Automation company, Germany

- Type of restructuring:
  (Avoiding) bankruptcy, Merger/Acquisition
- Employees before restructuring:
  50-249
- Employees after restructuring:
  50-249
- Nace/Sector:
  Manufacturing
- Country:
  Germany
- Date:
  08/09/2011

Abstract

This German provider of automation processes and switchboards offers systems, components and software for the logistical chain. Founded in the 1970s, the business (60 workers) was taken over in 1983 by the founder's son, who also owned a second firm (35 workers) in the transportation field. The latter business had to file for insolvency in the early 2000s due to high investments and the difficult economy. This led to both companies being taken over by a holding company, but retaining 80% of the workers.

Organisational profile

This case study deals with a German provider of automation and switchboards. The company offers systems, components and software for the complete logistical chain, aiming to support a quick and efficient linkage of all processes within the chain to store raw materials and manufactured products. The firm's services include documenting the client's electrical devices, constructing and assembling equipment, constructing switchboards or providing programmes/software according to the client's requirements.

The company was founded in the late 1970s and initially focused exclusively on switchboard construction. However, in the late 1980s and early 1990s the firm expanded into information technology and communication technology. In 2000, the founder's son who had been working in the company since 1983, took over the business as planned. At this point, the company had about 60 employees, and further plans concerning growth and improvement of quality were implemented.

The new head also owned another firm, with 35 workers. This second company was responsible for the construction or modification of vans to protect main company from any law suits for compensation in case of transport problems.

In the early 2000s, the company had to file for insolvency because of high investments and the difficult economic situation in Germany. A comprehensive restructuring was initiated, which led to both companies being taken over by a holding.

Background to restructuring event

About three years before the insolvency was filed for, the company was asked to equip a client's trucks with devices and control panels, in order to support the client's own new technique of transporting . The contract gave the client the right to contract a competitor instead, if the production capacities of the company were not sufficient.

The first order was fulfilled without problems, but the second order was delayed because of the larger order volume. With the third order it became obvious that the production capacities were not sufficient. At this point the company had only one production site which was remodelled in order to fulfill the orders. However, with increasing order volumes and a positive outlook in the overall market – this measure was not enough. The entrepreneur therefore decided to invest about € 700,000 on new land and the construction of a new production hall. Production processes were also overhauled; new machinery was bought and equipment constructed. This was funded from within the company.

However, shortly afterwards, the number and volume of orders from the main client began to drop. The client's own new technology was not meeting market expectations, and the client stopped the project without giving any notice to the company. This meant that the extended production capacities were redundant, and also that the company couldn't raise the funding required for the construction of the new production hall.

At about the same time, the company founder retired. He received a pay-off, and although this amount was much too low to compensate the work of his lifetime, it damaged the company's already weak liquidity, although neither father nor son realised this at the time.

The situation only became obvious when the general economic situation in Germany deteriorated and orders for the company's core business dropped. This stifled any possibility of financing the additional costs caused by the business expansion. The company was still making sales, but it was obvious they were not enough to cover future expenditure, and that the company's debts would increase.

Consequently, the company filed for insolvency and a comprehensive restructuring started.

Restructuring processes

The restructuring process started with filing the insolvency which was done by filling a simple form in the insolvency court. From this point on, the entrepreneur still was the owner of the company but was no longer managing it. Within few hours an insolvency administrator took over all the rights and obligations of managing the business. This meant, for example, that the entrepreneur had to get authorisation for any entrepreneurial activities and to point out, in all negotiations with clients, that any deals were conditional on getting the administrator's go-ahead. At a personal level this caused the entrepreneur some doubt about his role in the company, especially regarding clients or suppliers. However, his relations with the administrator were generally comfortable as the administrator recognised his expertise and accepted his suggestions.

The employees, according to the entrepreneur, had already known the company was in difficulties, having experienced a delay, of a couple of days, in their wage payments. They had been informed of this by the company, and accepted the situation. There were no non-payments nor wage reductions.

On the day of filing for insolvency, the entrepreneur on his own initiative released a press statement about the situation. He wanted to avoid the spread of rumours and half-truths, so that he could get the company back on its feet and continue running it. Even in the difficult situation of the company crisis, he was still interested in being an entrepreneur and facing the related challenges. Furthermore, after investigating the causes, he was convinced that the company in general offered high qualitative and competitive products and services, had good clients, and that the insolvency was not caused by a continuous deterioration of the business situation. Rather, he identified the high investment for the new production hall and the withdrawal of capital as the cause of the crisis. Accordingly, the entrepreneur together with his authorised commercial officer and the insolvency administrator developed a restructuring plan by, for example, rating the enterprise and establishing a liquidity and finance plan.

To do this he talked to his main clients and suppliers. These, due to their longstanding business relationship, were convinced of the quality of the company's services and wanted to continue dealing with the company. To maintain their trust, the company then supplied its main clients with the its monthly balance sheet to keep them informed about the development of the restructuring.

The banks were also approached and kept informed. Immediately after filing for insolvency the private accounts of the entrepreneur's family had been frozen but, relatively quickly, the banks were willing to negotiate. They saw the entrepreneur as a diligent businessman and agreed – after tough negotiations – to restructure the financial funds under consideration.

The professional crisis management proved to be successful: Potential investors quite soon approached the insolvency administrator as it became public that the company had a sound basis and good prospects if additional capital could be secured. Two months after filing for insolvency, a new company was founded and few months later took over all activities of the insolvent company. The entrepreneur kept 20% of the shares of the new company, with three new partners buying the rest. These were local investors known to the entrepreneur by name, but with whom he not previously had any business contact. Together they agreed on a plan for the new business.

The cash injection, plus the concentration on the firm's core competences meant the firm could regain its secure market position. About three years after the insolvency, the company profits were at the level before the crisis, and the number of employees was back to about 60 after the redundancies caused by the insolvency (see below).

About five to six years after the insolvency, a holding took over 80% of the shares of the company by buying out the new partners. This enabled the company to expand its range of services. At about the same time also the last administrative steps of the insolvency were completed.. The entrepreneur still owned 20% of the company.

About one year later, the holding also bought the entrepreneur's shares. He decided to do this because of plans to integrate the holding with the company. If he had not sold up, his share in the new company would have dropped from 20% to 8% with, to his dismay, his level of security collateral remaining the same, increasing his risk while at the same time reducing his possibilities to influence company decisions.

At the same time there were plans to expand the activities of the second company which had not been affected by the insolvency procedure. The plans included transferring selected employees and assets from the holding, but banks demanded the entrepreneur's private assets, including his home and life insurance, as collateral to finance the plan. As this was not feasible for him, he also sold the second company to the holding. The entrepreneur now acts as a chief executive officer of one of the firms of the holding.

Challenges and constraints of restructuring

The main challenge was dealing with the banks. Immediately after filing for insolvency, not only were the entrepreneur's business accounts closed, but also his private one. He had to apply to the banks before he could even cover private expenses. The bank employee who had been his longstanding contact was no longer responsible for him, so a new relationship of trust had to be fostered during intensive negotiations necessary as the suggested conditions partly were not feasible.

It was not possible to restructure without additional finance from banks or new partners, because of the firm's great need for capital, which therefore demanded the entrepreneur's private assets as collateral..

Restructuring advice and support

The entrepreneur and his tax consultant considered various possible solutions to the problem of falling revenue and increasing debt, but filing for insolvency was thought to be the most realistic. Later he was supported by the nominated insolvency administrator in the planning and implementation of the new strategies.

However, he received the most important support on restructuring from within his company, namely from his authorised commercial officer who supported him with business expertise and advice. He also received important personal support from his family.

The entrepreneur does not feel the company had any further need for support from public authorities or private consultants in the restructuring. However he mentions that, in general, a continuous system of support for medium-sized enterprises would be welcome – not only helping with the annual drafting of the balance sheet but also in cases of crisis whereby business consultants familiar with the enterprise might be able to pinpoint alternative courses of action.

Outcomes of restructuring

The restructuring process has led to two rebranded companies, now part of a group, which were previously run by an owner-manager. However, their profiles remain almost unchanged. The original owner is now chief executive officer and, in the third business year after starting the restructuring, the profits and the number of employees were the same as they were before the company crisis.

At the point of filing for insolvency the company had 60 employees, none of whom was dismissed at this time. The reason for this was that the company wanted to maintain sufficient resources for the hoped for upswing, as well as the loyalty of the family-led company towards long-standing employees. The workers also did not have to accept a reduction of working time or wages, although there sometimes was a couple of days delay in the payment.

In the medium term there only were minor personnel changes. The insolvency led to two staff members being dismissed, with about five others volunteering to leave the company in order to prevent further job losses if the company closed. Some of these workers have now returned to the company.

About eight years after the restructuring, about 80% of the workers employed by the two companies before the insolvency were still working in the new firms. The loss of the remaining 20% can be considered as a natural fluctuation.

From the entrepreneur's personal perspective, the company insolvency is an experience he does not want to repeat. Nevertheless, it did have a benefit, in that he has a new perspective on banks, brought about positive learning effects. He now sees himself and his company, more as customers than as applicants; increasingly comparing the quality and prices of offers and negotiating more.

The integration of the initially owner-managed companies into the holding structure introduced administrative changes for the company's management. There are more restrictions on investment planning or staff decisions which partly result in less flexibility and a more limited scope for action. However the holding's strong financial backing means that larger orders can be fulfilled without problems, and better deals can be had from suppliers or providers of services (such as insurance).

Commentary

The entrepreneur says an important factor for success in entrepreneurial activity is expertise in the economic/commercial field, next to technical know-how. He feels that there is a lack of public support for making available business education and advice on business management. Many entrepreneurs become self-employed because of their strengths in the technical field. Even if they are good at administration they may need expert support because of their work load and the complexity of identifying, for example, appropriate financial instruments or strategies for development. A medium-sized company often cannot afford to employ a specialised worker for this area, instead hiring temporary external consultants who lack continuity of knowledge about the company as well as familiarity with the long-term aims and working methods of the entrepreneur. Often only the current status of the company is assessed, but no courses of action for the future are pinpointed as soon as a first sign of deterioration of the situation is seen. This results in a lack of an early warning system early pinpointing potential drawbacks.

He is convinced that company insolvency is not caused by a single, isolated aspect, but by a combination of various elements which can be internal or external to the firm. Internal aspects can include entrepreneurial mistakes such as keeping employees on for too long, partly in order to be ready for the hoped for upswing, and party due to a feeling of social responsibility of a family-led company towards the employees.

He also feels that there should be two people that a company can turn to in time of insolvency: someone that can give social or psychological support, as well as an economic/business expert within the company in order to internally discuss strategic decisions.

Above all, he recommends that companies experiencing such a crisis should carefully evaluate the causes and approach relevant stakeholders such as banks, employees, clients and suppliers, communicating with them openly, telling them of the situation and of plans for the future. Furthermore, one's own initiative and creativity is also necessary to develop and implement strategies. In negotiations with banks or other finance providers he recommends being confident, having the courage to negotiate, while being open to the perspectives and requirements of the negotiation partner.

Author

Irene Mandl, Eurofound

Information sources

Interview

Previous owner/manager and now chief executive officer of the company

- Multilingualism
- Templates for Eurofound reports
- Eurofound style guide
- Management Board extranet
- Map - how to get to Eurofound
- FAQ
- Sitemap

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