Seong-Ho Cho[1]

LBO TAKEOVER: KUMHO ASIANA – KOREA EXPRESS CASE STUDY*

This paper examines the case of the largest Korean LBO acquisition by Kumho Asiana Group (a Korean chaebol) over Korea Express Co, Korea's #1 logistics company. The paper explores two important issues. First, was the bid of 4.1 trln won reasonable? Second, how well was it structured to finance the deal? In the acquisition amount of 4.1 trln won, more than 50% (2.4 trln) was financed through commercial borrowings such as bank loans and exchangeable bonds (XBs). This paper examines the Kumho Asiana's exit strategy to recover from heavy debt load. The actual net cash paid for the acquisition (3.4 trln) was effectively reduced via this exit plan (1.5 trln via capital reduction and 1.2 trln via XBs).

Keywords: *LBO; exchangeable bonds; chaebol; bank loan; debt exit strategy.*

Сеонг-Хо Чо

ПОГЛИНАННЯ КОМПАНІЇ ШЛЯХОМ ВИКУПУ КОНТРОЛЬНОГО ПАКЕТУ АКЦІЙ ЗА ДОПОМОГОЮ КРЕДИТУВАННЯ: АНАЛІЗ КЕЙСУ KUMHO ASIANA – KOREA EXPRESS

У статті детально проаналізовано процес поглинання логістичної компанії "Korea Express" південнокорейським чеболем Kumho Asiana. Аналіз проведено відносно двох центральних питань. 1) Чи була економічно обґрунтованою ставка у 4,1 трлн вон?; 2) Наскільки вірною була фінансова структура проведення даної угоди? Понад 50% від суми угоди (або 2,4 трлн вон) було фінансовано шляхом банківського кредитування та облігацій. Проаналізовано стратегію, за якою у подальшому чеболь Kumho Asiana погашав свої боргові зобов'язання.

Ключові слова: *викуп контрольного пакету акцій; облігації, що конвертуються; чеболь; банківський кредит; стратегія погашення заборгованості.*

Рис. 3. Табл. 12. Літ. 10.

Сеонг-Хо Чо

ПОГЛОЩЕНИЕ КОМПАНИИ ПУТЁМ ВЫКУПА КОНТРОЛЬНОГО ПАКЕТА АКЦИЙ ПРИ ПОМОЩИ КРЕДИТОВАНИЯ: АНАЛИЗ КЕЙСА KUMHO ASIANA – KOREA EXPRESS

В статье детально проанализирован процесс поглощения логистической компании "Korea Express" южнокорейским чеболем Kumho Asiana. Анализ проведён относительно двух центральных вопросов. 1) Была ли экономически обоснованной ставка в 4,1 трлн вон?; 2) Насколько правильной была финансовая структура проведения данной сделки? Более 50% суммы сделки (или 2,4 трлн вон) были финансированы путём банковского кредитования и облигаций. Проанализирована стратегия, по которой в дальнейшем чеболь Kumho Asiana погашал свои долговые обязательства.

Ключевые слова: *выкуп контрольного пакета акций; конвертируемые облигации; чеболь; банковский кредит; стратегия погашения задолженности.*

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Background. On September 3rd, 2007, Korea Express Co. (Korea Express) got approval for its equity sale from Seoul Central District Court. Since 2000, Korea Express had been under chapter 11 due to its parent company's obligation to creditors. As a habitual practice which was then prevalent in Korean business, Korea Express guaranteed on behalf of its parent company Dong-Ah Construction Co. when they borrowed from financial institutions or issued corporate bonds. In October 2000 it was put under chapter 11, Korea Express's debt guarantee for Dong-Ah Construction Co. was 870 bln won.

Dong-Ah Construction was put under work-out process in 1998, but failed to survive. Accordingly, its subsidiary, Korea Express, was dishonored on November 1st 2000. Rather than imposing liquidation, the court decided to preserve the assets of Korea Express on November 7th, 2000 until December 31st, 2010 on the basis of the belief that its continuing value was far greater than its liquidation value. Since then, the company had managed to normalize its operations and financial conditions. In early 2007 the court began considering its disposal through M&A because a successful M&A would give Korea Express a chance to reborn after paying all its debt obligations to creditors. On September 3rd, 2007, the court approved the equity sale of Korea Express through an M&A.

History. In 1930 Korea Express Co. was established as Chosun Rice Warehouse Co., Ltd. In 1957 they went public and acquired Korea Transportation Co. In 1963 they changed the company's name to Korea Express Co. Since then, Korea Express has maintained its position as a Korea's #1 logistics company despite recent turmoil. In 1968 the company became an affiliate to Dong Ah Group through government privatization. Despite its market leader position, it fell under court receivership for corporate reorganization in November 2000 from excessive guarantee issuances to its parent company, Dong Ah Construction.

Market Leader. Despite recent court receivership, Korea Express was a leading company with almost 80-year history, large infrastructure and equipment. It provided high-quality logistics services based on know-how and technology gained from its long experience. In 2006 Korea Express's market share was 36.7%, and there was a big gap (11.5% point) with the second largest company, Hanjin. In terms of revenue Korea Express was 1.6 times ahead of Hanjin, and had maintained this stance for consecutive 10 years (Figure 1). The revenue was 1,267 (1,170) bln won in 2007 (2006), while its operating profit was 63 (60) bln won. Its debt-to-equity ratio was 104.2%, and the company's bond rating was credit A-.

Business Scope. The main business of Korea Express was professional and multiple transportation systems, from inland transportation to sea transportation and air transportation. To maximize the synergy, it expanded its business scope including home delivery, rent car service, third-party logistics, house moving and environmental business. There were 6 business divisions: inland transportation, sea transportation, parcel delivery, distribution business, car rental and other operations. Among them, inland, sea, and parcel deliveries took up approximately 75% of the total revenues, and they were the core business of Korea Express.

Core Competencies.

Networks: Korea Express possessed core competencies both in land carriage and shipping. They closely linked major international cities with 40 nationwide branches and offices, 500 agencies and 200 international networks like a cobweb. In terms of networks, Korea Express was by far the industry leader. High-tech transportation devices, prompt, accurate and safe transportation system, and the integrity of its 6,000 employees were the driving forces behind Korea Express in creating its unique services. Korea Express was also well known as a pioneer in the shipping industry. They were active in 22 among 28 domestic harbors and had business know-hows and great infrastructure.

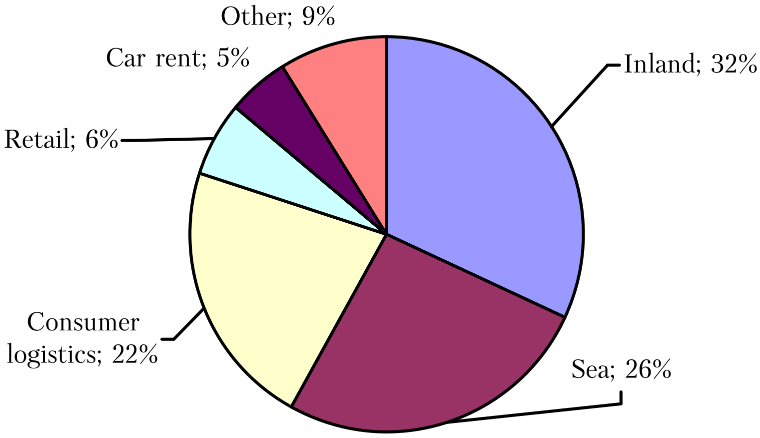

Figure 1. **Revenue Structure (2007),** *company's data*

People: Its employees had performed very high till lately since they were well-trained professionals. As a matter of fact, this company took a role of an academy in the domestic logistics, and it was well known that its employees were proud of their company. Although the labor union was active, they had a good relationship with the employer and there were no labor disputes for 47 years.

Real Estates: It possessed various valuable preemptive real estates in major cities of Korea. These real estate were valued about 830 bln won as of November, 2007. Most of them were located near rail road stations and express bus terminals.

Logistics Industry: High Growth Potential. Korea's domestic logistics industry fell behind the global performance in terms of efficiency, as can be seen in Figure 2. Korea lacked in infrastructure and the regulations were yet to become sufficient. Logistics cost per GDP was diminishing as the industry moved toward advancement, but was still high compared to developed countries. In 2004, Korea's logistics cost per GDP was 11.9% whereas the OECD average was 5–10%. The logistics cost per revenue for Korean manufacturing companies was 9.7% in 2008, which was above US's 7.5% and Japan's 4.8%. Such drastic figures were derived from the fact that Korean logistics was mostly on self-logistics and 2nd party logistics, with numerous small-sized companies also in the field, setting back the total potential efficiency. Therefore, the firms were paying too high logistics costs and this was weakening Korea's global competitiveness.

Korean government was actively promoting the logistics industry under the belief that logistics was the core for nation's competitiveness. With improved efficiency, logistics cost could be cut, which would further lead to strengthening corporate productivity. To enhance efficiency, the government was promoting 3rd party logistics through various tax support packages and encouraging M&A for conglomerates. 3rd party logistics took up approximately 42% of the total domestic industry, but was expected to go up to the 70–80% level as in advanced economies. Such government promotion and support would boost the size of the domestic logistics market.

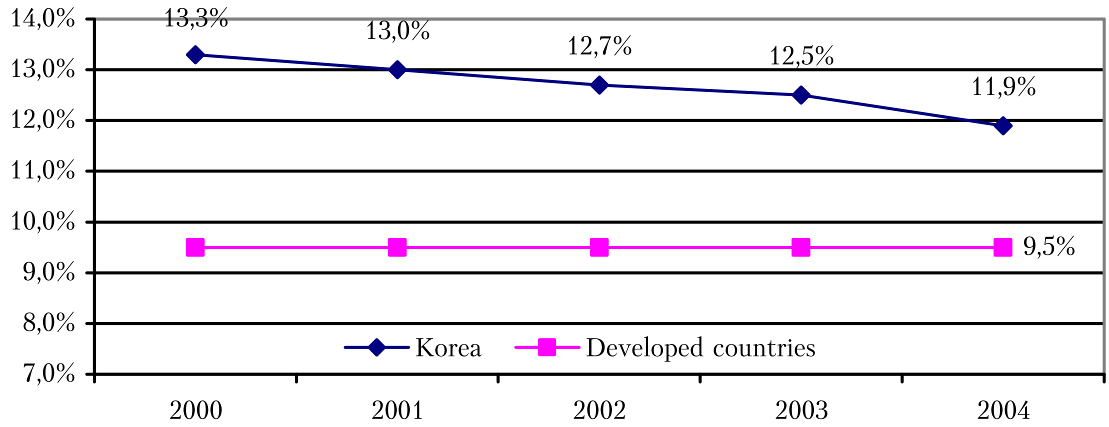

Figure 2. **Logistics Cost per GDP,** *author's construction*

FTA, geographic advantage, rapid growth of e-commerce and development of the third party logistics would boost domestic logistic industry's potential growth. The global container distribution quantity between continentals was expected to keep growing 7–8% annually. In the meantime domestic third-party logistic market was expected to grow rapidly with such a government support. Home delivery market was also expected to grow with expansion of e-commerce.

The most attractive target. Korea Express was considered as the most attractive M&A target at least for 4 reasons. First, acquisition of Korea Express would mean possessing the nation's largest integral logistics company. The logistics industry showed very high growth potential. As a market leader, it possessed competitive advantage over rivals in its business scope including inland transportation, sea transportation, parcel delivery, distribution business, car rental and other operations. It owned the largest networks and equipments, valuable preemptive real estate, and especially the best people in the industry. On the top of this, know-hows and technologies gained from its almost 80-year experience could provide top-quality logistics services to customers.

Second, Korea Express had achieved clean financial status through 7-year court management after bankruptcy. It was not common to see such a large net asset value (NAV) under the court resolution: its liabilities (360 bln won) were much smaller than its selling enterprise value (over 2.1 trln won). It was also expected that the cash of more than 2 trln would remain within the company after transaction. Furthermore, it was claimed that at least 1.5 trln won had been invested for developing new businesses or overseas network.

Third, the Libyan waterway construction project that was delayed since Dong Ah Construction's bankruptcy may be resumed. Finally, the revenue in 2005 increased by 4.74% from the previous year and marked positive figures in operating profits. The average ratio of operating profit to revenue during 2003–06 was 5.29%, whereas the average of 4 leading companies such as Hanjin, Sebang, Hansol CSN, and Dongbang was 4.52%. These recent accomplishments may show a signal for its turnaround.

Deal structure ordered by the Court. Korea Express was decided by the court to be sold to third parties by issuing 24 mln new shares, which is 150% of the outstanding 16 million shares. After new stock issuance, the total outstanding shares would become 40 mln and a bidder would own 59.8% of the total capital, which would be sufficient ownership from any hostile attempts by other shareholders.

If new shares were issued only 100%, Goldman Sacks would hold 12.97%, STX would hold 7.36%, and Kumho industry would hold 7%. The court believed that this weak ownership structure would cause undesirable dispute among shareholders, which was not the intent of the court. The court wished that once the creditors' debts were paid back, a new management shareholder could manage the company independently from the old shareholders.

The court also decided the minimum bidding price was 97,300 won per share, therefore the least bidding price to be 2,335.2 bln won for a company with 360 bln debts. The court decisions on paid-in capital increase of 150% rather than 100% affected to increase the takeover minimum price to 2,335.2 bln won from 1,556.8 bln. Specifically, the court ordered the deal to be done via increasing paid-in capital and details were summarized as follows:

- Issuance of new stock: 24 mln shares:
  - Acquirer had to purchase 59.8% of the capital stock after the merger;
  - Court reasoned that 59.8% ownership was necessary for sustainable operation;
- Previous number of shares: 15,989,654.
- Total number of shares following new offering: 39,989,654.
- Minimum bidding price per share: 97,300 won.

Pre-competition for Korea Express shares (Toeholds). As its recent performance rebounded, there was competition at the market to buy Korea Express shares for the purpose of potential acquisition (toeholds) or financial gain. Since 2005, Goldman Sacks had purchased its shares up to 25.95% through their subsidiary, Triumph II Investments (Ireland). STX Pan Ocean, a subsidiary of STX group, had bought 14.73% shares, and Kumho had 14.11% shares. Other major shareholders included Seoul Guarantee Insurance Company (10.06%) and Korea Asset Management Corporation (7.13%). It turned out that some shareholders like Kumho and STX bought its shares for potential acquisition.

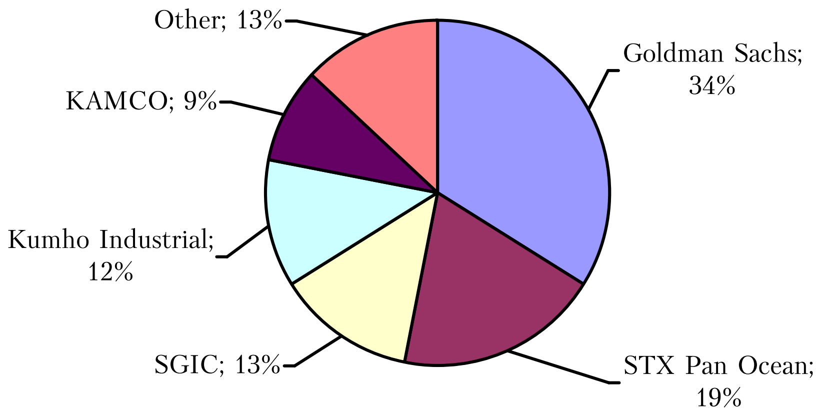

Figure 3. **Before Paid-in Capital Increase (16 mln shares),** *company's data*

The Bid. On December 11, 2007, 10 bidders submitted their LOIs, which included Kumho Asiana group, Hanjin group, GS group, Hyundai Heavy Industry group, LS group, CJ group, STX group, Hyosung group, Nonghyup, and Seoul Asset Management. Private Equity Funds (PEFs) rarely submitted LOIs because the court-proposed deal structure of 150% capital increase was too much of debt to finance. The court would like to prohibit pure LBO bidders because strategic buyers could bring more operational synergy to the target. For this purpose, the court did not allow the establishment of special purpose company (SPC) and the reduction of capital in a year after acquiring the target.

In January 2008, 4 bidders submitted their final offers for the bid. Their offer prices were as follows:

- Kumho Asiana group – 4,104 bln won.
- STX group – 4,300 bln won.
- Hyundai Heavy Industry group – 3,800 bln won.
- Hanjin group – 3,400 bln won.

Among these bidders, Kumho Asiana was finally selected as the preferred bidder. The consortium was composed of Kumho's daughter firms and non-Kumho affiliates. Kumho affiliated firms were Daewoo construction Co., Asiana airline Co., Kumho renter car Co., Kumho life insurance Co., Kumho P&B petrochemical, and Korea integrated freight terminal Co. Non Kumho affiliates included strategic investors (Hyosung, Lotte, Daesang, and Kolon) and financial investors (Kansas Asset Management, Seoul Asset Management).

The MOU was signed on January 25th 2008, and after a 3 week due diligence period, the main agreement was signed in the following month. The court announced that the bid amount obviously played an important role, but non-financial aspects like future business plans, efforts to increase distribution, and company vision was even more critical. In fact, the court adopted bidder appraisal criteria of measuring standard (60%) and non-measuring standard (40%), in which any bidders who offered more than 4 trln won got full scores on the measuring standard. Kumho Asiana got full scores on the non-measuring standard mainly because they promised the existing employees to be maintained for the next 5 years.

Kumho Asiana's Motivation. If successful in the deal, Kumho Asiana would be able to position itself as the nation's largest integral logistics company, and Kumho Asiana group became the 7th largest conglomerate in Korea's top-10. With the logistics portfolios that were mutually complementary, Kumho Asiana would be able to grow into an integral logistics company with networks in air, inland and sea. In particular Asiana Airlines would have strong synergy effects in air cargo transportation. Utilizing infrastructure provided by Kumho group affiliates, Korea Express would be able to transform itself into a global leader by designing new products and services in logistics.

Valuation. DCF method was used to value the share price of Korea Express. Since the portion of terminal value to enterprise value was more than 70%, two schemes were used to estimate its terminal value: perpetuity (Tables 1 and 2) and EBITDA multiple (Tables 3 and 4). Its growth rate of 3% p.a. and EBITDA multiple of 6.5 times were assumed as a normal case, and the sensitivity analysis was done for pessimist and optimistic cases.

WACC may be problematic in LBO valuation because target's debt-to-equity ratio could change very dramatically each year due to high leverage upon execution.

Table 1. **DCF Valuation based on Perpetuity,** *author's presentation based on the company's data*

Discounted Cash Flow Analysis – Perpetuity Method *(KRW in bln, except where noted)*

- Present values calculated as of Dec 31 2007					0.16180	0.14363	0.10315	0.09836	0.08999	0.08341	0.08210	0.08171	0.08221	0.08365
	Actual			Est.	Estimated									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenues	1,119.3	1,171.7	1,170.3	1,253.1	1,574.9	1,779.6	1,957.6	2,133.8	2,304.5	2,465.8	2,613.8	2,744.5	2,854.2	2,939.9
EBITDA	114.1	114.5	121.6	134.6	186.3	235.6	297.3	385.0	428.1	467.7	442.5	460.9	478.3	483.8
Less: Depreciation	(51.0)	(53.4)	(59.0)	(68.9)	(103.6)	(156.4)	(219.6)	(267.5)	(301.4)	(310.2)	(249.5)	(258.2)	(267.5)	(266.7)
Less: Amortization	(2.2)	(2.4)	(2.5)	(1.8)	(2.0)	(2.0)	(2.0)	(2.0)	(0.2)	0.0	0.0	0.0	0.0	0.0
EBIT	60.9	58.6	60.1	63.9	80.7	77.2	75.8	115.5	126.5	157.5	193.0	202.7	210.8	217.1
Less: Taxes @ 27.5%	(16.7)	(16.1)	(16.5)	(17.6)	(22.2)	(21.2)	(20.8)	(31.8)	(34.8)	(43.3)	(53.1)	(55.7)	(58.0)	(59.7)
NOPLAT	44.2	42.5	43.5	46.3	58.5	55.9	54.9	83.8	91.7	114.2	140.0	147.0	152.8	157.4
Plus: Depreciation					103.6	156.4	219.6	267.5	301.4	310.2	249.5	258.2	267.5	266.7
Plus: Amortization					2.0	2.0	2.0	2.0	0.2	0.0	0.0	0.0	0.0	0.0
Plus: Assets sale[1)]					17.2	17.7	18.2	41.5	54.0	55.4	56.9	58.5	60.1	61.7
Less: CAPEX					(254.8)	(255.6)	(201.9)	(209.9)	(207.4)	(205.7)	(214.6)	(224.2)	(234.7)	(245.9)
Less: Increase in WC					(20.2)	(20.2)	(22.8)	(32.3)	(18.1)	(15.3)	(17.8)	(20.0)	(22.4)	(25.2)
OFCF					(93.7)	(43.7)	70.0	152.6	221.8	258.8	214.0	219.3	223.3	214.6
# of shares		11,052,612	11,058,862	15,979,740	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654	16,134,654

[1)] Cash inflow from rent car sale.

Table 2. **DCF Valuation based on Perpetuity,** *author's presentation based on the company's data*

	A	+ B			= C			+ D	- E	= F					
Discount Rate	PV of OFCF ('08-'17)	PV of Terminal Value Perpetuity			Enterprise Value(A+B)			Non Operating Assets	Net Debt 3Q2007[1)]	Total Equity Value			Share Price @		
		2.50%	3.00%	3.50%	2.50%	3.00%	3.50%			2.50%	3.00%	3.50%	2.50%	3.00%	3.50%
9.0%	758.5	1,429.5	1,556.2	1,705.9	2,188.0	2,314.7	2,464.4	0.0	360.0	1,828.0	1,954.7	2,104.4	113,296.0	121,147.0	130,426.0
9.5%	733.2	1,268.0	1,372.2	1,493.8	2,001.2	2,105.4	2,227.0	0.0	360.0	1,641.2	1,745.4	1,867.0	101,721.0	108,179.0	115,714.0
10.0%	708.9	1,130.8	1,217.4	1,317.4	1,839.7	1,926.4	2,026.4	0.0	360.0	1,479.7	1,566.4	1,666.4	91,708.0	97,080.0	103,279.0
10.5%	685.5	1,013.1	1,085.9	1,169.1	1,698.6	1,771.4	1,854.6	0.0	360.0	1,338.6	1,411.4	1,494.6	82,963.0	87,476.0	92,633.0
11.0%	663.0	911.4	973.1	1,043.0	1,574.4	1,636.0	1,705.9	0.0	360.0	1,214.4	1,276.0	1,345.9	75,264.0	79,087.0	83,420.0

[1)] Interest bearing debts – excess cash.

Table 3. **DCF Valuation based on EBIDTA multiple,** *author's presentation based on the company's data*

Discounted Cash Flow Analysis – EBITDA Multiple Method (*KRW in bln, except where noted)*
- Present values calculated as of Dec 31 2007

	Actual			Est.	Estimated									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
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Less Depreciation	(51.0)	(53.4)	(59.0)	(68.9)	(103.6)	(156.4)	(219.6)	(267.5)	(301.4)	(310.2)	(249.5)	(258.2)	(267.5)	(266.7)
Less Amortization	(2.2)	(2.4)	(2.5)	(1.8)	(2.0)	(2.0)	(2.0)	(2.0)	(0.2)	0.0	0.0	0.0	0.0	0.0
EBIT	60.9	58.6	60.1	63.9	80.7	77.2	75.8	115.5	126.5	157.5	193.0	202.7	210.8	217.1
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[1] Cash inflow from rent car sale.

Table 4. **DCF Valuation based on EBIDTA multiple,** *author's presentation based on the company's data*

	A	+ B			= C			+ D	- E	= F					
Dis-count Rate	**PV of OFCF ('08-'17)**	**PV of Terminal Value 2017 EBITDA Multiple**			**Enterprise Value**			**Non Operating Assets**	**Net Debt 3Q2007**[1]	**Total Equity Value**			**Share Price @**		
		5.5x	**6.5x**	**7.5x**	**5.5x**	**6.5x**	**7.5x**			**5.5x**	**6.5x**	**7.5x**	**5.5x**	**6.5x**	**7.5x**
9.0%	758.5	1,124.0	1,328.4	1,532.7	1,882.5	2,086.9	2,291.2	0.0	360.0	1,522.5	1,726.9	1,931.2	94,362.0	107,028.0	119,694.0
9.5%	733.2	1,073.7	1,268.9	1,464.2	1,807.0	2,002.2	2,197.4	0.0	360.0	1,447.0	1,642.2	1,837.4	89,680.0	101,779.0	113,879.0
10.0%	708.9	1,025.9	1,212.4	1,398.9	1,734.8	1,921.3	2,107.9	0.0	360.0	1,374.8	1,561.3	1,747.9	85,209.0	96,769.0	108,330.0
10.5%	685.5	980.4	1,158.7	1,336.9	1,665.9	1,844.2	2,022.4	0.0	360.0	1,305.9	1,484.2	1,662.4	80,938.0	91,986.0	103,034.0
11.0%	663.0	937.1	1,107.5	1,277.9	1,600.1	1,770.5	1,940.9	0.0	360.0	1,240.1	1,410.5	1,580.9	76,858.0	87,419.0	97,979.0

[1] Interest bearing debts – excess cash.

Pleasem note that WACC assumes a constant capital structure. As a solution to this problem, Adjusted Present Value was suggested (Luehrman, 1997). In the case of Korea Express, however, debts to finance the deal were raised by equity investors, not by Korea Express. Although Korea Express guaranteed loans and exchangeable bonds, they were not the one who borrowed money, and thus their capital structure was not affected. Since the debt (360 bln won) was a very small fraction of enterprise value (1,566 bln won), at the same time, its impact would be minimal. In our analysis, WACC was used as a discount rate (Table 5).

Table 5. **Discount rate**

Unlevered Beta	0.71
Market premium	7.31%
Risk free rate (3 year treasury bond)	5.23%
Cost of Capital (ke)	10.42%
Cost of Capital (ke) levered	11.29%
Cost of Debt	8.36%
Debt	360
Market Cap.	1,566
Tax rate	27.50%
E/V	81%
D/V	19%
Levered Beta	0.83
WACC	10.31%

Characteristics of Leveraged Buyout. A leveraged buyout occurs when a small group of investors (financial sponsor) borrows money to acquire a controlling interest in a company's equity. It is a unique characteristic of LBO that a significant percentage of the purchase price is financed through leverage. The assets of the target company are used as collateral for loans, sometimes with assets and guarantees of the acquiring company. The bonds or other papers issued for leveraged buyouts are considered not to be investment grade (BBB+) because of the significant risks involved.

Because of the importance of debt and the ability of the acquired firm to make regular loan payments after the completion of a leveraged buyout, some features of potential target firms make for more attractive leverage buyout candidates, including:

- Low leverage (low existing debt);
- Stable and recurring cash flows;
- Small managerial ownership;
- Hard assets (property, plant and equipment, inventory, receivables) that may be used as collateral for lower cost secured debt;
- Large excess cash and liquidity;
- Inefficient incumbent management;
- Assets that can be separated if necessary;
- High marginal corporate tax rate;
- Appropriate financial structure: strip financing;
- Market conditions and perceptions that depress the valuation or stock prices.

Financing. To finance the acquisition amount of 4.1 trln won, Kumho Asiana formed a consortium. Within the 4.1 trln won, 3,441 bln won (or 84%) was financed by Kumho Asiana's affiliates, while the rest of 663 bln won (16%) was financed by outsiders like financial and strategic investors. As shown in Table 6, the total amount of 3,441 bln won to buy new shares was funded by Daewoo construction Co. (1,646 bln), Asiana airline Co. (1,397 bln), Kumho Renter Car Co. (298 bln), Kumho P&B Petrochemical (100 bln), and outside investors (663 bln).

Table 6. **Kumho Consortium Compositions,** *KRW bln shares*

Company	Investment Amount	Number of Shares	% of Total Shares
Asiana Airlines	1,397.0	8,169,612	20.43%
Daewoo E&C	1,645.7	9,624,000	24.07%
Kumho Rent-A-Car	298.3	1,744,404	4.36%
Kumho P&B	100.0	584,795	1.46%
Kumho Asiana Subtotal	3,441.0	20,122,811	50.32%
Strategic Investors	175.0	1,023,389	2.56%
Financial Investors	488.0	2,853,800	7.14%
Total	**4,104.0**	**24,000,000**	**60.02%**
Shares Previously Owned by Kumho		2,256,237	5.64%
Kumho Asiana Group Total		26,256,297	65.66%

To finance its share of 3,441 bln won, Kumho Asiana invented a unique scheme of utilizing exchangeable bonds (XBs). The newly issued 24 mln shares were the subject of exchange. Through XBs, financial investors such as merchant banks, domestic brokerages and pension funds could easily take part in the transaction.

Table 7. **Kumho Asiana's Financing Plan,** *bln KRW*

Company	Own funds	Exchangeable Bonds	Acquisition Financing	Total	Financing Cost Expected in 2008
Asiana Airlines	592.4	576.0	228.6	1397.0	24.2
Daewoo E&C	842.0	576.0	227.7	1645.7	23.3
Kumho Rent-A-Car[2)]	100.0		198.3	298.3	11.9
Kumho P&B[3)]			100.0	100.0	6.0
Total	1534.4	1152.0	754.6	3441.0	65.4

[1)] Exclude cash generated by disposal of non-core assets belonging to Asiana Airlines and Daewoo E&C.
[2)] Kumho Rent-A-Car: Financing through new share issue, bond issue (100 bln KRW) and loans (98.3 bln KRW).
[3)] Kumho P&B: Financing through bond issue (75 bln KRW) and loans (25 bln KRW).

Table 8. **Kumho Asiana's Financing Plan: Loans + XBs**

Loans from primary bank

	Contents
Total amount	1,223 bin KRW
Mandate advisor	KB, Shinhan, Woori Bank
Maturity	1.6 years
Distribution	Daewoo 550 (CD + 170 bp)
	Asian 550 (CD + 220 bp)
	Kumho renter car 98.3
	Kumho P&B 25
Guarantee	KOREA EXPRESS

XBs

	Contents
Total amount	1,152 bln KRW
Maturity	5 years
Exchange right	3 years after issuing
Exchange price	171,000 KRW
Yield	Daewoo face (2%), YTM (9%)
	Asiana face (2%), YTM (9.5%)
Underwriter	KB, Shinhan, Woori Bank
Guarantee	KOREA EXPRESS

Details of how Kumho Asiana financed the deal are summarized in Tables 7 and 8. Within 4,104 bln won, 2,376 bln won (58%) was financed through commercial borrowings such as bank loans (1,223 bln, 30%) and XBs (1,152 bln, 28%). 1,066 billion won (26%) was by Kumho Asiana's internal cash, while the rest of 663 bln won (16%) was by financial and strategic investors.

Kumho Asiana planned that their two subsidiaries, Daewoo E&C and Asiana Airlines, would issue the XBs that were exchangeable with Korea Express's new shares. The total amount of XBs was 1,152 bln won, bond's maturity was 5 years and it was exchangeable after 3 years. The bond holders would be KB, Shinhan, and Woori bank. Its exchange price was equal with the acquisition price of 171,000 won per share. As shown in Tables 9 and 10, the YTM for Daewoo E&C's XB was 9%, and that of Asiana Airline's was 9.5%. Since the face interest rate was 2%, if investors held the XBs until maturity, the only cash outflow would be the 2% face interest.

Table 9. **Asiana Airlines' Exchangeable Bond**

Amount	576 bln KRW
% against the total funding	43.32%
Coupon Rate	2%
YTM	9.5%
Maturity	5 yr
Condition	Exchangeable to Korea Express shares at 171,000 KRW

Table 10. **Daewoo E&C' Exchangeable Bond**

Amount	576 bln KRW
% against the total funding	35.02%
Coupon Rate	2%
YTM	9%
Maturity	5 year
Condition	Exchangeable to Korea Express shares at 171,000 KRW

What Happened? Kumho Asiana consortium paid 4.1 trln won to acquire mandatory 24 mln new shares (at 171,000 per share). 24 mln shares were composed of almost 60% of after-merger Korea Express equity. Afterwards, Korea Express purchased Korea Integrated Freight Terminal (KIFT) at 160 bln won. Korea Express also tried to purchase assets of Kumho Rent car. But, some shareholders like Goldman Sachs and STX opposed its acquisition claiming that the deal would destroy the firm's value.

They went to the court to exercise the appraisal right of dissenting shareholders. Korea Express compensated them including other small shareholders at the price of 89,205 won per share. The total amount was 696 bln won. From this transaction 19.42% of the total shares became treasury stocks. Kumho Asiana proceeded to sell Kumho Rent Car's assets to Korea Express at the price of 307 bln won returning 4.58% of shares owned by Kumho Rent car. From this event, Kumho Asiana secured about 85% ownership from previously 60%.

To recover from heavy debt financing, Kumho Asiana finally attempted to decrease paid-in capital. Out of the total 4,100 bln won, Kumho Asiana financed 3,441 bln won for acquisition. By selling Korea Integrated Freight Terminal (KIFT) and Kumho Rent Car to Korea Express, Kumho Asiana recovered 160 bln and 307 bln won, respectively.

Table 11. **Cash Recovered from Capital Reduction**

Category	Company Name	# shares	% shares	Decreased # Shares	Remaining # Shares	Recovered (100 mln won)
KUMHO	ASIANA AIRLINES	9,624,000	23.95%	4,159,493	5,464,507	7,113
	DAEWOO E&C	9,624,000	23.95%	4,159,493	5,464,507	7,113
	KUMHO LIFE	737,784	1.84%	318,870	418,914	545
	KUMHO P&B	584,795	1.46%	252,748	332,047	432
	KUMHO TRADING	47,065	0.12%	20,341	26,724	35
	SUBTOTAL	**20,617,644**	**51.32%**	**8,910,946**	**11,706,698**	**15,238**
Treasury Stocks	KUMHO Rent-a-Car Co. Treasury Stocks[1)]	1,744,405	4.34%	753,932	990,473	Retired
	Shares previously owned by Goldman Sachs & STX PAN OCEAN[2)]	6,504,032	16.19%	2,811,043	3,692,989	
	Shares previously owned by other minority shareholders[2)]	1,298,233	3.23%	561,096	737,137	
	SUBTOTAL	**9,546,670**	**23.76%**	**4,126,071**	**5,420,599**	
KOREA EXPRESS consortium (SI,FI)	LOTTE SHOPPING	584,795	1.46%	252,748	332,047	432
	DAESANG	292,397	0.73%	126,374	166,023	216
	KOLON	58,479	0.15%	25,275	33,204	43
	HYOSUNG	58,479	0.15%	25,275	33,204	43
	Tref il Arbed Korea Ltd.	29,239	0.07%	12,637	16,602	22
	Kansas Asset Management	923,976	2.30%	399,342	524,634	683
	Euzine KOREA EXPRESS	760,233	1.89%	328,573	431,660	562
	KOREA POST	1,169,590	2.91%	505,497	664,093	864
	SUBTOTAL	**3,877,188**	**9.65%**	**1,675,721**	**2,201,467**	**2,865**
Etc.	Old shareholders and other	6,135,222	15.27%	2,651,643	3,483,579	4,534
TOTAL		**40,176,724**	**100.00%**	**17,364,380**	**22,812,344**	**22,637**

[1)] Treasury stocks held through business acquisition of KUMHO Rent-a-Car Co.
[2)] Treasury stocks held through tender offer.

Table 12. **Recovery Plan,** *bln KRW*

Total Investment @170,000 KRW		4,104
Share Repurchase @89,205 KRW		696
Kumho's Cash Recovery		1,991
- KIFT	160	
- Kumho Rent a Car	307	
- Cash from Capital Reduction	1,524	
Cash from Capital Reduction (Non Kumho)		740
Cash left		678

As shown in Table 11, as a final step they announced heavy capital decrease of 43.22% at the price of 171,000 won equaling to the price of paid-in capital increase price at the acquisition. The total amount was 2.26 trln won leaving 1.5 trln won in the pocket of Kumho Asiana. To summarize, the cash of 1,967 bln won or sum of 160,307 and 1,524 bln won was returned to Kumho Asiana, while they held exchangeable bonds of 1,152 bln won which were guaranteed by Korea Express's new shares. Excluding the liabilities through XBs, the total cash used for the acquisition of 4.1 trln worth company by Kumho Asiana was only 300 bln won (Table 12).

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КНИЖКОВИЙ СВІТ

VITAE NON SCHOLAE DISCIMUS

СУЧАСНА ЕКОНОМІЧНА ТА ЮРИДИЧНА ОСВІТА
ПРЕСТИЖНИЙ ВИЩИЙ НАВЧАЛЬНИЙ ЗАКЛАД

НАЦІОНАЛЬНА АКАДЕМІЯ УПРАВЛІННЯ

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Організаційно-економічні аспекти інноваційного оновлення національного господарства: Наук. монографія / М.М. Єрмошенко, С.А. Єрохін, В.М. Шандра, О.І. Гуменюк та інші; За наук. ред. д.е.н., проф. М.М. Єрмошенка і д.е.н., проф. С.А. Єрохіна. – К.: Національна академія управління, 2008. – 216 с. Ціна без доставки – 22 грн.

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