

# EBRD – Non Performing Loans (NPLs) and Corporate Restructuring

Vienna, June 2015



**European Bank**  
for Reconstruction and Development

# EBRD – Non Performing Loans (NPLs) and Corporate Restructuring



**European Bank**  
for Reconstruction and Development

EBRD and addressing Corporate NPLs

EBRD's role in Corporate Restructuring in CoO

- Continued demand for restructuring as a result of the credit boom “hang-over”, which left lenders with high NPLs levels
- March 2012: EBRD approved a strategy paper for the restructuring initiative
- There is increased demand for financing from corporate clients as a result of:
  - ✓ Deterioration of performance of underlying operating businesses (especially businesses with high operating leverage exposed to cyclical end industries) affected by the economic slowdown
  - ✓ Disproportionate lack of liquidity/funding as Western Banks cut off lines/funding to local subsidiaries
  - ✓ Increasing NPLs in local banks portfolios leading to reduced risk appetite and need to restructure
- Lack of managerial experience in downturn and of restructuring at many banks leads to protracted lenders negotiations, lack of working capital or capex lines for businesses to operate
- EBRD can have a significant transition impact as “the new money provider”

- Deals brought to the attention of EBRD generally involve businesses with over-levered balance sheets and inability to attract new funding as a result of:
  - ✓ Manufacturing sectors affected by cyclical downturn and economic slowdown, reduction in volumes and profitability
  - ✓ Companies having embarked in aggressive external growth expansion leading to lack of liquidity
  - ✓ Strained relationships between shareholders or company/management and impaired lenders
- In most cases companies are in urgent need of financing to continue their operations, finance their working capital needs, require operational restructuring as well as balance sheet restructuring

- While each jurisdiction is different, generally most countries lack a clear regulatory framework to facilitate out of court restructurings via a negotiated agreement that would lead to a comprehensive balance sheet solution able to attract new funding to allow businesses to recover and grow:
  - ✓ Lack of clarity with enforcement/repossession legislation
  - ✓ Insolvency regulation at times promoting liquidation over rehabilitation
  - ✓ Slow bankruptcy process and court backlogs
  - ✓ Bilateral lending and lack of syndicated deals creating lack of coordination, hold out value for each individual lender
  - ✓ Unfavourable tax treatment of write offs and debt/equity swaps
  - ✓ Illiquid and underdeveloped NPL secondary market

- The most effective role EBRD can play is to provide new funding and act as a catalyst to a comprehensive restructuring of the corporate, backing a revised business plan allowing the business to recover and grow
- The proposal is to focus on investment opportunities (whether in the form of debt financing or equity financing) with the following characteristics:
  - ✓ New bank client
  - ✓ Lack or shortage of alternative funding available (most cases)
  - ✓ Viable operating business case leading to recovery in profitability
  - ✓ Comprehensive balance sheet restructuring with existing lenders having accepted or being prepared to accept a sound restructuring proposal in cooperation with shareholders
- Ideally, EBRD would invest or provide financing alongside a new investor and support the turnaround business plan

Each individual restructuring is unique, however, there are a few key factors which reduce the process to several stages and facilitate reaching optimal solutions:

- **Start of restructuring process:** greater chance of success if restructuring is started before a covenant breach, a default or liquidity squeeze
- **Analysis of potential bankruptcy or liquidation:** Lenders should better analyze the most realistic restructuring alternatives vs partial recovery in case of bankruptcy
- **Historic lender/ borrower relationship:** the approach and transparency of management and shareholders play a key role in convincing lenders to play along a consensual restructuring
- **Consultants appointment early in the process:** consultants help the management to present their business plan to the lenders and intermediate difficult discussions
- **Availability of new money:** new money should come as a first source from the shareholders and then from external sources to support the restructuring plan



- **Number and composition of lenders:** Syndicated loans tend to have a more straightforward restructuring process. The more bi-lateral loans are in place, the more difficult the negotiations and the higher the risk of failure. In some cases lenders with small exposures can block the process and ask for full repayment or other preferential treatments
- **Regulatory Framework:** In many cases banking regulations impact how lenders deal with NPLs and if there is a framework to encourage out of court restructurings
- **Bad Bank:** The creation of a Bad Bank enhances the process for large and complicated corporate restructurings, provided they have the right mandate and expertise



- Typically we have been approached when the situation is already significantly deteriorated
- Lack of experience by management teams and lack of restructuring skills within lenders leads to slow reaction and inaction in front of operating difficulties
- Lack of experience and precedents leads to inability to accurately reassess the liquidity needs, and to take important decisions early:
  - ✓ Borrowers and lenders tend to wait until a payment default or lack of liquidity to commence negotiations
  - ✓ Before restructuring, companies often enact solutions that are detrimental in the long term and do not reduce leverage (costly third party fundraising, pledging on new unencumbered assets)
  - ✓ Companies lack comprehensive and realistic business plans allowing them to present a solution to existing lenders and attract funding from new lenders in order to avoid bankruptcy
  - ✓ Typically existing lenders do not like bad news and last minute surprises, lack experience in assessing restructuring situations and opt for foreclosure and bankruptcy rather than a consensual restructuring

- Although the Restructuring Initiative is considered a challenging area of financing, it also constitutes a good Business Case
- The risk profile of a well structured “new money” facility benefits from higher margins (sometimes equity upside)
- In most of the cases “new money” should benefit from robust security packages and super-seniority (“last in-first out” structures)
- EBRD has limited resources in restructuring and would work on selective basis to ensure a higher success rate of restructuring transactions
- EBRD can promote best practices in “out of court restructurings” and also has worked together with lawyers and economists to help governments revise local bankruptcy legislations
- Corporate Restructuring will be also part of the Vienna Initiative
- EBRD is a good partner for private equity funds or investors in restructuring cases
- FI and Banking can work together on NPL portfolios where corporate restructuring is involved

- Work together with other IFIs (IMF, World Bank, IFC) & EC on a multi-country initiative to reduce NPLs (especially *corporate*)
- Regional NPL initiative with a focus on core countries: Hungary (lead support: EBRD), Croatia (World Bank), Serbia (IMF) & Montenegro (World Bank) plus Bulgaria, Romania, Slovenia and Greece (to be confirmed)
- Key initiative objectives:
  - ✓ Create incentives for NPL sales and facilitate corporate NPL restructurings
  - ✓ Mobilise all relevant authorities (government, regulators) to focus on NPLs
  - ✓ Work with banking groups on NPL sales and corporate restructuring principles
  - ✓ Support specific **country action plans** by policy advice, training, technical assistance and investments
  - ✓ Monitor specific country progress

# Annex: EBRD Successful Restructuring Deals

To date EBRD has worked on numerous corporate restructuring opportunities - below are listed the successful transactions where EBRD was able to provide financing:

## Ciech

- ✓ Provided senior debt in 2011
- ✓ Leading chemicals producer in Poland
- ✓ Balance Sheet and Corporate Restructuring
- ✓ Followed by a successful SPO listing

## Prista and Monbat

- ✓ Provided super senior debt, equity and convertible loan in 2012
- ✓ Leading Lubricants Oil and Car Battery producers in Bulgaria
- ✓ Balance Sheet, Corporate and Operational restructurings

## Sofia Med

- ✓ Provided super senior debt in 2013
- ✓ Leading copper producer in Bulgaria
- ✓ Balance Sheet and Operational Restructuring

## Celsa

- ✓ Provided super senior debt in 2011
- ✓ Leading r-bars producer in the Polish subsidiary
- ✓ Balance Sheet and Operational Restructuring

# Annex: EBRD existing engagements related to NPLs

## TurkAsset

- ✓ Invested debt & equity in 2011
- ✓ Leading NPL asset manager in Turkey
- ✓ Market is both retail and corporate
- ✓ All major private banks selling regularly

## Vostok Finance

- ✓ Provided debt in 2013
- ✓ Leading NPL asset manager & servicer in Ukraine & Russia
- ✓ Unsecured retail loan sales in both markets
- ✓ Most banks are sellers

## Frontex International

- ✓ Provided debt in 2014
- ✓ Leading NPL asset manager & servicer in Bulgaria
- ✓ Unsecured retail loan sales
- ✓ Most banks considering sales