COVID-19 CRISIS DISRUPTS MAJOR RETAILER'S DEBT RESTRUCTURING

BUYER:

J.C. PENNEY COMPANY, INC. (DBA JCPENNEY)

SECTOR:

RETAIL

JCPenney (JCP) was founded in 1902 and become one of America's largest department store retailers, operating approximately 850 stores throughout the United States and Puerto Rico. JCP's brick-and-mortar locations and e-commerce website feature apparel and accessories for numerous categories such as furniture, home decor, fine jewelry and cosmetics.

For the 2019 fiscal year, JCP revenues declined another 7% to $11.2B, had adjusted EBITDA of $538M, and a net loss of $268M. The 2019 results exceeded expectations for all five of JCPenney's financial guidance metrics with gross-margin improvement for three consecutive quarters and adjusted EBITDA for the full year increasing 2.6%.

Despite several quarters of operational improvements, the company's balance sheet was highly leveraged. Net debt to adjusted EBITDA was over 8x by the end of fiscal 2019. The company identified the need to deleverage and improve its capital structure. Unfortunately, discussions to restructure were interrupted as a result of COVID-19, and in May 2020, JCP announced it had filed for Chapter 11 bankruptcy protection.

RED FLAGS

- Highly leveraged balance sheet – net debt to adjusted EBITDA of over 8x
- Increasing competition and trend towards e-commerce
- Brick-and-mortar locations primarily at shopping malls, which experienced traffic declines
- Lack of cohesive long-term strategy due to substantial management turnover in 10 years
- Marketing unable to attract new customers or fully meet the needs of its existing customer base

FINAL STRAW

Leading up to COVID-19, JCP held numerous talks with lenders to restructure and was in the process of launching a tender offer for some of its term debt. With COVID-19, the company's primary revenue stream – in-store sales – evaporated seemingly overnight when many consumers became unable to patronize these locations, and talks to restructure came to a halt.

CONCLUSIONS

After entering bankruptcy, JCPenney agreed to sell its business and stores to a group of mall owners and lenders, saving it from liquidation.

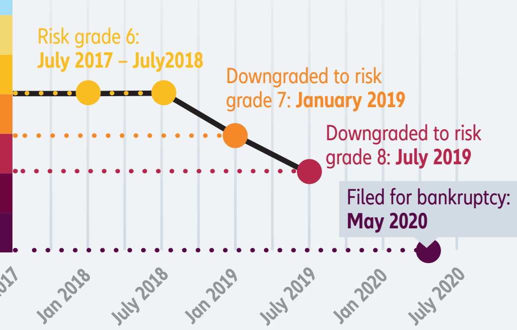
Although JCPenney maintained adequate liquidity in the short term, its balance sheet was unsustainable. High management turnover prevented the company from having a cohesive plan to deal with a difficult operating environment for retailers as consumers increasingly shift purchases away from brick-and-mortar to e-commerce. As a result, JCP was particularly vulnerable when COVID-19 hit and this resulted in additional disruptions it was unable to overcome.

Euler Hermes had been supporting over $100M in JCPenney invoices for our customers as recently as the 2018 Holiday period. As our risk team observed the red flags mentioned above and analyzed related data, our customers were advised of the growing trade risks. This helped many avoid payment defaults before JCPenney's bankruptcy.

RISK RATING

Euler Hermes' 1-to-10 risk ratings are reliably based on multiple sources of information and crosschecked thoroughly by our team of expert risk underwriters. **This chart shows how the risk rating for JCPenney progressed leading up to its bankruptcy.**

EH Risk Rating	Generic Description
1	Exceptional
2	Excellent
3	Strong
4	Good
5	Average
6	Watch
7	Substandard
8	High Risk
9	Uninsurable
10	Failed



Last updated September 2020

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