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- [Case studies](#)
 - [Attractive workplace for all](#)
 - [Ageing workforce](#)
 - [Workers with care responsibilities](#)
- [Database of wages, working time and collective disputes](#)
 - [Dispute resolution](#)
- [News](#)
- [Events](#)

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You are here

- [Home](#)
- [Observatories](#)
- [EMCC](#)
- [ERM](#)
- [Restructuring in SMEs](#)
- [Astel, Estonia](#)

Astel, Estonia

- Type of restructuring:
Business expansion
- Employees before restructuring:
50-249
- Employees after restructuring:
50-249
- Nace/Sector:
Manufacturing
- Country:
Estonia
- Date:
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- Keywords:
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Abstract

With the aim of making business processes more efficient, Estonian firm Astel decided to focus on its core activities by reducing its number of production units. While the remaining production site was technologically upgraded and expanded, resulting in an increase in staff numbers, some of the activities previously done in-house were outsourced within Estonia by increasing the volume of contracts already in place.

Organisational profile

Astel OÜ produces timber products, its main production comprising summer houses and garden cabins made of milled timber. These are mainly mass produced, but the models given by clients are also produced according to their specifications. The company aims to give a flexible service, small batches are produced and both small and large-scale special projects are carried out.

The company was established in 1991 and has produced timber products for over 20 years. Astel OÜ operates in a small town in South Estonia. Nowadays, the production has been concentrated in one factory in Râpina, but before restructuring, it was dispersed throughout the region with four different production units within a 30 km radius. The company has remained legally independent and has not belonged to any group during its activity.

It is a family company and the present owners include the representatives of different generations of the family. The company is managed by the Chief Executive, who is one of the owners of the company. The company employs 55 people, 70% of whom are skilled workers, 25% are unskilled workers and 5% are managers. The work at the factory is managed by the Production Manager and there are two foremen at the factory managing smaller production units. There are two persons working in the sales unit, a Sales Manager and Sales Assistant, and the company has one designer. The personnel of the company mainly comprise men aged 25–50 years. The employees of the company are not members of any trade union and no separate Human Resources or Corporate Social Responsibility strategy has been developed in the company.

The company is oriented towards exports, selling 99% of its production in foreign markets and only 1% in the Estonian domestic market. The main target countries include the Netherlands, Sweden, Spain, Finland and Germany. The products are also sold outside the EU, for example, in Norway. The company considers its strengths to be foreign markets, sufficient production capacity and fast delivery time. One major drawback is the fact that the clients have different preferences regarding timber houses in different areas. While this does not allow for cheaper mass production, it makes the company produce small batches and perform special projects which require more resources. The raw material necessary for the production of timber houses is imported by the company mainly from Russia and Latvia.

Background to restructuring event

As mentioned earlier, before restructuring, the company consisted of four different production units, all of which were involved in various activities related to the production of timber houses. Altogether, 74 employees worked in the company before restructuring.

The Niitsiku factory produced windows and doors for the houses. A total of 14 employees were employed at the Niitsiku factory and the production of the unit comprised around 10% of turnover. The Veriora factory dealt with the storage and distribution, sawing, drying of round wood and production of furniture pieces and also loading of timber delivered by rail; 20 persons were employed in this unit and its turnover comprised around 25% of the total turnover. The Rāpina 1 Factory produced hand-made log houses, employing ten persons and comprising around 10% of turnover. The fourth and largest production unit was the Rāpina 2 factory, which produced garden cabins made of milled logs. Before restructuring, it employed 30 persons and its turnover comprised over 50% of total turnover.

The company was dispersed within a 30 km radius in the region and there were duplicated functions and jobs in the sub-units of the company, which were mostly related to ancillary activities, for example security guards and cleaners.

At the beginning of 2008, there was a decline in foreign demand, the number of orders decreased and the payment record of clients deteriorated. The need for investments was also a high priority in the company, since the technology had not been updated in all fields of activity. It was clear that more up-to-date technology was crucial to ensuring the quality of the products in order to remain competitive in the production of timber houses in foreign markets. It was clear to the managers and owners that the necessary investments could not be made in all fields of activity, especially during the economic downturn. In addition, the economic crisis saw the start of a liquidity problem which deteriorated. A sharp decrease in the number of orders could be seen by the second half of 2008, which led to a decrease in company sales turnover.

Restructuring processes

The owners and manager of the company felt during the first half of 2008 that the company could no longer be effectively managed and all the various fields of activity in the different locations could no longer be kept in operation. In order to prevent the company from getting into financial problems and avoid the risk of liquidation, the owners of the company decided to undertake restructuring. A change in the structure of the company was planned: to focus on one main activity, close unnecessary production units and incorporate the production into one main place of business. In the course of restructuring, the number of employees also had to be reduced.

The plan for restructuring was developed by the owners of the company, using legal advice from relevant experts and the services of a law office. The employees of the company were not involved in the planning stage. There was a flexible scheduled plan for restructuring and it was agreed among the owners that the market situation would be followed carefully, both the financial situation and general situation of the timber market. The owners were ready to respond quickly to the changed situation.

No separate financing or financial benefits were used for the restructuring. The expenses related to restructuring were partially covered by the sale of assets. Negotiations were held with the main creditors – that is, banks – concerning the extension of short-term liabilities. Payment schedules were used with the suppliers, as a result of which the payment periods became longer. The expenses related to redundancy were partially covered by unemployment insurance.

The restructuring process was carried out during 2008 and 2009, in the course of which only the main activity in one location in Rāpina remained (see figure 2). In other locations, the activity was terminated and the production units were closed or expropriated. A holding company (Simpes Grupp OÜ) was established, to which the assets and sales unit of the company belong and Astel OÜ became a production unit.

The Niitsiku production unit was closed and the buildings were retained. The Veriora production unit was closed and the assets were expropriated to increase liquidity. The production of hand-made log houses was terminated and the assets were leased to an independent company which continued the same activity. The Rāpina 2 factory remained in operation and the main activity – the production of garden cabins made of milled logs – was expanded there.

In the beginning of 2009, an additional investment was made in the main production in Rāpina for the purpose of updating technology and the sales unit was expanded. The number of factory workers also increased. The new expanded production unit employed the skilled workers who had mainly worked in the units that had closed down.

The production process was reorganised and outsourcing within Estonia was used for the activities which had ceased. Before reorganisation, the proportion of outsourcing concerning the windows and doors was just 10% and own production was predominant. After reorganisation, 60% of all the windows and doors necessary for production were bought in. Astel used the same outsourcing partner as before reorganisation and

increased the volume of the contract. The owners were satisfied with the quality of their workmanship and the cooperation was positive.

The workers were not informed in advance of the plan and course of reorganisation. They were notified during the course of the process. However, most workers had noticed that the work volume had decreased and they expected that there would be changes. The owners and the Chief Executive relocated the workers within the company as much as possible. Skilled workers were offered the opportunity to start work at the Rāpina production unit. Some workers were relocated to work under a new owner after the sale of company assets. Redundancy was used where unemployment insurance compensated for the expenses, and lay-off with minimum salary was used for a certain period (mostly during reorganisation of the Veriora production unit).

One of the main problems related to the workers was their lack of interest in moving to work in another neighbouring region. The workers who were offered a job necessitating the same skills and competence were not interested in starting work in another region, although the distance between the Niitsiku and Rāpina production units is only 30 km. In Estonia the mobility of workers is quite low. The same problem occurred in Astel as well. Therefore, the workers left the company and tried to find a job nearer to home.

To sum up, the financial indicators of the company began to improve, the sales turnover and exports increased and new target markets could be entered.

Challenges and constraints of restructuring

One of the key issues for the owners was financing the restructuring. The situation in the financial market was poor and taking on an additional loan was out of the question. It was decided not to use additional financial resources for reorganisation, but rather manage with the money received from the sale of assets and with internal resources. Another important step in improving liquidity was negotiations with the creditors, mostly the banks, in order to extend the due dates of liabilities. Since many companies encountered financial problems in the sector, the banks believed it was very important to support the restructuring of companies and agreed to extend the liabilities. The negotiations held with the banks concerning the competent reorganisation plan and steps were of crucial importance. Thus, reorganisation was successful in part due to the fact that the creditors were flexible.

Another important challenge was to carry out the restructuring process in a way that would least affect the local labour market. Since it is a small region and the company was an important employer in the region where both owners and workers have lived in the same community for a long time and everybody knows each other, the owners did not want the reorganisation to damage the reputation of the company.

Changes in the company led to an increase in workload and more diverse tasks which the workers often did not want to accept. The owners were also forced to use fixed-term employment contracts and lower wages for some jobs. All these activities contributed to reducing the motivation of workers. After the changes were carried out, one of the greatest challenges for the Chief Executive was to restore and maintain the trust of workers.

In the course of the restructuring, the owners and Chief Executive realised that the current business plan had been too flexible and had not ensured sufficient efficiency. Therefore, it was decided to focus on mass production in the restructured production and only produce one type of log house. The manufacture of hand-made log houses was completely terminated and it was decided to close all ancillary activities, such as the storage and primary processing of raw material or manufacture of accessories for production. The purchase of raw material and use of outsourcing led to significantly increasing the efficiency of the main production. The performance of special projects according to clients' wishes was also cut to a minimum.

Restructuring advice and support

The plan for restructuring was developed mainly by the owners of the company. External legal advice was used and the Estonian Unemployment Insurance Fund was consulted. No additional financial help was used and the employees of the company were not directly involved in the decision process.

Outcomes of restructuring

After restructuring, the efficiency of the company was increased and a focus placed on the more profitable production by concentrating on one specific activity. The production process was reorganised and the raw material and accessories necessary for production are now purchased through outsourcing. The efficiency could also be improved by concentrating production activity in one region and hence avoiding duplicating functions.

After restructuring, the owners and the Chief Executive had to quickly stabilise the cash flows in which they succeeded as during restructuring attention was drawn also to improving the efficiency of the sales functions. In general, the recovery of foreign demand could be seen in the market for timber houses and the expanded sales unit was able to increase export activity. Today, the company exports 99% of its products and the portfolio of target countries is differentiated as the products are sold in the EU as well as outside of the EU., for example, in Norway, Iceland, etc. The sales turnover reached € 2.4 million in 2009 and € 3.2 million in 2010.

The restructuring meant that in a small town in south Estonia production activity and jobs could be preserved for almost 60 persons. Since the Estonian labour market is flexible, labour costs could be cut in various ways, especially since during the economic recession, salaries were lowered, fixed-term employment contracts are still used and seasonal workers are used. Stable conditions could be maintained for the current workers and the owners also plan to increase employment in line with the expansion of production.

The owners learned a lesson from the experience that foreign demand should be followed carefully and the so-called controlled growth planned according to demand when making future expansion decisions. The preconditions for growth are an effective work process, improvements in technology, following the prices of production inputs and flexible employment contracts.

Commentary

According to the owners and Chief Executive of Astel OÜ, the restructuring was successful due to the fact that the owners quickly and flexibly responded to the first signs of financial difficulties. Since the owners were familiar with the business activity through its management on an everyday basis, the signs of the approaching economic crisis were noticed very early on and decisions made quickly on carrying out the changes. It is one of the advantages of SMEs that the owners are often managers, as they are in constant and immediate contact with business activity and results.

For SMEs, the costs required for changes may be lower; however, if additional financial resources are not used, it could be more complicated to finance the changes, since the current cash flows are smaller and more unstable. The advantage that bigger companies have are a better financial basis, sufficient resources and more capability to use finances during turbulent periods, since the banks favour bigger and more stable companies.

During the restructuring process, it is important to equally follow all the production links: input, production basis, technology, production, production methods, and employees. Restructuring does not only imply closure, liquidation and redundancy, but to be successful investments must be made and new structural units created simultaneously, if required. In the case described above, the owners of the company saw the need for additional investment, in order to create an adequate production basis for the main activity.

According to the Chief Executive of the company, restructuring requires focusing on a well-considered, conservative business plan and not immediately being swept along in the change of tides. It is necessary to be constantly alert to the market conditions in order to quickly respond to the changes and be in a position to make quick and bold decisions.

Estonian companies are supported by a flexible labour market in carrying out their decisions. While operating in a single community in a small region, companies inevitably have a certain social responsibility; however, employees' readiness to be more flexible should be encouraged.

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Information sources

Interviews

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Secondary sources

Estonian Business Register Database

- [European Monitoring Centre on Change - EMCC](http://www.emcc.eu)

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