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# Creating Value By Investing In Distressed Assets

The difficult economic environment and recent severe dislocations in markets for stocks, bonds and other financial instruments present investors with opportunities to acquire distressed securities and businesses at bargain prices. We see three particularly important opportunities for private equity, hedge funds and other significant pools of capital:

Acquisitions of securitized instruments, whole loans, derivatives and structured credit products.

Acquisitions of distressed real estate assets and related debt.

Acquisitions of operating businesses likely to be divested by financial institutions.

Although opportunities in the distressed sector are likely to be plentiful, identifying the best opportunities and designing and implementing the optimal transaction structures and strategies will require significant expertise. Successful investors will need to navigate a complex array of contractual rights, financial structures and bankruptcy and regulatory issues to unlock value. Cadwalader assists sophisticated investors by providing an integrated distressed asset advisory team, including a prominent full service financial restructuring practice, leading private equity and M&A practitioners and attorneys with highly specialized structured products and securitization expertise.

Cadwalader played the preeminent role among law firms in structuring and documenting securitized instruments, whole loans, derivatives and structured credit products.

Cadwalader, as one of the leading law firms in real estate finance, played a central role in many of the largest and most complex recent real estate transactions, including Equity Office Properties, Hilton Hotels Corp. and Macklowe Properties.

Cadwalader is currently serving as a leading adviser on many of the most significant matters that have arisen as a result of the credit crisis, including advising Bear Stearns Cos. in its acquisition by J.P. Morgan Chase & Co., and more than 20 parties-in-interest in the bankruptcy of Lehman Brothers Holdings Inc.

## Acquisition of financial products

Investors will be presented with attractive opportunities across a variety of complex, difficult-to-value assets (such as CMBS, RMBS and other instruments covered by the Troubled Asset Relief Program, or TARP). Key factors driving value creation in this sector include the following:

**Lack of fungibility.** These products are highly customized. Structures, covenants, inter-creditor rights and underlying assets vary significantly. Cadwalader's experience in structuring these products uniquely positions us to assist our clients in evaluating the dense documentation governing these instruments to identify unique investment opportunities.

**Financing alternatives.** Creative financing structures are being

developed to encourage private pools of capital to acquire TARP assets. Investors will have the opportunity to create value by pursuing joint venture structures with selling financial institutions, the Treasury Department and other third-party bidders pursuant to which risk and upside is shared among the parties.

**Exit strategy.** Many of these assets must be amended, restructured, managed and/or repackaged before they can be resold. Investors will have extraordinary opportunities to create value by developing and implementing creative exit strategies.

## Acquisition of distressed real estate assets

Investors with a clear understanding of legal rights in complex real estate financings, foreclosure proceedings and the bankruptcy process can employ a variety of strategies to acquire real estate at bargain prices.

**Fulcrum security.** Investors can purchase debt or equity at the appropriate level in the capital structure and use contractual rights to acquire the underlying real estate assets. There are a variety of techniques for implementing such a strategy (including proposing a consensual plan of reorganization and using debt claims to "credit bid" in an auction process).

**Separation of real estate.** Operating companies in distress may have real estate assets that have a higher value when separated from a bankrupt or underperforming operating company. Investors can unlock significant value by implementing effective strategies to separate real estate assets.

**Bankruptcy process.** The bankruptcy process affords investors the opportunity to acquire real estate projects free of burdensome liabilities.

## Acquisition of operating businesses in the financial sector

In the wake of the recent financial crisis, several significant financial institutions have announced their intention to sell operating businesses to raise capital. We see this trend accelerating and anticipate that a range of businesses in the financial sector, including finance companies, asset managers, mortgage origination platforms and insurance businesses, will be priced attractively. These opportunities create a challenging legal issues for investors.

**Regulation.** Many of these businesses are subject to stringent federal and state regulation. Only investors with in-depth knowledge of such regulatory restrictions can appropriately value such businesses and execute on a transaction.

**Liabilities.** For certain financial businesses, identifying and isolating liabilities is essential to realizing value. Creative strategies are being developed to isolate liabilities, including using a separate structure to "ring fence" specified assets.

**Carve-Out Issues.** Separating operating businesses from large financial institutions can create difficult issues regarding the ability of such businesses to operate on a standalone basis. Investors and their advisors must have an intimate knowledge of how such businesses operate to ensure that a "carve-out" transaction is structured properly.

Cadwalader has the private equity, M&A, financial restructuring and regulatory expertise to help investors take advantage of these opportunities and implement effective acquisition and financing strategies.

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