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Hallwood Rescue Projects Earn Respect But Tough Negotiating Methods Draw Criticism

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Ten years ago, while lounging near a Beverly Hills, Calif., swimming pool, Anthony Gumbiner and Brian Troup would scan the annual reports of 17 troubled companies on their "hit list." They eventually chose five salvageable real estate companies and during the next few years took them over.

So began Hallwood Group Inc., an international merchant banker with British roots, based now in Cleveland. Publicly traded on the New York Stock Exchange only since 1984, the increasingly profitable company has earned a reputation for toughness for the way it restructures nearbankrupt companies. Rather than . liquidate them, Hallwood makes them solvent, even if shareholders and management are sometimes bruised in the process.

Hallwood's latest coup, the restructuring in June of Brock Hotel Corp., the Irving, Texas-based operator of Holiday Inns and owner of Showbiz Pizza Time Inc. restaurants, could provide more exposure for Hallwood, which has fewer than 60 employees. Hallwood erased $138 million of Brock's debt with a $40 million cash infusion as the company teetered near bankruptcy "This Brock Hotel deal should help Hallwood's credibility and profile immensely," maintains Jeffrey Kessler, an analyst at Cowen & Co.. New York.

Before the Brock transaction, Hallwood successfully restructured the five initial debt-ridden real estate investment trusts and, later, Saxon Oil Co., a Dallas-based independent oil driller, in 1984. Analysts say Hallwood's next targets for such rescues will be ailing financial institutions.

In fiscal 1985, Hallwood earned $6.2 million, or $1.40 d share. Mr. K essler says per-share earnings could total $1.30 for the fiscal year ended last Thursday and $'.10 for fiscal 1987 before tax benefits from carry-forward of net operating losses. The company has $65 million of tax-loss carry-forward to shelter future earnings.

He characterizes as strong Hallwood's cash flow from operations, including real estate sales, at a projected $2.75 a share for fiscal 1986 and $3.90 for fiscal 1987. Mr. Kessler believes the stock, which closed in composite trading yesterday at $19.25 a share, is undervalued. And he says the stock is trading at about a 30% discount from net asset value.
But Hallwood hasn't found it easy to gain respect from U.S. investors. One reason is that it has relied heavily on European and Japanese underwriters and is just beginning to use U.S. institutions as underwriters. Another is the irregular timing of its rescue-financing projects.

To produce steadier earnings, Hallwood has begun underwriting rights offerings for small growth companies. It also boosted its stock price, to attract institutional investors, by declaring a 1-for-14 reverse stock split in February. Mr Kessler believes those changes should help Hallwood overcome "anonymity among investors "
Hallwood's chief driver, as its chairman and chief executive officer, is Mr. Gumbiner, a flamboyant, 41-year-old Englishman who races Formula One speedboats for a hobby and works from his Monte Carlo apartment overlooking the Mediterranean. As Hallwood's president, Mr. Troup, 39, a soft-spoken Scotsman, tracks faltering companies from a personal computer at his 150-acre Scottish Highlands farm, where he raises deer and pheasant.
The two tapped Cleveland as their base because that's where Twenty Seven Trust Hallwood's initial U.S. real estate management and liquidation team, was based. Its institutional backers are in London and Japan, Switzerland and the Netherlands.

The partnership began about 15 years ago when the two men began buying publicly held, but unquoted, British companies. As a hobby, the reticent Mr. Troup scoured historical files at a central registry in England and found about 6,000 old companies, formed between 1850 and 1950, whose stock had been handed down among family members. The stock rarely traded, and as a result its price didn't reflect the escalating value of the assets the company controlled. Recognizing an opportunity, the partners would buy a majority of the stock of a company, usually at an estate sale, sell most of the assets and reap huge profits.

One such company was G.W. Dray & Son, a sleepy stationery company that sat on valuable property in the fashionable London neighborhood of Chelsea. Hallwood bought the company and its land for about $4.5 million, and recovered most of that by selling the business. Hallwood expects that once it sells the real estate, it will post a gain from the entire transaction of $10 million to $15 million.
In brief, what Hallwood practiced was asset-stripping, which often is contested and can be uglv. Mr. Gumbiner says Hallwood no longer does contested buys. "You do that when you're hungry," he says.

Instead, the two men turned to restoring companies on the verge of bankruptcy. And in the late 1970s, they switched their focus to the U.S. Aided by a proprietary computer program developed by Mr. Troup, they track about 400 troubled U.S. companies. "We want something just before Chapter 11," says Mr. Troup. "That way they have no alternative." From Cleveland, Hallwood continues to manage and develop properties from those initial REIT targets. But Messrs. Gumbiner and Troup now devote almost all of their time to restructuring. The Brock Hotel transaction typifies their approach
Last September, the Holiday Inn and pizza restaurant franchisee was in deep trouble. With a negative net worth of $27 million and $189 million

of long-term debt, Brock had few alternatives but to seek protection under federal bankruptcy law. Unbeknownst to Brock president Thomas Corcoran, Mr. Troup was compiling a restructuring plan, as well as calculations of what Brock, its creditors and its shareholders would be left with if it filed for bankruptcy-law protection. Mr. Gumbiner presented the figures to Brock and told the company dispassionately: "If you want us to save you, we want control of the board, 10% of the company's stock and, from the day you sign the engagement letter, you do what we tell you to do."

In return, Hallwood pledged to invest $40 million.

"Our first reaction was, 'Is this guy for real?' " recalls Mr. Corcoran. "I called a half dozen people in New York before I found anyone who knew them."

Hallwood was for real. Nine months later, on June 25, the transaction was comnleted and Brock had a positive net worth f $70 million.

It wasn't easy, and Mr. Gumbiner admits to arm-twisting. Hallwood worked out 300 distinct agreements with the 9,300 creditors, offering between 55 cents on the dollar-to the secured bank creditors, including Wells Fargo & Co.-and 12 cents, to unsecured banks and landlords. About 96% of the creditors accepted the deal, thus reducing debt to $35 million from $138 million.

Tough negotiating has earned Hallwood some sharp criticism. "It's Draconian," says Cowen's Mr. Kessler. Shareholders, including management, were "more or less wiped out," he said, noting that someone with 100 shares was left with four or five. One creditor who prefers anonymity said Hallwood, which didn't yet hold its stake in Brock, was in a position of power and could freely twist arms. "We're hardly ecstatic about them," he said. Brock's Mr. Corcoran, however, calls Hallwood "an angel."

To raise the $35 million to pay Brock's debt, Hallwood offered Brock holders the right to purchase deeply discounted shares of the restructured company. Rights not purchased by holders were sold to international investors backing Hallwood and in effect acting as sub-underwriters. Hall wood ended up with about 14% of Brock's stock, and Messrs. Gumbiner and Troup vow to keep the stock for five years and stay on the board until voted out.

"We're the last alternative before the guy jumps off the windowsill," says Mr. Gumbiner. "But I think we're a much better alternative to bankruptcy."