Key Elements to a Successful Corporate Turnaround

20th March 2015

Luka Vesnaver
Today’s Agenda

<table>
<thead>
<tr>
<th>Section</th>
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<tbody>
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<td>5</td>
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We are observing multiple challenges...

**Our understanding of the situation**

- Increasing share of non-performing loans
- Continuous high political and economic insecurity
- Generally poor quantitative and qualitative information on clients available
- Limited history of workout/restructuring experience and expertise:
  - Lack of experience on the banks’ side and on the corporate side
  - Difficult to obtain experienced work-out staff
- Increasing efforts to facilitate centralized monitoring and decision-making within banks

**Financial advisors’ role**

- **Increase transparency** on troubled portfolio companies with consideration of both quantitative and qualitative performance factors
- Identifying viable options and elaborating **clear restructuring strategies** for selected companies
- Providing sufficient **resources and know-how** to implement strategies/initiatives agreed-upon on a single client level
... and several recurring deficiencies across Central and Southeast Europe markets

**Areas of risk**

- Non transparent ownership structures; inherent risk for banks, exit strategies
- Denial of problems, initiative and the bulk of restructuring efforts lies with the banks
- Restructuring implementation issues, key personnel overburdening (CEO, CFO, Head of Accounting/Controlling)
- Poor CF management
- Limited focus on WC optimization (AR collection, obsolete inventory and non-core assets divestments)
- Limited visibility on contribution profitability by product/customer – both historical and forecasting
- Lack of detailed CAPEX planning, weak justification of investments
- Inappropriate legal environment

**Suggestion for improvement**

- Identification of economic beneficiaries as first priority
- All stakeholders should play a proactive role in identifying issues and deriving a viable restructuring scenario
- Appointing qualified (foreign) CROs should become a practice
- Companies should set up robust CF monitoring and planning systems
- Companies should improve WC management and monitoring systems - quick wins
- Companies should hire key personnel, set up business processes and IT platforms that would allow for such monitoring on a continuous basis and proper business planning
- Every investment should have its investment plan and effect on profitability plan
- Revision of existing legislation
Early identification of oncoming crisis is crucial, yet the companies often react late.

Stages of corporate crisis

1. Strategic crisis
   - Difficulties are approaching and beginning to appear
   - The company is not entirely conscious of the issues
   - The problem appears on the:
     - Income Statement

2. Profitability crisis
   - The Company is aware of the issues
   - No activity
   - Management restructuring plan

3. Liquidity crisis
   - Loss of control
   - Advisor is involved
   - Creditors
   - Shareholders
   - Management

The share of distressed companies addressing the crisis is indicated by the graph.
In restructuring the common objective is to identify the highest NPV solution for all stakeholders involved.

**Creditors’ options after IBR process**

- **Sale of NPL to 3rd parties**
  - Non-performing loans are sold with discount to third parties
  - 6-15 months

- **Bankruptcy**
  - Distressed sale - creditors typically obtain lower recovery rates
  - Type and value of secured assets is crucial
  - 3-9 months

- **Compulsory Settlement**
  - Reorganization - creditors typically obtain higher recovery rates
  - Strong role of management
  - Constraints of the legal framework
  - 3-6 months

- **Restructuring**
  - 6-18 months

- **Business Turnaround**
  - Complex option including all three restructuring pillars – strategic, operational and financial restructuring
  - Proper implementation is a key success factor
  - 12-18 months

- **Financial Restructuring**
  - New sustainable debt structure reflects agreed financial plan and cash flow after restructuring measures
  - 6-12 months

- **Working Capital Optimization**
  - Main objective is to release tied up cash
  - The WC optimization project can accompany any restructuring activity
  - 1-12 months
Business turnaround is a complex process including all three restructuring pillars – strategic, operational and financial restructuring.

Restructuring process (out of court)

- **IBR**
  - Time: 6 – 8 weeks
- **Quick wins**
  - Time: 6 weeks
- **Strategic restructuring**
  - Time: 6 – 12 months
- **Operational restructuring**
  - Time: 3 – 12 months
- **Financial restructuring**
  - Time: 6 – 12 months

Regular independent monitoring for banks

**Complete turnaround process**

Time
Definition of key success factors is a prerequisite of a successful business turnaround

Key factors

► Address the crisis as **early as possible and react appropriately**.

► **Achieve an appropriate level of trust** between the key stakeholders involved in the process.

► Involve **experienced independent external advisors** (with good reputation) before short standstill agreement is signed.

► Engage in a **complex restructuring process** with a detailed restructuring plan and its implementation.

► Define a **viable business strategy** with clearly defined operating model and assure all necessary resources.

► Assure a **clear definition of restructuring measures, implementation milestones and responsibilities**.

► Assess major risk related to each scenario and prepare for **risk mitigation**.

► Assure the **right team of experts with experiences and qualifications** to manage both growth and distressed situation (crisis management).

► Appoint **CRO** and avoid turnaround to be led by the same management who led the company into distressed situation.
Existing management structures often lack competencies and independence required in a turnaround

An interim role of a CRO is very often a prerequisite for the successful turnaround

Why appoint an interim CRO?

► Ability to identify the interests and motivations of each stakeholder
► Experience of how to deal with corporate crisis situation
► Experience with how to manage anxiety and uncertainty of various stakeholders during transition
► Experience with project management – setup of clear goals, responsibilities and strong orientation on results
► Experience with change management – focus on the areas that could impede a successful restructuring and increase motivation and creditworthiness of the change

Principles of cooperation

► Project management base
► Interim role
► CRO performance is supervised by the CEO
► In a daily contact with the management and employees
► Key role - coordination of the restructuring plan implementation, and monitoring of results

Benefits to the stakeholders

► Independent credible advisor restores confidence of all key stakeholders
► Unbiased advice based on prior experience
► Incumbent management can focus on business operations while interim manager focuses on strengthening the organisation for growth and change management

Where appropriate, EY may take executive appointments to manage change and to sustain/restore stakeholder confidence

Team structure

Owner
Change Management
Stakeholder Management
CEO
CRO
CFO
Sales & Marketing
Operations

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Case studies

► Case 1: A large diversified industrial conglomerate with five diverse divisions, financial debt of €175m and debt to EBITDA at 10X

► Case 2: Automotive group, burdened by past investments into non-core underperforming businesses

► Case 3: One of the leading players in meat processing industry in the Adriatic Region
Case 1: A large diversified industrial conglomerate with five diverse divisions, financial debt of €175m and debt to EBITDA at 10X

Company overview

Core businesses

- Division 1
- Division 2
- Division 3

Non-core businesses

- Division 4
- Division 5

A large diversified conglomerate

2013 Consolidated key financials [EUR m]:
- Revenues: €200m
- EBITDA €17.5m
- Financial debt: €175m
- FTE: cca 2,000
We focused on several major project streams in order to achieve an optimal sustainable debt structure.

Financial restructuring

Simplification of financial debt complexity

Business turnaround

<table>
<thead>
<tr>
<th>Starting</th>
<th>Target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt/EBITDA</td>
<td>10</td>
</tr>
<tr>
<td>Debt/Equity</td>
<td>1.2</td>
</tr>
<tr>
<td>(LT debt + Equity) / Fixed assets</td>
<td>1.0</td>
</tr>
<tr>
<td>ST debt / (WC + Fin assets)</td>
<td>0.8</td>
</tr>
<tr>
<td>ROA</td>
<td>5%</td>
</tr>
</tbody>
</table>

- Increasing productivity and assets utilization (reduction of labor costs)
- Reduction of material costs (operational measures)
- Reduction of other administrative expenses (OAE)
- Improved contribution margin according to product group and customer revenues
- Reduction of accounts receivable
- Reduction of inventories
- Reduction of investments
- Sale of non-operating assets
The newly proposed bank loans tranches reflect fully the changes requested by banks - tranches simplification into amortizing and bullet loan

### Loan amount [EURm]

<table>
<thead>
<tr>
<th>Bank</th>
<th>Loan specification</th>
<th>Loan terms</th>
<th>Collateral</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>AMORTIZED</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tranche 1</td>
<td>EUR 118m 67%</td>
<td>Long term</td>
<td>Market level margins</td>
<td>• Cash sweep mechanism for disposal of pledged asset</td>
</tr>
<tr>
<td>Tranche 2</td>
<td>EUR 29m 17%</td>
<td>Long term</td>
<td>Yearly repayments of EUR 6m starting from 2014</td>
<td>• Extra cash sweep mechanism for pledged assets disposal, WC optimization and/or free cash from business operations.</td>
</tr>
<tr>
<td><strong>BULLET</strong></td>
<td></td>
<td>Bullet</td>
<td>Market level margins paid monthly/quarterly</td>
<td>• Structuring of the debt into 2 tranches (amortized and bullet) was based on current loan structure of current banks.</td>
</tr>
<tr>
<td><strong>Excluded from financial restructuring</strong></td>
<td></td>
<td></td>
<td></td>
<td>• The volume of yearly repayments of tranche 1 is based on the cash flow plan.</td>
</tr>
<tr>
<td>Bank X</td>
<td>EUR 28m 16%</td>
<td>Long term</td>
<td>Interest rate according to current terms</td>
<td>• Bank X is expected to be out of the consortium and to provide additional cash sources in 2015.</td>
</tr>
</tbody>
</table>

#### Additional comments:
- **Cumulative balance:** EUR 147m
- **Cumulative share:** 88%

- **Cumulative balance:** EUR 175m
- **Cumulative share:** 100%
Post restructuring monitoring of key KPIs suggests a positive development of events

### Fulfilment of KPIs in Q4 2014

<table>
<thead>
<tr>
<th>KPI</th>
<th>Threshold</th>
<th>Allowed deviation</th>
<th>Achieved</th>
<th>Deviation from the threshold</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contribution margin</td>
<td>40%</td>
<td>No</td>
<td>44.9%</td>
<td>12%</td>
<td>✓</td>
</tr>
<tr>
<td>EBITDA</td>
<td>EUR 15m</td>
<td>-30%</td>
<td>EUR 14.6m</td>
<td>2%</td>
<td>✓</td>
</tr>
<tr>
<td>Cash balance</td>
<td>1%</td>
<td>-0.5 pct points</td>
<td>4.0%</td>
<td>3.0 pct points</td>
<td>✓</td>
</tr>
<tr>
<td>Overdue receivables</td>
<td>25.0%</td>
<td>5 pct points</td>
<td>31.1%</td>
<td>6.1 pct points</td>
<td>✗</td>
</tr>
<tr>
<td>CAPEX</td>
<td>EUR 6.5m</td>
<td>-</td>
<td>EUR 5.2m</td>
<td>-20%</td>
<td>✓</td>
</tr>
<tr>
<td>Overdue payables (60+ days)</td>
<td>13%</td>
<td>3 pct points</td>
<td>9.3%</td>
<td>-3.7 pct points</td>
<td>✓</td>
</tr>
</tbody>
</table>
Case 2: Automotive group, burdened by past investments into non-core underperforming businesses

Background

- Group invested intensively into non-core real-estate and acquisitions during years of maximum profitability
- During crisis sales & profitability dropped, non-core investments become illiquid
- Quick solution to deleverage the group are not possible or too costly
- Unsustainable debt level prevent required capex, WC is depleted and recovery after the crisis is not possible even on core companies
- Debt levels threaten the existence of the whole group due to cross-guarantees and other inter group relationships

Period of heavy investment into non-core activities, mainly real-estate and M&A, followed by a drop in underlying profitability increased leverage to unsustainable levels.
Restructuring focused on rationalization of group structure to increase transparency and ring-fence core companies from non-performing assets.

- Complex web of cross-guarantees given for bank loans threaten the existence of viable companies.
- Inability to repay loans on non-core companies threatens the viability of the entire group.

### Guarantees

Guarantees = ; C = Core company; NC = Non-core company or investment

### TARGET STRUCTURE

- Elimination of cross-guarantees between core groups and complete ring-fencing of core business activities from the non-core (SPV).
- Core groups are now free from the threat of debt taken to finance non-core investments.
- Bank exposure on SPV secured by shares in TopCo (provided by owners).
Core groups transfer loans and non-core assets to non-core SPV to reach target debt/EBITDA multiple below 5x and net off intra group relations. Non-core companies are merged into the SPV.

- 4 bank syndicates are created
- Each bank participates in core group according to its original relative exposure
- Excess core debt is transferred to the non-core SPV
- SPV assumes all excess debt from core and all debt from non-core companies
Newly proposed bank loan tranches are structured according to long-term needs and possibilities of individual core groups.

<table>
<thead>
<tr>
<th>Core syndicates consolidated</th>
<th>Loan amount [EURm]</th>
<th>Loan specification</th>
<th>Loan terms</th>
<th>Collateral</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>REVOLVING</td>
<td>EUR 10m</td>
<td>Revolving and guarantees Super senior</td>
<td>Market level margins</td>
<td>Fixed assets above agreed value</td>
<td>Cash buffer to cover potential excess debt on SPV agreed</td>
</tr>
<tr>
<td>AMORTIZED</td>
<td>EUR 25m</td>
<td>Long term Amortized Senior</td>
<td>Market level margins Increasing quarterly repayments 5 year maturity</td>
<td>Only assets owned by individual core groups</td>
<td>No cross default between core groups</td>
</tr>
<tr>
<td>BULLET</td>
<td>EUR 65m</td>
<td>Long term Bullet Senior</td>
<td>Market level margins paid monthly/quarterly 5 year maturity</td>
<td>No cross guarantees</td>
<td>Core groups ring fenced from SPV</td>
</tr>
</tbody>
</table>

- Each core group has only one syndicated loan facility split into 3 tranches
- Pik toggle interest payment option

### Comments
- Cash buffer to cover potential excess debt on SPV agreed
- No cross default between core groups
- Core groups ring fenced from SPV
- All loans within same core group consolidated on largest company within the core group
- Each core group has only one syndicated loan facility split into 3 tranches
- Pik toggle interest payment option

### Tranche 1
- EUR 50m
- 4 + 2 years repayment period PAYC
- Cash sweep
- Core + mark up of 175bps PAYC

### Tranche 2
- EUR 25m
- Long term Amortized Senior
- Market level margins Increasing quarterly repayments 5 year maturity
- Only assets owned by individual core groups
- No cross guarantees

### Tranche 3
- EUR 65m
- Long term Bullet Senior
- Market level margins paid monthly/quarterly 5 year maturity

### SPV
- EUR 100m
- Shares of TopCo
- Excess cash of core groups if available

Cumulative balance: EUR 100m
Cumulative share: 2/3

Total balance: EUR 150m
Cumulative share: 100%
Case 3: One of the leading players in the meat processing industry in the Adriatic Region

**Key causes leading to distressed situation**

1. **Poor/Faulty financial/investment decisions**
   - Investment in third party’s shares valued at EUR 26m as of Dec-FY13
   - Intercompany loans to 2 external parties totaling to EUR 10m
   - **Investments are partially or completely lost - all third parties currently in bankruptcy proceedings**

2. **Unfavorable movements of raw material prices**
   - Negative effect to Group Net sales in FY12, FY12 due to increase in raw material prices

**Business allocation/Group structure [EURm, FY13]**

- **Location of the key entities within the Group**
- **Location of other entities within the Group**

- **Mother Company in Slo**
  - Assets: 208.7
  - Sales: 141.6
  - EBITDA: 12.5
  - Debt/EBITDA: 6.75
  - Debt: EUR 82m

- **Entity in Croatia**
  - Assets: 30.4
  - Sales: 46.4
  - EBITDA: 2.6
  - Debt/EBITDA: 0.55

- **Entity in Serbia**
  - Assets: 25.5
  - Sales: 42.9
  - EBITDA: 1.8
  - Debt/EBITDA: 3.26

- **Entity in BiH**
  - Assets: 34.6
  - Sales: 38.3
  - EBITDA: 3.3
  - Debt/EBITDA: 4.17

Source: Indexmundi

Source: Management information, Annual reports, Financial data as of FY13
Due to different jurisdictions within the Group, MRA was implemented on the mother company, with commitment of yearly CF from subsidiaries and implementation of Operational restructuring measures

### EY’s selected approach

#### Financial restructuring of the mother company in Slovenia

<table>
<thead>
<tr>
<th>Loan amount [EURm]</th>
<th>Loan specification</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>AMORTIZED</strong></td>
<td></td>
</tr>
<tr>
<td>Tranche 1</td>
<td>EUR 18m</td>
</tr>
<tr>
<td>Fixed amortizing tranche</td>
<td></td>
</tr>
<tr>
<td>Key source of funds: mother company’s operations</td>
<td></td>
</tr>
<tr>
<td>Priority repayment</td>
<td></td>
</tr>
<tr>
<td><strong>AMORTIZED</strong></td>
<td></td>
</tr>
<tr>
<td>Tranche 2</td>
<td>EUR 21m</td>
</tr>
<tr>
<td>Variable amortizing tranche</td>
<td></td>
</tr>
<tr>
<td>Key source of funds: CF from subsidiaries</td>
<td></td>
</tr>
<tr>
<td><strong>BULLET</strong></td>
<td></td>
</tr>
<tr>
<td>Tranche 3</td>
<td>EUR 1.5m</td>
</tr>
<tr>
<td>Bullet</td>
<td></td>
</tr>
<tr>
<td>Flexible instalments</td>
<td></td>
</tr>
<tr>
<td>Key source of funds: CF received from Non-core asset disposal and excess cash from Tranche 2</td>
<td></td>
</tr>
</tbody>
</table>

#### Operational restructuring measures

- Commitment on cash inflows from the subsidiaries to the mother company from the following sources:
  - Dividends
  - Repayment of IC receivables towards the mother company
  - Repayment of IC loans to the mother company
- Business optimization and improvement measure to be implemented by the mother company.
- Revamping of Group’s corporate governance model, including:
  - Centralization of financial management and reporting
  - Centralization of strategic development
  - Centralization of strategic marketing and procurement

#### Optimization of Group’s asset base

- Identification of Non-core assets for business operation within the Group
- Differentiation of the assets into two groups:
  - Assets available for immediate disposal
  - Assets potentially available for disposal

Implementation of financial restructuring plan in the FY15-FY20 period with monitoring of key KPIs on the mother company and operational restructuring measures implemented in FY15-FY20 on the Group level. Disposal of Non-core assets in FY15, FY16 should additionally deleverage the mother company and serve as repayment of Tranche 3.
Any questions?
Thank you for your attention!

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