fewer parties involved.
- Short-term fixes such as forbearance, waiver, and amendments to loan documents can provide temporary relief.
- Lenders may ease lending conditions or provide over-advances as a bridge to restructuring.
- Debt-for-debt or debt-for-equity exchange offers are considered but may require 100% creditor participation.
- Creative financings such as uptier and drop-down transactions have been used but can face legal challenges.
- Operational and financial restructurings often require an in-court solution, such as filing for chapter 11 bankruptcy.
- Chapter 11 offers benefits including the automatic stay, debtor in possession financing, and the ability to alter sacred rights through voting classes.
- Prepackaged or prearranged chapter 11 cases can shorten the duration and reduce expenses and risks.
- Other supervised restructuring options include receivership for businesses with limited assets and assignment for the benefit of creditors for liquidating assets.
- Creditors may resort to exercising contractual and legal remedies to recover on their claims, prompt a broader restructuring, or both.
- Creditors have various options, including exercising setoff rights, taking over ownership or control of a company through equity pledges, and consensual or forced foreclosure on goods or real property, to recover their claims.

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