The Distressed Debt Report

News, Information, and Analysis of Distressed Debt in the Middle Market

Volume VI, No. 8 distresseddebt.dealflow.com April 27, 2010

IN THIS ISSUE

CHAPTER 11 FILINGS DECLINED IN Q1

But Restructuring Pros Expect Lull to Be Short-Lived

by Kirk O'Neil

The number of Chapter 11 bankruptcies declined in the first quarter as the economy improved and capital became more available.

But restructuring professionals expect the slowdown in bankruptcy filings to be short-lived, as an impending commercial real estate collapse could crowd the bankruptcy courts by the end of the year.

An easing of Chapter 11 filings during the first three months of the year gave bankruptcy and restructuring professionals a little breather after a very busy year in 2009, Bill Brandt, CEO of turnaround and restructuring firm **Development Specialists Inc.**, in Chicago said. But Brandt believes a flood of commercial real estate loan defaults, which are just beginning to hit, will accelerate Chapter 11 bankruptcy filings by the end of the year.

"The next wave is likely to be the commercial real estate/CDO distress," he said.

Other factors could also contribute to a faster rate of bankruptcy filings, Brandt said.

"There could be about four, five or six major ingredients that could raise the rate of bankruptcies by the end of the year," he said. "It could be commercial real estate, the financial markets, consumer spending, or inflation. It's very unpredictable.

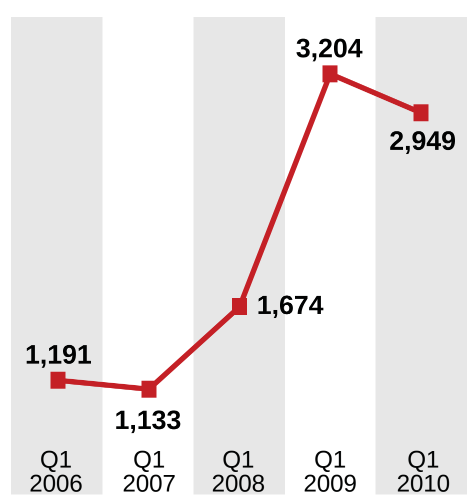
"I don't see a great Christmas season this year," Brandt said. "It could be better than last year, but we could have pretty high inflation. If consumer confidence isn't there, it won't be good."

The number of Chapter 11 bankruptcy filings declined by about 7% to 2,949 in the first quarter from 3,204 in the first quarter of 2009, according to data provider AACER. Last month alone, there were 1,068 filings, 20% less than the 1,347 bankruptcies in March 2009.

Brandt said that although he has seen

Continued on page 9

FIRST QUARTER CHAPTER 11 COMMERCIAL BANKRUPTCY FILINGS



Source: AACER

IN DEBATE OVER PE AND DEFAULTS, AGREEMENT OVER RECOVERY PROSPECTS

by Paul Springer

Debt rating agencies have an ongoing disagreement with the Private Equity Council, a trade group for private equity firms, over the effect of PE-related debt on default rates.

But both sides of the argument agree that recoveries for investors are relatively high for PE-backed companies whose debts are restructured.

"A review of U.S. corporate issuer defaults in 2009 suggests that creditors of private-equity-backed companies may realize better recoveries than creditors of companies with strategic owners," Moody's Investors Service said in its recent report on the subject.

Moody's found that even when significant leverage is involved, PE-backed companies are more likely to survive distressed situations.

"The presence of private equity may be positive during periods of dis-

Continued on page 7

The Distressed Debt Report
DealFlow Media, Inc.
P.O. Box 122
Syosset, NY 11791
T (516) 876-8006
F (516) 876-8010
subscribe@dealflow.com
www.dealflow.com

The Distressed Debt Report™ is published on the second and fourth Tuesday of every month, except the second Tuesday of August and the fourth Tuesday of December. Subscription rate: $1,595 per year for 22 issues, delivered electronically.

DISTRESSED HEDGE FUNDS LOOK FOR ANOTHER GOOD YEAR

Hedge funds can expect another good year for their distressed debt plays as they launch new funds to focus on the strategy, advisors say.

Several hedge fund managers launched new funds in recent weeks after raising capital to acquire debt or assets from troubled companies and to finance companies in distress.

Hedge fund advisory firm **Hennessee Group**'s index that tracks funds that focus on distressed debt gained 8.37% in the first three months of this year, outperforming 22 other Hennessee indexes that track hedge funds with other strategies. Hennessee's Distressed Index gained 42.5% in 2009, ranking second only to an index that tracks funds that invest in Latin American assets.

"We think distressed debt will be one of the best performers for hedge funds," said Charles Gradante, co-founder and principal of Hennessee Group.

Gradante said some of the keys to a successful year for distressed funds will be good performances by high-yield bonds, asset sales by the Federal Deposit Insurance Corp., and investors converting distressed debt to equity.

"The FDIC is closing down a lot of regional banks and needs to put a lot of bank assets on the market for deep, deep discounts," Gradante said. "Many of these banks have loans with small and mid-size companies that are viable entities. It's all good money, but the FDIC has to get rid of them."

Meanwhile, high-yield bonds are yielding five percentage points more than Treasuries.

Managers of the distressed debt hedge funds will be able to achieve higher returns by investing in more illiquid securities, Gradante said. "Fund managers who open new illiquid funds with three-year lockups that won't need to meet redemptions for three years can go for returns of 30% or more."

Hennessee usually looks for annual gains of more than 20% in funds where it advises clients to invest, Gradante said.

Richard Wilson, managing director of the **Hedge Fund Group**, agrees that distressed debt hedge funds should do well this year.

"Many distressed debt hedge funds will do well in 2010 and 2011," he said. "2008 and 2009 were position building years as part of 2010 will be, but I think some of the largest returns on these investments are still to be seen.

Hedge funds are also likely to deepen their involvement in the commercial real estate market, with a wave of commercial real estate debt defaults expected to hit this year, Wilson said.

"Commercial real estate is a good market for hedge funds long-term," he said. "During 2007 to 2009, many hedge funds took market share from banks that couldn't lend to real estate projects or businesses but had in the past. Hedge funds are moving up the learning curves of financing, developing, and real estate investing. I believe every downturn in the economy just helps hedge funds evolve into more diversely talented animals."

Centrecourt Asset Management said it would launch its third distressed fund this month, the CAM Distressed/Credit Opportunities Fund. Centrecourt's distressed fund will invest in securities of companies not able to secure financing from the capital markets, securities from good companies with less-than-optimal capital structures, and securities which have been mispriced due to market imbalances, the firm said.

GSO Capital Partners, a subsidiary of **Blackstone Group**, is raising a $2 billion fund to invest in distressed companies in dire need of cash, and **Monarch**

Alternative Capital is raising $400 million for a distressed fund for companies with heavy debt that need restructuring, *Bloomberg* reported. —*KO*

CMBS Loan Defaults to Surpass 11% by Year-End, Fitch Says

The default rate on loans included in commercial mortgage-backed securities will continue to rise, with an additional 4.4% likely in 2010 bringing the overall default rate past 11% on deals rated by Fitch Ratings, the firm said.

Separately, Moody's Investors Service said the delinquency rate on loans included in CMBS recorded its largest increase ever last month, rising by 69 basis points to 6.42%.

Fitch said that new CMBS loan defaults increased by more than five-fold in 2009, with 1,464 conduit loans totaling $17.75 billion defaulting last year. Defaults in the fourth quarter amounted to 34% of the principal balance of defaulted loans for the year, according to Fitch's U.S. CMBS 2009 Default Study.

Fitch said it's concerned about the number of large loan defaults, which rose considerably last year. A total of 56 loans over $50 million in size defaulted in 2009, while only five such loans defaulted in 2008.

Loans originated in 2007 defaulted in the largest numbers last year, accounting for 35.6% by principal balance. Fitch said that aggressive underwriting and higher leverage accounted for the higher percentage of 2007 defaults.

Retail property loans led all property types with 32.3% of all defaults in 2009, multifamily housing properties amounted to 22.1% of defaults, office properties had 20.2%, and hotels amounted to 17.8% of all defaults.

Moody's Delinquency Tracker report said that 45 basis points of the increase in the CMBS default rate last month was due to the $3 billion delinquent loan on the Peter Cooper Village/Stuyvesant Town apartment complex in New York City.

Some 343 loans included in CMBS had become delinquent in March, increasing the overall delinquent loan balance by $4.3 billion.

The addition of the Peter Cooper/Stuyvesant loan to delinquent status caused the multifamily loan delinquency rate to rise by 283 basis points in March to 12.19%. Multifamily became the worst-performing commercial real estate loan sector, although the total number of delinquent multifamily loans only rose by eight, according Moody's.

Delinquency rates on other commercial properties also rose in March, as hotels jumped 63 basis points to 11.27%, retail delinquencies jumped by 35 basis points to 5.57%, industrial rose 30 basis points to 4.57% and offices increased 14 basis points to 4.12%.

Moody's Delinquency Tracker tracks all loans in conduit and fusion deals issued in 1998 or later with a current balance greater than zero.

Inland's Auction Puts Big Discounts on CRE Opening Bids

Inland Real Estate Auctions has set opening bids with big discounts for several commercial real estate buildings and development sites for a May 19 auction of bank-owned properties and court-ordered property sales.

Among the properties with opening bid prices significantly discounted from appraised values is a 49,978 square-foot multi-tenant office building in Rolling Meadows, Ill. The building was appraised at $3 million, but is subject to a minimum opening bid of $1.75 million.

A bank-owned 8,620 square-foot office/strip center building in Richton Park, Ill., was appraised at $510,000, but will go on the block for a minimum bid of $119,000. Other properties include 1.25 acre bank-owned industrial development sites in New Lenox, Ill., previously priced at $115,000, but offered at minimum bids of $47,500.

Commercial Real Estate Prices Decline for First Time in Four Months

Commercial real estate prices, as measured by Moody's/REAL Commercial Property Price Indices, recorded their first month-to-month decline in four months.

The price index fell by 2.6% in February.

Commercial real estate prices have fallen by 41.8% from their peak in October 2007, but have come back by 3.4% from their October 2009 low, Moody's said. The ratings agency said that commercial real estate prices increased by an aggregate 6.3% from November 2009 through January 2010, before falling again.

Transaction volume fell in February from January by 10% as measured by dollar value and nearly 30% by number of transactions. The index's February calculations were based on 66 repeat sales of the same properties, which totaled about $540 million.

The percentage of repeat sales classified as distressed increased from 4% in 2008 to approximately 20% in 2009. Distressed sales have continued to rise this year, reaching 25% in January and about 32% in February.

Commercial Real Estate CDO Delinquencies Rise, Fitch Says

Commercial real estate loan collateralized debt obligation delinquencies rose by 30 basis points last month, edging up to 12.8% as asset managers' disposals of troubled assets began to slow the rising delinquency rate, according to Fitch Ratings.

However, Fitch analysts said that the rate of realized losses increased almost three-fold. The amount of realized losses for March totaled $121.2 million, while February's was $41.8 million.

Fitch said that 19 assets were added to its CRE loan CDO delinquency total last month, and 17 assets were removed with nine disposed of at a loss.

Fitch said that 34 of its 35 rated CRE loan CDOs reported delinquencies in March, ranging from 1.4% to 41.1%. Fitch's universe of 35 rated CRE loan CDOs encompasses about 1,100 loans and 350 rated securities, or assets with a total balance of $23.8 billion.

Apollo's Innkeepers USA Trust Defaults on $825M Hotel Loan

Innkeepers USA Trust, which is controlled by private equity investor **Apollo Investment Corp.**, defaulted on an $825 million CMBS hotel portfolio loan.

The loan was transferred to special servicer **Midland Loan Services**, according to Fitch Ratings.

Apollo said in an April 14 filing with the Securities and Exchange Commission that Innkeepers USA had failed to make payments on certain debt and may not make future payments on the debt.

Innkeepers USA currently owns 73 hotels with approximately 10,000 rooms in 19 states.

Innkeepers USA Trust was purchased by Apollo near the peak of the hotel market in June 2007 for $1.5 billion, including $800 million in cash.

Magic Brands, Owner of Fuddruckers Restaurants, Files Chapter 11

Magic Brands LLC, the parent company of the Fuddruckers and Koo Koo Roo restaurant chains, filed for Chapter 11 bankruptcy and agreed to sell its assets to private equity firm **Tavistock Group** for $40 million.

Magic Brands said it would file a motion to establish bidding procedures for the sale, which will allow for qualified bidders to submit higher offers. The Austin, Texas-based company expects the sale to be completed in 60 to 90 days.

Magic Brands owns 85 Fuddruckers hamburger restaurants in 11 states and 13 Koo Koo Roo chicken restaurants in California. The company said it planned to terminate certain leases and close 24 corporate-owned Fuddruckers restaurants by April 30. None of the 135 franchisee-owned Fuddruckers restaurants are included in the Chapter 11 filing.

Tavistock, based in Windermere, Fla., already owns restaurants including Japanese eatery Sapporo in Scottsdale Ariz.; ZED451 with locations in Chicago, Boston and Boca Raton, Fla.; and the Napa Valley Grille, with restaurants in Westwood, Calif., Paramus, N.J., and Bloomington, Minn.

Wells Fargo Capital Finance, which was already Magic Brands' senior lender, is providing $14 million in debtor-in-possession financing to facilitate the sale, Magic Brands said in a statement.

FocalPoint Securities is Magic Brands' investment banker, and **Goulston & Storrs** is its lead bankruptcy counsel.

Noyack Medical Partners Forms Distressed Real Estate Fund

Noyack Medical Partners, a New York-based real estate investment company, said it formed a $200 million private equity fund for distressed real estate and repositioning opportunities in the health care, student housing and self-storage sectors.

The fund will concentrate its investments on the Eastern Seaboard, but it won't restrict itself if a suitable opportunity arises elsewhere, Noyack said. The fund will target transactions in the $10 million to $50 million range, with leverage levels below 70%. The fund will acquire assets and provide debt in a limited capacity.

Golub Capital Funds Mezz Loan to Recapitalize Biotech Firm

Golub Capital said it provided $12 million of senior subordinated debt to recapitalize biotech firm **Integrated DNA Technologies**.

The mezzanine loan was the first investment made by Golub's sixth middle-market mezzanine fund, GC 2009 Mezzanine Partners L.P.

Integrated DNA Technologies, based

in Coralville, Iowa, supplies custom nucleic acids to U.S. academic, government and commercial researchers in biotechnology, clinical diagnostics and pharmaceutical development.

Point Blank Solutions Files Chapter 11

Point Blank Solutions, a Pompano Beach, Fla.-based manufacturer and distributor of protective body armor, filed for Chapter 11 bankruptcy.

The company said it also secured an agreement for up to $20 million in debtor-in-possession financing which needed bankruptcy court approval. Point Blank said it intended to continue all of its business operations and to honor all of its customer commitments once it received the DIP approval from the court.

Point Blank said in a statement that its decision to file bankruptcy was driven by continued expenses tied to legacy issues from former management, as well as the lack of financing available because of the credit crisis.

Investors Want Nonperforming Loans; Deals Scarce, E&Y Survey Says

A new survey on the distressed commercial real estate debt market shows that 60% of respondents bid on or priced nonperforming loan portfolios last year, but fewer than 17.5% of those bidders were able to complete transactions, according to **Ernst & Young**.

The survey revealed that although investors were eager to buy loan portfolios, sellers were unwilling or unable to sell. Ernst & Young's Real Estate Distress Services Group surveyed real estate investment and opportunity funds, private equity funds, institutional investors, and real estate developers for the survey in late December.

Simon Sweetens Offer to Recapitalize General Growth

Simon Property Group offered to invest $2.5 billion in a recapitalization of bankrupt real estate investment trust **General Growth Properties** at the same share price as a reorganization plan sponsored by rival **Brookfield Asset Management** but with more favorable terms for General Growth and its stock holders, according to a letter from Simon CEO David Simon.

Simon said his company's proposal is more favorable because it doesn't include highly dilutive warrants that General Growth proposes to issue to Brookfield and its investment partners **Pershing Square** and **Fairholme Capital**. Simon's proposal includes a $1 billion co-investment commitment by **Paulson & Co.**

Simon offers to acquire 250 million shares of General Growth common stock for $2.5 billion, or $10 per share, which matches Brookfield's offer. Simon would not receive any warrants, payments or fees in connection with the General Growth investment, in contrast to Brookfield's offer. Warrants to be issued under Brookfield's plan could dilute General Growth's stock holders' investment by $895 million or $2.75 per share, Simon said.

Brookfield informed General Growth that it will not change its offer, the *Wall Street Journal* reported.

A bankruptcy court hearing to consider the bidding process for the sale of General Growth was postponed until May 4 to give the company more time to negotiate with Simon and Brookfield.

General Growth said in a statement that other matters not related to the bidding process will go forward as planned at a hearing this Thursday.

Hirings and Firings

Deutsche Bank hired Stephen Byrne as its head of distressed asset trading in Europe.

Byrne, who will be based in London, joins Deutsche Bank after 14 years at **Goldman Sachs**, where he was recently co-head of European high yield and public loan trading. He spent the last five years in Europe building Goldman Sachs' leveraged loan trading platform, Deutsche Bank said.

The following tables include data about publicly traded companies that have filed for bankruptcy and that have defaulted on debt in the 30 days through April 22. Data is provided by Capital IQ.

Public Company Bankruptcies

Company (Ticker)	Date	Enterprise Value (M)	Market Cap (M)	Revenue (M)	EBITDA (M)	Net Income (M)	Total Debt (M)
MDI, Inc. (OTCPK:MDIZ)	Apr. 16	4.63	3.77	-	-	-	-
Point Blank Solutions (OTCPK:PBSO.Q)	Apr. 14	9.32	6.22	203.1	-18.5	-17.3	42.2
Xerium Technologies (NYSE:XRM)	Mar. 30	676.7	59.6	500.1	95.1	-112.0	640.1

Debt Defaults

Company (Ticker)	Date	Revenue (M)	EBITDA (M)	Total Debt (M)
Daewoo Motor Sales Corp. (KOSE:A004550)	Apr. 20	2,546.4	72.1	2,104.3
Nord Resources Corp. (OTCBB:NRDS)	Apr. 9	19.9	2.59	23.6
Winalta Inc. (TSXV:WTA.A)	Apr. 1	40.2	-5.81	62.2
Liquidation World Inc. (TSX:LQW)	Apr. 1	147.2	(9.47)	8.87
Selectcore Ltd. (TSXV:SCG)	Mar. 30	77.3	0.86	2.5

Continued from front page

tress and default," the firm said. "Private-equity owners' access to capital, strong relationships within the capital markets, and financial sophistication give them tools to preserve value during periods of illiquidity and economic challenge."

Private equity investors are more likely to reorganize the companies they back outside of Chapter 11 protection, Moody's found. And recoveries are often superior for companies that reorganize, or at least plan their reorganizations, outside of bankruptcy court.

From 1987 to 2009, recoveries averaged 69% for companies that restructured through distressed exchanges and 54% for those that filed pre-packaged bankruptcies, Moody's said. That compared with average recoveries of 49% for those that reorganized after filing for Chapter 11.

Private Equity and Defaults

The question of whether PE sponsorship contributes to the likelihood of debt defaults remains open to debate. Moody's published a report last month titled "Private Equity 2009: Nearly Half of Defaults, But Better-Than-Average Recovery Prospects."

"The problem with leverage is that it is agnostic – it magnifies success both up or down," Kelly DePonte, a partner with private equity placement agent **Probitas Partners**, told *The Distressed Debt Report* in an email. "It also does not take a lot of skill to lever something, which is the reason LPs don't value it compared to the ability to make operational changes that increase earnings."

For private equity general partners, "leverage is like gambling because they are not focused on predicting market cycles," he said. "Strong returns strictly through leverage are a matter of luck – and when luck turns against you, the results can be horrific."

But the Washington, D.C.-based Private Equity Council objected to Moody's claim in the report that almost 50% of last year's defaults involved private equity. The group conducted its own analysis of companies that had PE involvements from 2000 through 2009 and found that only 2.8% defaulted in the recession of 2008 and 2009. That compared to 6.2% for other "similarly-financed businesses," the council said.

The Private Equity Council argued that Moody's analysis relied on an expansive definition of the term "default" that included voluntary transactions to deleverage companies.

"The reality is that PE firms have not been static for the last two years," Michael Granoff, CEO of private equity firm **Pomona Capital**, told *The Distressed Debt Report*. "Last year, there was a lot of debt restructuring. When you read the annual reports, the annual letters of PE funds this year, a prominent part of almost every buyout fund's report is 'here's how much debt we restructured last year.' I've never seen that before."

But the Private Equity Council's review of related research concluded that there are worse problems a company can have than excessive leverage.

"A company that defaults from an unsustainable capital structure tends to have a greater probability of emerging from bankruptcy in healthy condition than a company that defaults due to economic distress like increased competition, technological upheaval, or an antiquated business model," the Private Equity Council report said.

Banks have grown more willing to work with middle market borrowers that have taken steps to restructure and streamline operations, said William Welnhofer, head of the corporate restructuring group at Milwaukee-based investment bank **Robert W. Baird & Co**.

"If we're talking about a company that had a bloodbath in the fourth quarter of 2008 and maybe the first of 2009 and then put together a restructuring plan and then made some money in the last six months of 2009 and is making money now because of cost-cutting, it's not too difficult to walk into **PNC** or **Wells Fargo** or B of A and get financing – and at reasonable terms," he said.

Limited Options

But to be sure, smaller companies, whether private equity-backed or not, are less likely to be able to restructure their debts than larger ones.

"For smaller companies, bank lending is still way down as there is little appetite to add debt to balance sheets," Probitas Partners' DePonte said. "And the old syndication sources – CDOs, CLOs, hedge funds – either are not around or have little risk appetite themselves."

And the bank financing that is available is likely to come with tighter covenants than in the past.

"Many middle market companies refinancing debt are seeing an increase in covenants and a decline in availability," said **BDO Consulting** private equity practice partner Kevin Kaden, in an email.

The banks are, in fact, more focused on covenants than price when it comes to the middle market, where rates vary according to situational variables, according to another BDO executive.

"We are not seeing larger interest charges but tighter covenants," said private equity practice partner and leader Lee Duran, in an email. "Banks are pushing down leverage and increasing interest coverage ratios. Typically, however, with a mid-term loan, middle market borrowers are seeing about 400 basis points over prime."

Options are fewer for struggling companies toward the lower end of the middle market, according to J. Scott Victor, managing director of Philadelphia-based middle market investment bank **SSG Capital Advisors**.

"There've been a lot of Chapter 11 plans filed in the last 10 months where the bondholders or lenders are converting debt to equity – if the company is big enough and there is enough cash flow and if you have a good sophisticated lender group," Victor said.

"But when you have a typical asset-based lender in a distressed situation, you don't have the choice of restructuring. You either have a going concern sale either inside or outside of bankruptcy or you have a liquidation for the lower middle market companies with an asset-backed lender."

Mezzanine funds are also playing a bigger role in restructuring the debt of middle market companies than they were a few years ago, Pomona Capital's Granoff said.

Middle Market Buyouts

Aside from distressed investments, some private equity investors are stepping away from larger deals to focus on middle market companies.

"We find the mid-cap buyout sector much more attractive than large-caps, particularly in the United States and Europe, and we have focused our 2010 tactical buyout allocation to this area," **Neuberger Berman** said in its 2010 private equity allocation report. "The current environment presents opportunities to buy sound businesses at lower cash-flow multiples, and activity in this realm is more robust than for larger deals, as financing for smaller transactions is easier to obtain than it is for large and mega-cap deals."

Baird's Welnhofer sees leverage multiples increasing at a surprising pace in this arena, after credit markets were mostly shut down a year ago.

"In 2007, PE shops were used to getting seven times leverage on certain kinds of transactions," he said. "And today, even though things have come back quite a bit, the high water is five times. We already traced our steps back to five times. We're like we were in 2006, so it's getting frothy."

Paul Springer may be reached at paul@dealflow.com.

Continued from front page

Chapter 11 filings from lower middle-market to large companies tail off recently, he does not think it's a long-term trend.

"We saw the crest of the wave hit in late 2008 through 2009," he said. "Now we're seeing that trough before the next wave hits. We're going through a lull in this bankruptcy cycle. We're just between waves. It's not a bad thing, as many bankruptcy firms were exasperated. It kept a lot of people busy."

Craig Barbarosh, an attorney with **Pillsbury Winthrop Shaw Pittman**'s bankruptcy and restructuring practice, said the law firm has seen a decline in large company filings, but the firm is still quite busy.

He also expects a serious commercial real estate meltdown to occur by the end of the year.

"We're slowing down on Chapter 11 filings on the operating side, and we're in the early stages of Chapter 11 filings on the commercial real estate side," Barbarosh said. "The next wave of bankruptcies will be commercial real estate with a strong focus on commercial mortgage-backed securities loans.

"There are a lot of CMBS loans in default or restructuring right now," he said. "A lot of loans will begin maturing next year that lack sufficient cash flow, have insufficient valuation, and will need to be refinanced. We're still at the early stages of the commercial real estate meltdown, but it has started."

Defaults on loans included in CMBS have escalated this year, and could exceed an overall default rate of 11% by the end of the year, credit rating agency Fitch Ratings recently forecast. Last year, 1,464 CMBS loans totaling $17.75 billion defaulted, which is more than the cumulative number of defaults from the inception of the CMBS market in 1991 through 2008.

Barbarosh said to expect commercial real estate Chapter 11 filings to accelerate as lenders get more aggressive in trying to collect their collateral.

"Hospitality and office properties are going to be hit pretty hard," he said. "With vacancies rising and rents falling, there's not sufficient cash flow to cover the loans. Defaults and delinquencies on commercial real estate will lead to Chapter 11 filings."

The expectation that bankruptcies will pick back up is not universal, however.

Kenneth Simon, a managing director in **Loughlin Meghji + Co.**'s bankruptcy and restructuring advisory practice, thinks the slowdown will continue through the end of the year as commercial real estate and other lenders continue the practice of amending loan terms and extending maturities to avoid delinquencies, defaults and foreclosures.

"As a result of lenders amending and extending loans, I believe there will be a slowdown in the number of bankruptcy filings," said Simon.

But Barbarosh thinks the slowdown is ending now.

"We're starting to see a lot of deals in pre-workout mode," he said. "It should accelerate over the next several months as commercial real estate filings begin."

Mark Thomas, an attorney in the **Proskauer Rose** law firm's bankruptcy and restructuring practice in Chicago, said he thinks that Chapter 11 filings will increase again because of a lack of liquidity for commercial real estate and middle market companies.

"Last year, we had an unprecedented number of filings," he said. "Things were hectic in 2008 and 2009. Then we had a natural slowdown."

Although, there has been a drop-off in Chapter 11 filings, Thomas expects a resurgence in filings later this year.

"It will depend on how much liquidity there is in the market for middle market companies," he said. "There has been more liquidity for large companies, but middle-market companies are still struggling to get liquidity. For loans written in 2007 that are coming due this year, will companies be able to refinance? I think there will be more commercial real estate bankruptcies this year.

"Looking at bankruptcies industry by industry, the automobile industry had its shakeout," Thomas said. "The airlines had their shakeout. Newspapers have gone through their cycle. I'm not sure there are more newspaper bankruptcies out there. There is a lot of commercial real estate that is overleveraged and needs to be fixed with values down and maturities coming."

Brandt, who has been in the bankruptcy and restructuring business for almost 35 years, said that this bankruptcy cycle is moving from busy to slow and back to busy. The weak economy and commercial real estate distress could make the next wave severe, he said.

"If you look at the economy per se, it's not a good place to be right now," Brandt said. "I think the next wave is going to be a big one. One big wave has broken. Now, one has to wonder how big the next one will be and how fast it will hit the beaches."

Kirk O'Neil may be reached at kirk@dealflow.com.