



Succeeding in Turbulent Times

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ADVISORY

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Agenda

- Introduction
- Debt Capital Markets New Realities
- Balancing Cost Take-Out While Sustaining Business-Building Capacity
- Managing the Risks – Distressed Business Acquisitions
- Question & Answer



Debt Capital Markets New Realities

New Market Realities

- Economic slow down is from a level that had been enabled by unsustainable financing
- Credit-led downturn is unique in modern history
- Financial Contagion not a new concept, but a new experience for Canadian business
- The instability in global banking markets coupled with economic slow down is a potent poison
- Trillions of dollars are (trapped) in various loan conduits
- Institutions have lost the ability to sell financing instruments into securitization conduits which reduced capital requirements in the past – now capital is scarce and more expensive

The United States – A Perspective on U.S. Led Contagion based on Projected 2007 GDP



Overview of Current Economic Conditions United States

US economy in recession as consumers pull back

Struggling to cope with the significant issues in the banking system and financial sector

Economy expected to bottom out in mid 2009 with unemployment at 8% according to US economic outlook conference

Real unemployment is much higher

GDP Growth	Q3	- 0.1%
	Q2	2.8%
	Q1	0.9%
Retail Sales Growth	Q3	- 2.3%
	Q2	1.3%
Unemployment Rate	30-Nov-08	6.7%
Housing Index	07 Q3 to 08 Q3	- 4.0%
Source: US Bureau of Economic Analysis		

Overview of Current Economic Conditions Canada

Canadian economy has fared better than US so far

Financial sector in better condition when compared to the US

However, manufacturing sector linked through the auto industry and restructuring yet to be felt

Commodity prices are having a big impact on capital spending and Canadian stock markets

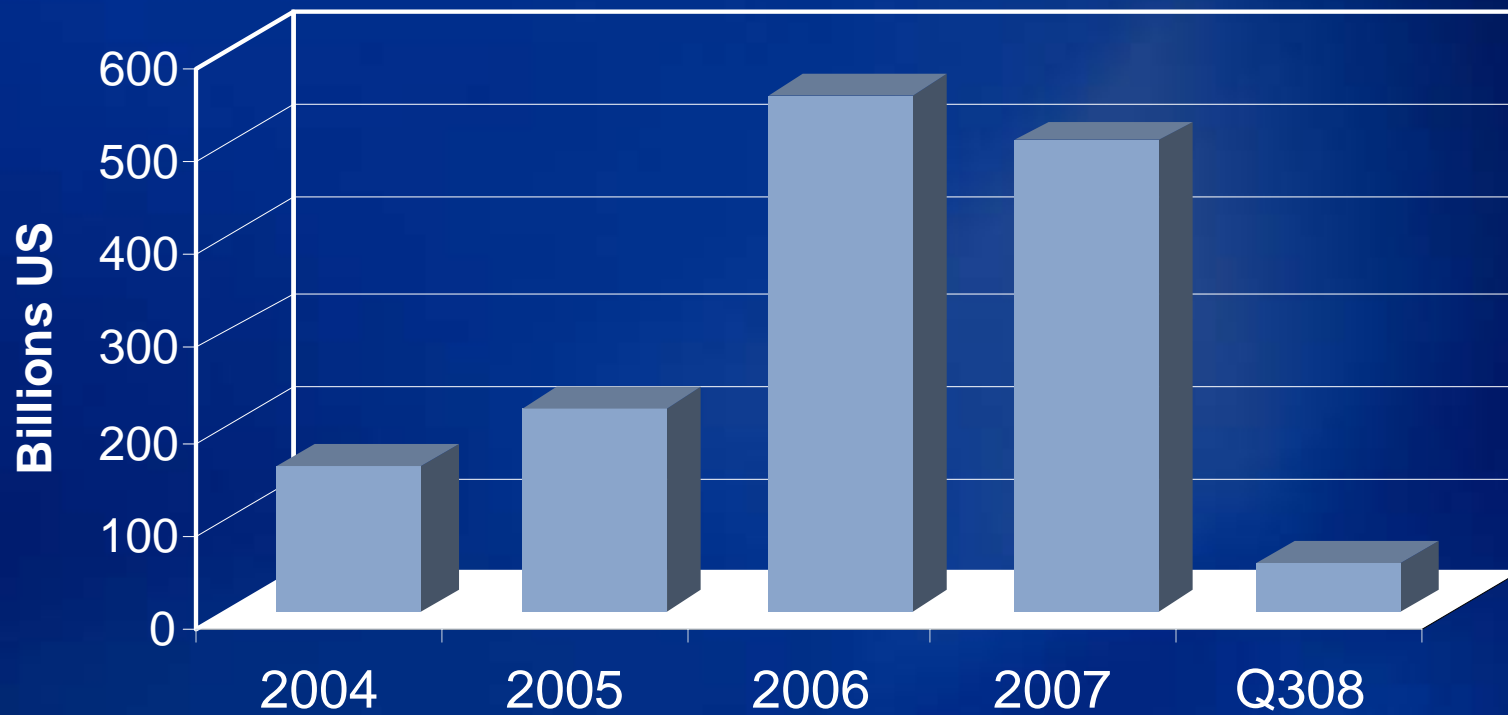
GDP Growth	Q3	0.1%
	Q2	0.8%
	Q1	0.2%
	Sept – Oct	- 0.9%
Retail Sales Growth	12 mos Oct	4.1%
Unemployment Rate	30-Nov-08	6.3%
Raw Material Index	Oct – Nov	- 13.40%
Housing Index	12 mos Oct	-1.5%
Source: Conference Board of Canada/Stats Canada		

Secondary Banking Market

- Loans in conduits are being “dumped” onto the market because of pressure experienced by conduit managers
- Hedge funds, insurance companies, other institutional investors who need capital force the sales
- Discounts on debt in secondary market range from 10% to 30% on par for good loans, more for distressed borrowers, putting pressure on primary lending rates
- Banks not lending to each other
- Cost of funds is way up

CDO Issuance Has Tanked

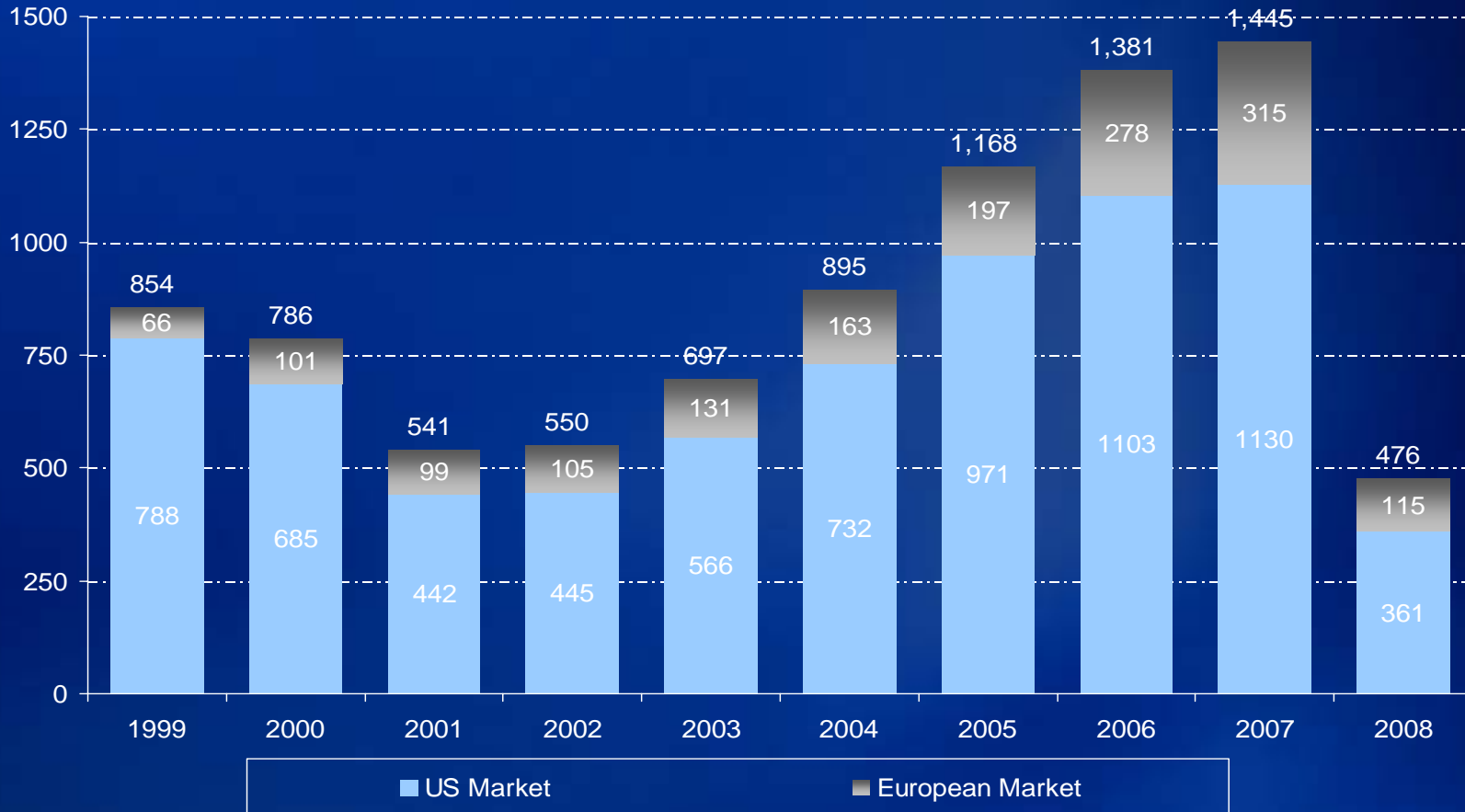
Global CDO Annual Issuance



Source: SIFMA/S&P

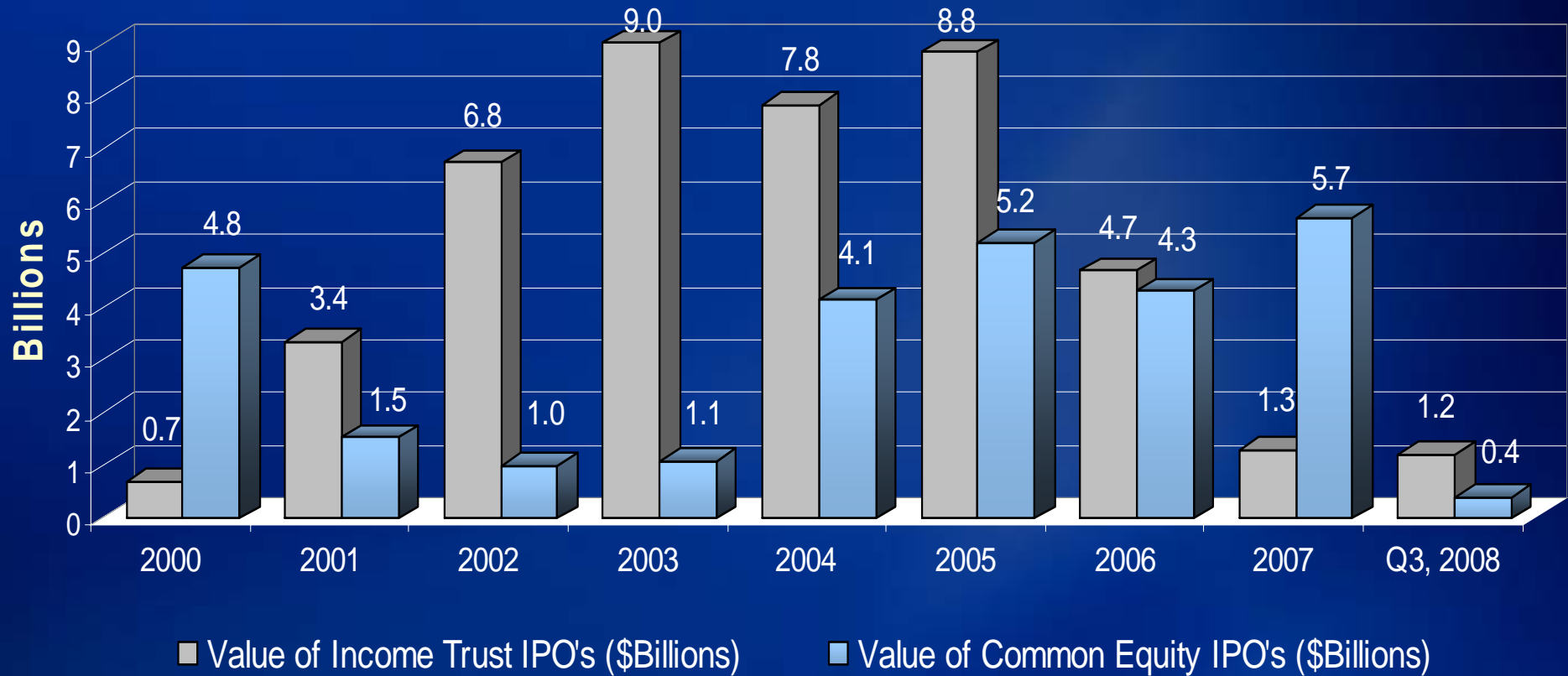
Predictable Private Equity Slow Down

Senior Loan Volume US and Europe - Sponsored Transactions



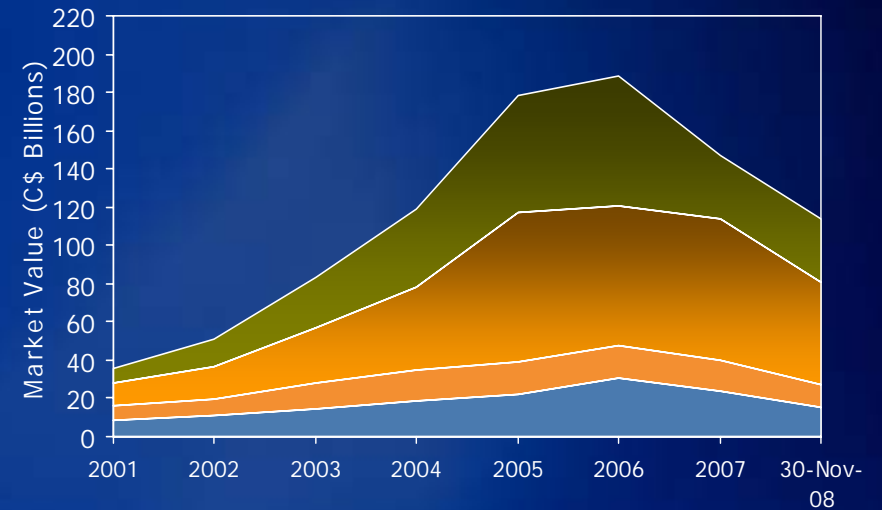
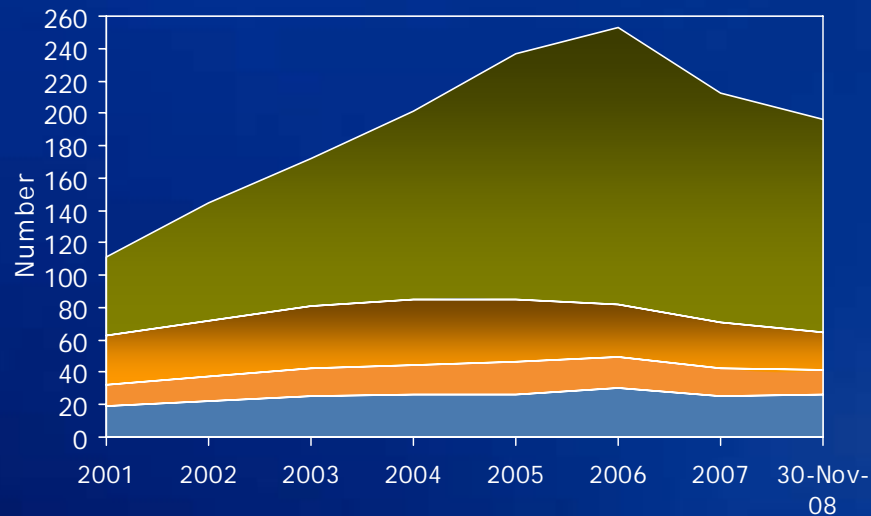
This chart reflects the estimated primary volume to the US and European loan markets. Deal Count combines first and second lien portions of the same transaction into one event and excludes amendments.

Almost No Canadian IPO Activity



Source: Investment Industry Association of Canada

Income Trusts: Numbers and Values Down



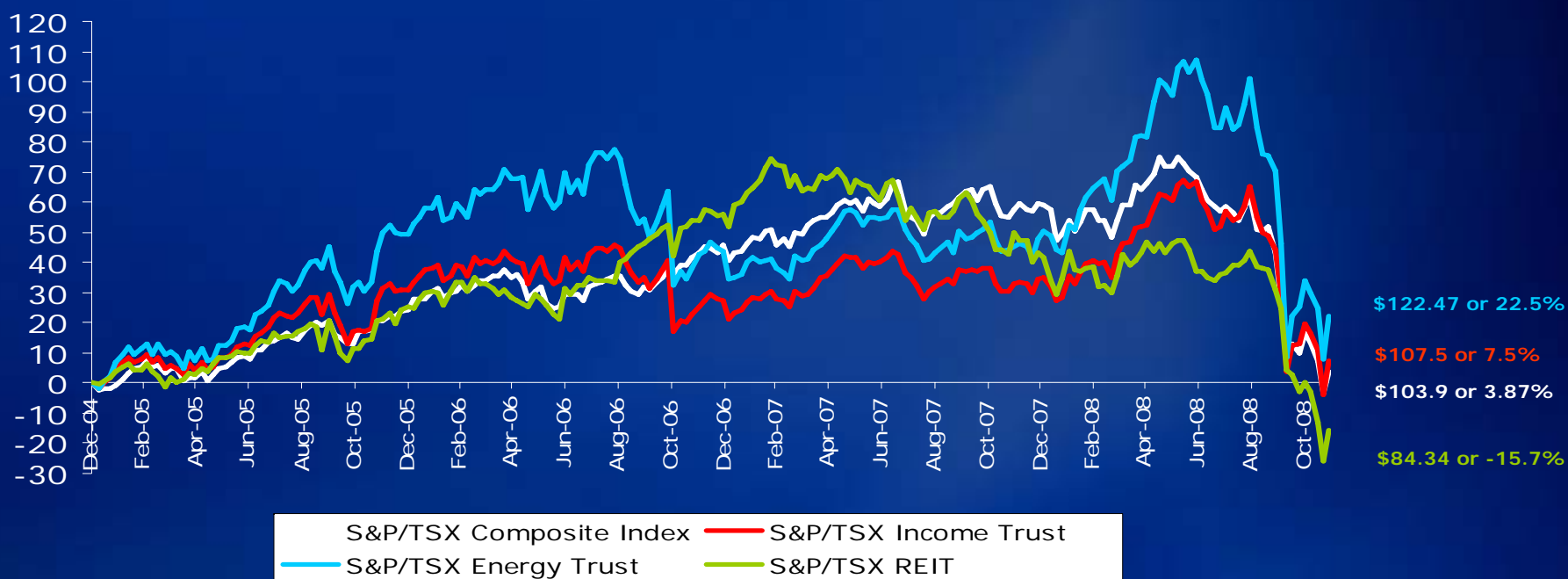
REIT Power & Pipelines Energy Trust Business Trusts

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Source: TSX (as at Oct 31, 2008)

Canadian Market Performance

Total Return Performance
S&P/TSX Composite Index vs. Trust Indices



*Assumes initial investment of \$100
December 31, 2004 to November 27, 2008

Source: TSXConnect

Changing Debt Markets – Some Benchmarks

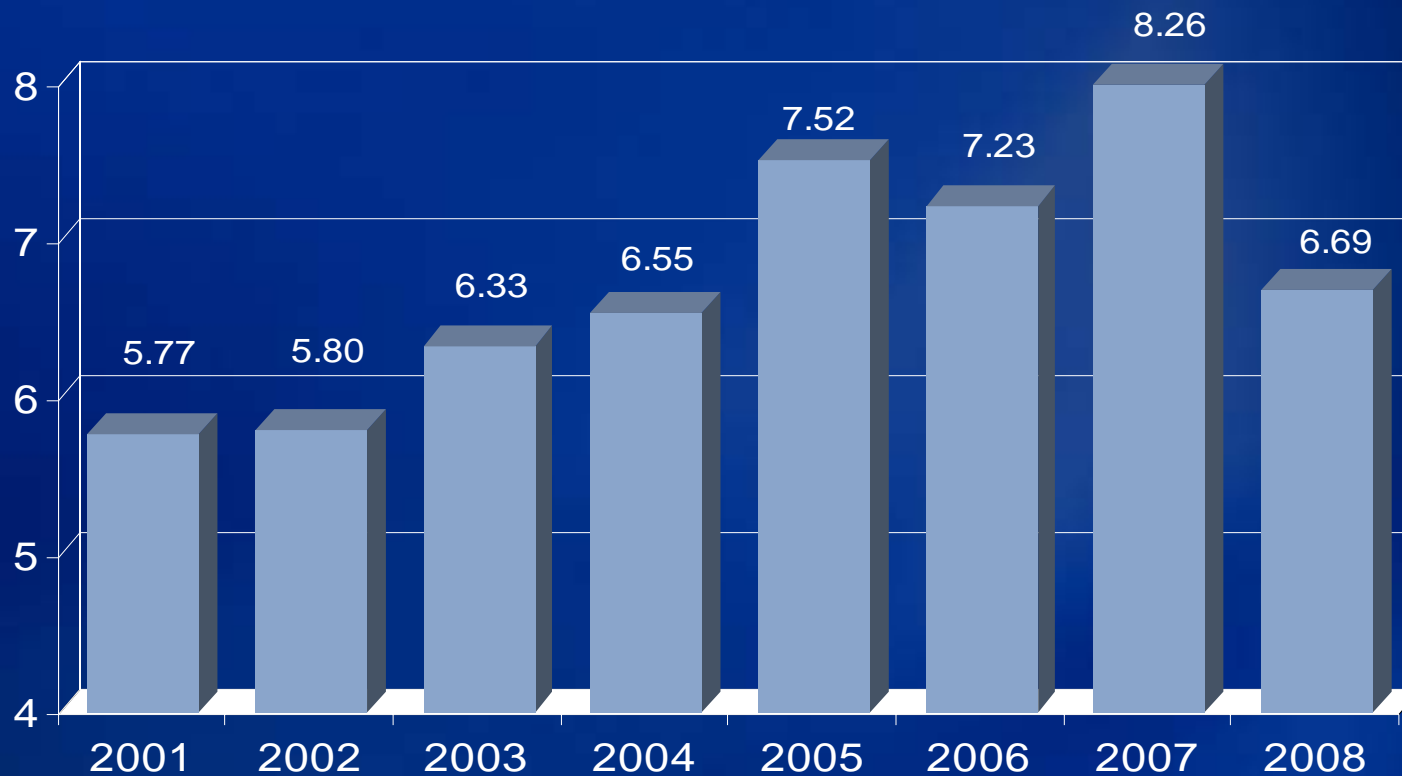
	Prior to August, 2007	Current - 2008
Credit Environment <ul style="list-style-type: none"> • Senior Debt Borrowings • Total Debt Borrowings • Fixed Charge Coverage • Equity/Total Capital 	Aggressive - very liquid <ul style="list-style-type: none"> • 3x to 4x EBITDA • 4.5x to 5.5x EBITDA • 1.00 to 1.20x • Reducing 20% to 30% 	Conservative – modest liquidity <ul style="list-style-type: none"> • 2.25x to 2.75x • 3.25x to 3.50x • 1.25 to 1.50x • Increasing 40% to 60%
Cost of Debt <ul style="list-style-type: none"> • Senior Debt • Subordinated Debt • Transaction Fees 	Low <ul style="list-style-type: none"> • LIBOR + 2.0% to 3.00% • All-in-rate: 11% to 14% • 0.75% 	Increasing <ul style="list-style-type: none"> • LIBOR + 4.0% to 6.0% (Rising) • Coupon: 15% to 18% • 1.0% to 2.0% • Warrants on Junior Debt
Typical Bank Hold Limits	\$40-60 million	\$15-30 million

Impact of Tight Credit Markets

- A global problem – loan syndication very difficult to undertake, transaction multiples impacted
- Broken syndicates may pose future risks
- A number of lost lenders
- Secondary loan markets offer better yields reducing primary financing availability
- Refinancing risks are high because hold limits are down and pricing is going up
- WACC out of whack – de-leveraging will be the end result
- Equity capital not easy to come by, although PE and some strategic buyers in the market

Transaction Multiples

**Average Purchase Price/Adjusted EBITDA Multiples:
LBOs < \$250 million**



Source: Standard & Poor's LCD

How to Cope

- Lender confidence is paramount
- Canadian business will need to get ahead of the curve
- Overall de-leveraging is going to take place given liquidity constraints
- Companies will have to manage working capital and cash employed and convert redundant assets to cash
- The cashless merger has been used in the financial and airline sector in the US as a means of coping with the problem; the auto industry is thinking about it. With credit pressures on, being open to this type of transaction will become a staple of good governance
- Canadian business will need to think about it as well

M&A Impact

- Some strategic buyers are on an “acquisition strike”; others see this as a great opportunity
- A good time to buy or merge
- Mergers can be pre-emptive, help defend against economic downturn, preserve and restore shareholder value
- Lots of debt for sale. Purchase of debt may be the best first step to facilitate a business acquisition
- Acquisition opportunities will present themselves as many companies experience financial distress

A man in a dark suit and tie is shown from the chest up, sitting at a desk. His hands are clasped together in front of him, and he has a thoughtful expression on his face. The background is a blurred office setting.

Balancing Cost Take-Out While Sustaining Business-Building Capacity

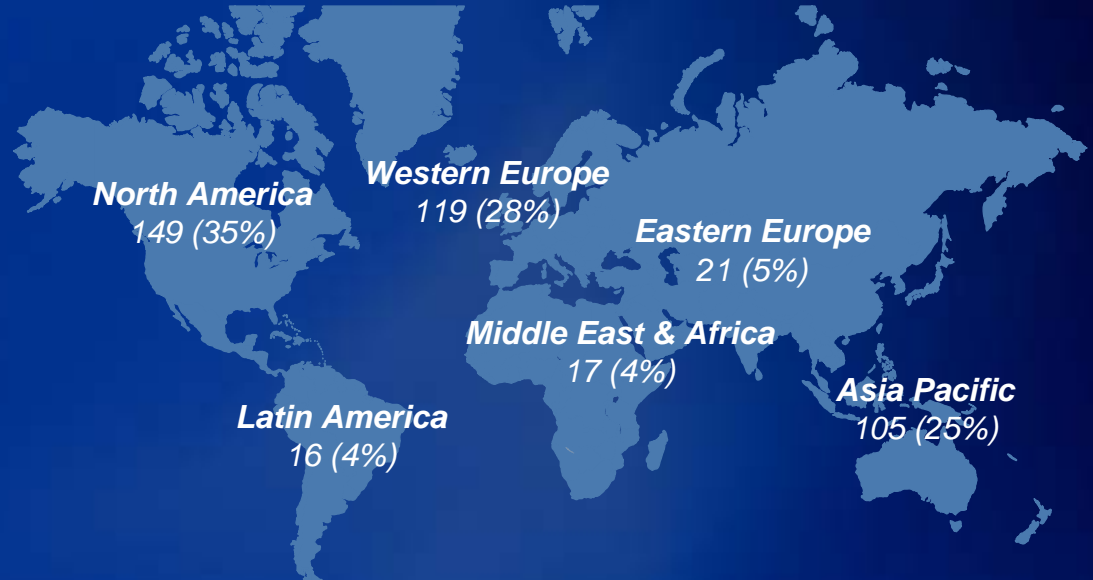
“

Cost optimization is never a static goal. It is an evolving process that requires constant monitoring, adjustment, and improvement. ”

“

We started an evolution that began with cuts. But cutting costs and not meeting business objectives doesn't solve problems. ”

KPMG's Global Survey



- KPMG retained the Economist Intelligence Unit
- Survey of 427 companies globally
- Detailed interviews with C-level executives and practitioners

Challenges in Cost Optimization



Cost strategies are failing



Cost ownership is unclear and too narrow



Revenue growth has eroded cost discipline



Cost strategies are too cautious



Cost discipline is not embedded in the culture



Cost drivers are not clear or transparent

Cost Strategies are Failing

In practice, cost initiatives often disappoint

- Companies are achieving only 59% of expected savings
- Only 8% of businesses reach or exceed their targets
- Most lack adequate processes to drive cost reduction
- Changing cost structures requires extraordinary focus – not ‘business as usual’
- Look past the “low-hanging fruit”
- Look beyond individual departments to take a broader view of your value chain

Unless you raise your game, savings will not materialize

Revenue Growth has Eroded Cost Discipline

Cost reduction requires extraordinary focus

- 42% of companies admit that revenue growth has led their businesses to take the eye off the ball on cost
- Companies are setting low targets: average only 2% per year
- Keep a relentless focus on delivery
- Monitor and track benefits to ensure they are preserved
- Develop contingencies if core plans need to change as a result of unpredictable events

Today, profitability means cost, not revenue

Cost Ownership is Unclear and Too Narrow

Strong backing from the very top is vital

- CEOs and CFOs have “significant responsibility” for cost reduction at less than 2/3 of companies
- Only 44% of companies say all managers have responsibility for cost management
- Only 45% of businesses provide incentives for success in cost cutting
- Articulate a clear vision and communicate from the top
- Leaders must show clear commitment to the process for its duration

Every single person in your business has a role

Cost Strategies are Too Cautious

Companies too often take the easy way out

- Improving process efficiency the most popular approach to finding savings
- Shared services, outsourcing, and off-shoring provided the greatest savings but remain among the least popular strategies
- Be bold and thinking holistically
- Understand how your business model impacts costs
- Make changes at the strategic level

Are you prepared for major changes to your business model?

Cost Drivers are Not Transparent

Companies need more insight into what drives cost

- Cost cutting must be targeted correctly and success properly measured
- Many companies do not have a clear view of what drives costs
- Less than half of those surveyed make costs and profitability of individual units transparent
- Develop a deep understanding of what drives value
- Balance short term “quick wins” with longer term returns
- Align cost strategies to anticipate declining earnings

IT has a major role to play in providing better information

Cost Discipline is Not Embedded in the Culture

A diet helps you lose weight for a while ...

- It is hard to get people excited about cost management initiatives
- Cost reduction and management has to be built into the organization's planning, initiatives and on-going operations
- Prepare for a “cultural reset” to a drive to control cost
- Embed the new way of doing things into the day-to-day behaviours
- Empower those with operational responsibilities to achieve results

... but a lifestyle change can deliver long-term health

Success Will Require You To ...

- Get visibility, quickly
- Know what is possible with your costs
- Rapidly bank your quick wins – but don't panic
- Be bold, think holistically and go for agility
- Create a culture around “caring about cost”
- Worry about cash as well as cost
- Make it clear who is responsible for cost – lead from the top



Managing the Risks – Distressed Business Acquisitions

Environment

- Growing number of financially troubled businesses
- Few unaffected sectors
- Changing secured lender attitudes
- Opportunities

Positive Factors

- Attractive valuation... (lower price)
- Avoid / limit goodwill and other intangible assets
- Possibly less competition for the transaction
- May get court order – assurance on title
- May find some tax losses

Challenges

- Time lines compressed
- Customers and employees may be in fatigue mode
- May be a “wasting asset”
- Situation may be worse than you think
- Information may be in rough shape
- Parties under extreme pressure, may turn hostile
- “As is, where is” approach to reps and warranties
- Capex and other investments deferred/ignored
- Acceptance of issues by the target

Getting Started

- Be Clear on Your Goals
 - Why are we chasing this?
 - Strategic fit, critical defensive move
 - Cost savings / synergy
 - “Opportunity knocks”, “Why not”
- Examine Your Upside and Downside
 - In the end, it’s a risk-reward decision
 - Understand how much you’re betting
- Complexity of the Transaction
 - Public vs. Private
 - Cross-border issues

Degree of Distress

Not all troubled companies are in the same spot...

- Stressed

- Lender relationships deteriorating, covenant breaches / default
- Incurring losses
- Loss of key customers
- Some Capex deferred
- Working cap restrictions

- Distressed

- Loss of Lender Support
- Significant defaults
- Suppliers on COD
- Deferral of all Capex
- Contemplating/entering formal insolvency proceedings
- Statutory claims building

Often not clear exactly where the target sits...

Identify Stakeholders

- Normal M&A
 - Shareholders
 - Board
 - Management
- Distress – above plus:
 - Senior lenders, junior lenders
 - Trade creditors, preferred creditors
 - Customers
 - Landlords, regulators
 - Unions, pensions

Different Transaction Focus

- Normal M&A
 - Maximization of shareholder value
- Distress M&A
 - may not be any/much shareholder value
 - Lenders have more say
 - Fast resolution valued
 - Little regard for non-cash consideration
 - Certainty of closing a priority

Various Forms of Transaction

- Private negotiation – pre-insolvency
 - Normal rules, target under duress
 - Conflicting goals, disagreement among stakeholders
 - Value of warranties / concerns over hidden liabilities
- Distress – formal proceedings
 - CCAA, BIA, other statutory
 - US – Chapter 11

Normally an Advisor involved running or facilitating the transaction process

CCAA / Chapter 11

- Court-sanctioned process
 - Meant to facilitate restructuring and related benefit
 - Court order is a powerful device
 - Interim - time granted to develop and execute a plan
 - Stakeholders represented
 - Normally court-appointed Monitor – important role, objective, balance interests of the parties having regard to their legal position
 - Sale of all or parts of the Company may be the solution
 - Court order sanctions the transaction
 - Stalking horse concept

Conclusions

- Distress M&A
 - Complex, time sensitive
 - High stakes
 - Accurate & timely information often unavailable
 - Morale all around may be low
 - Rules of the game are different
 - Investing time, money no guarantee of success

Not a core competency for most business people

Conclusions

- Surround yourself with Experienced Advisors
 - Lawyers who specialize in insolvency matters
 - Technical advisors – environmental, industry specialists
 - In-house team – bring your company's expertise to the table
 - Technical, Financial, Market/Sales, HR
 - Industry connections will yield information
 - Appoint a Project Leader
 - C-Level commitment & leadership is key
 - Financial Advisors experienced in Distressed Investing
 - Due diligence, Tax, Financing and Deal Structures – all different



Question & Answer

AUDIT ■ TAX ■ ADVISORY

Additional KPMG Resources

Succeeding in Turbulent Times – KPMG’s Global Site

<http://www.kpmg.com/Global/IssuesAndInsights/ArticlesAndPublications/Pages/Succeedinginturbulenttimes.aspx>

Sustaining Value in a Changing Economy – KPMG.ca

<http://www.kpmg.ca/en/services/advisory/sustainingvalue.html>

KPMG and Canadian Business Magazine Podcast Series

http://www.kpmg.ca/en/services/advisory/sustainingvalue_podcast.html



Thank You



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