THE M&A ADVISOR

FEBRUARY 2016

THE M&A ADVISOR SYMPOSIUM REPORT

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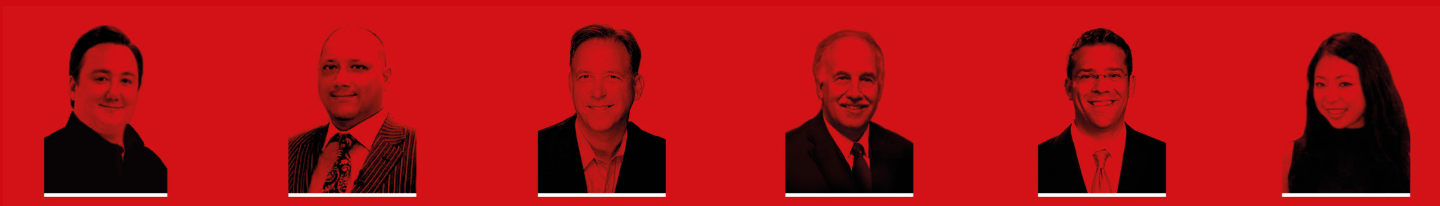

Charles Dabrowski
Financial Life Advisor
Telemus Capital Partners LLC

Karl D'Cunha
Senior Managing Director
Madison Street Capital

Brian A. Demkowicz
Managing Partner and
Co-Founder
Huron Capital Partners

Patrick O'Keefe
Founder and CEO
O'Keefe LLC

Michael Pokrassa
Managing Director
Raymond James

Jodi Xu Klein
Reporter – Corporate Finance
and Distressed Credit
Bloomberg News

STALWARTS ROUNDTABLE
INVESTORS OUTLOOK FOR 2016

At The M&A Advisor's Annual Distressed Investing Summit in Palm Beach, Florida, January 27-29, 2016, Patrick O'Keefe, Founder and CEO, O'Keefe LLC, chaired a Stalwarts Roundtable discussion entitled "2016 Restructuring Industry Outlook." O'Keefe was joined by Karl D'Cunha, Senior Managing Director, Madison Street Capital; Jodi Xu Klein, Reporter at Bloomberg News, Corporate Finance and Distressed Credit; and Michael Pokrassa, Managing Director at Raymond James.

In this report, we gather the insights and reflections of these M&A Stalwarts. They participate in (or in the case of Jodi Xu Klein report on) restructurings and distressed investing deals in a variety of industries and sectors – and across borders. The pages to follow highlight their views on how 2016 will differ from the past year, which saw the highest level of M&A activity since before the Great Recession.

The principle topics addressed in this symposium report include:

- Rocky Start to 2016 Bodes Busy Year for Distressed Investing
- Energy: The Elephant in the Restructuring Room
- Finding Value in Intellectual Property and Brands
- Risks in Cross-Border Distressed Investing
- Dodd-Frank and Shadow Banking – Impact of Regulation
- Additional Insight: Outlook from Two M&A Stalwarts

Distressed investing, restructuring and bankruptcy proceedings carry the patina of bad tidings in the minds of many people. But the value importance of these processes in the global economy cannot be overstated. Businesses must take risks and with risk comes failure – but out of failure arises new opportunity. Our Stalwarts discuss how this storyline will likely play out in 2016.

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Executive Summary

In 2015, the value of mergers and acquisitions worldwide reached its highest level since before the Great Recession. Yet, storm clouds were on the horizon. China devalued its currency, setting off global market gyrations in August of last year. Many hedge funds experienced poor performance in 2015 while many private equity funds kept their investing powder very dry. At the dawn of 2016, concerns over China and global growth internationally sent shudders through the global markets. Against this backdrop, the Stalwarts Roundtable discussion, "2016 Restructuring Industry Outlook", convened at The M&A Advisor's Annual Distressed Investing Summit in Palm Beach, Florida, January 27-29, 2016. The panelists envision a very busy year.

"I just want to start off by saying that for anyone who is involved in the restructuring space this year, our year has arrived. So congratulations for everyone – get ready to get busy!"
– Jodi Xu Klein

Introduction

At The M&A Advisor's Annual Distressed Investing Summit, Patrick O'Keefe, Founder and CEO, O'Keefe LLC, chaired a Stalwarts Roundtable discussion entitled "2016 Restructuring Industry Outlook."

In this report, we summarize the observations and insights of these veteran M&A professionals as well as an experienced business journalist as they looked ahead to the 2016 distressed investing industry investment landscape. The panelists were:

- Patrick O'Keefe | Founder and CEO, O'Keefe LLC
- Karl D'Cunha | Senior Managing Director, Madison Street Capital
- Jodi Xu Klein | Reporter – Corporate Finance and Distressed Credit, Bloomberg News
- Michael Pokrassa | Managing Director at Raymond James

Rocky Start to 2016 Bodes Busy Year for Distressed Investing

Patrick O'Keefe opened the session with an encomium to the M&A Advisor's 10th Annual Turnaround Awards (which followed the Distressed Investing Summit): "A great milestone of a decade of recognizing this industry." He also noted the steady rainfall that fell throughout the conference as a possible precursor to the year ahead in the markets and the economy. The panelists agreed.

Michael Pokrassa of Raymond James said he is focused primarily on restructuring but also does some private placements. "I think the market is certainly off to a weak start as we've all talked about for various global issues, but I think when you delve into the financial market side of things, it's sort of what's driving the stress. I think really what we're going to see is a lack of public market opportunities." He noted that 2016 opened with anemic equity and debt underwritings. "In my view, that's going to drive people towards where to put capital," he said. "I think that's going to be in the direct lending middle market opportunities and people focusing on secondary opportunities and really looking for the catalysts for the market in terms of driving returns." Pokrassa also said he thinks leverage levels are "really at pre-recession levels."

"I just want to start off by saying that for anyone who is involved in the restructuring space this year, our year has arrived. So congratulations for everyone – get ready to get busy!" said Jodi Xu Klein of Bloomberg News. Xu Klein noted that she covered the U.S. auto industry restructuring in 2008-2009 when she was with the Wall Street Journal. "What I've seen in January is pretty, pretty significant. My take on the outlook of this year is we are ripe for restructuring to pick up significantly." Stress in the high-yield (AKA "junk") bond market will likely lead to more defaults, she added. "A lot of the companies are not doing well, and their bonds are trading down. Unless we see a quick turnaround in the economy, that's going to happen." Capital market liquidity has also shrunk – "For the first month of this year, we're seeing $33 billion in high-yield bond issuance. That's the lowest in the last 10 years. Yeah, we're going to see a lot more defaults this year," Xu Klein predicted.

"I believe 2016 has all the makings of a very volatile year internationally, which will clearly ripple through the economy."
– **Patrick O'Keefe**

Karl D'Cunha, who at Madison Street Capital provides investment banking in the middle market with deals in energy, healthcare, industrial and financial services, said: "I think we're going to have a really busy year in 2016. With the current capital markets, there are a lot of opportunities because, at the end of the day, this is not like the credit crisis where people weren't prepared and there was a massive shortage of liquidity. There's a lot of liquidity and I think people are going to be very opportunistic in certain markets. We expect to be very busy both on the sell side and the buy side."

Pat O'Keefe, whose firm provides strategic and financial advisory as well as turnaround and restructuring services to the M&A middle market, said that in the fourth quarter of 2015 he saw "more deals in those three months than we have in the last three years in the middle market." He pointed to the dramatic market selloff that opened 2016, upticks in gold and silver prices, and stress in the high-yield bond market as harbingers. "Goldman Sachs believes that financials, utilities and energy will continue to be down in 2016 and the big healthy prospects relate to healthcare, IT, and consumer discretionary," O'Keefe said. He added that while Ford Motor Company announced record profits recently, the auto industry is keeping a "watchful eye" on any signs of economic downturn. "Cash outperformed the market in 2008 to 2010. We've had unprecedented return since then. I expect cash will be king in 2016 and 2017," he said, adding that he does not expect a quick rebound in oil prices. "The Saudis will continue to protect their market share," he said, noting that the U.S. and Saudi Arabia have an incentive to keep prices low to counter Russia in geopolitics. "As a consequence, I believe 2016 has all the makings of a very volatile year internationally, which will clearly ripple through the economy."

Turning to U.S. politics, O'Keefe observed: "When an incumbent runs in the presidential election, the market generally does very well. When you have newbies running for election, the economy generally tanks in the year of the elections. Well, 2016 is already shaping up to continue the trend of negative returns in the S&P 500." Finally, O'Keefe said housing starts may be an indicator of economic weakness this year. "We really haven't had the robust construction that one would expect. The US peaked in 2006 in terms of housing starts and even with the bump up in the last few years we are still only about half of where we were at the peak. Housing drives a lot of industries as does the auto and I just don't see housing improving here over the next year or two."

Energy: The Elephant in the Restructuring Room

Panelists agreed the elephant in the restructuring room this year is energy. "Oil and gas for sure," said Karl D'Cunha, "but I think it's not as transparent or, I guess, as easy as people think it's going to be. There are a lot of companies out there that are more prepared and it's not like a credit crisis where everything happened really fast and people were rushing around and there's all this distress out there. I think this will be a much more planned process and people are going to be very careful on the type of deals that they move on." He added that industries that sell into the energy sector – payment technologies as an example – are "feeling the squeeze right now in terms of their fee structures and how their clients come back to them and ask them if they can renegotiate their deals. That's an area people haven't really thought about that's going to get really impacted."

"Everyone is focused on energy and it's hard to not talk about it. There are other sectors but energy is – aside from just being prominent – where I think there's the largest amount of capital when you think about sizes of the equity offerings and public debt raises."
– Michael Pokrassa

"Everyone is focused on energy and it's hard to not talk about it," said Mike Pokrassa. "There are other sectors but energy is – aside from just being prominent – where I think there is the largest amount of capital, when you think about sizes of the equity offerings and public debt raises. People have already started to take large positions in distressed companies. We saw the first wave of bankruptcies last year. It's going to continue this year." Pokrassa said lenders will be forced to make tough decisions – "Do they ride it out, own the assets, or do they put more dollars in and see what happens? The question is, when does oil come back?

"Energy is all about timing", said Bloomberg's Jodi Xu Klein. "Last year, a lot of the hedge funds got in early in the year saying that they were calling the bottom. That didn't pan out. Hedge funds are feeling a lot of pain. Some of them folded, some of them had to cut their head counts. This year, I think we're going to see the same thing going on but where we are now with the commodity prices is very different. How much lower can we get? That's the question everybody's asking." Given the pain felt by energy investors over the past two years, Xu Klein said, "This year the difference is people are going to time it very, very carefully when they get in – because a lot of people got a lesson."

Private equity funds were less active than hedge funds in 2015, Michael Pokrassa added. "I think virtually 100 percent of the distressed funds are focused on raising money this year," he said. They may have been a little bit more patient and I think the distressed funds also have more strategic angles than they used to. I think we'll see them be more competitive on a pricing standpoint in the future."

"Everybody's energy, energy, energy," said Patrick O'Keefe. "What is the trickle down to that potentially?" he asked Jodi Xu Klein, further asking if there are other industries that could have distressed situations in 2016.

"If you think of service providers, Master Limited Partnerships (MLPs), transportation guys were kind of holding on last year, and some of the smaller ones might get into trouble this year," Xu Klein said. "People are looking at shifting their focus from strict energy and production companies to downstream." She noted that the coal industry is under particular stress. "Six of them [coal producer companies] filed for bankruptcy in the last two years. Arch Coal, the second largest coal miner in the United States, and Peabody is on everybody's mind. This is going to unfold this year and probably pretty quickly. Why? Because Arch Coal tried everything that Peabody supposedly can do and failed. They tried to negotiate a debt exchange deal trying to bring their leverage down. It didn't work."

Cross-border distressed investing, particularly with Canada in its energy sector, is a "huge, huge opportunity," said Karl D'Cunha. "Canada's currency is getting killed, at a 16-year low," he said, citing the perception of the nation's dependence on natural resources and commodities. "Ninety percent of Canada has nothing to do with resources," he said. "We're seeing beautiful companies, really profitable companies that are going into the bucket of this distressed country that's so dependent on oil and gold prices. And guess what, US private equity firms, they love it! In Canada, the legal system and accounting system is very similar to the US. There's no brain damage in terms of learning what this company does and how to get a deal done. I think that's positive out of all this oil distress."

"Cross-border distressed investing, particularly with Canada in its energy sector, is a "huge, huge opportunity."
- Karl D'Cunha

Finding Value in Intellectual Property and Brands

Traditionally healthy industries can fall victim to commodity price cycles, Patrick O'Keefe observed, citing scrap yards as an example. "Scrap yards that have been in existence for six or seven generations are being stressed, because commodity prices for non-ferrous metals have just fallen off the face of the earth." He said middle-market lenders generally don't want to take possession or ownership of such businesses. "They just don't have tolerance for a small credit where they can easily sweep it under the rug and just get rid of it. They are not going to take the commodity risk of their client. We have three scrap yards that we're dealing with that have been healthy companies for decades now trying to figure out what to do and how to manage their production with demand and how much they're willing to take risk from the inventory standpoint. It's a scary proposition."

"A counter-intuitive example of a distressed situation is the U.S. auto industry," O'Keefe added. "It's just fascinating to me. Here we have north of 17.5 million units being built in North America, a rather robust industry. Ford recently announced record profits and an oil bonus chec to their UAW employees, yet the stock if off 20%. Investors are concerned that competitors like Google and Apple with Smart cars and industry dynamics of Uber may shrink the market and produce more competition. However, again, we have companies that have hitched their bets globally. They've been told by Ford, General Motors, Honda, to expand their operations globally. Now they are finding capital constraints as everything shrinks back. I have seen most recently a lot of middle market auto companies that are facing either the dynamic of the shortage of working capital or their major customers are starting to pull parts back into the plant. These things all roll into cycles."

O'Keefe asked the panelists if they find that certain industries are tougher to restructure or acquire. "Healthcare," said Michael Pokrassa. "A lot of it is formula based, and I think there is just uncertainty on reimbursement rates and where they would end up. I think certain folks have an appetite for that and understand reimbursement risk, and others don't. Karl D'Cunha cited technology companies – especially ones, without long-term track records – as being vulnerable in 2016. "I think distressed buyers are a little more educated. For example, there's a group that I deal with where they essentially hire 10 analysts to focus on patents. When they look at a deal now, they'll totally scour the IP [intellectual property] and assess the value. Whereas 5 or 6 years ago, they would just look at it, ask 10 questions about our deal and they would make a judgment based on that and say 'Yeah, this is for us,' or 'This is not for us.'" Pokrassa added, "I think certainly other areas that just have high fixed costs. For example, energy both on the production side and on the equipment side, it's going to be a challenge." Also, distressed companies that have invested in dual-purpose heavy equipment are "hugely valuable right now, especially in the energy world." From a lender's standpoint, he said, "If you've got dual purpose collateral, that is opening up more ability to get the lenders to the table."

"You have companies that don't spend the time documenting their intellectual property, thinking about it, how to protect it, and whether or not it's a real asset."

- Patrick O'Keefe

O'Keefe asked the panel whether companies that are forced into distressed asset sales through so-called 363 bankruptcies have more success if they have intellectual property or other unique aspects to their operations that buyers find attractive. "I've seen both," said Karl D'Cunha. "I've seen ones where it's purely an IP transaction and they go through the 16 different patents to find the one patent that's got the most value. In this case, 15 patents were worthless. The one that was of interest was what was driving the auction." In other cases, he said, opportunities to acquire an infrastructure have proven successful. "I've seen opportunities where the eventual buyer had a huge operation in India, where they're off-shoring this particular service. When they bought this company in bankruptcy, they were able to leverage what they already had in India. For them, they actually overpaid. I think it was triple the amount of sales based on the infrastructure they had built in India."

O'Keefe interjected that sometimes it can be the company's brand that's most valuable in a 363 auction. "The greatest story that I have heard is the Penthouse bankruptcy," he said. "The domain name 'penthouse.com' was bought for $50 million and none of the secured lenders had tied it up, which created a windfall to the unsecured. You have companies that don't spend the time documenting their intellectual property, thinking about it, how to protect it, and whether or not it's a real asset."

Michael Pokrassa then cited two examples of deals he worked on that brought full value to creditors. One case was "purely brand driven, in terms of where they could drive the business going forward. You had to put some capital into it. It's a healthcare company, a well-known name." The other case didn't involve a brand, but rather an IP technology platform, he said. "It wasn't making any money on its own but they had a processing business that had billions and billions of dollars running through it not making money. They leveraged the technology and basically offloaded it to someone else who could essentially reduce the cost by half."

From the due diligence perspective, O'Keefe asked the panelists where they begin to assess real value from a distressed company or asset. "How do you develop maybe some unforeseen target strength that the average buyer might not be paying attention to?" he asked.

Karl D'Cunha said the first step is to know "your own capabilities and where this would fit in your platform because I think sometimes people rush that part too and don't really figure out how this particular acquisition or asset will fit, and then they end up having a square peg trying to fit it into a round hole." Secondly, D'Cunha said, savvy investors will call in outside help, "especially when it comes to IP because you really have to understand how IP works or is it a good brand." In assessing the value of a brand, he cited Macy's purchase and rebranding of Marshall Field's several years ago. "There is a huge value to the Marshall Field's name even though right now it's not in use. It's dormant but one day, you never know Macy's might want to do a new Marshall Field's line of retail stores or brand. But how do you assess that? You need people who actually do that every day to come up with a value."

"There's too many opportunities in North America. I guess the argument would be why focus on South America, like Brazil for example, when you can get a perfectly good opportunity in California."

- Karl D'Cunha

O'Keefe added that his firm began bringing brand consultants into deals to assist clients in developing their portfolio of intellectual property. Why? Says O'Keefe: "Some business owners really don't think about it. We have a case right now with an automotive staffing company that has developed some desktop tools and they view it as a tool to solve a commodity-driven staffing hours. We said, 'The valuation for technology companies far exceeds staffing companies, so why not figure out how to shift gears as to how the public and your customers perceive the tools that you provide to them?'" Eventually, he said, the owners decided to re-package the business. "It's a distress transaction now, and a great opportunity to take the next step if they can figure out the branding strategy. I think companies don't spend enough time thinking about it, and there is a lot of intellectual property that gets rushed to the wayside in bankruptcies that people don't normally see."

Risks in Cross-Border Distressed Investing

Turning to global macroeconomics, O'Keefe noted that the "Turnaround Management Association has expanded into a global organization and The M&A Advisor now has more conferences and things globally than they've ever had, and cross-border M&A has been very hot. I'm wondering, with China slowing down and showing some signs of weakness, what the opportunities are."

D'Cunha said that in distressed investing, cross-border deals are tough. "They're hard and it's hard, to get people interested. If you're talking about multi-billion dollar sales companies, there's going to be activity, but on a smaller scale, at least from the U.S.-based investors that I deal with, they don't want to touch emerging markets or even develop markets that are international. They think it's too much risk. There's too many opportunities in North America. I guess the argument would be why focus on South America, like Brazil for example, when you can get a perfectly good opportunity in California. I think although there will be opportunities in places like China, my suspicion would be they'd have to be very big transactions, where it's ground breaking like a huge car manufacturer example bought by GM or something."

Presented by

O'Keefe
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O'Keefe noted that, in the U.S. "We have a fairly stable political, judicial and legislative environment that allows us to conduct business. I don't know how many of you saw but I think a couple of months ago, the first patent infringement case in China was favorably awarded to a western company for being able to protect some intellectual property they had." He added that the ability to get capital out of China is not easy.

Jodi Xu Klein observed that the slowdown in China's economic growth is rippling through all industries and markets. "We'll go back to coal. Coal is used to make steel. Demand for that has dropped significantly because of the China slowdown. The coal companies that actually leveled up and borrowed money back in 2011 made huge bets on coal prices going up and haven't seen that pan out." There has been a "huge outflow of capital from China," she said. "[It] is a reversal from what we have seen over the years. Instead of US money going in, now it's all the Chinese money coming out. Does that mean that we're going to have more liquidity here? I'm not sure. You do see a lot of Chinese buyers buying off US assets in different sectors. You see that in the media industry."

> "I think now hedge funds will finally be able to exercise or execute their strategy on a playing field that they're used to."
> **- Michael Pokrassa**

O'Keefe asked the panelists whether the hedge funds are in a better position than in 2008 If the China slowdown results in a global slowdown in 2016. "Do you think hedge funds are able to move quicker now? Were there any lessons learned? What do you guys see?"

"I think they have to be decisive because the folks in that last go around were indecisive," Pokrassa said. "For example, it took seven, eight months, nine months in bankruptcy to figure out if they want to own the assets or take their losses. I think they did poorly, and I think this time around they've learned their lesson – and they're being decisive on taking action."

D'Cunha agreed. "No offense to Florida," he said, citing that in 2007-2008 hedge funds were invested in "risky Florida real estate projects, life settlements, film rights, you name it – all sorts of crazy asset classes." But now, he said, "I think funds are much better, more responsible. I think they do more due diligence on the different investments that they're in or loans that they've issued. Although there are still some risk takers, I think it's not like 2008. That being said, 2015 was a bad year for hedge funds in terms of performance." He advised: "Watch 2016 to see a lot more activity because they got to prove to their investors that they can beat the S&P, because in 2015 most funds were below it."

O'Keefe then asked Pokrassa if hedge funds have "tempered their yield requirements in light of what's happened over the last year or so."

"No, I don't think so," Pokrassa responded. "I think now they will finally be able to exercise or execute their strategy on a playing field that they're used to. Last year was tough." Pokrassa added that on the private equity side, "I think some of the PE folks are okay with a lower targeted threshold and are looking to potentially get in on the debt and say, 'Look, if I only get 15 percent, 20 percent return, that's kind of my base case.' I think we're going to see a lot more of that this year."

Jodi Xu Klein said, "Fifteen percent is pretty good." O'Keefe agreed. "Most funds last year didn't achieve 10% to 12%. We do a lot of analysis on pension fund performance and actuary underwriting and when you look at historically most pension funds have expected 8% to 10% yields on their overall fund balance, and most of them are barely scraping 5, 6 and some have had loses over the last year and you see everybody shifting their expectations down. So where maybe PE funds wanted 20% to 25%, they can't get it anymore and so maybe they've got to shift expectations."

Xu Klein added: "I think 2016 is probably going to be a better year no matter what for hedge funds and private equity because so many guys who had a lot of losses are going to be more thoughtful and cautious. I see a lot of rescue financing on the top of the capital structure – Debtor in Possession (DIP) loans, pieces like that. I don't think there is any appetite to getting junior pieces anymore like what people have done last year."

Dodd-Frank and Shadow Banking – Impact of Regulation

O'Keefe wrapped up the Industry Outlook panel discussion by asking the panelists "If you had to pick a couple of events that could move the needle either way, what do you think drives the economy this year and the ability for distressed investing?"

"Banks are so reluctant of taking risks nowadays. Essentially, you have your regulator standing over your shoulder and they're looking at what you're lending. The most cautious approach to deal with that is do not lend or lend very carefully."

- Jodi Xu Klein

Jodi Xu Klein said the impact of new Dodd-Frank regulations may impact the distressed market in 2016 – "The reason being it's going to impact directly on the lending bases and who the lenders are. The lenders are going to change because of that." Because of Dodd-Frank, she said, "Banks are so reluctant of taking risks nowadays. Essentially, you have your regulator standing over your shoulder and they're looking at what you're lending. The most cautious approach to deal with that is do not lend or lend very carefully. Guess who is going to fill the gap? Hedge funds and the private equity firms – we've seen a lot of that."

O'Keefe observed that such "shadow banking" now makes up about 25 percent of the business lending market, and asked Xu Klein if the government will begin to regulate that.

"I think that's been talked about for a while – whether the unregulated piece of Wall Street should be regulated – and I think a lot of people's answers would be 'Yes, it should,'" she said. "Would that happen any time soon, my personal take is [that] I think the Fed has bigger problems at hand. They have to deal with the big banks and prevent us from falling into another financial crisis. I think that's the priority. It's going to be priority of this year, and then maybe next year. Shadow banking will be the next thing on their agenda. I don't see they are going to get to that any time soon."

"I think the one thing that concerns me is political and social unrest," O'Keefe said in closing. "To me, that could be a real deal mover one direction or another. You've seen, since the first of the year, there's been a number of big layoffs – and I often wonder in some areas how you can have solid democracies without a strong middle class. The middle class over this expansion has been hammered. The people at the top have done really well – but the people in the middle, not so much."

Additional Insight: Outlook from Two M&A Stalwarts

In conjunction with the Stalwarts Panel "2016 Restructuring Industry Outlook," The M&A Advisor asked two additional industry stalwarts to prognosticate on what the year ahead may hold. They are Brian A. Demkowicz, Managing Partner and Co-Founder of Huron Capital Partners, an operationally focused private equity firm based in Detroit, Michigan; and Charles Dabrowski, a Financial Life Advisor with Telemus Capital Partners LLC, based in Southfield, Michigan. Following are their responses to our questions:

"The opportunity set in distressed has widened significantly following the meltdown in high yield. The market has thrown the baby out with the bathwater."
- Charles Dabrowski

Q1: Are there new opportunities for investments in distressed debt in 2016? How may that differ from 2015?

Demkowicz: The retail sector could be an area to look, particularly small and mid-sized chains trying to compete with large online retailers. High yield bond in the energy and metals industries took quite a beating in 2015 with falling oil and commodity prices, so this could be an area for those with the courage to jump in.

Dabrowski: The opportunity set in distressed has widened significantly following the meltdown in high yield. The market has thrown the baby out with the bathwater. We think it will be a slower recovery than in the past, and that distressed risk should be gradually added here. It is important to hone in and do credit work to differentiate those names which have strong fundamentals and just appear distressed versus those that will face a tough path to recovery and are likely to file for bankruptcy. What will be different in this cycle from prior ones is that with interest rates near zero, even an accommodative monetary policy environment will not be enough for distressed issuers to refinance. There will be more bankruptcies and exit financing and capital will be harder to come by.

Q2: Is the energy sector a place to avoid or to find value in 2016?

Demkowicz: I think there will be some great value plays for disciplined and courageous investors. The energy market was hit hard in 2015 and there are likely some quality opportunities among the carnage.

Dabrowski: There certainly is opportunity in the space, but we think one has to be discerning and differentiate the extent to which a long energy name is just an oil beta call versus one with real alpha. Last year many distressed funds stepped into Exploration and Production (E&P) debt which proved to be a calamitous move. The problem was that even those situations where there was an exchange that had some process driven alpha, it was overwhelmed by the move in the commodity and liquidations of bonds in the space. We have seen an interesting dynamic in the past week where the large mutual fund company Franklin liquidated huge positions in the energy space. Franklin had been a huge player and often owned 15-30 percent of a single bond issue. Franklin was forced to sell some positions over the past few weeks driving some bonds down 30-40 percent.

Getting back to the main question: if energy bonds were appealing a year ago when oil was in the 50s, they should be more appealing here when everyone wants out and prices are hovering in the low 30s. That being said, there will be a number of filings in the space among the lower-quality names that have higher costs of extraction and more levered capital structure.

We would avoid energy names where a default is likely, and try to focus on higher-quality producers who can wait out the price declines. What is interesting about the rout in oil bonds is that there are many fallen angel bonds of larger well capitalized investment grade issuers that are now trading at highly distressed levels. We would prefer buying those higher quality E&P's and avoiding the lower tier companies that have a higher probability of filing for bankruptcy with currently very low recovery rates.

"While many banks and financial institutions tend to have short memories, I think Hedge Fund managers are much more cognizant of the "Black Swan" effect and have managed their portfolios accordingly."

- Brian Demkowicz

Q3: Are hedge funds, particularly those with large holding in energy, vulnerable? Is this year akin to 2007 for hedge funds?

Demkowicz: While many banks and financial institutions tend to have short memories, I think Hedge Fund managers are much more cognizant of the "Black Swan" effect and have managed their portfolios accordingly. Those who were long with large energy holdings obviously did not do well, however, they can still profit in this environment as these positions begin to recover.

Dabrowski: We think most of the pain is past for distressed hedge funds. The decline in energy re-priced all risk in the space leading to broader carnage and markdowns from a vicious cycle of redemptions and illiquidity. This was largely a 2015 event, with perhaps some carryover into 2016, but so many of the lower-quality energy names have been impaired to extreme levels, where the impact has to be mitigated on a going forward basis.

A year ago a typical lower quality E&P (e.g. Halcon, Sandridge, Energy 21, 77 Energy, Midstates Petroleum) had unsecured debt in the 60s and newly minted second lien bonds trading at 95. Today those 2nd liens are priced at 20-30, the unsecured at 0-3, and barring a quick $30 move up in oil they will all file for bankruptcy in 2016. A year ago there were frequent hypothetical discussions as to whether oil prices would stabilize and potentially get back to $70 a barrel. In those circumstances, the conventional wisdom was that these companies could escape bankruptcy. Today, with oil prices at $30 [a barrel], even a significant move up probably will not save these companies.

Q4: What industries appear more favorable for distressed investing in 2016?

Demkowicz: Energy, metals, retail

Dabrowski: We think there is opportunity away from energy in media and consumer-focused names.

Q5: What distressed industries are the most difficult companies to acquire and turn around?

Demkowicz: In our experience retail companies tend to be the most difficult. High fixed costs (rent), fierce competition from online retailers and the need for constant innovation to stay on trend are a few reasons.

Dabrowski: Even in a good oil environment E&P and natural resource companies that are forced into uncontrolled chapter 11 will face a challenging restructuring. Recovery rates thus far have been extremely low even for second lien or secured lenders. This has partly been a function of the price environment but there are fundamental aspects of this industry that make a restructuring more challenging:

1. The business is capital intensive and becomes severely cash flow negative given the high decline rate on existing wells if there is not further drilling.

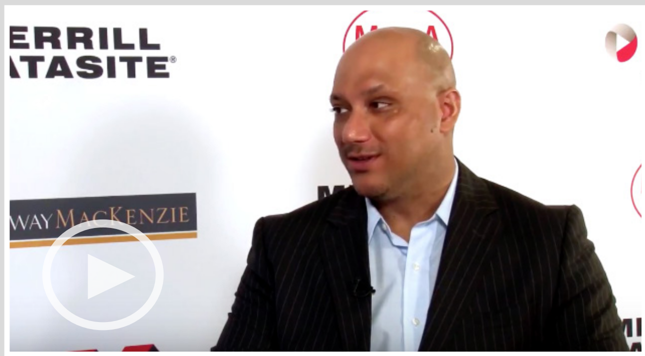
2. Many of these companies have joint venture contracts under which chapter 11 is an event of default or there is a requirement for certain levels of capital expenditure.

3. Companies may lose their drilling concessions in some jurisdictions if they are not actively drilling.

For the above reasons we anticipate a trend of prepackaged bankruptcies where new money comes in via rights offerings around the "fulcrum security". These plays may prove to be profitable but will still have significant exposure to the commodity.

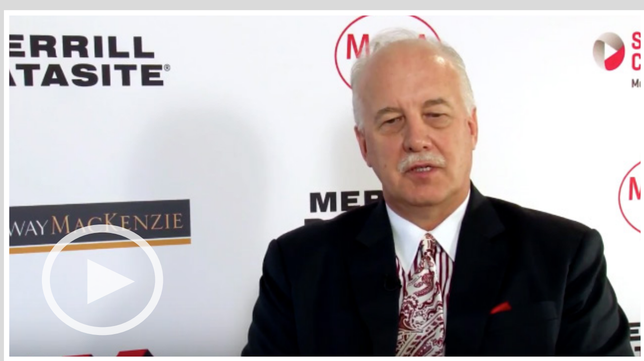
Video Interviews

To watch exclusive M&A Advisor interviews with these industry experts on "2016 Restructuring Industry Outlook", click on the following images:



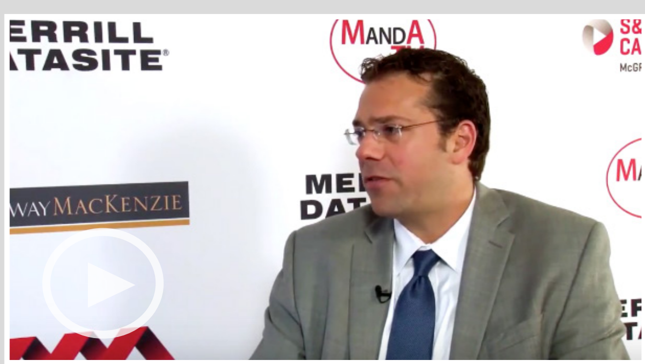
Karl D'Cunha

Senior Managing Director
Madison Street Capital



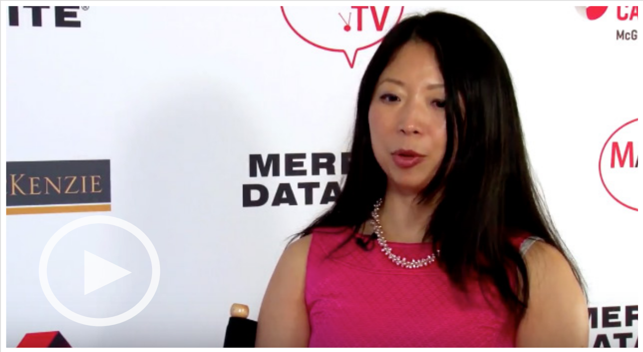
Patrick O'Keefe

Founder and CEO
O'Keefe LLC



Michael Pokrassa

Managing Director
Raymond James



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Symposium Session Video

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2016 Restructuring Industry Outlook

Presented by
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Clarity. Results. Together.

Contributors Profiles

Charles Dabrowski
Financial Life Advisor
Telemus Capital Partners LLC

Charles Dabrowski is a Financial Life Advisor with Telemus Capital Partners LLC, based in Southfield, MI. He works directly with his clients to devise comprehensive financial life plans that meet their short and long-term financial needs. He earned his undergraduate degree from the University of Michigan, his Juris Doctor from Wayne State Law School, and his Master of Law in Taxation from Chicago-Kent College. Mr. Dabrowski also gives much back to his community. He is currently the Intermediate Board President of the Detroit Athletic Club as well as a member of the Club's Strategic Planning Committee. He sits on and is the CFO of the Leaders for Kids Board of the Children's Hospital of Michigan Foundation. He is the founding chair of the Boy Scouts of America's Dodge for Detroit Dodgeball Tournament, which raises money for inner-city youth activities through scouting.

Karl D'Cunha
Senior Managing Director
Madison Street Capital

Karl D'Cunha is a Senior Managing Director at Madison Street Capital where he oversees the firm's services geared towards public companies, large private companies and asset management firms. The range of services include M&A Advisory, Capital raising, Fairness & Solvency opinions, Portfolio Valuation, Financial Reporting Valuation and Structured Finance Advisory services. Mr. D'Cunha has broad financial services experience including over 13 years experience in the asset management industry working with some the largest fund managers globally on valuation, M&A advisory and portfolio transactions. Mr. D'Cunha has been actively involved in investment company related services and has prepared, supervised, or consulted upon assignments geared towards US and International private equity, venture capital and hedge funds, investment advisors, mutual funds and other entities. Mr. D'Cunha holds a B.A. in Finance and Economics from University of Western Ontario and a Graduate Diploma in Accounting from McGill University.

Brian A. Demkowicz
Managing Partner and
Co-Founder
Huron Capital Partners

Brian A. Demkowicz is the Managing Partner and Co-Founder of Huron Capital Partners, a leading operationally-focused private equity firm with a long history of growing lower middle market companies through its customized buy-and-build investment model. Over the past 25 years, Brian has established a successful record of acquiring and growing middle market companies in partnership with experienced operating executives. He has extensive experience in executing middle market acquisitions, recapitalizations, restructurings, growth financings, and divestitures, closing over 200 transactions valued at over $2.0 billion. Brian holds a B.S. in Accounting from Purdue University, an M.B.A. from the J.L. Kellogg Graduate School of Management at Northwestern University, and is a CPA.

Patrick O'Keefe
Founder and CEO
O'Keefe LLC

Patrick O'Keefe is Founder and Chief Executive Officer at O'Keefe. Mr. O'Keefe is recognized as an expert in the fields of corporate reorganization, debt restructuring, turnaround consulting, refinancing solutions, due diligence support, valuation and litigation support. Mr. O'Keefe has been approved by the U.S. Department of Justice to act as a Chapter 11 trustee and has performed as a court appointed receiver for numerous operating companies. For over 25 years, Mr. O'Keefe has been active as a financial consultant and turnaround advisor to under-performing businesses in various industries including, retail, construction, automotive, manufacturing, and real estate, and has successfully completed assignments in out-of-court and Chapter 11 restructurings. Mr. O'Keefe is qualified in the area of litigation support services and has been accepted as an expert in federal and state court matters involving lost profits, valuation and economic damages. He is one of a handful of experts recognized by the Institute of Business Appraisers as a business valuator accredited in litigation.

Michael Pokrassa
Managing Director
Raymond James

Michael Pokrassa is Managing Director at Raymond James. Mr. Pokrassa works on advising clients on debt origination transactions in a variety of industries. Prior to joining Raymond James, Mr. Pokrassa spent two years in the portfolio group for privately held distressed and non-distressed investments at Silver Point Capital. Before Silver Point Capital, Mr. Pokrassa provided restructuring advisory services for six years at FTI Consulting, Inc. and PricewaterhouseCoopers LLP on behalf of distressed companies and their creditors. Mr. Pokrassa graduated with distinction from the BBA program at the University of Michigan Business School.

Jodi Xu Klein
Reporter – Corporate Finance and Distressed Credit
Bloomberg News

Jodi Xu Klein is a Reporter at Bloomberg News. Jodi is a multimedia financial journalist covering distressed investing and restructuring of corporate debt on the Corporate Finance team at Bloomberg. Jodi writes and speaks on TV and radio about levered companies and its balance sheet issues in struggling sectors, including oil and gas, coal, metals and mining, and retail. Coverage also includes distressed hedge funds and private equity firms' strategies in investing in distressed credits.

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Emerging Leaders Summit - New York, NY - June 10, 2016
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Live Web Broadcast "2016 European M&A Outlook" - London, UK - February 22, 2016

For additional information about The M&A Advisor's leadership services, contact Liuda Pisareva at lpisareva@maadvisor.com.