

Golden Gate Is Zale's Best Friend

By Ann Zimmerman and Peter Lattman
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Irving, Texas -- Jewelry retailer Zale Corp. said it has secured the rescue financing needed to fund its business as the company struggles with dwindling sales.

Zale, based in Irving, Texas, closed late Monday on a \$150 million secured loan from Golden Gate Capital Inc. The firm will receive warrants to purchase 11 million Zale shares at \$2 each.

The company's shares ended the regular session at \$3, up 27 cents, and were at \$3.15 in late trading.

If Golden Gate executes the warrants, it would own 25% of Zale, making it the company's largest shareholder, a perch presently held by activist investor and Zale board member Richard C. Breeden, who owns about nine million shares.

The interest rate on the five-year loan is a steep 15%. "That is market rate for this type of loan," said Zale Chief Financial Officer Matt Appel.

Golden Gate, whose retail holdings include Eddie Bauer, J. Jill and Express, will receive two board seats. The company said chairman John B. Lowe Jr. won't seek reelection to the board when his current term ends.

The deal gives Zale the cash it needs to fund its operations as it begins placing orders for the important Christmas season. Holiday sales account for the majority of the company's profit and almost 50% of its sales.

Appel says the deal "provides a financial runway, but we still have to execute against that. We believe we can."

Zale operates over 1,930 locations. For the second quarter ended Jan. 31, the company swung to a \$6.7 million profit from a \$31.8 million loss in the

year-earlier quarter. However, revenue fell 14.3% to \$582 million and same-store sales declined 11.2%.

Zale chose San Francisco-based Golden Gate over proposals from TPG Capital and Centerbridge Partners, according to people familiar with the deal. It also rejected a bid from Apollo Management LP that called for the company to sell its Canadian operations and mall-based kiosks and to install a new management team provided by Apollo.

The company has faced several years of declining revenue. In early January, Zale fired its chief executive, Neal Goldberg, and two of his top lieutenants.

Zale also closed on a new bank credit facility that amends and extends its existing asset-backed credit facility. The new facility consists of two tranches - an extended one with total commitments of \$530 million and a non-extended tranche, with total commitments of \$120 million.

Golden Gate's investment gives Zale much-needed liquidity without diluting public shareholders' interest, said Joe Stein, managing director of Peter J. Solomon Co., the New York-based investment bank that advised Zale in the transaction.

"Zale was seeking additional liquidity to improve its financial flexibility during an operational turnaround," Stein said.

Golden Gate was also chosen because of its retail expertise, said Stein. That comment was echoed by Zale executives during a conference call Monday.

"The company now has significant liquidity to execute its turnaround plan with support of an experienced investor who endorsed the plan," Stein said.

-Shasha Dai and John Kell contributed to this report.

<http://www.goldengatecap.com>
<http://www.zalecorp.com>