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"DEBT RESTRUCTURING: CONTENT AND PROCESS. THE STEFANEL CASE"

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PREFACE

The purpose of this study is to review the literature concerning the concept of corporate distress and to analyse in depth a concrete case of the Italian economic scenario.
In the first chapter, the main objective is to describe the characteristics of a company in distress, analysing and comparing the various responses given by different Authors of the economic literature regarding symptoms, stages of the process, causes.
The crisis is a physiological phase of companies' life cycle, the important thing for the management is to become aware of it in time and promptly implement corrective actions to facilitate the restoration of a normal condition for the firm.
The last few years have been characterized by one of the most intense economic and financial crises in recent history: many companies have suffered from this general climate of instability, stagnant consumption, difficulties in recovering financial resources from credit institutions, need to cut costs due to a contraction in revenues. Adding to these problems possible internal inefficiencies, inability to react to market pressures, slow change of business strategy, many companies have found themselves in a real difficult situation, especially those of small-medium size that have paid the highest price for this economic downturn.
In a period of economic slowdown, the attention to companies in difficulty is important: in fact, both from an economic and social point of view, the failure of a company not only implies significant costs to shareholders, creditors and employees, but also to the related community.
In addition, the first chapter also deals with the procedures made available by the Italian Legislator to protect the interests of the various stakeholders involved; in particular the distinction between out-of-court and in-court procedures with the related requirements, objectives, consequences, costs and benefits is underlined. A particular focus is given to the latest legislative modifications of Italian Bankruptcy Law, especially with reference to Article 182-bis.
Rehabilitating and restructuring a company in difficulty means taking significant risks, from both a financial and an operational-industrial point of view. For this reason, not everyone is willing to take on this responsibility, but in the last years a particular kind of operators have begun to care about this sector, also following the trend of the American and Anglo-Saxon markets. The second chapter will take into account the activities of private equity funds, especially in relation to turnaround operations in companies with economic and financial difficulties. This particular type of institutional investors, thanks to a huge background in

terms of corporate restructuring, is able to provide risk capital but also strategic and operational consulting with wide knowledge and experience.
In Italy, this type of activity is not generally carried out by Private Equity Funds, but rather by the banking sector. Although in recent years, also as a result of the Italian economic scenario, Private Equity Funds have found several opportunities on the national territory with regard to corporate restructuring operations.
In the third chapter, we will begin to talk about a practical case of an Italian listed company that is experiencing a strong distress condition and the intervention of Private Equity Funds: *Stefanel S.p.a.*
Stefanel is one of the Italian "historic" brands in the fashion and apparel industry but, in combination with the rise of the economic crisis in 2007-2008, have revealed some operational and strategic problems. In this chapter, a comprehensive analysis of the Stefanel Group's structure, strategy and business will be made. Then, the discussion will be implemented through the analysis of the Group's historical results of the last seven years (2010-2017) and the path to the crisis from its early stages with the main related causes and consequences. The examination also includes an analysis of the apparel and fashion industry in which Stefanel operates.
In the fourth chapter, the crisis of the Stefanel Group will be reviewed from the point of view of the procedures offered by the Italian Bankruptcy Law and used by the management team to resolve the situation. In fact, the Company has been forced to face a very difficult path of continuous treatment and rescheduling of the terms of financing with credit institutions, because of non-compliance with the financial covenants, until the intervention in 2017 of two Private Equity Funds to support a more structured and specific turnaround operation, as a last chance of salvation for the Company.

CHAPTER 1 – Corporate crisis and instruments

1.1 Introduction

In the last years, the business crisis has assumed a great importance; a crisis can be a sudden or gradual change that gives rise to a problem which needs to be solved immediately. For a company, the crisis means anything that could potentially damage its profit, its employees and all other people involved in business life. Companies have had to face and manage a particularly delicate moment characterized by radical changes in consumer tastes and habits, by a severe economic-financial crisis but also by an economic-industrial one, by a growing market dynamism, by the phenomenon of globalization, which have increased the riskiness of economic activities. This first chapter aims to investigate the meaning of "corporate crisis", what are the causes behind this phenomenon, what kind of effects it produces on companies and what are the solutions offered by the Italian Legislator. The chapter can be divided into three different sections: the first part, more theoretical, tries to give a definition to the issue of business crisis starting from the economic literature, analysing the evolutionary stages and describing the possible causes and anticipatory symptoms; the second part focuses on possible judicial and extra-judicial ways taken by the management to solve the crisis situation; while the last part focuses, coherently with the case study that will be developed later, on the art. 182-bis of the Italian Bankruptcy Law concerning the debt restructuring agreement.

The crisis is not a phenomenon that exists or does not exist, but it is a determinant factor in the degeneration of the company condition, which can be represented in a stage process, with different intensities and origins, that leads companies to the deterioration of their condition without a rapid reaction aimed at returning to a balanced situation. There are several alternatives made available by the Italian Legislature for the resolution of the crisis situation. The methods of intervention are multiple but can be distinguished into two categories: those aimed at business continuity and those aimed at corporate liquidation. The attention is focused on those aimed to treat the firm as a going concern, due to the case study that will be examined in the following chapters.

1.2 Firm's crisis: concept and definition

1.2.1 The crisis concept according to Literature

Over the years, the phenomenon of business crisis has been the subject of numerous studies, researches and publications, which have led to both innumerable interpretations by the various Authors regarding the definition of the phenomenon and the identification of various causes related to it, taking into consideration the historical moment, the managerial culture and the place in which they were developed. In particular, Italian literature, specifically with reference to Brugger (1984), Vergara (1988) and Guatri (1995), began to study and develop models on corporate crises in the early 1980s, subsequently analysing the crises of industrial systems, to then propose empirical-theoretical elaborations based on the Anglo-Saxon model.

According to the economic-managerial literature[1], the business crisis is the expression of the acute phase of a corporate pathology, called *decline*, which occurs through continuous economic losses, lower performance than competitors' ones, a growing illiquidity, the impossibility of fulfilling the obligations contracted, and the increasing degree of risk in the management of the company if no corporate reorganization process is put in place.

In particular, according to Guatri's studies (1995) "*the crisis takes the form of instability of profits that leads to ruinous economic and capital losses, with consequent disruptions in financial flows, loss of credit worthiness due to a lack of trust from the financial community, but also from customers and suppliers, thus triggering a dangerous vicious circle* ".

Not only there are difficulties in defining the concept of crisis unequivocally in the economic literature, but it is even possible to find a complete different view considering it from a financial point of view as a "*synonym of insolvency*" (Piseddu, 2011), considering in crisis "*the company which is not able to meet its obligations, or better, when there are no more the liquidity and credit conditions necessary to regularly fulfil the obligations contracted* ".

However, it should be emphasized that the prevailing point of view in literature considers the business crisis as a process in stages, applying a clear distinction between the concept of crisis and the one of insolvency. The crisis should not be interpreted as a phenomenon that exists or does not exist, but as a process composed of several stages characterized by different levels of gravity and different modes of development. In the next paragraphs, we will identify the

[1] Bertoli, (2000)
Guatri, (1995)
Sciarelli, (1995)

warning symptoms, the developmental stages of the crisis and the causes underlying the phenomenon.

1.2.2 Symptoms of the crisis

The fundamental premise to avoid the spread of the crisis is represented by the timely detection of the phenomenon. The direct identification of the causes is not easy, so it is useful to start with the recognition of symptoms.

Today, the market dynamics are so fast that the transition time from a first stage of a potential crisis to the next much more serious stages can take place over a period of months rather than years, as happened in the past. As a result, as soon as the company is able to perceive the symptoms of its own critical situation, the greater the possibility to implement corrective actions aimed at restructuring process. To highlight the most significant signs and symptoms of a possible crisis, and to conduct a deep analysis of its operational and financial developments, it is possible to use the data and indicators taken from the financial statements. The first signs of imbalance that arise from the reclassification of the Balance Sheet and the Income Statement are the contraction in revenues and productivity. The deterioration of the operating result, in some cases, may result in the inability to cover fixed costs of management, personnel payment and financial expenses; this results in economic losses that corrodes the equity and reserves of the company. It is not uncommon the need to apply a cost reduction policy, in line with the new sales potential, even if there is often an undifferentiated cost cutting without focusing attention on a targeted recovery through commercial or product strategies.

From a financial point of view, there is a strong reduction in liquidity, an imbalance in the financial structure, the difficulty in finding new financial resources, causing the beginning of financial crises. Regarding the financial crises, a first expression is represented by the inability to comply with the covenants on debt, those clauses included in the loan contracts through which the lender is entitled to change some of the contractual conditions upon the occurrence of specific events specified by the clauses. According to these clauses, the creditor-debtor relationship is subject to specific constraints that, if not respected, legitimize the creditors to request the early repayment of the loan or to renegotiate the financing conditions. The financial covenants refer to balance sheet data for the definition of indicators which have to comply with and respect threshold values. The covenants of this type are

generally expressed through a relationship between two financial values; some of the most used are:
- EBITDA or EBIT / net financial expenses
- NFP / EBITDA
- NFP / net assets

With the first index, we want to keep under control the company's ability to meet the payment of financial expenses using operational resources. The ratio between net financial position and EBITDA gives us the measure of the number of years theoretically necessary to repay the debt; it is aimed at monitoring the ability to face net financial debt using the cash flows from current operations. The last index expresses the leverage, the degree of dependence of the patrimonial autonomy of the company with respect to third parties.

Summarizing, some of the anticipatory signs may be: declining operating performance, rising inventories, falling debt ratings, higher volatility of the stock price (for listed companies), slowing revenue growth, resignations of managers or other relevant employees, worsening of average collection of receivables, problems with customers.

1.2.3 Developmental stages of the company

Each organization is characterized by a life cycle composed by the following phases:

- Creation (aggregation and organization of elements)
- Evolution (adaption, development, implementation)
- Decadence (progressive difficulties in responding to the demand, the environment and to put in place the conditions for achieving the objectives)
- Extinction (disruption and cessation of activity)

The life cycle of any company takes place with an alternation of positive and negative phases, the latter may be short and cyclical or, in the worst case, may have a structural character and generate a situation of decline. The most careful and endowed companies put in place preventive measures in advance, they prevent the crisis by deleting the premises when the first symptoms occur, before the crisis factors can generate imbalances and shortages or losses. Sometime the intervention takes place when the crisis is already present, but before it has produced its most serious consequences such as insolvency and failure. The goal is to restore the conditions of economic and financial equilibrium, more or less seriously compromised.

During a crisis, the company must promptly take the necessary measures to overcome the negative trend of decline. Depending on the severity of the crisis, which can lead the company from a situation of decline to failure, it is possible to distinguish different stages of development.

According to the approach adopted by Guatri (1995), the crisis can be interpreted according to four stages represented below.

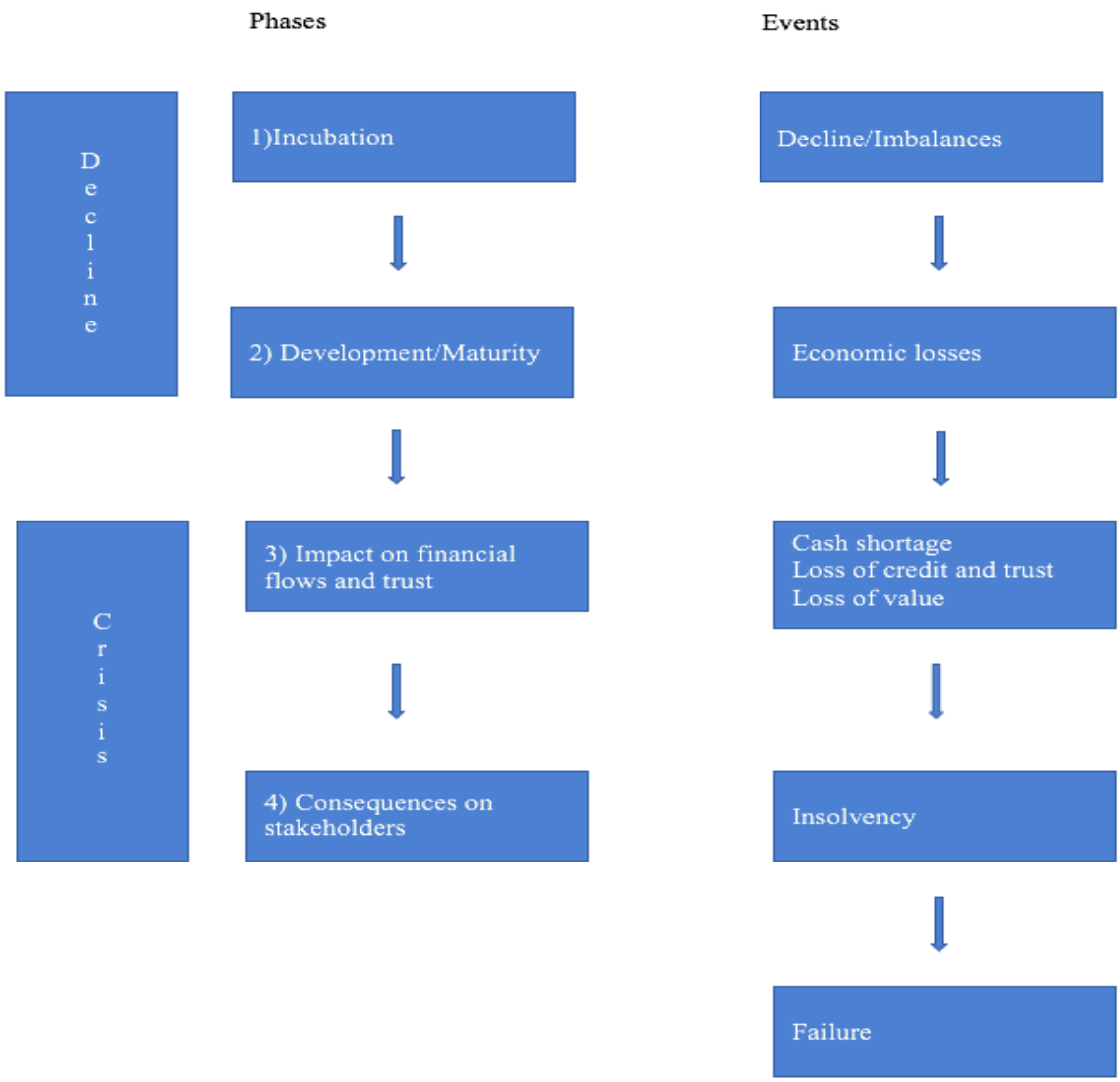


Figure 1.1 *The crisis process*

Source: Guatri, 1995

This process is composed by two different phases: the decline and the crisis.

The decline is the first phase and represents the moment in which the first inefficiencies and imbalances occur, it is the phase in which the income capacity of the company begins to be eroded and the corporate image tends to weaken, leading to a worsening of the quality of the products or services offered, but also to the deterioration of relationships with customers and suppliers. In this phase, the economic flows tend to decrease over time, although they do not necessarily take on a negative sign. This condition can become irreversible when the necessary corrective measures are not put into place promptly. The decline phase is composed of the incubation and maturity stages. The first one emerges through signs of decadence and imbalance that will lead to significant economic losses if the management does not perceive them and does not put in place the right remedies. The second one represents a worse evolution of economic conditions reaching a borderline situation between decline and crisis. The final effect is the shortage of cash to meet commitments. During the decline, top management has the opportunity to remedy the causes of inefficiencies, stop the decline and reorganize the company through a strategic plan, thus avoiding an irreversible crisis, since in the first phase the economic losses and the decrease in flows did not reach such levels as to cause a situation of insolvency. Turnaround processes are therefore first aimed at containing the loss of value that is recorded in this first phase and, only later, to stop it: only after having remedied the losses and downsized the risks, it will be appropriate to adopt strategies for the re-launch in the medium / long-term in order to generate new value.

The crisis is the evolution, in the absence of interventions, of the decline, leading to a situation of instability. If the situation becomes irreversible, it results in a state of crisis characterized by significant economic losses, imbalances in financial flows, decreased access to credit, drastic reduction of payment extensions granted by suppliers with a consequent increase in the financial needs necessary to cover the circulating capital requirements, tensions and disharmonies in the relationship with employees, loss of trust by the stakeholders, up to insolvency, or the inability to fulfil their obligations.

The reorganization of a company is configured as a complex process, which involves the assumption of significant risks, not only from the financial point of view but also at an industrial and operational level, which not everyone wants, or can, deal with.

Regarding to this argument, Buttignon (2008) proposes a model that allows analysing the evolutionary path of the crisis by identifying three distinct phases: potential crisis, governable or reversible crisis and the irreversible crisis (Figure 1.2). Through this scheme, the relationships over time between operating cash flows, going-concern value, debt and the liquidation value of the company are illustrated.

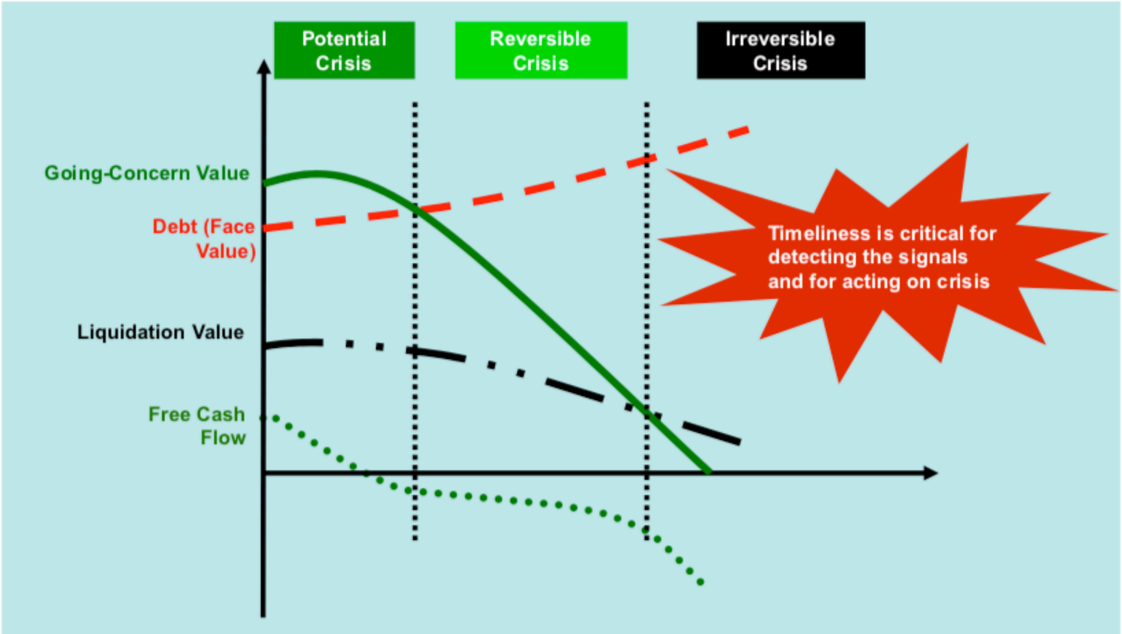


Figure 1.2 *Different types of crisis*

Source: F. Buttignon, *Firm's crisis and turnaround: Debt restructuring (2017)*, Advanced Corporate Finance Course

First of all, the situation of potential crisis is characterized by negative prospects for expected operating cash flows which appear destined to decrease in time following a series of specific strategic and operational phenomena of market and company (decay of demand, price pressure, loss of product competitiveness, cost dynamics, etc.).

Given an initial economic operating value, we can expect a more or less rapid decline of this value, depending on the prospects for future operating cash flows. However, the operating value, in this first phase, is perceived to be greater than the value of the debt but with a decreasing dynamic, which could lead to the critical point of the crisis: when the operating economic value equals the value of the debt. In this situation, the crisis occurs in an effective form, with the potential transition of control rights over assets from shareholders to creditors. The critical point does not depend only on the expected dynamics of the operating flows, but also on the amount of the debt. The higher the debt, the closer is the critical point, maintaining equal conditions. Regardless of the final results, the analysis and forecasting capabilities of the company's key players (management and ownership) are fundamental in order to identify the signs of the future crisis. Therefore, at the stage of the potential crisis the following aspects related to the principle of timeliness are relevant:

- Identification as soon as possible of the structural causes of decline in operating cash flows;

- Action on the causes of the crisis with internal management operations (restructuring plans and strategic-operational turnaround);
- Possible recourse to external ways for the resolution of the crisis (industrial alliances, entrance of new shareholders, transfer of control, etc.);
- Intervention on the financial structure aimed at acquiring new finance, as well as redefining the duration and conditions of the debt.

In the case that the potential crisis does not find a solution, the second stage, characterized by the governable crisis, occurs. The situation is characterized by the existence of an operating value of capital lower than the debt, but higher than the liquidation value. In Figure 1.2, the nominal value of debt is assumed to grow due to the worsening of the operating situation and the liquidation value is seen as decreasing due to the probable negative effects of the current crisis. The characteristic of this type of crisis is the progressively declining trend in the operating value of the company, which shows the need to operate promptly and efficiently to interrupt the fall. Timeliness concerns the awareness of the current crisis which, especially in the early stages, is not always evident to the subjects of internal control, to the identification of its causes and to the definition of the lines of intervention, which, at this point, must be necessarily both operational and financial.
The last one is the irreversible crisis identified with the situation in which the liquidation value is higher than the operating value, so that the use of a strictly liquidation procedure is justified in terms of allocative efficiency. The occurrence of this condition may derive from the lack of timeliness and efficiency of the interventions in the previous stages, however even at this stage it is necessary to promptly intervene. However, if there are no prospects for the recovery of corporate operating flows, not even following a restructuring process (highly probable at this stage), and if the value of single assets is positive, it is necessary to proceed with the disintegration of the business complex placing each asset to the highest bidder.
In the border area between the current stage and the previous one, it is possible to suppose "hybrid" situations in which the company as a whole can identify sub-groups of assets still endowed with a potential operating value higher than the liquidation one. Generally, these are values related to business units or individual business areas which, if isolated from negative factors, could have a positive autonomous value; in such cases it is advisable to separate the company into functioning and potentially efficient sub-complexes. In this sense, timeliness can still be a reference principle to preserve the so-called “precious elements” of a company in crisis, in the interests of current shareholders.

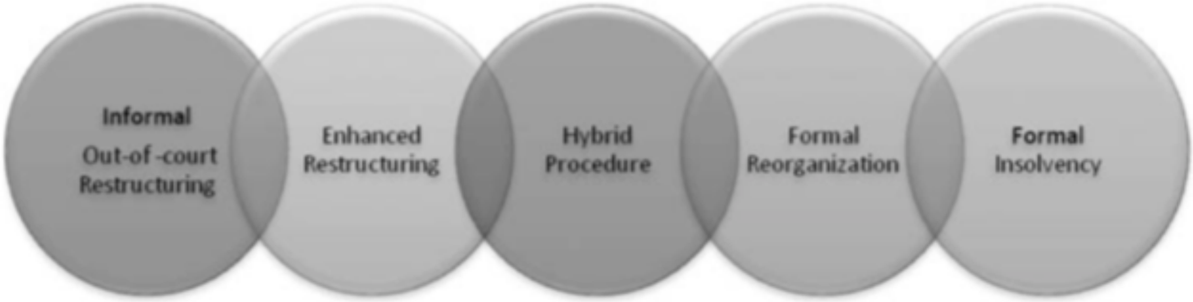


Figure 1.3 *The continuum of procedures for the treatment of financial difficulties*
Source: World Bank

The European Commission Communication of 2014 "*Community Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty*", which replaces the one of 2004 "*Community Guidelines on State aid for rescuing and restructuring firms in difficulty*", highlights the circumstances under which undertakings could be considered affected by the crisis:

"*For the purposes of these Guidelines, an undertaking is considered to be in difficulty when, without intervention by the State, it will almost certainly be condemned to going out of business in the short or medium term. Therefore, an undertaking is considered to be in difficulty if at least one of the following circumstances occurs:*

(a) In the case of a limited liability company, where more than half of its subscribed share capital has disappeared as a result of accumulated losses. This is the case when deduction of accumulated losses from reserves (and all other elements generally considered as part of the own funds of the company) leads to a negative cumulative amount that exceeds half of the subscribed share capital.

(b) In the case of a company where at least some members have unlimited liability for the debt of the company, where more than half of its capital as shown in the company accounts has disappeared as a result of accumulated losses.

(c) Where the undertaking is subject to collective insolvency proceedings or fulfils the criteria under its domestic law for being placed in collective insolvency proceedings at the request of its creditors.

(d) In the case of an undertaking that is not a SME, where, for the past two years:

i. the undertaking's book debt to equity ratio has been greater than 7,5 and

ii. the undertaking's EBITDA interest coverage ratio has been below 1,0."

These guidelines deal with three types of aid: rescue aid, restructuring aid and temporary restructuring support.

- Rescue aid is by nature urgent and temporary assistance. Its primary objective is to make it possible to keep an ailing undertaking afloat for the short time needed to work out a restructuring or liquidation plan. The general principle is that rescue aid makes it possible to provide temporary support to an undertaking facing a serious deterioration of its financial situation, involving an acute liquidity crisis or technical insolvency. Such temporary support should allow time to analyse the circumstances which gave rise to the difficulties and to develop an appropriate plan to remedy those difficulties.
- Restructuring aid often involves more permanent assistance and must restore the long-term viability of the beneficiary on the basis of a feasible, coherent and far-reaching restructuring plan, while at the same time allowing for adequate own contribution and burden sharing and limiting the potential distortions of competition.
- Temporary restructuring support is liquidity assistance designed to support the restructuring of an undertaking by providing the conditions needed for the beneficiary to design and implement appropriate action to restore its long-term viability. Temporary restructuring support may only be granted to SMEs and smaller State-owned undertakings.

1.2.4 Causes of corporate crisis

In order to build an industrial plan for company reorganization, the identification of the triggering causes of the crisis is one of the most important steps to understand where it comes from and what actions to take to solve it. This is therefore a crucial phase because it depends on the effectiveness of recovery measures. The literature has discussed about the matter over a long period, then coming to define two main lines of thought:
- Subjective-behavioural (such as Hambrick, 1996), which attributes the responsibility of the crisis to the human factor, such as the entrepreneur, managers and other members;
- Objective (such as Mc Gahan and Porter, 1997), which identifies as triggering factors the external elements linked to the dynamics of the sector, to the demand or to the financial markets.

However, business crises cannot be linked to a single triggering, endogenous or exogenous, cause but to the presence of factors both internal and external to the company itself.
So, analysing the crisis in a deep way we can find internal and external causes.

Among internal causes we recognize subjective and objective factors[2].
Subjective factors include:

- ownership,
- management,
- lender responsibilities.

While, among the objective factors we have:

- inefficiency crisis, if efficiency is low there is a cost differential compared to competitors;
- overcapacity crisis, collapse in demand due to the crisis in the sector, loss of market share compared to competitors, preparation of investments related to a forecasted demand growth that has not occurred,
- decay of products, decreasing of the margin and lack of coverage of fixed costs,
- a crisis due to a lack of programming / innovation, a non-proactive company, a lack of programming of objectives and resources,
- financial crisis, it is an effect and rarely a cause, it occurs in the financial dimension when there is an imbalance between monetary income and expenditure, but also in the equity dimension when the losses erode the capital and the insolvency of the company occurs.

Usually, external causes are not the triggering reasons for a crisis but they contribute to accelerate the decline. Among the external causes we can distinguish:

- macro-economic reasons,
- cultural and environmental movements,
- catastrophic events,
- industry and sector problems.

A recent classification of the triggering factors of the crisis was proposed by Capizzi (2012), which distinguishes between three categories of factors:

1. Macroeconomic factors (economic, cultural and catastrophic);
2. Sectoral factors (exogenous, linked to the life cycle and to the sector regulations);
3. Business factors (qualitative, quantitative and quali-quantitative).

[2] Falini, 2011.

The first two classifications refer to the type of objective crisis, as the business crises deriving from these factors cannot be attributed to the behaviour or errors committed by management, but rather to sectoral and cyclical dynamics. In Figure 1.4, a series of factors (macroeconomic, sectoral and business ones) are presented, showing how they present themselves and the impact they have on companies.

Macroeconomic Factors	Phenomenology	Impact on firms
Financial crisis	Volatility of rates Contraction of commercial transactions Fall in share prices	Contraction of revenues Increase of financial expenses Devaluation of assets Reduction of profits Increase of inventory
Globalization	Competition with emerging economies	Contraction of revenues Decrease of profits
Geopolitical tensions	Volatility of raw material prices	Decrease of margins Decrease of profits
Terrorism	Fall in share prices Contraction of commercial transactions	Contraction of revenues Increase of financial expenses Devaluation of assets Decrease of profits Increase of inventory

Sectoral Factors	Phenomenology	Impact on firms
Change in regulations of the specific sector	Liberalization Reduction of incentives Increase in technical or formal requirements to obtain licenses or concessions	Contraction of revenues Increase in financial expenses Devaluation of assets Decrease of profits Increase of inventory
Innovation	Introduction of new products or processes by competitive firms	Decrease of revenues Decrease of margins Decrease of profits Increase of inventory
Decline of sectoral life cycle	Consumption changes Introduction of new commercial or production models	Decrease of revenues Increase of financial expenses Devaluation of assets Decrease of profits Increase of inventory

Change in competitive intensity	More contractual power of clients and suppliers More potential new competitors and/or more substitutes More competition	Contraction of revenues Increase of financial expenses Devaluation of assets Decrease of profits Increase of inventory

Business Factors	**Phenomenology**	**Impact on firms**
Inappropriate governance	Inappropriate objectives Lack of operational leadership	Loss of contractual power Impact on balance sheet in the medium-long period
Loss of competitiveness	Obsolete products Inefficient production process	Decrease of revenues Decrease of margins Decrease of profits Increase of inventory
Operational rigidity	Excess of fixed costs	Decrease of margins Decrease of profits
Excess of debt	High financial leverage	Increase of financial expenses Decrease of profits
Inefficiency	Cost differential unfavourable compared to the competitors	Decrease of EBITDA
Incapacity in the timely detection of the crisis	Presence of the listed factors first in a soft way then in a strong way	Aggravation of the crisis

Figure 1.4 *The causes of corporate crisis*
Source: Capizzi (2012)

Once the crisis has been detected, it is necessary to analyse its causes and plan possible actions to remove them through the restructuring project, on the basis of which the choice between reorganization or liquidation will be made. This choice lead to compare the costs and revenues of liquidation with reorganization costs and value of the economic capital of the company restored at the end of the process. In making the choice it will be necessary to consider that in the liquidation process a high cost is represented by the destruction of a large part of the value of the intangible assets of the company. Choosing the reorganization leads to decide between privatistic solutions or the use of both administrative and judicial public procedures.

There is no doubt that situations of decline or crisis represent negative phases in the life of a company, but they should not be considered as catastrophic events, they can represent new managerial challenges in strategic, behavioural, organizational and cultural terms.

1.3 Choice of the instrument: judicial solution vs extra-judicial solution

The life cycle of a company is characterized by phases of prosperity and success, but also by phases of difficulty and crisis. Once accepted the situation of crisis, ascertained the causes and formulated a judgment in this regard, for the economic entity the first decision to be taken will be to choose between the continuation or the cessation of the productive activity. The possible alternatives among which the top management are called to choose are:
- Starting a rehabilitation process with continuity prospects of corporate processes and maintaining the current ownership and control structure;
- The sale of the company through which it continues to exist under the control of new shareholders;
- The liquidation of individual assets, or the independent sale of individual assets on the market.

The more convenient hypothesis will be the one according to which the expected benefits minimize the costs of implementation.
The evolution of the economic situation and the changing needs of crisis management have led the Italian Legislator to intervene on the Bankruptcy Law by introducing new instruments correlated to the current Italian scenario. The objective of the Law is to provide the entrepreneur with instruments that are less invasive and capable of intervening in the early stages of the crisis to resolve what should be a temporary difficulty, in contrast to the predilection of insolvency proceedings. The Bankruptcy Law, before the 2005 reform, offered suitable instruments to manage the irreversible crisis. Between 2005 and 2013 the Legislator intervened 15 times to modify the Bankruptcy Law by introducing 6 main reforms of bankruptcy proceedings for small and medium enterprises. After the changes introduced, the Bankruptcy Law has increased the possibility of managing the business crisis by entrusting the solution not only to the Courts, but, in the less serious cases, to those whose interests are directly involved in the business. Often the crisis is not sudden, but it allows to see symptoms and signals that should warn entrepreneur and stakeholders.

Pre-judicial instruments should be used promptly in the cases in which the company shows signs of concern and can no longer create value over several periods, without necessarily having negative economic results. In the absence of effective interventions, this situation can degenerate becoming irreversible. In this case the decline becomes an effective crisis, until it reaches a state of insolvency. The corporate crisis can get solution through two alternatives depending on the time of intervention, the degree of intensity of the crisis and the direct and indirect costs of the crisis for the company and its creditors: the judicial or in-court solution and the extra-judicial or out-of-court solution.

In the case of a judicial hypothesis, the company is subject to bankruptcy proceedings, in order to obtain the liquidation, and the crisis is considered irreversible.

The pros of this choice are represented by:

- the official nature of the procedure and
- the guarantee of fair/equal treatment.

The cons are:

- the length of the procedure,
- the very low recovery rates,
- the destruction of the intangible assets,
- may have social costs.

Instead, for the out-of-court hypothesis, the crisis is still considered reversible and the entrepreneur will have to choose the most suitable instrument based on the following elements: the intensity of the crisis, the need for confidentiality, the type of intervention required, the composition of the creditor class, the requirements of asset protection. It involves changing the composition and the structure of assets and liabilities of debtors in financial difficulty without resorting to a full judicial intervention and with the objective of promoting efficiency, restoring growth, and minimizing costs associated with the debtor's financial difficulties. These restructuring activities can include the restructure of debtor's business or finances. It is very important because, in many situations of financial distress, the debtor and the creditors can protect their respective interests more effectively with an informal solution, and can preserve the business value and the interests of other stakeholders to the benefit of the creditor as a whole. The most important advantages of informal workouts are:

- flexibility and easy adaptation to the specific needs of the debtor's business (it allows creditors and debtor to reach agreements with a wide variety of contents),
- ease of negotiation,
- timing issues (time is important to avoid the liquidation of the business and informal workouts are typically shorter than formal insolvency procedures),
- confidentiality (informal procedures are much more private processes than a formal insolvency, and they are perceived to cause less reputational damages),
- continuation of the debtor's business,
- no Court involvement,
- lower costs (workouts are less costly in terms of time, money and reputation).

The most important disadvantages are:

- analysis of the debtor's situation (insolvency proceedings are more detailed in totally analysing the finances of the debtor),
- punishment of fraudolent behaviour (formal insolvency is more suited to deal with fraud and criminal conducts connected to insolvency),
- lack of unanimity requirement.

In order to encourage the use of pre-bankruptcy instruments for the resolution of the corporate crisis, the Italian Legislator has made significant changes to the bankruptcy law with particular reference to the certificate plan, debt restructuring agreements and the composition with creditors.

The first procedure, the certificate plan, governed by the art. 67 of the Bankruptcy Law, is configured as a private agreement between the company in difficulty and its creditors, and not, therefore, as a bankruptcy procedure. The legislator leaves absolute freedom to define forms and behaviours to be adopted towards creditors, since different solutions can be presented, with different percentages of credit satisfaction, adapting the solution to the importance attributed to the counterpart. The fact, then, that the external professional must certify only the reasonableness of the plan and, above all, the absence of advertising are additional factors that lead many companies to choose this tool to face difficult situations.

On the other hand, the article 160 of the Bankruptcy Law concerns the possibility for companies in crisis of using the composition with creditors, whose main characteristics have been revised. In particular, the Legislator has moved in the direction of greater privatization of the procedure, allowing great importance to the agreements between debtor and creditor, to which ample discretion is left. Among the main new features of the new law, it should be noted the abolition of the minimum ceiling of 40% to be paid to unsecured creditors, while the possibility of dividing creditors into classes is introduced, offering each one a different percentage of credit satisfaction. Moreover, compared to the previous regulation, the majorities required for the approval of the procedure have been modified: first, in fact, the favourable vote of half plus one of the voters and two-thirds of the total amount of credits were required. Today, however, the percentages have been reduced and the approval of many creditors is sufficient as many represent the majority of credits or, in the case of distribution in classes, the favourable vote of the majority of the classes is required. Therefore, greater flexibility was introduced, with a view to safeguarding company values.

Finally, with the new Bankruptcy Law, a completely new instrument was introduced, governed by Article 182-bis, namely the debt restructuring agreement. This is a bankruptcy procedure, simpler than the prior agreement, which provides for individual agreements with the main creditors.

	Certificate Plan	**Restructuring Agreement**	**Composition with Creditors**
Regulations	Art. 67 co. 3 Lett. d) L.F.	Art. 182-bis L.F.	Art. 160 L.F.
Intensity of the crisis	Reversible crisis	Reversible crisis	More appropriate for a serious and irreversible crisis because it is invasive
Confidentiality requirements	Private agreement between firm and creditors, extra-judicial agreement, the publication in the commercial register is discretionary	The publication in the commercial register is mandatory, requirement of individual communication, possible coordination	The publication in the commercial register is mandatory, invasive, absolute transparency
Type of intervention	Financial operations, infra-group acts, reorganization	Agreement with creditors, faster, less invasive	Company transfer, variation in the composition of shareholders, personnel reduction

Creditor class composition	Few qualified creditors: it allows confidentiality, speed and flexibility	Few qualified creditors: more uncertainties, possible individual agreements	Fragmentation of creditors by type of credit: approval by majority method, no individual agreements
Requirements in order to protect equity capital	No specific requirements, except particular agreements	Possible advanced protection, limited in time	Possible advanced protection, maximum protection until conclusion

Figure 1.5 *Choice of the appropriate instrument*

Source: Convegno API, aprile 2013, intervento Avv. Carlo Tabellini, Torino

During the decisional process, first of all, it is necessary to consider not only the company itself, but the group as a whole, analysing the positions of the shareholders and any subsidiaries, affiliated or controlling companies, since only with an overview the consequences for the debtor in difficulty are limited.

Another very important variable is the time, since acting on time means being able to choose the best alternative and precede the situation of irreversibility.

The intervention time is crucial for two aspects:

a) It is essential to act immediately

b) Once the intervention plan has been drawn up, it must be respected.

The action must be on time to prevent the crisis from being irreversible and therefore not resolvable. This does not mean that decisions must be rushed, but that there is a conscious awareness of the situation of business difficulty.

One of the main reasons, why the reaction to the corporate problems is slow, is the perennial hope of making it in order to avoid the "shame" of bankruptcy due to the punitive culture towards errors. In other cultures, such as the American one, failure is not considered a fatal event, but a moment of learning during the entrepreneurial life. This different approach to mistakes and failures in addition to undermining entrepreneurial creativity can hamper decision making.

It is important to underline that the recent reform of Italian Bankruptcy Law has mitigated the previous approach by introducing a series of solutions aimed at safeguarding and revitalizing the healthy part of companies in the perspective of business continuity. Once the intervention plan has been set up, it is necessary to respect times and methods of action not mechanically and automatically, since it is important to periodically review the plan in light of the changes that will inevitably arise. Equally important is identifying the roles, responsibilities and tasks of those involved in the management and proper implementation of the reorganization on the basis of the action plan that has been decided.

1.4 Corporate Restructuring

After having identified the dimensions and the indicators of crisis situations, it is necessary to evaluate the degree of reversibility or recoverability of the crisis in order to start rehabilitation processes. The alternatives for restoring the company include interventions on assets (asset restructuring), and interventions on liabilities (liability restructuring) or financial restructuring.

- **Asset restructuring**

It should be the basic element on which to build the recovery plan, because otherwise if the business does not have prospects it would be useless to restructure the liabilities. This process is divided into three levels: the rationalization of the existing, the disposal of assets, and extraordinary finance operations such as spin offs, mergers and divisions. To understand what to dismiss and what to preserve, it is necessary to map the strategic areas in which the company is active and to evaluate the synergies and links between the different areas. It is therefore convenient to distinguish the core business areas and the other ones. When the core business can still be considered a sector with strategic potential for the company, the main objective will be to relaunch the company among the best competitors of the sector, improving performance and margins thanks to an increase in revenues and / or reduction of costs. The need to implement the action on the core business for a strategic relaunch of the company will force the operators to focus resources on it by subtracting them from less profitable areas. Recovery is more problematic when the core business has lost attractiveness. In this case, the search for a strategy that allows the company to simply rank above the industry average is not enough, but it will be necessary to focus on critical resources, branding, technologies and innovative capacity.

The asset restructuring is composed of:

<u>Income actions</u>

- Reduction / revision of the main activity and secondary activities. Identification of profitable and non-profitable activities, as it is necessary to eliminate inefficient cost centres and increase profitability, taking into account the current market but also future forecasts, because some products or services may currently be non-remunerative but have potential in medium / long term.
- Reduction / revision of the offices. The same analysis is applied to company offices, as the reduction of non-strategic sites will lead to significant cost savings without sometimes reducing revenues.
- Actions on costs. They include internal reorganization to improve efficiency, reduce fixed costs, restructure and reorganize the workforce and personnel, internalize or outsource production phases.
- Actions on revenues. They include the search for new markets and new products, the reorganization of sales and discounts, payment extensions.

<u>Property actions</u>

- Sale of non-profitable branches of business
- Dismission of properties

- **Financial restructuring**

- Debt restructuring. It is necessary an analysis of the composition of sources and their balance with respect to uses. Among the possible strategies there are: the renegotiation of bank debt, the rescheduling of debts to suppliers, the preparation of repayment plans with suppliers, the payment of tax debts.
- Procurement of new resources. Both with credit institutions already familiar to the company and with new ones because it is necessary to find the cash necessary to implement the actions of the turnaround plan.
- Intervention on capital by shareholders. The stakeholders, intervening on the capital, demonstrate to believe in the operation and in the company. Interventions by shareholders can be divided into capital contributions, waiver of shareholder funds with conversion to capital, refusal of interest or profits already approved.
- Credit collection

The financial restructuring carried out with banks involves the use of the following instruments:
- Standstill agreement concession, moratorium agreement. Banks' limited duration commitment to not request the payment of any amount, even if expired, due to encourage business continuity according to an industrial and financial plan for debt restructuring.
- Consolidation / rescheduling of existing loans. Review of the contractual conditions such as amortization schedule, rates and covenants. The purpose is to forecast the repayment flows on the basis of the cash flows expected in the financial plan. It is the most applied form of intervention.
- Grant of new financing resources. It can be appropriate when it is destined to finance investments that contribute to the process of recovering the company's value and to an expansion of the working capital to meet temporary liquidity needs. It is one of the most delicate and controversial tools because it increases risk profiles.
- Conversion of credits into shares or other equity instruments. Strengthening the relationship between the bank and the company in the short term may also mean that the bank uses methods of direct involvement in support of the company.
- Search for industrial or financial partners in order to recapitalize. This is a sign of trust for the banks in the business plan by current or new shareholders to support debt restructuring. In the absence of availability for recapitalization by current shareholders, other third investors, such as industrial partners in the event of synergies or financial partners such as private equity funds, can be involved with the aim of reorganization and turnaround actions.

The restructuring has also to include the revision of the business model strategy, the consulting on the adoption of temporary managers, any change in the company's governance, possible repositioning of the market, entry of new financial or industrial partners within the company.
<u>Management Actions:</u>
- Management change. It is one of the most drastic solutions used mainly in the Anglo-Saxon countries. In Italy, this solution is adopted in large companies but is not easily accepted in small and medium-size enterprises.
- Management training. Less drastic and the most used tools are coaching and mentoring. The coaching provides a training plan through the clarification of the objectives and awareness of the potential of the person. In the turnaround phase, executive coaching is addressed to senior managers and consequently to all personnel. Mentoring, on the other hand, involves the assistance of a senior consultant and / or manager (mentor) for a limited period of time. It is

fundamental for both the concept of individual empowerment from which the whole company will benefit.
- Temporary management. The use of external managers who intervene for a limited period (from 3 to 24 months) and who, thanks to their professionalism and experience, manage to carry out an effective and incisive targeted intervention.

A restructuring process can be considered concluded only when the company is able to create value; it is important to emphasize that although the income dimension constitutes the most important element, it has to be linked to competitive, social and innovation dimensions whose positive long-term performances are the basis of durable value creation.

1.5 Focus on the Restructuring Agreement: Art. 182-bis Italian Bankruptcy Law

The new law rises in a context in which, after the financial crisis that has hit the international markets, there are many Italian companies that have to deal with a declining profitability, with the inability to face punctually payments and with the difficulty of honouring their debts. Banks, affected by the problem of liquidity, have interrupted the flow of loans to companies, especially to small and medium-sized ones, creating a vicious circle that has involved not only companies already in difficulty, but also healthy ones. On the one hand, banks, in order to improve their economic and financial position, restrict credit, on the other, small and medium-sized companies suffer from the liquidity crisis. Consequently, many companies, even listed and even if not in situations of insolvency, in these months are facing moments of crisis, observable by the analysis of different factors, such as the decline in cash flows, the difficulties in paying the employees and in collecting the credits or the delays in the payments from its customers, which require to postpone the deadlines. In the last period, it is common to hear about restructuring processes, with renegotiations of deadlines and terms of financing, recapitalization and new business plans. The goal is to preserve the value of companies in difficulty, ensuring continuity, and thus protect the interests of stakeholders. The attention has been shifted to the state of crisis as a situation of general difficulty of the company that does not necessarily degenerate into a state of insolvency, but can be considered transitory. The current legislation also focuses on the firm in order to guarantee economic continuity, and leaves more space for private autonomy.

Article 182-bis Italian Bankruptcy Law

The entrepreneur in a state of crisis may request, by filing the documentation referred to in Article 161, the approval of a debt restructuring agreement signed with creditors representing at least 60% of the claims, together with a report prepared by a professional, appointed by the debtor, in possession of the requirements of article 67, third paragraph, letter d) on the truthfulness of company data and the viability of the agreement with particular reference to its suitability to ensure full payment of creditors unrelated to the agreement to the following terms:

a) within one hundred and twenty days from the approval, in case of credits already expired at that date;

b) within one hundred and twenty days of expiry, in case of credits not yet expired on the date of approval.

The agreement is published in the commercial register and takes effect from the day of its publication.

The restructuring agreement is not considered part of the bankruptcy proceedings for obvious reasons that are listed here:

- there is no procedure, nor a provision of opening
- there is no appointment of bodies such as a commissioner, a judicial administrator, a delegated judge, a committee of creditors;
- there is no bankruptcy regulation of insolvency, not all creditors are involved in the agreement and any regulation chosen and implemented with the agreement does not involve all creditors;
- creditors are not organized as a collectivity of creditors but as the sum of many heads;
- the debtor remains the owner of the business, not only because it continues in its full powers of management and control, but also because there is no form of dispossession, as its acts are not subject to any constraints or control.

The debt restructuring agreement is therefore an out-of-court negotiation procedure, it is implemented by the entrepreneur through agreements signed with creditors representing at least 60% of the loans and providing for the full payment of creditors who do not take part in the agreement. The objective assumption of this alternative is a situation of reversible financial crisis. The Italian legislator emphasizes the autonomy of the debt restructuring agreement with respect to the composition with creditors, considering them as alternative instruments. The former, in addition to being an expression of the entrepreneur's autonomy, also allows a different treatment of creditors, whose individual agreements should be effective independently from the homologation of the Court. The process of debt restructuring agreement is divided into three distinct phases:

- Out-of-court agreements between debtor and creditors representing 60% of liabilities
- Approval of the agreements in front of the Court
- Implementation of the plan, which is not regulated by the legislator and which takes place without the presence of judicial bodies

The debt restructuring agreement is a negotiating agreement with a private nature between the debtor and his creditors, with whom the terms and conditions for the fulfilment of the related claims are established. It is combined with the report of an expert attesting the truthfulness of the company data and its feasibility, and it is published in the register of companies and approved by decree of the Court. During the approval phase, the Court does not comment on the substance of the opinion expressed by the professional who drafted the report, but it will only assess the consistency and completeness of the procedural and argumentative process of the professional, with the consequence that the approval of the agreement does not involve the judicial verification of its feasibility. On the other hand, in the case in which some oppositions are presented by creditors that are not satisfied with their percentage, the Court, without going into the details of the choices, must also verify the reliability of the agreed program.

The restructuring agreement implies a situation with two categories of creditors: those involved in the agreement and those that are unrelated. The formers share the industrial and financial restructuring project with the company, accepting the unequal treatment with respect to the unrelated creditors, for whom full satisfaction is requested. The latter, in the first approach of the reform, appeared in an excessively asymmetric position because they were aware of the crisis situation and the terms of the restructuring project, but they fully retained their rights. This constraint heavily conditioned the entrepreneur in difficulty who was forced to allocate an important part of his resources to the satisfaction of non-participating creditors, in contrast to those who had accepted the restructuring of the debt. In this context, the creditors were not encouraged to join the restructuring plan, in order to keep the credit as a whole, without granting any extensions or discounts. In its new formulation, after the changes introduced by the law n. 134/2012, the article 182-bis of the Italian Bankruptcy Law, in addition to the changes of the payment terms of the unrelated creditors, has removed these restrictions by introducing a compulsory moratorium for creditors who do not adhere to the debt restructuring agreement. The judicial institution tries to face the situation where two conditions exist: the plan sharing between the company (including any new shareholders) and the creditors involved, and these creditors must unanimously approve the plan in an out-of-court context; and, on the other hand, the full payment toward creditors unrelated to the plan. The advantages seem to be the limited Court protection on the individual actions of creditors and the full protection of the risk of revocation on acts, payments and guarantees put in place in execution of the plan. The risks are linked to: the expert's judgment (which may not be in line with the prospects of the company and of the creditors involved); the possible negative effects induced by full publicity on the state of crisis; the areas of discretion of the Court regarding the approval (and the problems in case of negative judgment).

The OIC principle 6 defines the debt restructuring operations as follows: "*debt restructuring means an operation by which the creditor (or a group of creditors), for economic reasons, makes a concession to the debtor in consideration of the financial difficulties of this one, a concession which otherwise would not have been granted. For these reasons, the creditor is willing to accept a restructuring of the debt that involves methods and procedures that are more favourable to the debtor. The creditor's concession consists in the refusal to some contractually defined rights, which result in an immediate or deferred benefit for the debtor, which benefits from such refusal, and in a corresponding loss for the creditor* ".

Consequently, two conditions must occur simultaneously to talk about "*debt restructuring operation*":

- The debtor must be in a situation of financial difficulty
- The creditor, due to the debtor's financial difficulties, makes a concession in his favour with respect to the original conditions of the contract.

As already pointed out, with the reform of the Bankruptcy Law the Legislator enhances the role of private autonomy in managing the crisis in which the company is involved. The scope of the Legislator is clearly to find solutions to the default risk of the entrepreneur that implies less public intervention of the economy in order to reduce inefficiencies and delays.

The doctrine has spoken about "privatization" of insolvency in contrast to the old "publicist" approach. This underlines the willingness of the legislative bodies to leave to the debtor and creditors, who are the subjects suffering directly from negative effects of the business crisis and having a particular interest in avoiding the dispersion of the productive resources, the task of overcoming the crisis with the new instruments, where possible, rather than "sanctioning" with a judicial intervention entrepreneur in difficulty leading merely to liquidation process (F. Di Marzio, "*The right to negotiate the business crisis*", Milan, 2011).

CHAPTER 2 – Private Equity Funds and Turnaround operations

2.1 Introduction

As already highlighted in the previous chapter, corporate crisis situations can lead to bankruptcy if there are no timely interventions aimed at solving company problems. Rehabilitating and restructuring a company in difficulty means taking significant risks from both a financial and an operational-industrial point of view. For this reason, not everyone is willing to take on this responsibility: industrial buyers, although possessing specific skills related to the activity of the sector, are often penalized by the lack of knowledge of technical and legal aspects; while banks often do not have an adequate structure to support the operational risks that the restructuring processes may involve. In recent years, however, following the trend of the American and British markets, even in Italy this activity has started to be carried out by private equity funds, within which a particular segment has started to develop, "the turnaround", dedicated to companies in difficulty. This specific category of institutional investors is not limited to the only provision of risk capital, but also gives an important contribution in terms of strategic and operational consulting, thanks to highly specific knowledge and experience. In Italy today, the turnaround segment within private equity is still underdeveloped and the number of subjects specialized in this category of investments remains rather low.

In this chapter, we will first try to make a general overview of private equity activities highlighting the main features, then we will analyse in detail the turnaround operations as investments in companies in crisis, and in particular the role of funds in these operations, giving a picture of the current scenario in the Italian market compared to the foreign one. It is a moment of great opportunity for the actors in this market, especially for the Italian case, since up to now the turnaround has remained on the margins of the operations carried out by private equity funds. Thanks to such interventions, assuming in part or totally the entrepreneurial risk and the responsibilities of relaunch, the specialized operator can facilitate the recovery of deteriorated situations, allowing the detention of economic value destined otherwise to serious economic and social outcomes.

2.2 Private Equity Funds

2.2.1 Definition

Private equity was created to offer the opportunity to invest in private companies to institutional investors: this is a riskier investment class, but also with higher returns compared to investments in listed companies (so-called public equity).[3]

The Italian Association of Private Equity, Venture Capital and Private Debt (AIFI) defines the private equity business as "*An investment activity in the risk capital of unlisted companies, with the objective of increasing the value of the company until its disposal within a medium-long term period* ".

The Private Equity fund is a collection of investors, retail and institutional, that pool funds to invest in ownership of company with the aim of improving its financial performance in view of capital gains upon an exit event as a sale transaction[4]. The key values of Private Equity funds are:

- high risk and potentially high return, because investments promise above-average real adjusted returns to compensate for the many risks committed capital is subject to;
- performance driven incentive system, because performance is the consequence of a strong alignment of interests between fund managers, management teams of the portfolio companies and the investors in the fund;
- active value creation, because funds must create value by providing resources to firms, being responsible owners and actively supporting management to improve company outlook;
- confines investment power, it is confined to the fund manager, once the capital is committed investors have no say in the investment process;
- flexibility as a strategic value, because extreme flexibility and creativity allows funds to catch emerging opportunities and capitalize on new markets and varied strategies.[5]

In this kind of operations, the private equity fund is placed in an intermediate position between other forms of financing, such as the granting of long-term credit offered by the banking system, equity invested by private shareholders and capital obtained through the

[3] Carlotti (2012)
[4] Berwin (2006)
[5] Acharya et al. (2013)

stock exchange, and it becomes an excellent and, sometimes, necessary way to pursue company growth.
The investment can take place either through the purchase of existing shares or through the subscription of newly issued shares, with the objective of increasing the value of the company, defined as "*target*", and the value of the shares acquired for the purpose of a subsequent liquidation of the investment within a medium-term period. Kaplan and Strömberg (2009) identify three different types of value increasing actions: financial engineering, governance engineering and operational engineering. They are not mutually exclusive, but each firm can choose to focus on some actions more than others. According to financial engineering, private equity investors provide strong equity incentives to the management of target companies and, on the other hand, leverage puts pressure on managers not to waste money. Governance engineering is related to the control of boards by investors and a more active participation than public company directors and public shareholders. In operational engineering, private equity firms bring their industry and operating expertise inside target companies. So, funds do not only provide capital, but also professional experience, technical-managerial skills and a network of contacts with other investors and financial institutions; they also require a restructuring of the management of the company from a managerial, administrative, organizational point of view. The creation of value is based on the corporate objectives formulated in the business plan, an essential document for obtaining an investment from these specialized investors.
The financial investor takes the form of a temporary partner, who will aim to monetize the value created when the objectives are achieved. The result of the fund in a given transaction is measured in terms of return on invested capital and therefore as capital gain. In more practical terms, the fund aims to obtain a "n" multiplier on the invested capital, usually an indicative annual return of 20-30%.

2.2.2 Activities

Private equity provides various benefits to the business sector; one of the most important functions is to provide the financial support necessary for start-up companies or companies in a different life cycle, which build their development plans on new strategies or growth through acquisitions. In addition, it provides risk capital for the development of new products or new technologies, to pursue internationalization, to increase working capital and to strengthen the company's financial structure or to restructure the company; it can also be used to solve problems related to property, such as generational change or both partial and total replacement of outgoing members.

The literature makes a segmentation of the types of investment taking into account the phase crossed by the target company, because the logic is that different stages of business are related to different needs, and, consequently, the specialized operator must have different characteristics to answer appropriately to these needs.[6] (Figure 2.1)

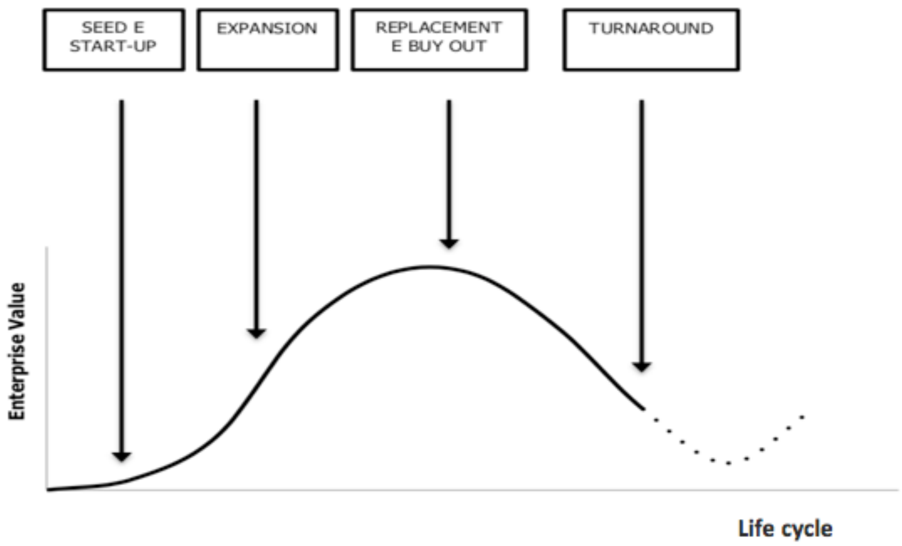


Figure 2.1 *Private equity operations and life cycle of companies*

Source: Gervasoni A., Sattin F., *Private equity e venture capital: manuale di investimento nel capitale di rischio*.

A first macro differentiation distinguishes between private equity and venture capital; the latter refers in particular to the financing activity in the early stages of company life or in the first period of expansion in which the yield-risk ratio is quite high.

According to these considerations and assumptions, it is possible to highlight the most popular segmentation accepted by most of the Authors of the economic literature.[7]

1. The financing of the first stages of the business includes the so-called *early stage interventions*, divided into:

- *seed financing*, investment in the very first phase of experimentation of the business idea, when the technical validity of the product / service is not demonstrated yet;

[6] Gervasoni, Sattin, (2007)
[7] Carlotti, Mougenot, (2001)

- *start up financing*, investment in the starting phase of a business activity when the commercial validity of the product / service is not yet known but there is already at least one prototype in the market.

2. In the second phase the aim is the support and development of the established company, investing in firms with high growth potential where it is important the consulting role of the fund for the benefit of entrepreneur or management regarding the financial and strategic matters. This phase includes *expansion financing* or *development capital*, implemented through a capital increase and aimed at expanding an existing business geographically or merchandisingly. These are investments in companies with rapidly growing positive cash flows and cash requirements linked to market development.

3. *Replacement capital*, when the objective is to replace or reorganize the corporate structure of a company in which the specialized investor temporarily replaces one or more minority shareholders, who are no longer interested in continuing the business, often linked with generational change.

4. In a different case, we can have the radical change in ownership due to various reasons, such as the willingness to liquidate the business activity, the impossibility of identifying an appropriate successor, the willingness to transfer activities from the public sphere to the private one. In all these circumstances, the investor's objective is to financially support the change in the ownership structure by assisting the new business group. From a technical point of view, these operations fall within the category of *Buy Outs*. Generally, the subjects are medium-large companies in which management plays an important role in the transaction by taking over the company together with a private equity fund. There are various types based on the role assumed by management within the operation:

- Management Buyout (MBO), the case in which among the new members there are company's managers
- Management Buyin (MBI), the case in which there are external managers who enter the shareholding structure
- Buyin Management Buyout (BIMBO), a mix of internal and external managers who control the company.

5. Finally, the category of *turnaround financing*, in which highly specialized operators focus their investments in companies characterized by situations of failure in order to restructure and make them profitable again.

2.3 Institutional Investors

The operators of this sector are specialized investors, who use the resources, collected from third parties and subjected to the regulation and control of the Supervisory Authorities, to carry out this particular type of operation and invest in a portfolio of companies. The typical structure of a Private equity partnership is the one showed in the figure below (Figure 2.2):

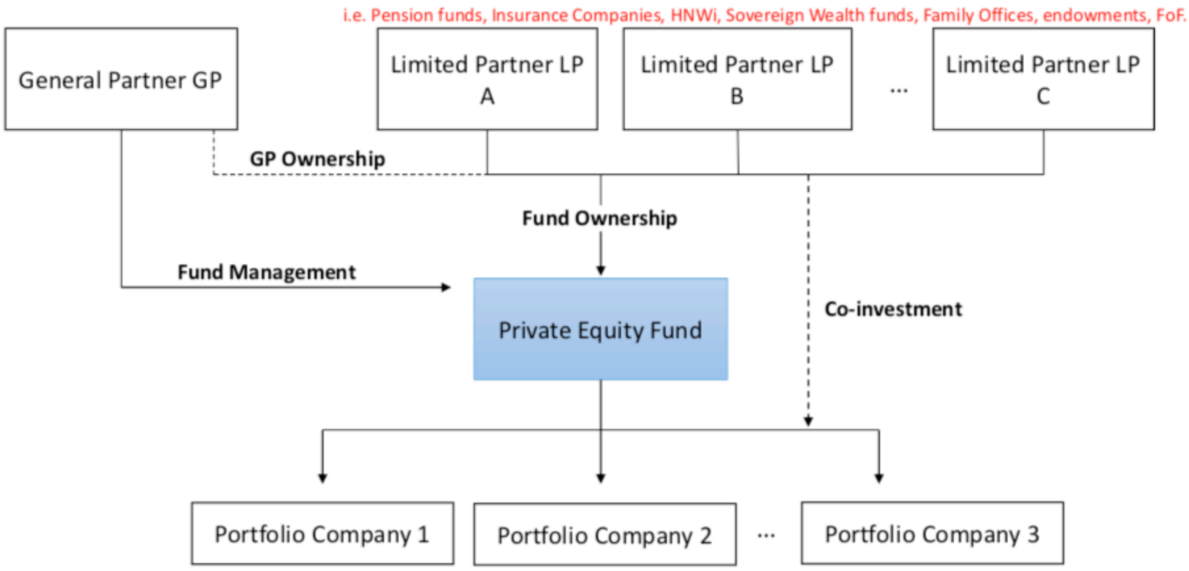


Figure 2.2 *Typical structure of a PE partnership*
Source: G. Chesini, *Il private equity e gli investitori istituzionali nel capitale di rischio delle imprese.*

The European Venture Capital Association (EVCA) defines investors in risk capital:
- who perform as main activity the concession of financing for the start-up or development of companies, or for the restructuring of companies or for the transmission of property
- who have as main objective the achievement in the medium-long term of capital gains to remunerate risks assumed
- whose investments mainly concern unlisted securities
- who can provide active support to management in subsidiary companies.

With regard to the Italian market, AIFI recognizes as operators those:

- who, as main activities, make investments in companies in the form of risk capital through the purchase, management and sale of stocks mainly in not listed companies on the stock exchange;
- who have a relevant involvement in the development of subsidiary companies without taking on the entrepreneurial responsibility.

These investors are specialized economic entities which finance and invest for a medium-long period of time in unlisted companies, with the aim of achieving a capital gain at the time of disposal.

Analysing what the institutional investor can do to create value in the company, the contribution of capital and the financial support are really important factors for the realization of projects otherwise not feasible, the financing of investments necessary for dimensional growth, the structural reorganization or the possibility of making acquisitions.

Another aspect, that should not be underestimated, is that the risk capital contribution allows the company to obtain credit in an easier way from the banking institutions, because the presence of new capital will have a positive effect on the grant of loans, the presence of institutional investors improves the corporate image towards credit institutions and makes possible to exploit the negotiation skills and knowledge of the financial market. In addition to the financial profile, the investor's role also offers benefits through improvement of the operational and strategic management control techniques, making the corporate structure more efficient, selecting management with professional competence, facilitating M & A activity with other companies belonging to the same sector, during the expansion phase it can support the listing process. The specialized operator, which invests in the target company, is also interested in correct and loyal information: it is necessary a daily flow of information and data in order to keep under control the company's progress, an analysis of the reliability of the administrative function and a certification of the financial statement. If there are particular objectives, it may also request a financial contribution from the other shareholders, such as capital increase or retained dividends for a certain period.

Institutional investments are not permanent, so the "*exit*" is an intrinsic phase of every deal and it is very important for the investor. The precise time of disinvestment is not easily established ex ante, because it depends on the performance of the subsidiary under various aspects. Usually, the most appropriate moment is considered when the company has reached an adequate level of development by increasing the value of the stock, or when the company is in a really difficult condition and has matured the idea that not even the presence of an institutional partner can be help in overcoming the critical situation. Obviously, if in the first case the exit is considered successful, in the second one we talk about write-off. Private equity investors need also to estimate a terminal value for their investment at the expected time of exit and they can use, at least, three possible ways of valuation: the discounted value of a growing perpetuity of the final year cash flow in a CAPM-framework, the value of comparable or similar public companies, and the value of acquisitions or transactions involving comparable or similar companies. The empirical observation, carried on by Gompers, Kaplan and Mukharlyamov (2015), indicates that funds are much more likely to use comparable methods than discounted cash flow methods.

Another important phase of the exit is the definition of the most appropriate divestment channel. The most frequent modalities are the sale of the shares on the stock market, the transfer of the shareholding to an industrial partner (*trade sale*), the transfer to another private equity operator, or the repurchase of the shareholding by the original partner who has maintained majority or minority shares for the entire duration of the restructuring process (*buy back*).[8]

2.4 Turnaround operations

The term *turnaround* indicates all the processes of reorganization and revitalization of companies. The principal aim of any corporate turnaround is to remove the company quickly from any immediate danger of going into liquidation, to focus on activities and tasks that restore corporate value and to build enterprises in which future buyers want to invest.[9] In fact, investors and buyers look for businesses that:

- create value in the medium-long term;
- have a high probability of future cash flows or have a history of performance and improvements;
- possess a market-oriented management team with a focus on producing revenues;
- are able to sell and compete, develop, produce and distribute products, grow in the right direction;
- exhibit a realistic return potential;
- have exit options with a high ROI realized at time of resale.[10]

[8] Cooke (2008)
[9] Downey (2009)
[10] Collard (2010)

The turnaround process can start both during the decline phase or when the crisis is already in a more complex phase, and the probability of success will depend mainly on the timing of intervention. It is a particularly complex intervention, both for the number of actors and for the many variables involved, and it is also affected by a certain level of uncertainty about its success. It is also an operation that needs a medium-long time period. The turnaround is a process that develops on different phases, starting from the identification of the crisis, with its diagnosis through a budget analysis, and from these data it is established if it is possible to carry out the turnaround operation. If this is possible, one of the tools provided by the Italian bankruptcy law will be used to ensure business continuity: certificate plan, restructuring agreement, composition with creditors. Even though the corporate restructuring cases are all different from each other, the literature has hypothesized a logical order of the different phases divided into four macro classes[11]:

1. recognition of the decline and change of management
2. evaluation
3. definition of a turnaround plan
4. rebalancing and growth

The first fundamental objective of a company in crisis is the survival and the achievement of a positive cash flow, only afterwards it will implement strategic policies with objectives of growth, acquisitions, launch of new products and positioning in new markets.

The awareness of the crisis situation and the recognition of errors is the first step towards a process of rehabilitation. Very often the replacement of the management or part of it with the introduction of a new CEO as a *turnaround manager* is necessary to implement the restructuring plan correctly, and to make the challenging and controversial decisions required to restructure the business[12]. The advantages of bringing in an external specialist are that: he has significant experience about turnaround techniques, he has no emotional “baggage” associated with any of the company’s previous business decisions and is not committed to the status quo, he is not part of the organization’s hierarchy and therefore often able to challenge the company’s management more freely. It is also possible to remove any senior managers who might obstruct the turnaround effort.[13] There are also situations, even if not so common, in which the decline in performance is not attributable to the managers of the company, but to economic recession: in such situations, the retention of the existing management is the most

[11] Sicca, Izzo (1995)
[12] Masciocchi (2007)
[13] Tourtellot (2004)

appropriate strategy[14]. At this stage, a key aspect is the presence of specialized advisory body, which can be represented by investment banks, management consulting firms, auditing firms, law firms or accountants with experience in the sector, supporting the drafting of the reorganization plan and everything related to the negotiations with external creditors and stakeholders.

The second phase is the evaluation and analysis of the current situation, supported by the identification of the causes and the formulation of a diagnosis, with the aim of understanding what are the possibilities for the company to complete a turnaround strategy. Only if the evaluation is positive, this analysis culminates in a preliminary action plan, stating what is wrong, how to fix, and which key strategies can turn the entity in a positive direction, and taking into account the reasons for the decline, the market position of the company, the losses incurred, the starting balance sheet, the life cycle of the business and how it relates to the chosen turnaround strategy, the projections in the short and medium term of the results obtainable.

In the restructuring plan, the third phase, we find the real project of restructuring and re-launching, which must involve not only the financial part but the entire strategic-industrial reorganization. According to Masciocchi (2007), the turnaround plan must have specific connotations:

- must interact with the phases described above and, depending on the urgency, can be set when some other interventions are already in progress
- must be a priority for the organization and help to re-establish the product strategies, the choice of the customers, the financial resources and the personnel selection
- must be approved by the board of directors and addressed not only to internal management, but to a wider audience that includes shareholders, stakeholders, public supervisory bodies
- must evaluate possible risks and consider possible alternatives to the first plan

The result depends in large part on a correct and clear communication, on the stakeholders' involvement and awareness of change, but also on the rationality of the plan that must be based on shared principles, on the consistency between objectives and expected results, on the convenience and conviction of the various subjects involved.

According to Bibeault (1999), the recovery process could be divided into three sub-phases:

1. the emergency phase: the objective is to guarantee the survival of the company by focusing on the cash flows of the core activities (6-12 months)
2. stabilization phase: transition from financial to economic logic, recovery of profitability (12-36 months)

[14] Whittington (1991)

3. growth phase: development of market share and medium-long term objectives (3-5 years)
In the fourth and last phase, rebalancing and growth, the turnaround plan focuses on the creation of new value, evaluating the business areas capable of producing future results and eliminating those unable of generating income. Managing these interventions is one of the critical aspects in the implementation of the plan, because it puts in place first the cuts discussed and then all those operations aimed at refining productivity. Various actions are necessary, from the attention to the product margins to the implementation of researches aimed at introducing new products on the market. In addition, many areas, like management control, administration and marketing, require the appropriate care to achieve improvements in effectiveness and efficiency. Finally, the recovery of trust, inside and outside the company, is an essential element to bring the business back to pre-crisis levels. The external credibility is essential to recover relations with stakeholders and obtain normal conditions for credit access, while the internal trust must involve and motivate all the staff. When the company returns to recreate the value the turnaround process ends.

In this process, the critical factors that require significant attention, and that are only partially influenced by management, are the coordination of creditors, the ways of renegotiation, the request for new finance.
Concerning the coordination of creditors, first of all, it is necessary to highlight the role they play, because their collaboration is fundamental for the success of the project[15]. The problem arises from the lack of resources, and it is not possible to satisfy all creditors with them. Moreover, each of them, with the tools available, will try to impose their personal interests, in contrast with those of other creditors, and finding an equilibrium in this context is not simple. The renegotiation of debt is another critical factor, since the positive outcome of the transaction is not exclusively dependent on the turnaround plan, but also on the availability of delays or refinancing by creditors. The management have therefore to formulate attractive proposals not only for the needs of the company, but also to those of the creditors. The success of the operation is also linked to the provision of new finance, especially in sectors that require frequent investments. This necessity creates a situation of impasse, in which it is necessary to borrow again to get back from the debt position.

[15] Fazzini (2011)

2.5 Role of Private Equity Funds in Turnaround operations

Compared to the past, the difficult economic situation has led, on one hand, investors to consider new investment opportunities, and, on the other hand, the companies to receive the intervention of third parties in a new way, where the entry of new members was not seen as mere speculation in favour of the funds' holders, but as a structured intervention in the medium-long term able to revitalize the company.

However, in Italy, compared to other financially more developed markets, the identification of the target company is one of the main problems. In markets, such as Great Britain and the United States, the managers or entrepreneurs look for a partner by their own and provide investment opportunities directly to specialized operators, while in Italy the search for investment opportunities falls exclusively on the funds that have to seek investment opportunities with a waste of resources; this derives from the lack of knowledge of these tools by companies.

A turnaround fund has the goal:

- to buy, generally at very low prices, companies with economic and financial conditions in decline, more or less advanced, but potentially still good
- to restructure companies to reduce operating costs and boost revenues by optimizing the level of invested capital
- to extinguish or, better, restructure the debt with banks and suppliers
- to intervene actively in operational management

The term *turnaround investors* refers to those involved in restructuring operations of mature companies, in a state of decline, but before the crisis is at an advanced and irreversible stage. Such investors must be highly specialized in terms of knowledge and skills in all phases of the operation. What differentiates institutional investors in special situations with respect to other private equity operators is not just a specific know-how in the sector, but also the ways in which the investment is addressed, such as the choice of the target company, the management of the intervention and the expected return. Turnaround leaders need to be able to articulate clearly the company's direction and rationale, convey a sense of calm, control and confidence to all stakeholders, replace any under-performing individuals quickly, motivate staff to achieve the required outcome, deal with board strategic issues while managing day-to-day operations.[16]

[16] Slatter, Lovett, Barlow (2006)

The turnaround investors look for companies operating in interesting sectors and with a good positioning based on significant distinctive elements: for example the brand, the company's history, creativity in product innovation, the superiority of the product itself or any other characteristic that makes the company attractive[17]. Target companies are selected by funds specially if the relaunch is not based exclusively on a recovery of sales, but also on a reorganization of products, control of costs and improvement of the distribution network or production process[18]. In turnaround operations, the purchase price involves not just a flow of expected income, typical of a company with a history of constant income and cash flow, but a set of tangible and intangible assets that the previous management was not able to translate into profitable results.

In the restructuring process, the investor brings his ability to identify the main problems and the consequent ability to simplify complex situations in order to concentrate on the change of few strategic factors. His intervention also guarantees a better negotiation experience, very useful in negotiations with creditors. Unlike other private equity operators, those who act in this sector always try to enter into company as a majority partner, in order to be able to exercise with certainty the power to make drastic but necessary decisions in very critical moments.

The role of such subjects requires a precise responsibility, first of all because they are in charge of raising situations often compromised. The development of these professional operators is highly appreciated in the industrial, institutional, banking and professional world as they represent an excellent solution in contrast to the cessation and liquidation of companies in crisis, and the consequent dispersion of their economic and social value. In fact, the intervention of specialized funds allows the saving not only of companies in difficulty, but also of brands, names and business stories that otherwise would have to be dissipated.

The importance of private equity ownership provides some natural advantages over public ownership (Figure 2.3). The key differences are the active role private equity boards play in setting the ground rules and their willingness to hold management teams accountable for driving a turnaround. The empirical observation shows that the most successful private equity company boards are able to quickly and significantly change the rules of engagement, clearly communicate specific performance targets, set an explicit timetable for action, and decide whether the CEO and management team have the mind-set and capabilities required to

[17] Gervasoni, Sattin (2007)
[18] Carlotti (2012)

execute the plans. Not all company boards must follow these prescriptions. Some may lack the time to do so, others have incentives different from those of private equity directors.[19]

	Turnarounds under public ownership vs	Turnarounds with active private-equity ownership
Alignment	**Blazing the trail** Board communicates goals, strategy, and expectations	**Setting the pace** Board communicates timelines, milestones, and targets
	CEO engagement Board primarily engages with CEO	**Senior-management engagement** Board engages with senior management, with or without CEO's guidance
Planning	**A "push" approach** CEO and senior management report to board at regular intervals	**A "push and pull" approach** Board actively seeks information updates as needed in between regular reports
	Top-down targets Board approves top-down targets, such as budgets	**Bottom-up scrutiny** Board monitors and holds management accountable for specific initiatives
	Long-term incentive plans Board develops incentive plans for long-term growth, taking into account corporate, unit, and individual performance	**Turnaround-attuned plans** Board incorporates specific goals and targets of the turnaround into individual incentive plans
Execution	**CEO-determined senior management** CEO hires and fires members of senior-management team, with board input	**Jointly determined senior management** CEO and board determine senior hierarchy, with board playing dominant role
	Strategy Board communicates intent and leaves management to execute	**Tactics** Board supports management in the "how" and not just the "what"
	Carrots and sticks Board sets incentives and communicates consequences	**Helping pull the cart** Board is available and present as an active thought partner to management (even if they don't ask for it)

Figure 2.3 *Private equity governance provides clear advantages during tough times.*
Source: McKinsey&Company

2.6 Turnaround Market in Italy

In Italy, this type of operation is still rarely used, because the link with debt capital and bank financing is too strong, although it is developing. There is still a lack of knowledge in this

[19] Kazimi, Tan (2016)

sector by entrepreneurs and institutions and only few of them fully understand the various possibilities it can offers and the differences with the use of debt capital. In the collective imagination, one of the main risk associated with private equity is that when one of these funds enters in the company, the entrepreneur loses control of the business. Actually, the entrepreneur remains the head of the business, but the fund intervenes and supports him in the decisions thanks to the great background and experience in its possession.

Obviously, the investor will have an important role in some crucial decisions as a new investor holding shares and very often will want to make changes to personnel, way of operating, business plan, but with the final goal of increasing the performance of company. The change wants to have positive effects.

Italian companies are mainly small and medium-sized family businesses, this characteristic has its advantages, but also its disadvantages. One of the risks is that the generational change does not lead to the expected results, due to incapacity to manage the company activity. While the fund, when it intervenes, does not worry about the family ties, but it thinks only to the improvement of the company and, if necessary, removes those who carry losses and not benefits. So, there is this difficulty by entrepreneurs in accepting risk capital and external partners, also due to the presence of an Italian entrepreneurial culture of closed property in contrast with other economies.

However, the other side of the coin has also to be considered: risk capital involves higher costs, tax legislation is complex, and the presence of an institutional investor changes the *modus operandi* of the company. The high costs also derive from the legislation, that does not encourage the development of the private equity market in Italy, even if the situation is improving and is harmonizing at the European level.

Considering the increasing value of the turnaround within private equity market, in 2010 the Private Equity Monitor created the Turnaround Monitor, a particular observatory that analyses investment operations aimed at company restructuring. The data collected by the Turnaround Monitor show, on one hand, that the turnaround segment represents a niche of the market (Figure 2.4), on the other hand, that the financial and industrial crisis has increased the situations of distress and, consequently, the market share of this segment.

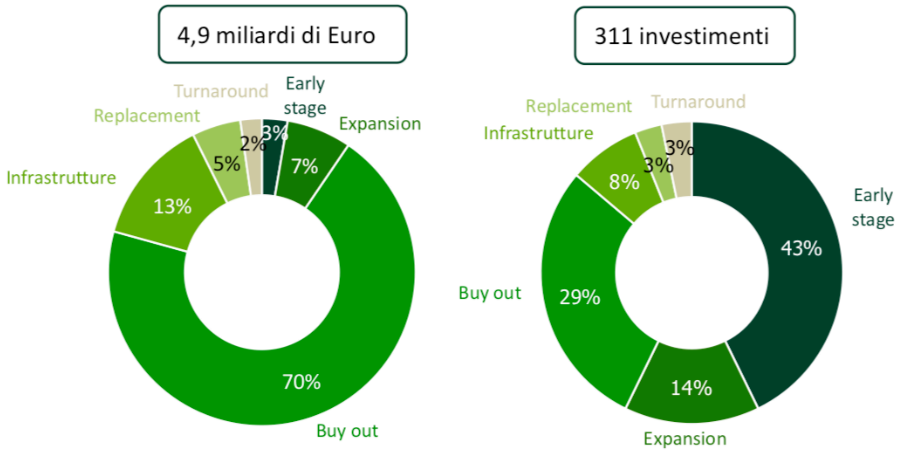


Figure 2.4 *Private Equity investments distribution 2017*
Source: AIFI 2018

Making a comparison between 2016 and 2017 we can see how the turnaround segment is growing with the realization of 10 investments in 2017, compared to 3 in 2016, while the monetary amount increased from 66 to 111 million Euro. (Figure 2.5)

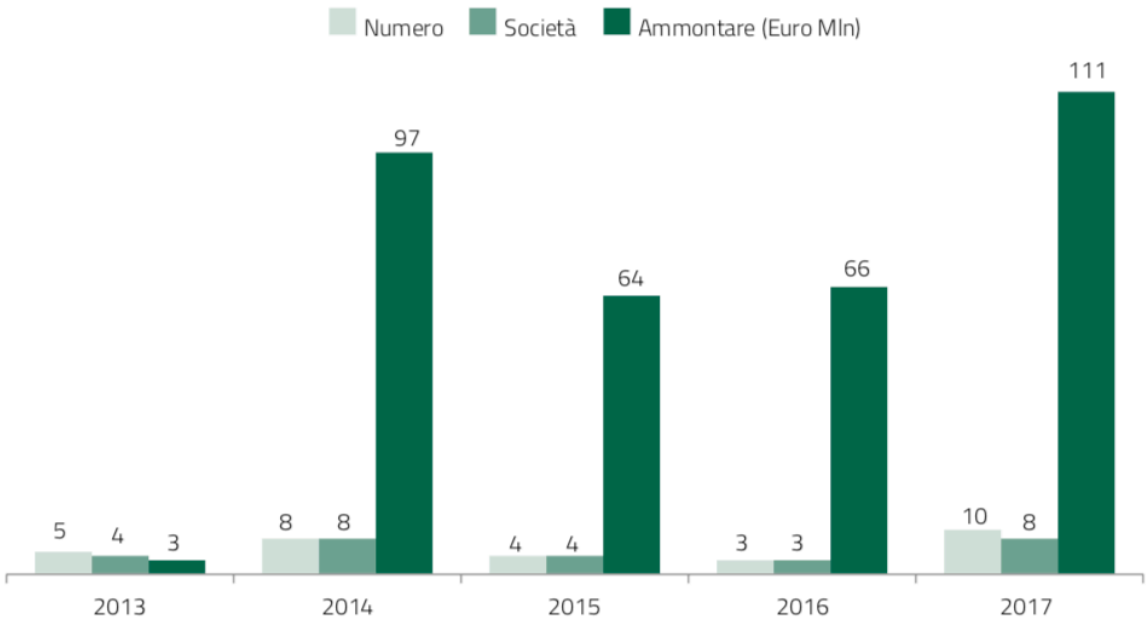


Figure 2.5 *Turnaround: historical trend (2013-2017)*
Source: AIFI 2018

Analysing the turnaround operators, we notice that only few specialized funds have operated in a continuous and systematic way on the market; in any case it is attributable to them a market leadership: in particular in Italy, among the major operators specialized in turnaround there are Atlantis Capital Special Situations and Orlando Italy. With regard to the remaining active operators, probably they operate using an opportunistic logic or they are general-purpose funds.

Focusing on their nationality, more than 70% of them are Italian funds, while the others are foreign funds. Concerning the geographical distribution, most of the market is concentrated in the North of Italy and the target companies belong mainly to industrial and consumer goods sectors[20].

Furthermore, operators prefer to choose companies characterized by the presence of a strong brand awareness and a highly recognizable brand. This shows a substantial difference compared to the other types of investment implemented by private equity funds, in fact there is a particular attention on intangibles by turnaround investors.

As highlighted before, today, turnaround is the less developed, but at the same time, the most promising sector of private equity thanks to the current economic situation, which offers many possibilities in this area. Companies that successfully come out of turnaround are often stronger in terms of management, operations and responsiveness to market conditions. Having been through massive change during the turnaround, they are better able to plan, manage and respond to changes in their business environment. In Italy, at the moment, we can observe very few cases of turnaround operations through private equity funds, so it is difficult to find information in the Italian economic literature, but also to collect empirical data about this kind of operations. The turnaround is, in any case, a developing sector on which it will be possible to acquire, with the time, more and more awareness, also taking into consideration what is happening abroad about this market.

[20] AIFI, 2018.

CHAPTER 3 – The Stefanel Crisis

3.1 Introduction

After having discussed in the previous chapters the causes and characteristics of a company in crisis and having highlighted the different procedures provided by Italian bankruptcy law applicable in such situations, in this chapter these concepts will be developed in a real case study about an Italian listed company, that has suffered on itself a real distressed situation: Stefanel Spa.

Stefanel, since its birth in 1959, has been considered one of the most valid Italian companies in the men's and women's clothing sector, becoming a symbol of Italian fashion and excellence.

It started from a local network and then developed, through an international vocation, a much wider network, establishing its presence in the main European fashion districts such as London, Berlin and Milan. In fact, its collections are distributed under the Stefanel brand through a consolidated shop network that boasts over 400 stores in more than 50 countries.

However, in recent years, the company has faced a very difficult period, due to a crisis that began in 2007/2008, at the same time as a global financial and economic crisis, and that struggles to recover, even today, despite the countless recovery attempts.

The purpose of this chapter is, initially, to briefly present the company from the points of view of history, corporate structure and governance, to give a complete view of the business we are dealing with, then to analyse the performance history of the company in the last seven years (from 2010 to 2017), identifying the symptoms and causes that led Stefanel to a serious financial instability, but also to lose market share in the relative sector.

The stages of the corporate crisis will be reviewed using the tools provided in the first chapter of this paper.

The 2007 was the year in which Stefanel recorded for the first time a significant loss in the balance sheet, the crisis then continued in a slow and insidious way, trying to be healed through countless increases in capital, sale of assets, continuous extensions with debtors and agreements (such as art. 67) with banks, until in 2017 when it was necessary the intervention of two Private Equity Funds, Attestor Capital LLP and Oxy Capital Italia S.r.l., to try to save the situation.

3.2 Group overview: structure and history

The history of the Stefanel Group began in 1959 in Italy, when Carlo Stefanel inaugurated the *Maglificio Piave* in Ponte di Piave, a small town in the Veneto region, starting a production activity in the knitwear sector.

Things changed in 1970, when his son Giuseppe took over the business and the innovations made since then represent a radical turning point in the company's history.

Giuseppe brings changes, especially in the commercial sector, by introducing a retail sale, strengthening the presence of the company on the domestic market and starting to think about an international development. In 1979 the family name became the brand representative of the company, encouraging the opening of first mono-brand stores, initially in Italy and then abroad, in Europe and the USA. Moreover, thanks to a series of acquisitions and strategic alliances, the business began to diversify, focusing not only on knitwear, but also on jeans and sportswear in general.

Figure 3.1 Stefanel Brand
Source: Stefanel official website

This expansion process is financed both by internal growth and by the decision to become public being quoted on the Italian Stock Exchange in 1987. In 1990, Stefanel acquired Interfashion, a business unit dedicated to the production and sale of clothing with licensed brands. In 2002, it completed the acquisition of 50% of the Nuance Group, an important international operator in the airport retail sector, with the aim to boost sales. In 2007, Interfashion began to sale clothes under the *HIGH* brand and concluded a license agreement with the famous Italian fashion designer Antonio Marras for the brand *I'm Isola Marras*.

Today the business operates through two different business units, both operating with a total look commercial proposal, which includes all the main types of clothing such as dresses, coats, trousers, skirts, shirts and sweaters.
Going into more detail, the first one takes care of the production and distribution of *Stefanel* clothing and accessories collections, whose products are characterized by quality and creativity, strong of a specific know-how resulting from the long tradition in the production and sale of knitwear. For this business unit, a process of repositioning has been underway for some years now, which aims to place the *Stefanel* brand in a higher segment of the market, the so-called "*accessible griffe*", which stands for quality designed clothes at accessible price, structured on the basis of the brand guarantee but with more calibrated price characteristics, recovering and revisiting those values that have distinguished it, such as the craftsmanship of the product and the image of Italian style.
While *Interfashion*, managed by Interfashion Spa, totally owned by the Group, is responsible for the production and international distribution of women's clothing with its own or licensed brands, is known for its consolidated experience in the jeans & casual sector of high positioning and for the know-how in the management of long-term business relationships with the best retailers at international level.
The Group's current strategy involves:
- The continuation of the repositioning project of the *Stefanel* brand, with the aim of having a distinctive offer, in particular knitwear, with an excellent price-quality ratio;
- The continuation of the development of the *HIGH* brand for the Interfashion business unit, with particular focus on foreign markets, also through a selected network of mono-brand stores managed directly or by third parties, as well as the development of the online channel.
After 59 years of history, the current group structure is composed by the holding Stefanel Spa and other subsidiary companies that mainly operate in the apparel fashion industry:

STRUTTURA DEL GRUPPO al 31 dicembre 2017

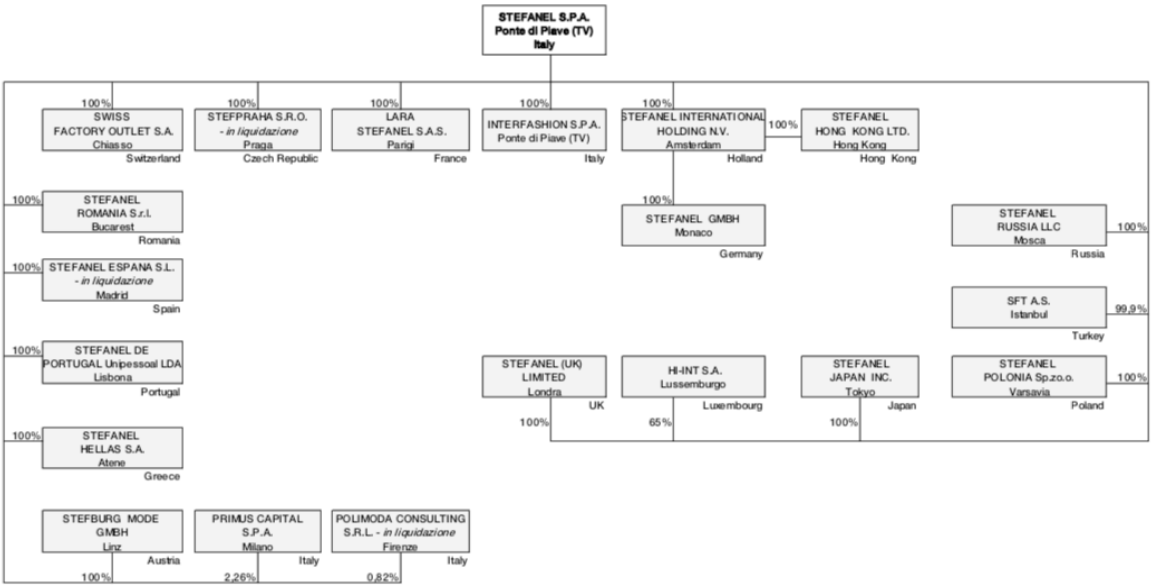
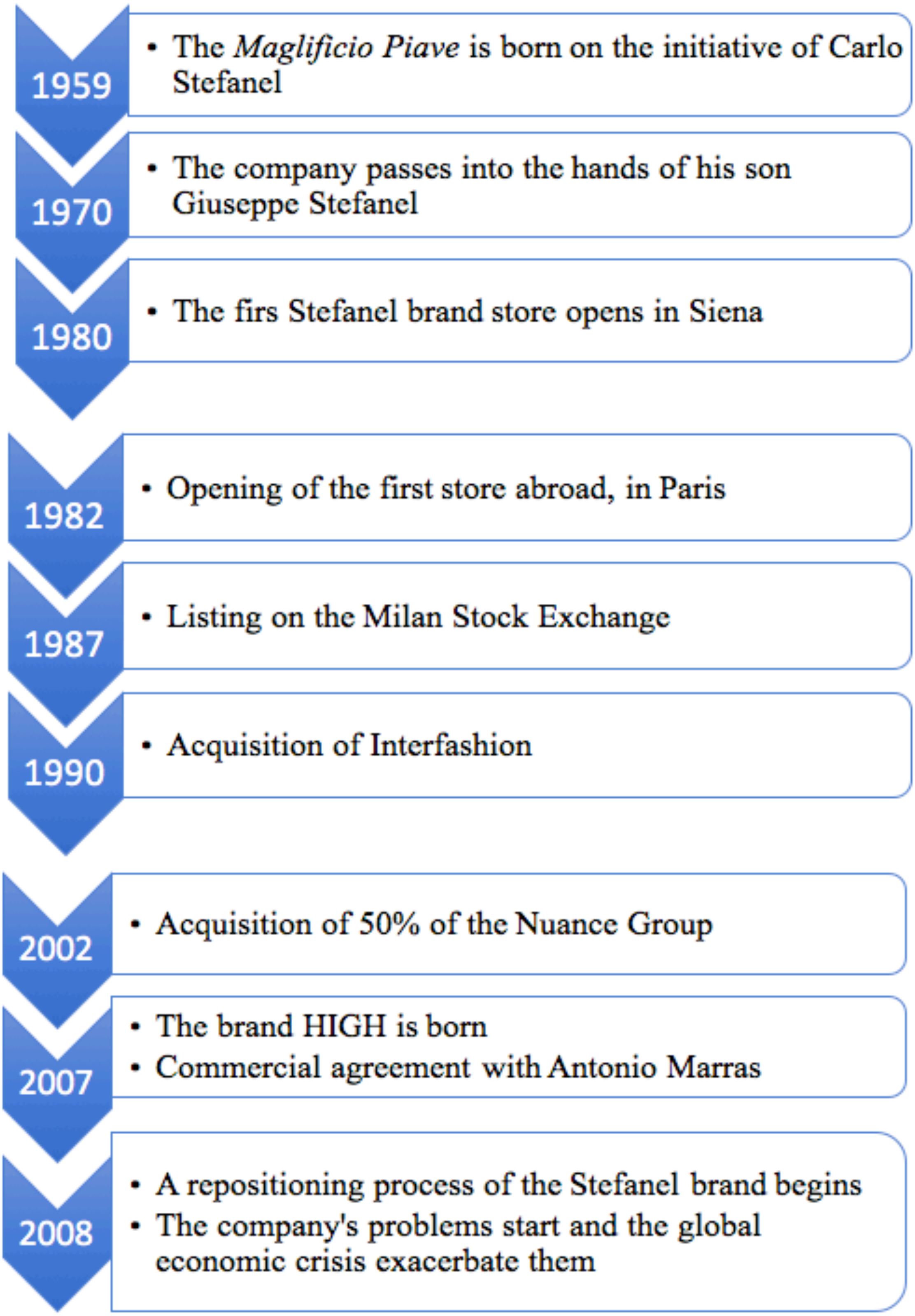


Figure 3.2 *Stefanel S.p.a. structure 31.12.2017* Source: Stefanel Consolidated Financial Statement 2017

Regarding the shareholder composition, following a capital increase operation on 21 December 2017, control of the Group passed from Mr. Giuseppe Stefanel to River Tre S.p.A., which in turn holds 71% of the share capital of Stefanel S.p.A. River Tre is directly controlled by Trinity Investments Designated Activity Company, a company managed by the Attestor Capital LLP fund.

The mission of the company is highlighted in the typical sentence of the company "*Fashion first. Italian always. Quality forever*." Stefanel has always tried to propose versatile collections in order to satisfy the evolving costumers' needs, but with a recognizable style and design and Italian quality.

Below are reported the main stages that have characterized the history of the Group:



Source: Personal elaboration

3.3 Historical economic and financial performance of Stefanel Group

The purpose of this paragraph is to analyse the performance of the group in the last 7 years, because this period has been characterized by the intensification of the financial crisis and by different attempts of the management to solve the crisis situation of the company through different strategic plans and restructuring agreements.

To introduce the period of analysis, we start from the early 2000s, when the company began to show the first symptoms of the crisis. Increasing competition from foreign countries, stagnant consumption and a low propensity to buy, which characterized the apparel sector in those years, have strongly compromised Stefanel's economic and financial balance.

The situation seems to have recovered in 2005, when a positive trend in revenues was recorded, deriving for more than 53% of the total from the Stefanel brand, and a profit of 6.0 million Euros after several years of losses.

In 2006, problems began to arise in terms of company margins, although at the end of the year a positive result of 1.1 million Euro was recorded, significantly lower than in the previous year.

In 2007, the company recorded a loss of 27 million Euros. This was, mainly, due to a large reduction in EBITDA, that reflected higher costs of the shop networks and higher investment in advertisement and promotion.

This preliminary period of the company crisis also coincides with the beginning of a global financial crisis and the consequent deep slowdown of consumptions in all over the world. Precisely for this reason, the already present problems of profitability were also followed by financial uncertainties about the availability of financial resources to implement the Group's strategic plan.

In the following years, Stefanel faced a situation of growing financial difficulty, with the consequent impossibility of respecting the financial covenants, provided in the existing financing agreements with various credit institutions, and renegotiation of the terms and conditions of the same.

The 2008 is the first accounting year entirely influenced by the global economic crisis and characterized by a negative result, and it is also the year in which Stefanel brand's repositioning strategy begins through greater communication, product development, a restyling of the sales network, and a more efficient organization of operating activities. The year ended with a loss of 20.8 million Euros and a contraction in sales, especially in the Italian market, which was particularly penalized by the slowdown in consumption.

Going through the last seven years, that is the period 2010-2017, the Group has obtained unsatisfying results from several perspectives. First of all, Group's total revenues have showed a diminishing path, mainly because of the effects of the global crisis, which has been responsible for a severe crunch in consumers' spending power, which consequently has diminished the level of consumptions. Furthermore, since the apparel and fashion industry is a mature market highly correlated to the GDP level, it has particularly suffered the negative effects of the crisis throughout all the last years. The decrease in revenues is attributable to the underperformances of both the *Stefanel BU* and the *Interfashion BU*.

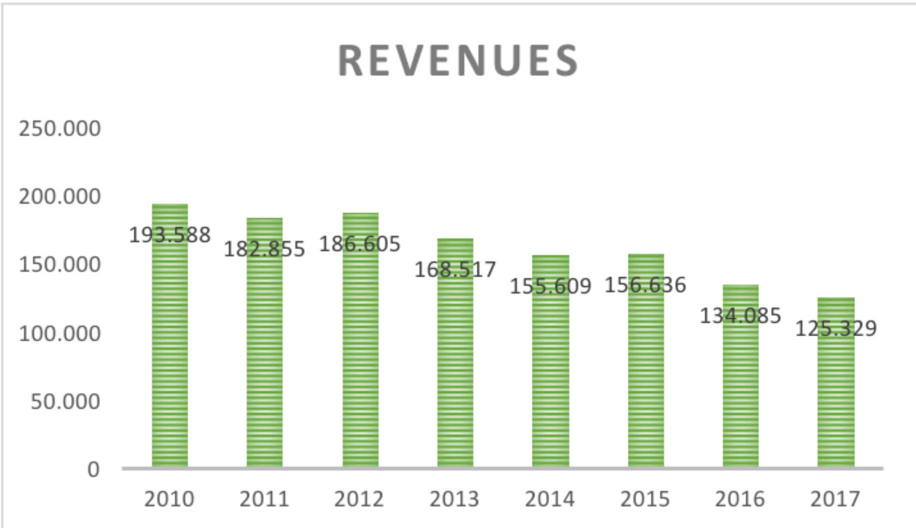


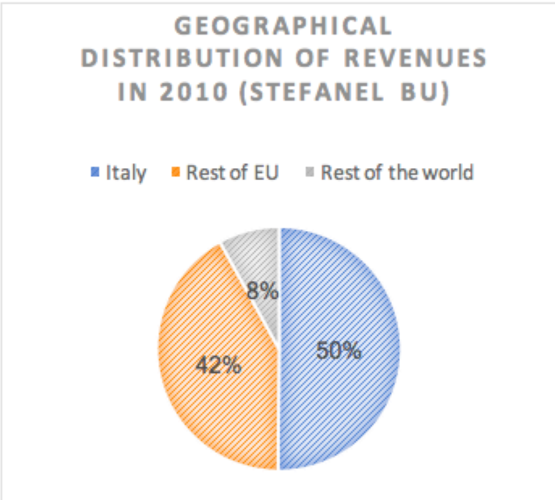
Figure 3.3 *Revenues Path 2010-2017* (thousand of Euros) Source: Stefanel Financial Statements

For what concerns the geographical distribution of revenues (Figure 3.4), in particular for the Stefanel business unit which is the most relevant for the Group, there has been an important trend during the last seven years: a decrease of the revenues realized in Italy, which was the primary market of the Group, and a slightly decrease of the sales collected in the rest of the world. Instead, the rest of Europe has become the most important market (Figure 3.5).

Geographical distribution of revenues Stefanel BU (million Euro)

	2010	2011	2012	2013	2014	2015	2016	2017
Italy	75,6	77,6	69,6	57,6	51,2	51,0	39,7	33,1
Rest of EU	63,1	71,6	75,8	71,9	67,8	69,4	58,3	56,6
Rest of the world	12,1	6,8	5,6	5,0	5,4	4,5	3,6	2,1
Total revenues	150,8	156,0	151,0	134,5	124,4	124,9	101,6	91,8

Figure 3.4 *Geographical Distribution of Revenues 2010-2017* Source: Stefanel Financial Statements



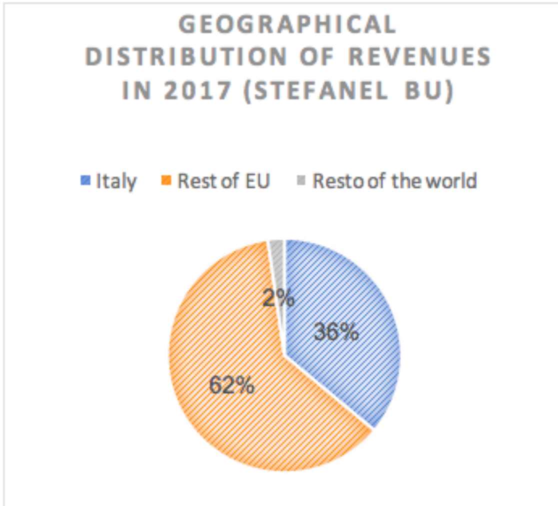


Figure 3.5 *Geographical revenue distribution in 2010 and 2017 (% of total revenues)*
Source: Stefanel Financial Statements

Analysing the evolution of EBITDA and EBIT (Figure 3.6), we can notice that from 2010 to 2014 the trend is opposite with respect to the one of revenues. In that period, the company reduced the cost structure and pushed down operational and advertisement costs to increase marginality and improve efficiency. While, from 2015 to 2017, both trends are decreasing and the operating margins are always negative, because revenues continue to diminish and costs cannot go down further, showing some relevant strategic and business model related inefficiencies.

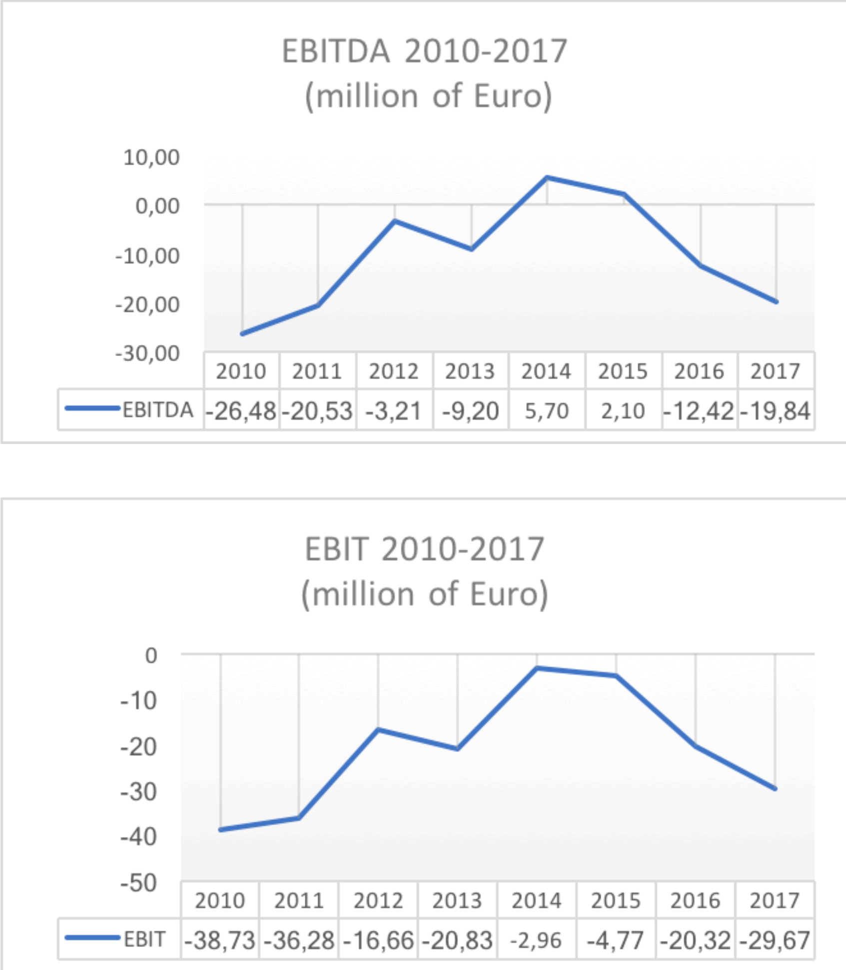


Figure 3.6 *EBITDA and EBIT 2010-2017* Source: Stefanel Financial Statements

The evolution of the Net Result (Figure 3.7) shows the fact that the worst performances were obtained in 2009-2010. In 2011, the performance became positive only thanks to a non-recurring operation: the sale of some assets considered no more strategic for the Group's operations, in fact Stefanel sold its 50% stake of equity investment in the Luxembourger company Noel International S.A., which owned the 100% of the Nuance Group, leader in the airport retail sector, the sale agreement included also the loan that Stefanel had previously granted to Noel International S.A. Without this non-operating transaction, Stefanel would have had another economic loss in 2011. For the subsequent years until 2016, the net result has always showed a negative sign, because the core operations were consuming, instead of generating, resources. In 2017, the net result is positive for 13,715 million of Euros, also thanks to the recording of non-recurring net financial income for 52,714 million of Euros, related to the accounting effects of the Restructuring Agreement that came into force in the same year.

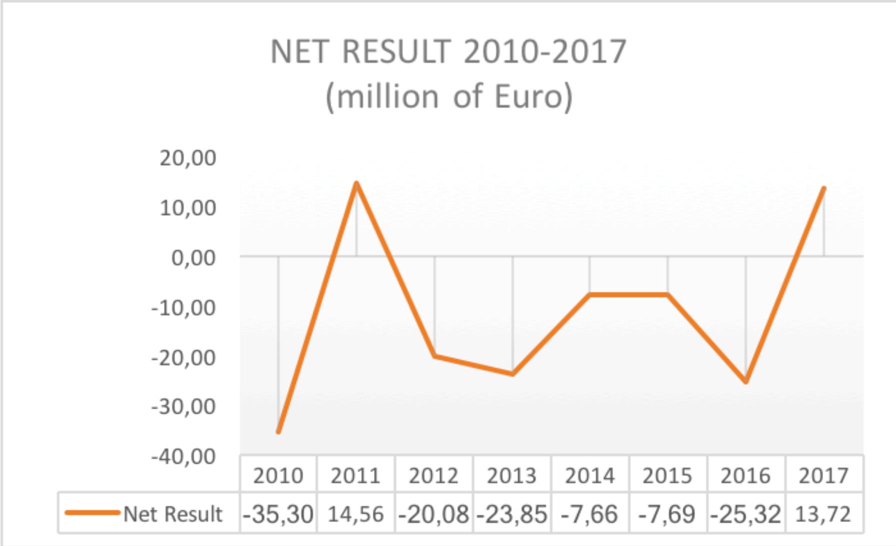


Figure 3.7 *Net result evolution 2010-2017* Source: Stefanel Financial Statements

In Figure 3.8, we can notice that the Net Financial Position has been considerably high through the last seven years, especially in comparison with the company's EBITDA, except for the 2011 during which there was the special sale of assets previously mentioned.

This analysis shows how, over the years, management has had to constantly seek out amounts and sources of financing or to enter into special agreements with banks to extend debt maturities. The situation is particularly serious in 2016, when the NFP is considerably high and equity is even negative. It was precisely in this context, that more specific and intensive actions were needed through the investment of two Private Equity Funds. At 31 December 2017, the Group's shareholders' equity was positive as a result of the capital increase, the issue of equity instruments and the positive result for the year. Consolidated net financial indebtedness is down sharply compared to 31 December 2016 for the effects deriving from the Restructuring Agreement corresponding to: 25 million Euros for the conversion of bank debt into capital and 23.8 million Euros for the disbursement of new financial resources.

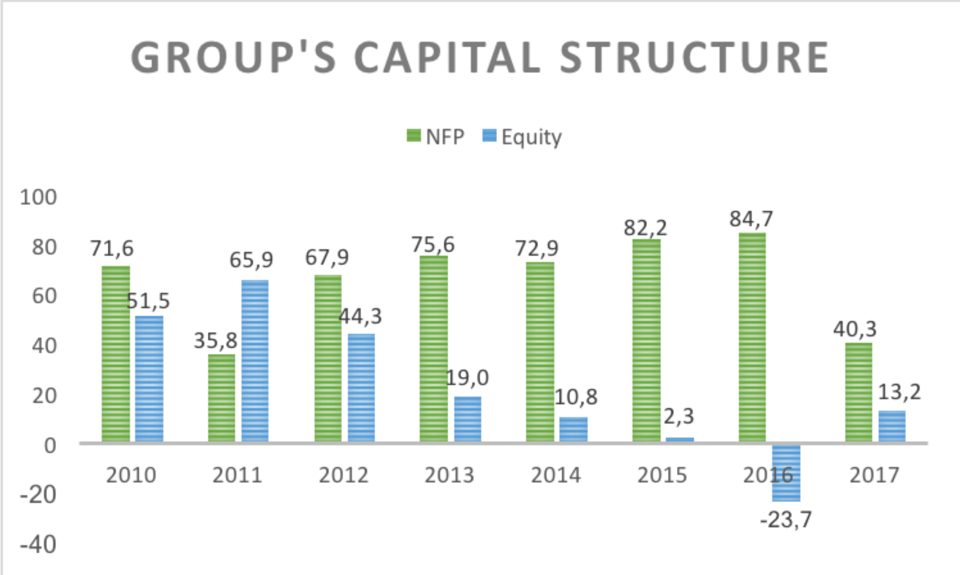


Figure 3.8 *Group's Capital Structure 2010-2017* Source: Stefanel Financial Statements

Now, the analysis moves to the coverage ratio, comparing the operating results in terms of EBITDA and EBIT with interest expenses that the firm has to cover due to the big amount of debt. As can be seen from Figure 3.9, negative operating results affect the coverage ratio EBITDA/financial interest, which is always negative, except in the years 2014 and 2015 when EBITDA is positive. This means that the company is creating less through its operating transactions than it would need to repay the cost of financing the core business itself. If this trend will continue in the coming years, the Group will continue to pay interest on its debt without having a positive effect on the creation of new resources.

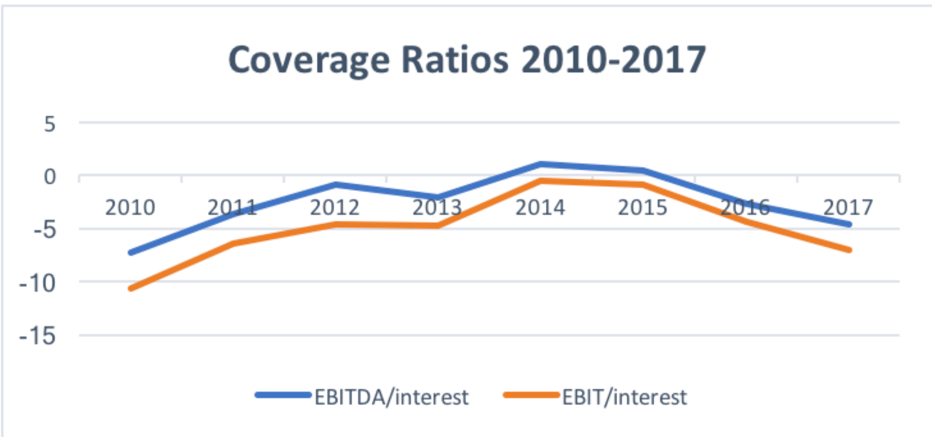


Figure 3.9 *Coverage Ratios 2010-2017* Source: Stefanel Financial Statements

Taking into account the balance sheet of the Stefanel Group, it is interesting to consider also which is the situation related to the liquidity and the leverage of the company.
Regarding the liquidity, it is appropriate to analyse the *quick ratio*, which compares current assets to current liabilities excluding inventories from the numerator. We can see that the quick ratio for the years 2010 to 2016 is much lower than the safe level of one, which means that the company did not have enough resources to repay its expiring debts within one year. This is why Stefanel has had to redefine the financing terms with the banks several times in the last 7 years. In 2017, however, this ratio grows above level one as a result of the Restructuring Agreement with Private Equity Funds.

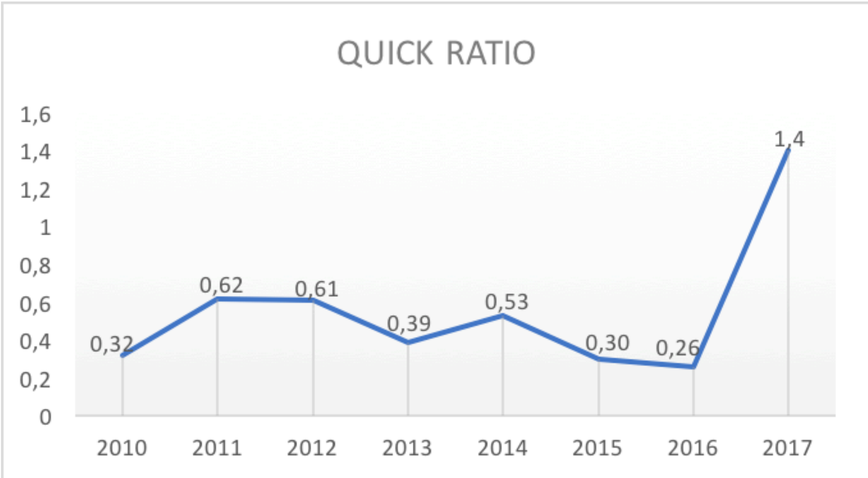


Figure 3.10 *Quick Ratio 2010-2017* Source: Stefanel Financial Statements

Looking at the leverage, the consolidated financial statements show that the problem is mainly related to debt maturities. Since the debt is mainly short-term, it is impossible for the company to repay it, which is the reason why, in recent years, it has been necessary to reschedule the maturity with a massive reduction in short-term debt and an increase in medium-term debt. There is also uncertainty from the point of view of the availability of financial resources, as banks are not inclined to grant long-term loans, because of the company's low creditworthiness due to the trend of recent years.
To sum up, in the period 2010-2017 the group's operations were considerably unprofitable, with net results more or less always negative, a very high level of debt, and an inability to generate value and repay the financing received from the banking system with the income from the core business. A little breathing space has only come with the 2017 Restructuring

Agreement, which facilitated the injection of liquidity and resources, but the results have not yet fully manifested and there is a risk that the company will still not be able to maintain a positive trend. Uncertainty about the company's performance and the difficulty in fulfilling its obligations have also affected the Stefanel share price in the stock market, which has fallen significantly in recent years.

Figure 3.11 *Evolution of Stefanel's share price in Euro from 01.01.2010 to 01.01.2018*
Source: Italian Stock Market

3.4 The context of the crisis: apparel and fashion industry

In order to have a more complete picture of the context in which Stefanel faced the corporate crisis and to better understand the causes, it is advisable to analyse not only the environment internally but also externally.

The reference sector is the one of apparel and fashion industry, and in this paragraph we will analyse the main characteristics that have served as a backdrop for fashion companies, like Stefanel, in recent years.

Italian fashion has not been able to avoid being the victim of the marked change in the purchasing behaviour of Italians, who have suffered from the crisis since 2009-2010. Companies were forced to find solutions in a very short time, to reduce costs as much as possible to maintain profit margins on products sold, to review product lines and distribution channels, but not all of them have had the possibility, but also the ability, to adapt or change their business model to seize the opportunities of these changes.

By comparing the price with the perceived quality, we can say that Stefanel in recent years has positioned itself in the medium segment of the industry. On one hand, its position is certainly higher than that of fast fashion brands, such as Zara, H&M, Mango, Pull&Bear, with which, however, Stefanel, like several other Italian players born from textile factories, has to deal because of the totally different logic: the new players in fast fashion not only offer much lower prices, but thanks to a combination of design factors, efficient production and supply, they also have a fresher and more contemporary style proposal, with collections that change continuously after few weeks at the expense of the "*six months of pret-à-porter*" and with a very clear value proposition. On the other hand, its position is lower than that of brands, such as Tommy Hilfiger, Lacoste, Diesel, Ralph Lauren, Calvin Klein. Stefanel in recent years has activated a repositioning process of the brand at a higher level, towards a logic of accessible luxury.

This level of market in the fashion industry is very challenging, first of all because there are other Italian brands with a clear positioning and a good product in the medium-high range, such as Twinset, Fabiana Filippi or Falconeri; then because the last few years have been characterized by a difficult economic situation and consequent marked competition, caused by a general decrease in sales for many companies and a change in average consumer preferences towards low cost clothing solutions.

In fact, the apparel sector is particularly sensitive to changes in consumer spending choices and macroeconomic variables and can consequently be influenced by the global economic context, interest rates, taxation, local economic conditions, uncertainty about future economic prospects and the shift in spending choices towards other goods and services.

Moreover, in the fashion sector the concept of brand is fundamental and it is not easy to change the idea that the market has of the company, especially in a difficult situation of indebtedness and it could take many years to complete the process of repositioning.

In order to better understand the apparel and fashion industry structure and in particular the medium sector, in which Stefanel is positioned, it might be useful to identify the main factors that operate inside them through the *Porter's five forces model* (Figure 3.12), a model that aims to assess the potential profitability of the company through the impact of five forces: degree of rivalry, threat of new entrants, threat of substitute products, buyer's power and the supplier's power. Each variable result to have a grade in a scale from 0 to 5, where 0 indicates a very weak or, in some cases, inexistent impact and 5 indicates a very strong impact.

The degree of rivalry among existing firms is high, due to the volatile and variable growth rate of the industry, the absence of high exit barriers, the absence of switching costs for costumers, the competition among them is quite relevant, even if it is also very important the brand recognition and the fidelity of costumers.
The threat of new entrants in this market is strong, because of the low entry barriers, the absence of switching costs and the different relationships that firms have with costumers.
The threat of substitute products is defined as medium, substitutes can be unbranded or lower quality clothes, the threat depends on the taste of each consumer and perception about price and quality, but the market offer is really wide for all kinds of taste.
The bargaining power of buyers is weak, because the switching costs are irrelevant, the volume per buyer is small, and the number and type of buyers is inestimable.
The bargaining power of suppliers is not high, because there is a really wide choice of suppliers, especially from emerging countries, such as the Far East, even if values such as sustainability and other ethical standpoints are becoming more and more relevant.

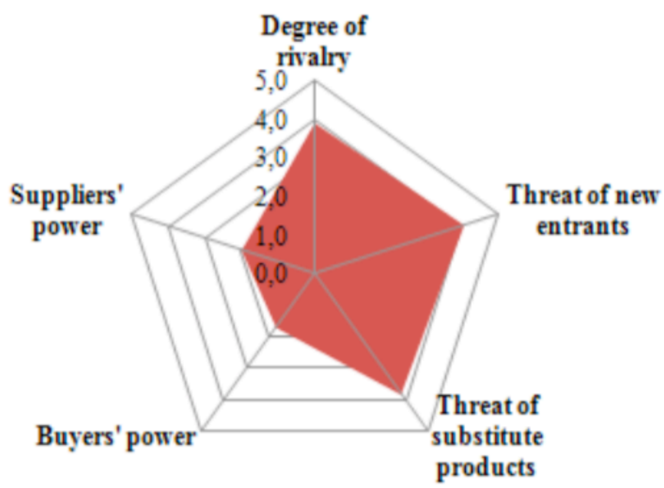


Figure 3.12 *Porter's Five Forces Model* Source: Personal elaboration

3.5 The determinants of the Stefanel crisis and the current situation

As highlighted in the previous paragraphs, the first signs of the crisis began to appear in the early 2000s and coincide with the beginning of a global crisis and the consequent slowdown in consumption in general, which immediately caused not only problems in profitability but also financial problems.

The Stefanel Group, which at the beginning of its history had a winning and innovative idea, that is to build a trendy and quality *Made in Italy* clothing style inspired by high fashion, then, over the years, had to face more and more the strong foreign competition.

The trend towards low-cost clothing solutions has brought competition to unprecedented levels, which are difficult to deal with, especially by companies in the medium segment such as Stefanel. Neither the business model nor the brand image have been able to keep the company's acquired market position.

The issue of image has proved to be one of the relevant causes of the crisis: Stefanel has tried to establish a competitive advantage based on differentiation, but it seems that consumers have not perceived the differentiating traits that the company has tried to spread and that there has been a real misinterpretation of the brand image, and also of the quality of products and design. The Group operates in a very competitive environment, and has shown to be very vulnerable in facing the challenges of the market, in particular:

- consolidation of retail distributors and competition for best retail store locations,
- outsourcing of production,
- new players in the market, because of low legal and entry barriers in general,
- seasonality of sales,
- inventory level, in fact the ability to predict the level of future demand is critical and heavily affect firms' margins and net result,
- brand reputation and consumers' perception (especially in Italy),
- potential problems with the undertaken optimization of the shop network,
- change of consumers' purchasing behaviour towards retail fast fashion and outlet centres,
- failure in the implementation of the repositioning strategy,
- low level of liquidity to exploit possible growth opportunities,
- great exposure to the fluctuation in the EUR/USD exchange rate (reflected in the purchasing cost of a great portion of purchased and contracted works)

The risks to which the Group has been and is most exposed can be identified at a strategic, market, operational and financial level.

Strategic risks include factors that influence the opportunities and threats related to the company's business, such as incorrect assessment of investments in new geographical areas or business segments or sales channels.
Market risks include the effects that changes in the market may have on the business of the various business units.
Operational risks are defined as possible adverse consequences linked to internal processes, organisation or systems and external events associated with the day-by-day management of corporate activities. Stefanel is subject to the risks associated with commercial development and the strengthening and repositioning of its brands. The company's performance also depends on its ability to offer products that meet consumer taste, this relates to the repositioning of the *Stefanel* brand, which entails a substantial change in the reference customers; while the *High* brand is still working to strengthen the market share achieved.
The expansion and growth strategy adopted in recent years has increased fixed operating costs, and has led to major investments in the shop network. Such investments expose the company to the risk that some chosen locations may prove to be unsuitable, due to demographic changes or other characteristics of the commercial areas, and also involve the risk of achieving significant operating losses. It is increasingly important to be able to organize and coordinate integrated production/logistics and commercial processes, in order to meet the needs of an increasingly complex commercial calendar.
On the other hand, financial risks include exchange rate, interest rate, liquidity and credit risks. With regard to exchange rate risk, the Group's assets, liabilities, sales, costs and operating result are and will continue to be affected by fluctuations in exchange rates on the prices of products sold, on the cost of goods sold and on the final result. The Group also holds assets and liabilities sensitive to interest rate fluctuations, which are necessary to manage liquidity and financial requirements.
In particular, as far as liquidity is concerned, the risk may arise from the inability to find the financial resources necessary for the normal course of business. The two main factors that influence liquidity are, on the one hand, the resources generated or absorbed by operating and investment activities and, on the other, the characteristics of the maturity and renewal of the debt or the liquidity of the financial investments. The requirements are monitored by the Parent Company's central functions, in order to ensure that financial resources are effectively obtained and that adequate amount of liquidity is invested.
Finally, the risks associated with the internalisation of activities and therefore political and economic instability in some countries in which the company operates must be considered.

To sum up, Stefanel is currently facing the risk that the strategic actions it is implementing to reposition its brand could fail, and that market demand will not respond positively to the communication campaign and production efforts. Moreover, the Group has to deal with the risk of not being able to find the financial resources necessary to cover the current shortage due to the difficulty of generating cash from the core business and to make investments.

The company should try to recover its strengths and the opportunities that the market offers. It should revitalize and enhance the concept of the Italian historic fashion brand, in order to implement the image of the brand and attract the attention of consumers; in fact, all over the world and especially for fashion, "*Italian*" is synonymous of style, quality, passion, sophistication.

Other important resources are specific know-how on the knitwear production and long-lasting relationships with key distributors of the sector. The company can certainly exploit the advantage of flexibility, thanks to the outsourcing of production, which allows it to change suppliers with great ease and to adapt more quickly to any changes in consumer and market preferences, but it has also to pay attention to the disadvantages that such a choice may involve in relation to dependence on contractors and the risks of a production system performed externally.

With regard to the possible opportunities to be exploited, could be more evaluated:

- online sales through e-commerce, very popular channel among consumers and object of the Group's new Business Plan,
- potential expansion in emerging markets (particularly inside the EU area),
- potential expansion in related segments, taking into account that the company operates mainly in the women's clothes and accessories segments,
- move towards the premium segment of the apparel fashion industry,
- work in partnership with other brands, considering the high fragmentation of the apparel and fashion industry,
- M&A transactions,
- find new business partners to consolidate the financial position.

The phenomenon of the business crisis is a physiological phase of the life cycle and of the production system. According to the Value Theory, the vitality of a company can be measured in terms of its ability to increase the value of its economic capital, if the propensity to grow slows down and then reverses, this means that the company is destroying value over time.

In this context, in the life of a company, the real underlying problem is to become aware of critical situations, in order to grasp the emergence of a crisis state. At the base of the actions to be taken in order to face situations of corporate crisis, there is obviously the identification of the triggering causes.
In addition to the growing complexity and dynamism of the markets, there is an increasingly strong correlation between internal causes and external phenomena.
A mix of these factors has been fatal for Stefanel, and also after several years the recovery is slow to manifest, making necessary in 2017 the intervention of external funds in a broader restructuring project.

CHAPTER 4 – The path towards the 2017 Restructuring Agreement

4.1 Introduction

After having analysed the causes of the crisis and reviewed the Company's performance in recent years, in this chapter the crisis will be revisited from the point of view of the procedures, provided by the Italian Bankruptcy Law, which have been put in place to restore the debt situation of the Stefanel Group.

As already highlighted, the state of economic distress was due to the impact of the global economic crisis and to some internal problems related to the competitive strategy and value proposition model. Another important fact is that the firm asked for a massive loan in an untimely historical moment, 2006, just before the break down of the world economic crisis. Furthermore, Stefanel has not revised in depth its competitive strategy or its model of doing business, thus during the years it was obliged to adopt some temporary solutions, which usually entail the sale of non-strategic assets or businesses, hoping for the general economic condition to re-establish. As consequence, the Group has shut down some of its subsidiaries because of unprofitability problems: this is what happened, for example, to Stefanel Espana S.L. and Stefanel Hungary Kft.

In a context of severe and persistent financial crisis, the Group was forced to face a situation of increasing difficulty, with the consequent impossibility of complying with the financial parameters provided for in the financing agreements that the Issuer has in place with the various credit institutions.

Precisely for this reason, from 2006 until today, the company has had to continuously review its business plan and re-establish conditions with its lenders, with the use of deferrals and recovery plans (art. 67 Italian Bankruptcy Law), during a very slow and insidious crisis process.

The final aim of this chapter is to clarify and explain Stefanel's path to the current Restructuring Agreement of 2017, which involved the two Private Equity Funds: *Attestor Capital LLP* and *Oxy Capital S.r.l.*

4.2 The first Amending Agreement 2008 and the Business Plan 2008-2010

In 2006, the management team took some questionable decisions with regard to the amounts and sources of financing. In particular, Stefanel asked for and obtained from several credit institutions a medium-term loan of 150 million Euros, that pushed up the net financial indebtedness: unfortunately, this choice was made at an inappropriate time. In fact, once the company was hit by the economic crisis and suffered significant losses, its capital structure stretched out towards debt capital and led the company to bear additional costs, with consequent erosion of equity.

Starting in 2007, the Stefanel Group embarked on a difficult path, characterised by negative results and a progressive reduction in EBITDA, with the consequent growing difficulty in complying with the scheduling of payments and the duty to sell its assets in order to reduce the amount of debt capital.

That year, despite having benefited from significant capital gains from the sale of some stores, the Parent Company recorded a significant operating loss, which resulted in the failure to meet the financial covenants set out in the medium-term pool loan agreement for an original amount of 150 million Euros.

The failure to comply with the financial parameters, set out in the syndicated loan, gives rise to subsequent renegotiations of its terms and conditions, which entail the release by the banks, involved in that Agreement, of several *Waivers*, containing their renounce to take advantage of the remedies provided by the syndicated loan, in the event of non-compliance with the financial parameters.

In particular, on 20 March 2008, the so-called *Amending Agreement* was stipulated with the banks of the syndicated loan, and through it new financial parameters were defined and with the aim to be verified on the basis of the indicators relating to the periods ended 31st December 2008, 30 June 2009 and 31st December 2009. This Agreement was drawn up taking into account the Business Plan for the years 2008-2010, which the Group approved on 14th February 2008.

The 2008-2010 Business Plan was essentially aimed at returning to profitability through the pursuit of well-defined strategic objectives. In particular, with regard to the Stefanel business unit, the decision was confirmed to reposition the Stefanel brand upwards through greater communication and product requalification, to carry out a restyling of the current sales network and to organise operating activities more efficiently together with greater training for sales personnel.

More specifically, the Plan stated the necessity of improving Stefanel business unit's profitability through the combined effect of the following actions:

- increase in revenues with respect to the same number of employees and stores;
- reduction of the incidence of costs related to fixed assets and retail network as well as a review of the procedures of products emission into the market;
- increase of the communication efforts which have to enhance the importance and visibility of the brand;
- ideation and roll out of a new format and layout for stores in line with the new image of the brand;
- investments in new collections, in particular with the identification of new designers and stylists which have to meet the new strategic goals.

The main objective for the Interfashion business unit, on the other hand, is to focus at this time on the development of the new *HIGH* brand and the license for the *I'm Isola Marras* brand.

The Stefanel's Board of Directors expected that all the Plan's illustrated processes would have taken four years to be carried out.

The 2008 financial year, however, did not bring the expected improvements; in fact, it closed with a loss and also with a contraction in sales due to the decrease in sales in Italy. As a result of these economic and financial performances, the financial covenants provided in the above-mentioned medium/long-term loan agreement with *Banca Antonveneta*, *Banca Intesa San Paolo*, *Unicredit Banca d'Impresa* and expiring on 30 June 2013 are not satisfied.

In the same year, Stefanel started a recapitalization process which ended in July: 108,367,086 newly issued ordinary shares were offered to the owners of ordinary and savings shares according to a ratio of 2 newly issued ordinary shares for 1 ordinary or savings share owned and at a price of 0.369 Euro each for total proceeds equaling almost 40 million Euros. The capital increase was entirely underwritten and the proceeds were used to reduce Stefanel's financial exposure, in accordance with the terms agreed with banks on 20/03/2008, and to finance the strategic actions planned in the Business Plan 2008-2010.

However, due to the Company's negative performance, management was forced to ask Borsa Italiana to exclude Stefanel shares from the STAR segment of the Milan Stock Exchange and transfer them to the Standard Class 1 segment of the MTA.[21]

4.3 The First Restructuring Agreement (2010)

The 2009 ended with a loss, also influenced by the difficult general market conditions caused by the international economic crisis and the negative repercussions on consumption in the clothing sector. All these reasons caused even greater financial tension and a negative evolution of the debt/EBITDA ratio, well beyond the "*attention threshold*".

After this further deterioration in the Group's results, on 25th March 2009, the Company obtained a new *Waiver* from the lending banks, with the stipulation of a new *Amending Agreement*, aimed at the exemption to the application of the obligations and consequences deriving from the non-compliance with the financial parameters to be respected within the 2008 financial year. Within the framework of this Agreement, the forecasts of the pool financing, concerning the definition of new financial parameters for the financial year 2009, are further modified.

As a prerequisite for the release of the *Waiver 2009*, it is expected that extraordinary transactions will be carried out, expiring on 30 June 2010, for example the sale of companies included in the Group, with the aim of raising additional financial resources, or an equity injection of proceeds corresponding to an amount not less than 40 million Euros.

As a consequence of this assumption, in August 2009, the Company decided to sell 100 % of its subsidiary Hallhuber GmbH, a German clothing retailer firm operating in Germany, Austria and Holland through almost 100 stores. It was a profitable company and Stefanel sold it just because of an immediate need for liquidity.

In order to pursue the established strategy, reductions in operating costs needed to be undertaken, and the related activities included: a significant reduction in the workforce, the closure of the Salgreda (TV) production site and the relocation of the related production lines to the Company's headquarters in Ponte di Piave (TV), the restructuring of the foreign sales network with the closure of non-profit sales outlets, and finally the centralization of

[21] MTA stands for *Mercato Telematico Azionario* and it is the Electronic Stock Market. The difference between *Standard* and *Star* derives from the fact that in the *Star* segment, securities with high requirements and belonging to small and medium sized companies with good prospects are traded, they must meet additional requirements compared to those required for admission to the *Standard* and meet particular commitments in terms of liquidity, transparency and corporate governance.

administrative services at the Ponte di Piave site, with the consequent elimination of the related functions at the Group's peripheral offices.

Furthermore, on 29th December 2009 Stefanel reached a *Standstill Agreemen*t with all the banks, valid until 15 February 2010: this agreement provided for the commitment of the banks to keep the current credit lines available and not to request the residual principal payment of the loans.

During the same year, the Group's Board of Directors approved a three-year Business Plan for the period 2010-2012, despite the fact that it identified some strategies and actions partially similar to those considered in the 2008-2010 Plan. Compared to the latter, the new Plan took into account the changed economic scenario and conditions around the Group and also implemented some differences in terms of restructuring and rationalization of activities to bring the Group back to positive operating results:

- increase in advertising costs up to a level of 8-9% of total sales with the aim of implementing the brand image;
- make significant investments to modernize mono-brand stores, always with the aim of increasing the image of the brand;
- focusing on KVDs for stores' results, investing mainly in personnel training
- rationalize the distribution network with focus on core geographical markets and close or sale non-performing stores in Italy and abroad.

Subsequently, in 2010, although there was a slight improvement, the achieved operating result showed that the Company still needed strong actions before reaching the recovery objective and a sustainable situation. During the year in question, the events of April were particularly significant. On 26th April, in fact, the first Debt Restructuring Agreement between the Company and the financing banks was finalized and took effect.

The main purpose of this Agreement was to partially amend the terms and conditions of the existing financing structure, including the rescheduling of certain instalments of medium/long-term financing that were expiring. The Restructuring Agreement, supported by the Business Plan for the period 2010-2012 and valid until 31st December 2012, included:

- Suspension of payment of the principal amount of medium/long-term loans, including the initial loan of 150 million Euros;
- Confirmation of the main credit lines;
- Equity injection for 50 million Euros;

- Commitment of shareholders, in particular the principal shareholders Giuseppe and Giovanna Stefanel, and Bestinver Gestiòn SGIIC SA (a private owned investment manager), to subscrive their respective shares of equity injection;
- A series of resolving clauses in the presence of which the termination of any original medium/long-term loan contract and of the Restructuring Agreement itself may occur. These conditions include the failure to meet the deadlines set by specific financial parameters, with a variable margin of variance: consolidated shareholders' equity which, from 31 December 2010, must not be less than 50.873 thousand Euros, the ratio NFP/EBITDA, half-yearly EBITDA and the ratio of consolidated net financial debt to consolidated shareholders' equity which, as from 31st December 2010, must not exceed 2.69.

Subsequently, on 28th April, the negative result recorded by the Parent Company, together with the losses of previous years, determined the recurrence of the conditions set out in art. 2446 of the Italian Civil Code concerning capital reductions for losses.
The extraordinary shareholders' meeting of the Group covered the loss by using all available reserves and reducing the share capital. Thus, in June, as required by the Agreement, the capital increase was resolved by issuing 81,275,275 new ordinary shares, offered to the owners of ordinary and savings shares according to a ratio of 25 newly issued ordinary shares for 1 ordinary or savings share owned and at a price of 0.615 Euro each, for a total maximum amount of almost 50 million Euros. The 99.05 % of the total offered shares were underwritten, and the 70.5% were directly or indirectly underwritten by Giuseppe Stefanel and Bestinver Gestiòn SGIIC SA.

4.4 The Second Restructuring Agreement (2011)

The 2011 was characterised by a positive result, due to the sale on 17th February 2011 of its 50% stake in the company *Noel International SA*, which in turn owned the 100% of the Nuance Group, for a total price of 130 million Euros, among which 85.5 million Euros were used to repay the Company's debts. Without the capital gain and the proceeds of this operation, Stefanel would have closed again with a loss.
As a result of the sale, on 23rd June a new Debt Restructuring Agreement was finalised between the Company and the lending banks: this Agreement included stringent clauses to be verified every six months on compliance with the financial statement parameters; in particular, once again the focus was on the values of consolidated shareholders' equity,

consolidated net financial indebtedness, consolidated EBITDA, and the ratio of consolidated net financial indebtedness to consolidated shareholders' equity. The 2011 Debts Restructuring Agreement entailed these conditions:

- Early repayment of some medium and long–term loans through the use of part of resources coming from the sale of *Noel International SA* for a total amount of 85.5 million Euros;
- Banks' commitment to provide to the Group a further line of credit for 12 million Euros, given the observance of the established covenants;
- Suspension until 2014 of the repayment of the principal amount on the remaining medium and long – term loans with subsequent amortization;
- Confirmation of the main lines of credit until 31.12.2013.

The definition of this Agreement took place after the presentation to the financing banks in March of the new industrial and financial Plan valid for the years 2011-2015, which became necessary because of the sale of the stake equity in the Nuance Group, not contemplated in the previous industrial Plan 2010-2012 and including the same strategies and related actions of the previous Business Plan, except for advertising costs, which were reduced because rather unsustainable to maintain considering the financial conditions of the Group.

4.5 The third Restructuring Agreement (2014)

In recent years, with both divestments and capital injections, Stefanel has received resources for 160 million Euros, net of 90 million for debt repayment. However, this liquidity has not healed the accounts and, although the first weak effects of the restructuring policy were beginning to be seen in that period, the years 2012 and 2013 have not been without problems.
Although EBITDA and EBIT showed an improving trend in 2012, the new implemented strategies were not delivering the expected effects.
The 2013 financial statements closed with a negative net result, despite the fact that the accounts were beginning to improve, even if not yet enough to bring the accounts back to profit. But more than the line of profit that still indicates suffering, the most worrying figure was the consolidated net revenues, that continue to fall while the consolidated net financial debt was not falling.

The losses were again covered by decreasing the company's share capital and it was necessary to close some non-strategic stores and sale unprofitable assets. In addition, the covenants provided for in the New Agreement were not respected on 30 June 2013, with the consequent loss of the benefit of the term on the medium/long-term loans in place, in addition to the accrual by the banks of the right to revoke the operating credit lines, expiring on 31 December 2013, and to limit the use of the funds available to the Group.

Both in 2012 and 2013, Stefanel again was obliged to apply the resolutions provided for in article 2446 of the Italian Civil Code, covering the losses as already done for 2010.

Another important event was the resignation of Luciano Santel on 12 September 2013 from the position of Chief Executive Officer and General Manager of Stefanel. The previous Geox manager, hired in 2009 with the specific task of restructuring the company, left Stefanel because he was called by the luxury brand Moncler for a new career path. At his place on the Board of Directors Federico Girotto was co-opted, he was the corporate vice-president and manager responsible for preparing the company's financial reports. The Board of Directors also resolved to set up an Executive Committee, assigning it the task of strategic direction, composed of Giuseppe Stefanel and the directors Roberto Chemello and Federico Girotto.

In 2014 EBITDA and EBIT started to improve, on the basis of this positive trend there was an improving performance with an increase in the gross margin percentage and a significant decrease in fixed costs.

However, the composition of debt was still very unbalanced, showing a clear prevalence of short-medium term debt over long-term debt with the certainty for the Company of not being able to meet its obligations (Figure 4.1).

Details of short, medium and long-term borrowings (data in million Euro)			
Financial Institute	**2014**	**1 Year < Due date < 5 Years**	**Due date > 5 Years**
Pool (*) Tranche A	24,2	20,8	3,4
Pool (*) Tranche B	6,2	5,4	0,9
Pool (*) Tranche C	4,7	4,0	0,6
Banca Popolare di Verona	0,5	0,5	0,0
Mediocredito del Friuli Venezia Giulia	3,7	3,2	0,5
Monte dei Paschi Antonveneta	2,8	2,4	0,4
Monte dei Paschi di Siena	0,8	0,7	0,1
BNP BNL	1,2	1,0	0,2
Unicredit	2,7	2,4	0,4
Intesa Cassa di Risparmio del Veneto	2,7	2,4	0,4
Intesa Cassa di Risparmio di Venezia	0,8	0,7	0,1
EFI Banca	0,7	0,6	0,1
Total	**51,0**	**44,1**	**7,1**

(*) Banca MPS Spa, Cassa di Risparmio del Veneto Spa, Cassa di Risparmio di Venezia Spa, Unicredit Corporate Banking Spa, Efibanca e Banca Nazionale del Lavoro

Figure 4.1 *Details of short, medium and long-term borrowings*

Source: Stefanel consolidated financial statement 2014

In order to better understand the proportion of debt financing, we can analyse the evolution of some ratios which measure the ability of the Firm to cover the debt expenses (Figure 4.2). The NFP/Equity takes into account the proportion between debt financing and equity financing. Until this moment, it has always been increasing, next to 7 times the equity capital in 2014. The NFP/EBITDA indicates how much debt the company has contracted with respect to the earnings and it is meaningful to understand the financial instability of the Group. The EBIT/Interest Expenses explains how many times the Firm is able to cover the interest expenses on debt through the operating income. From 2008 to 2014 this ratio is negative, implying that the Company has not been able to sustain those payments with the earnings from the core business.

LONG-TERM SOLVENCY RATIOS

	NFP/Equity	NFP/EBITDA	EBIT/Interest Expenses
2008	1,6	73,4	(1,1)
2009	3,7	(4,1)	(7,9)
2010	1,2	(2,3)	(6,6)
2011	0,7	(2,2)	(8,7)
2012	1,7	(23,6)	(4,7)
2013	4,4	(9,1)	(6,4)
2014	7,2	13,5	(0,6)

Figure 4.2 *Long-term Solvency Ratios*

Source: Stefanel Financial Statements

On 10 June 2014, after 12 months of negotiation, the Group signed a new Debt Restructuring Agreement with the lending banks, replacing the previous one finalized in June 2011.

The 2014 agreement expired on 31st December 2017 and set out the main conditions:

- the moratorium until 30 June 2016 on the repayment of principal medium/long-term loans, with subsequent amortization from December 2016;
- confirmation of the operating lines of finance used at 30 September 2013 until 31 December 2017;
- verification of compliance with certain financial parameters at the level of the consolidated financial statements on a half-yearly basis.

On the basis of the above-mentioned Restructuring Agreement, a new industrial and financial Plan for the Company for the period 2013-2017 had also been drawn up, as certified by article 67 of the Italian Civil Code and with the hope that it would finally have brought the Group back to a more stable economic and financial situation.

The strategy implemented in the Business Plan 2013-2017 presented the following main lines of action in order to compete in the premium segment:

At the company level:

- increase revenues and exploit the potential e-commerce
- develop the shop network both directly managed and franchising mono-brand stores, with focus on most remunerative and profitable geographical markets
- improve EBITDA through better sourcing and initial mark-up policies

At the business units level:

- Stefanel BU: continue the market repositioning of brand towards a higher segment through a unique product offering. Implement the product and promotion levers through the strengthening of the design, the rationalization of advertising and promotion expenses, the refurbishment of retail stores.
- Interfashion BU: further develop the HIGH brand with a particular focus on foreign market, also through a selected network of mono-brand shops.

With this plan, the Group was expecting to achieve positive EBITDA and operating cash flows in the following years, earn a positive net result from 2016, decrease the net financial position from 2016, get access to new sources of financing.

According to the consolidated financial statements at the end of 2014, it is true that EBITDA turned positive after years of negative numbers, but operating cash flows, even if they were increasing, did not meet the expectations. However, the Group's core business started producing cash and not burning resources.

The main problem of the Group was that revenues showed few signs of possible recovery.

In 2014, in fact, the external environment was still very much influenced by the consequences of the economic and financial crisis, such as the increase in unemployment and the reduction in the disposable income of consumers, which caused a slowdown in consumption.

This still very unstable situation in the economic environment was accompanied by a change in the purchasing habits of consumers, attracted by retail fast fashion chains and outlet centres. All this was identified by the management as the cause of revenue reduction.

The Group seemed to be at the beginning of a long phase of recovery for the return to normality, but there were still concerns due to the lack of liquidity, so it was forced to plan again the sale of some retail stores, for example in Dusseldorf.

4.6 The New Restructuring Agreement (2017)

The 2015 results were generally not in contrast with the improvement trend exhibited in 2014, but still below expectations, also due to the perseverance of the economic downturn, with the apparel and fashion market that has showed slightly improvements.

In addition, the Group was forced to reduce its share capital again to cover the 2014 net loss and the existing negative reserves.

On 16th March 2016, the Board of Directors was involved in:

- Revisiting the terms and conditions of the 2014 Debt Restructuring Agreement, because on 31.12.2015 the Firm breached some of the financial covenants stated in the Agreement and the non-fulfilment implied the risk of losing the benefit of the term on medium and long-term loans;
- Contract a period, at least until 31.12.2016, of Standstill Agreement with creditors;
- Evaluating and planning the possible operations for the strengthening and balancing of Group's capital structure;
- Drafting the new Business Plan 2016-2019, keeping the general lines of the previous one and expecting positive EBITDA and operating cash flows in 2016 e 2017, positive net results from 2018. However, there is still a high degree of uncertainty about the assumptions made in the Plan due to the trend in revenues, operating margins and cash flows, the reaction of the market to the implementation of the brand, the evolution of the EUR/USD interest rate.

The Stefanel Group instructed the financial advisor *Rothschild S.p.A*. to look for possible partners and investors in the market, because its financial structure was totally dependent on banks and the Company needed liquidity and investments to fund planned actions.

Nevertheless, the financial institutions owning the majority of Stefanel's debt have always guaranteed the support necessary for the going concern of economic operations, even in situations of non-compliance with the financial covenants and commitments set out in the Restructuring Agreements. This behaviour of credit institutions has been fundamental in all these years for the survival of the Company.

It is precisely in this period that the interest of Private Equity Funds towards the Company was born, in order to start a more structured turnaround operation.

This seems to be the last possible solution to give a strong input to the business trend, since the Group has already sold all the assets considered non-strategic and closed every store not profitable. After this slow and insidious crisis, the Company recognizes that it has reached a point of no return in its life cycle, so at this time any action, even if risky, is worth trying to save the business.

The difficult market conditions, caused by the economic crisis, and the negative repercussions, that have heavily affected consumption in the clothing sector, have contributed to significant operating losses, that have also directly affected the Parent Company. On 2nd November 2016, these circumstances led the Board of Directors to submit the application for admission to *Composition with Creditors*[22], so called "*blank*", in order to obtain the protective effects of the Parent Company's assets provided for by the applicable regulations for the protection of all the interests involved and as part of a broader process of strengthening the Group's capital and financial position.

Subsequently, on 31st July 2017, the Parent Company filed an appeal with the Court of Treviso for approval of a Debt Restructuring Agreement, together with the report prepared by the appointed professional, which certifies the truthfulness of the Company's data at 31st December 2016 and the feasibility of the Restructuring Agreement, also with reference to its ability to ensure full payment of foreign creditors. On 3rd August 2017, this Agreement has been published in the Companies Register.

This Restructuring Agreement, approved on 11th October 2017 by the Court of Treviso, was reached following the Framework Agreement signed on 23rd March 2017 with the funds *Attestor Capital LLP* and *Oxy Capital Srl*, which made it possible to define with the banks and the main creditors of the Parent Company an agreement for the Group's capital and financial restructuring in preparation for its relaunch over a period of 5 years.

On 21st July 2017, the Parent Company accepted and signed the final Agreement aimed at restructuring the debt and strengthening the capital and financial position of the Company and the Group.

On 28th July 2017, with the signing of the Agreement also by *Banca Mediocredito del Friuli Venezia Giulia Spa*, which, for operational reasons only, was unable to sign on 21st July, the 2017 Restructuring Agreement was finalised.

The Agreement includes the following main conditions:

[22] Article 161 Italian Bankruptcy Law.

1

- The disbursment of the *New Plan Finance* for a total amount equal to 23,763 thousand of Euros, respectively for 11,250 thousand of Euros from River Tre, for 11,263 thousand of Euros by some banks and for 1,250 thousand of Euros by Giuseppe Stefanel; used by the Company to reimburse the *New Emergency Finance* and with the remainder to support the implementation of the 2016-2022 Business Plan.

2

- The repayment of the *New Emergency Finance* amounting to 10,000 thousand of Euros, disbursed on 13rd April 2017, following the authorisation by the Court of Treviso to contract a pre-deductible loan, according to Article 111 of Bankruptcy Law, and related interest expense of 630 thousand of Euros, through the use of the proceeds from the disbursment of the *New Plan Finance*.

3

- The transfer without recourse by the main creditor banks, the so-called *Consolidated Debt Banks* of the Company, to a newly incorporated company; *River Tre S.p.a.*, 100% owned by the Investors, of 25,000 thousand of Euros of the credit claimed by themselves towards the Company, which was used to approve the capital increase for 10,000 thousand of Euros and the issue of equity financial instruments for 15,000 thousand of Euros.

4

- The consolidation and rescheduling by the *Consolidated Debt Banks* for an amount of 67,254 thousand of Euros - in terms of principal and interest - until the reference date of 2nd November 2017, plus the related interest amounts, accrued up to 21st December 2017, not paid and calculated in accordance with the provisions of the Agreement. A fixed rate of 1% will be applied to consolidated indebtedness starting from 21st December 2017. The full repayment of the consolidated indebtedness will take place in the form of *bullet* and must be carried out by 31st December 2022 as expiry date.

5

- The write-off of the debt towards the factoring company and of the trade payables subject to specific remission agreements for 4,791 thousand of Euros and 10,830 thousand of Euros respectively, and the rescheduling of the remaining part on the basis of specific agreements. They were subject to the approval of the Restructuring Agreement 2017. Repayment in full of the debt towards the factoring company and of the trade payables will be in place by 2025.

6

- The rescheduling of mortgage debt for 3,846 thousand of Euros, increased by the related interest accrued up to 21st December 2017 and calculated in accordance with the terms of the Agreement. On mortgage indebtedness will accrue interest at a fixed rate of 1% from 21st December 2017. The mortgage indebtedness will be reimbursed: (i) 1,600 thousand of Euros, in 8 semi-annual instalments of equal principal amount, the first expiring on 30 June 2020 and the last one on 31st December 2023; (ii) while the residual amount of the mortgage debt in a single instalment expiring on 31st December 2024.

7

- The verification on an annual basis of compliance with certain financial parameters, *covenants*, at the level of consolidated financial statements, from the financial year 2018.

As part of the provisions included in the Restructuring Agreement, on 21st December 2017 the capital increase was issued, after the approval by the Extraordinary Shareholders' Meeting of 21st September 2017. The Company issued 206,944,327 ordinary shares at a price of €0.0483 per share (among which €0.0135 to be allocated to capital and €0.0348 to be allocated to the share premium reserve), to be offered on a reserved basis to *River Tre*, thus excluding the option right in favour of the current Shareholders according to the art. 2441 of the Italian Civil Code. As a result of this transaction, the control of the Group was transferred from Mr. Giuseppe Stefanel to *River Tre Spa*, which now holds 71% of the share capital of Stefanel Spa. In turn, *River Tre* is directly controlled by *Trinity Investments Designated Activity Company*, a company managed by the *Attestor Capital LLP Fund*.
The Issuer has issued equity financial instruments, the so-called *Stefanel SFP*, for a nominal value of 15,000,000 of Euros subscribed by: (i) River Tre for 14,099,279 Euros; (ii) from Banca Monte dei Paschi di Siena S.p.A. for 397,398 Euros; (iii) from Unicredit S.p.A. for 349,636 Euros and (iv) from Banco Popolare for 153,687 Euros.

The main economic, equity and financial effects that were reflected in the consolidated financial statements for the year ended 31st December 2017 in relation to the implementation of the Restructuring Agreement are shown below (Figure 4.3):

values in thousands of Euros	Effects on Income Statement	Effects on Balance Sheet	Effects on Gross Financial Position
Capital increase and issue of equity financial instruments	-	25.000	(25.000)
New Plan Finance	(5)	-	23.763
Rescheduling of existing financial debt :			
Financial income from the fair value measurement of consolidated debt and mortgage debt	32.863	32.863	(32.863)
Financial charges arising from the amortised cost of consolidated debt and mortgage debt	(124)	(124)	124
Financial charges arising from the amortised cost of the financial debt covered by the previous restructuring agreement	(725)	(725)	725
Agreements for the remission and rescheduling of payables towards suppliers and factoring companies:			
Income from agreements with suppliers and factoring companies	15.621	15.621	-
Financial income deriving from the fair value measurement of payables towards suppliers and factoring companies	6.313	6.313	-
Financial charges deriving from the amortised cost of debt to suppliers and factoring companies	(259)	(259)	-
Transaction Charges:			
Capital increase and issue of equity financial instruments	-	(1.365)	-
New Plan Finance	-	-	(1.296)
Rescheduling of existing financial debt	(2.083)	(2.083)	-
Total Gross Effects of the Operation	**51.601**	**75.241**	**(34.547)**
Tax Effects of the Operation	(4.197)	(4.197)	-
Total Effects of the Operation	**47.404**	**71.044**	**(34.547)**

Legenda:
Increase/(decrease) in the period result and in shareholders' equity
Increase/(decrease) in net financial position

Figure 4.3 *Effects on 2017 Financial Statement*

Source: Stefanel Consolidated Financial Statement 2017

The corporate strategy reflected in the 2016-2022 Plan, underlying the 2017 Restructuring Agreement, initially approved on 20 April 2017, then on 23rd June 2017 and finally approved in its final version on 20 July 2017, supported by obtaining new financial resources from outside, takes into account the progress of the corporate relaunch project, with particular reference to:

1. the completion of the relaunching process of the Stefanel brand, acting mainly on product and communication levers through a greater focus on knitwear, the strengthening of the stylistic line, the increase in advertising expenditure and the refurbishment of points of sale;
2. further rationalization of the direct shop network, through the definition of a plan for the closing of non-performing sales outlets;
3. the development of the indirect channel (wholesale), with the aim of rebalancing the revenue mix between the direct and indirect channels in favour of the latter; continuous strengthening of the presence abroad in euro and non-euro areas, focusing on growing geographical areas;
4. the increase in like-for-like sales which, compared to the growth forecasts of the "women's clothing" market, include elements specific to the company and the brand such as, for example but not limited to, the size of the market share held, the shares identified for the purpose of repositioning the brand, the relative performance of sales in recent years;
5. the implementation of a new approach in merchandising with the aim of improving sell-through during the period of regular sales;
6. the implementation of a new sourcing strategy by increasing production in Italy and the Mediterranean area compared to that in the Far East;
7. the maintenance of the gross margin thanks to the strengthening of the sourcing and initial mark-up policies, as well as the implementation of a mark down policy on retail sales more consistent with the new product positioning.

With regard to the main performance indicators, the 2016-2022 Business Plan provides for to achieve:

- a positive consolidated EBITDA and positive operating cash flows starting from the year 2018 and up over in the period of the Plan;
- a positive net result for 2017, due to the positive components deriving from the write-off of trade payables and payables to the factoring company and the measurement at fair value of the portion of financial payables subject to consolidation and the portion of trade payables and payables to the factoring company, subject to specific write-off and rescheduling agreements, due beyond the year;

- positive consolidated shareholders' equity as from 2017, mainly due to the net result for the period and the expected capital increase and issue of equity financial instruments;
- positive consolidated net results due to the effect of ordinary operations starting from financial year 2020 and growing over the plan period.

Also following the implementation of the 2017 Restructuring Agreement, 2017 shows a profit for the year of 13,714 thousand of Euros, after having recorded net non-recurring expenses of 10,906 thousand of Euros and net financial income of 52,714 thousand of Euros. At 31st December 2017, consolidated shareholders' equity was positive at 13,188 thousand of Euros due to the capital increase and the issue of equity instruments. Consolidated net financial indebtedness at 31st December 2017 amounted to 40,303 thousands of Euros, a net decrease compared to 31st December 2016 (euro 84,700 thousand), due to the effects of the 2017 Restructuring Agreement corresponding to: (i) 25,000 thousands of Euros for the conversion of bank debt into equity, (ii) 23,763 thousands of Euros for the disbursement of new financial resources, net of transaction costs of 1,296 thousands of Euros and (iii) 32,863 thousands of Euros for the fair value measurement of the bank debt being consolidated.
However, these trends show significant negative deviations from the Plan's forecasts in terms of EBITDA and shareholders' equity, while the value of cash and cash equivalents is in line with the Plan's forecasts, after having considered some timing effects relating to payments linked to the Restructuring Agreement that were made in the early months of 2018.
Although the Directors believe that there are still uncertainties relating to events or conditions that could give rise to significant doubts as to the ability of the Company and the Group to continue to operate on a going concern basis, connected with the ability of the Company and the Group to achieve the economic and financial forecasts contained in the 2016-2022 Business Plan, they have a reasonable expectation that the Group will be able to continue operating in the foreseeable future.

4.7 The first visible results of the 2017 Restructuring Plan

Stefanel, after the entry of a new controlling shareholder, composed by the Private Equity Funds Oxy Capital and Attestor, and after completing a plan to strengthen capital, started a phase of relaunching the company and its brand with the aim of returning to the top of the reference market.

The strategy studied by the new top management team, initially, was led by the CEO Cristiano Portas, appointed by the Board of Directors on 17^{th} January 2018 for his experience in turnaround operations, and is focused on an industrial plan characterized by the Company's core values, such as high product quality, high professionalism at all stages of the value chain and attention to the customer. These elements, together with new marketing strategies, attention to new digital channels and a new approach within existing stores, will allow, according to the management, to regain a leading role for the company in the Italian and international fashion scene.

The ability to forecast the evolution of the Group's management in the coming months is closely linked to the timing and outcome of the turnaround and relaunch process of the Group, which began, as we have seen previously, in 2017.

The Restructuring Plan was drawn up in a context in which the clothing sector, as well as the reference markets, have not yet fully recovered, since they are still characterised by significant uncertainty and stagnation in consumption, as well as by deep changes in the sector, together with a particularly complex geo-political, economic and social context at international level, which affects the countries in which the Group mainly operates, making the scenario extremely uncertain and making forecasting even more complex.

We can now analyse the effects of the new Restructuring Plan that occurred in the early months of 2018.

Stefanel's Board of Directors has decided to postpone the approval of the half-yearly report, continuing to support a situation of uncertainty. The Company explained that, also due to the negative trend in sales in the spring-summer 2018 season and in the start of the autumn-winter 2018 season influenced by unfavourable weather conditions, it was not possible to fully comply with the Restructuring Plan approved last December and forecast the volume of profits in the coming months.

However, the management has announced that the Plan has been partially implemented, in particular 67 direct stores between Italy and abroad have been closed and the number of employees has risen from 987 to 858. In addition, corrective actions were implemented, ranging from more effective commercial action to revision of the merchandising plan and design.

A revision of fixed costs and points of sale is currently underway, with greater emphasis on digital distribution channels and international distribution partnerships.

The Board took note of the results at 30 June 2018, which show significant deviations from what was assumed in the 2018 forecasts, with particular reference to the items "revenues" and "gross margin". In particular, consolidated revenues and gross margin at 30 June 2018 were respectively -12.3% and -14.5% lower than what forecasted for 2018 and -9.2% and -8.0% lower compared to the same period of the previous year. This trend, although slightly improving in July and August for the spring-summer collection, was also confirmed overall in the third quarter. Against this trend in revenues, management took steps to contain costs as early as the second quarter of the year, which partly offset the loss in margins due to the performance of the business.

From month to month, the hypothesis of non-compliance with the Group's financial covenant relating to EBITDA for 2018, as decided in the Restructuring Agreement in force with the banking sector, appears increasingly concrete. In the monthly market disclosure, as required by Consob, we can see that Stefanel has admitted a negative deviation from the 2018 forecast data; in addition, if this situation should continue, some cash conflicts could arise in the coming months and the probability that the EBITDA closes the year with a negative value.

Then, with regard to Stefanel's net financial indebtedness, at 31st August 2018, it exceeded 60 million Euros, compared to over 40 million at 31st December 2017, and as a result of the Restructuring Agreement it was entirely medium/long-term.

The table below provides a breakdown of Stefanel's net financial debt at 31st August 2018 and 31st December 2017:

(thousand of Euros)	**31.08.2018**	**31.12.2017**
A. Cash and equivalents	21	279
B. Bank deposits	2.282	115.166
C. Securities held for trading	-	-
D. Liquidity (A)+(B)+(C)	**2.303**	**15.445**
E. Current financial receivables	**4.447**	**5.576**
F. Current bank payables	-	845
G. Current portion of medium/long - term bank loans	-	-
H. Other current financial payables	-	-
I. Payables and other current financial liabilities (F)+(G)+(H)	**-**	**845**
J. Net current financial indebtedness (D)+(E)+(I)	**-6749**	**-20237**
K. Non-current bank payables	11.431	10.681
L. Non-current portion of medium/long - term bank loans	43.011	39.352
M. Non-current shareholders' loan	12.688	11.855
N. Other non-current financial payables	2.334	2.301
O. Non-current financial indebtedness (K)+(L)+(M)+(N)	**69.463**	**64.189**
P. Net financial position (J)+(O)	**62.714**	**43.952**

Figure 4.4 *Net Financial Position 31.08.2018 vs 31.12.2017*
Source: Monthly market disclosure pursuant to art. 114, C. 5, D. Lgs. n. 58/98 at 31.08.2018

The Company promptly informed the financing banks of the current economic and financial situation, anticipating the possible request for a *Waiver* for the failure to comply with the covenant.
The Board of Directors resolved to meet in October to start studying a corporate reorganisation project that would allow the Group to continue to operate on a continuous basis, even if sales performance did not allow the objectives of the current plan to be pursued.
The Board of Directors also found that, also on the basis of the balance sheet at 30 June 2018, the economic data updated after 30 June 2018 could lead to the emergence of a loss such as to bring the Company within the scope of Article 2446 of the Italian Civil Code. Therefore, the Board of Directors resolved to set the date of the shareholders' meeting for 14th December 2018, in order to pass the relevant resolutions.
It seems that the "star" of the fashion economy of the North-east of the Eighties is not able to find peace and the Restructuring Plan approved in its final version only a year ago must already be reviewed, because the expected timing is skipped.
In addition, in July 2018, CEO Cristiano Portas, who had arrived at Stefanel only six months earlier, resigned to take on new professional challenges. This very short term of office of Portas is both a spy and a symptom of the difficulties faced by Stefanel. The new administrator will arrive once the right profile has been identified. In the meantime, the proxies have been given ad interim to the director-shareholder Stefano Vassalli.
For the period so far observable, the scenario for the Group does not seem to be the best, on the contrary, the events manifested in the financial year 2018 do not seem to give great signs of change or improvement and could negatively affect the going-concern of the business.

CONCLUSION

Over the years, the phenomenon of business crisis has been the subject of numerous studies, researches and publications, with the aim to elaborate interpretations, models and guidelines to support the corporate management in this delicate phase of the company life cycle.

In the economic literature, various Authors have discussed regarding the definition and the development of the phenomenon; in particular in Italy, starting from the early 1980s, authors like Brugger (1984), Vergara (1988) and Guatri (1995) have analysed the situations of crisis in the Italian industrial scenario proposing empirical elaborations based on real cases.

All possible causes of a distress situation can arise both from potential internal problems, they are specific to each company and depend on firm's decisions and actions, and from consequences of external causes, which can affect only a specific industry or the entire economic system, as described in the arguments of Falini (2011) and Capizzi (2012); but the final resolution of the corporate crisis essentially depends on how and when the management decides to act to restore a situation of normal business activity and value generation. As soon as the company is able to perceive the symptoms of its own critical situation, the greater the possibility to implement corrective actions aimed at restructuring process.

The objective of this study is precisely to start from the economic literature, concerning the process of corporate crisis, and Italian Bankruptcy Law in order to analyze in depth a real case of a relevant Italian company.

As we have seen, Stefanel's crisis was caused by a mix of internal and external factors and led to a difficult situation, that worsened year by year through a slow and heartbreaking process.

To better understand the phases of prevention and resolution of distress, it was necessary to take into consideration the firm's business model and strategy in relation to the continuously changing external competitive environment.

The management, initially, tried to solve the crisis on its own, trying to recover resources where possible, through the sale of unprofitable assets, costs cutting, change of strategy and agreements with credit institutions, using the tools made available by the Italian Legislator in a going-concern perspective.

In 2017, however, it reached a point of no return, in which it was necessary to intervene with an external and specialized operator. With the Private Equity Funds, Oxy Capital and Attestor, a delicate Debt Restructuring Plan was formalized (art. 182-bis B.L.). The principal aim of any corporate turnaround, according to Downey (2009) and Collard (2010), is to remove the company quickly from any immediate danger of going into liquidation, to focus on activities and tasks that restore corporate value and to build enterprises in which future buyers want to invest

The characteristics and contents of the Stefanel's Restructuring Plan, which regulates relations between the Company and its main creditors and financial institutions, have been analyzed in detail, in conjunction with a reformulation of the Firm's Business Plan.

Stefanel is one of the first Italian cases in which it is possible to analyze in a concrete way a turnaround operation carried out by Private Equity Funds; an event that is very common abroad, especially in the American and Anglo-Saxon markets. While in Italy today, the turnaround segment within private equity is still underdeveloped and the number of subjects specialized in this category of investments remains rather low.

It was, therefore, interesting to discuss the costs and benefits of this intervention for the Company and the differences compared to a mere financing action by the banking sector, taking into consideration the interpretations of some authors, such as Berwin (2006), Cooke (2008), Acharya (2013) and Kazimi (2016). In particular, thanks to the previous studies of Kaplan and Strömberg (2009), it was possible to analyse the Stefanel case in terms of financial engineering, governance engineering and operational engineering of the turnaround operation.

The operation started in 2017, and since it is still on-going, it was not possible to carry out an analysis of the conclusions ex post with the case closed. Despite this, some effects of the Plan are already visible in the first half of 2018 and it has also been possible to identify some signs for a possible future forecast looking at the numbers of the Company.

Today, Stefanel cannot be considered safe from the crisis, because it has not yet been able to achieve the objectives set and the procedures put in place have not led to the decisive change hoped for; in addition, the resignation of the CEO, that occurred a few months ago, do not bode well.

Appendix

Appendix 1 - Income Statement as reported

Data in € mln

INCOME STATEMENT AS REPORTED	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Sales of goods and services	275,4	181,9	182,9	193,6	186,6	168,5	155,6	156,6	134,1	125,3
Raw materials, consumables, goods and services	(110,1)	(79,8)	(76,7)	(84,5)	(84,7)	(76,0)	(62,8)	(66,9)	(61,0)	(56,3)
Advertising and promotions	(12,0)	(9,7)	(15,0)	(15,2)	(11,1)	(5,6)	(3,7)	(3,8)	(3,1)	(2,6)
SG&A	(151,4)	(126,5)	(117,6)	(114,3)	(94,0)	(96,1)	(83,4)	(83,8)	(82,4)	(86,3)
GROSS OPERATING INCOME	**1,8**	**(34,1)**	**(26,5)**	**(20,5)**	**(3,2)**	**(9,2)**	**5,7**	**2,1**	**(12,4)**	**(19,8)**
Depreciation, amortisation and impairment losses	(13,1)	(16,5)	(9,8)	(18,2)	(13,5)	(11,7)	(8,6)	(6,9)	(7,9)	(9,8)
NET OPERATING INCOME	**(11,3)**	**(50,6)**	**(36,3)**	**(38,7)**	**(16,7)**	**(20,8)**	**(3,0)**	**(4,8)**	**(20,3)**	**(29,7)**
Net interest income (expense)	(12,2)	(7,0)	(3,7)	(5,7)	(3,6)	(4,4)	(5,2)	(5,4)	(4,7)	(4,3)
Net interest income (expense) non recurring	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	52,7
Income (expense) from equity investments	4,3	(0,1)	0,0	0,0	(0,1)	(0,4)	(0,1)	(0,1)	(0,1)	(0,4)
RESULT BEFORE TAXES	**(19,3)**	**(57,6)**	**(39,9)**	**(44,4)**	**(20,4)**	**(25,6)**	**(8,2)**	**(10,1)**	**(25,1)**	**18,4**
Taxes	(2,0)	1,1	0,1	1,1	(0,4)	(1,7)	0,5	2,4	(0,2)	(4,7)
NET PROFIT OF CONTINUING OPERATIONS	**(21,3)**	**(56,6)**	**(39,8)**	**(43,3)**	**(20,8)**	**(27,3)**	**(7,7)**	**(7,7)**	**(25,3)**	**13,7**
Income from disposal of assets held for sale and from discontinued operations	0,5	8,0	4,5	57,9	0,7	3,5	0,0	0,0	0,0	0,0
NET RESULT	**(20,8)**	**(48,6)**	**(35,4)**	**14,4**	**(20,2)**	**(23,9)**	**(7,7)**	**(7,7)**	**(25,3)**	**13,7**
attributable to:										
Shareholders of the parent company	(20,8)	(48,7)	(35,4)	14,4	(20,2)	(24,0)	(7,8)	(7,8)	(25,5)	13,5
Minority interests	0,0	0,1	0,1	0,2	0,1	0,1	0,2	0,1	0,2	0,2

Appendix 2 - Balance Sheet as reported

Data in € mln

BALANCE SHEET AS REPORTED	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
NON-CURRENT ASSETS										
Tangible fixed asstes	50,2	35,8	39,3	38,1	32,8	27,0	23,1	21,6	18,6	15,1
Intangible fixed assets	57,9	46,7	45,3	41,7	35,1	31,4	27,2	29,1	24,9	19,6
Shareholdings valued using the equity method	11,5	15,8	0,3	0,2	0,6	0,5	0,5	0,5	0,5	0,2
Financial assets and other non-current assets	47,4	51,1	0,0	0,0	0,1	0,3	0,2	0,7	0,5	0,0
Other receivables and non-current assets	17,1	12,1	10,6	10,7	10,6	5,8	6,7	7,3	7	4,4
Deferred tax assets	6,7	7,2	7,5	8,3	7,7	7,5	9,4	11,8	11,8	7,2
TOTAL NON-CURRENT ASSETS	**190,8**	**168,8**	**102,9**	**99,0**	**86,8**	**72,4**	**67,1**	**70,9**	**63,2**	**46,6**
CURRENT ASSETS										
Inventories	52,7	40,7	44,5	54,8	51,4	46,2	47,4	46,8	35,9	30,7
Trade receivables	24,2	23,4	24,1	25,5	41,2	32,2	24,4	27,2	19,1	15,9
Other receivables and current assets	18,2	16,9	20,0	18,5	14,3	16,3	12,3	14,1	14,6	12,6
Financial assets and other current assets	0,1	1,1	2,4	1,7	0,0	0,6	0,9	0,1	0,2	0,1
Cash and cash equivalents	27,0	17,3	25,9	31,3	11,7	8,1	12,1	5,4	7,6	22,4
TOTAL CURRENT ASSETS	**122,1**	**99,5**	**117,0**	**131,8**	**118,6**	**103,5**	**97,0**	**93,5**	**77,5**	**81,7**
ASSETS HELD FOR SALE	0,0	0,0	75,6	0,0	0,0	0,0	2,2	0,0	0,8	0,0
TOTAL ASSETS	**312,9**	**268,2**	**295,5**	**230,8**	**205,4**	**176,0**	**166,3**	**164,4**	**141,6**	**128,3**

Appendix 3 - Balance Sheet as reported (continued)

Data in € mln

BALANCE SHEET AS REPORTED - continued	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
GROUP EQUITY										
Share capital	88,9	88,9	97,5	97,5	55,2	27,0	27,0	16,5	16,5	19,3
Other reserves	14,1	(1,8)	(10,8)	(46,4)	9,5	(8,7)	(9,2)	(9,7)	0,0	0,1
Other equity components	0,0	0,0	0,0	0,0	0,0	(0,6)	(0,5)	(0,6)	(0,6)	(0,6)
Retained earnings/(losses)	0,0	0,0	0,0	0,0	0,0	1,1	(6,8)	(4,1)	(29,6)	4,3
Profit (loss) for the year	(20,8)	(48,7)	(35,4)	14,4	(20,2)	0,0	0,0	0,0	0,0	0,0
Total group equity	82,2	38,4	51,3	65,6	44,5	18,8	10,6	2,1	(24,0)	13,0
Total minority interest	0,3	0,4	0,2	0,3	0,5	0,2	0,2	0,2	0,2	0,2
Total equity	**82,5**	**38,8**	**51,5**	**65,9**	**44,9**	**19,0**	**10,8**	**2,3**	**(23,8)**	**13,2**
NON-CURRENT LIABILITIES										
Non-current financial liabilities	14,4	10,9	0,6	28,6	40,5	0,0	51,0	0,0	0,0	61,9
Other non-current liabilities	0,0	0,0	0,4	0,2	0,0	0,0	0,4	0,0	0,0	11,1
Non-current provisions	2,9	3,2	3,1	2,2	2,5	3,2	3,6	3,2	1,8	1,8
Provisions for employee benefits	6,2	5,6	5,0	4,6	3,8	3,8	2,6	2,2	2,3	1,8
Deferred tax liabilities	5,7	5,0	4,9	4,4	3,7	3,6	4,3	3,8	3,6	2,3
Total non-current liabilities	**29,2**	**24,6**	**14,0**	**40,0**	**50,6**	**10,6**	**61,9**	**9,3**	**7,7**	**78,8**
CURRENT LIABILITIES										
Current financial liabilities	133,3	138,9	154,6	40,2	39,2	84,6	35,1	88,4	93,1	0,8
Trade payables	52,4	52,0	59,6	68,9	58,7	51,0	45,9	55,3	55,0	24,7
Current provisions	0,6	2,0	1,6	1,4	0,2	0,4	0,4	0,0	0,0	0,3
Other payables and current liabilities	14,9	12,0	14,1	14,4	11,8	10,5	12,2	9,1	9,4	10,4
Total current liabilities	201,3	204,8	229,9	124,9	109,9	146,4	93,6	152,8	157,6	36,3
Total liabilities	**230,5**	**229,5**	**244,0**	**164,9**	**160,5**	**157,0**	**155,5**	**162,1**	**165,3**	**115,1**
TOTAL EQUITY AND LIABILITIES	**312,9**	**268,2**	**295,5**	**230,8**	**205,4**	**176,0**	**166,3**	**164,5**	**141,6**	**128,3**

Appendix 4 - Reorganized Balance Sheet (Invested Capital)

Data in € mln

REORGANIZED BALANCE SHEET (INVESTED CAPITAL)	2010	2011	2012	2013	2014	2015	2016	2017
Working cash*	9,1	9,7	9,3	8,8	12,9	5,4	7,6	22,4
Trade receivables	24,1	25,5	41,2	32,2	24,4	27,2	19,1	16,0
Inventories	44,5	54,8	51,4	46,2	47,4	46,8	35,9	30,7
Trade payables	(59,6)	(68,9)	(58,7)	(51,0)	(45,9)	(55,3)	(55,0)	(35,8)
Trade working capital	**18,1**	**21,1**	**43,2**	**36,2**	**38,8**	**24,1**	**7,6**	**33,3**
Other operating current assets	20,0	18,5	14,3	12,9	12,1	14,1	14,6	12,5
Other operating current liabilities	(14,1)	(14,4)	(11,8)	(10,5)	(12,2)	(9,1)	(9,4)	(10,6)
Other current assets and liabilities	**5,9**	**4,1**	**2,5**	**2,4**	**(0,1)**	**5,0**	**5,2**	**1,9**
Net working capital	**24,0**	**25,2**	**45,7**	**38,6**	**38,7**	**29,1**	**12,8**	**35,2**
Tangible assets	39,3	38,1	32,8	27,0	23,1	21,6	18,6	15,1
Operating intangibles	45,3	41,7	35,1	31,4	27,2	29,1	24,9	19,6
Total operating fixed capital	**84,6**	**79,8**	**67,9**	**58,4**	**50,3**	**50,7**	**43,5**	**34,7**
Operating receivables and other non-current assets	10,6	10,7	10,6	5,8	6,8	7,3	7,0	4,4
Operating deferred tax assets (liabilities)	0,5	1,9	1,9	1,8	0,7	0,8	0,7	0,6
Operating non-current liabilities	(5,0)	(0,2)	0,0	0,0	(0,4)	0,0	0,0	11,1
Operating provisions	(0,3)	(2,2)	(2,4)	(3,2)	(3,5)	(3,2)	(1,8)	(1,8)
Total other non-current operating assets and liabilities	**5,8**	**10,2**	**10,1**	**4,4**	**3,6**	**4,9**	**5,9**	**14,3**
Invested capital excluding goodwill and similar intangibles	**114,4**	**115,2**	**123,7**	**101,4**	**92,6**	**84,7**	**62,2**	**84,2**
Goodwill and similar intangibles	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Deferred tax asset (liabilities) on similar intangibles	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Goodwill and other similar intangibles	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**
Invested capital including goodwill and similar intangibles	**114,4**	**115,2**	**123,7**	**101,4**	**92,6**	**84,7**	**62,2**	**84,2**
Non-operating current assets	75,6	0,0	0,0	3,5	2,3	3,1	2,6	2,3
Other non-operating current liabilities	0,0	0,0	0,0	0,0	35,1	6,2	18,9	0,8
Non-operating non-current assets	0,4	0,2	0,7	0,8	0,7	1,2	1,0	0,2
Non-operating deferred tax assets (liabilities)	2,0	2,0	2,0	2,1	3,8	2,9	2,9	1,7
Non-operating non-current liabilities	0,6	28,1	40,5	0,0	50,60	0,0	0,0	61,9
Non-operating assets	**78,6**	**30,3**	**43,2**	**6,4**	**92,5**	**13,4**	**25,4**	**66,9**
Total funds invested	**193,0**	**145,5**	**166,9**	**107,8**	**185,1**	**98,1**	**87,6**	**151,1**

Appendix 5 - Reorganized Balance Sheet (Sources of Financing)

Data in € mln

REORGANIZED BALANCE SHEET (SOURCES OF FINANCING)	2010	2011	2012	2013	2014	2015	2016	2017
Excess cash	(55,8)	(4,4)	(11,8)	(9,0)	(13,2)	(6,2)	(8,4)	(22,4)
Adjustments on short-term borrowings	0,6	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Long-term borrowings	0,0	28,3	40,5	0,0	51,0	0,0	0,0	61,9
Short-term borrowings	126,8	11,9	39,2	84,6	35,1	88,4	93,1	0,8
Net financial position	**71,6**	**35,8**	**67,9**	**75,6**	**72,9**	**82,2**	**84,7**	**40,3**
Provision for employee benefit	3,10	4,60	3,80	3,8	2,6	2,2	2,3	1,8
Non-operating provisions	1,7	1,5	0,3	0,4	0,5	0,4	0,3	0,3
Debt equivalents	**4,8**	**6,1**	**4,1**	**4,2**	**3,1**	**2,6**	**2,6**	**2,1**
Net financial position and debt equivalents	**76,4**	**41,9**	**72,0**	**79,8**	**76,0**	**84,8**	**87,30**	**42,4**
Minority interests	**0,2**	**0,3**	**0,5**	**0,2**	**0,2**	**0,2**	**0,2**	**0,2**
Shareholders' equity	**51,5**	**65,9**	**44,3**	**19,0**	**10,8**	**2,3**	**(23,7)**	**13,2**
Total sources of financing	**128,1**	**108,1**	**116,8**	**99,0**	**87,0**	**87,3**	**63,8**	**55,8**

Appendix 6 - Reorganized Income Statement

Data in € mln

REORGANIZED INCOME STATEMENT	2010	2011	2012	2013	2014	2015	2016	2017
Revenues	**182,9**	**193,6**	**186,6**	**168,5**	**155,6**	**156,6**	**134,1**	**125,3**
Operating cost (personnel and D&A excluded):	(168,5)	(173,2)	(151,6)	(145,9)	(120,2)	(125,4)	(118)	(119,9)
Raw materials, consumables, goods and services	*(76,7)*	*(84,5)*	*(84,7)*	*(76,0)*	*(62,8)*	*(66,9)*	*(61,0)*	*(56,3)*
Advertising and promotions	*(15,0)*	*(15,2)*	*(11,1)*	*(5,6)*	*(3,7)*	*(3,8)*	*(3,1)*	*(2,6)*
Other operating costs	*(76,7)*	*(73,4)*	*(55,8)*	*(64,2)*	*(53,6)*	*(54,7)*	*(53,9)*	*(61)*
Personnel expenses	(40,9)	(40,9)	(38,2)	(31,8)	(29,8)	(29,1)	(28,5)	(25,3)
EBITDA	**(26,5)**	**(20,5)**	**(3,2)**	**(9,2)**	**5,7**	**2,1**	**(12,4)**	**(19,8)**
Total D&A	(12,2)	(15,8)	(13,5)	(10,8)	(8,5)	(6,9)	(7,9)	(9,9)
Depreciation	*(10,4)*	*(12,9)*	*(10,8)*	*(8,5)*	*(6,3)*	*(4,8)*	*(5,9)*	*(8,2)*
Amortization of operating intangibles	*(1,8)*	*(2,9)*	*(2,7)*	*(2,3)*	*(2,2)*	*(2,1)*	*(2,0)*	*(1,7)*
EBITA	**(38,7)**	**(36,3)**	**(16,7)**	**(20,8)**	**(3,0)**	**(4,8)**	**(20,3)**	**(29,7)**
Amortization of assets similar to goodwill	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
EBIT	**(38,7)**	**(36,3)**	**(16,7)**	**(20,8)**	**(3,0)**	**(4,8)**	**(20,3)**	**(29,7)**
Impairment losses	(0,7)	(0,7)	(2,4)	(0,9)	(0,8)	(0,0)	(0,0)	(0,0)
Non-recurring and extraordinary items	1,0	55,8	5,6	5,6	1,3	0,0	0,0	52,7
Interest income (expense) from equity investments	0,0	0,0	(0,1)	(0,4)	(0,1)	(0,1)	(0,1)	(0,4)
Net financial result:	(3,7)	(5,7)	(6,1)	(5,6)	(5,5)	(5,2)	(4,5)	(4,0)
Exchange rate (losses) gains	*1,9*	*(1,9)*	*(0,7)*	*(1,2)*	*(0,9)*	*(0,1)*	*(0,2)*	*(0,3)*
Interest (expense) income	*(5,5)*	*(4,5)*	*(5,4)*	*(4,4)*	*(4,6)*	*(5,1)*	*(4,3)*	*(3,7)*
EBT	**(35,4)**	**13,5**	**(19,7)**	**(22,1)**	**(8,2)**	**(10,0)**	**(24,9)**	**18,6**
Taxes	0,1	1,1	(0,4)	(1,7)	0,5	2,4	(0,2)	(4,7)
Net Income	**(35,3)**	**14,6**	**(20,1)**	**(23,8)**	**(7,7)**	**(7,6)**	**(25,1)**	**13,9**
Minority result	(0,1)	(0,2)	(0,1)	(0,1)	(0,2)	(0,1)	(0,2)	(0,2)
Group Net Income	**(35,4)**	**14,4**	**(20,2)**	**(23,9)**	**(7,9)**	**(7,7)**	**(25,3)**	**13,7**

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