

The Deal Pipeline

[\[RETURN TO ARTICLE\]](#)

Bankruptcy

Share Reprint Save to My Articles

Neck and neck

By [Jamie Mason](#) Updated 04:22 PM, Dec-14-2011 ET

Surviving the rough-and-tumble bankruptcy auctions of 2011 took serious staying power.

A combination of fewer deals, more liquidity and strategic and financial buyers re-entering the market resulted in auctions professionals variously describe as rigorous, robust, spirited and intense. In 2011, stalking-horse bidders often didn't win auctions, or they were forced to pay more to win the assets.

"The gap between the stalking-horse offer and the ultimate purchase price has increased like never before," bankruptcy lawyer [David Heller](#) of [Latham & Watkins LLP](#) says.

As an example, after almost 11 hours of bidding, Hussey Copper Corp. was sold in November to competing bidder [Patriarch Partners LLC](#) for \$107.75 million. Lead bidder Kataman Metals LLC initially had offered \$88.7 million for the maker of copper products.

The purchase price for [Graceway Pharmaceuticals LLC](#) increased by 65% during its auction, rising from \$275 million to \$455 million. And SSI Group Holding Corp. sold its Souper Salad restaurant chain for more than 2 times the stalking-horse price after a seven-hour auction, where the price rose from \$1.6 million to \$4.2 million.

Such large gaps between stalking-horse and winning offers, Heller says, are a sign of the times.

"People don't know if they are going to get up one morning and find out that the bottom has fallen out the capital markets," he says. As a result, companies are willing to take a lower lead bid. "There is a premium on a floor offer and a safety net," he concludes.

Historically, stalking-horse bidders win most deals because they are the most aggressive throughout the process, but in the past 24 months there have been more active auctions, and the stalking horse is not always coming out on top, investment banker [Matthew Karlson](#) at [SSG Capital Advisors LLC](#) says.

According to The Deal Pipeline, the percentage of stalking-horse bidders winning bankruptcy auctions has remained stable at about 76% since 2007. But in 2011, it plunged to 68%.

Looking at the big picture, total sales have declined this year, while volume has increased, boosting the average deal size nearly 73%.

Through Dec. 2, buyers of assets in bankruptcy court had spent \$10.5 billion in 181 announced deals, compared with \$8.13 billion in 242 deals over the same period a year earlier. (Withdrawn sales were not included in these numbers.)

"The sheer number of auctions was down because the number of cases were down, but as a proportion, there were more sales than reorganizations," Heller says.

"I think this clearly has been a slower year, but the sales that have occurred have drawn tremendous interest," says Heller, who was debtor counsel to Graceway Pharmaceuticals. Heller adds that fewer deals meant more competition at the auctions that did occur.

He points to the middle market as the hot spot for bankruptcy mergers and acquisitions.

Michael Goodman, an investment banker at middle-market advisory firm SSG Capital Advisors, agrees, saying SSG had its busiest year ever in 2011.

According to Goodman, in 2008 and 2009, banks were reluctant to push companies into bankruptcy protection because their own balance sheets were distressed and they couldn't afford big write-downs. This led to more reorganizations, since banks needed to stay in the deal as there weren't other options available.

In the past two years, however, banks have felt more comfortable taking write-offs for select transactions where there was leverage available, Goodman says.

"There is a lot more liquidity, there are private equity dollars in the market, strategic buyers are more comfortable with their own operations and have more cash to deploy," colleague Karlson adds.

Private equity funds are anxious to put their money to work, and strategic buyers are anxious to re-establish their growth deals, Goodman says.

Bankruptcy lawyer **Scott Rutsky** of **Proskauer Rose LLP** agrees, stating there is a lot of money on the sidelines and distressed value players out there who want to maximize their return on underperforming assets.

The robust M&A market in 2011 was driven in large part by low-cost financing, William Weinhofer says. The **Robert W. Baird & Co.** investment banker says available financing is driving prices up, and assets are generally being sold on the high end of reasonable valuations.

"There is simply a lot of liquidity available to finance transactions, and this is fueling prices, which in turn is fueling high sale activity," he says.

Heller points out that strategic buyers are willing to release more dollars in auctions because a company may be worth more to them than it would as a pure financial play.

"The consolidation in various industries has returned for a host of reasons. People are seeking the synergies

and efficiencies that come from those," Heller says, adding that he is hearing the word "rollup" like he never has before.

Still, some of the most active auctions in 2011 were for companies' intellectual property, both brands and patents. The largest deal was for the patent portfolio of **Nortel Networks Inc.**, which fetched \$4.5 billion.

The Nortel IP auction began with a \$900 million lead bid from **Google Inc.** and ended four days later with the winning bid for the 6,000 patents from **Apple Inc.** and Rockstar Bidco LP, a consortium of **Microsoft Corp.**, **Sony Corp.** and other buyers.

According to Rutsky, in many cases the IP became the crown jewel of the auctioned assets. IP is popular with buyers who don't want the infrastructure of a business but think there is a viable brand that can be used in another platform, he says.

Gabe Fried, founding principal of IP consulting firm Hilco Streambank LLC, says his firm was only involved in one IP auction in 2011, for **Tavern on the Green LP**, where the firm received no competing bids.

More typical was **Borders Group Inc.**, which sold its IP to five different bidders for a total of \$15.77 million after roughly 40 rounds of bidding.

Berklene/BenchCraft Holdings LLC received more than 400 bids for its intellectual property. Stalking-horse bidder **Ashley Furniture Industries Inc.** was forced to increase its bid from \$850,000 to \$6.07 million to win the auction.

Finally, **Circuit City Stores Inc.** sold its remaining patents to Innovative Video Security LLC for \$6.03 million. Imaging Transfer Co. LLC had kicked off the battle among seven bidders with a \$750,000 lead offer.

Fried says consumer product companies are often reluctant to engage in big M&A transactions because they have limited appetites for large integration projects. They still may desire the brands of bankrupt companies, however, because their names, customer lists and Internet sites can carry a strategic advantage.

On the patent side of IP, bidders can have three motives, he explains. First, patents provide a company with a lower-cost alternative to engineering its way around an existing patent. Second, they aid both offensive and defensive litigation, and protect against a company potentially being sued if it is doing something that violates a patent. Third, a company can license the patents and thus enhance its income stream.

Bankruptcy professionals agree that there won't be a slowdown in M&A any time soon.

"In 2012, there will continue to be a high number of [Section] 363 sales because they have become the most common and expedient way to auction and cleanse even a moderately distressed company," Heller says. "This will continue to accelerate until the judges decide to implement strict rules that there should only be a sale if there is no meaningful alternative."

Goodman, though, notes that the health of lending institutions and their willingness to absorb more losses will shape the deal landscape of 2012. Banks have been deteriorating in recent months because of exposure to Europe and might be less likely to realize losses in a forced sale.

— *Jamie Mason*

Share Reprint Save to My Articles

[Privacy](#) | [Terms and Conditions](#) | [My Account](#) | [Contact Us](#)

@Copyright 2011, The Deal, LLC. All rights reserved. Please send all technical questions, comments or concerns to the Webmaster.