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Fiat/Peugeot Merger and Samson Resources M&A Demonstrate Post-Bankruptcy Events Can Drive Profitable Opportunities

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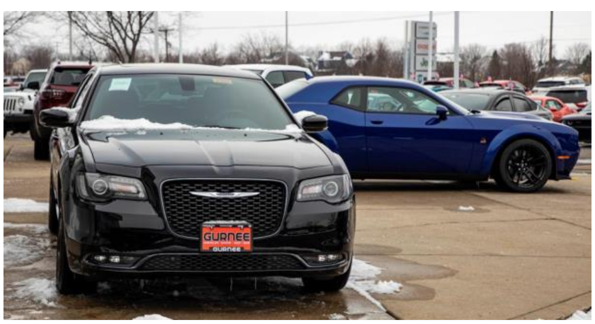
Last year was a difficult one on so many levels—from the onset of the COVID-19 pandemic, through a rancorous national election and on through the end of the year. It was an active one for distressed securities investors as many companies, particularly those already saddled with heavy debt loads, made moves to come to terms with creditors and, failing that, filing for Chapter 11 protection. A complex bankruptcy can take years to resolve, presenting many opportunities along the way to invest in distressed securities (before, during, and after distress.) Events like spinoffs, mergers, and special dividends can help generate the final gains at the tail end of a distressed securities investment cycle.



Samson Resources is coming to the end of a 10-year cycle dating to shortly after it was taken private by KKR in a $7.2 billion LBO in 2011 – this was the largest oil & gas leveraged buyout at the time. Four years later, it was forced into Chapter 11 making it the largest energy company bankruptcy of its day. It emerged from reorganization in 2017 after eliminating $4 billion in debt and, since then, has paid numerous special dividends (over $13.00/share between 2017-19) to its new shareholders who were former creditors. On January 4, Samson announced the sale of all its remaining Powder River Basin oil reserve assets for $215 million. The company will use the proceeds to pay off approximately $13 million in debt and then make a final special dividend (estimated at over $8.50/share) to shareholders. The deal will close in early March with Samson then beginning its final dissolution.

The Samson Resources story shows the full evolution of a distressed company – from the leveraged buyout stage by private equity and through bankruptcy – with former creditors receiving the new post-reorganization equity. It also shows that, even in a difficult market for the energy industry, a patient distressed securities investor who buys the right asset at the right time can profit, in this case by receiving liquidating special dividends over the years.

Another new year development that can be traced back to a major bankruptcy is the closing of the merger between Fiat Chrysler Automobiles NV and PSA Group, the European automaker whose largest brand is Peugeot. This combination will create the fourth largest automaker in the world with an annual sales volume of more than 8.5 million vehicles.

Chrysler was an iconic American company which was forced into bankruptcy in 2009 during the great financial crisis. By reorganizing this way, it was able to eliminate $20 billion in balance sheet debt which allowed Fiat to acquire it at an extremely attractive price ($0)! It was also the first ever corporate bankruptcy announced by an acting U.S. president. Chrysler serves as an excellent example of how companies can come out of distress much stronger and in a better position to compete. Over the years since then, Fiat spun off to shareholders its profitable Ferrari business (ticker: RACE) and also paid over €3 billion in special dividends.

The merged Fiat Chrysler/PSA Group entity with a roster of 15 vehicle brands will be renamed Stellantis NV. Its management expects the combination to produce over €5 billion in annual savings. Fiat Chrysler shareholders will also receive another special dividend (€3 billion) before closing. Like Samson, the Chrysler story shows how a company can evolve after distress and how subsequent catalytic events – like spin offs, special dividends, and M&A – can provide opportunities for profit years after a bankruptcy.

Also related to historic auto industry bankruptcies is the Motors Liquidation Company GUC Trust (MTLQU) which was created to settle claims of unsecured creditors against GM. Those creditors were due to receive a mix of new securities—new GM stock as well as two classes of warrants when it emerged from bankruptcy. The challenge was that the total size of the creditor pool was unknown at the time but was estimated to be as high as $300 billion. Many of these claims were disputed so a trust was set up for the benefit of GM's old unsecured creditors. Over the years, attorneys reduced the size of the total claims against GM, and, with each successful reduction, the trust made special dividends of cash and/or securities. The Motors Liquidation Trust recently settled its remaining claims which allowed it to pay out another large special dividend. That represents an additional favorable post-distress catalyst for an auto industry case which has been ongoing since 2009.

As noted at the top, 2020 was a very active year for distressed investing in general. Some companies liquidated entirely, some restructured their debt and others are still working their way through the process. Default rates have ticked down recently but there remain numerous very large bankruptcies, like Chesapeake Energy and Hertz, that are still winding their way through the court system.

For 2021, there will continue to be many opportunities for distressed securities investors because of elevated levels of debt outstanding. The economic recovery is taking place more slowly than many anticipated so, for those firms with tight loan covenants or insufficient liquidity, it will be tough to continue without addressing their liabilities through bankruptcy. The potential for a significant number of bankruptcies this year will therefore likely preset many opportunities for short selling companies as they run out of financing options.

Investors can also capitalize on companies in distress by buying their distressed debt at pennies on the dollar during times of heightened uncertainty. However, sometimes the best payoffs in distressed investing come from investing in late stage "post-distress" trades which focus on equities issued by firms that formerly reorganized. That trade can generate event driven returns due to special dividends, spinoffs and M&A as shown in the Samson, Chrysler and GM examples above.

2021 will be a year with many possibilities for distressed investors but, as these examples show, to succeed in this specialized field requires diligent research, an understanding of different markets and an ability to be nimble by investing before, during or after distress.