

# **INTERNATIONAL TURNAROUND CASE STUDY**

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# Economic context

- reduced economic activity has been managed fairly well
- low interest rates, deferred capex and rescheduled credits
- amend and extend - reduce debt service to cash flow available to avoid provisioning and defaults
- future growth and/or new money needs may make the 'do nothing' option unsustainable
- witness UK zombies & low insolvencies (apart from retail)
- operational improvement can grow value and provide internal finance, but...
- lack of turnaround skills in the CEE/CIS region, where...
- management and banker denial and price sensitivity is common.

# Management DIY solutions

- objective forecasts and KPIs can provide early warning
- good communication instils confidence and can buy time
- timely action to restore liquidity include:
  - focus on performance improvement
  - cash and working capital management
  - revisit strategy and management team
  - right size operations back to core?
  - look for balance sheet quick wins
  - renegotiation of credit terms
  - sell, fix or close
- managers for growth may struggle in periods of decline

# Funding challenges – CEE/CIS

- easy credit has gone, now facing 20% NPLs in some countries
- managers need quality business plans to compete for credit
- foreign owned banks dominate several markets - a systemic risk
- International Financial Institutions very active to support:
  - SME lending and local capital market development
  - municipal credit and PPP structures, energy efficiency.
- Vienna Initiative 2.0 is designing a regional stakeholder solution:
  - central resolution authority
  - single supervisory mechanism
  - common system for deposit guarantees
- little use of Asset Based Lending, some private equity and FDI
- many company and state balance sheets are in poor shape.

# Restructuring challenges – CEE/CIS

- local insolvency processes may be slow and inefficient:
  - legislation, judges, interpretation, precedent, delay, tactics
  - insolvency practitioners, regulation, incentives
  - director liability (“goldilocks” - protection vs straightjacket)
  - creditor behaviour either passive or aggressive, often unilateral
  - weak compliance and public prosecutor “form over substance” risk
- little use or capacity of out of court remedies or turnaround
- Central Bank attitude to debt/equity conversions
- slow reform of labour intensive state owned industries
- Serbia’s energy EPS + Bulgaria’s rail BDZ = #SEECashcrisis.

# Gallery Media – case study

- Gallery Media, outdoor media group in Russia and Ukraine
- Russia and Ukraine combined population 188m. UK is 63m.
- \$100m PIK notes and \$175m senior secured notes in 2006
- financial crisis caused big drop in advertising spend
  - 2008 turnover \$213m 2009 turnover \$105m
- first Russian high yield bond to default (2009)
- J.P. Morgan hired to conduct a financial restructuring
- bonds held in BVI, Luxembourg, Cyprus offshore structures
- Centre of Main Interest shift to UK to use Scheme of Arrangement.
- Gallery Media management focused on operational improvements and future revenues

# J.P. Morgan acted as exclusive financial advisor to the company on the debt restructuring of Gallery Media Group

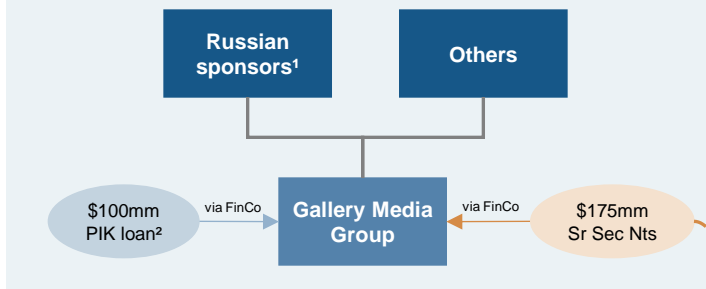


## Transaction details

- In May 2009, Russian outdoor advertiser Gallery announced the postponement of the semi-annual coupon payment on its 10.125% Senior Secured Notes (issued in May 2006) and enter into formal restructuring negotiations with the bondholders
- In October 2009, Gallery announced that it has reached a **consensual agreement** with the bondholders
  - Under the terms of the agreement, total indebtedness is reduced to \$95mm (“New Notes” to be issued)
    - The New Notes will have a 10% annual interest rate (PIK in year 1, cash thereafter) and a 5-year term
    - The existing PIK loan is wiped out
  - Following the completion of the restructuring, the existing bondholders will own 70% of the equity in a new company (NewCo) which will essentially own all the assets of Gallery
  - Two existing shareholders of the group, Baring Vostok Capital Partners and founder and former CEO Anatoly Mostovoy, will invest \$5mm in NewCo and provide ongoing support in return for 30% of the equity of NewCo and 10% of the New Notes
- The restructuring will be effected by way of a Scheme of Arrangement under UK law

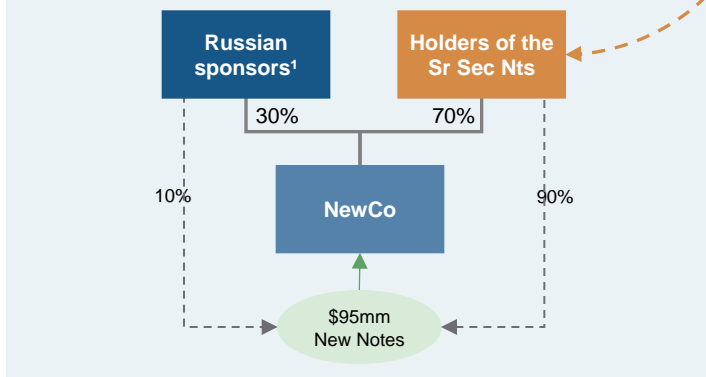
## Group structure

### Current structure



### UK scheme of arrangement

### New structure



<sup>1</sup> Baring Vostok Capital Partners and Anatoly Mostovoy <sup>2</sup> Initial principal excl. accrued interest



# Gallery Media – debt/equity outcome

- UK Schemes of Arrangement are popular to convert debt to equity
- COMI (Centre of Main Interest) shifts are common
- correcting the balance sheet to restore solvency needs to be coupled with positive future cash flow
- high risk of loss of control if a creditor triggers local insolvency
- J.P Morgan commissioned Grant Thornton to set up offshore provisional liquidators on stand-by as a contingency plan
- shareholders usually wiped out if the value breaks in the debt
- key future commercial impact of shareholders reflected in NewCo
- back on track: 2011 turnover \$164m, 9M 2012 turnover \$135m.

# How far can zombies walk?

- at what stage will the stress or growth agenda move the market from:
  - amend, extend and pretend to...
  - mend, expand and realise potential?
- poorly managed or undercapitalised businesses may/should fail if they under or overreact to growth opportunities
- CEE/CIS financial stability underpinned by Vienna Initiative 2.0
- alternative credit sources may be in demand in 2013.

# Summary

- International challenges
  - Check local game rules: how to engage, how to deliver, how to by-pass
- Case study
  - Where does the value break and where will it be created in the future?
- Points for the future
  - Cash is king. Who will be the next king?
  - #SEEcashcrisis



# QUESTIONS?

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