Dechert Distressed Investing Forum
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We are approaching the end of one of the longest growth cycles on record.

For a number of years, Dechert envisioned a global discussion on the restructuring industry. Our Forum united academic thought leaders, distressed investors, investment bankers and industry professionals with our own experienced attorneys to discuss the most compelling current financial opportunities and legal challenges in the marketplace.

Today, we are approaching the end of one of the longest growth cycles on record. Our strategies are influenced by rising U.S. interest rates, increasing market volatility and devaluation of emerging markets currencies, all while tariffs and the potential trade war with China impact the financial performance of individual companies and the economy as a whole.

The Dechert Distressed Investing Forum focused on the areas that we believe have the potential to create the most value for our clients. Through this conversation, Dechert attorneys bring clarity to our clients as they seek to understand where to deploy their resources, and grasp the complex legal issues surrounding the sector.

Each session included lively exchanges of points of views and discussions of the most important questions of the day. All part of our effort to help our clients adapt and find value in the distressed investment marketplace.
The US economy has shown it is remarkably able to rebuild and restructure by incorporating new ideas into organizations in a way to show resilience.

Professor Goolsbee took the room of 150 industry leaders on a trip from the Wild West through to present day and into the future as he discussed the waves of economic success and the impact of distressed times. His insights into the global economy touched on growth prospects, the likelihood of a recession and the effects of the tax cuts, tariffs and trade war with China.

As he highlighted the trends driving success and potential recession catalysts, Goolsbee brought to light recent forecasts. For example, with the Fed having over-estimated their GDP growth and inflation projections 9 years in a row, Professor Goolsbee wondered whether the model is wrong or if the fundamentals and assumptions no longer apply. The implications of which are meaningful in light of the Fed’s recent raising of rates and our ability to predict future performance.

Goolsbee anticipates very little overall impact of government on the economy other than the effects of the tax cuts and the uncertainties surrounding trade policy, which he dubbed a “black hole.”

Looking forward, Goolsbee suggested the next slowdown will not look like 2008 but will more likely begin in markets subject to domestic currency fluctuation against the dollar where costs, prices and asset value may be affected, a trend potentially exacerbated by global trade policies.

Goolsbee remains positive about the favorable demographics, high productivity and unique innovation resonating in the U.S economy. He advised attendees to keep an eye on the emerging markets, where the first signs of stress were likely to appear, and to monitor the trade tensions that are a potentially destructive unknown.
The question isn’t just where the company is located, but where the assets are and from which court can we best control the creditors. If we can’t do that, we’re probably not going to get the outcome we want.

The changing landscape of jurisdictional courts and the industry impact resulting from the adoption of UNCITRAL Model Law.

Twenty years ago, the United Nations Commission on International Trade Law (UNCITRAL) issued the Model Law on Cross-Border Insolvency. Since then, legislation based on the model law has been adopted in 46 countries, including, with the 2005 addition of chapter 15 to the Bankruptcy Code, the United States. The model law was designed to maximize value for debtors’ stakeholders, while providing courts in one country the discretion to enforce the orders of courts in a different country to facilitate cross-border restructurings.

The Model Law is applicable on the same terms to restructurings involving companies located in developed nations as well as those located in emerging markets regardless of the development of such countries’ insolvency laws and adherence to the rule of law.

The Model Law provides a form of Modified Universalism, a mechanism for courts in one jurisdiction to have discretion to formally recognize a “foreign main proceeding” and orders of a foreign court. The recognition of a “foreign main proceeding” depends on whether the foreign proceeding is occurring in the country where the debtor has its “center of main interests.”

In the United States, if a foreign proceeding meets the requirements for recognition of a “foreign main proceeding,” the United States court has discretion to enforce orders of that court with respect to assets in the United States, including orders confirming plans of reorganization, if the orders and the process leading to them meet the requirements of the foreign jurisdiction and do not run afoul of United States public policy or other chapter 15 requirements even if such debts are governed by the laws of a U.S. state.

In the UK, however, in a recent case the UK court said it could not enforce a foreign plan where the debt documents were governed by the laws of England and Wales and the plan did not comply with UK law.

The percentage of defaults occurring in emerging markets, as percentage of entire global defaults, has been increasing. Many of the countries in which these emerging markets reside have not adopted the UNCITRAL model law. In addition, because the courts in certain such countries can provide a “home court advantage” to debtors, investors may have reason to question their confidence in such courts with respect to protecting the interests of international creditors. Accordingly, investors must take a multifaceted approach to attempting to maximize recoveries that may simultaneously involve negotiation regarding a consensual workout and litigation in the home country of the debtor as well as countries where ancillary proceedings, such as a Chapter 15 proceeding, have been commenced.
Opportunities and Challenges in Today’s Distressed Real Estate Market

The effects of rising rates, real estate bankruptcy trends, the plight of retail and emerging trends in office real estate.

The cost of borrowing has gone up, with the rise in interest rates outpacing credit spread compression to date. This may have a moderate impact on the number of transactions and may soon affect real estate cap rates as well. So the question becomes whether loans closed earlier in the cycle will become problematic as these deals approach maturity in a rising interest rate market. Are these borrowers going to be able to refinance?

Most panelists agreed that we are approaching a transitional period; one that should not be too prolonged in part because there is liquidity and capital available, currently sitting on the sidelines.

The prevalence of cash traps in CMBS 2.0 loans, the removal of fair value purchase options, the change in incentives to servicers in CMBS 2.0, and the move to the appraisal reduction method for control instead of realized losses will have an impact on workouts and the sales of distressed loans in CMBS going forward.

Voluntary bankruptcies are a less viable opportunity for distressed borrowers. Bankruptcy recourse provisions and pro-lender case law on the enforceability thereof have reduced the number of voluntary real estate bankruptcy filings (except where the sponsor itself is also insolvent (e.g., Toys R Us), so out-of-court restructurings are more likely to happen.

In retail, the sector with the highest delinquency rate, the outlook is guarded and all panelists agree that retail repositioning is critical to appeal to changing consumer patterns and tastes. Similarly in the office sector, the “WeWorks” of the world have changed how tenants think about leasing and their expectations for space. This has resulted in a general decrease in the length of the term of office leases and an increase in the amount of capital needed due to tenants seeking more pre-built out spaces containing more robust amenities. While the “WeWork” model may work in NYC, will it work in secondary and tertiary markets?

Opportunities remain. In the U.S. market, there is substantial capital sitting on the sidelines. As certain asset classes (retail) are struggling and others (office) are going through a transitional period, there are opportunities for agile and forward-thinking investors through repositionings.
Hurricanes in the Caribbean: Recent Developments in Venezuela, Puerto Rico and More

What can bondholders expect now that Crystallex has pierced the veil between Venezuela and PDVSA – and is now the time to sue? And should creditors of Puerto Rico and its many public corporations be concerned to the extent that their constitutional rights are protected? The answers are complicated.

The potential sale of PDVSA’s most valuable assets in the U.S. for the benefit of Canadian mining company has provoked concern among holders of both Venezuela and PDVSA bonds that so-called “award creditors” are many months ahead in their collections efforts, and that bondholders will lose out if they don’t begin asserting their legal rights soon.

Another question on bondholders’ minds is whether Crystallex’s landmark “alter-ego” decision will be affirmed on appeal, and whether the lower court will order the sale of PDVSA’s most significant U.S. asset before the appellate court can weigh in. The case that Venezuela controls PDVSA is strong and supports the alter-ego decision. But how can it be that a court can take away PDVSA’s property without having to find that it has jurisdiction over PDVSA?

These are difficult questions with potentially monumental implications for sovereigns and their creditors alike. Bondholders who choose to watch from the sidelines will do so at their own peril.

Complicating the issues are the sanctions the U.S. has in place on Venezuela. Although described as solely designed to influence regime change by explicitly targeting the country’s ability to access new debt funding, these sanctions severely constrain U.S. bondholders’ freedom to act and are simultaneously driving Venezuela to borrow from China and Russia – decreasing the influence of the U.S. in its backyard, and benefiting no one but Russia and China.

Similarly complex with potential for precedent-setting results is PROMESA, The Puerto Rico Oversight, Management and Economic Stability Act. The bill is designed to help Puerto restructure its debt and expedite the process for critical infrastructure projects. As the territory looks to restructure debt, the extent of the protection provided to lien guaranties under the Fifth Amendment’s guarantee that “private property shall not be taken for public use, without just compensation,” has become an issue.

Opportunities appear likely in multi-creditor and third party brokered deals.

Moderator
Dennis Hranitzky, Partner and Co-Chair, International and Insolvency Litigation Group, Dechert

Panelists
Eric Brunstad, Partner, Dechert
Lee Grinberg, Portfolio Manager, Elliott Management Corporation
Darshak S. Dholakia, Associate, Dechert
Aviva Werner, General Counsel, Emerging Markets Traders Association
Raising Credit and Distressed Debt Funds

Opportunities for distressed capital despite cost pressures and regulatory headwinds. The question is where and when.

Even with a strong environment there are opportunities for distressed debt. The speakers were quick to point out prospects in specific distressed sectors such as fossil fuel, retail, and energy. Right now there's approximately $25 billion available in the market focused on distressed debt.

It's still a challenging stretch for investors. They are seeking innovative fee structures, battling changing SEC regulations about fiduciary duties, seeing more complex tax structures and trying to understand disclosure compliance requirements. While all this is going on, they must remain focused on investment strategies and disciplined in their asset allocation.

Where are the investors? For that, the panel suggested, you have to look at geography. While it's hard to raise capital in the U.S., the distressed market in Europe never slowed down and the European banks are forecasting their biggest year ever. They discussed how geographic location drives investment policy, investors’ preferences and product selection.

The panelists examined fund consolidation and liquidation issues. The discussion of a fund’s end highlighted the evolution of secondary markets with new entrants, new strategies and new, often more creative structures. While investors will focus on the fund performance, the life of the manager becomes just as critical as the life of the product.

Who’s smart enough to predict a changing event? For this group, timing is still a mystery facing lenders, borrowers and investors. The best scenario would be gradual change, allowing businesses to adjust to new environments rather than one event leading to a monumental crash.

Moderator
Thomas Friedmann, Partner and Co-Chair of Global Corporate Finance and Capital Markets Group, Dechert

Panelists
Jackson Craig, Managing Director, Bayside Capital
David Klein, Managing Director, Credit Suisse Private Fund Group
Ron Rawald, Head of International Real Estate and Senior Managing Director, Cerberus Capital Management
Cynthia Williams, Partner and Co-Head of CLO Group, Dechert
About Dechert

Dechert’s Financial Restructuring Group

Comprehensive global experience in sophisticated restructuring, bankruptcy and insolvency matters.

Dechert offers broad experience in handling the most complex assignments, representing creditors, investors and troubled companies in all types of in-court and out-of-court restructuring matters around the world.

Dechert advises clients in highly sophisticated, precedent-setting matters involving many of the largest and most complicated deals. We work in emerging markets across a broad range of industries.

Dechert draws upon the expertise of our other top-ranked global practices to deliver high-quality advice in complex restructuring matters. Applying our collective skills and backgrounds allows us to provide seamless cross-disciplinary representation in any insolvency, restructuring or reorganization situation.

About Dechert

Dechert is a leading global law firm with 27 offices around the world. We advise on matters and transactions of the greatest complexity, bringing energy, creativity and efficient management of legal issues to deliver commercial and practical advice for clients.
Thank you

Ranked among the top 30 restructuring law firms globally.
Global Restructuring Review, 2018

Ranked among top firms for corporate restructuring (incl. bankruptcy) in the U.S.
The Legal 500 (U.S.), 2018

 Ranked among top firms for bankruptcy/restructuring.
Chambers USA, 2018

Our success is a reflection of our clients’ success.

“Law Firm of the Year” for the Americas, Europe and Asia-Pacific. The first time a single firm won in all three regions.