

REPRESENTING SENIOR LENDERS AS TURNAROUND ADVISER: WHAT MAKES A DIFFERENCE

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Most turnaround professionals I know prefer to represent only debtors and not to represent senior lenders. They would rather spend their time representing debtors, because they believe that is where the real action lies — at

the operating company, developing and implementing turnaround plans. To them, the financial adviser to the senior lenders is in more of a “watchdog” role without any real impact on the outcome.

While it is certainly true that there is more activity on the debtor side, it would be completely incorrect to assume that there is no action or impact from representing the lender side. Quite the opposite — the activities of the lender’s adviser are often a key component of a successful outcome for both lenders and debtors.

Scope of activities

Here is a typical scope for representing senior lenders in the middle market credit with multiple banks participating (usually between three and 12):

- Review the 13-week cash forecast to assess the feasibility of the borrower’s short-term financial plans,
- Review the borrower’s business plan, identifying:
 - Key opportunities for plan enhancement;
 - Management and key operational personnel capabilities;
 - Significant risks; and
 - Operating, financial and industry issues.

- Review and assess any management work product or recommendations relating to operational improvement opportunities,
- Prepare an asset sale valuation analysis that addresses the likely proceeds from sale of the borrower’s assets and the resulting recovery to the lenders, and
- Serve as financial advisers to the lenders.

To carry out this scope requires full access to the borrower’s management and to any relevant financial and operations information.

What’s Missing?

It would seem that the challenges are pretty straightforward: Understand what’s happening to the cash, assess the viability of the business and the plan to turn it around, perform a liquidation analysis to assess downside risk, and recommend and assist the lenders with appropriate restructuring alternatives.

So why do so many competent professionals achieve poor or mediocre results? What’s missing?

The short answer is that they need to get out from behind the spreadsheets and get actively involved in the process. Here’s my short list:

1. Strong communication to the lenders. No matter what the analytics show, each lender will have its own perspective, and financial advisers must keep the bank group from becoming dysfunctional.
2. Develop a collaborative relationship with the debtor-side adviser. The chances for a successful outcome will be enhanced by a protocol of positive collaboration, openly discussing analytical differences and establishing an open back-channel for communication.
3. Visibly immerse yourself in the ongoing monitoring “on-site” at the company.

A Recent Example

I recently advised a group of six senior lenders with a \$100 million exposure to a

fashion accessory company. The lenders were faced with a significant decision before a full turnaround plan could be developed: whether to immediately fund \$25 million of working capital to allow the company to produce product for the Christmas season. Without it, the company would not survive.

Our analysis confirmed that a forced liquidation would likely mean a loss of \$35 million to \$50 million for the banks. On the other hand, if the lenders were willing to fund there was a strong chance that they would have no additional funding exposure at the end of the season and the company would have nine more months to effectuate a turnaround plan.

It was a tough decision for the lenders, but the deal got done and the lenders funded the season. This is what made the difference:

1. We became the communications focal point, with daily phone calls and lots of one-on-one conversations. We received approval from all six lenders — no easy task.
2. Strong collaboration with the debtor’s financial adviser led to trust, and we agreed on a funding plan that included achieving certain milestones along the way.
3. We advised the lenders to require that the debtor’s financial adviser be appointed chief restructuring officer, that monitoring and reporting be increased, and that the company undertake a recapitalization or sale effort within the one-year forbearance period.

As a result, a year after we began, the lenders were taken out at par plus payment of all deferred interest. What made the difference? One-third analytics, and two-thirds actively managing the process. Who says all the action is at the debtors’ level?