

Summary of Conclusions on Corporate Governance Review of
Takin Ltd
November 2009

CG RISK AREA	RISK CONCLUSION (High, Moderate, Low)	MITIGANT/COVENANT
1. Inadequate board structure and function	Moderate (See page 4)	Client feature that acts as main mitigant: 5 non-executive, non-family, experienced directors on 13 member board. Vigorous board discussions Comment/Recommended covenant: An audit committee
2. Inadequate risk management and controls	Moderate/High (See page 3,4)	Client feature that acts as main mitigant: Absent Comment/Recommended covenant: Poor controls over related party transactions, exposure to transfer pricing risk. Arm's length covenants needed.
3. Inadequate financial disclosures	Low (See page 3)	Client feature that acts as main mitigant: Listed company; Repeat IFC client that submits unqualified, annually audited accounts to the IFC; Meets all local accounting standards; Deloitte audits Comment/Recommended covenant: Implement audit committee
4. Abuse of minority shareholders	Low (See page 4)	Client feature that acts as main mitigant: Non-executive directors very vocal Comment/Recommended covenant: Arm's length covenants
5. Lack of commitment	Low (See page 2)	Client feature that acts as main mitigant: Listed company with full organic documents; Basic rules on family employment. Comment/Recommended covenant: None

Report on the Corporate Governance Review (CGR)

of

Takin, S.A. de C.V.

Introduction:

The Transaction: Takin, S.A. de C.V. (the “Company” or “Takin”) is seeking an IFC corporate loan of \$12.5M to fund its 2005-07 strategic expansion plan (the “Project”) for the construction of 72 new Takin stores and environmental and social and health and safety improvements at some of its facilities.

Ownership and Corporate Structure: The Company is listed on the Bexhillian Stock Exchange since 1984, but remains family owned and managed. It is held by the Takin-Theo family and the current shareholders include the 5 Takin brothers (sons of the original founder), two of whom are actively involved in the management of the Company. The shareholding structure is shown in Annex 2.

CG Risk Tiering: Given the size and type of transaction, the risk tiering indicated a CGR. For the initial engagement with the client a corporate governance matrix (CGM) was used. For the appraisal, a CG Review Generator was used to guide the data collection and analysis.

Finding from the Corporate Governance Review

Corporate Governance Matrix: While Takin fared well in terms of required attributes for transparency and disclosure (in compliance with Bexhillian GAAP guidelines), it only partially complies with those related to: commitment to corporate governance, structure and functioning of the board, and shareholders. In terms of IFC’s CGM for listed entities, Takin, does not comply with the majority of the requirements.

Commitment: In the last few years, Takin increased its commitment to good corporate governance and has taken several steps to adopt some best practices in corporate governance (in line with its stock listing and public debt issuance), such as: (i) reducing to two (from five) the number of family members working in the Company¹; (ii) requiring minimal qualifications for family members to be entitled to work in the Company; and (iii) having five non-executive directors at the board. Nonetheless, the Company is still fully-owned by the Takin Theo family and continues to be run as a family entity. For instance, all decisions are centralized in the CEO (as the board acts only as an advisory committee), and there are no guidelines on the family use of Company’s assets and resources.

Succession. The CEO, at 56-years old, has not quite reached the age where succession is an issue but is nonetheless training his younger brother, Bart, as his shadow CEO (as Bart will eventually

¹ Currently only 2 of the 5 sons to the founder occupy senior management positions, Enrique as CEO and Bart, the General Manager.

succeed him). Thus, Bart Takin currently has two roles in the Company, the General Manager role, and the shadow-CEO. In addition, the family has identified 5 members of the third generation who, despite their young age (middle- to late twenties in the average) seem to have good prospects for eventually succeeding Bart.

Board. Takin's board is composed of 13 members, 7 of whom are family-related, one whom is a company executive, and the remaining 5 of whom are non-executive directors. While the board meets once a month to design/implement Takin's policies, discuss business strategies, and monitor its performance and results, in actual fact, it functions as an advisory committee to the CEO, as none of the members have voting rights and the CEO is ultimately responsible to take all decisions. This arrangement was agreed by the founder and the five sons, but ultimately does lead to disagreements between the CEO and his four siblings. For instance, the team found out that whereas the CEO does not intend to take measures to have its shares trade with liquidity at the stock exchange, the remaining four-brothers would welcome this as they have no exit alternative other than to exchange shares among themselves².

Related-Party Transactions. The family uses loopholes in Bexhillian corporate and tax law to generate advantageous situations for themselves. However, Takin and the family's creativity (and flexibility) in adapting to the Bexhillian corporate and fiscal system is probably no exception to the rule (other than for listed corporations), and we have seen some of this creativity even with some of our investee entities (such as Salvatore Ltd). The difference is that (i) Takin has been transparent enough to openly disclose these schemes with us; and (ii) Takin is not too sophisticated, so we were able to identify some of these on our own. In fact, Takin has represented to us that while it takes advantage of weaknesses in the corporate and tax laws, they are committed to operate within the law. In fact, the appraisal team believes Takin's schemes are more a reflection of an inefficient Bexhillian tax regulation system. The Project Team has discussed these issues with the Takin's legal and tax advisors (KPMG) and a clean opinion will be issued from them in the following days.

Financial Reporting, Internal Controls and Internal Audit: This transaction would be IFC's third transaction with the Company, including an indirect loan through Cabecoa Credit Line in 1997 for US\$20.0 million, which has been fully repaid. IFC's first direct investment in Takin is relatively recent; it was disbursed in 2002 and repayment period will start in September 2005. Since disbursement, the Company has remained in compliance with IFC's covenants. These covenants include the timely filing of audited, unqualified annual financial statements, quarterly reports, internal audit summaries and management reports on the internal controls. The reports reflect a well run reporting, control and audit function.

² The Takin brothers have right of first offer if one of them wants to sell all or part of its shares.

Summary of Main Corporate Governance Related Risks and Issues.

The most issues relevant are as follows:

- Transfer Pricing. This is generated by related party transactions, primarily with Marge³. Given the size of these transactions⁴, the team is proposing to have Marge as a guarantor of the IFC Loans. At the Company's request, IFC also considered to have Marge as a co-borrower, but in the end decided not to as Marge would not have been able to meet all the stringent requirements to become an IFC Borrower. With regard to other (smaller) transactions with other family entities, IFC is introducing arm's-length covenants;
- Board of Directors (BoD). The Company does not have a traditional of a board of directors and its decisions are heavily centralized in a single person (the CEO). This is not unusual for family members and the CEO has taken the right steps in carefully selecting a mix of highly experienced non-executive directors (one of whom is the chairman for one of Takin's main competitors, Fugees Ltd.), together with the more seasoned executives of the Company and other individuals who have been heavily involved in Takin since its creation. In this way, the CEO is pushed to ensure that any proposals/rejections from him are well substantiated; otherwise he faces constant criticism from the board. The committee structure can be strengthened by the establishment of an audit committee (incorporated as a term sheet requirement);
- Family-Run Company. This risk stems mainly from: (i) the lack of policies on the personal use of Company's assets; (ii) lack of disclosure on related-party transactions to other long-term creditors⁵.

APPENDICES

Appendix 1: Shareholding Structure

Appendix 2: Persons Interviewed and Documents Reviewed

³ During 2003, the Takin-Theo family separated its retail and real estate businesses by creating an entity (Marge, S.A. de C.V. – “Marge”) to build and lease the new stores and distribution centers/warehouses to Takin. As of today, 35% of the Company's sales floor is leased, 86% of which is leased from Marge, and the remaining 14% is leased from third-party real estate investors. Marge is not consolidated with Takin, and its majority shareholders are the spouses of the Takin-Theo brothers. Please refer to Annex 5 for Marge's financials.

⁴ In 2004, transactions between Takin and Marge represented around 10% of Takin annual revenues.

⁵ The Company has US\$158.3 million of bonds outstanding in the local debt market.