

WORKING THROUGH THE RETAIL SLUMP

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Retail Liquidations

According to the International
Council of Shopping Centers
Approximately 5,770 retail stores will close in 2008

What is Driving the Trend

- Macro-Economic Factors – “The Current Economy”
- Too Many Retail Locations
 - Expansion into New Markets
 - Capital Expenditures
- Over Leveraging both in Bank Deals and Capital Structures
- Inventory Management
 - Stockpiling of Inventory
 - Valuation of Inventory
 - Collateral “Catch 22”
- Understanding Cash Flow
- To be successful in business one must recognize the world as it is, not as you would like it to be – Jack Welch

Delayed Reaction into the Asset-Based Market

- Bank Market has been slower to react, but it is reacting
- Source of large asset-based loans is shifting, lack of CLO formation
- When will you get “The Memo”

Its Not Quite over Yet

- Already We've Survived:
- Sub Prime Wipeout
- Debt Market Crash
- Massive Chargeoffs
- Financial Market Layoffs

Still to Come

- Recession
- Defaults
- New Strategies
- Impact of Low Rates
- Regulatory Response
- Surprises

Financial Reporting

- Developing and Understanding the 13 week cash flow
 - Hoard cash – critical operating expenses only
 - Understanding retail, and markets within retail, is very seasonal
 - Collateral base- adequate protection while the “ice cube is melting”
- Completing an Assessment of the situation beyond the income statement
- Well founded, fact based plan: finding the business model that works
 - Evaluating Strategic Options

Warning Signs and Defensive Measures: The Lenders Perspective

- Financial Information – Financial Reporting Issues
- Management Issues
- Increased use of leverage to finance losses
- Appraisal of Inventory and use of field examiners
- Increased Borrowing Base Reporting/Advance Rates/Borrowing Base Block
- Need for a 13 week cash flow from a Turnaround Group

Evaluating Viability of the Business

- Is there a viable business?
- Is there a source of financing?
- Is there an asset base to support new financing?
- Issues need to be carefully evaluated prior to embarking on a course of action

Strategic Options

- Chapter 11 Filing
 - 363 Sale
 - Plan
- Out of Court
 - Rehabilitation
 - Refinancing
 - Equity Infusion
 - Reamortizing Debt
 - Going Concern Sale
 - Liquidation

Benefits of a Bankruptcy Filing

- The Automatic Stay/Bankruptcy Court Venue
- Obtaining Additional Credit
- Lease Obligations
- Limited Rights of Suppliers of Goods
- Exit Strategies Including 363 Sale

Challenges of a Bankruptcy Filing

- Involvement of Third Parties
- Utilities
- Unpaid Goods Received in Twenty Days
- Lease Obligations
- Easy Entrance/Hard Exit

Exit Strategies

- Out-of-Court Options:
 - Rehabilitation
 - Refinancing
 - Equity Infusion
 - Reamortizing Debt
 - Going Concern Sale
 - Liquidation

Out-of-Court Options

- It is becoming harder for small to medium sized retailers to emerge from bankruptcy
- More cases are being converted to Chapter 7
- More companies are trying to avoid bankruptcy by seeking concessions from lenders
- Certain industries will lose their vendors if they file for bankruptcy (e.g. Rolex, Tag Heuer watches)
- May not be possible if the company has public note debt because most Trust Indentures require 100% noteholder approval to restructure debt

The “Out of Court” Restructuring

- Consideration/Negotiation Needed with All Constituents
- Need to Establish and Earn Credibility with Constituent Group
- How did we get here?
- Develop a Well Organized Plan and Proposed Course of Action
 - 4 wall EBITDA Analysis
 - Focus on the core profitable cash flowing stores
- No Secrets/No Surprises
- Do what you communicated to do
- Present Plan against the backdrop of alternatives
- Proposed Plan vs. Ch 11 liquidation Analysis

Recent Examples

U.S Business Journal – Weekly Summary of Troubled Companies June 9, 2008

- Borders: cut 270+ corporate staff to reduce expenses by \$120 million; seeking to sell its international business
- Callaway Golf: closing manufacturing plant to outsource production to China
- Coors and Miller: seeking \$500 million in cost savings by joint production venture, subject to Justice Department approval

Examples (continued)

- Mrs. Fields and Bennigan's/Ponderosa both in talks with lenders seeking to avoid bankruptcy, but publicly expressed they were prepared to file Ch. 11 if necessary
- Ford and General Motors: SUV and truck sales are dropping as gas prices rise; Ford is seeking to consolidate its dealerships while GM decided to phase out production at four of its plants in North America
- Lowe's: reduced expansion plans

Examples (continued)

- Sears: analysts fear that hedge fund chairman, Edward Lampert, will not be able to pull off his promised turnaround, but selling off assets in the current economic market is not a good idea either
- Wendy's: received Federal Trade Commission approval to go ahead with its agreement to be acquired by Triarc Cos. Inc. (owner of 3,700 Arby's restaurants)

Equity Infusion

- May be the only option if potential asset purchasers want expensive solvency opinions and existing lender unwilling to lend or subordinate liens to new lender
- Working with Private Equity Investment firms
- Hedge Funds search for and target undervalued companies and pursue aggressive and high-risk investment strategies
- Frequently comes at a high price, including the loss of controlling the company's future

Going Concern Sale v. Liquidation

- Going concern premium versus liquidation value – uncovering the hidden value (e.g. lease designation rights)
- Define the Timeline
- Prepare the Offering Memorandum
- Manage the Sale

Going Out of Business (GOB) Sale / Liquidation

- Preparation of the Bid Package
 - Information to be included
 - Working with the GOB community
- The Agency Agreement
 - Key point to be included
 - Sending out the blank agreement
 - Process and Timelines
- The Stalking Horse Agreement
 - Key points in the Stalking Horse Agreement
 - The Break Up Fee
- The Auction Process
- Problems: markets already flooded in hardest hit industries, e.g. jewelry

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