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INDUSTRY

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Outlook on turnaround and restructuring in Asia Pacific 2016 –a race against the clock

At A Glance

Times are getting tougher for corporations in Asia Pacific, and survey participants say they expect market conditions across the region will only worsen.

In the year ahead, 92% say restructuring and turnaround activity is going to increase—an anticipation that vastly overshadows expectations four years ago, when only 66% of respondents said they held similar beliefs. As part of respondents' general sentiment this year, many say China's slowdown will have a much deeper impact on corporations' abilities to adapt and thereby remain competitive in a slow-growth world. There are also concerns that companies facing persistent "sickness" may soon begin perishing under the weight of increasing debt burdens and because of lost market share.

Despite those reflections on the growing need to reorganize business operations and improve financial performance, management teams may not be heeding the call to make changes and transform their companies while there's still time. A surprisingly large number of respondents (40%) say restructuring or other efforts to turn their businesses around would take place only once serious signs of distress—either operational distress or financial decay—become apparent. The numbers are alarming, as conventional wisdom and experience show that the sooner a management team begins executing serious changes to the business, the sooner a recovery can begin and the better the chances of a successful turnaround.

Why then, are management teams waiting until the writing is already on the wall, so to speak? It may be due partly to complacency. Many companies in Asia Pacific haven't seen a serious crisis since 1997, and they've become accustomed to good growth—or to riding out rough patches when market conditions are less than ideal. It could also be due to inexperience or flagrant denial that something is indeed wrong. In general, many managements' reaction times to detecting and addressing negative shifts in the market and within their own organizations have started to lag.

In this report, our fourth annual examination of market sentiment in the restructuring and turnaround space, we analyze those issues and their impacts on companies of varying degrees of health. As in past years, we also look at strategies for managing and achieving a successful turnaround and at country- and industry-specific trends and expectations for the year ahead.

As always, we hope you find this report a valuable and insightful read, and we welcome the chance to discuss with you in more depth the issues covered here as well as others affecting market participants and their shareholders.

Masahiko Fukasawa
Managing Director, Co-head of Asia Business Unit
and Co-Japan Representative

Executive summary

THE OUTLOOK: CONDITIONS CONTINUE TO WORSEN

Ninety-two percent of survey respondents say they expect an increase in corporate restructurings in the year ahead. Of that 92%, close to half (48%) say they expect the increase will be significant, which is a noticeable change from only 37% with the same expectations in last year's survey. Various factors may contribute to corporate restructuring activity, with, according to respondents, the impact of slow growth in China (68% of respondents compared with 40% in 2015) taking an increasing toll on corporate performance across the region.

WAITING UNTIL IT'S TOO LATE?

Rather than striking quickly when conditions within the company begin to falter, 40% of respondents say restructurings will begin only once signs of serious distress begin to emerge. This was an alarming increase from 2015, when only 13% of respondents said the same; and it's especially troubling given that respondents overwhelmingly agree that a restructuring that gets a late start can negatively affect the success of the overall organization. (Fully 58% say that that impact will be significant, and 40% say it will be significant to some extent.)

MANAGEMENT TEAMS: RIGHT FOR THE JOB?

Part of the reason for delays in the restructuring process seems to be attributed to corporate leadership and participants who drive the process. Respondents (54%) say restructuring activities are driven largely internally by CEOs and other C-suite executives. Respondents add that those teams may not always be best equipped to manage the kind of changes needed during a turnaround, and in extreme cases, those teams may not recognize declining conditions in the market or the company until it's too late.

THE CHIEF RESTRUCTURING OFFICER

To support or replace, existing management teams, respondents say, chief restructuring officers (CROs)—either lender appointed (11%) or company appointed (5%)—are likely to have the most influence in the restructuring process in the year ahead. This represents a substantial increase from 2015, when only 1% of respondents said CROs would drive the turnarounds in ailing Asian businesses.

OPERATIONAL-DRIVEN RESTRUCTURING

Whereas 54% of respondents say debt/capital structure restructuring will be distressed companies' focus in the year ahead, 49% say operational restructuring would pose a greater challenge while also yielding more promising outcomes for companies. Improvements in operations would enable a company to emerge from the restructuring/turnaround process as a reinvigorated enterprise ready for rapid growth and expansion.

TOOLBOX FOR RESTRUCTURING: ASSESSING THE OPTIONS

Looking at the options available, 98% of respondents say they expect companies will complete acquisitions—a mergers-and-acquisitions (M&A) strategy—as part of restructuring strategies. Respondents add that they expect companies will strive for better cash flow forecasts (cash management strategy) and consider scaling back production (overhead optimization strategy) to prevent inventories from increasing. Respondents also say they expect restructuring and management teams to consider exploring new market segments (revenue enhancement strategy).

THE HIDDEN VALUE OF CROSS-BORDER M&A

Expansion across borders would enable companies to unlock a unique dimension of value that may be unavailable in the company's home market. Of the 98% of respondents who say they expect acquisitions to play a part in their companies' restructuring plans, 49% say these will be cross-border endeavors, with 59% anticipating cross-border transactions to be greater than last year and 38% saying cross-border transactions will at least equal 2015's.

COUNTRY FORECASTS

Respondents say that across the Asia Pacific region, they expect companies to undergo restructuring in varying degrees. In China, that sentiment reached 100% as respondents pointed to slow domestic growth and overcapacity within key industries as the culprits. South Korea will likewise see a massive wave of restructuring (according to 100% of respondents), as debt levels of the country's largest corporations may reach untenable levels. Ninety-one percent of respondents say they expect increases in restructuring in Japan (dipping from 97% last year), as uncertainty in the domestic economy causes mounting concerns. This is followed by India (90%), Australia and New Zealand (82%), and Southeast Asia (75%).

INDUSTRY FORECASTS

Similar to trends in 2015, industrial and automotive companies' declining market conditions will lead to increased numbers of restructurings in those sectors, according to 68% and 64% of respondents, respectively. The most noticeable year-on-year increase in respondent sentiment was in the pharmaceuticals sector, with 68% anticipating restructuring within the industry this year compared to only 15% in 2015. Demand growth for high-quality, affordable healthcare solutions and better medicine has seen interest in the sector balloon in recent years, and industry leaders are attempting to develop scale and achieve synergies to expand.

LONG ROAD AHEAD FOR ASIA'S RESTRUCTURING MARKET

Generally, respondents say the restructuring profession in Asia has considerable ground to cover before reaching a level of parity with that in North America or Europe. Somewhat surprisingly, the gap seems to be widening, as 70% of respondents—compared with 57% last year—say the Asian market is less mature than markets in the West. More than half of respondents (55%) also say that execution of a restructuring in Asia Pacific is more difficult than in North America or Europe.

Corporate Asia update: the clock is ticking

An ominous countdown seems to have begun for corporations in Asia Pacific, as disappointing economic growth, falling commodity prices, and approaching debt maturities converge to form a cocktail of rising stress.

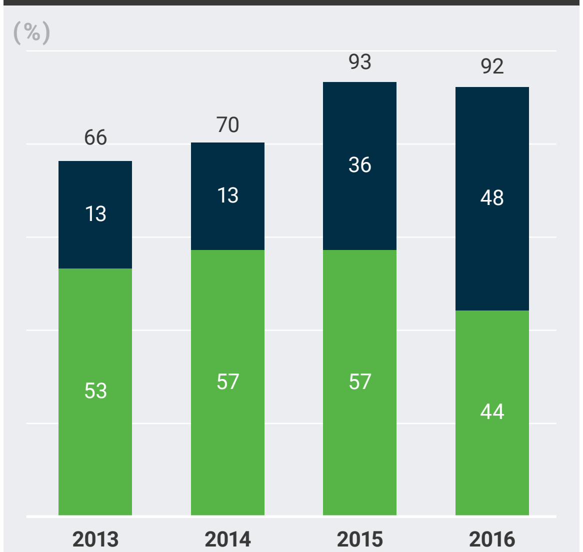
According to findings in AlixPartners' A race against the clock, that regional melancholy is expected to continue, as 92% of corporate restructuring and turnaround professionals anticipate business reorganizations will increase in the year ahead (figure 1). And although that was only one percentage point lower than last year, differences in sentiment with regard to how extreme the measures are expected to be illustrate growing concerns about the health of the region's corporates as well as their levels of awareness of impending challenges in 2016 and beyond.

In contrast to last year, expectations of a significant increase in the number of corporate restructurings rose from 37% in 2015 to 48% in 2016 (figure 2). Some of the sentiment reflects positively on those corporate reorganizations—in anticipation that management teams will take proactive measures to adjust their corporate structures as they transform while the relative health of the enterprise is stable. But it's worrisome that in most cases, respondents say that efforts to manage change within organizations will be largely distress-driven, as corporate teams struggle to deal with mounting financial and operational impediments to growth.

Macroeconomic uncertainty was first among factors expected to contribute to such strains in the year ahead—a sentiment shared by 27% of respondents (figure 3). In that vein, according to 68% of respondents, underwhelming economic growth in China will play an even larger role affecting the corporate restructuring space in Asia Pacific than it did last year, when only 40% pointed out the country's impact on the market.

FIGURE 1: EXPECTATIONS FOR RESTRUCTURING/ TURNAROUND ACTIVITY IN ASIA PACIFIC IN THE NEXT 12 MONTHS

FIGURE 2: ANTICIPATED INCREASES IN RESTRUCTURING ACTIVITY ACROSS ASIA PACIFIC



Increase slightly ■ Increase significantly

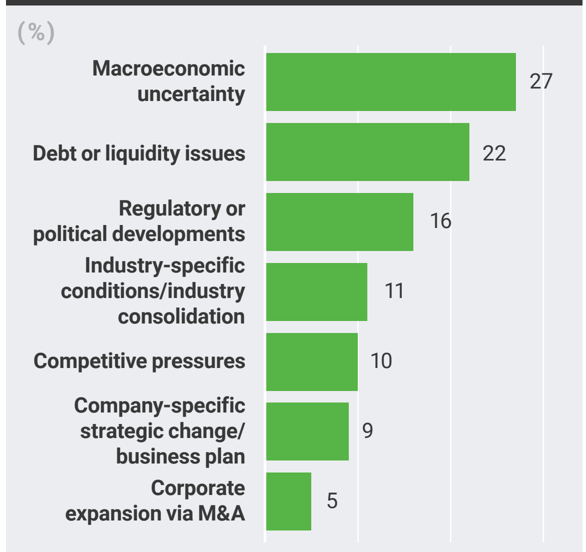
Note: Figures in bold represent total expected increases per year.

Debt and liquidity concerns will likewise be drivers (22% of respondents) because frenetic borrowing since the 2008 financial crisis seems to have led corporate debt to reach historic highs. This has been particularly evident in the region's emerging markets, wherein corporations took advantage of low interest rates and assumed greater debt so they could pursue aggressive growth plans. Now, for many corporations, it's payback time, with close to US$1 trillion in debt due for repayment in the next four years. Refunding of that debt could prove more difficult than in previous years, as market volatility causes confidence to wane and as an appreciating US dollar collides to create less-than-favorable credit conditions.[1]

Recognizing the need for the region's corporates to begin deleveraging, 54% of respondents say companies would have to prioritize the restructuring of their debt/capital structures over other considerations (figure 4). The director of an India-based hedge fund says, "Financial restructurings will take center stage as many corporations in Asia Pacific sink deeper into distress, reaching a financial tipping point as debt reaches new heights and as liquidity dries up."

Aside from the immediate benefits of improving financial position and avoiding often costly—in cash and reputational damage—court-driven proceedings, the partner of a Hong Kong–based private-equity firm says the restructuring of finances can free up financial resources for reinvestment in operational

FIGURE 3: PRIMARY DRIVERS OF RESTRUCTURING IN ASIA PACIFIC IN THE NEXT 12 MONTHS

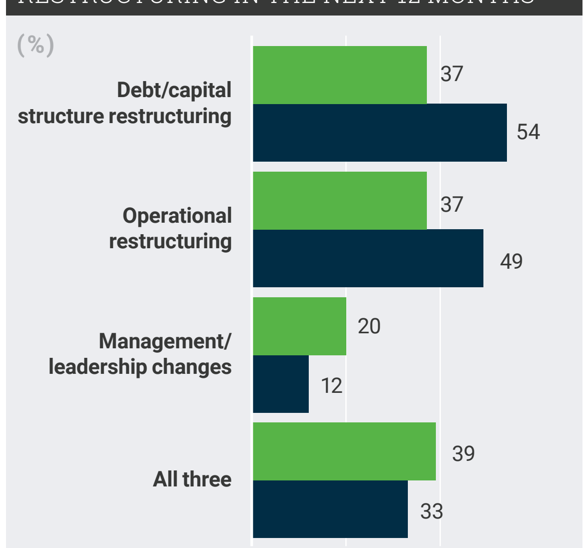


improvements and infrastructure. Close to half (49%) of respondents agree, anticipating that the introduction of new technology or new processes and focusing on reinvigorating stagnant or underperforming businesses would provide the most benefit for enterprise improvement.

A TROUBLING LACK OF URGENCY

Even as conditions continue to worsen, corporates' awareness of the current and impending economic turbulence does not seem to be keeping pace with overall expectations for the restructuring activity

FIGURE 4: PRIMARY FOCUS AREAS FOR RESTRUCTURING IN THE NEXT 12 MONTHS



■ 2015 ■ 2016

[1] Chris Brewer and Jennifer Hughes, "S&P warns of Asia's corporate repayment risk." Financial Times. 24 February 2016.

FIGURE 5: WHEN ARE RESTRUCTURINGS LIKELY TO COMMENCE AS PART OF CORPORATE REORGANIZATIONS IN ASIA PACIFIC IN THE YEAR AHEAD?

illustrated in figure 2. Indeed, management teams are taking action to mitigate damage later than in previous years. According to 40% of respondents, those teams consider a restructuring plan only once serious signs of operational decay or financial losses become apparent (figure 5). This represents a substantial increase from 13% in 2015.

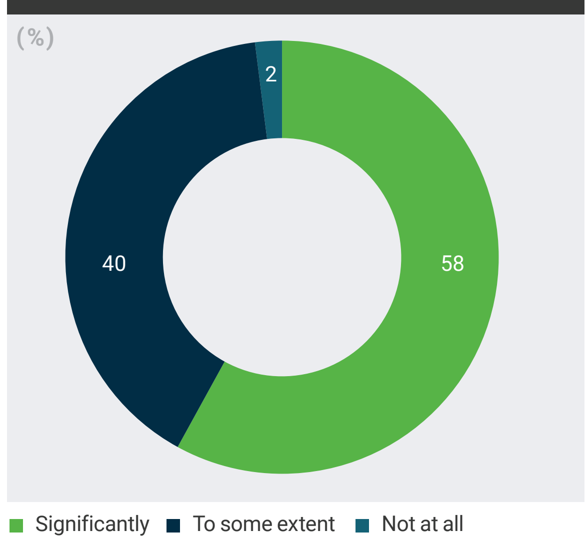
Some respondents noted a lack of resources—citing insufficient cash reserves or management's preoccupation with other corporate activities—as one possibility for inaction. However, overall opinions honed in on two significant factors: (1) lack of awareness that mounting stress was taking a toll on the business (as one respondent described it, an "if-it's-not-broken-don't-fix-it" approach) and (2) active disregard that a situation has become urgent enough to warrant such change even though clear indicators of distress have become apparent. Such results are troubling, especially because respondents almost unanimously agree that failure to act will only increase exposure to risks and to the likelihood of a negative outcome once the company emerges from the restructuring process (figure 6).

Even more alarming may be the fact that respondents say they anticipate that those management teams will be the predominant driving forces behind future restructuring efforts, with CEOs and other C-suite executives commanding leading places among the various participants (figure 7). Whereas CEOs are typically best placed within organizational ranks to effect change, several respondents say that despite those leaders' power and influence, those leaders may lack the perspective and experience necessary for managing a true and effective transformation. Even more of them may be willing to "ride out the storm," thereby effectively putting the fate of their company into hopes that market conditions will improve in the short term.

Even though that approach has worked in the past, the problem with such thinking today, as several respondents point out, is that the proverbial storm may be more prolonged than most management teams are prepared to endure. Indeed, the most recent period of significant financial distress was in 1997, and since then, the collective sentiment holds that corporations in Asia Pacific have become complacent given the relatively healthy rate of growth experienced within markets across the region—even following fallout from the 2008 global recession.

Whatever the rationale for its decisions, as the partner of a law firm in Hong Kong says, if corporate leadership fails to act by waiting until deeper signs of stress, lost market share, or financial losses take form, then the nature of the company's restructuring will be exclusively a rescue effort, not one aimed at transforming the business or positioning it as a leader within its industry. Likewise, a plan formulated and implemented in haste "increases the chances that something gets overlooked," says the managing

FIGURE 6: TO WHAT EXTENT DOES THE LATE START OF A RESTRUCTURING/TURNAROUND NEGATIVELY IMPACT THE SUCCESS OF THE OVERALL REORGANIZATION?



director of a corporate and commercial bank in China. "This could then have a domino effect of knocking down or postponing other parts of the restructuring to shocking effect."

CHANGING MANAGEMENT TO MANAGE CHANGE

The unsettling reality that upper management and key decision makers are failing to recognize the urgency of a situation or are struggling to make the right decisions—or in some cases, any decisions at all—raises the question, Who, then, should promote and push these efforts?

While anticipated involvement from middle management increased slightly since 2015, from 11% to 16% this year, these leaders may lack the skill sets and experience needed for navigating the complexities of a restructuring. Corporate boards may likewise fail in their ability to navigate the process, although they do command authority to remove ineffective executives who are perceived not to be acting in shareholders' interests.

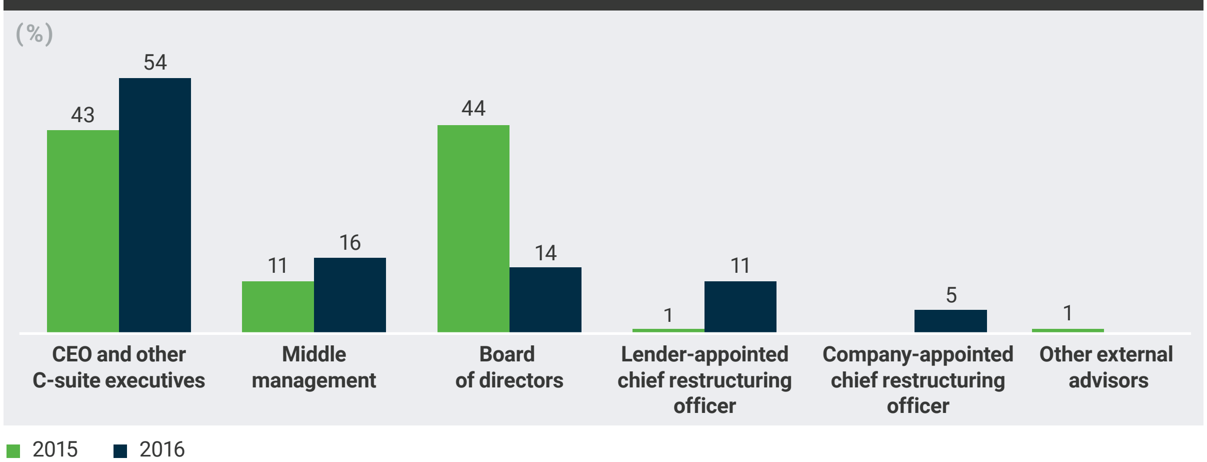
For those reasons, respondents say, there would be increased likelihood of involvement by third-party consultants and advisors in the form of chief restructuring officers (CROs). As 16% of respondents note, those CROs would be either lender appointed (11%) or company appointed (5%). According to the managing director of a Hong Kong–based investment bank, "CROs are going to come into wider use because they have the experience and the outside perspective that corporate management teams may lack." Other respondents reinforce that opinion, noting that the problem isn't that management teams are incapable of managing the process but, rather, that the current financial or operational turmoil is leaving them blind to obstacles in the medium to long term.

CROs can act in several capacities. Sometimes they serve as interim managers once the board of directors has elected to remove current leadership. Other times they serve in advisory roles, providing insight and expertise for managers at various levels of the organization while also managing communication with the board of directors.

Although the interim management option is uncharacteristic of such duties in Asia Pacific—as indicated by the low percentage of respondents in figure 4 who say leadership changes alone were unlikely—the managing director of a Japanese private-equity firm raises the point that "the driving force in any organization is its top management. If the company is underperforming, it means the current leadership is not taking sufficient steps to avoid distress. If the leadership can't change the situation, then it must be changed and replaced with a management team that is capable of revitalizing the business and restoring the company's reputation."

Indeed, strong leadership—be it on the part of current management or third-party CROs—is what's usually required to drive the level of change needed for turning around an ailing business. As we will see in the next section, that leadership is key—especially for companies taking the path of operational restructuring as they make internal changes before entering new markets and new product spaces.

FIGURE 7: WHO WILL HOLD THE MOST INFLUENCE IN DRIVING CORPORATE RESTRUCTURING AT COMPANIES IN ASIA PACIFIC IN THE NEXT 12 MONTHS?



Chasing growth: key strategies

Successful turnarounds have already become rare, and delays in the restructuring process can cause fatal errors from which many corporations may not recover—or, at the least, errors that may cause them to emerge from the process as organizations weakened from their former strengths.

With the growing list of factors playing to their disadvantage, corporations that fail to realize the immediate signs of value erosion will also see the options available for revitalizing the business or reinvigorating growth slowly begin to evaporate.

OPERATIONAL-DRIVEN RESTRUCTURING

As respondents mention, adequate time, and an early start as well as an effective management team geared toward change are all necessary if a company is to turn its current struggles into opportunities for growth. Some of the roads to restructuring, however, demand the presence of these factors more so than they demand others. "Whereas companies in Asia certainly need to get their capital structures under control, managers should not become too fixated on financial performance," says an Indonesian law firm partner. "They should be placing equal if not greater emphasis on adopting new technologies to grow and expand. There's also the need for stronger and better management teams to guide that growth."

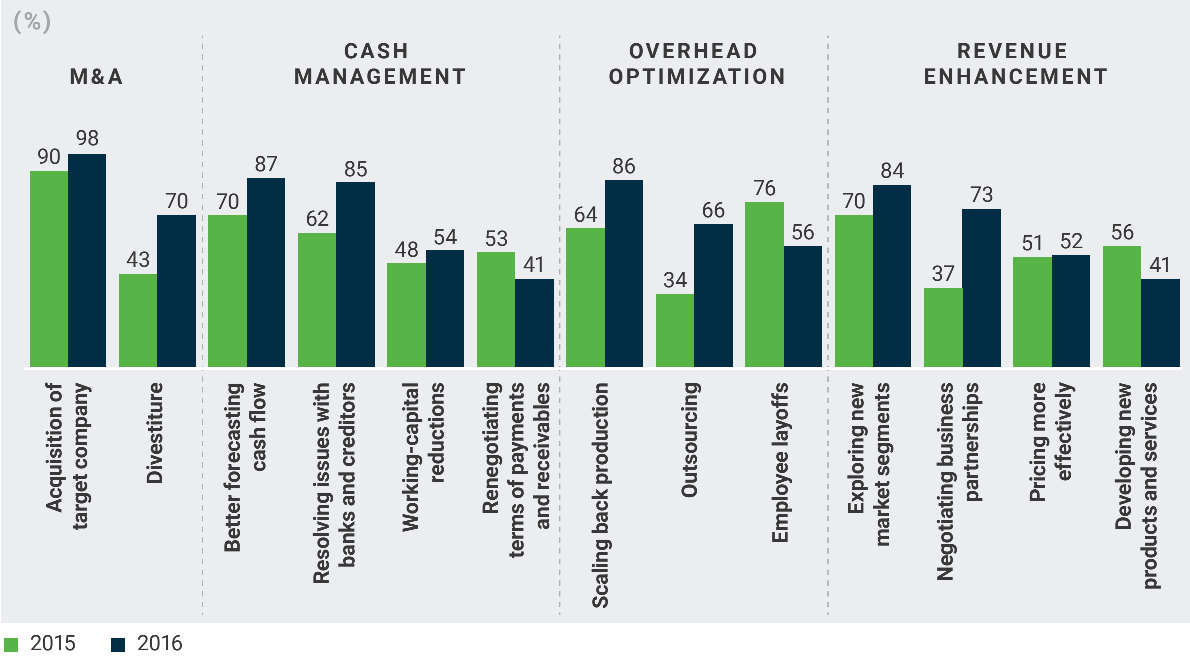
Unlike getting cost structures and the balance sheet in line, the operational side of a restructuring usually demands greater amounts of time, more resources, and additional guidance to realize optimal results. The stakes can also be higher, and failed operational changes that disrupt business as usual can become setbacks that companies cannot afford, especially if top- or bottom-line growth is already flatlining.

A holistic approach inclusive of financial, operational, and leadership changes—while expected to be implemented to a lesser extent this year than last, as indicated in figure 4—is an equally credible solution. As the managing partner of a Malaysian private-equity firm says, "Distressed companies in the region must pay down debt so they can focus their financial resources on growth and innovation to their operations. They will also have to improve their management teams and hire the right leaders who embrace a change mentality if current leadership is ineffective at achieving this."

STRATEGIES FOR SUCCESS

In looking at the various routes to restructuring, we once again analyze four key focus areas for change.

FIGURE 8: WHICH OF THE FOLLOWING RESTRUCTURING/TURNAROUND STRATEGIES WILL BE APPLIED MOST IN THE NEXT 12 MONTHS?



- **Mergers and acquisitions (M&A)** to complete acquisitions or divestitures that will drive the corporate growth agenda and expand operations
- **Cash management** to ensure a company's financial stability and solvency
- **Overhead optimization** to alleviate cost redundancies across various internal corporate functions in order to reduce the outflow of cash
- **Revenue enhancement** to explore and develop new products and services that would maximize profits

Following results from last year, respondents say acquisitions (98%) will represent the key strategy for corporate restructuring in the year ahead (figure 8). Better forecasting cash flow (87%), scaling back of production (86%), and exploration of new market segments (84%) were also among the top selections. Even though several of the top strategies from last year retained their places as preferred options during a financial or operational restructuring—with many of them increasing since 2015—several choices received smaller degrees of support from survey participants. Some of that change in sentiments was company specific, but to a large extent, economic shifts are boosting several tactics to prominence; others are being considered only as secondary possibilities.

M&A

In Asia Pacific, M&A has become an integral part of corporate growth strategies during the past decade. Levels reached record highs in 2015, posting year-on-year increases of 13% in volume terms and 45% in value to reach almost US$1 trillion in completed deals, according to M&A intelligence provider Mergermarket. The wave is likely to continue in 2016 as corporations engage in an aggressive M&A buying spree to either expand within domestic and offshore markets (discussed in greater detail on page 17 in Unlocking Value Through Cross-border M&A) or divest ancillary businesses.

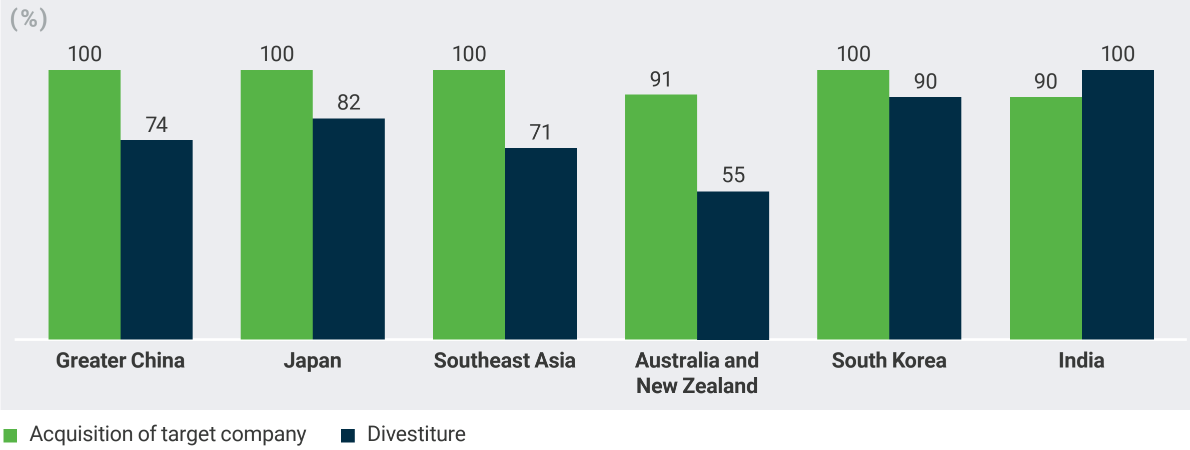
TABLE 1: M&A

RESPONDENT TOTALS FROM FIGURE 8

98%
acquisitions of target company

70%
divestiture

FIGURE 9: ANTICIPATED USE OF M&A AS A RESTRUCTURING STRATEGY IN THE YEAR AHEAD (GEOGRAPHIC PROFILE)

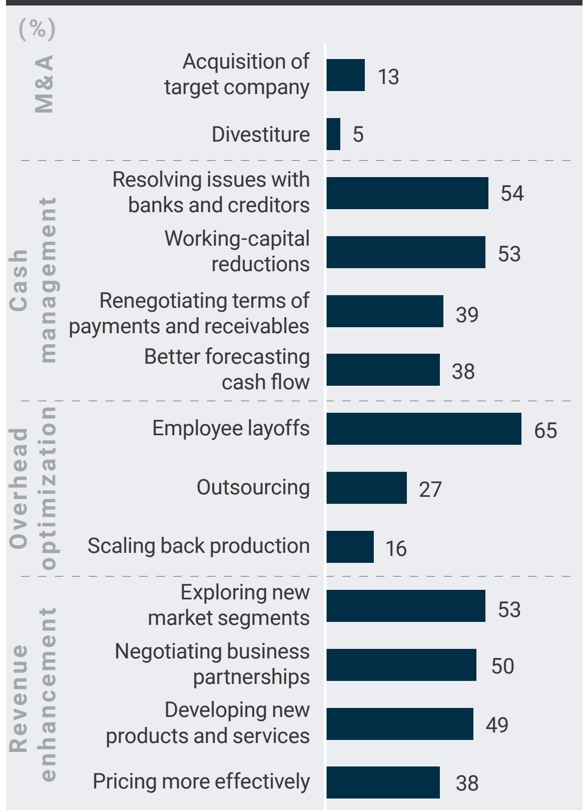


In support of that trend, the vast majority of respondents say they anticipate high levels of acquisitions within each jurisdiction in the year ahead (figure 9). Acquisitions and selling assets through divestitures were also seen as relatively risk free with regard to the challenges they pose (figure 10). Respondents say that with proper planning and leadership and, most important, ample time to execute each step in the transaction, M&A can prove an effective tool. "Deal making has accelerated since recovery from the global financial crisis and is unlikely to stop anytime soon. Today corporates are equipped with the right levels of capital to facilitate growth through M&A," says a hedge fund partner based in Singapore.

Indeed, access to financing has encouraged buying among the region's corporates—particularly in China, where sweeping industry consolidation in strategic industries has seen smaller companies absorbed by state-owned enterprises, as indicated by year-on-year increases of 39% by deal volume and 65% by value in domestic transactions from 2014 to 2015, according to Mergermarket data. Likewise, data shows that consolidations and domestic solutions may also be parts of similar activity in South Korea, as the country's chaebol (domestic conglomerates) search for new sources of growth, although future acquisitions may be more focused and more strategic than past, opportunistic buys. M&A in Japan will likely be more internationally focused, as Japanese corporates search offshore for growth opportunities.[2]

Conversely, for some companies, priority will first center on pruning current portfolios as those companies reassess and divest underperforming

FIGURE 10: STRATEGIES THAT WILL BE MOST CHALLENGING WHEN IMPLEMENTING TURNAROUND AND RESTRUCTURING



or noncore assets. Indeed, 70% of respondents agree that divestments will see wider use in the year ahead as part of cost-cutting initiatives and sales of underperforming businesses. That's a noticeable increase from last year, when only 43% of respondents had similar opinions.[3] As divestments increase, acquisitions will increase in tandem, as more targets—many of them the offshoots of previously profitable

2 Leo Lewis and Kana Inagaki, "Japan Inc: M&A's big spenders," Financial Times, December 22, 2015.
3 "Opportunity Knocks: Success in Restructuring," AlixPartners, May 2015.

TABLE 2: CASH MANAGEMENT

RESPONDENT TOTALS FROM FIGURE 8

Better forecasting cash flow	87%
Working-capital reductions	54%
Resolving issues with banks and creditors	85%
Renegotiating terms of payment and receivables	41%

business lines—come to market, which is a trend that could develop in India, South Korea, and Japan, as respondents indicate.

CASH MANAGEMENT

Cash is a company's number one resource. For distressed companies, a depletion in cash reserves could see the business heading to bankruptcy court or insolvency. As respondents note, effectively managing cash flows and generating liquidity place more options for financial and operational restructuring at a company's disposal. Respondents seem to be realizing that concept, given the increasing sentiments indicated in figure 8 that cash management strategies would be used in the year ahead.

Better forecasting of cash flow (87%, an increase from 70% the year before) was given the most consideration by respondents because it enables companies to manage debt and reduce financial risk. As the managing partner of an Indian private-equity firm notes: "Managing capital is critical in financial planning and long-term projections for the business. Companies are going to focus on this more in the year ahead, although they need to pay attention to managing cash flow and capital commitments in the short term so as not to lose sight of their long-term objectives."

Other respondents say that resolving issues with lenders (85%, an increase from 62% last year) is needed to mitigate financial issues arising from market volatility. "In the next 12 months, renegotiating terms with lenders and banks will be paramount, as many companies will be unable to satisfy the strict policies they originally agreed to. Keeping these lines of communication open will let lenders know exactly what is going on and what solutions are being implemented. And in some cases, they may be willing to support the debtors," says the managing director of a Chinese corporate and commercial bank.

FIGURE 11: WHICH CASH MANAGEMENT STRATEGIES DO YOU THINK ARE THE MOST CHALLENGING WHEN IMPLEMENTING TURNAROUND AND RESTRUCTURING? (GEOGRAPHIC PROFILE)

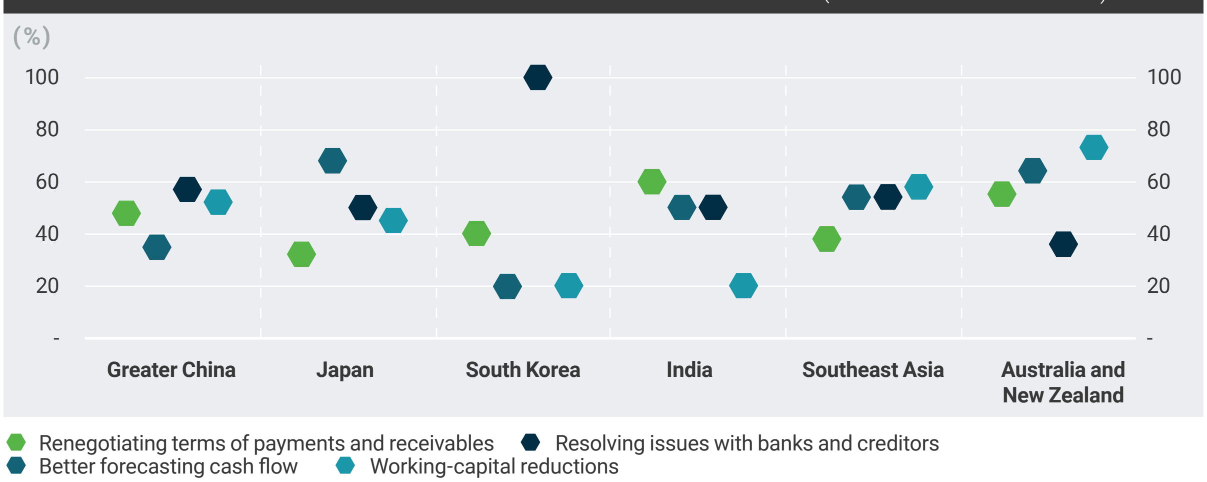


TABLE 3: OVERHEAD OPTIMIZATION

RESPONDENT TOTALS FROM FIGURE 8

86% scaling back production

66% outsourcing

56% employee layoffs

Providing additional support for the idea of resolving issues with banks and creditors, the partner of a China-based private-equity firm says such resolution of issues would have the greatest impact on restructuring because it can help take financial pressure off the company and management teams, thereby freeing them to focus on operational improvements. Resolving issues with banks and creditors was also seen as one of the most challenging (54%), and it ranked highly among cash management considerations on a geographic basis (figure 11). As the managing director of a Japanese investment bank says, "It is very difficult to resolve these issues because [banks and creditors] may not fully understand the whole process or appreciate delays that occur. Creating value or executing a turnaround can be quite difficult and stressful in these situations."

Working-capital reductions were also seen as more challenging than other options in the cash management vein. According to the vice president of a Thailand-based bank: "Reducing working capital will be difficult because of the time crisis element: making reductions in this cash vein would put a strain on supplies and lead to operational delays and disruptions to production that would reverberate throughout the business. This will expose the company to further risks such as loss of customers, delays in orders and deliveries, and production stoppages due to inventory issues."

OVERHEAD OPTIMIZATION

Overhead costs (those not associated with making a product or delivering a service) can grow slowly and sometimes go unnoticed until finally becoming major financial drains. Indeed, excessive overhead costs can be major threats to companies already in financial peril, and as such, respondents anticipate that several measures for overhead cost reduction will see greater use in the year ahead.

Mitigating these expenses was raised as a major issue by respondents who say optimizing overhead costs would best be accomplished by scaling back production, according to 86% of respondents, an increase from 64% in 2015. As unused inventories continue piling up, corporations will have to reassess their production cycles to determine whether there is sufficient current-market demand for their goods and services. Scaling back production was also seen as

FIGURE 12: WHICH OVERHEAD OPTIMIZATION STRATEGIES DO YOU THINK ARE THE MOST CHALLENGING WHEN IMPLEMENTING TURNAROUND AND RESTRUCTURING? (GEOGRAPHIC PROFILE)

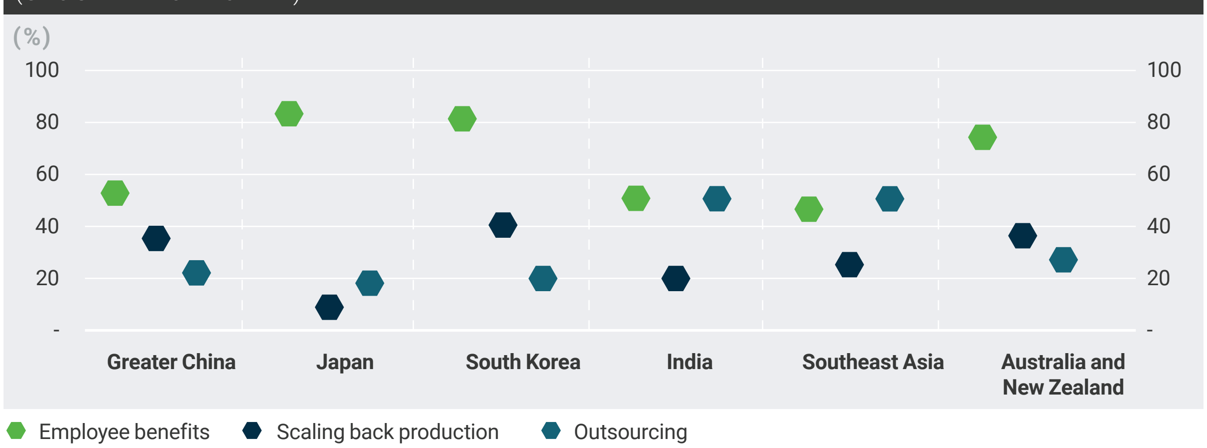


TABLE 4: REVENUE ENHANCEMENT

RESPONDENT TOTALS FROM FIGURE 8

Exploring new market segments
84%

Negotiating business partnerships
73%

Pricing more effectively
52%

Developing new products and services
41%

one of the least challenging prospects for restructuring in the year ahead, with only 16% of respondents citing concerns about the process's exerting some kind of negative impact on the restructuring or on the company's operations.

Conversely, employee layoffs were seen as possessing some of the greatest challenges to restructuring (as indicated in figure 10) and as one of the few restructuring measures analyzed in figure 8 that respondents say will decrease in the year ahead. Even though employee layoffs often represent the quickest solution, in varying degrees respondents note these difficulties as they would pertain to specific countries across Asia Pacific (figure 12). According to the head of investment at a Japanese corporate and commercial bank: "Employee layoffs can be more difficult than most people think. Removing employees who are not effectively adding to the company's growth can save on costs, but rehiring people for the positions can be costly—especially if the company is in a less-than-stable condition. And training can add to those costs."

Because of rigid employment laws and well-established social contracts in Japan, South Korea, Australia, and New Zealand, respondents say the downsizing of a workforce can prove difficult in those countries. Ambiguous termination procedures and lack of transparency make workforce rationalization both arduous and risky in Greater China and across Southeast Asia. For those reasons, respondents say, thorough knowledge of local legal frameworks that protect workers' rights is important before making layoff decisions.

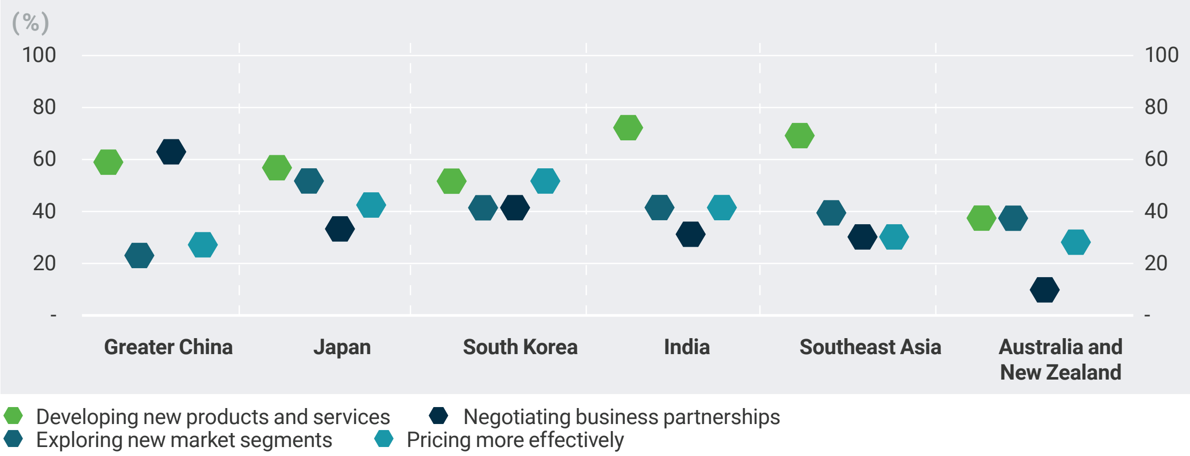
Other respondents within each geography say outsourcing presents the greatest risk. The managing director of a Chinese bank says, "Outsourcing would be the most challenging strategy during the implementation of a restructuring—especially an operational restructuring—because if the outsource partner fails to deliver on quality of service, it will be the company, not the vendor, that bears the most risk in terms of reputational damage with clients and other customers."

Adding to that, the CEO of a Singapore-based hedge fund says: "Although outsourcing enables the business to concentrate on its core business and leave remaining tasks to outsourcing firms, those firms' working cultures may be vastly different and unpredictable. Cultures that are too divergent could percolate into the quality of the company's product or service and cause disruptions with existing customers."

REVENUE ENHANCEMENT

Identifying revenue enhancement opportunities and developing a plan to increase top-line performance see respondents' sentiments split between several rollout options. Large percentages of respondents say exploring new market segments (84%, an increase from 70% last year) poses the best bet for improving the quality of revenue streams. Even though growth in certain markets has suffered in recent years, the managing partner of a South Korean private-equity firm says, exploring new market segments enables companies to "unlock new synergies and economies of scale crucial in enhancing the long-term value, growth, and capability to withstand unpredictable market conditions. In the past few years, companies have constantly invested in expansion strategies to create global footprints, and they will continue doing so in the search for growth."

FIGURE 13: WHICH REVENUE ENHANCEMENT STRATEGIES DO YOU THINK ARE THE MOST CHALLENGING WHEN IMPLEMENTING TURNAROUND AND RESTRUCTURING? (GEOGRAPHIC PROFILE)



Negotiating business partnerships sees the greatest increase in respondents' sentiments, leaping from only 37% to almost three-quarters of survey participants (73%) this year. As respondents note, business partnerships enable companies to optimize resources and even engage in other revenue-enhancing processes—such as exploring new market segments and developing new products and services—through shared resources and shared potential risk.

Of forming such partnerships, the executive vice president of a Thailand-based bank says: "This will be one of the most-applied strategies because companies will look to consolidate and then mine each other's strengths to reinforce their own current positions in the market. This will let both grow while keeping costs under control, sharing risk, and driving combined R&D to produce innovative products and services."

Even so, respondents say that forging such ties could prove risky. Especially in Greater China, the sometimes convoluted web of professional networks and ties to local communities can make it difficult for partners unfamiliar with a local business landscape to perform effective due diligence with prospective business partners (figure 13).

Although respondents mention that developing new products and services would be used to some extent—with the managing director of a Singapore-based bank saying, "to survive in this competitive market, innovation is important, and companies will look for new ways of introducing products and services to attract customers and increase demand"—many are also apprehensive about the challenges involved in such a resource-intensive process. This is especially true if a respondent's company is distressed or lacks the financial resources necessary to embark on the resource-intensive product development cycle.

Adding to that, the senior director of investment at a Malaysian private-equity firm says: "The biggest risk when introducing a new product is customer acceptance. Will it be well received in the market? And if not, how much additional capital will be required to perfect the design or pique consumer interest? Ultimately, developing new products and services might turn out to be only a short-term fix in the face of much more significant fallout from declining financials or failure to upgrade other key products, and developing a unique product requires tremendous amounts of R&D and other capital to make it worth the effort."

In the Indian and Southeast Asian markets, respondents note that the number of competitors in these markets makes introducing new products and services an incredible uphill battle. Customer loyalty usually cedes to competitive pricing of similar, cheaper alternatives. The same is true, but to a lesser extent, in Greater China, Japan, and South Korea, with respondents noting similar market pressures.

Unlocking value through cross-border M&A

As 98% of respondents mention, M&A will prove invaluable to corporate restructurings in the year ahead. Of that group, 49% say they expect M&A transactions to be cross-border deals because Asian companies are making regional and international forays to expand beyond their own borders (figure 14).

But even though the prospects of attaining greater returns and market share may be higher in international M&A than in domestic-bound deals, respondents also acknowledge that the risks are equally great.

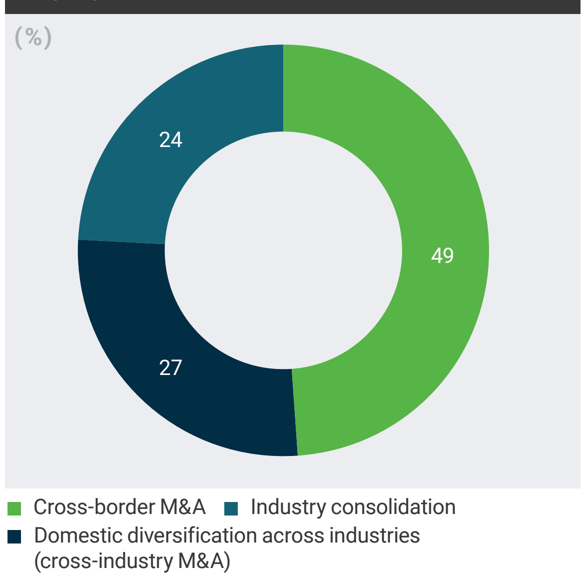
Trends shaping the region indicate corporations in Asia Pacific are increasingly implementing cross-border M&A programs, thereby extending their reach from domicile geographies to neighboring and international markets (figure 15). Deal activity in 2015 reached a four-year high, with deal values totaling US $278 billion. Many industry analysts speculate this wave has yet to peak, given the weak economic and demand growth that is causing many Asian companies to seek more-prospective shores.[4]

Respondents' sentiments likewise reinforce that viewpoint by supporting ongoing deal momentum, with 59% anticipating this year's cross-border transactions to be greater than last year's and with 38% saying it will at least be equal to 2015s (figure 16).

DRIVERS

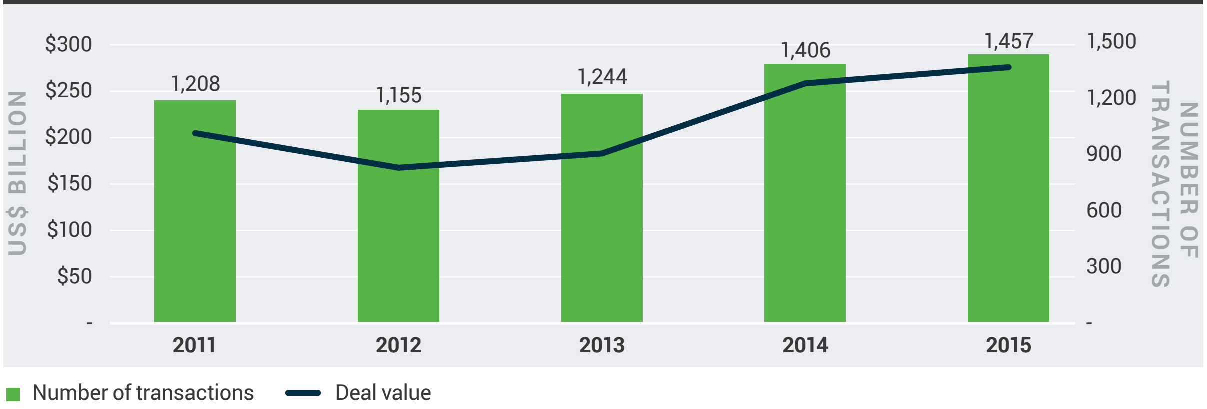
Accessing overseas markets and tapping new revenue streams are among the top motivations that respondents say they expect will drive cross-border pursuits. Indeed, as competition in several economies sees their market shares eroded, traditional business leaders are turning to foreign markets to regain lost momentum. That rationale, along with a significant demographic shift as the nation's populace shrinks and grows older, has dominated the recent massive outbound wave of corporate acquisitions emanating from Japan.[5]

FIGURE 14: WHICH TYPE OF M&A IS LIKELY TO OCCUR AS PART OF A TURNAROUND IN ASIA PACIfiC IN THE YEAR AHEAD?



[4] Falguni Desai, "Asia M&A activity grows, led by strong China deal flow," Forbes, April 3, 2016.
[5] "North Asia M&A review: Trends shaping the region," Mergermarket – Merrill Corporation, February 2016.

FIGURE 15: CROSS-BORDER M&A IN ASIA PACFIC



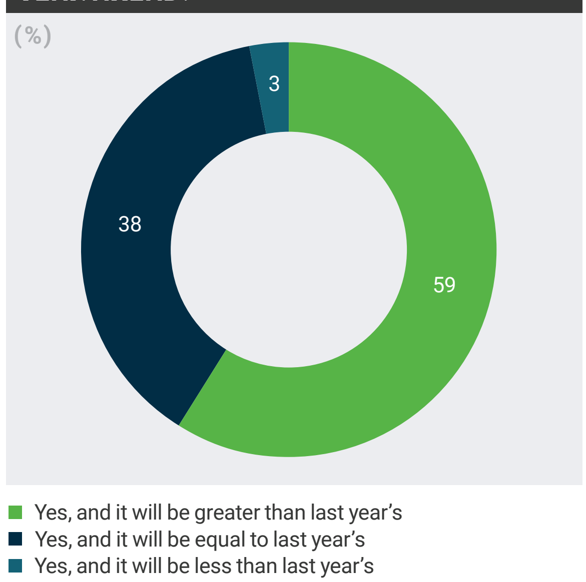
Cross-border deal making also gives access to modern, state-of-the-art technology or innovative processes not available in home markets. Respondents say cross-border deal making will be the predominant driver of international acquisitions—particularly with regard to targets in the pharmaceutical industry, wherein high-value drug patents and healthcare solutions offer significant value add (figure 17). Technology-driven transactions would likewise drive cross-border transactions in both the renewable energy space and the technology, media, and telecommunications sector, wherein ongoing innovation by established businesses and start-ups is creating similar value-amplifying opportunities.

Regulatory support and improvement of brand image are likewise among the top factors serving to encourage this trend, as many corporations have started receiving government support to venture abroad in head-to-head competition against international brands, says the head of a South Korean investment bank. Regulatory support and improvement of brand image have been behind a number of recent South Korean outbound transactions as well as the cross-border wave coming from China, where both state-owned enterprises and privately owned enterprises have been especially acquisitive in recent years.[6]

Among a small group of respondents, confidence runs high in the abilities of Asian corporations to execute these intricate international transactions. Elaborating on that, a partner at a Singapore-based hedge fund says, "Cross-border M&A will retain a strong position among corporate strategies going ahead because many corporates have gained the right amount of exposure to the global marketplace, and they have the capital and expertise to grow globally."

Other respondents are less sure. Several note the importance of an effective plan, adequate timing, and decisive leadership in taking a transaction from the boardroom to reality—a delicate process many corporate leaders have yet to firmly grasp. Equally important, research and respondent feedback from our survey last year (Opportunity Knocks: Success in Restructuring) indicated that the postmerger integration process inherent in M&A is causing headaches for deal makers (figure 18). Decidedly, 30% of respondents say that integration of business units posed the greatest challenge in their recent transactions, whereas only 10% say that that phase received the most time and resources

FIGURE 16: FOR ASIAN COMPANIES THAT ARE FACING STAGNANT NATIONAL GROWTH IN THEIR DOMESTIC MARKETS, WILL CROSS-BORDER M&A BE A COMPONENT OF THEIR TURNAROUND STRATEGIES IN THE YEAR AHEAD?



[6] "State-owned enterprises expected back at the forefront of Chinese outbound deal," Mergermarket, January 14, 2016.

from management teams. Adding to this, 99% of respondents last year said a poorly managed postmerger integration would have a negative impact on the newly minted organization and on the restructuring process as a whole.

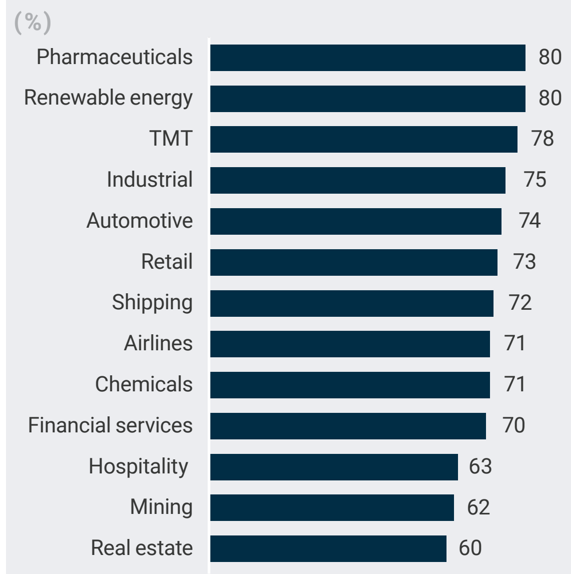
For those reasons, cross-border M&A could prove a greater challenge than anticipated for acquisitive Asian corporations, many of them unfamiliar with the intricacies of deal making or of operating in foreign markets. Although several notable, high-profile acquisitions have taken place in recent years, the list of failures has also grown; and respondents caution that even with adequate knowledge of the cross-border process, reaching out to advisors for additional support can only increase the odds of a successful transaction and turnaround.

CROSS-SECTOR AND INDUSTRY CONSOLIDATIONS

Not all corporations have reached the point where cross-border M&A has become part of their immediate short-term turnaround strategies. More than half of respondents say M&A will be a domestic affair in the year ahead as companies focus on reaching across industries rather than across borders to diversify (27%). An additional 24% say M&A will be governed by companies consolidating businesses within their primary industries (24%).

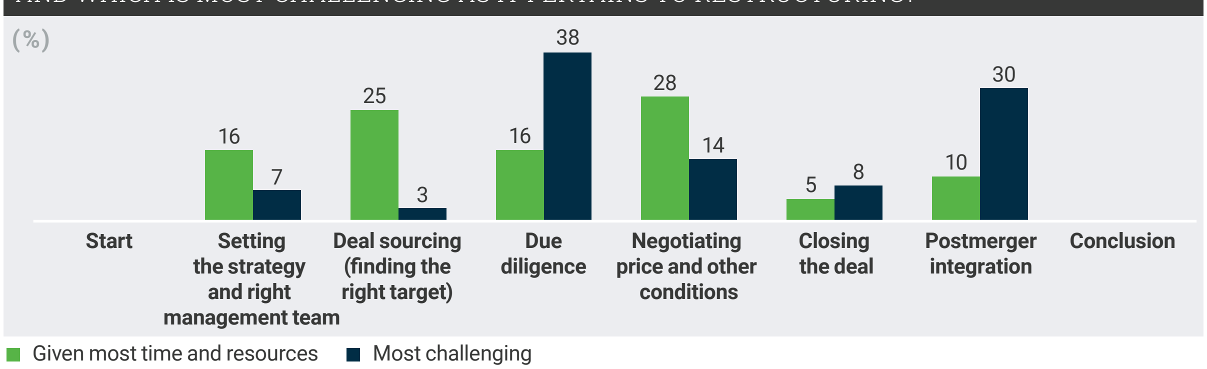
Focusing on industrial targets within their home market allows for diversification in an environment companies are already familiar and comfortable with while accomplishing their immediate growth targets. “Most businesses want to strengthen their presence in the existing market first, and so I think domestic transactions will be high in order to diversify and explore new opportunities in emerging industries,” says the executive vice president of a South Korean corporate and commercial bank.

FIGURE 17: WHICH INDUSTRIES WILL BE THE LIKELY TARGET OF CROSS-BORDER M&A IN THE YEAR AHEAD?



Growth can likewise be achieved through industry consolidation. A partner at a South Korean law firm says, “Similar-size businesses in the same industry are collaborating to take proactive steps against the market odds by focusing more on building up their core competencies and by adding up their capabilities to excel and ensure sustained growth in the market.” Noting distress across the region in industries suffering from overcapacity or competition from new market entrants, a partner at a China-based private-equity firm says: “I think industry consolidations will take place in the year ahead as companies with similar profiles that are undergoing crises join together and work toward resolving those shared issues. Given their familiarity with their respective industries, they will be able to increase one another’s level of support both operationally and financially and achieve synergies—or increase scale more efficiently.”

FIGURE 18: DURING THE ACQUISITION, WHICH TASK IS GIVEN THE MOST TIME AND RESOURCES, AND WHICH IS MOST CHALLENGING AS IT PERTAINS TO RESTRUCTURING?



Note: Results in figure 18 taken from AlixPartners’ Opportunity Knocks: Success in Restructuring survey conducted in 2015

Sundown in Asia Pacific: market forecasts and comparisons

The country-specific reasons may differ, but corporate restructuring activity is expected to post a noticeable increase across markets and industries in Asia Pacific.

Within those markets, changes that establish regimes for the process are also taking shape, albeit at a slower pace than corporate leaders and restructuring professionals hope for.

COUNTRY FORECASTS

Stemming largely from its decelerated economic growth and an explosion in corporate debt in the past three years, respondents unanimously (100%) say Greater China will see the highest increases in turnaround and restructuring activity in the year ahead (figure 19); 61% say those increases will be significant—a noticeable uptick from 2015, when only 41% held similar views. Much of the activity is anticipated to be distress driven, but a small group of respondents say Chinese corporations will be proactive in restructuring their businesses by way of internal assessment and outbound M&A, with the end goal of transforming into global corporations.

As noted previously, industry consolidation will likely be a key theme in the year ahead. Equally, depressed performance and forecasts by notable Western

FIGURE 19: OVER THE NEXT 12 MONTHS, WHAT DO YOU EXPECT WILL HAPPEN TO THE LEVEL OF RESTRUCTURING/TURNAROUND ACTIVITY IN EACH GEOGRAPHY?

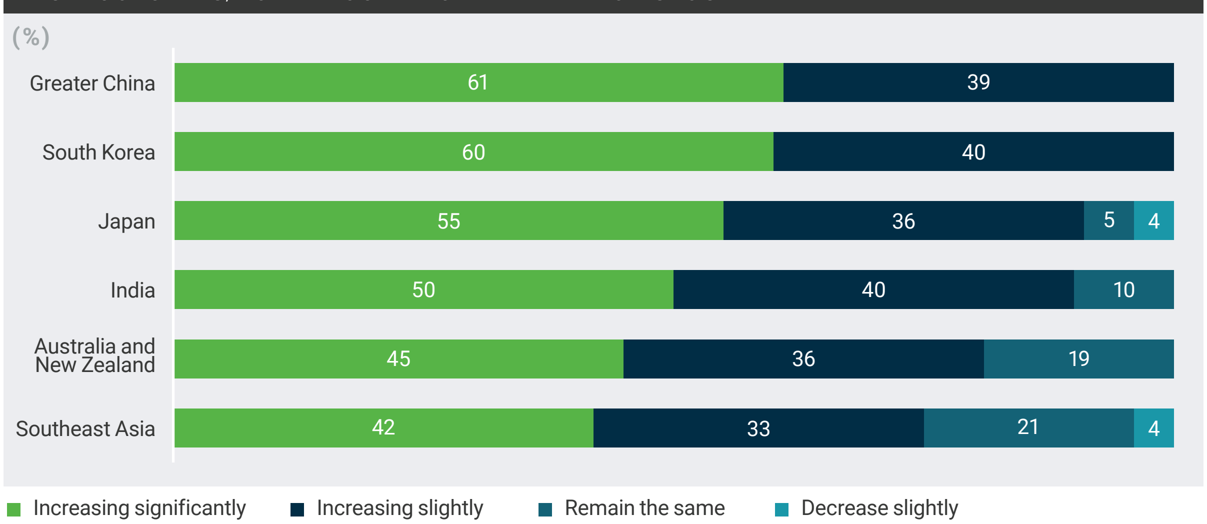
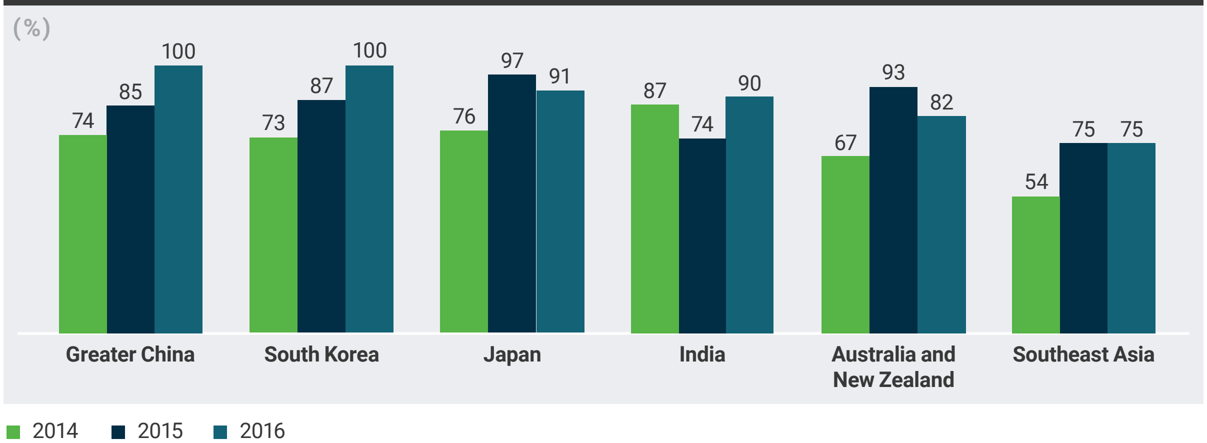


FIGURE 20: EXPECTED INCREASES IN RESTRUCTURING ACTIVITY ACROSS ASIA PACIFIC



corporations will serve as bellwethers for the market. For instance, feeling the effects of China's slowdown, US-based Caterpillar anticipates that the already sharp decline in demand for excavators and heavy equipment will continue. And although the company says it expects that a pickup in China could produce better results than in 2015, the chances of levels' returning to 2011–12 peaks are slim.[7]

Like in China, 100% of respondents say they anticipate some level of increase in corporate restructurings in South Korea in the year ahead. Slowed economic growth and intensifying competition from China and Japan will lead to a wave of restructuring in South Korea as the government there cracks down on zombie companies that have remained afloat on generous government subsidies.[8] As respondents note, distress that previously was contained within specific, export-oriented industries has started percolating throughout the South Korean industrial system, resulting in increasing expectations for restructuring during the past three years (figure 20).

While one of the few countries where a decrease, albeit minimal, in restructuring is anticipated, more than half of respondents (55%) say they expect restructuring to increase significantly in the year ahead in Japan and that that increase will be driven largely by asset sales and spin-offs as Japanese corporates divest noncore assets to focus on their primary lines of business.

In India, despite promising economic growth, the quality of that growth continues to be questioned as companies continue carrying heavy debt loads. For that reason and others, respondents say they anticipate a 16% bump in the likelihood of increases in restructuring activity in India in 2016 over 2015.

Volatility in commodity prices continues to weigh heavily on Australia and New Zealand, which continue feeling the backlash from China's economic slowdown and from the end of Australasia's mining boom, according to respondents. And even though the resources space will continue to drive restructuring activity in the year ahead, services-based companies could likewise seek turnaround opportunities as Australia and New Zealand rebalance from resource-dependent economies to economies focused on service industries.

In Southeast Asia, sentiment is more subdued. Although countries there have also been hard hit by China's slowdown, positive and sustained economic growth paints a more promising picture for companies in the subregion, according to respondents.

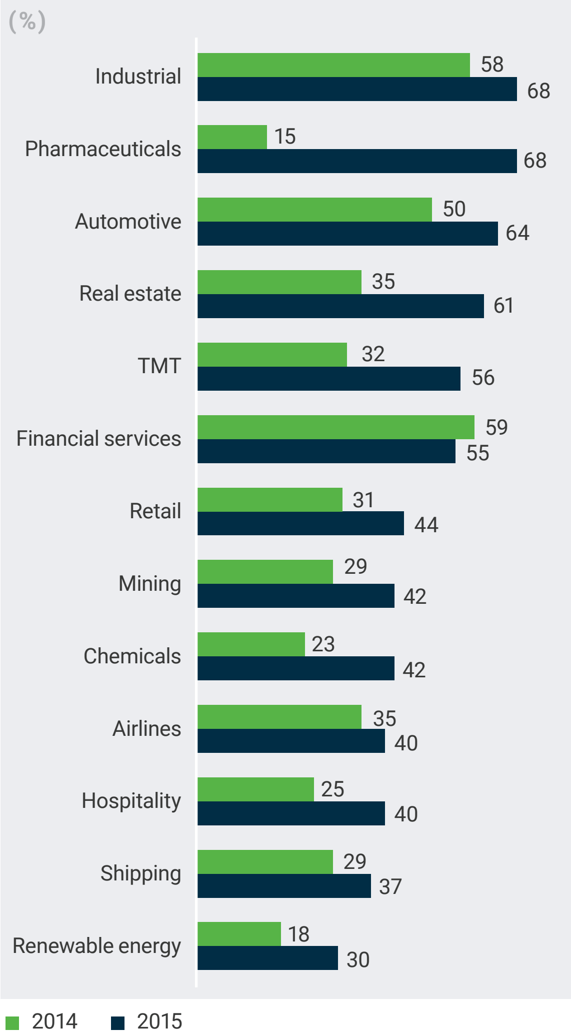
INDUSTRY FORECASTS

Pharmaceutical companies are anticipated to be among the top industries to see the greatest number of restructurings in the year ahead, according to 68% of respondents (figure 21). This is a noticeable increase in sentiments from 2015, when only 15% held similar beliefs.

Across Asia Pacific, respondents say rising demand for high-quality and affordable healthcare and medical solutions means pharmaceutical companies must focus on developing scale and on restructuring operations to adequately meet that demand. As a partner at a South Korean law firm notes: "The pharmaceutical industry has a lot of investor support and backing to realize its plans for growth. We're seeing many companies reduce their noncore units to boost R&D and acquire newer capabilities so they can gain the edge over local, regional, and international competitors."

[7] Leo Lewis and Kana Inagaki, "Japan Inc: M&A's big spenders," Financial Times, December 22, 2015.
[8] "Opportunity Knocks: Success in Restructuring," AlixPartners, May 2015.

FIGURE 21: WHICH INDUSTRY SECTORS WILL EXPERIENCE THE GREATEST AMOUNT OF TURNAROUND/RESTRUCTURING ACTIVITY OVER THE NEXT 12 MONTHS?



Similar to trends in past years, the industrial (68%) and automotive (64%) sectors are also anticipated to undergo restructuring as manufacturers consolidate or shutter operations amid slumping exports and declining sales both across the region and internationally. "The automotive sector will experience the greatest amount of turnaround and/or restructuring activity in the next 12 months due to changes in market demands," says a partner at a Singaporean law firm. "Consumer preferences are changing, and to meet their new tastes, auto giants will have to develop a new structure in order to develop new designs and car models."

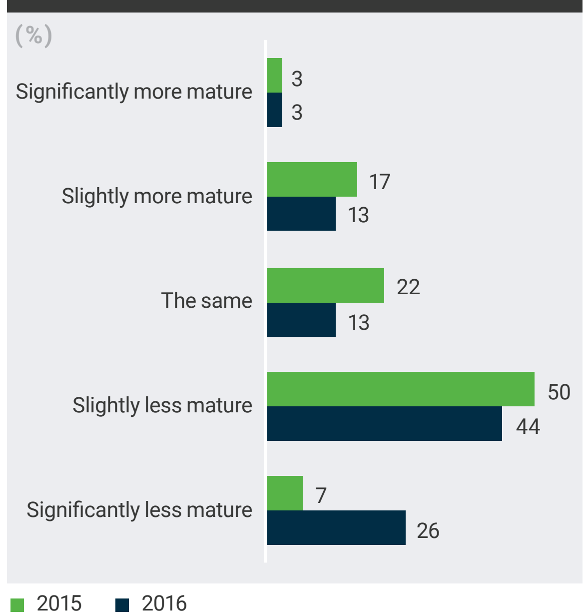
Technology, media, and telecommunication (TMT) companies are likewise anticipated to see an uptick in restructuring, with respondents' sentiments increasing from 32% to 56% because large firms are engaging in broad divestment programs as they focus on their core growth businesses and as they branch out into new tech fields, such as mobile and cloud computing.

"TMT will have the most turnarounds as they adapt to changing consumer demands, especially in emerging markets," says the managing director of a South Korean sovereign wealth fund. "They will now undertake new product development and roll out new services to remain competitive."

COMPARISONS

As in past years, respondent feedback has shown that Asia Pacific's restructuring environment has considerable ground to cover before it can reach a state of development on par with that of advanced markets in North America, and in Europe, the Middle East, and Africa (EMEA). Somewhat surprisingly, though, that gap seems to be widening amid a large increase in the number of respondents who say this landscape is significantly less mature than landscapes in the West (figure 22).

FIGURE 22: HOW WOULD YOU DESCRIBE THE RESTRUCTURING ENVIRONMENT IN ASIA PACIFIC COMPARED TO THAT IN NORTH AMERICA AND EMEA?



Note: Numbers do not add to 100% due to rounding.

FIGURE 23: HOW DOES EXECUTING A TURNAROUND OR RESTRUCTURING IN ASIA PACIfiC COMPARE TO SIMILAR ACTIVITY IN NORTH AMERICA OR EMEA?

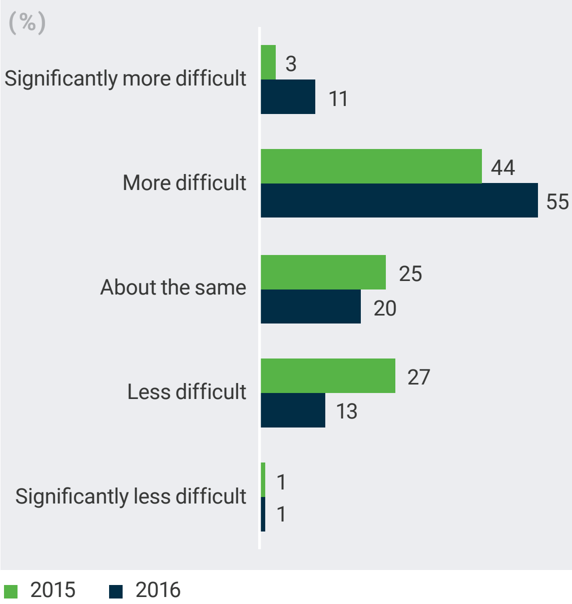


FIGURE 24: WHICH OF THE FOLLOWING WILL POSE THE GREATEST CHALLENGE TO CORPORATE RESTRUCTURING IN THE YEAR AHEAD?

Respondents say that the region's diversity may be contributing to that widening gap, with the reasons ranging from individual national policies and economic growth to complexities in trade and cross-border acquisitions. Respondents also point to several recurring areas where Asia-based companies are lacking, such as:

- Lack of skilled restructuring professionals
- Lack of corporate leadership
- Lack of regulatory frameworks
- Lack of a sense of urgency about the restructuring process

Backed by decades of experience with both successes and failures, corporations and management in North America and Europe are pioneers in the restructuring space, and they have developed an effective playbook of best practices to follow, according to the managing director of a corporate and commercial bank in Greater China. A partner at a Japanese law firm reinforces that point, noting that the knowledge gap in carrying out a restructuring puts Asia-based companies at a disadvantage.

While many countries across Asia Pacific have enforced corporate restructuring regimes, generally the region still remains underdeveloped in that respect. Rules and regulations are prone to ambiguities or may in some way—either advertently or inadvertently—hinder the reorganization process, the managing director of a Japanese investment bank says. And amendments to existing frameworks have been slow to adapt to today's rapid changes in international business.

However, it may be lack of a sense of urgency among corporate leaders that poses the greatest obstacle. As the senior vice president of a China-based bank says: "Our businesses lack maturity, in that timing, strategizing, and then executing a restructuring are not as in-depth as those in North America and Europe. Our approach [in China] is more traditional and lacks the innovation of international companies and business leaders."

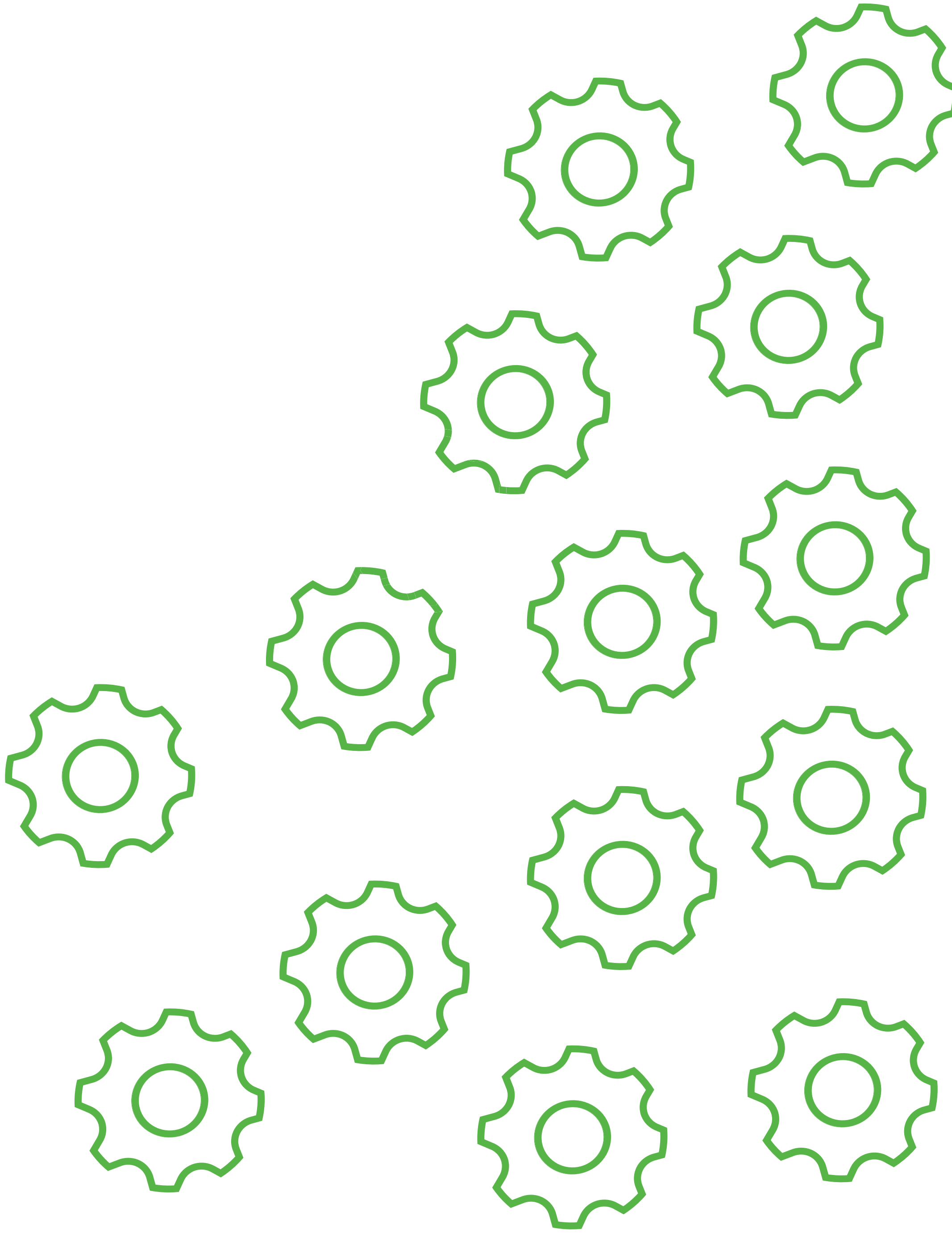
Adding support to the idea of early and adequate preparation, the executive director of a Malaysian investment bank says: "Advancements in the United States and EMEA mean that they can consult quality forecasting for future growth, which starts by planning a restructuring much further in advance than we do in Asia. This also gives them time to use technologies and harness efficiencies. And more important, it cuts down on the number of surprises that can often arise during these complex reorganizations."

For those reasons, the majority of respondents say that executing a restructuring or turnaround is more difficult in Asia Pacific than it is in North America or EMEA (figure 23).

CHALLENGES IN 2016

After a year of market volatility, respondents remain uncertain as to how the rest of 2016 will progress. As such, creating accurate financial forecasts remains the top challenge for corporate restructuring in the year ahead as the impact of economic conditions in North America and EMEA (65% of respondents say this would be significant) and the slowdown in China (68% of respondents say this would be significant) take their roll on Asia Pacific (figure 24).

Global and regional uncertainty will also make maintaining relationships with lenders, suppliers and customers an ongoing obstacle, alongside refinancing debt with banks and negotiating with creditors.



Conclusion

Headwinds are clearly creating the need for restructuring, as slow economic growth and volatility may become long-term problems and not just short-term inconveniences. And even though many companies are indeed taking steps to reconcile losses and underperformance, more work is needed in stressing the importance of taking those steps.

A good starting point in this ongoing conversation is to address respondents' general view that these drives are being launched at such a late stage as to suggest that they are not being taken seriously. Remedying that matter is of utmost importance, lest restructuring remain a back-burner issue or a process that when executed is done to such ill effect that it causes more harm than good to the enterprise's health.

Given the overwhelming expectation that restructuring will be a top-down venture driven internally by CEOs and upper management, those concerns could be difficult topics to broach. Those leaders, after all, may be the reason restructuring efforts are consistently delayed or given secondary priority status after other corporate activities. But the reality is that if those management teams are indeed unable or unwilling to put actions toward restructuring efforts into motion or if they are failing to act before conditions reach distressing levels, then consideration of alternative leadership should become part of the discussion about ways to return the company to profitability status.

As one possible solution, greater shareholder involvement and activist investors can help motivate current management to action or provide additional insight and support. Corporate boards, too, should place greater confidence in interim management and CROs if the task seems to be an overwhelming burden or a drain on managers already embroiled in day-to-day responsibilities.

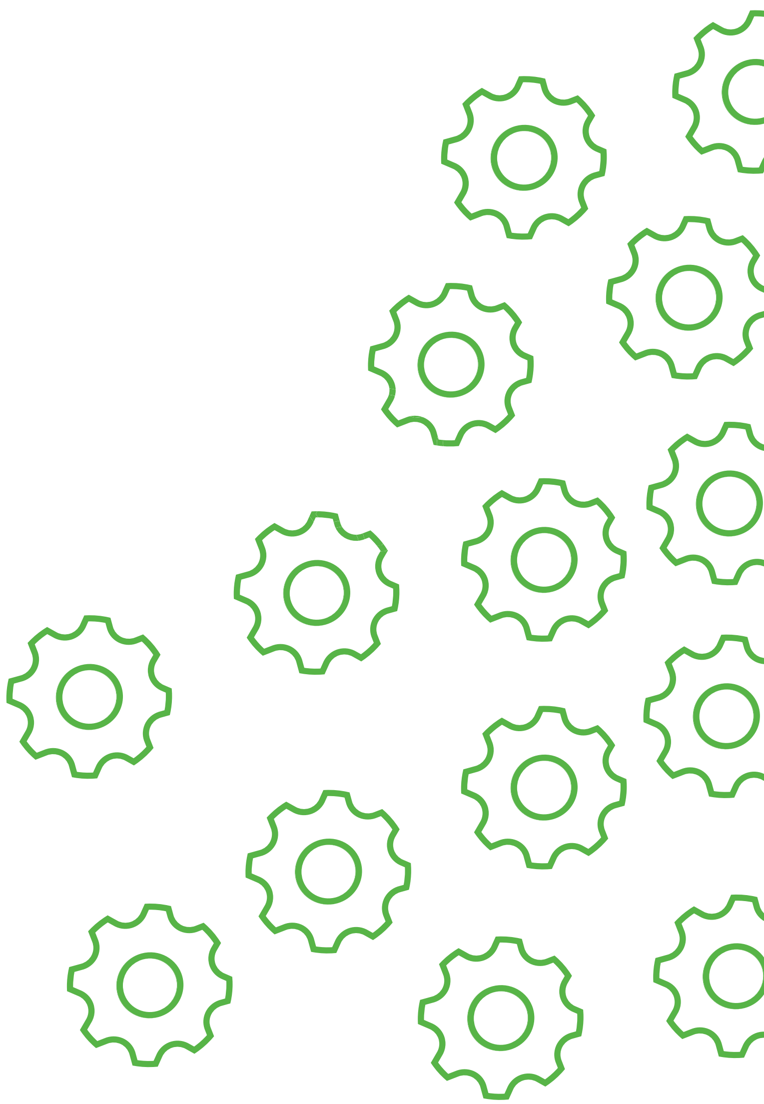
Without strong leadership at the core of a company turnaround, the available list of restructuring options may prove futile. And the longer those decision makers take in choosing which areas of the business to address first, the shorter that list becomes.

The importance of a robust management team becomes apparent particularly in the undertaking of an operational restructuring. The complexities of that kind of change demand (1) the involvement of managers aware of the requirements and challenges of such change and (2) managers' recognition of the time needed so that execution is not so hasty as to cause thing to run off track. Nowhere is this more important than in the area of cross-border M&A, an increasingly tried and tested means of starting transformative change but one that requires aggressive, mindful management to stay on course.

Given the findings this year—and as corporate distress becomes more visible—corporate leaders and management teams will find it to their advantage to consider doing the following.

- **Stay ahead of distress.**
  Finding a solution to whatever is ailing the business requires an expeditious approach. Waiting for deeper signs of distress to show means it may already be too late, and losses so far sustained may be difficult to recoup. Staying ahead of distress places more options at your disposal, and it gives management teams a needed advantage when undertaking an already challenging change process.
- **Call for backup.**
  The best corporate leaders know that successful turnarounds require an all-hands-on-deck approach. Sometimes the process necessitates interim managers in the form of CROs. Although a contentious topic in Asia Pacific, these participants should be considered for their value-adding abilities, not as potential threats to internal operations.
- **Choose wisely and know the challenges.**
  Consideration of the several options—M&A, cash management, overhead optimization, and revenue enhancement—when restructuring demands careful reflection on short- and long-term goals. Companies consistently plagued by financial issues may want to consider operational changes that would boost their capital positions and reinvigorate other parts of the business. Operational restructuring, however, usually has higher requirements for achieving desired outcomes, and management teams should be aware of them before a pursuit of operational restructuring.

Asia Pacific continues to make progress in the restructuring and turnaround space. However, the speed of that progress leaves much to be said. Whereas corporate reorganizations are indeed taking place, the overall volume, speed, and success rates of those actions show that regional corporations and management teams still have lessons to learn from their advanced-market counterparts in North America and Europe. The key concern now is that corporate Asia should realize that the volatile nature of the market may be more prolonged than in previous eras of slow growth and that they must act accordingly.



Methodology

From December 2015 to February 2016, Remark, the publishing division of Mergermarket, surveyed 100 lawyers, banks, and fund managers across Asia Pacific who had completed turnarounds or restructurings. The 100 consisted of 20 respondents from law firms, 20 from investment banks, 20 from corporate and commercial banks, 26 from private-equity funds, 10 from hedge funds, and 4 from sovereign wealth funds.

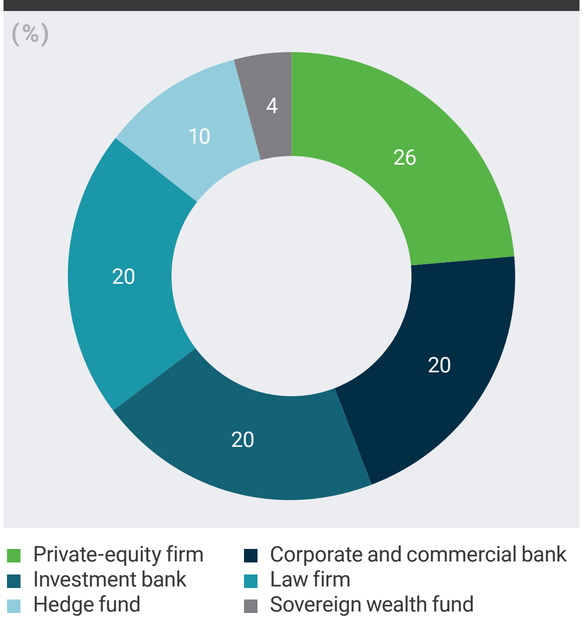
Survey results and graphs whose figures add up to more than 100% resulted because respondents were allowed to choose more than one answer.

All $ symbols refer to US dollars unless otherwise stated.

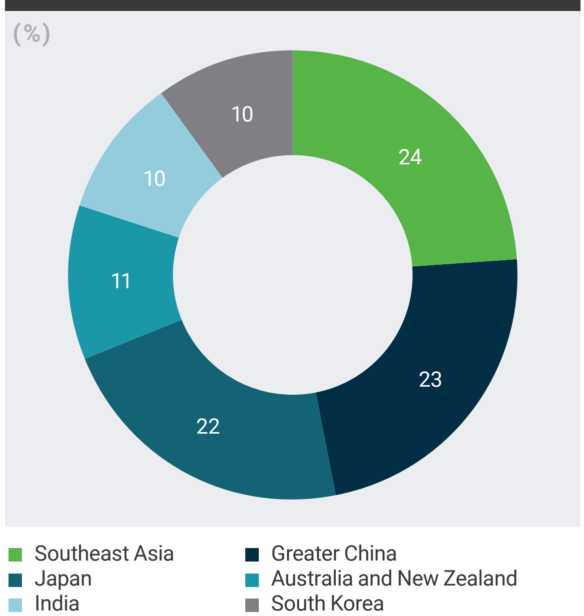
Greater China in all references comprises mainland China, Taiwan, Hong Kong, and Macao.

All data quoted is proprietary Mergermarket or AlixPartners data unless otherwise stated.

RESPONDENT PROFESSIONAL PRACTICE



RESPONDENT BASE IN ASIA PACIFIC



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Mergermarket is an unparalleled, independent mergers and acquisitions (M&A) proprietary intelligence tool. Unlike any other service of its kind, Mergermarket provides a complete overview of the M&A market by offering both a forward-looking intelligence database and a historical deals database, achieving real revenues for Mergermarket clients.

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