DEAL OF THE WEEK

andrew.woodman@incisivemedia.com / tim.burroughs@incisivemedia.com

IMM, Mirae forge POSCO steel investment

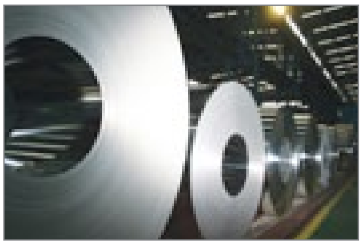
POSCO STAINLESS STEEL (PSS) CAME into being 1997 when steelmaker POSCO bought most of manufacturing facilities of Sammi Specialty Steel, one of a host of Korean corporates struggling to service its debts in the midst of a credit crisis.

Just over 15 years on the wheel has come full circle. POSCO – faced with falling profits and consolidated debts of KRW39.6 trillion ($35.3 billion), as of March – has been forced to sell off part of PSS. After an attempted $424 million IPO was abandoned last December following a downturn in the steel industry leading, POSCO turned to financial investors.

Enter IMM Private Equity and Mirae Asset Management, which together acquired a 24% stake in the company last week for KRW250 billion ($223.6 million). Each is putting in KRW125 billion, subscribing to 8.6 million convertible preference shares with a conversion price of KRW29,000 per share and a maturity of five years. The deal values the company at around 7x EBITDA.

"This is a classic special situation investment opportunity for us," says Jay Kim, vice president at IMM. "PSS was looking to secure more than KRW250 billion but there were not many Korean GPs who could take up such an offer. We were invited with Mirae to look at the deal and it took just a few months before we decided to invest."

PSS, which has its main factory in Seoul, produces stainless steel, tool steel and special alloy steel with an annual capacity of 960,000 metric tons. It supplies the automotive, aviation, shipbuilding and electronics industries. The company wants to achieve a capacity of 2.5 million tons by 2020 with turnover reaching KRW4.5 trillion.



POSCO SS: Forging ahead

Capital is required to meet this expansion target. PSS invested more than $1 billion in its Korean operations – it wants to move up the value chain into more specialized steel products – and has also entered Vietnam, with the POSCO SS-VINA steel mill opening last year.

"We anticipate the Vietnam operation will become the second or third biggest player in the country by capacity. Once the business stabilizes, it is expected the subsidiary will be half the size of the Korean operation," says Kim.

PSS has been actively enlarging its regional footprint since 2008, opening offices in China, Thailand and Japan. Its client base spans Europe, North America, the Middle East and South Africa, as well as Asia.

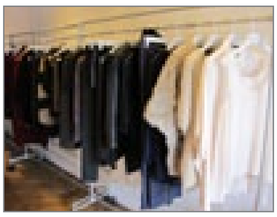
IMM hopes get an attractive valuation when it exits the company via IPO in the next 4-5 years, once the global steel industry recovers. "PSS had already passed its initial conditions to get listed so when the time comes we believe listing will be easy," Kim says.

IMM's investment comes from its second fund, which closed at KRW756 billion in December 2012. With this latest transaction the vehicle is just over 50% deployed.

CDH, Belle to make Baroque big in China

SECONDARY DIRECT DEALS FREQUENTLY stumble on valuations. Private equity investors are sitting on either side of the table and both are hardwired to get the best possible price; the lingering fear is leaving the table with a deal that is either significantly underpriced or overpriced.

External factors also play a role – a PE firm may be under pressure to return capital to investors or an investment team might be suffering a dry period in a particular geography and keen to get a deal done.



Baroque: Exporting style

In the case of apparel Baroque Japan, which was majority-owned by CLSA Capital Partners, it came down to the buyers' expectations for growing the business outside of its domestic market. Convinced that they could expand the apparel company in China faster and on a larger scale than the company was planning, CDH Investments and its strategic partner Belle International, China's leading women's shoe retailer, were comfortable with the price.

"The plan was to open 30 stores in China over a three-year period and this growth was factored into the selling price. But CDH brought in Belle to help with the due diligence and they said they could open 300 stores in three years," a source familiar with the transaction tells *AVCJ*. "In this context, the valuation became more attractive."

CLSA acquired a 54.94% stake in Baroque six years ago via its 2006 vintage CLSA Sunrise Capital Partners fund and backed its expansion to nearly 350 stores. With the vehicle winding down an exit in some form or other was looming.

Hong Kong-listed Belle has agreed to buy 31.96% of Baroque for $93.96 million. CDH, which is also an investor in the shoe retailer, is picking up the remainder. Based on the valuation of Belle's portion, the private equity firm is paying $67.62 million. Following the acquisition, Belle will support Baroque in China through a series of joint ventures, taking its overall investment to no more than HK$924 million ($119 million).

"It's a growth story, but it's not just about betting on GDP growth," the source adds. "Baroque is going into malls in China and Belle can say we want this space or we will pull out our seven other stores. Japanese management couldn't do this on its own."

The Belle growth story has been remarkable, driven by sportswear as well as shoes. In 2006, the year before it went public, the company generated RMB6.2 billion ($1.01 billion) in revenue and RMB976.6 million in net profit from 5,300 self-managed retail outlets. As of 2012, the network had grown to more than 17,500 stores; revenue was RMB32.9 billion and net profit came to RMB4.3 billion.

Now, though, Belle expects a prolonged phase of structural rebalancing and moderate growth, and it has identified e-commerce, mass-market brands and multi-brand stores as the way forward. Baroque's stable of brands – which offer exposure to the fashion apparel space and a following among young female consumers – are seen as a good strategic fit.