

## Distressed Debt News

# TMA panel: Retailers expected to 'muddle through' 2010 with help of consumers, lenders

By *Stephanie N. Rotondo*

Portland, Ore., Feb. 25 – As the economy inches toward a recovery, some experts believe that the retail arena will see some signs of improvement – but optimism is cautious at best.

Such was the crux of the discussion during Turnaround Management Association's industry outlook webinar held Thursday, entitled "What's in store for the retail industry in 2010?"

Retailers suffered greatly during the economic downturn that began in mid-2007. Come 2008-2009, discretionary spending hit all-time lows, resulting in weaker revenues and, in some worst-case cases, bankruptcies and liquidations.

In response to the weakening economy, many retailers took to reducing costs and inventories and increasing discounts, seeking to attract the new consumer: that is, the "value shopper."

But as 2010 gears up, the question remains: How will retailers rebound?

## Sales help recovery

There are some signs of recovery in the retail world, as typified by the 2009 holiday season.

In 2008, holiday sales were among the worst ever seen, according to Kenneth Latz, director of Conway Mackenzie Inc. and moderator of the TMA webinar. Revenues during that time were down 10% to 30%. As 2009 began, sales "continued to soften," he said.

But when the 2009 holiday season arrived, retailers were better prepared than a year before. Inventories had been reduced – in some cases drastically – and cost structures had been cut, restructurings done or in process. The result was a holiday sales season that "outperformed expectations."

Joel Glasky, president of Financo Securities, noted the "old adage: Retail leads us into a downturn and then leads us out" into recovery.

"I don't think anyone is convinced that

we are out of the woods yet," he said, but added that there was some comfort in the rebounding sales figures seen in the last few months. What is an important part of that recovery is how retailers have responded to things such as lower discretionary spending, unemployment and the like.

Still, total sales are "only one part of the equation when we evaluate financial performance," Glasky said. The bottom line is an obvious factor, but the "intangible value" of a company and whether it is on a "path for success" also play a role.

And, it's the fundamentals of the industry that will prove which companies have what it takes to "muddle through" 2010 and emerge stronger and more stable.

## Consumers, come back!

Consumers, for their part, have a role to play as the retail sector poises itself for recovery. Without consumers, retailers cannot improve sales and thus their fundamentals will remain shaky.

Currently, unemployment rates are at nearly 10%, the highest point since 1983. According to industry reports, consumer spending was flat in January and is expected to remain so in February, according to Glasky.

But the news isn't all bad. While unemployment is certainly high and concerns about job security have resulted in higher consumer saving rates, retailers are seeing a modest uptick in sales, which Glasky believes is largely due to the discounts being offered.

"Now, it is OK to buy, but value is key," he said.

For example, he said, consumers have learned that if they find an item they like, if they wait three weeks, they can come back to find that same item discounted "20, 30, 40%."

Even luxury retailers, such as Saks, have attempted to attract the "largely absent" aspirational shopper by "reaching down into lower price structures."

Still, 2010 won't be without its problems, as consumer credit continues to be tight. But Glasky speculates that credit issues – at least as far as the consumer goes – are not "the key ingredient."

"Clearly, it's not going to help," he said. "Consumer credit is a factor, but I wouldn't say it's a driver.

"We know there is cash out there," he added. Really, it is the "reluctance to spend" that is affecting the "psychology of influencing individuals' behavior."

## The role of the lender

After the surge of bankruptcies and liquidations seen in 2008 and 2009, debtors and creditors have become adverse to such actions and are instead "buying time," as Gregg Galardi, a partner at Skadden, Arps, Slate, Meagher & Flom, put it.

"As a result of liquidations in 2008/2009, ABLs and lending rates were cut as far back as they could go," Galardi said. Some companies, however, were still unable to get financings at reasonable terms, which resulted in "out-of-court actions," such as store closures and inventory clearance sales.

"Lenders are going along with that because they did take some heat from the last round," he explained. And such efforts have helped to avoid Chapter 11 filings.

In 2010, Galardi said he expects to see creditors – specifically secured lenders – providing amendments and waivers, "letting retailers have enough rope to get through 2010."

Jeffrey Bloomberg of Gordon Brothers Group, however, sees those actions as simply "people kicking the can down the alley." Glasky also sees that point, calling such efforts "amend and pretend."

"Clearly [the recession] has biased both debtors and creditors against the bankruptcy option," Glasky said. "It's really got to be more of a financial restructuring, which in the retail world is very difficult" as that

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## AbitibiBowater files NAFTA arbitration notice for C\$500 million claim

By Caroline Salls

Pittsburgh, Feb. 25 – **AbitibiBowater, Inc.** has filed a notice of arbitration under the North American Free Trade Agreement (NAFTA) in connection with the expropriation of its assets and rights in Newfoundland and Labrador, Canada, according to a company news release.

The company contends that the provincial government's December 2008 enactment of Bill 75, which expropriates an extensive array of Abitibi's rights and assets, "was arbitrary, discriminatory and illegal under international law."

AbitibiBowater said its claim seeks direct compensation for C\$500 million of damages, plus additional costs and relief deemed appropriate by the Arbitral Tribunal, making it one of the largest claims ever filed against Canada under NAFTA.

Under international law, the Canadian Federal Government is responsible for the actions of Newfoundland and Labrador in violation of the investment protection provisions of NAFTA.

In early December 2008, AbitibiBowater said it announced capacity-reduction measures in Canada and the

United States, including the permanent closure of its Grand Falls-Windsor, Newfoundland and Labrador mill, because of the economic downturn and decline in product demand.

In retaliation, the company said the province hastily passed Bill 75, without any attempt to consult with AbitibiBowater and without holding any public hearings.

According to the release, the company has claimed that the bill "unquestionably breaches Canada's NAFTA obligations on a number of grounds," including unlawful expropriation, fair compensation, treatment in accordance with international law, the bill's seizure of the company's rights violated standards, denial of justice and discrimination.

"The expropriation was detrimental to the financial position of our company," AbitibiBowater president and chief executive officer David J. Paterson said in the release.

"After operating in Newfoundland and Labrador for more than a century and contributing significantly to the region's economic, social and sustainable development, the nationalization of AbitibiBowater's assets was unexpected

and unnecessary.

"AbitibiBowater has been engaged with the Government of Canada and the Government of Newfoundland and Labrador in an effort to achieve a fair and equitable settlement and avoid a protracted NAFTA case.

"Unfortunately, despite those extensive discussions, we are unable to resolve the matter at this time and the company has no choice but to file a formal claim under NAFTA.

"It is our obligation to defend the interests of our stakeholders and ensure we receive compensation for the fair market value of the expropriated assets, plus additional damages."

The company said it has invested hundreds of millions of dollars in the province over the last century, ranging from capital investments in mill and hydroelectric generation operations to road projects that have helped build rural Newfoundland.

AbitibiBowater, a Montreal-based producer of newsprint, commercial printing papers, market pulp and wood products, filed for bankruptcy on April 16, 2009. Its Chapter 11 case number is 09-11296.

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will not change the fundamentals of the industry.

#### Fewer bankruptcies, more opportunities?

How, then, do all these factors add up? The panel members all agreed that 2010 will see fewer bankruptcies and liquidations than the last few years as lenders and companies attempt to work together to turn around the sector.

"Unless somebody absolutely has to, I don't expect to see any big retail bankruptcies," Galardi said. "Maybe in

2011, if fundamentals don't change, perhaps we will see another surge of filings."

For those companies that are "hemorrhaging money," Bloomberg puts it like this: "Those that have no *raison d'être* will go down the line and basically cease to exist."

Still, there are some opportunities in the distressed debt – and even non-distressed debt – arena that investors could take advantage of.

For Glasky, it will require a lot of homework on the part of the investor to find specific credits within the retail sector that represent real value. One of the

key things to look at, he said, is the level of leverage as well as the fundamental enterprise value.

"It's much more selective world," said Bloomberg. "Some [bonds] are overpriced right now" and "investors will have to work to find value."

In the end, retailers are largely believed to be preparing for the worst but hoping for the best.

"The caution flag is still out," Glasky said. While there is some optimism, "the lessons learned in the last year" were taken to heart and retailers are modeling for downsides.